

# **The Mid Yorkshire Hospitals NHS Trust**

**Annual Audit Letter 2008/09**

**14 September 2009**

# The Mid Yorkshire Hospitals NHS Trust Annual Audit Letter 2008/09

## **Purpose of this Letter**

The purpose of this Annual Audit Letter (letter) is to summarise the key issues arising from the work that we have carried out during the year at The Mid Yorkshire Hospitals NHS Trust (the Trust). Although this letter is addressed to the directors of the Trust, it is also intended to communicate the significant issues we have identified, in an accessible style, to key external stakeholders, including members of the public. The letter will be published on the Audit Commission website at [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk) and also on the Trust website.

This letter has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. This is available from [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk).

## **Responsibilities of the external auditors and the Trust**

We have been appointed as the Trust's independent external auditors by the Audit Commission, the body responsible for appointing auditors to local public bodies in England, including NHS trusts.

As the Trust's external auditors, we have a broad remit covering financial and governance matters. We target our work on areas that involve significant amounts of public money and on the basis of our assessment of the key risks to the Trust achieving its objectives. It is the responsibility of the Trust to ensure that proper arrangements are in place for the conduct of its business and that public money is safeguarded and properly accounted for. We have considered how the Trust is fulfilling these responsibilities.

## **The scope of our work**

Our responsibility as your external auditors is to plan and carry out an audit that meets the requirements of the Audit Commission's Code of Audit Practice (the Code). Under the Code, we are required to review and report on:

- the Trust's accounts
- whether the Trust has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

This letter summarises the significant matters arising from these areas of work and highlights the key areas for action for the Trust in 2009-10. A list of all reports issued to the Trust in relation to the 2008/09 audit is provided in Appendix A and we have included details of our audit fees in Appendix B.

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## **Audit of the Trust's Accounts**

Our audit of the Trust's accounts included

- review of the Trust's internal control systems
- audit of the annual accounts to support our accounts opinion

### **Review of Internal control systems**

We reviewed key financial controls and the Trust's overall Information Technology (IT) control environment for the purpose of designing our programme of work for the financial statements audit. Our evaluation of the Trust's key financial control systems did not identify any control issues that present a material risk to the accuracy of the financial statements.

The results of our reviews, including our review of work performed by the Trust's internal auditors, provided assurance that we could rely on the Trust's systems of internal control to reduce our detailed testing at the final accounts audit, in accordance with our audit strategy.

Whilst there were no significant weaknesses affecting our audit opinion, our work identified some areas where control procedures could be improved which we have reported separately to the Trust.

We are pleased to report that the Trust has introduced an improved process for approving its Statement on Internal Control (SIC). Following the review of integrated governance arrangements last year each of the Trust's main sub-committees now reviews the contents of the SIC against their knowledge of their respective elements of the control environment to ensure that the SIC fairly reflects all risks of which they are aware.

We note the Audit Committee's commitment to meeting best practice and during the year we continued to work with the Trust in implementing the action plan arising from the Committee's self assessment against relevant standards of best practice.

### **Our audit opinion on the accounts**

We issued an unqualified opinion on the Trust's accounts confirming that the accounts give a true and fair view of the Trust's financial affairs and of its income and expenditure for the year.

We completed our report on 5 June well within the deadlines set by the Department of Health.

We again received a complete set of draft accounts in advance of the accounts submission deadline set by the Department of Health. This represents a considerable achievement for the Trust as the deadline was brought forward by over a week as part of the DH faster close initiative.

We met regularly with the Trust over the year to discuss accounts planning issues and the approach to potentially difficult technical accounting matters. This enabled us to agree matters such as the accounting treatment and disclosures in respect of the Financially Challenged Trust Agreement prior to the start of the final accounts audit.

## **Audit of Accounts 2008-09 Annual Audit Letter**

The accounts were supported by working papers which were, overall, of a good quality, although there were areas, particularly in relation to deferred income where we requested the Trust to provide additional information as part of our audit. We have agreed with the Trust's finance team areas where improvements could be made for future years.

There were no misstatements uncovered by our audit which the Trust had to adjust to ensure that the accounts showed a true and fair view.

Our audit identified a number of unadjusted misstatements which we reported to the Audit Committee through the ISA 260 Report to those charged with Governance. The net effect of these accounts misstatements was not considered to be material in relation to the overall financial position.

The accounts included a number of areas where management has exercised judgement in relation to the amounts to be included in the accounts. These areas related mainly to the estimation of provisions for future liabilities and the timing of recognition of certain sources of income received in the year. Our detailed audit findings report, issued on 29th May 2009, drew to the attention of the Audit Committee a number of matters on which we sought representation from the Trust to inform our audit conclusions.

Following our recommendation last year relating to the accounting for deferred income the Trust has improved its own records over the way it has received and used funding from Primary Care Trusts (PCTs). However, the documentation between the Trust and its commissioners did not in all cases clearly specify the purposes for which the funding had been provided. We were able to obtain further evidence from the PCTs in some areas but there were still a number of areas where the Trust had to exercise its judgement and on which we requested and obtained management representation. We have, accordingly, reiterated our recommendation of last year on the importance of ensuring that the specific terms of funding from PCTs is fully recorded at the time funding is provided.

We recognise that there is some inherent conflict between the PCTs requirement to account for expenditure in the year in which resources are granted and Trusts being required to recognise income when they earn the right to the income through performance. This is a generic matter with the financial regime for the NHS and not specific to Mid Yorkshire.

### **The Trust's Annual Report**

The Trust has continued to develop its arrangements for the preparation and design of the annual report and in particular its consultation with users of the report. This improvement is reflected in our assessment of the financial reporting element of the Auditor Local Evaluation set out below. We have supported the Trust by making some suggestions as to how presentation could be improved which the Trust has taken on board.

We received a complete draft annual report in sufficient time to undertake the required audit procedures prior to reporting to the Audit Committee. We reviewed the Trust's procedures for ensuring that the Annual Report complies with the NHS Manual for Accounts reporting requirements. There are no matters we consider need including in our formal report.

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**Achievement of Financial Targets for 2008-09**

We summarise below in the following table the Trust's performance against its statutory financial targets.

	Target	Actual	Met?
Surplus (after Financially Challenged Trust Agreement)	£31.4m	£32.7m	Y
Capital Cost absorption	3.5%	2.2%	N
External Financing Limit	£-75.8m	£-76.7m	Y
Capital Resource Limit	£13.5m	£11.6m	Y

The Trust achieved its key statutory financial targets with the exception of the Capital Cost Absorption Rate (CCAR). This duty measures the percentage relationship between the dividends paid on public dividend capital to the average relevant net assets. The variance from the target of 3.5% was due to changes in assumptions regarding working capital arising from the Financially Challenged Trust agreement and which occurred after the dividend requirement for the year was set by the Department of Health.

The Trust's headline financial outturn for 2008-09 includes the impact of the exceptional one-off benefit of the Financially Challenged Trust Agreement (FCT). This agreement was reached to enable the Trust to pay off outstanding working capital borrowing requirements. Under the FCT Agreement the PCTs provided resources to enable the Trust to settle a working capital loan of £31.4m and related interest.

The FCT was treated as an exceptional item in the accounts to enable the underlying financial position to be determined. This recorded a modest operational surplus position of £2.9m for the year. We note that this was in part achieved through non recurrent measures as the full value of planned recurrent Cost Improvement Plans (CIP) was not fully met during the year. This represents a second successive year of surplus on its operations

**Looking ahead to 2009/10 and beyond.**

The Trust's financial reports show that it is again on-course to achieved budgeted break-even in 2009-10. This position is dependent on the delivery of significant cost savings. The Trust's financial forecasts and Medium Term Financial Plan (MTFP) show that the Trust will be required to achieve further significant cost savings to sustain financial balance in the medium term. The scale of this financial challenge is due to a number of key factors including

- year on year efficiency gains required through the national tariff for completed activity
- the net additional cost of investment in new hospital facilities
- the impact of accounting for PFI under IFRS
- making recurrent cost improvement plan requirements from previous years

The issues faced by the Trust are unlikely to be capable of resolution by it acting alone and a whole system response is necessary for the Mid Yorkshire health economy to achieve a sustainable service and financial position. We understand that the Trust is currently in discussions with local primary care trusts and the NHS Yorkshire & Humber on this matter.

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We note that the Trust Board has recognised the importance of achieving sustainable financial balance over the medium term. The Board should continue to monitor progress against any action plans developed to ensure that the Trust's financial position remains balanced over the medium term.

### **The Trust's use of resources**

We are required to issue a conclusion on whether we are satisfied that the Trust has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the value for money conclusion.

We are also required to assess how well NHS organisations manage and use their financial resources by providing scored judgements on the Trust's arrangements in five specific areas. This is known as the Auditor's Local Evaluation.

### **Our use of resources conclusion**

We are satisfied that the Trust put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. Accordingly, we were able to issue an unqualified use of resources conclusion for the 2008/09 financial year.

The use of resources conclusion for NHS bodies comprises an assessment of the arrangements in 12 Code of Practice areas. These areas are closely linked with the Auditors Local Evaluation (ALE) judgements. In order for an unqualified use of resources conclusion to be provided, an NHS body should achieve the minimum standards at Level 2 under all ALE judgements.

We assessed the Trust's arrangements against five Key Lines of Enquiry (KLOE) using the 1-4 scoring system introduced by the Audit Commission, where:

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

<b>Area</b>	<b>2008/09 Score *</b>	<b>2007/08 Score</b>	<b>2006/07 Score</b>
Financial reporting	3	4	3
Financial management	3	3	3
Financial standing	3	2	1
Internal control	3	3	2
Value for money	3	2	2
<b>Overall Score</b>	3	2	1

\* The scores for 2008/09 will be formally published by the Audit Commission in late September 2009. The scores reported above are as notified by the Audit Commission to the Trust, are consistent with our assessment and which the Trust has not sought to challenge.

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This table shows an overall improvement in the scores achieved by the Trust. This increase in ALE score was a key objective for the Trust in 2008-09. Our work showed that the Trust has made significant progress in 2008-09 with value for money and financial standing now being assessed as 'performing well' at level 3 resulting in an overall increase for the Trust to level 3 overall. The improvement in KLoE scores reflects the efforts made by the Trust on both value for money and financial standing to deliver the ALE Action Plan agreed at the end of the 2007-08 audit.

To support the Trust in this objective we held a number of meetings with Trust officers and an ALE workshop, to highlight the areas where improvements were needed to support a level 3 score.

The slight overall reduction on the Financial Reporting score reflects the unadjusted misstatements and accounts uncertainties arising from the evidence produced to support the deferral of income and some accruals. This was mitigated by an increase in the score for promoting external accountability arising from improvements in the processes relating to the Annual Report.

The principal areas we noted where further progress on ALE could be made are as follows:

- to formally test or regularly benchmark the Trust's corporate services and identify areas where efficiencies could be made
- to further develop Service Line Reporting such that opportunities or areas of underperformance can be identified and action taken where appropriate
- to implement a procurement strategy, showing how the Trust intends to take forward procurement in order to meet corporate objectives.

On the basis that the overall ALE score of 3 is confirmed we would not be required to perform a detailed review during 2009/10. It is proposed that this would be replaced by a combination of

- reviews against specified high level indicators
- review of any new assessment criteria

This would release audit time to enable us to perform alternative project based Use of Resources work in 2009-10.

We have discussed this with the Finance Director and will reflect this anticipated change in our 2009-10 Audit Plan.

## **International Financial Reporting Standards**

The implementation of International Financial Reporting Standards (IFRS) required the Trust to restate its opening balance sheet as at 1 April 2008 and to prepare restated accounts for the 2008/09 financial year on an IFRS basis. The Trust met the respective deadlines of December 2008 and 4 September 2009 for these requirements.

The Trust has robust arrangements in place to meet the challenge of IFRS. The Trust has a nominated IFRS lead and has worked against an internal action plan to identify areas where adjustments would be required under IFRS. During 2008-09 we held an IFRS accounts workshop in order to support the Trust with preparing for the introduction of IFRS.

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The Trust had presented its IFRS Implementation Plans and regular progress reports through the Audit Committee. We have continued working with the Trust over the year to discuss detailed accounting issues arising from the Trust's IFRS work to ensure that the deadlines for adopting IFRS are met.

**New Hospitals Development Project - Private Finance Initiative (PFI)**

The Trust will be required to account for the new Hospital Development Project (HDP) scheme under IFRS in 2009-10. The Trust's HDP scheme will provide the Trust with new hospital facilities under a 35 year concession contract which also includes provision of lifecycle maintenance and specified services. The Trust is charged an annual fee, known as the unitary charge, for the provision of the property and related services.

The accounting for this scheme under IFRS is complex and is likely to have a significant impact on the Trust's future financial position. The work performed by the Trust and ourselves to date has highlighted several significant technical accounting and modelling issues. We have agreed the principles to be adopted in accounting for PFI under IFRS and are working with the Trust to understand and resolve these issues in 2009-10 to provide certainty on the impact that this will have on the Trust's future financial position.

**Key areas for action**

The key areas that we feel need the most urgent attention by the Trust Board over the coming year are:

- continuing to monitor progress against any actions plans being developed to ensure that the Trust's financial position remains balanced over the medium term
- ensuring that all technical accounting issues relating to the PFI scheme are fully resolved in 2009-10 to provide certainty on the impact that this will have on the Trust's future financial position.
- ensuring that the specific terms of funding from PCT's is fully recorded at the time income is received.

We have followed-up the recommendations that we made in our Annual Audit Letter for 2007/08 and are pleased to report that the Trust has taken necessary action to implement them.

**Closing Remarks**

This letter will be presented to the Audit Committee on 23 September 2009 and to the Board on 24 September 2009.

We would like to take this opportunity to express our appreciation for the assistance and co-operation provided during the course of the audit. Our aim is to deliver a high standard of audit, which makes a positive and practical contribution that supports the Trust's own agenda. We recognise the value of your co-operation and support.

**Grant Thornton UK LLP**  
**14 September 2009**

## A Reports issued in relation to the 2008/09 audit

<b>Report</b>	<b>Date Issued</b>
Audit plan	20 November 2008
IFRS accounting workshop	5 November 2008
Report to Audit Commission on procedures for restating the transition balance sheet at 1 April 2008 under IFRS	March 2009
Use of Resources - Auditors local evaluation and interim audit	3 May 2009
Information technology controls	29 May 2009
ISA260 communication of audit matters to those charged with governance	29 May 2009
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## B Audit Fees 2008/09

The table below summarises the planned and actual audit fees charged to the Trust during 2008/09

Audit Area	Plan	Actual	Actual
	2008-09	2008-09	2007-08
Accounts	61,750	91,750	61,000
Use of resources	110,375	80,375	109,000
<b>Total - Trust</b>	<b>172,175</b>	<b>172,175</b>	<b>170,000</b>

The revised allocation of fees above reflects the additional time required to complete the final accounts audit this year due to the number and complexity of issues.

We have also charged £13,500 for work mandated by the Audit Commission in respect of the restated IFRS balance sheet at 1 April 2008.



# Grant Thornton

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