



Annual Audit Letter

Tees, Esk and Wear Valleys NHS Foundation
Trust

Year ended 31 March 2020





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Reports and letters prepared by the auditor and addressed to the Foundation Trust are prepared for the sole use of the Foundation Trust and we take no responsibility to any member or officer in their individual capacity or to any third party.

1. EXECUTIVE SUMMARY

Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor for Tees, Esk and Wear Valleys NHS Foundation Trust (the Trust) for the year ended 31 March 2020. Although this letter is addressed to the Trust, it is designed to be read by a wider audience including members of the public and other external stakeholders.

Our responsibilities are defined by the NHS Act 2006 (the 2006 Act) and the Code of Audit Practice issued by the National Audit Office (the NAO). The detailed sections of this letter provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

Area of responsibility	Summary
Audit of the financial statements	Our auditor's report issued on 24 June 2020 included our opinion that the financial statements give a true and fair view of the Trust's financial position as at 31 March 2020 and of its financial performance for the year then ended.
Value for Money conclusion	Our auditor's report stated that we had no matters to report in respect of the Trust's arrangements to secure economy, efficiency and effectiveness in its use of resources.
Reporting to the group auditor	In line with group audit instructions issued by the NAO, on 24 June 2020 we reported that the Trust's consolidation schedules were consistent with the audited financial statements.
Statutory reporting	Our auditor's report confirmed that we did not use our powers under schedule 10 of the 2006 Act to issue a report in the public interest, or make a referral to the regulator.
Quality Report	Due to the impact of the COVID-19 pandemic, NHS Improvement issued guidance in March 2020 that external assurance work on the Trust's Quality Report should not be undertaken for 2019/20, and any testing underway should stop. As such, we did not complete this work in 2019/20 and there are no findings to report.

2. AUDIT OF THE FINANCIAL STATEMENTS

Opinion on the financial statements

Unqualified

The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the financial reporting framework applicable to the Trust and whether they give a true and fair view of the Trust's financial position as at 31 March 2020 and of its financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by the NAO, and International Standards on Auditing (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the Trust's circumstances and have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and
- the overall presentation of the financial statements provides a true and fair view.

Our auditor's report, issued to the Trust on 24 June 2020, stated that, in our view, the financial statements give a true and fair view of the Trust's financial position as at 31 March 2020 and of its financial performance for the year then ended.

Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider the concept of materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for specific items of account (specific materiality) due to the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Audit and Risk Committee. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 March 2020:

Financial statement materiality	Our financial statement materiality is based on 2% of Gross Operating Expenditure, adjusted for impairments.	£7.466 million
Trivial threshold	Our trivial threshold is based on 3 % of financial statement materiality.	£0.224 million
Specific materiality	We have applied a lower level of materiality to the following areas of the accounts: - Director's remuneration	1 band

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2. AUDIT OF THE FINANCIAL STATEMENTS

Our response to significant risks and key audit matters

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the Trust's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit and Risk Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report.

Key audit matters are defined as those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

The table below outlines the identified significant risks and key audit matters, the work we carried out on these, and our conclusions.

Identified significant risk	Key audit matter?	Our response	Our findings and conclusions
<p>Management override of controls</p> <p>In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.</p>	No	<p>We addressed this risk through performing audit work over:</p> <ul style="list-style-type: none"> Accounting estimates impacting on amounts included in the financial statements; Consideration of identified significant transactions outside the normal course of business; and Journals recorded in the general ledger and other adjustments made in preparation of the financial statements. 	Our work provided the assurance we sought.

2. AUDIT OF THE FINANCIAL STATEMENTS

Identified significant risk	Key audit matter?	Our response	Our findings and conclusions
<p>Revenue recognition</p> <p>The Trust recognised £385 million of revenue (Operating income from patient care activities and other operating income) in the Statement of Comprehensive Income. The Trust's primary source of revenue is through contracts with commissioning bodies in respect of the provision of healthcare services. Notes 3 and 4 to the financial statements provide further information on the nature and source of the Trust's revenue.</p> <p>Auditing standards include a rebuttable presumption that there is a significant risk in relation to the timing of income recognition, and in relation to judgements made by management as to when income has been earned. The pressure to manage income to deliver forecast performance in a challenging economic environment increases the risk of fraudulent financial reporting leading to material misstatement and means that we are unable to rebut the presumption.</p>	Yes	<p>Our audit procedures included, but were not limited to:</p> <ul style="list-style-type: none"> Evaluating the Trust's accounting policy in respect of revenue recognition to ensure that it is in line with the requirements of the Group Accounting Manual (GAM). Testing revenue transactions that had been recorded by journal entries. Journals were selected for testing on the basis of meeting one or more fraud risk indicators that we determined to be applicable to the revenue recognition significant risk. Testing a sample of revenue around the year end by agreeing the transactions to appropriate source documentation and obtaining assurance that each item was recorded in the correct financial year and at the correct value. Testing a sample of year end receivables by agreeing the transactions to appropriate source documentation and obtaining assurance that each item was recorded in the correct financial year and at the correct value. Considering information provided by the Department of Health and Social Care in respect of year-end intra-NHS transactions. We identified any significant differences between the Trust's position and that of the counterparty and obtained assurance that the Trust's position was supported by appropriate evidence. 	Our work provided the assurance we sought.

2. AUDIT OF THE FINANCIAL STATEMENTS

Identified significant risk	Key audit matter?	Our response	Our findings and conclusions
<p>Property valuations</p> <p>Land and buildings are the Trust's highest value assets and Note 17.1 to the financial statements discloses information on the Trust's holding of property, plant and equipment (PPE). This includes £122.4 million of land and buildings held at current value at 31 March 2020. These assets are subject to periodic revaluation in line with the requirements of the Group Accounting Manual (GAM). Note 1.9 to the financial statements describes the Trust's accounting policy with respect to the valuation of land and buildings and note 17.1 discloses further information on the balance.</p> <p>Management engage a valuation expert ('the valuer') to provide the Trust with current values of property and land in accordance with Royal Institution of Chartered Surveyors (RICS) requirements. Changes in the value of property may impact on the Statement of Comprehensive Income depending on the circumstances and the specific accounting requirements of the Group Accounting Manual. The valuations require judgement and a high level of estimation in determining current values.</p> <p>The significant risk of material misstatement is further increased due to the additional estimation uncertainty arising from the COVID-19 pandemic.</p>	Yes	<p>Our audit procedures included, but were not limited to:</p> <ul style="list-style-type: none"> • Obtaining an understanding of the skills, experience and qualifications of the valuer, and considering the appropriateness of the instructions to the valuer from the Trust. • Obtaining an updated understanding of the basis of valuation applied by the valuer in the year. This included understanding and challenging the methodology applied to estimate the gross replacement cost of the Trust's operational land and buildings on a modern equivalent asset basis. Specifically, we evaluated the Trust's application of a 'single-site' valuation methodology which covers its existing hospital sites. • Sample testing the completeness and accuracy of underlying data provided by the Trust and used by the valuer as part of their valuations. • Testing the accuracy of how valuation movements were presented and disclosed in the financial statements. • Making direct enquiries with the valuer to understand the nature of the material valuation uncertainty disclosed in his valuation report. • Using relevant market and cost data to assess the reasonableness of the valuation as at 31 March 2020. In doing so, we also considered relevant, publicly available valuation indices to assess the effect of any potential material valuation uncertainty related to the COVID-19 pandemic. 	Our work provided the assurance we sought.

2. AUDIT OF THE FINANCIAL STATEMENTS

Identified significant risk	Key audit matter?	Our response	Our findings and conclusions
<p>Accounting for any potential liability at 31 March 2020 from the PFI termination</p> <p>One of the Trust's PFI arrangements terminated in 2018/19. As PFI termination is rare, there is an increased risk that the accounting treatment of any liabilities arising from the termination is misstated.</p>	Yes	<p>Building on our audit work and knowledge from our 2018/19 audit, our audit procedures included, but were not limited to:</p> <ul style="list-style-type: none"> • Holding discussions with the Trust's legal advisors to obtain evidence about their views. • Reviewing and challenging the Trust about the accounting treatment adopted for any potential liabilities at 31 March 2020 associated with the termination. • Considering the proposed accounting by the Trust against the requirements of IAS37 to determine the appropriate method to account for the potential liabilities. 	Our work provided the assurance we sought.

We also recognised an area of enhanced audit risk. The table below outlines the identified enhanced risk, the work we carried out, and our conclusion.

Identified enhanced risk	Key audit matter?	Our response	Our findings and conclusions
<p>Accounting for the Trust's ongoing PFI arrangements</p> <p>The method of accounting for PFI assets/liabilities is complex and this therefore raises the risk of misstatement.</p>	No	We reviewed the Trust's adopted approach for accounting for its ongoing PFI assets and liabilities including reviewing any changes from prior years to the long term financial model used, and considered any changes to the schemes in year in order to conclude on the appropriateness of the accounting entries in the Financial Statements.	Our work provided the assurance we sought.

Internal control recommendations

As part of our audit we considered the internal controls in place that are relevant to the preparation of the financial statements. We did this to design audit procedures that allow us to express our opinion on the financial statements, but this did not extend to us expressing an opinion on the effectiveness of internal controls.

Our audit identified the scope to improve the operation of controls the Trust has in place in relation to oversight of, and access rights to, the ESR system. Management have agreed actions to implement in 2020/21 in order to improve internal control.



3. VALUE FOR MONEY CONCLUSION

Value for Money conclusion

Unqualified

Our approach to Value for Money

We are required to consider whether the Trust has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider. We are only required to report if we conclude that the Trust has not made proper arrangements..

The overall criterion is that, 'in all significant respects, the Trust had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.' To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- Informed decision making.
- Sustainable resource deployment.
- Working with partners and other third parties.

Our auditor's report, issued to the Trust on 24 June 2020 confirmed that we had no matters to report in respect of the Trust's arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2020.

Sub-criteria	Commentary	Matters to report
Informed decision making	<p>The Trust has a constituted and documented governance structure and strategy in place, which is kept under review by the Board.</p> <p>There is regular reporting to the Board of performance and financial information. Board members have a mix of experience and background.</p> <p>Arrangements to manage risk are in place, and reviewed and updated periodically. The Trust acknowledges that some elements of the Internal Control process require review and further improvement, as set out in its 2019/20 Annual Governance Statement.</p>	None
Sustainable resource deployment	<p>Medium Term Financial Plans are in place, with savings plan requirements clearly identified.</p> <p>Asset register and capital business case approval process in place.</p> <p>The Trust has a history of meeting financial targets, and achieved its financial plan for 2019/20.</p>	None
Working with partners and other third parties	<p>The Trust works closely with its Local Authority partners and other health bodies. It is engaged in the local Sustainability and Transformation processes.</p>	None

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3. VALUE FOR MONEY CONCLUSION

Significant Value for Money risks

The NAO's guidance requires us to carry out work to identify whether or not a risk to the Value for Money conclusion exists. Risk, in the context of our Value for Money work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Trust being inadequate. In our Audit Strategy Memorandum, we reported that we had identified one significant Value for Money risk(s). The work we carried out in relation to significant risks is outlined below.

Risk	Work undertaken	Conclusion
<p>Implications of CQC findings on our VFM conclusion</p> <p>CQC rated the Trust as 'Overall Good' in their October 2018 report. Following CQC visits during summer 2019 to Child and adolescent mental health wards at West Lane Hospital, Middlesbrough the CQC used their powers under section 31 of the Health and Social Care Act to take enforcement action and placed conditions on the Trust's registration. To adhere to the requirements of the notice the Trust managed the closure of the wards and arranged for the service users to be moved to alternative services and providers.</p> <p>The CQC findings may impact on our responsibilities, and as such we needed to undertake work to assess any implications on our work, and then use that information to inform our VFM Conclusion.</p>	<p>We reviewed the CQC reports issued in 2019, and discussed them with relevant officers. We also considered the report issued by CQC in March 2020, which amended the Trust's overall rating to 'Requires improvement'.</p> <p>We challenged management about the robustness of the risk and performance management monitoring arrangements the Trust had in place in 2019/20.</p> <p>We also carefully considered other relevant information including the CQC's assessment of the 'Well led' domain reported in March 2020 of 'Good' overall, the findings of the Trust's internal auditors for 2019/20, and overall Head of Internal Audit Opinion for the year, and the Trust's Annual Governance Statement for 2019/20.</p> <p>We also considered the action the Trust has taken in response to the CQC findings, or is planned to take.</p> <p>We found, in summary:</p> <ul style="list-style-type: none"> the matters that led to closure of West Lane were very serious and not insignificant; the Trust acknowledges the way parts of its Internal Control processes did not fully operate as they should (in relation to that facility) to either mitigate the risks faced, or more clearly report the potential regulatory impact, and are taking action to improve arrangements, and has been clear about this in its Annual Governance Statement; the other relevant information we considered gave us assurance that the internal control matters were not widespread, and as such we did not conclude that arrangements at the Trust, taken as a whole were 'inadequate'. 	<p>Our work mitigated the risk we identified at the planning stage, and we concluded that in overall terms the findings from the work did not have an adverse impact on our VFM conclusion.</p>



4. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	No matters to report
Governance Statement	No matters to report
Consistency of consolidation data with the audited financial statements	Consistent
Other information published alongside the audited financial statements	Consistent

The NAO's Code of Audit Practice and the 2006 Act place wider reporting responsibilities on us, as the Trust's external auditor. We set out below, the context of these reporting responsibilities and our findings for each.

Matters which we report by exception

The 2006 Act provides us with specific powers where matters come to our attention that, in our judgement, require reporting action to be taken. We have the power to:

- issue a report in the public interest; and
- make a referral to the regulator where we believe that a decision has led to, or would lead to, unlawful expenditure, or an action has been, or would be unlawful and likely to cause a loss or deficiency.

We have not exercised any of these statutory reporting powers.

We are also required to report if, in our opinion, the governance statement does not comply with the guidance issued by NHS Improvement or is inconsistent with our knowledge and understanding of the Trust. We did not identify any matters to report in this regard.

Reporting to the NAO in respect of consolidation data

The NAO, as group auditor, requires us to report to them whether consolidation data that the Trust has submitted is consistent with the audited financial statements. We have concluded and reported that the consolidation data is consistent with the audited financial statements.

Other information published alongside the financial statements

The Code of Audit Practice requires us to consider whether information published alongside the financial statements is consistent with those statements and our knowledge and understanding of the Trust. In our opinion, the information in the Annual Report is consistent with the audited financial statements.

5. OUR FEES

Fees for work as the Trust's auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to the Audit Committee in December 2019.

Having completed our work for the 2019/20 financial year, we can confirm that our final fees are as follows:

Area of work	2019/20 proposed fee	2019/20 final fee
Delivery of audit work under the NAO Code of Audit Practice	£34,600 plus VAT	£40,170 plus VAT *

* In line with the fees reported in our update letter to the Trust in June 2020 as a result of additional work required.

Fees for other work

We commenced our assurance work in relation the Trust's Quality Report, however we ceased our work in March 2020 when NHS Improvement wrote to all NHS Foundation Trusts to outline the next steps on the NHS Response to COVID-19 Financial Arrangements. In this communication, it was made clear that "auditor assurance work on quality accounts/reports should cease for 2019/20".

A fee of £7,000 plus VAT was originally envisaged for our assurance work in relation the Trust's Quality Report. At the end of March 2020 we had completed the planning phase of our work, and liaised with key officers. We therefore agreed a reduced charge for time spent and work completed of £1,325.

We can confirm that we have not undertaken any other non-audit services for the Trust in the year.

Services provided to other entities linked to the Trust

We were also appointed to undertake an independent examination of the Trusts Charitable Funds, for a fee of £400 plus VAT.

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6. FORWARD LOOK

Operational outlook

The Trust has had a challenging year in 2019/20. The events at West Lane Hospital, followed up by visits from CQC and their subsequent reports have been, and remain very high on the Trust's management and Board agenda throughout the year.

In addition, the arrival of the COVID-19 pandemic has led to significant challenges.

We will continue to monitor the position in both of these areas as part of next years audit programme.

Financial challenges

The balance between meeting the ongoing financial challenge, including achieving cost efficiencies, and ongoing improvements in patient care remain a challenge for the Trust, and we will keep this under review as part of our audit for 2020/21.

The Trust continues to face financial pressures for the foreseeable future, and the long term impact of COVID-19 and the continued national drive to re-establish financial control over the NHS provider sector remains unclear. Whilst the current NHS financial regime has guaranteed block contract payments to 31 July 2020, trusts will be required to submit updated operational and financial plans for the remainder of the 2020/21 financial year, where an increased level of financial accountability is anticipated to be in place.

At the same time the Trust must cope with any changes to its income levels, and also national cost pressures.

We will also continue to keep the position on the PFI termination at Roseberry Park under review, in respect of our audit responsibilities on both the accounts and consideration of the Trust's value for money arrangements.

Our ongoing support to the Trust

We will continue to support the Trust through our audit work including:

- liaising with AuditOne (the Trust's Internal Auditors) to minimise duplication of work;
- attendance at Audit and Risk Committees where we will continue to inform the Committee about progress on the audit, report our key findings and update it about developments in the NHS and the wider environment;
- attending Council of Governors' meetings to present the findings from our work; and
- hosting events for staff, such as our NHS Accounts workshop.

The Trust has taken a positive and constructive approach to our audit and we wish to thank the Board, Audit and Risk Committee, and Trust staff for their support and co-operation during our audit in the past year.

We are committed to supporting the Trust as your external auditor. We will meet with the Trust to identify any learning from the 2019/20 audit and will continue to share our insights from across the NHS and relevant knowledge from the wider public and private sector.

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