



2020/21 year-end reminders for non-executive directors and lay members



This paper is intended to provide non-executive directors and lay members with key reminders as they review their 2020/21 annual report and accounts. Issues should be brought to the attention of the audit committee throughout the year and discussed as early as possible. This paper briefly sets out the main issues to be aware of for the 2020/21 annual report and accounts as well how they may be considered by non-executive directors and lay-members.

Further information for finance teams is included in the HFMA's *2020/21 annual report and accounts checklist*.¹ This briefing paper has been written following the pre-accounts planning conference held in February 2021 and the audit conference in March 2021. It may be updated as the issues develop over the year-end period.

Submission deadlines

All NHS bodies are required to prepare their annual report and accounts in accordance with the *Group accounting manual 2020/21*² (GAM) issued by the Department of Health and Social Care (DHSC). The only exception is that foundation trusts prepare their annual report in accordance with the *Foundation trust annual reporting manual 2020/21*³ (FT ARM) published by NHS England and NHS Improvement rather than chapter 3 of the GAM.

¹ HFMA, *2020/21 annual report and accounts checklist*, March 2021

² DHSC, *Group accounting manual 2020/21*, updated January 2021

³ NHS England and NHS Improvement, *Foundation trust annual reporting manual*, February 2021



The key dates in the timetable for 2020/21 are:

Final date for providers to apply for the extended submission deadline ⁴	19 March 2021
Agreement of balances data submission ⁵	27 April 2021
Submission of draft annual report and accounts (except for providers working to the extended deadline)	27 April 2021
Submission of the draft annual report and accounts for providers working to the extended deadline	3 – 11 May 2021
Agreement of balances resubmission	11 May 2021
Audited accounts submission (except for providers working to the extended deadline)	15 June 2021
Audited accounts submission for providers working to the extended deadline	29 June 2021

When deciding whether to apply for the extension, NHS providers need to discuss with their auditor whether they are able to undertake their work to gain sufficient assurance over the accounts to meet the earlier deadline. If auditors have flagged the potential need for the extra two weeks, that should be discussed with them as they may not have the resource to meet the earlier deadline even if the finance team is able to.

All NHS providers and commissioners are responsible for submitting their summarisation schedules to the consolidating bodies. Auditors are responsible for submitting summarisation schedules to the NAO. It is vital that the same version is submitted to the consolidating body and the NAO – each year differences are found which take time and resource to resolve.

To consider:

Are arrangements in place to ensure draft annual report and accounts submitted for audit are as accurate as possible?

Has a plan been agreed for audit to meet the submission timetable?

Are quality review arrangements in place to ensure that the summarisation schedules submitted by NHS bodies and auditors are consistent?

2020/21 annual report and accounts

The impact of Covid-19

On the NHS body

While the 2019/20 annual report and accounts preparation was impacted by the pandemic and, in particular, the first lockdown, it is the 2020/21 annual report and accounts that will reflect the impact of Covid-19.⁶ Aside from the specific accounting issues below, differences between the current and prior year comparatives may need to be explained, estimates and judgements will need to be revised and reconsidered in the light of the fact that the year has been anything but normal.

Materiality assessments will need to be reviewed and it may be that some items are not material in numerical terms but are material in the context of the pandemic, for example, the impact of the pandemic on private patient income is unlikely to be material but it may need to be discussed in the context of the financial position of the NHS body.

⁴ NHS England and NHS Improvement, *NHS accounts timetable and year-end arrangements - with provider annex*, 15 January 2021

⁵ DHSC, *Annual report and accounts timetable: 2020/21*, December 2020

⁶ Caroline Clarke (HFMA President), *Painting by numbers*, February 2021

Other items may not be material but are part of the story of the year. For example, the generosity of the public in the first lock down should be reflected in the narrative of the annual report even though the value of the gifts will be recognised in the NHS charity annual report and accounts.

On the NHS financial regime

The financial regime in 2020/21 was completely revised as a result of Covid-19. This has resulted in a number of accounting issues that will impact on the annual report and accounts. Guidance has been issued by the DHSC and NHS England and NHS Improvement in relation to:

- reduced reporting requirements meaning that the performance analysis can be omitted from the annual report, as well as allowing reference to the NHS Digital website in relation to sickness absence data and the staff turnover disclosure
 - IFRS 16 implementation has been deferred to 2022/23 (see below)
 - the impact of Covid-19 on the PDC dividend calculation. It is likely that the amount of PDC dividend payable will be different in 2020/21 to previous years. Where assets have either been centrally or locally procured specifically as a result of Covid-19 these are excluded from the PDC dividend calculation. The changes to the financial regime mean that the cash balances held by NHS provider bodies will be different to those in previous years
 - accounting for centrally procured personal protective equipment (PPE) – this inventory will be treated as grant income with the PPE that has been used shown as expenditure. Where there is a balance of unused PPE at 31 March, there will be a mismatch between income and expenditure. Guidance has also been issued to those bodies where stock balances are immaterial, so consumables are expensed when purchased. The donation of centrally procured PPE and those transferred between trusts should be excluded from the agreement of balances process
 - accounting for centrally procured equipment. Where NHS providers are using equipment from the national loan stock of ventilators and other equipment, it will be effectively donated to them from the DHSC. It will therefore have to be reflected in the non-current assets of the NHS body as at 31 March. There will be a process in 2021/22 to confirm whether NHS bodies wish to keep the equipment or return it
 - accounting for Nightingale facilities where NHS bodies have been hosts for these facilities
 - year-end inventory balances. NHS bodies will need to consider how they will undertake stock takes at the year-end. It is possible that some audit opinions will include a limitation in scope in relation to material inventory balances again in 2020/21 where auditors cannot attend or undertake alternative procedures in relation to stock counts. In 2019/20, 29 providers' audit opinions were qualified in this way and it is expected that limitation will also be reflected in those opinions in 2020/21.
 - Covid-19 vaccines and testing kits should not be considered as own items of inventory
- NHS England and NHS Improvement guidance on accounting for 2020/21 items⁷ will be updated on an ongoing basis during March, and possibly April.

To consider:

While the annual report does not need to include a detailed performance analysis, does the annual report and account reflect the impact that the pandemic has had on the body and all of the changes that have been made as result?

Have material changes between current and prior period been considered?

How has the year-end specific guidance been dealt with in the accounts and what impact has it had?

Do the accounting policies reflect the changes to the NHS financial regime?

What arrangements have been put in place to ensure guidance is identified and actioned as issued?

What arrangements have been put in place to undertake stock takes at the year end?

⁷ NHS England and NHS Improvement, *Guidance on accounting for 2020/21 items*, March 2021

What discussions have been held with auditors about year-end stock takes?

Is stock/ inventory likely to be material as at 31 March?

For host bodies, what disclosures will be made in relation to Nightingale facilities?

Change to the capital and cash process

Reforms to the NHS capital and cash regime were announced in April 2020⁸. Some NHS bodies will have been given additional public dividend capital (PDC) to repay loans from the DHSC. Where that is the case, a narrative disclosure should be included in the annual report as well as the accounts to reflect the impact of these changes on the financial standing of the organisation.

To consider:

Does the annual report and accounts reflect the impact of the changes to the capital and cash regime announced in April 2020?

Provisions

NHS bodies should particularly consider whether provisions are required in relation to:

- Untaken annual leave – IAS 19 requires that untaken holiday at the year-end is provided for. Usually, there is a limit on the amount of holiday that staff can carry forward. However, due to the pandemic arrangements for carrying forward leave have been relaxed as staff will not have had the opportunity to take all of their annual leave. This provision should be revisited in the light of Covid-19. NHS England and NHS Improvement will be providing some funding to cover the cost of the annual leave provision – this should be shown as additional income in the year and may need to be separately disclosed if material. It is expected that additional guidance will be provided in relation to this provision.
- Clinical pensions - clinicians who were members of the NHS Pension Scheme and who faced an annual allowance tax charge for work undertaken in 2019/20 could elect to have this charge paid by the NHS Pension Scheme⁹. If this is the case, the employing trust will have a liability to make a payment to that clinician when they retire. Under IAS 37, a provision will have to be established. NHS England and NHS Improvement will issue guidance on how the provision should be calculated.
- There are a number of employment tribunals in relation to whether, and which type of, overtime should be included when calculating holiday pay¹⁰. Some NHS bodies may need to establish provisions for these claims. As there has been no change in the legal position during 2020/21, NHS bodies will only need to amend their provision if new information has come to light within the organisation. The appeal to the Supreme Court¹¹ of the Flowers case in relation to holiday pay and overtime is unlikely to have been heard by March 2021 but the case should be kept under review in case it has been heard by the time the accounts are signed off in June 2021.
- From 4 November 2020, Regulations imposed a £95,000 cap on exit packages. However, on 12 February, the government revoked the cap using a Direction until the regulations can be revoked¹². Where staff had a capped exit payment between November 2020 and February 2021, their exit payments will need to be revisited and other redundancy provisions need to be reviewed in the light of the removal of the cap.
- Final pay control payments in relation to increases in salary in the three years before a staff member retires¹³.

⁸ NHS England and NHS Improvement, *Guidance on the cash and capital regime for 2020/21*, April 2020

⁹ NHS England and NHS Improvement, *Pensions tax annual allowance*, updated 11 March 2020

¹⁰ HFMA, *Holiday pay and overtime – accounting and governance issues*, February 2020

¹¹ Supreme Court, *Permission to appeal*, March 2020

¹² HM Treasury, *Guidance on public sector exit payments*, 12 February 2021

¹³ HFMA, *Final pay controls – accounting and governance issues*, November 2019

To consider:

Has the impact of the pandemic as well as other developments in 2020/21 been considered when determining the level of provisions required?

Has any funding received to offset the cost of holiday pay been accounted for?

Valuation of non-current assets

NHS bodies generally have a full valuation every five years with interim (desk based) valuations in between. However, the accounting standard requirement is that NHS bodies should satisfy themselves that their non-current asset valuations are not materially misstated. NHS bodies and their valuers need to determine how the accounting requirement will be satisfied and what this means in terms of site visits. Clearly, site visits will be subject to additional health and safety requirements at the moment and may simply not be possible.

Where specialised assets are valued on a modern equivalent asset (MEA) basis, consideration should be given to whether the assumptions still hold in the Covid-19 world. For example, does the MEA take into account the need for social distancing and, potentially, additional ICU capacity? The HFMA has issued a briefing on valuation and accounting issues¹⁴.

In 2019/20, the Royal Institute of Chartered Surveyors (RICS) provided guidance to its members on statements of material uncertainty¹⁵ as a result of Covid-19 that meant that most valuations included that statement. Since then, RICS have indicated that statements of material uncertainty are not generally required¹⁶ and it is for the valuer to determine whether to include one.

To consider:

If a new valuation has been obtained, how has the NHS body satisfied itself that updated valuation guidance is being followed?

If a new valuation is not needed, how has the NHS body satisfied itself that non-current asset valuations are not materially misstated?

Financial position and going concern

The Covid-19 financial regime for NHS bodies means that the financial difficulties seen in previous years may not be as much of an issue in 2020/21. However, it is unlikely that contracts for 2021/22 will be signed before the 2020/21 accounts are signed and that uncertainty may impact on the going concern assessment for NHS bodies. When considering going concern both management and auditors need to look ahead 12 months from the date of signing the accounts which will cover a period for which no contracts are in place. Therefore, other evidence that services will be provided will need to be considered.

Due to the HM Treasury reporting requirements, NHS bodies are highly unlikely to prepare their accounts on any basis other than going concern. However, material uncertainties around the financial position must be disclosed in the financial statements¹⁷. It is management's responsibility to consider going concern and, in particular, any significant uncertainties.

IAS 1 Presentation of financial statements requires the disclosure of those judgments which have the most significant effect on the amounts included in the accounts and the sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the accounts in the next financial year. The disclosure should therefore focus on material and significant judgments and estimates and should provide enough detail for the reader of the accounts to understand why they are critical and what impact they could have on the financial position of the reporting body.

¹⁴ HFMA, *Property, plant and equipment: accounting and valuation issues*, December 2019

¹⁵ RICS, *Material uncertainty in valuation*, October 2019

¹⁶ RICS, *RICS Material Valuation Uncertainty Leaders Forum UK*, updated January 2021

¹⁷ HFMA, *Going concern - Assessment and reporting requirements in difficult times*, October 2019

Auditors will want to test the underlying data and discuss any differences between their assessment and management's. They may use different assumptions or data when looking at management's judgements. The impact of the Comptroller and Auditor General's (C&AG) report on the DHSC's annual report and accounts 2019/20 may also mean that auditors are more concerned about management override of controls and the impact of judgements and estimates on financial performance¹⁸ and ¹⁹.

To consider:

Has clear documentation of judgements and estimates made by management, including an assessment of going concern been presented to the audit committee during the year and have these been understood and robustly challenged?

Has management prepared a report considering any significant uncertainties relating to its going concern status?

What is the process for approving manual journals?

Have management made manual adjustments to the financial position reported in the underlying records?

Does the underlying cash flow support the reported financial position?

Fraud/ losses and special payments

The DHSC has a material risk in relation to fraud. The NAO is therefore asking auditors to consider the completeness of losses and special payments disclosures by NHS bodies. In particular, auditors will consider whether the disclosure of losses and special payments has been reconciled to the local counter fraud report. The two will not be the same as there are timing differences in the issues reported but these will form the reconciling items.

To consider:

How has the completeness of losses and special payment disclosures been considered?

Has the losses and special payments disclosure note been reconciled to the local counter fraud report and any other relevant information?

Brexit

The UK left the EU on 31 January 2020 and the transitional period ended on 31 December 2020. While no specific disclosures are required in relation to Brexit, any uncertainties that NHS bodies face as a result should be disclosed in the same way as any other operational risks.

To consider:

Has the impact of Brexit on uncertainties been considered and, if appropriate, disclosed in the accounts?

Usual year-end considerations

There are a number of areas that NHS bodies need to consider every year, or that have been known about for some time:

Discount rates for 2020/21 and probability of non-recovery of injury cost revenue

These rates are published annually by the DHSC in the year-end additional guidance²⁰. Finance teams should have assessed the impact on NHS bodies' financial position.

¹⁸ HFMA, *How to review and scrutinise the numbers during the year*, October 2017

¹⁹ HFMA, *The importance of strong financial governance*, June 2017

²⁰ DHSC, *Group accounting manual additional guidance*, January 2021

Employer contributions to the NHS pension scheme

Since 2019/20, NHS employers have been paying an employer contribution of 14.38% to the NHS pension scheme but the employers' pension contribution is 20.68%. The difference of 6.3% has been funded and paid to the NHS BSA centrally by NHS England and NHS Improvement. This arrangement has been agreed until 2021/22.

In NHS bodies' accounts, the full contribution must be recognised by all NHS employers²¹. The fact that it is being paid by NHS England and NHS improvement will be reflected in nominal income so the effect on the bottom line is neutral. The amount that should be reflected as income and expenditure will be calculated by NHS England and NHS Improvement and NHS bodies are expected to use the figures provided by the regulatory bodies. However, they need to put in place arrangements to review these amounts for reasonableness, particularly where changes of circumstances mean that the extrapolation of the full year impact based on month 9 or 10 will not be materially correct.

Standards issued not yet adopted

The adoption of IFRS 16 has been deferred to 2022/23 – reflecting the fact that finance teams have not been able to focus on the new standard as a result of the pandemic. The HFMA has prepared a detailed briefing on its practical implementation²² as well as a briefing aimed at non-finance staff²³ and these will be updated soon. There have been changes to the way that the standard will be adopted in the NHS in relation to irrecoverable VAT and PFI schemes.

In terms of the 2020/21 accounts, IAS 8 requires disclosures in relation to standards that have been issued but have not yet been adopted. This disclosure will cover IFRS 16 *Leases* and IFRS 17 *Insurance contracts*.

In the case of IFRS 16, the disclosure made in 2019/20 should be updated to reflect any work done during the year on leases as well as to update the information published. There will be more to disclose about the impact of the new accounting standard than usual because of the work that has already been done to assess its impact.

Provisions vs accruals

For NHS bodies, the decision whether a liability is a provision, or an accrual does not make any difference to the bottom line and is largely presentational. However, for NHS England and the DHSC, the difference between a provision and an accrual makes a difference to their position against their financial targets. The financial position of the DHSC group means that auditors take an interest in the classification of accruals and provisions.

Partially completed patient spells

From 1 April 2020, the financial regime changed, and contracts were on a block basis or similar. Therefore, provisions for income for patients who are part way through their treatment at 31 March 2021 are not required.

Specific guidance has also been issued in relation to the treatment of patients on the maternity pathway.

Agreement of balances

In 2019/20, the thresholds for agreement of balances were increased to help ease the burden of preparing the annual report and accounts in lockdown. Those thresholds have been retained in 2020/21 and there have been no major changes to the guidance. Generally, the results of the agreement of balances exercise have been improving in recent years but the mismatch increased in

²¹ NHS England and NHS Improvement, *Accounting for additional employer pension contributions 2020/21*, January 2021

²² HFMA, *IFRS 16 leases: practical application*, February 2020

²³ HFMA, *Accounting for leases: why it affects you*, November 2019

month 9 of 2020/21 raising concerns about the consolidation. Agreement of balances, remains a material risk for the DHSC so it is vital that the guidance is re-read and followed each year.

To consider:

Has the cost impact of the published discount rate for provisions been assessed and managed?

Have the income and expenditure figures provided nationally relating the contributions to the NHS pension scheme been reviewed to ensure they are materially correct?

How have finance teams ensured they have a good understanding of the impact of IFRS16? For example, are they up to date with the latest guidance issued on the dedicated webpage?

Are disclosures on standards issued but not adopted in line with IAS 8 requirements?

Has there been a robust assessment of contracts that might contain a lease under the current accounting standards?

Are arrangements in place to review leases in line with IFRS 16?

Are arrangements in place to ensure accurate and timely IFRS 16 returns to NHS England and NHS Improvement?

Are processes in place to ensure that provisions and accruals are appropriately classified?

Are there clear processes in place for the agreement of balances exercise?

Are there any significant non-agreed balances and if so why?

Annual governance statement

NHS bodies are reminded that they need to include a conclusion which lists significant internal control issues or states that there are none. Control issues are not the same as listing the risks that the NHS body is facing.

To consider:

Does the annual governance statement include significant internal control issues and are these in line with discussions had throughout the year?

Letter of representation

Also, ISA (UK) 580 requires auditors to request written representations from management with appropriate responsibilities and knowledge of the matters concerned before their report is issued. Non-executive directors and lay members should ensure that this is appropriately considered.

To consider:

Has a letter of representation been prepared setting out managements' responsibilities and key judgements?

Changes to the audit regime

Changes arising from the new *Code of audit practice*

VFM arrangements

On 1 April 2020, a new *Code of audit practice* (the Code)²⁴ came into force and applies to audits of the 2020/21 financial statements onwards. The new Code includes a significant change in the way auditors are expected to approach and report their work on value for money (VFM) arrangements. A VFM commentary replaces the binary VFM conclusion. It covers financial sustainability, governance and improving economy, efficiency and effectiveness. There is also the requirement to make a recommendation where significant weaknesses are identified.

²⁴ NAO, *Code of audit practice*, April 2020

The commentary provides auditors with the opportunity to include context on arrangements such as governance over decision-making at pace and managing the financial impact of the pandemic. *Auditor guidance note 3* provides further detail on auditors' work on VFM arrangements.²⁵

Auditors annual report

The new Code places a requirement on all auditors to issue an auditor's annual report (AAR). This replaces the annual audit letter. The AAR is a public document and must be made available to members of the public free of charge – usually this means that it is published on the body's website. The AAR includes a summary of the work on the accounts opinion; commentary on VFM arrangements work; recommendations and follow up; and details of any other powers exercised such as the issuing of a public interest report.

To consider:

Are timely arrangements in place to review the VFM commentary and to consider the actions required in response to any recommendations made?

Are arrangements in place to make the auditor's annual report available to the public?

New auditing standard on estimates and judgements

ISA 540 (revised) *Auditing accounting estimates and related disclosures*²⁶ is effective for audits of financial statements beginning on or after 15 December 2019. The revision reflects an increasing focus from regulators and other stakeholders on estimates, especially those which are complex and require significant judgements. It aims to foster a more independent, challenging and skeptical mindset in auditors.

As a result, auditors will place an increasing emphasis on understanding and assessing internal controls over accounting estimates. As set out in the section on the financial positions above, auditors will want to test the underlying data and discuss any differences between their assessment and that of management. Common areas of focus are likely to be: property, plant and equipment; accruals; provisions; value of stock; and defined benefit pension liabilities.

To consider:

Are there clear internal controls over accounting estimates? Where necessary, are individuals with specialist skills used to advise on complex accounting estimates?

Are you clear about how management identified the methods, assumptions and source data used for each material accounting estimate? If changes were made do you understand why?

HFMA's briefing, *The external audit: best practice in working well together*²⁷ may be useful when planning the year-end process.

²⁵ NAO, *Auditor guidance note 3*, October 2020

²⁶ IAASB, *ISA 540 (revised), auditing accounting estimates and related disclosures*, October 2018

²⁷ HFMA, *The external audit: best practice in working well together*, February 2020

About the HFMA

The Healthcare Financial Management Association (HFMA) is the professional body for finance staff in healthcare. For over 70 years, it has provided independent and objective advice to its members and the wider healthcare community. It is a charitable organisation that promotes best practice and innovation in financial management and governance across the UK health economy through its local and national networks.

The association also analyses and responds to national policy and aims to exert influence in shaping the wider healthcare agenda. It has particular interest in promoting the highest professional standards in financial management and governance and is keen to work with other organisations to promote approaches that really are 'fit for purpose' and effective.

The HFMA offers a range of qualifications in healthcare business and finance at undergraduate and postgraduate level and can provide a route to an MBA in healthcare finance. The qualifications are delivered through HFMA's Academy which was launched in 2017 and has already established strong learner and alumni networks.

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