

Practical Guide

AUDIT

NHS Audit Committee Handbook

Third Edition

Shaping healthcare finance



Published by the Healthcare Financial Management Association (HFMA),
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This guide was produced by Healthcare Financial Management Association (HFMA). The editor was Anna Green.

Cover design was undertaken by Mike Wyatt, setting by Academic + Technical Typesetting and printing by ESP Colour Ltd.

The NHS is always changing and developing – this edition reflects the structures and processes in place in May 2014. We are keen to obtain feedback on ways in which the content, style and layout can be improved to better meet the needs of its users. Please forward your comments to info@hfma.org.uk or to the address above.

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ISBN 978-1-904624-83-7

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Foreword and Introduction

Welcome to the 2014 version of the *NHS Audit Committee Handbook* which is designed to help NHS governing bodies and audit committees as they review and continually re-assess their system of governance, risk management and control to ensure that it remains effective and 'fit for purpose' across all that an organisation does. It has been developed by the HFMA's Governance and Audit Committee to provide a self-contained source of guidance for all members of audit committees and will also be of interest to those who serve on governing bodies.

The Handbook replaces the 2011 edition and, although it has been fully updated to take account of the many changes that the NHS has seen since then, the underlying principles, structure and content of the Handbook will be familiar to many. In particular, it continues to provide audit committee members with a succinct summary of what is expected from them and a series of practical tips and pointers to help them put the theory into practice.

In response to comments from users of the Handbook, we have also:

- Compared our guidance with other relevant documents including the *UK Corporate Governance Code*; the Financial Reporting Council's *Guidance on Audit Committees*; the Treasury's *Audit and Risk Assurance Committee Handbook*; Monitor's *Code of Governance and Audit Code* and the *NHS Wales Audit Committee Handbook*
- Reduced the number of appendices with relevant references included in the main body of the guidance.

As with earlier versions, this Handbook applies to NHS organisations in England – however, the principles and much of the practical guidance is broadly relevant across the rest of the UK. In terms of its content, the Handbook starts by explaining why governing bodies need audit committees and how they provide support in fulfilling statutory duties and organisational objectives. It then looks at how audit committees should be set up before moving on to focus in detail on what they do and how they work with others. Practical examples and case studies are included throughout to bring the theory to life and cross references to further sources of guidance are included both within the text and as an appendix.

Audit committees and their members continue to play a crucial role in the governance of every NHS organisation and members must take seriously their responsibility for scrutinising the risks and controls affecting every aspect of the business – not just in the finance and financial management sphere. We hope that you find this Handbook of real practical benefit as you carry out this demanding role.

If you have any comments or suggestions about how we could develop the Handbook in future, please let us know via publications@hfma.org.uk

Kevin Stringer
Chair, HFMA Governance and Audit Committee

Acknowledgements

This Handbook was developed by the HFMA's Governance and Audit Committee. The HFMA is grateful to all those who attend the committee's meetings (either as full members or guests) and their employing organisations for their help and support. In particular we would like to thank:

Kevin Stringer (Chair of the committee), Chief Financial Officer, The Royal Wolverhampton Hospitals NHS Trust
Francesca Annetta, Head of Finance, Care Quality Commission
Laura Brackwell, National Audit Office
Rod Barnes, Executive Director of Finance and Performance, Yorkshire Ambulance Service NHS Trust
Steve Connor, Deputy Director, Mersey Internal Audit Agency
Derek Corbett, Director of Audit, Barts and The London NHS Trust
Paul Dudfield, Consortium Director, CW Audit Services
David Gregory, Head of Internal Audit, Leeds Teaching Hospitals NHS Trust
Andrew Kendrick, Technical Manager, Audit Commission
Jenny McCall, Director of Audit, Audit South West
David Milner, Associate Manager (Health), Public Sector Consultants
Glen Palethorpe, Partner, Risk Advisory, Baker Tilley
Val Peacock, Head of Audit, City Hospitals Sunderland NHS Foundation Trust
Antony Rodden, Director, Shared Services Task Force
Phil Rule, Director, PHP Consulting Limited
Phil Sharman, Director of Audit and Assurance, NHS Wales Shared Services Partnership
Pat Shroff, Independent Consultant
Michael Townsend, Regional Managing Director, TIAA
Paul Traynor, Director of Finance, East and North Hertfordshire NHS Trust
Joanna Watson, Senior Manager, PriceWaterhouseCoopers
Clare Winch, Head of Assurance, Oxford University Hospitals NHS Trust
Lynn Wilson, Director of Performance, TIAA
John Yarnold, Independent Consultant, Mount Vernon Consulting.

The HFMA is also grateful to all those who commented on drafts of the Handbook.

The Handbook was edited by Anna Green, Technical Editor, HFMA.

Chapter 1: Why the Governing Body Needs an Audit Committee

This chapter explains that every governing body/board¹ is required to have an audit committee to support them in fulfilling their statutory and organisational objectives. It summarises the key ways in which audit committees provide this support.

1.1 Why a Governing Body Has an Audit Committee – the Statutory Basis

Every NHS organisation is required to have an audit committee that reports to its governing body.² The formal requirements to have an audit committee are set out in different documents, depending on the organisation:

- For clinical commissioning groups (CCGs), s14M of the *NHS Act 2006* (inserted by s25 of the *2012 Act*) and NHS England's *Model Constitution Framework* (section 6.6.3)
- For foundation trusts (FTs), *Monitor's NHS Foundation Trust Code of Governance*
- For non-foundation NHS trusts, the *NHS Trust Development Authority's Code of Conduct and Accountability*.³

1.2 What Does the Audit Committee do to Support the Governing Body?

NHS governing body members have a daunting task in overseeing some of the largest and most complex organisations in the country. To fulfil this role it is the governing body's responsibility to put in place governance structures and processes to:

- Ensure that the organisation operates effectively and meets its statutory and strategic objectives
- Provide it (i.e. the governing body) with assurance⁴ that this is the case.

However, even the best structures and processes can let down an organisation if they (and the assurances they provide) are not operated with sufficient rigour – this is where audit

¹ For many organisations the governing body is known as the board. In foundation trusts there is also a Council of Governors. To avoid repetition, we have used the generic term 'governing body' throughout this Handbook.

² All NHS bodies are required to have a governing body (or board) which comprises both executive and non-executive directors (NEDs)/lay members. This governing body is separate from the day-to-day management structure. The exact structure of each governing body is different for each type of NHS body and is set out in legislation and associated regulations. For non-foundation NHS trusts the relevant legislation is regulations 2 and 4 of the *1990 Trust Membership and Procedure Regulations (SI 1990/2024)*. For FTs, there is a board (or 'council') of governors and a board of directors as required in schedule 7 to the *NHS Act 2006*. For clinical commissioning groups (CCGs), the requirement to have a governing body (that has its functions delegated to it by the CCG 'council of members' on which all the CCG's constituent GP practices are represented, is set out in s14L of the *NHS Act 2006* (inserted by s25 of the *2012 Act*) and the associated regulations (SI 2012/1631).

³ *Code of Conduct and Accountability*, NHS Trust Development Authority, 2013: www.ntda.nhs.uk/wp-content/uploads/2013/04/CODE-OF-CONDUCT-AND-ACCOUNTABILITY-FOR-NHS-BOARDS.pdf

⁴ Assurance is defined by the Treasury in *The Orange Book: Management of Risk – Principles and Concepts* as 'an evaluated opinion, based on evidence gained from review, on the organisation's risk management and internal control framework'.

Chapter 2: How to Set Up and Support an Audit Committee

This chapter focuses on how audit committees are constituted and how they operate in practice. It also looks at the implications of collaborative arrangements that may exist in clinical commissioning groups and at the importance of reviewing the committee's own effectiveness via regular self-assessments.

2.1 How Many Members Should an Audit Committee Have?

The Treasury's guidance as set out in its *Audit and Risk Assurance Committee Handbook* should be followed – this states that audit committees should comprise at least three non-executive directors (or lay members).¹

2.2 Who are the Members of the Audit Committee?

The distinctive characteristic of the audit committee is that it comprises independent, objective non-executive directors (NEDs) or lay members² who are appointed by the organisation's governing body. In other words, audit committee members should satisfy the governing body's definition of 'independence' and:

- **Not** be employed by the organisation (other than in their capacity as members of the audit committee)
- **Not** claim a significant proportion of their 'trading income'³ from the organisation.

In foundation trusts (FTs), Monitor's *Code of Governance* (provision C.3.1) states that 'the board of directors should establish an audit committee composed of at least three members who are **all** independent non-executive directors'. For non-foundation trusts and clinical commissioning groups, the Department of Health's 2013 consultation paper *Health Service Bodies Audit Committees*⁴ proposed that the committee should 'normally, wholly or mainly, comprise of independent non-executive members of the governing board' and that it must have a majority of independent non-executive members.

¹ This is in line with the requirement set out in the FRC's 2012 *UK Corporate Governance Code* which requires boards in the private sector to establish an audit committee of at least three, or in the case of smaller companies, two independent non-executive directors. Monitor's *Code of Governance* builds on the UK Code and requires foundation trusts to establish an audit committee composed of NEDs which should include at least three independent NEDs.

² For clinical commissioning groups, schedule 2, paragraph 7 (3) of the *Health and Social Care Act 2012* says that 'Arrangements... **may** include provision for the audit committee to include individuals who are not members of the governing body.' However, NHS England's *Model Constitution Framework* for CCGs recommends that they should follow the *NHS Audit Committee Handbook*.

³ Trading income refers to income received from the organisation for services provided. This does not include a fee or expenses that may be received for serving as a NED or lay member.

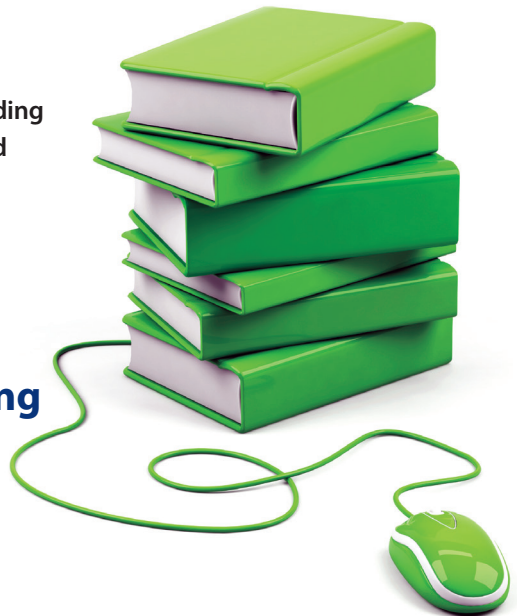
⁴ At the time of writing (April 2013), the Department's guidance had not been finalised. For the latest position go to: <https://www.gov.uk/government/consultations/new-requirements-for-nhs-audit-committees>

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ISBN 978-1-904624-83-7

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