The Annual Audit Letter for North Cumbria University Hospitals NHS Trust

Year ended 31 March 2015
July 2015

Jackie Bellard
Director
T 0161 234 6394 or 07880 456195
E jackie.bellard@uk.gt.com

Richard McGahon
Senior Manager
T 0141 223 0889 or 07880 456156
E richard.a.mcghahon@uk.gt.com

Richard Robinson
Assistant Manager
T 0141 223 0888
E richard.robinson@uk.gt.com
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Section 1: Executive summary

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Executive summary

Purpose of this Letter
Our Annual Audit Letter (Letter) summarises the key findings arising from the following work that we have carried out at North Cumbria University Hospitals NHS Trust (the Trust) for the year ended 31 March 2015:
• auditing the accounts (Section two)
• assessing the Trust’s arrangements for securing economy, efficiency and effectiveness in its use of resources (Section three)
• other audit related services carried out for the Trust during the years reviewing the Trust’s Quality Account (Sections four).

The Letter is intended to communicate key messages to the Trust and external stakeholders, including members of the public.

We reported the detailed findings from our audit work on the accounts and arrangements for securing economy, efficiency and effectiveness in its use of resources to those charged with governance in the Audit Findings Report on 2 June 2015 and reported the detailed findings from our work on the Trust’s Quality Account in our separate Quality Account Report on 30 June 2015.

Responsibilities of the external auditors and the Trust
This Letter has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission (wwwaudit-commission.gov.uk).

The Trust is responsible for preparing and publishing its financial statements, accompanied by an Annual Governance Statement. It is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources (Value for Money).

Our annual work programme, which includes nationally prescribed and locally determined work, has been undertaken in accordance with our Audit Plan issued on 18 May 2015 and was conducted in accordance with the Audit Commission’s Code of Audit Practice (the Code), International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

Audit conclusions
The audit conclusions which we have provided in relation to 2014/15 are as follows:
• an unqualified opinion on the accounts which give a true and fair view of the Trust’s financial position as at 31 March 2015 and the Trust income and expenditure for the year. Our opinion also included:
  ➢ An 'Emphasis of Matter' paragraph in respect of going concern and the uncertainty about the date of the Trust’s planned acquisition by Northumbria Healthcare NHS Foundation Trust and the future organisational form of the Trust.
  ➢ an explanation that the audit certificate was delayed until we have completed our consideration of the Trust’s documented response on its compliance with procurement requirements.

We were satisfied that these matters did not have a material effect on the financial statements or a significant impact on our value for money conclusion so we were able to issue our opinion on the accounts on 4 June in line with the deadline set by the Department of Health.
Executive summary (continued)

• a qualified adverse conclusion in respect of the Trust's arrangements for securing economy, efficiency and effectiveness in its use of resources as a result of the following factors:

  ➢ the Trust delivered a deficit of £16.4 million in 2014/15 and is projecting a deficit of £42.5 million for 2015/16 and a further deficit in 2016/17. The deficit plans include the provision of additional cash support
  ➢ the Trust has not achieved its Cost Improvement Plan for 2014/15, delivering £6.9 million of savings against a plan of £11.0 million
  ➢ the Trust has not achieved the Better Payment Practice Code (BPPC) target in 2014/15 as a result of cashflow problems
  ➢ in 2013 a review led by Sir Bruce Keogh, the Medical Director of NHS England, identified shortcomings in the quality of care delivered by the Trust and the Trust was placed under a special measures regime. The Trust was re-inspected by the Chief Inspector of Hospitals in April 2014 but remained in Special Measures and is awaiting the outcome of a further re-inspection by the Chief Inspector of Hospitals
  ➢ the Trust does not have a fully costed clinical strategy and service line reporting is not sufficiently embedded to be used to support routine decision making
  ➢ the Trust did not have adequate arrangements in place to ensure that contracts always represented best value for money or had been properly approved in accordance with the standing financial instructions in 2014/15.

• We also issued a qualified limited assurance report in respect of the Trust’s Quality Account in relation to this separate engagement because the indicator reporting the percentage of patients risk-assessed for venous thromboembolism (VTE) did not meet the data quality requirements.

Key areas for Trust attention
Issues which came to our attention during our audit which we draw to the Board's attention are:

• the Trust is budgeting for a deficit of £42.5 million for 2015/16. This includes a cost improvement plan to save £10 million which represents a significant challenge for the Trust and will need to be closely monitored
• at 30 June 2015 the Trust had still not agreed with Cumbria Clinical Commissioning Group (CCG) the final position on its performance against the 2014/15 CQUIN targets or agreed targets for 2015/16. Agreeing the final outturn position for the year in a reasonable timescale ensures that attention can be turned to, agreeing CQUIN targets for the next year, and putting in place arrangements to achieve these targets;
• the Trust identified the need to take action on non-compliance with fire regulations at the Cumberland Infirmary, Carlisle (PFI Hospital) which gave rise to a material impairment in the value in the accounts. Ensuring patient safety in these circumstances is the Trust's priority but the Board also needs to ensure the cost of the rectification work is identified recovered where appropriate and does not impact on the already challenging financial position;
• the need to ensure the Trust's draft accounts are supported by its documented consideration of the key critical judgements and accounting treatments for material or significant figures in the draft accounts. In 2014/15 the Trust's failure to do so has led to a significant additional fee;
• the outcome of the inspection by the Chief Inspector of Hospitals is due soon and will determine whether the Trust will be removed from Special Measures. Whatever the outcome of this inspection the Trust needs to continue its work with Northumbria Healthcare NHS Foundation Trust to secure financially sustainable service delivery;
Executive summary (continued)

• the Trust identified that it needed to make improvements in its procurement processes and joined a shared service in January 2015. This should mean that the Trust has a more planned and timely approach to contracting which are key to getting value for money
• the Trust’s performance against the Better Payment Practice Code (BPPC) improved slightly in 2014/15 but as the Trust’s cashflow position improves in 2015/16 the Trust needs to ensure improvements in BPPC are achieved;
• the Trust needs to finalise its clinical strategy and ensure that this is fully costed.

Acknowledgements
This Letter has been agreed with the Director of Finance.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Trust’s staff.

Grant Thornton UK LLP
July 2015
Section 2: Audit of the accounts

01. Executive summary
02. Audit of the accounts
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Audit of the accounts

The key findings of our audit of the accounts are summarised below:

Preparation of the accounts
The Trust presented us with draft accounts in accordance with the national deadline. Unfortunately, this did not include the Trust’s consideration of a number of key critical judgements and accounting treatments for material or significant figures in the draft accounts such as £5 million assumed insurance proceeds for the Whitehaven fire damage. Trying to obtain this information was very time consuming and significantly impacted on the amount of senior audit staff time on the audit in pursuing this information, and consideration within the firm of the impact the lack of this information on our audit opinion. The additional cost is reflected in our additional audit fee for 2014/15.

Issues arising from the audit of the accounts
We have identified four adjustments affecting the Trust’s Statement of Comprehensive Income (SOCI). The only material adjustment has been an impairment of the PFI hospital, Carlisle of £13.8 million. Overall the four adjustments have only a trivial impact on the Trust’s reported deficit position for 2014/15. (The impact of the impairment of the PFI hospital building is adjusted to report against the Department of Health financial target which was a deficit of £16.4 million). Due to the nature of these adjustments these have impacted on the Statement of Financial Position (SOFP), Statement of Changes in Taxpayers Equity (SOCITE) and the Statement of Cashflows (SCF). We have also made a number of adjustments to improve the presentation of the financial statements.

The key messages arising from our audit of the Trust’s financial statements are:
- The PFI hospital, Carlisle has been impaired by £13.8 million to reflect the issues with fire compartments
- Presentational change on SOCI to show Property, plant and equipment: impairments and revaluations separately between upward and downward movements
- Additional disclosures made in ‘Critical judgements’ to explain the Trust’s assessment that the accounts should be prepared on a going concern basis
- There is one unadjusted error of £1.972 million.

Annual Governance Statement and Annual Report
The Annual Governance Statement was prepared in reasonable time and was subject to scrutiny by the Audit Committee. Amendments were made to it to provide more detail on deficit position in 2014/15 and future budgeted deficits. Additional disclosure was also made about the non-compliance with fire regulations at the Cumberland Infirmary (the PFI Hospital). The Annual Report was prepared later and a number of amendments were required to ensure its contents agreed with the requirements and other key documents.

Conclusion
Prior to giving our opinion on the accounts, we are required to report significant matters arising from the audit to ‘those charged with governance’ (defined as the Audit Committee at the Trust). We presented our report to the Audit Committee on 2 June 2015 and summarise only the key messages in this Letter.
We issued an unqualified opinion on the Trust’s 2014/15 accounts on 4 June 2015, meeting the deadline set by the Department of Health (DH). Our opinion confirms that the accounts give a true and fair view of the Trust’s financial affairs and of the income and expenditure recorded by the Trust. Our opinion also included an 'Emphasis of Matter' paragraph in respect of going concern and the uncertainty around the date of acquisition of the Trust by Northumbria Healthcare NHS Foundation Trust. We have not issued our audit certificate until we have considered the documented response the Trust is to provide on its compliance with procurement requirements.

**Financial performance 2014/15**
The Trust’s Performance against its financial targets is set out in the table below:

<table>
<thead>
<tr>
<th>Target</th>
<th>Actual</th>
<th>Met?</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Surplus/ (deficit)</strong></td>
<td>Breakeven</td>
<td>No</td>
</tr>
<tr>
<td><strong>Capital cost absorption rate</strong></td>
<td>3.5%</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Capital resource limit</strong></td>
<td>Not to exceed £34.622 million</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>External finance limit</strong></td>
<td>Not to exceed £42.682 million</td>
<td>Yes</td>
</tr>
</tbody>
</table>

**Looking forward**
The Trust is budgeting for a deficit of £42.5 million for 2015/16. This includes a cost improvement plan to save £10 million. The Trust will need at least £52.5 million of distress funding in 2015/16 to help it meet working capital requirements.

The Trust is currently awaiting the outcome of an inspection by the Chief Inspector of Hospitals that could determine whether the Trust will be removed from Special Measures. The Trust is working towards being acquired by Northumbria Healthcare NHS Foundation Trust to secure financially sustainable service delivery but this will not proceed until the Trust is removed from the special measures regime.
Section 3: Value for Money
Value for Money

**Value for Money conclusion**
The Code describes the Trust's responsibilities to put in place proper arrangements to:

- secure economy, efficiency and effectiveness in its use of resources
- ensure proper stewardship and governance
- review regularly the adequacy and effectiveness of these arrangements.

We are required to give our VfM conclusion based on the following two criteria specified by the Audit Commission which support our reporting responsibilities under the Code:

The Trust has proper arrangements in place for securing financial resilience. The Trust has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.

The Trust has proper arrangements for challenging how it secures economy, efficiency and effectiveness. The Trust is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

**Key findings**

**Securing financial resilience**
We have undertaken a review which considered the Trust's arrangements against the three expected characteristics of proper arrangements as defined by the Audit Commission:

- Financial governance
- Financial planning
- Financial control.

Our work highlighted that the Trust is not financially resilient. It reported a £16.4 million deficit in 2014/15. This was only achieved after significant 'One off' items were brought into account including £12 million from NHS England to support healthcare delivery in distressed trusts, £5 million income to compensate for the fire at the Energy Centre, Whitehaven and £1.97 million reduction in the payment to the PFI provider. The Trust also required £45 million funding in the form of permanent public dividend capital of which £17.9 million was for revenue. The budget for 2015/16 shows a significant deficit of £42.5 million is expected with £52.5 million of distress funding and there is no robust projection for 2016/17 although this will also be a deficit.

The Trust did not meet any of the four targets for the Better Payments Practice Code (BPPC). Performance against the BPPC targets has improved in some areas in 2014/15 but the Trust's on-going liquidity problems mean it will continue to be unable to pay all their suppliers within 30 days. Only 60% of the value of Non-NHS invoices paid within target.

**Challenging economy, efficiency and effectiveness**
We have reviewed whether the Trust has prioritised its resources to take account of the tighter constraints it is required to operate within and whether it has achieved cost reductions and improved productivity and efficiencies.

Our work highlighted that the Trust only achieved a CIP of £6.9 million (63%) against the required £11.0 million although it has introduced new project management arrangements to help the in year delivery of the CIP. Service Line Reporting (SLR) has improved and been refined during the year and although some evidence of it being used to support decision making limited progress on the routine production and embedding of SLR reporting. Progress made on consulting on the options for a clinical strategy but this will then needed to be costed.
The Trust self assessment against it Chief Inspector of Hospitals improvement plan showed that by the 31 March 2015 58% of the ‘Must do’ items would be delivered and 75% of the ‘Should do’ items but acknowledges some will require longer term solutions. The outcome of the inspection at the end of March 2015 by the Chief Inspector of Hospitals is due soon and will determine whether the Trust will be removed from Special Measures. Whatever the outcome of this inspection the Trust needs to continue its work with Northumbria Healthcare NHS Foundation Trust to secure financially sustainable service delivery.

We identified that procurement procedures were not always complied with for consultancy contracts. We also observed from our attendance at Audit Committee meetings that there were a large number of contract waivers. The Trust identified that it needed to make improvement in its procurement processes and joined a shared service in January 2015.

Overall VfM conclusion
On the basis of our work, and having regard to the guidance on the specified criteria published by the Audit Commission, the matters reported in the basis for adverse qualification paragraph above prevent us from being satisfied that in all significant respects North Cumbria University Hospitals NHS Trust put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2015.

Adverse Value for Money conclusion
In considering the Trust’s arrangements for securing financial resilience, we identified the following matters:

- The Trust has not achieved its Cost Improvement Plan for 2014/15, delivering £6.9 million of savings against a plan of £11.0 million.
- The Trust has not achieved the Better Payment Practice Code (BPPC) target in 2014/15 as a result of cashflow problems.

These issues are evidence of weakness in arrangements in respect of the Trust's strategic financial planning, financial governance and financial control.

In considering the Trust's arrangements for challenging how it secures economy, efficiency and effectiveness, we identified the following matters:

- In 2013 a review led by Sir Bruce Keogh, the Medical Director of NHS England, identified shortcomings in the quality of care delivered by the Trust and the Trust was placed under a special measures regime. The Trust was re-inspected by the Chief Inspector of Hospitals in April 2014 but remained in Special Measures and is awaiting the outcome of a further re-inspection by the Chief Inspector of Hospitals.
- The Trust does not have a fully costed clinical strategy and service line reporting is not sufficiently embedded to be used to support routine decision making.
- The Trust did not have adequate arrangements in place to ensure that contracts always represented best value for money and had been properly approved in accordance with the standing financial instructions.

The issues identified constitute evidence of weakness in arrangements in prioritising resources and improving efficiency and productivity.
Section 4: Audit related services

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Audit related services

**Quality Accounts**
For 2014/15 the Trust is required to obtain external audit assurance on its Quality Account. In order to provide this assurance we have undertaken limited assurance procedures in accordance with guidance issued by the Audit Commission to assess whether:

* the Quality Account is prepared in all material respects in line with the criteria set out in the Regulations
* the Quality Account is consistent in all material respects with the sources specified in the NHS Quality Accounts Auditor Guidance 2014/15 issued by the Audit Commission (‘the Guidance’)
* the indicators in the Quality Account identified as having been the subject of limited assurance, are reasonably stated in all material respects in accordance with the Regulations and the six dimensions of data quality set out in the Guidance.

**Key findings**
We provided the Trust with a report setting out the detailed findings of our work on 28 June 2015. The key matters arising from our work are:

* the draft Quality Account report for 2014/15 was available for external consideration from 8 May 2015 which was a week earlier than last year and responses have been received from stakeholders, considered by the Trust and included in the Quality Account
* the draft Quality Account did not include a number of disclosures and some of the commentary on performance had not been updated since 2013/14. For the 2015/16 Quality Account the Trust will need to ensure that its draft Quality Account for stakeholder consultation is more complete to make it easier for stakeholders to undertake a meaningful and informed review of the Trust's quality performance

* there is a need to improve arrangements to ensure that information sources, both internal and external, are regularly checked throughout the process so that the Quality Account includes the most up to date information
* priority improvements for 2015/16 lacked SMART (Specific, Measurable, Achievable, Relevant, Time bound) targets making it difficult for the Trust to carry out robust monitoring of progress and assess success
* we qualified the indicator for the percentage of patients risk-assessed for venous thromboembolism (VTE) as it was based on patients discharged rather than admitted as required by the definition
* there is a greater need to provide context on how the Trust has performed compared with other trusts in respect of the national staff survey
* the Trust needs to ensure that the performance on CQUIN targets for the reporting year, and targets for the following year, have been agreed within a reasonable timescale so that these can be reported in the final Quality Account
* the Trust needs to ensure there is a process in place to identify and consider whether emerging issues need to be disclosed e.g. the PFI Hospital and fire compartments compliance and the Trust now being part of the 'Success Regime'.

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Conclusions
We provided a qualified limited assurance opinion on the Trust’s Quality Account, in accordance with requirements, on 30 June 2015 because the indicator reporting the percentage of patients risk-assessed for venous thromboembolism (VTE) did not meet the six dimensions of data quality in the following respects:

* **Accuracy and Validity** - the Trust calculated the indicator based on patients discharged in the reporting period rather than those admitted, consequently the Trust cannot demonstrate that the correct numerator and denominator have been used;

* **Relevance** – the data used to calculate the indicator incorrectly included patients that did not meet the definition for inclusion and incorrectly excluded patients that should have been risked assessed for VTE in 2014/15;

* **Completeness** – as a result of the Trust basing the indicator on those patients discharged in 2014/15 rather than those admitted in 2014/15 some patients will be incorrectly included in the indicator and other patients will be incorrectly excluded from the indicator. We are therefore unable to conclude whether the number of VTE assessments and the number of adult inpatient admissions used to calculate the indicator are complete.
Appendices
Appendix A: Reports issued and fees

We confirm below our final fees charged for the audit and non-audit services.

**Fees for audit services**

<table>
<thead>
<tr>
<th>Service</th>
<th>Per Audit plan £</th>
<th>Actual fees £</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust audit</td>
<td>90,060</td>
<td>124,734</td>
</tr>
<tr>
<td>Charitable fund audit</td>
<td>4,260</td>
<td>To be agreed</td>
</tr>
<tr>
<td><strong>Total audit fees</strong></td>
<td><strong>94,320</strong></td>
<td><strong>To be agreed</strong></td>
</tr>
</tbody>
</table>

**Charitable fund audit fee**

The Charitable Funds for 2014/15 are within the limits that allow us to undertake an independent examination rather than a full audit. We have agreed we will undertake an independent examination and although the fee will be lower we have still to agree the fee.

**Fees for other services**

<table>
<thead>
<tr>
<th>Service</th>
<th>Fees £</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit related services</td>
<td></td>
</tr>
<tr>
<td>- Quality Accounts</td>
<td>10,000</td>
</tr>
<tr>
<td>Non-audit related services</td>
<td>Nil</td>
</tr>
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</table>

**Reports issued**

<table>
<thead>
<tr>
<th>Report</th>
<th>Date issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit Plan</td>
<td>May 2015</td>
</tr>
<tr>
<td>Audit Findings Report</td>
<td>June 2015</td>
</tr>
<tr>
<td>Quality Account Report</td>
<td>June 2015</td>
</tr>
<tr>
<td>Annual Audit Letter</td>
<td>July 2015</td>
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</table>

An additional fee will be charged for the audit due a significant increase in the work required by ourselves so that we could give our opinion on the 2014/15 accounts. This included:

- the impact of the breaches of the Standing Financial Instructions (SFIs) in terms of seeking assurances and needing to undertake additional work on purchasing contracts
- additional meetings with the Audit Committee Chairs and Senior Officers at the Trust
- trying to obtain the Trust's documented consideration of a number of key critical judgements and accounting treatments for material or significant figures in the draft accounts
- work on the late material adjustment to impair the Cumberland Infirmary, Carlisle (PFI hospital) by £13.8 million to reflect the issues with fire compartments
- meetings to consider whether we needed to qualify the audits or delay the opinion
- needing to have a Peer Reviewer to reflect the increased risk on the audit

All of these issues required significant input from our senior staff.