

**Royal Cornwall Hospitals NHS Trust**

**External Financial Review**

**Report to the South West Peninsula  
Strategic Health Authority  
May 2006**

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*The matters raised in this and other reports that flow from our review are only those which have come to our attention arising from or relevant to our work that we believe need to be brought to your attention. They are not a comprehensive record of all the matters arising, and in particular we cannot be held responsible for reporting all risks in the Trust or all internal control weaknesses. This report has been prepared solely for the use of South West Peninsula Strategic Health Authority and the Trust and should not be quoted in whole or in part without our prior written consent. No responsibility to any third party is accepted as the report has not been prepared for, and is not intended for, any other purpose.*

# 1 Introduction and scope of review

- 1 The Trust's financial plan for 2005/06 showed a balanced budget requiring savings of £7.53m. In month 7, the Trust reported to the SHA a risk to achievement of financial balance of £4.98m deficit. At month 10 this increased to £8.05m, £9.05m at month 11 and £10.43m at month 11+. The draft accounts submitted to the SHA/Department of Health and External Audit on 8 May 2006 showed a deficit of £15.687m.
- 2 KPMG LLP was appointed by the Department of Health to assess the Trust's readiness for Foundation Trust status, and a further review was completed by Devon Internal Audit.
- 3 We have been commissioned by the SHA to:
  - Validate the Trust's outturn deficit for 2005/06.
  - Validate the key evidence to support the outturn deficit.
  - Identify clearly the reasons for the deficit.
  - Identify the role of the following in financial management of the Trust and to identify weaknesses in control and/or decision making
    - Board
    - Audit Committee
    - Executive Team
    - Group General Managers
    - Clinical Directors
    - Finance Team
  - To establish the key actions required to address the weaknesses identified by this Review.
  - To review procedures and controls put in place, as part of the overall framework for improving financial governance and assess whether or not they will address any weaknesses identified in this review. To make specific proposals, as necessary, as to how the control environment can be strengthened.
- 4 Following the KPMG report, the Trust commissioned PwC to prepare a turnaround plan. This work is fundamental to securing the Trust's recovery. The PwC turnaround team is led by a director from our Business Recovery Service. At the time of writing this report, the turnaround plan was in the process of being compiled, and we make no comment on it in this report.

## 2 Executive summary

### Outturn

- 5 The budget for the year was balanced, including £7.5m of CRES savings. £11.1m of risks were recognised and reported to the Board at its July meeting. We observed that budgeting and forecasting was, in some cases, optimistically based on the previous year's results rather than a detailed plan. Other than Agenda for Change, risks were not formally monitored or tracked during the year.
- 6 The financial outlook of the Trust deteriorated rapidly in the second half of the year from a position of balance to a deficit of £15.7m, over twice the level of savings recognised in the budget, and significantly more than the total of risks identified.
- 7 Information was provided to the NEDs and Strategic Health Authority on the deteriorating position of the Trust but a number of assumptions and judgements were made in forecasting the outturn position which were not communicated. Even in the last month of the year the Trust was anticipating that significant savings would be achieved before the year-end. We calculated that the reporting process lacked transparency and rigour. The key changes to the reporting position in month 12 from £10.5m to £15.7m are set out in table 2 on page 6.
- 8 We have not audited the year end accounts but from our interviews with staff and conversations the external auditors we are informed that there may be a further increase in the deficit for 2005/6. This includes:
  - resolution of income due from the PCT of £1.6 million – there is a dispute with the PCTs whether activity completed near the year end was 2005/06 or 2006/07 activity. There is also some dispute on the level of creditors (£800k) and some of the balances relate to prior years. These amounts have been included in the adjustments line of the intra-NHS agreements. The external auditors will need to take a view on whether these amounts are correctly recorded in the accounts
  - Validity of fixed assets - management completed a fixed asset verification exercise and identified assets recorded on the register which were not still owned by the Trust. An estimated figure was made by the internal auditors but this was based on cost rather than net book value. In addition there were some outstanding queries on the items capitalised as part of the Knowledge spa project (approximately £500k). This could increase the charge to the income and expenditure account.
  - Valuation of stock – the Trust has a historic estimated figure for calculating the valuation of certain stock items – the external auditors are seeking additional support to the valuation of the stock. In our experience usually sufficient evidence can be produced to support an estimation.
  - Payroll – the external auditors have been unable to place full reliance over the controls in the new ESR payroll system and the audit was still ongoing when we discussed this with them. Usually sufficient testing and evidence can be provided to support the year end figure.
- 9 Based on our limited review and conversations with staff and auditors we do not believe that the deficit will decrease. If anything the deficit could increase to £17.2 - £18.5 m depending on the resolution of the PCT balances and whether all the costs affecting the knowledge spa are allowed.

### Role of individuals in financial management of the Trust

- 10 Roles and management structures in the Trust are not unusual, but information and follow through of decisions and plans is in our view poor. This means that the Board, whatever its composition and skill, will struggle to satisfy the requirement on it for financial stewardship and proper

governance. This can only be rectified through stronger leadership from the Board and management.

- 11 The Finance Committee papers were often tabled and did not cover well enough the significant issues. We concluded that the Committee was not in a position to conduct its business successfully.
- 12 We have not carried out a detailed assessment of the skills and experience of the Board or senior managers. What is striking is that although the financial position of the Trust has been weak for a number of years and there have been a series of attempts to rectify the underlying financial position, there does not appear in the record of the business of the Trust to have been any significant and sustained challenge internally of the financial position. This leads us to question whether the Board and management have the necessary skills to deal with the situation. A skills assessment needs to be completed to ensure that the Board has a balanced skill base.
- 13 Leadership of the Trust needs to be strengthened. New structures and financial management arrangements will not have any effect unless there is clear leadership from the Board.

### **Budget setting and Recovery plans**

- 14 The Trust needs to drive and own its budget but the timetable for signing and agreeing the LDP is often well into the new year. The Trust needs to agree its annual budget before the start of the year so that all managers are clear about their financial objectives. Annual budgets need to be driven from longer term plans, for at least 3 years, which identify key changes and issues, and can form a more robust basis for negotiation with commissioners and others.
- 15 Recovery plans need to be robust with clear actions, an assessment of financial impact, individual risk assessments of delivery and clarity on how saving will be made and monitored. The Trust is introducing groups such as the Performance Review Group. These forums need to raise the priority of recovery plans and hold individuals to account to deliver savings. The Board should receive regular updates of progress, including a balanced assessment of the prospect of achieving the plan, and should be ready to make decisions to deal with any shortfall. There are already arrangements in place for the management and monitoring of the Turnaround Projects in place.

### **Controls and finance**

- 16 The Trust is working with the turnaround team to identify savings plans which will be profiled over the year. Savings plans will need to be measured financially and monitored regularly to demonstrate that savings are being realised. In addition, other cost pressures will need to be identified promptly and reported by the groups *along* with proposals on how the overspend will be 'clawed' back so that balance will be achieved. The risk is that savings realised will be 'leaked' during the year on other cost pressures so having a nil impact on the overall position of the Trust.
- 17 We are aware that there have already been some changes to the financial controls and procedures. The challenge for the Trust is to change the culture of the organisation so individuals are accountable for their budgets. Arrangements are in place to improve the project management over action plans. However unless there is a change in the culture of the Trust (demonstrated from the top) that individuals will be held accountable, then these further controls or project management arrangements will not be effective.

## Conclusions

- 18 The Trust's financial position has deteriorated rapidly and significantly. Leadership in the Trust has not been sufficient to motivate and bring together everyone to bring about financial recovery. Plans were not sufficiently developed or detailed for action to be directed and monitored and financial information was not sufficiently developed for the Board and senior staff to manage effectively.
- 19 This review was carried out in very short measure to ascertain how the deterioration came about. Our key recommendations are that:
- Leadership needs to be strengthened at Board and Executive. Without effective individuals and teams at this level the situation is unlikely to improve, and important actions are unlikely to be followed through
  - All staff need to understand their individual and collective responsibility for finance. This will need clear documented and approved planning, monitoring and escalation processes and commitment from leaders to address issues effectively as they arise.
  - A clear plan for recovery needs to be established and seen through

These recommendations represent a significant programme of change for the Trust. Investment will be required in programme and project management, organisational development and performance management. The extent of this investment and the way it is deployed depends fundamentally on the leadership of the Trust.

### 3 Outturn position for 2005/06

- 20 The LDP was signed in July 2005 and final budgets were issued to group general managers (GGMs) four months after the start of the year.
- 21 The Trust submitted a balanced budget. However, during the budget setting process the Trust identified considerable pressure to make significant savings. Budgets were reduced. GGMs indicated to us that they felt that budgets were unrealistic; overspends in costs such as oncology drugs were therefore forecast at the start of the year. There appeared to have been a lack of acceptance of the challenges of making savings or reducing expenditure. There was a lack of ownership of the budgets at all levels. We were unable to identify any sustained additional action to identify further realistic recovery plans or to mitigate the risks identified.
- 22 Some of the risks identified at the start of the year within the groups, materialised into key cost pressures ('hotspots') and were monitored during the year.

#### Observations

- 23 *The LDP and consequently the budgets were agreed after the year-end. If the Trust is going to effectively manage its budget then this needs to be set and monitored at the start of the year. Inevitably the LDP will be agreed after the year end and any subsequent variations should be recognised as budget variations. In addition, the Trust did not have a medium term financial strategy which identified in detail potential risks, a range of options and high level plans for reducing cost. Without this it was unable to engage with staff to achieve the savings required over a very short period of time. We recommend that the Trust build on the turnaround to develop a longer term financial plan.*
- 24 The budget includes £7.5 million of CRES savings. Although some of this was attributed to specific actions, detailed plans were not in place in every case. Additionally the original budget included a number of high risk assumptions amounting to about £11 million, reported separately to the July Board meeting, as follows:

**Table 1:**

<b>Risks identified</b>	<b>Value £000</b>
Agenda for Change	2,500
Capital charges	2,100
Reduce 4/5 outturn recognition	2,000
Increase non recurring recovery plan target	1,500
Additional PMS contribution	1,000
Budget reductions for activity changes	1,000
Anticipated increase in stock and year end income	1,000
<b>Total</b>	<b>11,100</b>

#### Observations

- 25 *The above risks were identified as part of the budget finalisation but Agenda for Change was the only item that was regularly tracked and reported. We found no evidence that actions to mitigate the other risks were formally developed or reported.*
- 26 The new Director of Finance and Information (DoFI) presented a report to the Finance Committee on 19 May 2006 including a reconciliation of the month 11 deficit of £10.5 million to the outturn deficit of £15.687 million:

**Table 2:**

	<b>£000</b>
Position at month 10	10,500
Underestimation of capital charges	2,034
Impact of in year budget adjustments	1,996
Increase in stock anticipated but did not materialise	528
Impact of anticipated year end income which did not materialise	451
Costs above trend – net position	362
Net balance of minor changes	(184)
<b>Position at month 12</b>	<b>15,687</b>

## Capital charges

- 27 In 2004/05 the Trust extended some fixed asset lives and there was slippage on the capital programme. Overall this reduced the level of capital charges in 2004/05. The budget for capital charges for 2005/06 was based on the assumption that the capital programme would continue to slip and following the District Valuer's (DV) revaluation there would be a similar reduction in capital charges.. The Chief Executive (CE), DoFI and Head of Finance met on the 30 June 2005 and as part of the 'creation of a balanced budget' paper, they took the decision to reduce the budget for capital charges by £2.1 million.
- 28 This was one of the risk areas identified at the start of year to achieve a balanced budget(as detailed in table 1) and was flagged as a significant risk flagged in the July finance papers but there was no detail to justify how this level of saving would be achieved.
- 29 External audit raised a number of concerns in their SAS 610 report on the 2004/5 audit about the Trust's capital accounting. The Trust responded by implementing a new asset register and appointing a new capital accountant. All assets were transferred to the new system in January. A capital charges forecast report was run from the new system which seemed to confirm the £2 million reduction in capital charges. However, we are informed by the Head of Finance and the capital accountant that the wrong report was run and when the correct report was re-run at the end of the financial year it showed there was an overspend of £2 million on capital charges. When the initial report was run there appeared to be no challenge raised on the accuracy of the figure against the budget 'risk' and savings which was the correct report was run proved to be an accurate estimation of the charges.
- 30 Internal audit have completed a review of the fixed asset system but this has been a traditional audit of the controls over fixed assets rather a review of the new system being implemented. Given the higher risks usually associated with implementing a new system, we were surprised that they were not involved in any of the implementation and testing of the new system, the controls and project management and that this was not included as a higher risk in the audit plan which the audit committee would have wanted assurance on.
- 31 Although there was some slippage of the 2005/06 capital programme, the rebasing of asset lives, the DV's revaluation and revenue to capital transfers did not net to the anticipated £2 million.

## Observations

- 32 *The reduction in the capital charges by £2.1 million was over-optimistic. The amount was based on the assumption that the lower capital charges in 2004/5 would continue into 2005/6, but there was no detailed analysis to show that this would be the case. We found no evidence of monitoring during the year to ensure that capital charges were in line with expectations.*

## Impact of budget adjustments

- 33 Every month the CE, DoFI and Head of Finance met to discuss the summary budget position. Variances to date were reviewed with straight line projections to the year end. GGMs were required to provide a revised year end group forecast to supplement the overall straight line view.
- 34 At this meeting the CE and DoFI would make judgements as to the further savings that could be achieved. However, we could not find detailed working papers or support to justify their assumptions. We found no evidence of detailed plans to deliver these amounts.
- 35 Therefore the monthly year end forecasts were significantly understated and there was also no communication to the NEDs of the judgements that had been made in the forecasts.

### **Observations**

- 36 The DoFI did not produce financial management information setting out risks and the range of realistic outturns which could be reviewed by Executive Directors and NEDs. In addition assumptions made by the DoFI and CE were not communicated to the Board effectively and there was no adequate follow-up to ensure that assumptions and risks were being managed. In our view, this process lacked transparency and rigour.

## Stock adjustments

- 37 In previous years the levels of stock have increased at the year end as part of the year-end closedown. An assumption was made that this would continue this year and was one of the risk included this in balancing the LDP (see table 1). However, stock balances did not increase at the year-end and the additional 'savings' were not realised.

### **Observations**

- 38 *We would not expect any significant fluctuations in stock levels unless there are fundamental changes in the service. Adjustments at the year-end are not a reliable predictor of future performance. We concluded that the assumption made was flawed. We found no detailed supporting analysis.*

## Impact of anticipated year end income

- 39 In previous years additional income has been received from the Department of Health as a late allocation. This was built into the LDP although no formal confirmation had been received that this income would be receivable.

### **Observations**

- 40 *Although though this was included as a risk, we found no detailed support to show how this would be achieved or any evidence of monitoring.*

## Further risks to the 2005/06 outturn

- 41 We have not completed a detailed audit of the year end figures which will be completed by external audit in the forthcoming month. However, the following risks to the reported year end position have already been identified from our meetings with Trust staff and our interviews with external audit

### **Fixed asset validation**

- 42 Following recommendations made by external audit in 2004/05 and internal audit in the current year, management has just started a full fixed asset verification exercise. A number of issues were raised about the assets contained in the fixed asset register and whether the assets were still owned by the Trust. There is currently uncertainty as to the effect this will have on the current year's capital charges, although it is expected that they will increase. The figures provided by internal audit were based on cost rather than net book value. In addition the external auditors are

investigating whether all expenditure charged to capital (Knowledge spa was of a capital nature) and there is approximately £500k that is being investigated.

**PbR income**

43 There are unresolved disputes with the PCTs up to £1.6 million. There is a dispute with the PCTs whether activity completed near the year end was 2005/06 or 2006/07 activity. There is also some dispute on the level of creditors (£800k) and some of the balances relate to prior years. These amounts have been included in the adjustments line of the intra-NHS agreements. The external auditors will need to take a view on whether these amounts are correctly recorded in the accounts. These amounts have not been included in the forecast outturn.

**Stock valuation**

44 The Trust has used a historic estimated figure for the basis of valuing stock which is not substantiated and external audit are looking for additional support for this figure. In our experience we typically find that sufficient evidence is provided to support the overall figure.

**Payroll**

45 External audit have informed us that they have not been able to rely on controls in place over the ESR system and this is area of the external auditor's work was outstanding at the time of writing this report and may impact the income and expenditure figure.

## 4 Financial management

### Groups

- 46 The finance department was restructured in 2004/05. There are now five assistant Directors of Finance (ADFs). Three of these ADFs support the five main clinical groups. The ADFs meet with the Group General Managers (GGMs) on a regular basis and review the budget statements on a monthly basis. The ADFs are expected to provide financial support and challenge to the group finance.
- 47 During the 2005/06 financial year the groups did not receive final budgets until July 2005. This was due to the delays in agreeing the LDP. The budgets set for each group were based on a balanced financial outturn. The GGMs were forecasting deficits at the start of the year which were in line with the actual achievement at the year-end. From our interviews individuals felt that the budget was imposed and consequently not 'owned' by the groups. Insufficient action was taken to identify recovery plans or reduce expenditure.
- 48 GGMs receive monthly budget statements from finance. These reports are in an excel format and agree to the ledger. However, during 2005/06 the presentation of the budget statements was not consistent across the groups. Following the new Business Forum meeting in May 2006, a decision was made to standardise the budget statements.

### Observations

- 49 *The level of financial challenge and support varies across the groups. The ADFs were not always challenging enough of the GGMs when reviewing the monthly budget statements. However the GGMs should be accountable for any overspend and for identifying ways of finding further savings plans to deliver a financial balance. Going forward the ADFs need to robustly challenge the GGMs regularly and they must also work together to identify and deliver recovery schemes. The Executive should hold the GGMs to account for balancing their budgets and ensure that realistic and detailed action plans are in place. This needs to be supported by the leadership of the Executive and NEDs where the groups and GGMs are held to account*
- 50 *The culture of the Trust is such that the key priority is achieving and delivering patient related targets. We recognise that these are key targets but by always focussing and aiming to deliver the optimum patient care, priority is not always given to the financial implications of decisions made.*

### Recovery plans

- 51 During the 2005/06 financial year there was an inconsistent approach to recovery planning. There was no performance reporting framework to monitor the progress of the various plans. The original CRES schemes identified were £7.5 million. This was apportioned to the groups and corporate schemes. The clinical groups were responsible for identifying, managing, monitoring and delivering the saving plans. From our interviews with the GGMs, they felt that there was limited challenge in the Executive meetings on the delivery of specific schemes, and the main focus of these meetings was on achievement of breakeven overall.

### Observations

- 52 *We have identified that there were a number of gaps in the recovery targets assigned to groups. Other plans included specific actions, but these did not have financial targets.*
- 53 *There was an inconsistent approach to developing plans and actions to deliver them within the groups. There was no detailed monitoring and tracking of recovery plans to identify slippage/delivery of the plans or the adequacy of the plans in place. Management have confirmed that assumptions were made when reporting the financial delivery of plans, without the supporting financial evidence.*

- 54 *Furthermore as there were gaps there were no contingency plans in place to respond to in year financial cost pressures.*
- 55 *During the year reporting on recovery schemes to the Board was completed at a high level (Trust basis rather than individual group basis). Without sufficient detail it is difficult for the Board to understand the complete picture of the pressure points in the Trust. We noted that the minutes of the finance committee reported further contingency plans were required for the year but it is unclear if this action was taken and provided to them.*

## **Finance Committee**

- 56 The Trust has a finance committee of three NEDs which meet on a monthly basis. Finance papers were presented to each meeting, although there is limited evidence of effective challenge of the financial position at these meetings. The Committee received a narrative statement of the Trust's position and tables showing the summary budget, actual and forecast income and expenditure. The reports contained descriptions of reasons for variances and identified new risks as they emerged but did not address some of the high risks in the original plan. We concluded that the narrative was not sufficiently substantial and did not cover the key risks and issues satisfactorily. In addition, there were no robust arrangements for managing and reporting progress on CRES targets.
- 57 The Chair of the Finance Committee informed us that additional information was requested, but this was not minuted and there is no evidence that action was taken to address this further via the Board or the Chair.

## **Observations**

- 58 *We consider the detail in the finance papers, which were prepared during the 2005/06 financial year, to be inadequate. The detail in the narrative commentary was limited and there were no clear links between the issues affecting the financial position of the Trust and the actions being taken.*
- 59 *It is difficult to track risks through from consecutive Board papers. For example in the 13 September 2005 finance paper, it is documented that the Trust needs to seek additional non recurring solutions over and above the £1 million already in the Recovery Programme and a further £1 million savings from infrastructure costs. However, these risks are not reported in subsequent finance papers.*
- 60 *There has been a lack of training on finance and consequently a lack of robust challenge by the NEDs. This limits the ability of NEDs to impact the financial governance at the Trust.*
- 61 *Currently the finance papers can be presented to the finance committee up to six weeks after the month end to which the information relates. This is then presented to the Board later in the same month. With a deteriorating financial position the information is quickly out of date and subsequently informed decisions cannot be made. Finance information is often tabled at the meetings. This does not allow individuals sufficient time to review the content of the report and enable adequate and informed challenge.*
- 62 *The NEDs are responsible for challenging the information that is being presented by the Executives. If this is insufficient for them to monitor the Trust's financial position effectively (e.g. CRES savings actually being achieved) then they need to escalate their concerns to either the Board or the Chair to ensure that further information is provided*
- 63 *From May 2006 all non-executives will attend the finance committee and meetings will be held on the same day as the Board to ensure attendance. We have been informed that the meeting dates*

*are being reviewed to ensure financial information is tabled within three weeks of the month end. This will significantly improve the reporting of the financial information.*

- 64 Financial problems of the Trust have historically attributed to by external factors and influences. For example, the impact of the national and local tariff and previously the market Forces Factor has been debated by the Executives and NEDs for a number of years. The Trust has a significantly lower resource for the activity it undertakes, compared with national averages.
- 65 However with the introduction of Payment by Results and the National tariff is applied to an increased number of activities and procedures. The Trust needs to clearly identify which activities are affordable within tariff and which are net costs to the Trust. This has not been completed.

#### **Observations**

- 66 *Income is not matched to the related additional activity. Strategic decisions cannot be made on case mix. The Trust needs to analyse the actual costs for performing specific procedures, to enable management to evaluate accurately the net impact of increased activity.*

#### **Board**

- 67 Finance papers were presented to the Board, at each of their meetings by the Director of Finance and Information, except May 2005. There were no Board meetings in April, August and January.
- 68 During the year it was noted that the summary finance papers which were taken to the Board did not provide enough detail. Therefore the supporting tables, which were presented at the finance committee, were also taken to the Board.

#### **Observations**

- 69 *Following our review of the reports presented to the Board and finance committee we are concerned with the level of detail. The information presented is not sufficient to enable committee members to make informed decisions*
- 70 *Although the standard of reports were poor, the Board informed that there was a deteriorating financial position in the year but not the full extent of the year end position until recently. There were also two papers at the September and October 2005 meetings regarding contingency planning. There were a number of possible schemes proposed but there did not appear to be any significant decisions made on some of the more risky approaches. It appears that there was reluctance by the Board to make any contentious decisions that could have caused local opposition or that would have affected targets. They also appear to place reliance on the DoFI to identify additional savings plans or optimism that it would be resolved at the year-end.*

#### **Audit Committee**

- 71 The Trust has had a number of external reviews and receives reports from the external auditors. There is no comprehensive tracking system in place to monitor the implementation of the recommendations made in these reports. For example the external auditors raised issues in their accounts report over the controls over capital. The Trust's responses in a number of the points were 'ongoing'. No monitoring is completed after the initial presentation of the report to ensure that the action has been fully implemented.

#### **Observations**

- 72 The audit committee members need to be satisfied that actions and recommendations from all external reports made are fully implemented and are operating effectively.

## 5 Framework for improving financial governance

- 73 Following the appointment of the new DoFI we are pleased to see that a number of new financial management arrangements have been setup from April 2006. Most of these new changes in relation to the timetable for month end reporting were reported by the DoFI to the finance committee at their meeting in May 2006.
- 74 Previously the main Trust wide meeting group was the monthly Executive Meetings. These meetings are still held and there are now the following new groups in place;
1. Business Forum group
  2. Performance Review group
  3. Recovery Programme Project group
- 75 Furthermore there is also a documented financial controls procedure, which has been sent to NEDs, GGMs, ADFs and Clinical Directors. This paper outlines the new controls in place around procurement and staff. Previously these controls were not formally documented and different groups were using different approval limits.

### **Observations**

- 76 *The Trust has had a number of reviews completed in the past which has number a number of recommendations to improve the control procedures. To implement these controls effectively the Trust needs to be assured that the staff in place are appropriately qualified for their role and responsibilities. In addition the skill and experience of the Executive and the Non-Executives to lead and change the control and culture of the Trust. Until this is addressed further controls will not be effective or change the financial management and governance of the Trust.*

### **Internal audit**

- 77 We have discussed the profile of internal audit with the internal auditors who felt that recommendations was not always implemented promptly or given the sufficient priority. In addition the scope of the audit plan was also discussed. They felt that their resource was reduced by the finance team. Where resources are restricted, then the plan should focus on the key risks and assurance and where there is insufficient time to address these areas any concerns should be raised with the audit committee chair.
- 78 The internal audit completed a review of the financial balance and recovery plans which was finalised in March 2006. The report provided a number of positive assurances including monitoring of the progress of the recovery plan by the Executive team. They reported that there was a shortfall of savings schemes of £3.741m but they had been informed by the Head of Finance that the outstanding balance of savings plans had schemes in place to make savings. The key action points in the executive summary included the following points; action plans were not clear, financial risk was not included in the risk register and the recovery plan did not include contingencies. Whilst the report identified some of the failings of the recovery plans, we felt that tone of the report did not reflect the seriousness of some issues. A more direct and stronger conclusion to the audit committee of the issues would have assisted the Non-executives understanding of the position.

### **Observations**

- 79 *The audit committee should review the effectiveness of the internal audit provision and ensure that the resources address the key risks facing the Trust on a timely basis provide the necessary assurances for the NEDs.*

## **Finance staff**

- 80 The finance structure has been in place for over 12 months. There continues to be an over-reliance on the Head of Finance which, during the course of our work, we observed caused some bottlenecks. The new Director of Finance now presents the finance committee reports rather than relying on the detail from the Head of Finance. However we feel that there could be further delegation of tasks to the assistant heads of finance. There is an opportunity to review the skills mix required to strengthen the roles of the assistant heads of finance.

## 6 Summary of findings and agreed actions

Issue	Action Required	Action Plan
<p>The risks identified as part of the budget process finalisation other than Agenda for Change were not regularly tracked and reported. We found no evidence that actions to mitigate the other risks were formally developed or reported.</p>	<p>Risks identified as part of the budget setting process should be tracked and monitored throughout the year. The Executive Directors and NEDs should monitor and challenge the progress on the risks and ensure that they are followed through.</p>	
<p>The DoFI did not produce financial management information setting out risks and the range of <i>realistic</i> outturns which could be reviewed by Executive Directors and NEDs. In addition assumptions made by the DoFI and CE were not communicated to the Board effectively and there was no adequate follow-up to ensure that assumptions and risks were being managed. In our view, this process lacked transparency and rigour.</p>	<p>Financial information should be produced which includes the following:</p> <ul style="list-style-type: none"> <li>• Realistic range of worst, best and most likely outturn figures along with the associated risks in achieving these outturn figures</li> <li>• Any assumptions made by the DoFI and CE that affect the outturn figure should be clearly communicated in the papers presented to the Board</li> <li>• Progress or changes to assumptions should be monitored by the Executive Directors and NEDs</li> </ul>	
<p>Assumptions made by the DoFI and CE in outturn reports were not communicated to the Board effectively and there was no adequate follow-up to ensure that assumptions and risks were being managed.</p>	<p>Outturn reports should include details of any assumptions made by the Directors such as the level of savings that will be achieved.</p> <p>Risks and emerging issues should be clearly tracked and monitored from each meeting.</p>	

Issue	Action Required	Action Plan
<p>Financial management is the responsibility Finance, Executive Directors and GGMs. Whilst a number of staff at various levels (e.g. finance staff, GGMs and Executive Directors considered that the ADFs did not effectively challenge the GGMs to make a positive impact in the delivery of financial targets, it is the responsibility of <i>all</i> staff GGMs and the Executive to deliver services within budget.</p> <p>There was an inconsistent approach to developing plans and actions to deliver them within the groups. There was no detailed monitoring and tracking of recovery plans to identify slippage/delivery of the plans or the adequacy of the plans in place. Furthermore as there were gaps there were no contingency plans in place to respond to in year financial cost pressures.</p> <p>During the year reporting on recovery schemes to the Board was completed at a high level (Trust basis rather than individual group basis).</p>	<p>GGMs should be monitored against their responsibilities to deliver services within budget. This can be assisted by the ADFs providing financial support is offered to GGMs throughout the year to identify and calculate potential savings. They also need to robustly challenge the actual performance during the year.</p> <p>The Executive Directors should hold the GGMs to account for delivery of balanced budgets. This will include monitoring of detailed action plans to achieve savings.</p> <p>Sufficient detail needs to be presented to the Board so they can understand the pressure points within the Trust. There needs to be a clear link between the issue affecting the financial position of the Trust and the actions being taken. We are informed that this has already been implemented through the new Performance Arrangements.</p>	
<p>The timing of finance committee and Board meetings are too far after the month end to ensure the facilitation of effective decision making. Finance information is often tabled at the meetings.</p>	<p>We have been informed that the meeting dates are being reviewed to ensure financial information is tabled within three weeks of the month end. This will significantly improve the reporting of the financial information.</p>	<p>Agreed this has already been implemented.</p>

Issue	Action Required	Action Plan
<p>NEDs have significant responsibilities for ensuring the performance of the Trust. The skill mix of the NEDs and their ability to effectively challenge Executive Directors is key to monitoring financial performance of the Trust.</p> <p>From our interviews with NEDs and review of the minutes we were informed that they were not always able to effectively challenge the Executive Directors.</p> <p>The NEDs have not had the required training to be able to effectively challenge the financial information reported to them.</p>	<p>The Trust needs to review the current skill base of the NEDs to ensure that individuals are appropriately skilled in all key areas of the Trust's activities particularly finance.</p> <p>NEDs need to fully understand their personal responsibility and accountability for the financial outcome of the Trust. If individuals feel that they are not receiving adequate explanations or sufficiently detailed information then requests need to be escalated to the Board or Chair (and minuted as such) until sufficient explanation or information is received.</p> <p>The Trust should ensure that the NEDs have received sufficient training/briefings to understand NHS accounts and budget statements.</p>	
<p>The Trust has had a number of reviews completed in the past which has number a number of recommendations to improve the control procedures. To implement these controls effectively the Trust needs to be assured that the staff are appropriately qualified for their role and responsibilities. In addition, the skill and experience of the Executive and the Non-Executives to lead and change the control and culture of the Trust. Until this is addressed further controls will not be effective or change the financial management and governance of the Trust.</p>	<p>A review of the structures in the organisation needs to be completed and a skills audit of existing staff including the Executive Directors and Needs to determine if they have relevant skills and drive to lead and change the control and culture of the Trust.</p> <p>Once this is completed a detailed review of the procedures, controls and reporting of the Trust needs to be completed to ensure that there is financial management and governance of the Trust.</p>	

Issue	Action Required	Action Plan
<p>The LDP and consequently the budgets were agreed after the year-end. If the Trust is going to effectively manage its budget then this needs to be set and monitored at the start of the year. Inevitably the LDP will be agreed after the year end and any subsequent variations should be recognised as budget variations. In addition, the Trust did not have a medium term financial strategy which identified in detail potential risks, a range of options and high level plans for reducing cost. Without this it was unable to engage with staff to achieve the savings required over a very short period of time.</p>	<p>Budgets need to be set at the start of the year and LDP changes set as budget variations so there is clear accountability from day one of the new year.</p> <p>We recommend that the Trust builds on the turnaround plan to develop a longer term financial plan.</p>	
<p>From our interview with the internal audits and our review of the internal audit reports, internal audit did not seem to have a high profile in the Trust. We were surprised by the lack of involvement of internal audit in its programme of some of the risks and changes in the Trust. From reviewing reports on areas such as financial standing, the tone of the report we felt did not match some of the seriousness of the issues.</p>	<p>The audit committee should review the effectiveness of the internal audit provision and ensure that the resources address the key risks facing the Trust on a timely basis provide the necessary assurances for the Needs.</p>	
<p>Income is not matched to the related additional activity. Strategic decisions cannot be made on case mix.</p>	<p>The Trust needs to analyse the actual costs for performing specific procedures, to enable management to evaluate accurately the net impact of increased activity.</p>	

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