

Northumberland, Tyne and Wear NHS Foundation Trust

Board of Directors Meeting

Meeting Date: 25 May 2016

Title and Author of Paper: Audit Committee Annual Report 2015/16

Martin Cocker, Chair Audit Committee

Executive Lead: n/a

Paper for Debate, Decision or Information: Approval

Key Points to Note:

Monitor's Code of Conduct requires that a separate section of the Annual Report should describe the work of the Audit Committee in discharging its responsibilities.

The Report has been approved by the Audit Committee and will be used in the Annual Report.

The Board is required to review and consider the annual report of the Audit Committee and, if satisfied, approve that it be accepted by the Board and included in the Annual Accounts.

Risks Highlighted to Board :

Does this affect any Board Assurance Framework/Corporate Risks?

No

Equal Opportunities, Legal and Other Implications:

None

Outcome Required: Approval of the Annual Report of the Audit and its inclusion into the Annual Accounts.

Link to Policies and Strategies:

Audit Committee Annual Report 2015/16

Annual Report entry on the work of the Audit Committee

Overview

The Audit Committee provides a central means by which the Board of Directors ensures effective internal control arrangements are in place. The Committee also provides a form of independent check upon the executive arm of the Board of Directors. It is the job of Executive Directors and the Accountable Officer to establish and maintain processes for governance. The Audit Committee independently monitors, reviews and reports to the Board of Directors on the process of governance, and, where appropriate, facilitates and supports, through its independence, the attainment of effective processes.

Audit Committee Composition and Attendance:

The Audit Committee comprises three non-executive directors. Each of the members is considered to be independent and the Board is satisfied that the Chairman of the Audit Committee has recent and relevant financial experience.

The Audit Committee met six times during, and twice shortly after the end of, the financial year. Attendance at those meetings was as follows:

Member	Meetings	
	Total	Attended
Martin Cocker	8	8
Nigel Paton	2	1
Chris Watson	5	4
Alexis Cleveland	5	3
Peter Studd	3	2

Nigel Paton and Chris Watson ceased to be non-executive directors of the Trust on June 30, 2015 and December 31, 2015, respectively and left the Audit Committee on those dates

Alexis Cleveland was appointed to the Audit Committee on July 1, 2015 and Peter Studd on January 1, 2016.

In addition to the non-executive directors, the Director of Finance, Director of Quality and Performance, External Audit and Internal Audit, including Counter Fraud were all invited to each meeting during the year. All attended each meeting with the exception of the Director of Finance and the Director of Quality and Performance who were both unable to attend the meeting in February 2016. However, alternates did attend.

A representative of the Governors attended each Audit Committee meeting as an observer.

The Chief Executive and the Chairman of the Board were invited to, and attended, the April 2016 meeting at which the Annual Governance Statement was considered as well as the Opinion of the Head of Internal Audit which supports the conclusions within the Annual Governance Statement.

External Audit and Internal Audit were given opportunities at the end of each meeting to discuss confidential matters with the Audit Committee without Executive management being present.

Programme of Works

The Audit Committee follows an annual work programme that covers the principal responsibilities set out within its terms of reference. In 2015/16, this included, amongst other matters, the following activities:

- Assessed the integrity of the Trust's financial statements for the year ended March 31, 2016;
- Considered the effectiveness, independence and objectivity of the external auditor throughout the audit cycle;
- Reviewed the Annual Governance Statement in light of the Head of Internal Audit opinion, the External Audit opinion relating to the year end and any reports issued by CQC and Monitor;
- Reviewed External Audit's findings and opinions on the Quality Report, the securing of economy, efficiency and effectiveness, and the areas of the Annual Report subject to audit review;
- Considered whether the Trust's Business Assurance Framework ('BAF') and Corporate Risk Register are complete, fit for purpose and in line with Department of Health expectations;
- Reviewed the arrangements by which staff may raise in confidence concerns about possible improprieties in matters of financial reporting and control, clinical quality, patient safety or other matters;
- Reviewed the process established by the Trust to ensure compliance with Monitor's Code of Governance;
- Challenged and approved the internal audit programme, counter fraud and informatics plan, operational plans and detailed programmes of work for the year. The Audit Committee confirmed the effectiveness of internal audit and counter fraud and the adequacy of their staffing and resources;
- Considered the major findings of internal audit, counter fraud and informatics throughout the year. The Audit Committee agreed that the remedial actions proposed were appropriate and then monitored the timely implementation of those remedial actions by management;
- Reviewed the work of other Board Committees and considered how matters discussed at those committees impacted the work of the Audit Committee;

Significant Issues

Throughout the year, the Audit Committee has debated and concluded on a number of matters. The more significant issues to have come before the Audit Committee, and the actions taken by the Audit Committee to ensure that those issues were dealt with promptly and in an appropriate manner, are noted below.

1. *Integrity of financial reporting*

The Audit Committee reviewed the integrity of the financial statements of the Trust. This process included reviewing the accounting policies to ensure that they remained appropriate and had been complied with and debating the areas of significance in relation to the integrity of financial reporting. The review and debate took into account the views of the External Auditors, Mazars LLP ('Mazars').

The significant matters considered were:

Impairment and Revaluation of the Trust's Specialist NHS Buildings

The Trust records its specialist NHS buildings initially at cost and subsequently at their fair value. The fair value is calculated using the 'depreciated replacement cost' ('DRC') method.

The DRC method seeks to calculate the cost of an asset that would provide a similar function and equivalent utility to the asset being valued, but which is of a current design, constructed using current materials and techniques and is built on a site of optimal size and location.

Therefore, the valuation of the Trust's specialized NHS buildings is not a valuation of the existing buildings in their current locations. Rather, it is a valuation of the specialist buildings that the Trust could hypothetically build to deliver the services and occupancy levels as at the balance sheet date on a site that was of the optimal size and location.

Application of the DRC method typically results in an asset value that is significantly lower than the actual cost.

In addition, subsequent remedial capital expenditure on assets already revalued under the DRC method and which does not significantly increase either the value or expected life of the asset is unlikely to result in an increase in the fair value of the asset calculated using the DRC method.

Any reduction in value between the original cost and the fair value calculated under the DRC method is reported as an impairment in the financial statements.

Accordingly, the initial use of the DRC typically results in a significant provision for impairment. In addition, subsequent remedial capital expenditure on assets already revalued under the DRC method is likely to result in an additional provision for impairment.

Any increase in the fair value of specialized NHS assets at successive balance sheet dates is reported as a revaluation.

Non-specialist buildings fall outside the DRC valuation methodology and are carried at market value.

For the year ended March 31, 2016, the Trust has reported within 'Other Operating Income' a reversal of impairment of £11 million and a revaluation gain of £0.8 million within 'Other Comprehensive Income'.

In respect of these movements in valuation of specialised NHS assets, the Audit Committee has debated and challenged the work performed by Mazars, including their review of the work of the District Valuer.

Additionally, the Audit Committee has confirmed with management that assumptions made in determining the Trust's services and occupancy levels as at March 31, 2015 and in mapping those services onto an asset of equivalent capacity and function have not changed during the year.

The Trust has also reported a charge for impairment for the year of £3.4 million within 'Operating Expenses'. This relates mainly to capital expenditure incurred on specialised NHS assets in the year or specialised NHS assets that have been brought into use during the year and where the expenditure has not resulted in an increase in values or estimated lives of the assets.

In respect of this movement, the Audit Committee has questioned management as to the nature of the expenditure. The Audit Committee also challenged the work performed by Mazars to gain comfort that the expenditure had not resulted in any increase in value or estimated life of the asset.

After careful consideration, the Audit Committee has concluded that the adjustments to the level of impairment have been properly calculated and disclosed in the financial statements.

Provisions

The Trust has a number of legal or constructive obligations of uncertain timing or amount. Provision for these obligations is made where it is probable that there will be a future outflow of cash or other resources and where a reliable estimate can be made of the amount.

The Audit Committee has discussed with management the provisions made at March 31, 2016. The Audit Committee also challenged the work performed during the audit by Mazars to determine if the provisions were accurately calculated and complete.

After consideration, the Audit Committee was satisfied that the level of provision made in the financial statements reflects the best estimate of the economic outflow likely to occur.

Impairment of Accounts Receivable

The Trust makes provision against accounts receivables over 3 months past due unless there is a specific reason not to provide. Specific reasons include debts subsequently paid or balances where credible assurances have been received that the debts will be paid. In addition, where disputes are known, the Trust may provide for certain debts less than 3 months old.

The charge for the impairment of accounts receivables was approximately £819,000 for the year ended March 31, 2016.

The Audit Committee considered the methodology for identifying and assessing accounts receivable that may be subject to impairment and concluded that it remained appropriate.

The Audit Committee also discussed with the external auditors the work that they had performed during the audit to satisfy themselves that the provisions being made were complete and appropriate.

After consideration, the Audit Committee concluded that the provision for impairment of receivables was complete and appropriate.

Going Concern

The Audit Committee formally considered the assumptions relating the going concern basis of reporting of the financial statements. After careful analysis and debate, the Audit Committee recommended to the March 2016 Board meeting that the use of going concern basis for the preparation of the annual financial statements was appropriate.

2. Board Assurance Framework

The Audit Committee has a responsibility to ensure that the Trust's system of risk management is adequate in both identifying risks and how those risks are managed.

The Trust's principal risks and the mitigating controls are reflected in the Board Assurance Framework ('BAF'). The BAF is maintained by the Trust's Performance and Assurance group and formally reviewed by the Quality and Performance Committee ('Q&P').

The Audit Committee considered the review performed by Q&P. It questioned directly the Director of Performance and Assurance as to the system for the regular re-assessment of the principal risks and mitigating controls reflected in the BAF.

The Audit Committee also questioned directly the Head of Internal Audit to determine if the results of audits conducted to date and a comparison of the Trust's BAF to the equivalent documents in other similar organisations indicated any significant duplications or omissions in the Trust's governance systems.

Finally, the Audit Committee reviewed the Head of Internal Audit Opinion, presented to the Audit Committee in May 2016.

After careful scrutiny and consideration, the Audit Committee concluded that:

- The system of risk management is adequate in identifying risks and allowing the Board to understand the appropriate management of those risks; and
- The BAF was comprehensive and fit for purpose; and
- There were no significant omissions or duplications in the Trust's systems of governance.

3. Annual Governance Statement

The Audit Committee is required to consider the Annual Governance Statement and determine whether it is consistent with the Committee's view on the Trust's system of internal control.

During the year, a number of matters have been brought to the attention of the Audit Committee, mainly through the reports of Internal Audit. Therefore, the Audit Committee needed to formally consider these matters in forming its conclusion on the Annual Governance Statement. This was supported by other Audit Committee reviews such as of the Board Assurance Framework, Corporate Risk Register, the Head of Internal Audit Opinion and CQC registration.

After due challenge and debate, the Audit Committee concluded that the matters identified together with the remedial actions taken meant that its view on the Trust's system of internal control was consistent with the Annual Governance Statement. Accordingly, the Audit Committee supported the Board's approval of the Annual Governance Statement.

4. Clinical Audit

Clinical Audit continues to report to the Q&P and not to the Audit Committee. The Audit Committee continues to monitor the issues raised by Clinical Audit through a review of the minutes of the Q&P Meetings.

In addition, the Chair of Q&P brings to the attention of the Audit Committee any matters raised by Clinical Audit, and the proposed remedies, which impact any of the Trust's key risks as recorded in the BAF.

This ensures that the Audit Committee is aware of any key issues raised by Clinical Audit but does not add unnecessary bureaucracy, duplication or contradiction into the process.

External Audit

The Audit Committee places great importance on ensuring that there are high standards of quality and effectiveness in the Trust's external audit process.

Mazars was required to report to the Trust whether:

- The financial statements for the year have been prepared in accordance

with directions under Paragraph 25 of Schedule 7 of the National Health Service Act 2006; and

- The financial statements comply with the requirements of all other provisions contained in, or having effect under, any enactment which is applicable to the financial statements; and
- The Trust has made proper arrangements for securing economy, efficiency and effectiveness; and
- The Trust's Quality Report has been prepared in accordance with detailed guidance issued by Monitor.

In September 2015, Mazars presented the audit plan for the year to the Audit Committee. The audit plan was challenged robustly, particularly in terms of timing, resources required, impact on the Trust's day-to-day activities, areas of audit risk, interaction with internal audit and the quality and independence of the Mazars' team.

The cost of the external audit plan was proposed at £40,000 (excluding VAT). The Audit Committee challenged whether Mazars could deliver the audit plan as described for the fee proposed.

Following the challenge and debate, the Audit Committee was satisfied that the audit plan was appropriate for achieving the goals of the audit and that the proposed fee was reasonable for the audit of an entity of the size and complexity of the Trust.

Accordingly, the fee proposal was recommended by the Audit Committee to, and approved by, the Council of Governors in November 2015.

Throughout the audit process, Mazars reported to the Audit Committee, noting any issues of principle or timing identified by the audit, changes in the external auditor's assessment of risk and any significant control weaknesses or errors identified.

Mazars identified no changes in their assessment of risk nor did they identify any significant control weaknesses. The audit did identify some instances of minor misstatement. None of the misstatements identified were assessed above 'trivial'. The Trust's financial statements were adjusted for all the matters identified.

At the conclusion of the audit, the Audit Committee performed a specific evaluation of Mazars' performance with the aid of a comprehensive questionnaire and with input from the Trust's management and internal audit.

Based on the interaction with the auditor throughout the audit process and the feedback from Trust's management and internal audit, the Audit Committee has concluded that the Trust received an effective and cost-efficient audit for the year.

The Trust has a policy in place for non-audit services provided by External Audit, which has been approved by the Council of Governors. External Audit has not been asked to provide any non-audit services during the year.