

To: The Board

Monitor 2004/58

cc:

Date: 24/11//2004

For meeting on: 30/11/2004

Agenda item: 22.D.(iii)

To note and for discussion

Title: BRADFORD – KEY LEARNINGS

Issue: This paper summarizes the findings of the review of the assessment of Bradford to support the licensing decision on 1 April 2004. Its purpose is to understand how and if the issues that have since emerged were addressed by the assessment team and to draw out any implications for the assessment process going forward.

Recommended Board actions: That the Board **notes and discusses** the contents of the paper

A BACKGROUND

At their meeting on 21 October 2004, Monitor's Board were advised that the Director of Finance and Applications had instigated an internal review on the assessment process leading up to the decision to authorise Bradford on 1 April 2004.

I have led the review with assistance of staff who, like me, were independent of the decision making process. My analysis and conclusions are set out at Annex A to this paper.

B ANALYSIS

See Annex A.

C CONCLUSION

See Annex A.

D SCHEDULE OF ATTACHED PAPERS AND RELEVANT SOURCE MATERIAL

Annex A – Bradford – Key Learning Points

E SIGNATURE

McKinsey & Co

24.11.2004

MONITOR 2004/58

ANNEX A

CONFIDENTIAL
DRAFT FOR DISCUSSION

Bradford – Key Learnings



Independent Regulator
of NHS Foundation Trusts

24 November 2004

SUMMARY (1/3)

This report summarizes the findings of our review of the assessment of Bradford to support the licensing decision on 1 April 2004. Its purpose is to understand how and if the issues that have since emerged were addressed by the assessment team and to draw out any implications for the assessment process going forward.

1. At the date of licensing, the Board of the Trust, The Independent Accountants, Monitor and the external auditors were unaware of either the deficit for 2003/4 or of serious concerns about liquidity for 2004/5. However, by the 8th and 15th of April both David Jackson and Paul Earp had produced memos to the board highlighting both issues. It is unclear what led to such a substantial change in their view of the year end position and the 2004/5 outlook in such a short period of time.
2. As part of the assessment and licensing process the Board of Directors provided a written statement to the Regulator that 1) The working capital available to the Trust is sufficient to meet its present requirements, that is at least for the first 12 months from the date of licensing, and 2) They have established procedures which provide a reasonable basis for them to reach proper judgement as to the financial position and prospects of the Trust.

PwC, the Independent Accountants, was asked to provide a professional opinion on the statement of working capital adequacy and on whether the statement on Financial Reporting Procedures had been made after due care. PwC provided a clean working capital opinion to the Board with a £3m facility in place together with a clean opinion on financial reporting procedures. It now appears that the actual working capital needs could be as high as £20m.

The Working Capital statement by the Board and the professional opinion of PwC was provided despite a number of 'red flags'

- The last balance sheet provided by management was December 2003. Furthermore, no financial reports on current trading were provided or sought by PwC after that date
- PwC noted a history of overspending but this was assumed to be activity related and had always been funded by the PCT and therefore may not have been fully investigated and understood
- PwC noted specific concerns on the level of support for the cost improvement program and the extent to which the Consultant Contract and Agenda for Change costs were built into the Trust's projections for 2004/5
- PwC noted problems with the Shared Service Centre ("SSC") introduced in October 2003, particularly a backlog of payments to suppliers with some threatening to cut off support and incidences of double payments by the Trust and the SSC

SUMMARY (2/3)

The Financial Procedures statement and professional opinion of PwC was supported by very positive reports and inputs on the quality of financial management at the Trust from the Audit Commission, Internal Auditors, and Willis. However

- PwC did not receive or seek evidence that the reporting procedures noted in their report were in effect after December 2003
- PwC noted that the introduction of shared services had resulted in significant weaknesses in financial reporting, but they were satisfied with management's plan to address these weaknesses

3. To support their view on short term financial viability of the Trust, Monitor placed significant and appropriate emphasis on the statement by the Board, the opinion of PwC, the work of the internal and external auditors, and the assurance provided by David Jackson that activity for 2004/5 had been agreed with the PCT and contracts signed.

There are, however, a number of learnings for Monitor's assessment process from this review:

- In addition to meeting with the Independent Accountants and reviewing their report, The Monitor team should critically review and challenge the basis for the opinions provided. This should be based upon a detailed review of their report and an independent analysis of current trading and the financial plan for the next 12 months. In the case of Bradford, such a review should have raised concerns for discussion with the Board, PwC and the Trust's internal and external auditors before licensing
- The specific requirements from the Financial Reporting Procedures review has been extended for group 3 applicants. However, the Monitor team should ensure the Independent Accountants are fully briefed on the scope and expectations from this work
- The Monitor team should re-emphasise to the Board of the Trust their responsibility in providing a statement on working capital adequacy and Financial Reporting Procedures and recommend that they meet with the Independent Accountants to ensure they understand the basis of the Independent Accountant's opinion
- The Monitor Board should ensure that it meets and forms a view on the effectiveness of the non executive directors of each Trust as part of the Board to Board program of meetings. In the case of Bradford the Monitor Board met only the CEO, CFO and Chairman of the Trust
- Monitor should consider a more formal and explicit assessment of executive and Board capabilities.
- Monitor should review the extent to which reliance can be placed on the views of the External and Internal auditors concerning the quality of financial management in the Trusts

SUMMARY (3/3)

The first four recommendations are standard practice for Monitor, and Bradford appears to have been an exception to this practice. The fifth point is currently under review by Monitor and will be discussed at its 30th November Board meeting. The final point should be subject to better understanding the nature and quality of the work undertaken by these third parties

ASSESSMENT APPROACH

Assessment Area

Comments

Monitor

- Constitution Review
- Independent Analysis
- Trust Interviews
- Board to Board meeting
- Trust Self-Certification
- Other Third Parties

- Reviewed by Monitor legal advisor, satisfactory amendments received
- Reviewed Service Development Strategy, Financial Plan, and detailed supporting financial and governance submissions such as risk management and performance management documents
- Analysed in detail the financial plan and performed sensitivities on the Trust's base case
- Interviewed CEO, FD, Chairman, Director of Planning and Performance, Director of Hospital Services and Chief Nurse, Risk Manager, Audit Committee Chair, Assistant Finance Director, Operations Director, Health Informatics
- Attended by Chairman, CEO and FD. Other board members did not attend
- No issues raised
- Interviewed key stakeholders including the two largest PCTs and the SHA to gain external views on the Trust, positive reports
- External Audit (Audit Commission): Clean audit opinion for 2002/3 year end, no significant issues identified for 2003/4. Subsequently a clean audit opinion was signed in late July for the 2003/4 year end
- Internal Audit: no issues raised during assessment period
- Audit Commission report on Performance Management, positive report
- Willis Report on clinical, financial and governance risk management, positive report

Accounting Firm (PwC)

- Working Capital Review
- FRP Report

- Clean working capital opinion given with a facility of £3m:
 - Key financial targets have been met in the last 3 years without the need for brokerage¹
 - 90% of activity levels and 80% of income for 2004/05 backed by letters of intent²
- Clean FRP opinion given:
 - “Adequate procedures are in place in all areas over which the trust has direct control”³ including finance department staffing; financial instructions and standing orders; risk management; controls assurance; budgeting and budget monitoring
 - “reporting lines... of the finance department are fit for purpose”⁴

POST ASSESSMENT DEVELOPMENTS (1/2)

Key issues

Assessment Approach

Year end 31 March 2004

- 2004 year end deficit was £2.3m before brokerage, compared to a forecast breakeven at the date of licensing

- Trust Board, Monitor, PwC and the external auditors were not aware of the deficit
- PwC relied on the December 2003 balance sheet and management accounts and subsequent discussions with the FD and CEO to validate the forecast year end position
- Neither the FD nor the CEO informed the Trust Board, PwC or Monitor of significant risks to, or inaccuracies in, the 2003/4 year end outlook

PCT Contracts

- Trust has been unable to agree 2004/5 baseline despite assurances given at the time of licensing

- Specific assurance on PCT contract and baseline for 2004/5 made by David Jackson to Bill Moyes immediately prior to licensing

Activity Coding

- PCTs have questioned basis of coding at Bradford during and since assessment

- £2m projected additional revenue from tighter coding taken out of assessor case in financial sensitivity analysis
- No other evidence of coding issues was noted

Costs

- Since assessment there has been a substantial cost overrun

- PwC noted Trust had a history of overspends, however these were all assumed to be activity related and were fully funded by the PCTs
- Specific concerns on the quality of forecasts noted by PwC and Monitor:
 - Consultant contract and Agenda for Change costs not fully reflected in projections
 - Cost Improvement Program was not well supported and the Trust's track record in cost reduction was unclear
- No communication of concerns by the CEO/FD at the time of licensing though significant concerns were noted in memos from David Jackson and Paul Earp on the 8th and 15th of April

Budgeting Accuracy and Control

- There has been substantial variances from budget at year end and since assessment

- PwC Financial Reporting Procedures Report concluded that Trust's budgeting and control was adequate:
 - "monthly financial performance is reviewed with significant variances being investigated"⁵ (Although this did not include sight of board reports after December 2003)
 - Noted that Trust had met key financial targets in each of the last 3 years
- No direct analysis of performance versus budget after December 2003 was undertaken by PwC

POST ASSESSMENT DEVELOPMENTS (2/2)

Key issues

Internal Reporting

- Financial reporting to the Board may have broken down from as early as December 2003

Assessment Approach

- PwC FRP Review concluded that adequate procedures were in place for internal reporting, though there was no direct verification that these systems were in place in the last three months of the year
- Other third parties did not raise particular concerns:
 - External audit “Bradford has an excellent approach to performance management” and stated that it was the best Trust regarding financial management that they had come across⁶
 - Audit Commission wrote that Bradford has “an excellent approach to performance management”⁷
 - SHA said that they had no concerns on financial management⁸
 - Willis assessment scored Bradford 98% compliance on financial management⁹
- Assessment Team recorded that performance management appeared more clinically focussed rather than financially focussed, but relied on PwC’s FRP review on financial reporting

Shared Services

- The introduction of shared services in October 2003 has resulted in problems with financial reporting and financial management at the Trust

- PwC’s FRP Review indicated:
 - The introduction of shared services resulted in considerable weaknesses in financial reporting¹⁰
 - Significant payment backlog and suppliers threatening to stop supplying
 - Incidents of double payment by shared services and Trust to suppliers
 - PwC, however, were satisfied with management’s action plan to address these risks

Management Assessment

- Management and Board have failed to proactively and effectively address year end and subsequent financial issues

- Assessment Team interviewed: CEO, FD, Chairman, Director of Planning and Performance, Director of Hospital Services and Chief Nurse, Risk Manager, Audit Committee Chair, Assistant Finance Director, Operations Director, and Health Informatics representative
- Board to Board meeting had only the Chairman, Chief Executive and Finance Director present
- Assessment Team expressed concerns about Audit Chair in internal meeting minutes¹¹

IMPLICATIONS FOR THE ASSESSMENT PROCESS

Key Recommendations

Comments

• Review of Accountant’s and other Third Party Reports by Monitor

- Working Capital and FRP reports as should be received in sufficient time for the Monitor team to thoroughly review and discuss with the accounting firms and follow up with the Trust as required.
- Reports should be reviewed within Monitor by assessors with the appropriate skills
- The Monitor team should critically review and challenge the Independent Accountant’s findings based on a detailed review of the report and an independent analysis of current trading and the financial plan for the next 12 months

• Financial Reporting Procedures Report

- FRP instructions should be reviewed to emphasise the following areas:
 - Specific review of past forecasting accuracy and the way in which significant variances are analysed
 - Specific review of actual management and board reports in the 12 month period up to licensing as well as the reporting process, and any planned changes
 - Review of the nature and adequacy of the procedures performed by Shared Service Centres on behalf of the trust

• Working Capital Report

- Accounting firms should present their working capital and FRP review reports to the board of the trust, take questions thereon, and challenge the board to establish whether they fully understand the nature of the statement they are due to make and that it has been made with due care

• Management Assessment

- Monitor Board should meet all Executive and Non-Executive Directors
- Assessment of management should be strengthened and made more explicit

• Integrated finance and governance assessment

- Assessment Teams should share financial and governance assessment so that links between issues are appreciated by all assessors

• Reliance on other third party reports

- Monitor should review the extent to which reliance can be placed on the views of the External and Internal auditors concerning the quality of financial management in the Trusts

• Key meeting notes

- Monitor should ensure that all meetings material to the assessment process are documented to an appropriate level of detail and filed

FOOTNOTES

1. NHSFT Financial Assessment – Bradford Teaching Hospitals Final Report, PWC, 30th March 2004, p15
2. NHSFT Financial Assessment – Bradford Teaching Hospitals Final Report, PWC, 30th March 2004, p4
3. NHSFT Financial Assessment – Bradford Teaching Hospitals Final Report, PWC, 30th March 2004, p69
4. NHSFT Financial Assessment – Bradford Teaching Hospitals Final Report, PWC, 30th March 2004, p6
5. NHSFT Financial Assessment – Bradford Teaching Hospitals Final Report, PWC, 30th March 2004, p6
6. Monitor Meeting with External Audit, Interview Notes, 25th February 2004, Assessment File
7. Performance Management: Bradford Hospitals Teaching NHS Trust, Draft Report, Audit Commission, February 2004
8. Meeting with Richard Jeavons, SHA Interview Notes, Date Unknown, Assessment File
9. Performance Management: Bradford Hospitals Teaching NHS Trust, Draft Report, Audit Commission, February 2004
10. Bradford Teaching Hospitals Assessment Summary, Board Pack, 30th March 2004, Assessment File, page 70
11. Audit Committee and Monitor Meeting, Interview Notes, 25th February 2004, Assessment File