NORTH MIDDLESEX UNIVERSITY HOSPITAL NHS TRUST

ANNUAL AUDIT LETTER
Audit for the year ended 31 March 2016

28 June 2016

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EXECUTIVE SUMMARY

Purpose of the letter
This Annual Audit Letter summarises the key issues arising from the work that we have carried out in respect of the year ended 2015/16. It is addressed to the Trust but is also intended to communicate the key findings we have identified to key external stakeholders and members of the public. It will be published on the website of Public Sector Audit Appointments Limited.

Responsibilities of auditors and the Trust
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.

Our responsibility is to plan and carry out an audit that meets the requirements of the NAO’s Code of Audit Practice (the Code), and to review and report on:

• the Trust’s financial statements
• whether the Trust has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We are also required to review and report on the governance statement, annual report, remuneration report and the accounts summarisation schedules.

We also undertake a review of the Trust’s Quality Account, to confirm that it has been prepared in line with requirements and to test two performance indicators.

We recognise the value of your co-operation and support and would like to take this opportunity to express our appreciation for the assistance and co-operation provided during the audit.

Audit conclusions

FINANCIAL STATEMENTS
We issued an unqualified true and fair opinion on the financial statements on 1 June 2016.

We reported our detailed findings to the Audit Committee on 26 May.

USE OF RESOURCES
The financial outturn for 2015/16 was an £8.3 million deficit, reflecting a significant deterioration compared to the budgeted position. In addition, the Trust has forecast a deficit of £6.3 million for 2016/17. The deterioration in the Trust’s finances occurred due to being unable to deliver additional timely savings to mitigate the impact of the reduction in budgeted income and additional cost pressures.

As a result, we issued a qualified conclusion on the Trust’s arrangements for securing economy, efficiency and effectiveness in its use of resources on 1 June 2016 to report that these issues are evidence of weaknesses in proper arrangements for the financing of sustainable delivery of services.

QUALITY ACCOUNT
We reported our detailed findings in a separate report and issued an unqualified assurance report on the Quality Account on 28 June 2016.

BDO LLP
28 June 2016
FINANCIAL STATEMENTS

OPINION
We issued an unqualified true and fair opinion on the financial statements on 1 June 2016.

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error.

This includes an assessment of whether the accounting policies are appropriate to the Trust’s circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates, and the overall presentation of the financial statements.

Our assessment of risks of material misstatement
Our audit was scoped by obtaining an understanding of the Trust and its environment, including the system of internal control, and assessing the risks of material misstatement in the financial statements.

We set out below the risks that had the greatest effect on our audit strategy, the allocation of resources in the audit, and directing of the efforts of the audit team.

<table>
<thead>
<tr>
<th>REVENUE RECOGNITION AND NHS INCOME</th>
<th>RESPONSE</th>
<th>FINDINGS</th>
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</thead>
<tbody>
<tr>
<td>The agreement of balances process is designed to ensure that NHS commissioners and providers agree the outturn expenditure (payables) and income (receivables) under the NHS contracts. However, this process often generates differences between both parties either through misallocated transactions, disputes, cash timing differences or other discrepancies. There is a risk that NHS income is not accurately recorded where there are unreconciled differences between the Trust and NHS commissioners.</td>
<td>We reviewed the process for resolving discrepancies between the Trust and NHS commissioners through the agreement of balances process, and management’s estimate of amounts receivable where there are contract disputes. We reviewed significant contracts with other NHS bodies to form expectations for income and expenditure, and challenged management where variations exist.</td>
<td>Our review of the agreement of balances process for NHS income (and receivables) did not identify any material differences with other NHS bodies. The updated agreement of balances mismatches report provided by the Department of Health indicated that the Trust had recognised net £0.336 million more income than the NHS counterparties had recognised as expenditure. We have investigated a sample of the non-material differences with other NHS bodies and concluded that Trust’s reported transactions and balances are appropriate. These included the Trust recognising £0.484 million more income against London Commissioning Hub, £0.228 million more income against NHS Barnet CCG, and reducing income by £0.552 million for potential refunds for SLA under performance using the generic non contracted activity code.</td>
</tr>
</tbody>
</table>
NHS trusts are required to ensure that the carrying value of property, plant and equipment (PPE) is not materially different to the fair value at the balance sheet date.

A full valuation of land and buildings was obtained at 31 March 2015 and management reviewed the potential valuation movements to 31 March 2016 using available indices and concluded that there had been no material movement in valuations. There is a risk over the valuation of land and buildings where valuations are based on assumptions or where updated valuations have not been provided for a class of assets at year end.

We reviewed the work undertaken by management to ensure that asset values reported at 31 March 2016 are materially accurate. We reviewed available indices of movements in building tender prices and land valuations. We also reviewed the basis of valuation of significant building assets.

We confirmed that the basis of valuation for assets is appropriate based on their usage. We have confirmed that an instant build modern equivalent asset basis has been used for assets valued at depreciated replacement cost (DRC).

We reviewed valuations against indices of price movements for similar classes of assets and followed up valuation movements that appear unusual against indices. This suggested that buildings valued using DRC had increased by a material amount and management obtained information from RICS for NHS tender price movements and subsequently applied an increase of 2.9% for buildings.

<table>
<thead>
<tr>
<th>VALUATION OF LAND AND BUILDINGS</th>
<th>RESPONSE</th>
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<tr>
<td>NHS trusts are required to ensure that the carrying value of property, plant and equipment (PPE) is not materially different to the fair value at the balance sheet date. A full valuation of land and buildings was obtained at 31 March 2015 and management reviewed the potential valuation movements to 31 March 2016 using available indices and concluded that there had been no material movement in valuations. There is a risk over the valuation of land and buildings where valuations are based on assumptions or where updated valuations have not been provided for a class of assets at year end.</td>
<td>We reviewed the work undertaken by management to ensure that asset values reported at 31 March 2016 are materially accurate. We reviewed available indices of movements in building tender prices and land valuations. We also reviewed the basis of valuation of significant building assets.</td>
<td>We confirmed that the basis of valuation for assets is appropriate based on their usage. We have confirmed that an instant build modern equivalent asset basis has been used for assets valued at depreciated replacement cost (DRC). We reviewed valuations against indices of price movements for similar classes of assets and followed up valuation movements that appear unusual against indices. This suggested that buildings valued using DRC had increased by a material amount and management obtained information from RICS for NHS tender price movements and subsequently applied an increase of 2.9% for buildings.</td>
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</table>
Our application of materiality

We apply the concept of materiality both in planning and performing our audit, and in evaluating the effect of misstatements. We consider materiality to be the magnitude by which misstatements, including omissions, could influence the economic decisions of reasonably knowledgeable users that are taken on the basis of the financial statements.

Importantly, misstatements below these levels will not necessarily be evaluated as immaterial as we also take account of the nature of identified misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements as a whole.

The materiality for the financial statements as a whole was set at £3.5 million. This was determined with reference to a benchmark of gross expenditure (of which it represents 1.5 per cent) which we consider to be one of the principal considerations for the Trust in assessing the financial performance.

We agreed with the Audit Committee that we would report all individual audit differences in excess of £70,000.

Audit differences

All identified misstatements were corrected by management in the financial statements and there were no remaining uncorrected misstatements.

Summarisation schedules return

We are required to provide an opinion to the Trust to confirm that the financial information included in its accounts summarisation schedules return (and used in the preparation of the Group consolidation) is consistent with the audited financial statements.

We reported the summarisation schedule was consistent with the financial statements.
FINANCIAL STATEMENTS
Continued

Governance statement
The governance statement was not inconsistent or misleading with other information we were aware of from our audit of the financial statements, the evidence provided in the Trust’s review of effectiveness and our knowledge of the Trust.

Annual report
The annual report was not inconsistent or misleading with the financial statements or with our knowledge acquired in the course of our audit.

Remuneration report
The auditable parts of the remuneration report were found to have been properly prepared in accordance with the requirements directed by the Secretary of State.

Internal controls
We did not find any significant deficiencies in internal controls during the course of our audit. A number of other areas for improvement were identified which we have discussed with management.
Scope of the audit of use of resources

We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources based on the following reporting criterion:

• In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

As part of reaching our overall conclusion we consider the following sub criteria in our work: informed decision making, sustainable resource deployment, and working with partners and other third parties.

Our assessment of significant risks

Our audit was scoped by our cumulative knowledge brought forward from previous audits, relevant findings from work undertaken in support of the opinion on financial statements, reports from the Trust including internal audit, information disclosed or available to support the governance statement and annual report, and information available from the risk registers and supporting arrangements.

We set out on the following page the risks that had the greatest effect on our audit strategy, the allocation of resources in the audit, and directing of the efforts of the audit team.
USE OF RESOURCES
Continued

<table>
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<tr>
<th>SUSTAINABLE FINANCES</th>
<th>RESPONSE</th>
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<td>The Trust is facing challenging financial pressures. It had budgeted for breakeven in 2015/16 but reported a deficit of £8.3 million, with an underlying position of £10.3 million after the removal of some non-recurrent items. The Trust is forecasting a £6.3 million deficit for 2016/17 after taking into account the £9.4 million Cost Improvement Programme (CIP) target.</td>
<td>We investigated the reasons for the worsening financial performance, and tested the assumptions on 2016/17 performance and planned CIPs. We considered the actions the Trust is taking to address the issues, and reflected on the action taken in the previous year to inform the assessment of how achievable current plans are.</td>
<td>The deficit in 2015/16 was mainly due to non-achievement of national targets which led to SLA fines, failure to control agency spend in response to performance issues and failure to deliver all CIP schemes. The Trust achieved CIP savings of £5.7 million against a plan of £8.4 million. The reasons for this included the pressure faced by A&amp;E which resulted in less focus on CIP delivery, and instability in the management of CIP which meant there was a lack of continuity. The CIP planning process was not fully robust, and so some targets were unrealistic. The Trust’s was unable to deliver additional timely savings to mitigate the impact of the reduction in budgeted income and additional cost pressures. The CIP target for 2016/17 is ambitious and will be challenging. However, there is an improved approach to CIP identification and a more robust planning process after learning from previous failings. As a result of the planned deficit in 2016/17 and weaknesses in the arrangements for the financing of sustainable delivery of services, we issued a qualified conclusion on the Trust’s arrangements for securing economy, efficiency and effectiveness in its use of resources.</td>
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</table>
We issued an unqualified assurance report on the Quality Account on 28 June 2016.

Scope of the review of the Quality Account

Our responsibility is to form a conclusion, based on limited assurance procedures, on whether anything has come to our attention that causes us to believe that:

- the Quality Account is not prepared in line with the criteria set out in the Regulations
- the Quality Account is not consistent with the sources specified in the NHS Quality Accounts Auditor Guidance
- the two performance indicators subject of limited assurance review are not reasonably stated in all material respects in accordance with the Regulations and the six dimensions of data quality set out in the Guidance.

Specified indicators for testing

The core set of indicators to be included in 2015/16 Quality Account is set out in Regulations and the letter from NHS England dated 3 February 2016. The Auditor Guidance has not been updated since 2014/15, and requires that we selected two indicators for testing from the following list:

- Percentage of patients risk-assessed for venous thromboembolism (VTE)
- Rate of clostridium difficile infections
- Percentage of patient safety incidents resulting in severe harm or death
- Friends and Family Test patient element score.

<table>
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<tr>
<th>REQUIREMENTS</th>
<th>RESPONSE</th>
<th>FINDINGS</th>
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<tbody>
<tr>
<td>Review the content of the report and consistency with specified documents.</td>
<td>We reviewed the Quality Account against the publication requirements of the various Regulations and other good practice guidance. We read the information included in the Quality Account and considered whether it was materially inconsistent with information specified by the guidance.</td>
<td>The Quality Account has been prepared in line with the Regulations and is not materially inconsistent with our review of the information we are required to consider. We reported to management where there were omissions or where additional information and disclosure were required to comply with the guidance issued by NHS England. The Trust has amended the Quality Account to reflect our recommended changes.</td>
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</table>
### QUALITY ACCOUNT
Continued

<table>
<thead>
<tr>
<th>REQUIREMENTS</th>
<th>RESPONSE</th>
<th>FINDINGS</th>
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</thead>
<tbody>
<tr>
<td>Testing of rate of C. difficile infection.</td>
<td>We undertook testing to:</td>
<td>We tested 20 cases, including 15 negative results and 5 positive results, included in the indicator and confirmed that each was supported by the C. difficile test results.</td>
</tr>
</tbody>
</table>
| The Trust reported performance of 37 (28.2 per 100,000 bed days), against a target of 34 in the Quality Account. | • confirm the definition and guidance used by the Trust to calculate the indicator  
• document and walk through the Trust’s systems used to produce the indicator  
• undertake substantive testing on the underlying data against six specified data quality dimensions. | We found no issues in respect of the accuracy of the data used in the calculation and no incomplete or missing evidence to support that data. |
| Testing of patients who would recommend (as extremely likely or likely) the Trust to their family or friends. | We undertook testing to:                                                  | We tested a sample of the entries included in the Trust’s dataset for the categorisation of responses back to the source of the responses, which confirmed that the data had been correctly transferred from the source to the dataset used for the calculation of the reported performance. |
| The Trust reported A&E performance of Q1 85%, Q2 84% and Q3 63%.            | • confirm the definition and guidance used by the Trust to calculate the indicator  
• document and walk through the Trust’s systems used to produce the indicator  
• undertake substantive testing on the underlying data against six specified data quality dimensions. | Our testing of a sample of entries recorded in the dataset used to calculate the indicator confirmed that the dataset was appropriately recording the results from the source for responses. |
| The Trust reported inpatients performance of Q1 92%, Q2 96% and Q3 93%.     | We note that the Trust had set a local improvement priority for 2015/16 for improving family and friends test scores from 2014/15 baseline, but had used an assessment based on the number of people recommending as extremely likely, rather than the assessment in the national indicator as extremely likely or likely, and that the Trust had under performance against both the A&E and inpatients targets. | |
Reports issues
We issued the following reports in respect of the 2015/16 financial year.

<table>
<thead>
<tr>
<th>REPORT</th>
<th>DATE</th>
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<tbody>
<tr>
<td>Planning letter</td>
<td>28 April 2015</td>
</tr>
<tr>
<td>Audit Plan</td>
<td>29 February 2016</td>
</tr>
<tr>
<td>Final audit report</td>
<td>26 May 2016</td>
</tr>
<tr>
<td>Quality Account</td>
<td>28 June 2016</td>
</tr>
<tr>
<td>Annual Audit Letter</td>
<td>28 June 2016</td>
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</tbody>
</table>

Fees
We reported our original fee proposals in our Audit Plan. We have not had to amend our planned fees.

<table>
<thead>
<tr>
<th>AUDIT AREA</th>
<th>PLANNED FEES</th>
<th>FINAL FEES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Code audit</td>
<td>58,781</td>
<td>58,781</td>
</tr>
<tr>
<td>Non audit service fees</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Quality Account review</td>
<td>10,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Total</td>
<td>68,781</td>
<td>68,781</td>
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The matters raised in our report prepared in connection with the audit are those we believe should be brought to the attention of the organisation. They do not purport to be a complete record of all matters arising. No responsibility to any third party is accepted.

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