



# Annual Audit Letter

Sheffield Teaching Hospitals NHS Foundation  
Trust

Year ending 31 March 2019





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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 Sheffield Teaching Hospitals NHS Foundation Trust (the Trust) for the year ended 31 March 2019. 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	<p>Our auditor's report issued on 23 May 2019 included our opinion that:</p> <ul style="list-style-type: none"><li>the financial statements give a true and fair view of the Trust's financial position as at 31 March 2019 and of its financial performance for the year then ended.</li></ul>
Value for Money conclusion	<p>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.</p>
Reporting to the group auditor	<p>In line with group audit instructions issued by the NAO, on 23 May 2019, we reported that the Trust's consolidation schedules were consistent with the audited financial statements.</p>
Statutory reporting	<p>Our auditor's report confirmed that we did not use our powers under schedule 10 of the 2006 Act to:</p> <ul style="list-style-type: none"><li>issue a report in the public interest; or</li><li>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).</li></ul>

## 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 2019 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 23 May 2019, stated that, in our view, the financial statements give a true and fair view of the Trust's financial position as at 31 March 2019 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 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 2019:

Financial statement materiality	Our financial statement materiality is based on 1.8% of Gross Operating Expenditure.	£20 million
Trivial threshold	Our trivial threshold is based on 1.5% of financial statement materiality.	£300,000
Specific materiality	We have applied a lower level of materiality to the following areas of the accounts: - Remuneration of Senior Managers - Related Party Transactions	£5,000 £50,000

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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 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><b>Management override of controls</b></p> <p>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, there is a risk of material misstatement due to fraud on all audits.</p>	No	<p>We addressed this risk through performing audit work over:</p> <ul style="list-style-type: none"> <li>Accounting estimates impacting amounts included in the financial statements;</li> <li>Consideration of identified significant transactions outside the normal course of business; and</li> <li>Journals recorded in the general ledger and other adjustments made in preparation of the financial statements.</li> </ul>	<p>There were no significant findings arising from our work on management override of controls.</p>
<p><b>Revenue recognition</b></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.</p> <p>The pressure to manage income to deliver forecast performance in a challenging financial environment increases the risk of fraudulent financial reporting leading to material misstatement and means we are unable to rebut the presumption.</p> <p>We consider specific risks in relation to revenue recognition to be in the following areas:</p> <ul style="list-style-type: none"> <li>Recognition of income and receivables around the year end;</li> <li>Recognition of Provider Sustainability Fund (PSF) income during the year.</li> </ul>	Yes	<p>We evaluated the design and implementation of controls the Trust has in place which mitigate the risk of income being recognised in the wrong year. In addition we undertook a range of substantive procedures including:</p> <ul style="list-style-type: none"> <li>testing of material income and material year end receivables for accuracy, completeness and occurrence;</li> <li>testing receipts in the pre and post year end period to ensure they have been recognised in the right year;</li> <li>reviewing intra-NHS reconciliations and data matches provided by the Department of Health and Social Care and seeking direct confirmation from third parties as required; and</li> <li>testing of PSF income to year end confirmation from NHS Improvement.</li> </ul>	<p>There were no significant findings arising from our work on revenue recognition.</p>

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## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant risks and key audit matters (continued)

Identified significant risk	Key audit matter?	Our response	Our findings and conclusions
<p><b>Valuation of Land and Buildings</b></p> <p>Land and buildings are the Trust's highest value assets accounting for £320m of the Trust's £391m Property, Plant and Equipment balance. Management engages Cushman and Wakefield as an expert to assist in determining the current value of land and buildings to be included in the financial statements. Such valuations are subject to a significant degree of estimation and judgement. Changes in the value of land and buildings may impact on the Statement of Comprehensive Income depending on the circumstances and the specific accounting requirements of the Group Accounting Manual.</p>	Yes	<p>We evaluated the design and implementation of controls to mitigate the risk. We also:</p> <ul style="list-style-type: none"> <li>assessed the scope and terms of engagement with Cushman and Wakefield;</li> <li>assessed how management use Cushman and Wakefield's report to value land and buildings in the financial statements;</li> <li>reviewed the valuation methodology used, including testing the underlying data and assumptions (including the application of the new Royal Institute of Chartered Surveyors (RICS) guidance issued in year);</li> <li>assessed the competence, skills and objectivity of Cushman and Wakefield; and</li> <li>considered the reasonableness of the valuation by comparing the valuation output with market intelligence and challenging the Trust and the valuer where required.</li> </ul>	There were no significant findings arising from our work on the valuation of land and buildings.

### 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.

We identified one low risk deficiency in internal control as part of our audit - relating to journal authorisation. Management has highlighted a number of compensating controls to mitigate the associated risks and agreed to seek to address the recommendation when practicable. We are content with Management's response.



### 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 23 May 2019, 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

Sub-criteria	Commentary	Matters to report
Informed decision making	Our work has identified the Trust's arrangements include: <ul style="list-style-type: none"> <li>• established strategic and operational plans;</li> <li>• integrated performance, risk and assurance reporting;</li> <li>• an established governance structure and systems of internal control; and</li> <li>• a risk management policy and arrangements for risk identification, validation, mitigation, monitoring and reporting.</li> </ul>	None
Sustainable resource deployment	Our work has identified the Trust's arrangements include: <ul style="list-style-type: none"> <li>• budget setting, monitoring and reporting;</li> <li>• productivity and efficiency plans;</li> <li>• medium term financial modelling linked to service plans.</li> </ul>	None
Working with partners and other third parties	Our work has identified the Trust's arrangements include: <ul style="list-style-type: none"> <li>• strong engagement and lead role in the South Yorkshire and Bassetlaw Integrated Care System and the Sheffield Accountable Care Partnership;</li> <li>• active membership of the Working Together Partnership to secure shared improvements to patient care and efficiency across the South Yorkshire and Bassetlaw, North Derbyshire and Mid Yorkshire area; and</li> <li>• significant research partnerships and working with many public, private and community partners, to take forward the vision for the Sheffield City region.</li> </ul>	None



### 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. The work we carried out in relation to significant risks is outlined below.

Risk	Work undertaken	Conclusion
<p><b>Achievement of planned control total / cost improvement plans</b></p> <p>For 2018/19 the Trust agreed a control total surplus of £5.1 million with NHS Improvement. As in previous years, the achievement of the planned financial performance was dependent on delivering significant cost improvement / efficiency plans (£26.8 million). In addition the Trust needed to achieve agreed trajectories for operational performance to access £26.1 million from the Provider Sustainability Fund (PSF).</p> <p>As at Month 7 the Trust reported a £1.1 million deficit against its internal plan and a £2.5 million under delivery against cost improvement / efficiency plans.</p> <p>While the Trust was highly focused on improving its financial performance there remained a risk that the Trust's arrangements were insufficient to achieve its financial plans for 2018/19 and the medium term.</p>	<p>To evaluate the Trust's arrangements for securing value for money in its use of resources we:</p> <ul style="list-style-type: none"> <li>• reviewed the arrangements for delivering recurrent cost improvement schemes;</li> <li>• selected a sample of directorates to test the robustness of their efficiency plans for 2018/19 including seeking to identify the reasons for under and over delivery during the year; and</li> <li>• challenged the underlying assumptions and rationale supporting the Trust's 2019/20 financial plan.</li> </ul>	<p>Despite facing significant financial challenges during 2018/19, the Trust managed its resources to achieve a surplus for the year of £26.5 million (once technical adjustments are taken into account). This is a £13.2 million improvement on the Trust's financial plan before additional funding of £14 million from the national Provider Sustainability Fund (largely in recognition of the Trust's successful achievement of its Control Total set by NHS Improvement).</p> <p>The Trust planned to achieve recurrent efficiency savings of £26.8 million in 2018/19 and achieved £33.4 million (124%). This is against the background of significant service and demand pressures which materialised as increased patient activity levels in the year. Our sample testing of directorates found that whilst most delivered their budgets / CIPs, these demand pressures impacted some directorates ability to deliver their budgets / CIPs as planned.</p> <p>The Trust's agency spend, at £9.7 million, was comfortably below its agency spending cap of £17.3 million as set by NHS Improvement.</p> <p>The Trust has agreed contracts with commissioners and agreed a control total with NHS Improvement for 2019/20.</p> <p>To achieve this control total, the Trust will need to deliver further productivity and efficiency gains of £20.6 million in 2019/20. The Trust has made good progress in identify plans to deliver these savings through its 2019/20 Financial Plan and continues to plan further efficiency savings for 2020/21 and future years through its Making It Better Programme. The Trust recognises the significant risks and challenges in delivering these savings in 2019/20 and beyond.</p> <p>Through this work, whilst we recognise the challenges going forward, we identified no residual risks that affected our ability to form our VFM conclusion.</p>



## 4. OTHER REPORTING RESPONSIBILITIES

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

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 taken or begun to be taken which, if fulfilled to its conclusion, 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 Audit Committee in January 2019.

Having completed our work for the 2018/19 financial year, we can confirm that our final fees are as follows:

Area of work	2018/19 proposed fee	2018/19 final fee
Delivery of audit work under the NAO Code of Audit Practice	£45,130	£45,130

### Fees for other work

We also provided non-audit services as follows:

Area of work	2018/19 proposed fee	2018/19 final fee
Quality Report – external assurance on the Trust's Quality Report	£7,870	£7,870

## 6. FORWARD LOOK

### Financial outlook

The Trust continues to face significant financial pressures for 2019/20 reflecting the continued national drive to re-establish financial control over the NHS provider sector. The current NHS financial regime offers access to Provider Sustainability Funding (PSF) for trusts which agree to meet financial control totals set by NHS Improvement.

The Trust has agreed a control total for 2019/20 which requires it to achieve a surplus for the year of £0.5 million which gives the Trust access to £13 million of PSF. Receipt of funding depends on achieving challenging financial targets during the year.

The Trust needs to achieve savings for 2019/20 of £20.6 million through its productivity and efficiency programme. There are significant challenges to achieve the required efficiencies on a recurrent basis to further strengthen the Trust's financial sustainability for the long term.

At the same time the Trust must cope with national cost pressures and the impact of the rise in the Retail Price Index which determines the annual price uplift on many external contracts.

The Trust has made good progress in identify plans to deliver the required savings through its 2019/20 Financial Plan and continues to plan further efficiency savings for 2020/21 and future years through its Making It Better Programme. The Trust recognises the significant risks and challenges in delivering these savings in 2019/20 and beyond.

We will continue to review the Trust's financial performance as part of our audit for 2019/20.

### Operational challenges

The Trust continues to modernise and develop its services and estate to best meet the needs of patients. This includes

- continuing to address the operational, workforce and financial risks associated with the temporary closure of the Robert Hadfield building;
- pursuing the refreshed corporate strategy 'Making a Difference' to respond to the current and potential future challenges in the health and social care sector as new partnerships, structures and accountability arrangements continue to emerge and become business as usual.

The reduction in central government funding to local authorities creates significant challenges for the provision of robust social care services and can adversely impact on the NHS. The Trust is working hard with social care sector partners to ensure that vulnerable patients can be discharged to appropriate care settings on a timely basis.

### How we will work with the Trust

In the coming year we will continue to support the Trust by:

- attending Audit Committee meetings and presenting an Audit Progress Report including updates on regional and national developments;
- attending Council of Governors' meetings to present the findings from our work;
- continued liaison with 360 Assurance (the Trust's Internal Auditors) to minimise duplication of 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 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 its external auditor. We will meet with the Trust to identify any learning from the 2018/19 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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## CONTACT

### **Cameron Waddell**

Partner

Phone: 0191 383 6300

Mobile: 0781 375 2053

Email: [cameron.waddell@mazars.co.uk](mailto:cameron.waddell@mazars.co.uk)

### **Mark Dalton**

Senior Manager

Phone: 0113 394 5316

Mobile: 0779 550 6766

Email: [mark.dalton@mazars.co.uk](mailto:mark.dalton@mazars.co.uk)