Portsmouth Hospitals NHS Trust

Annual Audit Letter for the year ended 31 March 2020

14 July 2020

Building a better working world

Contents

The contents of this report are subject to the terms and conditions of our appointment as set out in our engagement letter dated 19 April 2017.

This report is made solely to the Audit Committee and management of Portsmouth Hospitals NHS Trust in accordance with our engagement letter. Our work has been undertaken so that we might state to the Audit Committee and management of the Trust those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee and management of the Trust for this report or for the opinions we have formed.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Hywell Ball, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Section 1

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Portsmouth Hospitals NHS Trust (the Trust) following completion of our audit procedures for the year ended 31 March 2020.

Covid-19 had an impact on a number of aspects of our 2019/20 audit. We set out these key impacts below.

Area of impact	Commentary
Impact on the delivery of the audit	
► Changes to reporting timescales	On 23 March 2020, NHSE/I wrote to all commissioners and providers setting out changes to the 2019/20 accounts reporting timescales as a result of Covid-19. The deadline for submission of audited accounts was changed from 29 May 2020 to 25 June 2020. We worked with the Trust to deliver our audit in line with the revised reporting timescale, and our Opinion was issued on 23 June 2020.
Impact on our risk assessment	
► Valuation of Property Plant and Equipment	The Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in the year-end valuation reports produced by the Trust's external valuer. We considered that the material uncertainties disclosed by the valuer gave rise to a need to undertake additional procedures to ensure the material accuracy of property, plant and equipment balances at 31 March 2020.
► Disclosures on Going Concern	Financial plans for 2020/21 will need revision for Covid-19, and the DHSC has suspended normal NHS operational planning for 2020/21 and moved to "block contract" arrangements until at least July 2020. We had already identified a significant risk in our audit plan with regard to the adequacy of disclosures relating to going concern. We reviewed management's assessment of going concern with particular reference to Covid-19 and the Trust's financial position and future cashflow projections.
► Adoption of IFRS 16 Leases	The adoption of IFRS 16 by the DHSC GAM as the basis for preparation of NHS financial statements has been deferred to 2021/22. The Trust was therefore no longer required to undertake an impact assessment, and disclosure of the impact of the standard in the financial statements did not now need to be financially quantified in 2019/20. However, as significant work had already been undertaken on this, the Trust included the disclosure in its 2019/20 accounts. We did not deem this an "area of audit focus" at the year-end due to the deferral of IFRS 16 but carried out procedures as necessary to review the disclosure which the Trust had made.

Executive Summary (cont'd)

Area of impact	Commentary
Impact on the scope of our audit	
► Auditor assurance on the Quality Account	In March 2020, NHSI removed the requirement for auditors to issue a limited assurance opinion on the quality account for 2019/20.
Changes to our audit procedures	
► Inventory	We worked with officers to adapt our audit procedures in respect of inventory. This was to avoid a limitation of scope arising from our inability to attend stock takes in late March as originally planned. This resulted in additional work being performed in excess of that which would usually be required to gain assurance over the inventory balance in the balance sheet. We would like to express our thanks to the Trust's staff for their assistance with this work.

Executive Summary (cont’d)

The tables below set out the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Trust’s:	
► Financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the Trust as at 31 March 2020 and of its expenditure and income for the year then ended. Our audit report referenced the material uncertainty on going concern disclosed by the Trust, and included an emphasis of matter in respect of property, plant and equipment valuations.
► Parts of the remuneration and staff report to be audited	We had no matters to report.
► Consistency of the Annual Report and other information published with the financial statements	Financial information in the Annual report and published with the financial statements was consistent with the audited accounts. In reviewing the Annual Report and other information published with the financial statements we took account of updated guidance issued to bodies in the light of Covid-19.

Area of Work	Conclusion
Reports by exception:	
► Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Trust.
► Referrals to the Secretary of State	We made a referral to the Secretary of State in relation to the Trust’s cumulative financial deficit.
► Public interest report	We had no matters to report in the public interest.
► Value for money conclusion	We had no matters to report.

Executive Summary (cont'd)

Area of Work	Conclusion
Reporting to the Trust on its consolidation schedules	We concluded that the Trust's consolidation schedules agreed, within a £300,000 tolerance, to your audited financial statements.
Reporting to the National Audit Office (NAO) in line with group instructions	The NAO did not include the Trust in its sample of DHSC component bodies. We had no matters to report.

As a result of the work we carried out we have also:

Outcomes	Conclusion
Issued a report to those charged with governance of the Trust communicating significant findings resulting from our audit.	We issued an Audit Results Report dated 5 June 2020 and discussed it at the 15 June Audit Committee.
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	We issued our certificate on 23 June 2020.

We would like to take this opportunity to thank the Trust staff for their assistance during the course of our work.

Kevin Suter

Associate Partner
For and on behalf of Ernst & Young LLP

Section 2

Purpose & responsibilities

Purpose & responsibilities

The Purpose of this Letter

The purpose of this annual audit letter is to communicate to the Board of Directors and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Trust. We have already reported the detailed findings from our audit work in our 2019/20 audit results report to the 15 June Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Trust.

Responsibilities of the Appointed Auditor

We have undertaken our 2019/20 audit work in accordance with the outline Audit Plan that we issued in January 2020 as well as the subsequent update to our Audit Pan we provided to management in May 2020, and summarised in our Audit Results Report in June 2020. We have complied with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

Expressing an opinion on:

- The 2019/20 financial statements;
- The parts of the remuneration and staff report to be audited;
- The consistency of other information published with the financial statements, including the annual report; and
- Whether the consolidation schedules are consistent with the Trust's financial statements for the relevant reporting period.

Reporting by exception:

- If the governance statement does not comply with relevant guidance or is not consistent with our understanding of the Trust;
- To the Secretary of State for Health if we have concerns about the legality of transactions of decisions taken by the Trust;
- Forming a conclusion on the arrangements the Trust has in place to secure economy, efficiency and effectiveness in its use of resources;
- Any significant matters that are in the public interest; and
- Reporting on an exception basis any significant issues or outstanding matters arising from our work which are relevant to the NAO as group auditor.

Responsibilities of the Trust

The Trust is responsible for preparing and publishing its financial statements, annual report and governance statement. It is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Section 3

Financial Statement Audit

Financial Statement Audit

Key Issues

The Annual Report and Accounts is an important tool for the Trust to show how it has used public money and how it can demonstrate its financial management and financial health. We audited the Trust's financial statements in line with the NAO's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other NAO guidance and issued an unqualified audit report on 23 June 2020. We reported our detailed findings to the 15 June Audit Committee. The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
Misstatements due to fraud or error A risk present on all audits is that management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly, and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Auditing standards require us to respond to this risk by testing the appropriateness of journals, testing accounting estimates for possible management bias and obtaining an understanding of the business rationale for any significant unusual transactions. .	We obtained a full list of the journals posted to the Trust's general ledger during the year, and analysed these journals using criteria we set to identify unusual journal types or amounts. We then tested a sample of journals that met our criteria. We tested the accounting estimates most susceptible to bias, being mainly the valuation of land and buildings. We did not identify any material weaknesses in controls or evidence of material management override. We did not identify any instances of inappropriate judgements being applied. We did not identify any transactions during our audit which appeared unusual or outside the Trust's normal course of business.

Financial Statement Audit (cont'd)

Significant Risk	Conclusion
Risk of fraud in non-NHS income and expenditure recognition Auditing standards also require us to presume that there is a risk that revenue and expenditure may be misstated due to improper recognition or manipulation. We judged this risk to be present in non-NHS income and expenditure transactions, specifically accrued non-NHS income and other operating costs (excluding payroll and finance expenditure).	We reviewed and tested manual creditors and accruals and the associated expenditure as well as manual debtors and accrued income balances and evaluated the estimates made by management for reasonableness. We used higher sample sizes for manual income and expenditure accruals reflecting the higher level of risk. No evidence of manipulation of these balances were identified. We reviewed post year-end cash book entries to identify any unrecorded liabilities through to 28 May. No unrecorded liabilities were identified. We tested the completeness of expenditure by performing cut off procedures from 1 March to 28 May. We were satisfied that the Trust's outturn position was consistent with in-year forecasting and budgeted income and expenditure.

Financial Statement Audit (cont'd)

Significant Risk	Conclusion
Going concern The Trust has been reporting deficit outturn positions for a number of years, and had a cumulative deficit balance of £110.5 million as at 31 March 2019. The Trust has been reliant upon Working Capital Loans to support its cash flow in previous years. The Trust has a plan in place, which aims to improve both its operational and financial performance over a three year period. However there is a risk that should the Trust not progress in line with this plan, the nature of the support from the Department of Health and NHS Improvement could change. The Trust needs to clearly demonstrate the appropriateness of the use of the going concern assumption in the preparation of the financial statements, and to ensure that sufficient disclosure is made of any material uncertainties in this regard.	We considered whether it is appropriate to prepare the financial statements on a going concern basis by: • Reviewing management's assessment that it is appropriate for the financial statements to be prepared on a going concern basis • Reviewing the Trust's cashflow forecast covering the foreseeable future, to ensure that it has sufficient liquidity to continue to operate as a going concern. • Challenging the disclosure made in the accounts and annual report in respect of going concern and any material uncertainty. In light of Covid-19, we extended these audit procedures as there was a risk that previously agreed arrangements could change. We, and the Trust, then considered the guidance issued by NHSI in May 2020. We also scrutinised the Trust's revised financial plans and cashflow, liquidity forecasts, known outcomes, sensitivities, mitigating actions and key assumptions. The Trust updated its draft going concern disclosure in note 1.2 to reflect the material uncertainty relating to the Trust's underlying deficit, reliance on additional support funding from NHS Improvement and NHS England, and the lack of national framework structure beyond July 2020. We drew attention to this through a 'material uncertainty related to going concern' paragraph in our audit report..

Financial Statement Audit (cont'd)

Areas of audit focus

In addition to the significant risks we have reported on pages 9-11, we also identified 2 other areas of audit focus.

Areas of Audit Focus	Conclusion
Valuation of land and buildings Land and buildings is the most significant balance in the Trust's balance sheet. The valuation of land and buildings is complex and is subject to a number of assumptions and judgements. A small movement in these assumptions can have a material impact on the financial statements including the Trust's charge for depreciation. Following the Covid-19 pandemic, the Royal Institute of Chartered Surveyors, the body setting the standards for property valuations, has issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in the year-end valuation reports produced by the Trust's external valuer.	We were satisfied that the Trust has accounted for its valuation of land and buildings appropriately and had made appropriate disclosures to reflect the material uncertainty in the valuer's report. Due to the inclusion of this paragraph within the valuer's report we undertook additional procedures, involving our own specialist valuer to provide assurance on the elements of land and buildings which were valued with reference to market information. We included an emphasis of matter paragraph in our audit report to draw attention to the disclosure of the material uncertainty in the financial statements. Our work also identified a material misstatement in prior period comparators. This arose because accumulated depreciation was not reversed on a full revaluation of assets in 2018/19 as required by DHSC GAM. This did not impact any of the primary financial statements. The error was corrected in the final version of the 2019/20 financial statements, with the 2018/19 comparators restated.
Private Finance Initiative The PFI liability and associated expenditure makes up the second largest balance on the balance sheet. The accounting for the PFI involves a number of judgements and impacts a number of areas of the accounts that can have a material impact on the financial statements.	We were satisfied that the current year PFI model was consistent with the prior year model, with appropriate updates, and therefore that we could continue to rely on the assurances provided by our specialist in prior years. Disclosures and balances in the financial statements were consistent with the model, and expenditure appropriately recorded. As a result, we had no matters to report with regard to PFI valuation and disclosures.

Financial Statement Audit (cont’d)

Areas of audit focus

We undertook amended and additional procedures to gain assurance over the inventory balance in the balance sheet as a result of the Covid-19 pandemic.

Areas of Audit Focus	Conclusion
Inventory As a result of Covid-19, we were unable to attend the stock take in the Trust’s theatres warehouse which had been planned for the final week of March. This is an essential part of our work on inventory. With the assistance of officers, we undertook a virtual stock count on 29 April, using video-conferencing technology to dial-in to a stock count and observe the procedures remotely. We then needed to undertake work to test movements in theatres stock between the year-end and the date of the virtual stock take, to “roll-back” the assurance gained on 29 April to the date of the financial statements (31 March). The elapsed time between the year-end and the date of the virtual stock take meant that significant work was required to perform this testing.	We were able to gain the appropriate assurance over the existence of the stock balances, and therefore avoid a Limitation of Scope in our audit opinion in respect of the inventory balance in the balance sheet. We were satisfied that the inventory balances within the financial statements were materially correct.

Financial Statement Audit (cont'd)

Audit differences

We identified a small number of misstatements in disclosures and the Annual Report which were corrected by management. None were above our performance materiality threshold of £4.79m. We also identified a number of issues with regard to the Trust's disclosure of the impact of IFRS 16, which were corrected by management. As reported above, we identified one material prior period error in the disclosure for property, plant and equipment, which has been amended in the final version of the financial statements.

We did not identify any misstatements above our reporting threshold of £0.3m which management declined to adjust.

Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	We determined planning materiality to be £6.39m as 1% of gross revenue expenditure reported in the accounts. We consider gross revenue expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Trust.
Reporting threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.3m.

We considered whether any changes to our materiality were required in light of Covid-19. Following this consideration we remained satisfied that the values for planning materiality, performance materiality and our audit threshold for reporting differences reported to you in our Audit Planning Report, as updated for the figures in the 2019/20 financial statements, remained appropriate.

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- Remuneration disclosures: We audited all disclosures and undertook procedures to confirm material completeness
- Related party transactions. We audited all disclosures and undertook procedures to confirm material completeness

Section 4

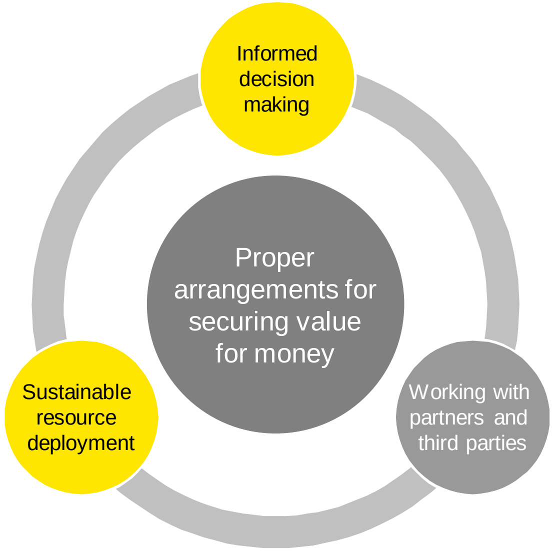
Value for Money

Value for Money

We are required to consider whether the Trust has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.



We identified one significant risk in relation to these arrangements. The tables below and on the following page present the findings of our work in response to the risk identified and any other significant weaknesses or issues to bring to your attention.

We had no matters to report about your arrangements to secure economy, efficiency and effectiveness in your use of resources.

On 16 April 2020 the National Audit Office published an update to auditor guidance in relation to the 2019/20 Value for Money assessment in the light of Covid-19. This clarified that in undertaking the assessment auditors should consider NHS bodies’ response to Covid-19 only as far as it relates to the 2019-20 financial year; only where clear evidence comes to the auditor’s attention of a significant failure in arrangements as a result of Covid-19 during the financial year, would it be appropriate to recognise a significant risk in relation to the 2019-20 VFM conclusion. We did not identify any value for money risks in relation to Covid-19.

Significant Risk in Audit Plan

The Trust continues to face a highly challenging financial position, as a result of financial pressures across the NHS, reductions in commissioner funding and an increased demand for services. The long term sustainability of its finances and the ability to demonstrate good financial health are critical to the future of the Trust. Achievement of the Trust’s in-year and strategic financial plans is predicated on a number of assumptions and saving plans.

In respect of 2019/20 the Trust has set a deficit budget of £17.5 million before the receipt of support funding from DHSC which will take the Trust to a breakeven position. The deficit budget included a £24.1 million cross cutting Cost Improvement Programme (CIP) requirement, with two thirds of this profiled to be delivered in the second half of the year. As at the end of month 6 the Trust continues to forecast meeting its control total but there are clear risks to CIP delivery.

Value for Money (cont’d)

Conclusion

The Trust achieved its control total for 2019/20, securing FRF/PSF funding and ending the year with a small Adjusted Financial Performance surplus of £0.525 million. This represented significantly improved performance compared with the last 5 years, which had all seen deficits. Financial forecasting for the year had consistently shown the Trust to be on track to achieve its overall target.

CIP achievement at year-end was 89% (£21.5 million), compared with 68% in the previous year. The Trust achieved a significant saving in agency staff costs of £6m compared with the prior year, which had been one of the key aims for 2019/20. From review of Board papers and Internal Audit reports, we are aware that work continued through the year to close the CIP gap. This was also confirmed through our meetings with management; but these also noted that other mitigating actions were being worked on alongside, to enable the Trust to achieve its financial plans. These included securing additional funding from Portsmouth CCG, which is supportive of PHT’s longer term improvement strategy.

Our review of the Trust’s 2020/21 operating plan shows that whilst it was challenging, it appeared stretching but achievable. Normal financial planning has been suspended due to Covid-19 and the Trust has put in place an emergency budget based on the currently-known national picture of block contracts through to July 2020, including assessing which CIP can continue in this period without impacting the pandemic response. This will be updated further once national guidance is updated. It is not yet known whether block contracts will continue for the whole of 2020/21 or whether normal financial arrangements will return at some point during the year. This uncertainty means the Trust cannot reasonably try to plan beyond July 2020 at this stage or to form realistic, firm CIP plans covering the whole period. This is a national issue and not a failing of the Trust or its underlying arrangements.

The overall trajectory of the Trust is becoming more positive. Internal Audit’s work on CIP in 2019/20 noted general improvements, and gave a reasonable assurance opinion on arrangements around the CIP programme. Financial performance in the year was improved, as noted above. The Trust remains committed to its 5 year Working Together strategy, and key policies and plans derive from this. The CQC inspection undertaken in November 2019 rated the Trust as Good overall, and Good in all but one of the sub-criteria reported on, demonstrating notable improvements from the previous inspection and showing how the Trust is linking quality outcomes with its financial planning.

Taking all of the above in combination, whilst the financial and operational challenges facing the Trust remain significant, and we will keep performance under review in future years, in our judgment the Trust has demonstrated that its arrangements in 2019/20 were appropriate.

Section 5

Other Reporting Issues

Other Reporting Issues

Department of Health and Social Care Group Instructions

We reported to the NAO that the consolidation schedule was consistent with the audited accounts. We are otherwise only required to report to the NAO on an exception basis if there were significant issues or outstanding matters arising from our work. There were no such issues.

Governance Statement

We are required to consider the completeness of disclosures in the Trust's governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it complies with relevant guidance. We completed this work and did not identify any areas of concern.

Referral to Secretary of State

We must report to the Secretary of State any matter where we believe a decision has led to, or would lead to, unlawful expenditure, or some action has been, or would be, unlawful and likely to cause a loss or deficiency. We made a referral to the Secretary of State in relation to the Trust's cumulative historic deficit.

Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Trust or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

We adopted a fully substantive approach and have therefore not tested the operation of controls.

Section 6

Focused on your future

Focused on your future

Future Accounting Developments

Area	Issue	Impact
New accounting standard	IFRS 16 will now be applicable for Trusts accounts from the 2021/22 financial year, having been deferred from 2020/21. Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for Trusts who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet. The only exclusions being low value leases and leases with a term of less than one year.	Whilst applicable to the 2021/22 financial year, the Trust should continue to build upon the work done in 2019/20 into 2020/21, to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Trust will no longer be able to expense operating leases but will instead have to recognise an asset on the balance sheet and recognise interest and depreciation. The Trust must therefore continue to ensure that all lease arrangements are fully documented.

Regulatory Update

Area	Issue	Impact
Updated Code of Audit Practice	The updated Code of Audit Practice issued by the National Audit Office has introduced some significant changes to the requirements regarding auditors' work on the value for money conclusion, which will be applicable from 2020/21.	The NAO are currently updating the Auditor Guidance Notes which will set out how the new Code of Audit Practice should be applied when carrying out value for money work. As such, the impact remains to be confirmed. Further updates will be provided when possible.

Appendix A

Audit Fees

Appendix A – Audit Fees

The table below sets out the planned fee and our final audit fee.

Description	Final Fee 2019/20 £	Planned Fee 2019/20 £	Final Fee 2018/19 £
Total Audit Fee – Code work	95,637*	83,250	77,250
Non-audit work Quality Accounts	900**	8,000	8,000
TOTAL	96,537	91,250	85,250

* 2019/20 final fee includes amounts to cover the following, where additional procedures were required:

- Value for money conclusion - £2,975
- Going concern assessment - £2,805
- Section 30 referral - £1,144
- Inventory testing - £4,035
- Property, plant and equipment valuations - £2,894
- Property, plant and equipment prior period adjustment - £720
- Consultations on auditor's report - £3,814

** We confirm that we have undertaken some non-audit work on the Quality Accounts. Non-audit work is work not carried out under the Code. In March 2020, NHSI removed the requirement for auditors to issue a limited assurance opinion on the quality account for 2019/20 and we suspended our work in this area. The fee above reflects the quantum of work performed up to the date of the announcement by NHSI. We have adopted the necessary safeguards in our completion of this work and complied with Auditor Guidance Note 1 issued by the NAO in December 2017.

The final fee has been agreed with the Chief Financial Officer.

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