



NAO Code of audit practice issues paper

Consultation response

Who we are

The Healthcare Financial Management Association (HFMA) is the representative body for finance staff in healthcare. For the past 60 years, it has provided independent and objective advice to its members and the wider healthcare community. We are a charitable organisation that promotes best practice and innovation in financial management and governance across the UK health economy through our local and national networks. We also analyse and respond to national policy and aim to exert influence in shaping the wider healthcare agenda. We have a particular interest in promoting the highest professional standards in financial management and governance and are keen to work with other organisations to promote approaches that really are ‘fit for purpose’ and effective.

Our comments

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Section One: Status of the Code, application and general principles

Q1 – Do you think a principles-based approach is appropriate for the Code of Audit Practice or should the approach be more prescriptive?

Yes, a principles-based approach remains appropriate for the Code. This allows the Code to be more easily applied across sectors and flexible to changes within each sector. This is particularly relevant in the current climate, as the NHS changes to deliver the *NHS long-term plan* and responses to the consultation on legislative change are considered.

For the financial statements, prescriptive requirements are set out in the International Financial Reporting Standards (IFRSs) and the International Standards on Auditing (ISAs), so a principles-based approach is sufficient.

Q2 – Are there any principles you think should be added or removed?

No, the current principles provide a good coverage.

Q3 – Do you think it would be beneficial to give more emphasis to some principles over others?

No, all principles are equally relevant and important.

Q4 – Do you think a single Code should be retained, or would sector-specific Codes be better?

Yes, a single Code should be retained. It supports consistency across the sectors which benefits auditors, audited bodies and the public. In many cases, auditors may undertake audits across a number of sectors and a single Code will help avoid confusion. A single Code also supports the increase in partnership working, including aligning reporting, across audited bodies.

The current approach to highlight requirement differences in the Code or detailed guidance to auditors should continue.

Q5 – How could the Code better support auditors' work on audited bodies' partnerships and joint arrangements?

The current Code does include a section on co-ordination and integration and recognises that local public bodies increasingly operate, commission and deliver services in a range of partnerships and other forms of joint working or contracts with other public, private or third sector bodies. The Code already sets out an integrated approach to the audit. Although the paragraphs included in the Code are not detailed, auditing standards can be used in these situations and the Code could point to them. For example, where working with third parties, pooled budget arrangements and group audits.

The Code could be strengthened further by clarifying the expected approach to:

- addressing information governance issues
- supporting auditors to work together to consider the impact of partnership working across a sustainability and transformation partnership (STP) or integrated care system (ICS) on:
 - management arrangements and the impact on decision-making
 - value for money
 - the impact of system wide targets/ initiatives on the corporate entity
 - the possibility of irregular expenditure for CCGs with money being spent on the population outside of their patch
- encouraging triangulation of information across partnerships, albeit recognising potential risks around data and confidentiality.

It would also be helpful to recognise that governance arrangements of partnerships are evolving, particularly with ICSs/STPs not being statutory bodies. When reviewing these new arrangements, it would be helpful to reinforce the principle that auditors should be working together to develop a better shared understanding of risks.

Also, additional supporting guidance for auditors would be welcomed on considering the impact of partnerships and joint arrangements. For example:

- how to assess value for money where the benefits will accrue to another organisation, such as money spent in the NHS that reduces costs in the police service
- what it will mean for auditors if an individual organisation reports weaker financial performance for the good of the wider system. How would the auditor assess the value for money from both a system and organisational perspective?

Section Two: Audit of the financial statements

Q6 – Do you agree the Code should continue to align its requirements with generally accepted auditing standards?

Yes, to support consistency and ensure the Code remains credible.

Q7 – Are there areas of the financial statements where it is currently difficult or inappropriate to apply generally accepted auditing standards?

The areas which are generally more difficult to apply generally accepted auditing standards are those which require an element of estimation or judgement, or those based on partnerships/ third party sources. The International Standards on Auditing (ISAs) set out clear requirements on auditors in these areas.

For NHS entities, the expenditure recognition risk is bigger than the revenue recognition risk. For example, CCG prescribing can be a significant area of audit risk as it involves estimation with large values, fluctuations and uncertainty. Going concern assessment is also a more difficult area to audit. It would be helpful to set the scene clearly on how this applies in the NHS and provide clarification further guidance for auditors in this area. Practice Note 10: Audit of financial statements of public sector bodies in the United Kingdom, does cover these they are areas where it is more complicated to apply the auditing standards.

Section Three: The auditor’s work on economy, efficiency and effectiveness of corporate arrangements (value-for-money arrangements)

Q8 – What are the key issues that you think the Code and National Audit Office guidance for this area of work will be need to be able to address in the coming years?

The key issues to consider for this area of work in the coming years are:

- financial sustainability and resilience
- cost improvement programmes
- managing resources across a system working (STPs and ICSs)
- new digital technologies
- shared reporting across organisations
- system wide decision-making and oversight arrangements
- financial value-based planning including longer term forecasting
- prevention and long-term planning.

Reflecting on the feedback from local bodies in paragraph 32 of the consultation, that ‘local bodies’ feel the output from auditors’ work in this area often does not add to their knowledge or understanding of the risks and issues they are facing, and that they would find more commentary around both current and emerging issues more helpful’, it would be helpful for the audit to cover plans to change arrangements to achieve value for money as well as current arrangements. For example, if an NHS body is planning to set up a subsidiary to save money, under current arrangements this would not be a current value for money issue and may not be considered by the auditor until plans are well advanced. It is management’s responsibility to assure themselves that appropriate arrangements are in place to secure value for money. While recognising this is a management function, it might be helpful for auditors to look at the arrangements in place to develop plans at the early planning stage. However, we recognise that there may be cost implications due to the additional audit work required.

Q9 – Are you content that the current terminology ‘VFM arrangements conclusion’ adequately describes the nature of the work undertaken and the conclusion?

The current terminology does describe the nature of the work, recognising its scope can be wide and also allows for work to be tailored to individual risks. Retaining the existing wording has the advantage of being familiar to auditors, local bodies and the public and will avoid any potential confusion if the terminology changes, but the substance of the work does not. However, while the wording may be familiar, we have concerns that the VFM arrangements conclusion is not well understood outside of the audit community. Consequently we issued a [briefing](#) explaining the different audit reports, including the conclusion on the arrangements to secure value for money.

If different terminology is used, it should continue to reflect the focus on financial and governance arrangements.

It would also be helpful to clarify the link with the NHS Improvement Use of Resources (UoR) assessment. The two assessments are different and auditors should look at the UoR assessment to help identify new risks. Guidance would be helpful to identify where the scope is different, understand why there are differences and ensure consistency where appropriate.

Q10 – Do you think the current, risk-based, approach to arrangements work focuses the auditor’s attention in the right areas?

The current approach does rely on local auditor judgement and can in some cases lead to a light touch approach. However, it does allow the auditor to specifically tailor work to the local audited body risks if needed.

Q11 – Do you think the Code should allow auditors to look in more detail at work in areas that may not meet the current definition of a ‘significant’ risk but nevertheless represent a concern to local auditors and local public bodies?

The current focus on ‘significant’ risks ensures across consistency and a proportionate approach. If the Code does allow further work on non-significant risks, thought would need to be given to how the risks are identified and who determines areas of additional work. If the concerns identified are not ‘significant’, it may not justify the additional costs to local audited bodies. It is likely that such risks are better addressed by other work by management or internal audit and if the Code allows auditors to look in more detail at non-significant risks, there is the risk of duplication.

Other audit areas that could be considered in more detail are future risks, recognising that although risks may not be considered significant now, they could have a huge impact later.

Section Four: Reporting the results of the auditor's work

Q12 – Do you think the information that is currently reported publicly by auditors helps local taxpayers understand the key issues and hold local bodies to account?

Yes, although in our opinion it could be clearer and more easily accessible.

Q13 – How could local reporting add more value to the audit for local public bodies and taxpayers?

Local auditor reporting could add more value by:

- consistency of reporting across the NHS. This could be by requiring auditors of all NHS bodies, not just foundation trusts, to produce the long form audit report rather than the annual audit letter or including a one page summary up front in audit reports of the key messages with consistent requirements across audit providers
- consistent reporting on the follow up to previous recommendations
- commentary on progress from period end to the date of the audit.

Q14 – In the section on the auditor's work on economy, efficiency and effectiveness we explained that the auditor reports their overall conclusion against the criterion of whether they are satisfied that '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'. Do you think a single, overall criterion for reporting the adequacy of arrangements enables auditors to effectively communicate relevant issues, or would a number of more specific criteria be more effective?

A single criterion does enable auditors to effectively communicate relevant issues, with the advantage of it being easy to understand and flexible enough to be tailored to specific issues. The advantage of splitting it down would be to improve consistency and transparency of reporting, including recognition of where there are no issues in an area, as well as only reporting by exception.

Q15 – Do you think the options of 'adverse' and 'except for' conclusions to report weaknesses enables auditors to effectively communicate relevant issues?

Yes, although perhaps the terminology could be clearer to reflect whether the nature of weaknesses is overarching or only in a specific area.

Q16 – How could the results of audit work on economy, efficiency and effectiveness be reported more effectively and clearly?

As reported in the NAO report on local auditor reporting in England, a significant proportion of local bodies may not fully understand the main purpose of the auditor's conclusion on arrangements to secure value for money. Further the importance of addressing those issues may be misunderstood. The Code could provide guidance on how this could be addressed. In response to the NAO report, the HFMA briefing, *External audit reports: the role of the audit committee* explains the difference audit reports and the importance of acting on them.

In our opinion, timely reporting with key messages summarised at the start of the report are most effective. Also, clarity over what has, and has not, been included in the scope of the work would be helpful.

For the public in particular, it would also be helpful if the sector context and regulatory requirements are clarified. For example, NHS control totals can lead to confusion, particularly where a surplus is achieved but the VFM conclusion is qualified because the control total has not been met. We recognise that this may be too detailed to be contained in the Code, but could be supplementary guidance.

Section Five: The auditor's additional powers and duties

Q17 – Do you think the Code should include more with respect to when auditors might be expected to use their additional powers?

Additional guidance, outside of the Code, on when auditors might be expected to use their additional powers would be helpful.

Section Six: Smaller authority assurance engagements

Q18 – Do you think the current approach set out in the Code to undertake work at smaller authorities under specified procedures will enable auditors to continue to respond to the challenges at smaller authorities?

We have no view as this is not applicable to NHS bodies.

Q19 – Do you think the current approach to considering economy, efficiency and effectiveness at smaller authorities is appropriate and proportionate to the size of the bodies being reviewed?

We have no view as this is not applicable to NHS bodies.

Section Seven: Potential implications of changes to the Code

Q20 – Do you think local auditors have the appropriate capacity and capability to meet their responsibilities and to respond to the issues set out in this consultation?

Yes, local auditors work to specific professional standards requiring them to have appropriate capacity and capability to meet their responsibilities. However, there are particular areas of the auditor's role which are becoming increasingly challenging, particularly with the increase in use of technology, partnership working and long-term planning.

In addition, since the *Local Government Accounts and Audit Regulations 2015* brought forward the deadline for the audit of local authority accounts from 30 September to 31 July from 2017/18, there is increasing pressure on auditors during April to July. One option to help address this capacity issue would be to consider providing the VFM conclusion at a different time of the year. Management arrangements change throughout the year so is it necessary for the VFM conclusion to relate the financial year? We recognise that this would be complicated when auditors change, but it would smooth the audit work across the year and may result in more detailed work being done.

Contact

We hope you find these comments useful. If you would like to discuss any of our comments in more detail please contact Lisa Robertson, policy and research manager, lisa.robertson@hfma.org.uk.