



**MID ESSEX HOSPITAL SERVICES NHS TRUST**

**ANNUAL AUDIT LETTER**

Audit for the year ended 31 March 2018  
12 July 2018

# EXECUTIVE SUMMARY

## PURPOSE OF THE LETTER

This Annual Audit Letter summarises the key issues arising from the work that we have carried out in respect of the year ended 31 March 2018. It is addressed to the Trust but is also intended to communicate the key findings we have identified to key external stakeholders and members of the public.

## RESPONSIBILITIES OF AUDITORS AND THE TRUST

It is the responsibility of the Trust to ensure that proper arrangements are in place for the conduct of its business and that public money is safeguarded and properly accounted for.

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

- The Trust's financial statements
- The auditable parts of the Remuneration and Staff Report
- Whether the Trust has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We are also required to review and report on the Annual Report, Annual Governance Statement and the Trust Accounts Consolidation schedules.

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

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

BDO LLP  
12 July 2018

## AUDIT CONCLUSIONS

### FINANCIAL STATEMENTS

We issued our unmodified true and fair opinion on the financial statements on 25 May 2018.

We reported our detailed findings to the Board on 22 May 2018.

We referred a matter to the Secretary of State under section 30 of the Local Audit and Accountability Act 2014 in relation to the Trust breaking its statutory breakeven duty.

### USE OF RESOURCES

We issued a full adverse opinion on the Trust's arrangements for securing economy, efficiency and effectiveness in its use of resources on 25 May 2018. This form of opinion was necessary because of the significant deterioration in financial position during the year.

The Trust achieved an outturn of £52.9m adjusted deficit compared to an original control total of £24.5m deficit in 2017/18 and needed to secure additional borrowings, which will need to be repaid, to finance activities in the year. The Trust has also prepared the 2018/19 budget, reporting a forecast deficit of £47.3m requiring savings of £19.4m (or 5% of spend, which is a particularly challenging level) to be delivered.

### QUALITY ACCOUNT

We issued our unmodified assurance report on the Quality Account on 29 June 2018.

We reported our detailed findings in a separate report on 29 June 2018.

# FINANCIAL STATEMENTS

## OPINION

We issued our unmodified true and fair opinion on the financial statements on 25 May 2018.

## SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

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

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

## OUR ASSESSMENT OF RISKS OF MATERIAL MISSTATEMENT

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

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

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT AND AUDIT FINDINGS	CONCLUSION
<p><b>Management override of controls</b></p> <p>Auditing standards presume that a risk of management override of controls is present in all entities and require us to respond to this risk by testing the appropriateness of accounting journals and other adjustments to the financial statements, reviewing accounting estimates for possible bias and obtaining an understanding of the business rationale of significant transactions that appear to be unusual.</p>	<p>We have responded to this risk by:</p> <ul style="list-style-type: none"> <li>• Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements</li> <li>• Reviewing accounting estimates for bias and evaluated whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud</li> <li>• Obtaining an understanding of the business rationale for significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual.</li> </ul>	<p>We have no issues to report.</p>

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT AND AUDIT FINDINGS	CONCLUSION
<p><b>Revenue recognition</b></p> <p>Under auditing standards there is a presumption that income recognition presents a fraud risk. For Trust's, the risks can be identified as affecting the completeness, accuracy and existence of income.</p> <p>Our risk is focussed on non-NHS revenue which is not subject to formal third party agreement through the Agreement of Balances (AOB) process.</p>	<p>We carried out audit procedures to confirm our understanding of the Trust's internal control environment for the significant income streams, including how this operates to prevent loss of income and ensure that income is recognised in the correct accounting period.</p> <p>We tested substantively an increased sample of non-NHS income.</p> <p>We refined our risk assessment following completion of our interim audit and review of the draft financial statements.</p>	<p>We have no issues to report.</p>
<p><b>Fair value of property, plant and equipment (PPE)</b></p> <p>PPE is a significant balance on the Statement of Financial Position and there is a high degree of estimation involved in the value of these assets. There is a risk over the valuation of land and buildings where valuations are based on assumptions or where updated valuations have not been provided for a class of assets at year-end.</p>	<p>We reviewed the instructions provided to the valuer and reviewed the valuer's skills and expertise in order to determine if we can rely on the management expert.</p> <p>We confirmed that the basis of valuation for assets valued in year is appropriate.</p> <p>We reviewed valuation movements against indices of price movements for similar classes of assets and followed up valuation movements that appear unusual against indices.</p>	<p>Our review of the valuations and the skills and expertise of the management expert did not identify any material issues.</p> <p>We identified that revaluation gains totalling £280k had been recognised in the revaluation reserve when such gains should have been recognised in operating expenses as a reversal of impairments.</p> <p>Management adjusted the financial statements for this issue.</p>

## OUR APPLICATION OF MATERIALITY

We apply the concept of materiality both in planning and performing our audit and in evaluating the effect of misstatements.

We consider materiality to be the magnitude by which misstatements, including omissions, could influence the economic decisions of reasonably knowledgeable users that are taken on the basis of the financial statements.

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

The materiality for the financial statements as a whole was set at £6.3 million. This was determined with reference to a benchmark of gross expenditure (of which it represents 1.75 per cent) which we consider to be one of the principal considerations for the Trust in assessing the financial performance.

We agreed with the Audit Committee that we would report all individual audit differences in excess of £126,000.

## AUDIT DIFFERENCES

Our audit identified no material audit differences.

## TRUST ACCOUNTS CONSOLIDATION SCHEDULES

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

We reported the Trust Accounts Consolidation schedules were consistent with the financial statements.

## REFERRAL TO THE SECRETARY OF STATE

We referred a matter to the Secretary of State under section 30 of the Local Audit and Accountability Act 2014 in relation to the Trust breaking its statutory breakeven duty.

## ANNUAL REPORT

Other information in the Annual Report was not inconsistent or misleading with the financial statements or with our knowledge acquired in the course of our audit.

## ANNUAL GOVERNANCE STATEMENT

The Annual Governance Statement was found to comply with NHS Improvement's guidance and was not inconsistent or misleading with other information we were aware of from our audit of the financial statements, the evidence provided in the Trust's review of effectiveness and our knowledge of the Trust.

## REMUNERATION AND STAFF REPORT

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

## INTERNAL CONTROLS

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



# USE OF RESOURCES

## CONCLUSION

We issued an adverse opinion on the Trust's arrangements for securing economy, efficiency and effectiveness in its use of resources on 25 May 2018.

## SCOPE OF THE AUDIT OF USE OF RESOURCES

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

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

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

## OUR ASSESSMENT OF SIGNIFICANT RISKS

Our audit was scoped by our cumulative knowledge brought forward from previous audits, relevant findings from work undertaken in support of the opinion on financial statements, reports from the Trust including internal audit, information disclosed or available to support the Governance Statement and Annual Report, the Care Quality Commission's assessments of the Trust, and information available from the risk registers and supporting arrangements.

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

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT AND AUDIT FINDINGS	CONCLUSION
<p>The Trust was forecasting a control total deficit of approximately £53m in 2017/18 and was in the process of reviewing its medium term forecasts in light of the current financial position.</p> <p>The Trust has not yet set a medium term financial plan that returns the Trust to a break even position, however, the Mid and South Essex Sustainability and Transformation Plan seeks to move the local health economy to a balanced financial position.</p>	<p>We have responded to this risk by:</p> <ul style="list-style-type: none"> <li>• Reviewing the 2017/18 outturn</li> <li>• Reviewing joint working arrangements with Basildon &amp; Thurrock Foundation Trust and Southend Foundation Trust</li> <li>• Reviewing the 2018/19 budget and any medium term plans</li> <li>• Holding interviews with key officers</li> </ul> <p>The Trust achieved an outturn of £52.9m adjusted deficit compared to an original control total of £24.5m deficit in 2017/18 and had to secure additional borrowings which will need to be repaid to finance activities in the year.</p> <p>There still remains no sustainable medium term financial plan to return the Trust to financial balance or break even. In January 2018 the Trust agreed to merge with the other two acute Trust's in south Essex, with whom they also share a joint Executive team. A detailed business case to support the merger proposal was being drafted whilst we were completing our work, however the merger is expected to deliver financial savings through sharing of functions.</p> <p>The three Trust's joint working continues to develop and there has been greater alignment and harmonisation in the year of policies and processes.</p> <p>A 2018/19 budget has been prepared, reporting a forecast deficit of £47.3m requiring savings of £19.4m (or 5% of spend) to be delivered. This will present a significant challenge to the Trust in the forthcoming year. The Trust will need to ensure that there is sufficient capacity to deliver operational performance as well as work needed to progress any merger plans so that financial targets are achieved and high quality healthcare is delivered.</p>	<p>Our opinion was modified in respect of sustainable deployed resources.</p>

RISK DESCRIPTION	HOW RISK WAS ADDRESSED BY OUR AUDIT AND AUDIT FINDINGS	CONCLUSION
<p>The Trust's financial position deteriorated significantly during the year with the forecast deficit increasing from £33.6m to approximately £53m.</p> <p>The cost improvement programme was £9.5m adverse to plan as reported in December 2017 which has contributed to the increase in deficit, as well as rising agency costs linked to the high nursing vacancy rate and fines incurred. The Trust has also received a "no assurance" report from Internal Audit in relation to their report on the Cost Improvement Programme.</p>	<p>We have responded to this risk by:</p> <ul style="list-style-type: none"> <li>• reviewing the governance and monitoring arrangements in relation to the cost improvement programme</li> <li>• reviewing the progress in implementing Internal Audit recommendations</li> <li>• reviewing the Trust's workforce strategy and recruitment planning</li> <li>• reviewing action plans and arrangements in place to monitor and manage the level of agency spend</li> <li>• holding interviews with key officers.</li> </ul> <p>The Trust has had an exceptionally challenging year. The Trust achieved an outturn of £52.9m adjusted deficit compared to an original control total of £24.5m deficit in 2017/18 and had to secure additional borrowings which will need to be repaid to finance activities in the year. This highlights a significant deterioration in the financial position during the year and has been attributed to a number of factors:</p> <ul style="list-style-type: none"> <li>• substantial increase in pay, including agency spend linked to workforce shortages</li> <li>• non delivery of cost improvement programme schemes</li> <li>• lost income from commissioner challenges</li> <li>• changes in site leadership</li> <li>• management capacity</li> <li>• accountability and ownership of plans</li> <li>• clinical engagement</li> <li>• operational performance</li> <li>• weaknesses in financial controls.</li> </ul> <p>Internal Audit have issued a qualified opinion at the end of 2017/18 which the Trust has reflected appropriately within the Governance Statement, following the issue of a number of reports which identified control weaknesses in the Trust's arrangements. The Trust has made some progress in addressing recommendations made.</p> <p>The Trust has demonstrated an awareness of the issues arising during the year and has taken positive steps to address these. However, there is a recognition that time is needed to implement and embed new, more robust arrangements and that there is still more work to be done, particularly in relation to workforce.</p>	<p>Due to the significant deterioration in the Trust's financial position caused by a wide range of factors, we issued an adverse use of resources opinion.</p>

# QUALITY ACCOUNT

## CONCLUSION

We issued an unqualified assurance report on the Quality Account on 29 June 2018.

## SCOPE OF THE REVIEW OF THE QUALITY ACCOUNT

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

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

## SPECIFIED INDICATORS FOR TESTING

The core set of indicators to be included in 2017/18 Quality Account is set out in Regulations and the letter from NHS Improvement dated 26 January 2018. The Auditor Guidance has not been updated since 2014/15, and requires that we select two indicators for testing from the following list:

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

REQUIREMENTS	RESPONSE	FINDINGS
<p>Review the content of the report and consistency with specified documents.</p>	<p>We reviewed the contents of the Quality Account and compared this to the guidance and Regulations issued by the Department of Health and Social Care.</p> <p>We read the information included in the Quality Account and considered whether it was materially inconsistent with:</p> <ul style="list-style-type: none"> <li>• Board minutes and papers relating to quality reported to the Board</li> <li>• Feedback from Commissioners, Local Healthwatch and Overview and Scrutiny Committee</li> <li>• The Trust’s complaints report</li> <li>• Latest national patient survey and staff survey</li> <li>• Head of Internal Audit’s annual opinion over the Trust’s control environment</li> <li>• Annual Governance Statement</li> <li>• Care Quality Commission’s quality and risk profiles.</li> </ul>	<p>The Quality Account has been prepared in line with the Regulations.</p> <p>We reported to management where there were omissions or where additional information and disclosure was required to comply with the guidance issued by NHS England. These amendments have been made to the final published version.</p> <p>The Quality Account is not materially inconsistent with our review of the information we are required to consider.</p>
<p><b>Testing of percentage of patient safety incidents resulting in severe harm or death</b></p> <p>The Trust reported performance of 0.44% in respect of the indicator in the Quality Account.</p>	<p>We undertook testing to:</p> <ul style="list-style-type: none"> <li>• Confirm the definition and guidance used by the Trust to calculate the indicator</li> <li>• Document and walk through the Trust’s systems used to produce the indicator</li> <li>• Undertake substantive testing on the underlying data against six specified data quality dimensions.</li> </ul> <p>We tested of a sample of cases included in the reported performance.</p>	<p>We found no significant weaknesses in the systems use to produce the indicator. For each case tested, the information was agreed to underlying records and had applied the appropriate guidance.</p>
<p><b>Testing of percentage of patients risk-assessed for venous thromboembolism (VTE)</b></p> <p>The Trust reported performance of 78.53% in respect of the indicator in the Quality Account.</p>	<p>We undertook testing to:</p> <ul style="list-style-type: none"> <li>• Confirm the definition and guidance used by the Trust to calculate the indicator</li> <li>• Document and walk through the Trust’s systems used to produce the indicator</li> <li>• Undertake substantive testing on the underlying data against six specified data quality dimensions.</li> </ul> <p>We tested of a sample of cases included in the reported performance.</p>	<p>We found no significant weaknesses in the systems use to produce the indicator. For each case tested, the information was agreed to underlying records and had applied the appropriate guidance.</p>

# APPENDIX

## REPORTS ISSUED

We issued the following reports in respect of the 2017/18 financial year.

REPORT	DATE
Audit Plan	10 January 2018
Section 30 referral to the Secretary of State	20 May 2018
Audit Completion Report	22 May 2018
Report on the Quality Account	29 June 2018
Annual Audit Letter	12 July 2018

## FEES

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

AUDIT AREA	FINAL FEES £	PLANNED FEES £	PRIOR YEAR FEES £
Code audit fee	56,115	56,115	89,483
<b>Total audit</b>	<b>56,115</b>	<b>56,115</b>	<b>89,483</b>
Fees for audit related services - Quality Account	4,880	4,880	10,000
<b>Total assurance services</b>	<b>60,995</b>	<b>69,995</b>	<b>99,483</b>

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The matters raised in our report prepared in connection with the audit are those we believe should be brought to the attention of the organisation. They do not purport to be a complete record of all matters arising. No responsibility to any third party is accepted.

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