Northumberland, Tyne and Wear NHS Foundation Trust

Board of Directors Meeting

Meeting Date: 25 May 2016

Title and Author of Paper:
Annual Accounts 2015/16 and the Management Representation Letter
Tracey Sopp, Head of Transactional Services

Executive Lead: James Duncan

Paper for Debate, Decision or Information: Decision

Key Points to Note:
The draft annual accounts 2015/16 were reviewed by the Audit Committee on 18th May 2016, along with the External Auditor's Completion Report 2015/16.

There will be a verbal update on the outcome of the Audit Committee and also the Management Representation Letter will be handed out at the Board meeting. Please note that the Letter cannot be completed until after the Audit Committee meeting.

Appendices are as follows:

1 Director of Finance's presentation
2 Draft Annual Accounts

Risks Highlighted to Board :
There are no risks to highlight to the Board.

Does this affect any Board Assurance Framework/Corporate Risks?
No

Equal Opportunities, Legal and Other Implications: N/A

Outcome Required: The Board of Directors is asked to:
Approve the Annual Accounts
Sign off the Management Representation Letter

Link to Policies and Strategies: N/A

BOARD OF DIRECTORS MEETING

25 MAY 2016

PRESENTATION OF DRAFT ACCOUNTS 1 APRIL 2015 – 31 MARCH 2016

Introduction

The amended draft accounts for the period are attached in appendix 1. The draft accounts include all amendments which have arisen during the course of the audit and in line with the Auditors Completion Report.

Statement of Comprehensive Income (Income and Expenditure) SOCI

A surplus of £11.7m has been reported for the financial year. A surplus was generated of £4.2m prior to exceptional items (net impairments of £7.6m made up of reversals of impairments of £10.9m and impairment charges of £3.3m) and a net loss on disposal of assets of £0.1m.

Other comprehensive income relates to the gains and losses charged to reserves. Revaluations relate to increases in valuations of £0.9m. This relates mainly to the valuation undertaken as at 31 March 2016 and relates to increases in buildings values above the amounts charged as reversals of impairments.

Impairments of (£0.1m) relate charges to the revaluation reserve for changes in the market price for land and buildings in accordance with the valuations provided by the District Valuer as at 31 March 2016.

Total other comprehensive expense is a net £0.8m.

Income (Notes 2 and 3)

- Overall income for the period is £317.0m (£314.9m 2014/15).
- Income from activities has increased by £6m and 2%. There is a reduction in cost and volume contract income mainly due to neuro wards 1 and 2 moving onto block contract income (£4m). Block contract income has increased due to this and other new investments including Gateshead Acquired Brain Injury Service £1.3m, Offender Health £1m and Out of area Treatments £2.5m.
- Other operating income has decreased by £3.9m. This relates to a profit on disposal in 2014/15 of £1.5m and a reduction in reversal of impairments of £2.5m.
- Operating lease income has increased due to a 7 year lease at Walkergate to IBM.

Operating expenses (Note 4)

- Overall operating expenses for the period is £299.4m (£340.1m 2014/15).
- The most significant variance which is explains the £54.0m decrease from 2014/15 is the decrease in exceptional items of impairment charges of £3.4m in 2015/16 (£51.8m 2014/15) which gives a variance of £48.4m. Impairment charges were high in 2014/15 due to a significant impairment for Hopewood Park land and buildings.
- The increase in Purchase of Healthcare from Non NHS bodies relates to an

increase in costs to provide out of area treatment in line with the income note above of £1.1m.
- The movement in legal fees relates to the reversal of the provision for equal pay in 2014/15 of £1.3m.
- There is an increase in consultancy due to using Meridian, the Deloittes Governance review and an increase in consultancy for NEQOS which we host
- Redundancy costs have increased due to the Transforming Corporate Services Programme and this links to note 6.1 and 7.3 in relation to exit packages
- The movement in other relates to a large increase in injury benefit claims in 2014/15 due to two new cases and an increase in the discount rate.

Senior Management Remuneration

- Senior management remuneration has increased due to an increase in pay and numbers of non-execs and there was only a part-year cost for the Chief Executive in 2014/15 as John commenced employment in June 2014. £57k increase due to non-execs and £54k saving in 2014/15 for part-year effect.

Finance Costs

- Finance income generated has increased due to more significant cash balances held and a slight increase in the rates available from the National Loans Fund.
- Finance expense has increased slightly due to additional interest costs for drawing down a further £10.4m of loans and due to a fluctuation in the PFI universal model interest payments.
- PDC dividends payable have reduced significantly due to the full year effect of the Modern Equivalent Asset valuation carried out in 2013/14 and due to high average daily cash balances held in government banking service accounts which reduce the dividend payable.

Share of Profit of Associates/Joint Ventures

- Deficit of (£8k) has been recognised for the 50% share of the profit in Newcastle Talking Therapies LLP joint venture of £37k (2014/15 £49k) and the recognition of a liability to South Tees Foundation Trust for the joint operation for the provision of NEQOS.

Statement of Financial Position SOFP (Balance Sheet)

Non Current Assets

Intangible Assets (Note 14)

- Intangible assets have increased in relation to the purchase of software licenses and the purchase of software in relation to the Electronic Prescribing and Medicines Admin scheme £154k.

Property, Plant and Equipment (Note 15)

- There is an increase in property, plant and equipment values of £17.2m. This relates to £15.6m increase from capital expenditure, (£0.8m) net reduction for disposals and assets transferred to held for sale, £8.4m of overall net revaluation gains and a reduction of (£6.0m) for depreciation charges. Investments in Associates (Note 16)

Investment in Associates and Joint Ventures (Note 16)

- 50% share of the 2015/16 surplus from the LLP of £37k has been included in the accounts and £49k in cash was received as 50% share of profit from the final audited 2014/15 LLP accounts.

Trade and Other Receivables (Note 21)

- There is an increase in prepayments over 1 year.

<u>Current Assets</u>

Net Current Assets and Net Current Liabilities (Notes 20, 21, 17, 22, 23, 24, 28 and 26)

- Working capital held (net current assets less net current liabilities) has decreased by (£1.4m), from £10.0m in 2014/15 to £8.6m in 2015/16. The significant movements in current assets and liabilities are:
- Decrease in Trade and Other Receivables of £7.3m. This mainly relates to
- £6.9m being paid for the second instalment of the Northgate Land sale in January 2016.
- Decrease in assets held for sale (note 17) of £1.6m from £1.6m to £0.0m. There are no assets held for sale at 31st March and the Social and residential homes held at 31 March 2015 were sold in year.
- Increase in cash and cash equivalents (note 22) of £6.8m from £20.6m as at 31 March 2015 to £27.4m as at 31 March 2016. Planned cash as at 31 March 2016 was £21.8m meaning cash was £5.6m above plan, mainly due to the surplus prior to exceptional items being £2.2m above plan and slippage on the capital programme.
- Current liabilities have decreased by (£0.7m). There are no significant movements on current liabilities.

Non-Current Liabilities Borrowings

(Note 24)

- Borrowings has increased by £4.6m. This relates to the draw-down of loans of £10.4m agreed from the Department of Health and the repayment of loans of £4.6m. Other borrowings have reduced due to repayments made in relation to obligations under finance leases and PFI contracts.
- Provisions has reduced due to the change in discount rate from 1.3% to 1.37% which decreases the non-current costs of pension and injury benefit provisions and an decrease as equal pay and employee litigation cases have now been settled or reduced.

Taxpayers Equity (as per the Statement of Changes in Taxpayers Equity)

Public Dividend Capital

- £0.7m of Public Dividend Capital (PDC) was repaid in relation to an agreement with Monitor to fund an agreed underspend on capital expenditure below plan as income and this was repaid as PDC.

Income and expenditure reserve

- Income and expenditure reserve has increased by £11.8m. This relates to retained surplus for the year of £11.7m and transfer in relation to revaluation reserve balances on asset disposals of £88k.

Revaluation reserve

- The increase in revaluation reserve of £0.7m relates mainly to a net gain in amounts credited to the revaluation reserve for the valuation undertaken as at 31 March 2016, where increases in the value of assets have exceeded the amounts previously charged to I&E.

Cash Flow

- There is an increase in cash of £6.8m as per above in net current assets and liabilities.

Significant transactions and key accounting entries in the 2015/16 accounts

1. Equal Pay

As part of a national equal pay issue the Trust received in excess of 800 potential claims associated with equal pay. During 2014/15 these legal claims progressed and a number of cases were closed and a provision remained of £246k as at 31 March 2015 for expected settlements in 2015/16. Claims have been settled for £305k in 2015/16 with £59k arising in year. There are no provisions outstanding at 31 March 2016.

2. Holiday entitlement not taken

Accruals were made in the 2014/15 accounts for annual leave due but not taken of £1.2m and amounts recoverable for leave taken but not yet due of £0.1m. The accrual was based on data gathered from managers of leave carried forward and was based on an overall 67% response rate. The Trust has undertaken the same process to gather the data and the 2015/16 accrual is based on a response rate of 70% and is £1.2m and a receivable of annual leave taken in advance of £18k.

3. Provisions for Impairment of Receivables

Each year the Trust assesses all outstanding debts to consider whether a potential irrecoverable debt provision should be made. The provision as at 31 March 2015 was £0.7m.The provision for 31 March 2016 is £0.7m and £403k relates to CCGs, the most significant of which is North Durham CCG £155k, £86k relates to FTs and £197k relates to trade and amounts owed from individuals.

In accordance with accounting policies, the methodology the Trust has applied to the was to assess all outstanding debts as at 31st March and provide for all debts over 3 months old as potential irrecoverable debts unless there is a specific reason not to provide. Specific reasons may include debts subsequently paid or balances where assurances have been provided that the debts will be paid. Where disputes are known, it may also be appropriate to provide for certain debts less than 3 months old.

4. Redundancy provisions and employee claims

The Trust had redundancy provisions of £0.1m in the 2014/15 accounts in relation to expected redundancy costs and provisions of £0.1m were made in relation to employee litigation claims.

Redundancy provisions as at 31 March 2016 are £0.4m in relation to phase 2 of Transforming Corporate Services. Redundancy costs arose and were paid in the year of £0.6m in relation to phase 1 of Transforming Corporate Services.

For employee litigation cases, legal advice has been provided to support the validity of any provisions made in the 2015/16 accounts. There are no significant employee litigation cases as at 31st March 2016.

5. Long-term pensions and injury benefit provisions

The provision for long-term pension liabilities as at 31st March 2015 was £1.5m. (£0.1m) was utilised in 2015/16 in respect of payments made to the NHS Pensions Agency. Due to changes in the Treasury FReM, provisions for long-term pension liabilities have been revised to reflect the change in the discount rate from 1.3% to 1.37%. The impact of the change in rate is not significant and there have been no significant changes in cases in 2015/16. Pension provisions as at 31st March 2016 are £1.4m.

The injury benefits provision is made on the same basis as the long-term pension provisions. The discount rate for injury benefit provisions has also changed from 1.3% to 1.37%. The provision as at 31 March 2015 was £5.0m. (£0.3m) has been utilised in respect of payments made to the NHS Pensions Agency. The impact of the revised provisions is £0.2m for the change in life expectancies and change in discount rate. Unwound discount of £0.1m will take the provisions to a closing position as at 31st March 2016 of £5.0m.

6. Other legal cases

A provision for legal claims was made in the accounts as at 31st March 2015 for £0.2m. This provision is based on information provided from the NHS Litigation Authority in relation to public liability and employer liability claims. The Trust's provision as at 31 March 2016 is £0.2m.

7. Prepayments

Each year the Trust accounts for a number of prepayments in the usual course of business. As at 31st March 2015 the Trust had made prepayments of £3.0m, £2.2m specifically related to prepayments in respect of leased car salary sacrifice contracts. The Trust has identified prepaid invoices as at 31 March 2016 of £3.4m, approximately £2.1m of which specifically relates to prepayments in respect of leased car salary sacrifice contracts.

8. Revaluations and Impairments

IAS 16 requires that the carrying value of property is not materially different to fair value at the balance sheet date. To ensure this reflected in the annual accounts a valuation has been undertaken by the District Valuer as at 31 March 2016 of land and buildings.

Specialised NHS buildings are valued on the basis of depreciated replacement cost (DRC).The DRC approach is based on the economic theory of substitution and is used in situations where there is no directly comparable alternative. The comparison therefore has to be made with a hypothetical substitute, also described as the modern equivalent asset.

In accordance with the Trust's accounting policies all non-operational properties which have not been reclassified as held for sale at 31 March and where there are no plans to bring the assets back into operational use will be valued at market value and based on the market land value of their current locations. These assets have been valued outside of the Trust's modern equivalent asset methodology.

Work has been undertaken by the District Valuer to review the asset values as at 31 March 2016. This work has resulted increase of 10% in NHS specialised buildings. Revaluation gains are recognised in the revaluation reserve, except where, and to the extent that, they reverse a revaluation decrease that has previously been recognised in operating expenses, in which case they are recognised in operating income.

A decrease in value is charged to the revaluation reserve, up to the point of previous year's gains until the revaluation reserve is fully utilised and then any further revaluation loss will be treated as an impairment charged to the Statement of Comprehensive Income.

The increase in valuations resulted in income for the reversal of previous impairments of £10.9m, with £3.4m charged as impairment charges and revaluation gains to the revaluation reserve of a net £0.8m.

9. <u>Additions and disposals/assets held for sale</u>

IFRS 5 states that an asset should be classified as held for sale at the lower of its carrying amount and fair value less costs to sell. Fair value is the amount an asset could be exchanged for between knowledgeable, willing parties in an arm's length transaction.

IFRS 5 also states that a non-current asset should be classified as held for sale if its carrying amount will be principally recovered through a sale transaction rather than through continuing use. Assets intended for disposal are reclassified as 'Held for Sale' once all of the following criteria are met:

- the asset must be available for immediate sale in any present condition subject only to terms that are usual and customary for sales of such assets
- it's sale must be highly probable, ie
- management are committed to a plan to sell the asset
- an active programme has begun to find a buyer and complete the sale
- the asset is being actively marketed at a reasonable price
- the sale is expected to be completed within 12 months of the date of classification as 'Held for Sale'; and
- the actions needed to complete the plan indicate it is unlikely that the plan will be dropped or significant changes made to it

Assets held for sale as at 31st March 2015 totalled £1.6m in relation to Social and Residential Homes. These homes were sold during the year. An asset was reclassified as held for sale during the year with a fair value of £0.7m. This asset was sold on 31st March 2016. There are no assets held for sale as at 31st March 2016.

10. <u>Purchase of Land and Buildings</u>

The asset which was reclassified as held for sale in the year was the Willows in Morpeth. The asset sale was part of a transaction with Northumberland County Council whereby the Trust received proceeds for this asset of £675k and two buildings were purchased in exchange totalling £375k. The assets purchased were Ashmore House in Ashington and

Wellington House in Blyth. Both properties were being leased by the Trust and the Trust had a liability for backdated rent and other costs in the accounts of £300k in relation to Wellington House. This was settled as part of the sale transaction.

Total capital expenditure for 2015/16 is £15.6m.

11. Consolidated Accounts and Limited Liability Partnership Assessment

The Trust will continue to account for the Limited Liability Partnership arrangements on an equity basis and this will be reported as an investment in a joint venture.

From 2014/15, IFRS 11 Joint Arrangements applied. A joint arrangement is an arrangement of which two or more parties have joint control. A joint operation exists where the parties that have joint control has rights to the assets and obligations for the liabilities relating to the arrangement. A joint venture exists where the parties that have joint control have rights to the net assets of the arrangement. Where an NHS Foundation Trust is party to a joint venture, it should recognise its investment through the equity method in IAS 27.

The profit/loss in the investment in the LLP with Insight is minimal and will be reported as an investment in an associate in line with 2014/15.

Recommendation

- Approval of the draft accounts
- Signing of the management representation letter

James Duncan
Director of Finance
May 2016