The Audit of Croydon PCT's 2010/11 Accounts

South West London Joint Health Overview and Scrutiny Committee
November 2012
The Audit Commission's role is to protect the public purse.

We do this by appointing auditors to a range of local public bodies in England. We set the standards we expect auditors to meet and oversee their work. Our aim is to secure high-quality audits at the best price possible.

We use information from auditors and published data to provide authoritative evidence-based analysis. This helps local public services to learn from one another and manage the financial challenges they face.

We also compare data across the public sector to identify where services could be open to abuse and help organisations fight fraud.
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Introduction

1 This briefing is provided to assist the South West London Joint Health Overview and Scrutiny Committee (JHOSC) in its inquiry into the financial management and governance arrangements at Croydon Primary Care Trust (PCT) in 2010/11.

2 The statement covers the:
■ role of the Audit Commission;
■ responsibilities of its appointed auditors; and
■ background to and findings of the Commission's review of the audit of Croydon PCT's 2010/11 accounts.

3 It supports material we have already provided to the JHOSC, in particular:
■ the report of the Commission's review of the audit of Croydon PCT's 2010/11 accounts; and
■ the 'Statement of responsibilities of auditors and of audited bodies' for local NHS bodies, issued by the Commission in March 2010.

4 Martin Evans, the Commission's Managing Director, Audit Policy and Steve Warren, Technical Director of the Commission's in-house Audit Practice, will also attend before the Committee at its meeting on 26 November.
The role of the Audit Commission

5 The Audit Commission is responsible for overseeing the local public audit regime in England. Under the Audit Commission Act 1998 (the Act), its statutory responsibilities in relation to audit are to:
- appoint auditors to local government and NHS bodies and specify their terms of appointment;
- maintain and keep under review a statutory Code of Practice, which prescribes the way in which auditors are to carry out their statutory responsibilities;
- set scales of audit fees and determine variations to the scale fees for individual bodies;
- make arrangements for the certification of claims and returns.

6 The Audit Commission does not itself undertake audits or issue audit opinions. Appointed auditors are public office holders in their own right and, once appointed, are required in law to discharge their statutory responsibilities and to exercise their professional judgement independently of the Commission. The Commission cannot interfere with the judgements or decisions made by an appointed auditor, as to do so could compromise the auditor’s independence.

7 The Commission may appoint firms of auditors or ‘officers of the Commission’ as appointed auditors. Until 2011/12, approximately 70 per cent of audits were carried out by District Auditors or Senior Audit Managers from the Commission’s in-house Audit Practice. The appointed auditor for Croydon PCT for 2010/11 was Shahida Nasim, a Senior Audit Manager in the Commission’s in-house Audit Practice.

8 Auditors from the Audit Practice were appointed as named individuals and exercised their powers as auditors in their own right, although the Audit Practice was responsible for providing the necessary technical support, training and advice, and management oversight.

9 The Audit Practice was run as a separate business unit within the Commission until its work was outsourced at the end of October. In the exercise of its statutory functions in relation to audit, the Commission treated the Audit Practice in exactly the same way as the other firms, which it appoints as auditors.

10 In support of its own statutory audit functions, the Commission:
- monitors auditors’ compliance with its regulatory requirements; and
- reviews the quality of auditors’ work, both directly and by commissioning independent inspections from the Audit Inspection Unit (AIU) of the Financial Reporting Council i.

i The FRC is the body responsible for the regulation of the accountancy profession in the UK. The AIU is responsible for reviewing and reporting
11 The Commission publishes annually the results of its compliance monitoring and quality review programme. The report is available on the Commission’s website at:

http://www.audit-commission.gov.uk/aboutus/auditqualityreports/Pages/qualityreviewprocess.aspx

12 The Commission’s Audit Practice was subject to an annual inspection by the AIU. The results of the inspection were published in the Audit Practice's annual quality report, which is available on the Commission's website at:

http://www.audit-commission.gov.uk/aboutus/auditqualityreports/Pages/annualqualityreport.aspx

13 Where the Commission deems it necessary, it will also undertake reviews of individual audits. It was in this context that the Commission carried out an independent review of the audit of Croydon PCT’s 2010/11 accounts.
The responsibilities of the appointed auditor

**Auditors' statutory responsibilities**

14 In discharging their responsibilities under the Act, appointed auditors are required to comply with the Commission's statutory Code of Audit Practice. The current Code of Audit Practice for local NHS bodies (the Code) was approved by Parliament in March 2010.

15 The audit of Croydon PCT's 2010/11 accounts was required to be carried out in accordance with this Code.

16 In relation to the audit of the financial statements, the Code states (at paragraph 17) that:

'At the conclusion of the audit of the accounts, auditors are required to give their opinion on the financial statements, including:

a. whether they give a true and fair view of the financial position of the audited body and its expenditure and income for the year in question;

b. whether they have been prepared properly in accordance with relevant legislation and applicable accounting standards; and

c. for specified NHS bodies i, on the regularity of the expenditure and income ii.'

17 The Code also requires auditors to 'review, and report on as appropriate, other information published with the financial statements, including the statement on internal control, the annual report and the remuneration report' (paragraph 19).

18 The Code goes on to state (at paragraph 22) that:

'In carrying out their responsibilities in relation to the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time, and have regard to any other relevant guidance and advice issued by the Auditing Practices Board (APB) iii, including that covering the work of auditors in relation to audited bodies' statements on internal control'.

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i Croydon PCT was a specified body

ii The Code defines regularity as ‘whether, subject to the concept of materiality, the expenditure and income of the audited body have been applied for the purposes intended by parliament, and whether they conform with the authorities that govern them’

iii The APB is the body responsible for setting professional standards of auditing in the UK and the Republic of Ireland
Statement of Responsibilities of auditors and of audited bodies

19 Auditors carry out and report on their work under the Code in the context of the Commission’s ‘Statement of responsibilities of auditors and of audited bodies’ for local NHS bodies (the Statement). The current Statement was issued to NHS bodies in March 2010 and applied to the audit of Croydon PCT’s 2010/11 accounts.

20 The Statement serves as the formal terms of engagement between the Audit Commission’s appointed auditors and NHS bodies. It summarises where the different responsibilities of auditors and of the audited body begin and end, and what is to be expected of the audited body in certain areas. Throughout the Statement, the term ‘audited body’ covers both the directors and senior officers of the body.

21 The Statement emphasises that the primary responsibility for preparing financial statements that give a true and fair view of the body’s income and expenditure, and financial position and for the system of internal controls that underpins those statements, rests with the body itself. It also indicates that in meeting their responsibilities auditors may obtain representations from management on specific aspects of the audit.

22 The Statement states that auditors will provide reasonable assurance that the statements prepared by the body give a true and fair view, subject to the concept of materiality\(^i\). Auditors of PCTs will also provide reasonable assurance on the regularity of expenditure and income, again subject to the concept of materiality.

23 However, the Statement points out that in carrying out an audit, auditors examine selected transactions and balances on a test basis only; they do not perform detailed tests of all transactions. Therefore the audit process cannot be relied upon to disclose all unlawful transactions or events that may have occurred or might occur.

24 The Statement also makes clear that auditors do not provide assurance to audited bodies on the operational effectiveness of specific systems and controls or the wider system of internal control, which underpin the financial statements, and cannot be expected to identify all weaknesses that may exist.

25 In this context, although auditors will review the body's annual statement on internal control for consistency with their knowledge of the

\(^i\) The concept of materiality is defined in the Code as ‘an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor’s report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects’
body, they do not express a formal opinion on the effectiveness of the audited body's corporate governance procedures or risk and control procedures.

26 The Statement also sets out the limitations on auditors' responsibilities in relation to fraud.

27 Auditors cross refer to the Statement in their audit planning documents, annual audit letters, reports and other audit outputs.

28 Relevant extracts from the Statement are reproduced in Appendix 1.

**What is an audit?**

29 The APB has defined 'an audit' as follows:\(^1\):

> 'An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the [audited body's] circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements'.

30 As we have indicated above, in planning and performing an audit under the Commission's Code appointed auditors are required to comply with auditing standards currently in force and have regard to any other relevant guidance and advice issued by the APB. The auditing standards relevant to the audit of Croydon PCT's 2010/11 accounts were the International Standards on Auditing (ISAs) (UK and Ireland) then in force.

31 ISAs (UK and Ireland) contain requirements which the auditor must comply with unless a particular ISA (UK and Ireland) or a requirement of an ISA (UK and Ireland) is not relevant. They require the auditor to:

- plan and perform an audit with professional scepticism recognising that circumstances may exist that cause the financial statements to be materially misstated; and
- exercise professional judgment in planning and performing an audit.

32 In forming an opinion on the financial statements the auditor will then conclude whether:

- sufficient appropriate audit evidence has been obtained;
- uncorrected misstatements are material, individually or in aggregate;
- the financial statements, including the related notes, give a true and fair view; and

\(^1\) In 'Scope of an Audit of Financial Statements of Private Sector Entities arising from the requirements of ISAs (UK and Ireland)'
the financial statements are prepared, in all material respects, in accordance with the requirements of the relevant financial reporting framework, including the requirements of applicable law.
Background to the Audit Commission's review of the audit of Croydon PCT's 2010/11 accounts

33 The Commission is committed to securing high quality audits and therefore takes very seriously any concerns about the quality of the work of appointed auditors, whether from audit firms or its in-house Audit Practice, and investigates any complaints it receives about their work.

34 The Commission first became aware of concerns about the conduct of the audit not from the PCT, or the SHA, but at a regular quarterly meeting with senior officials at the Department of Health on 19 December 2011. At that meeting, it was suggested that Croydon PCT's board had just, or was about to, pass a vote of 'no confidence' in its appointed auditor.

35 At this stage the Audit Commission was already aware that Ernst and Young had been engaged to undertake a review of the financial management of the PCT. The appointed auditor was co-operating fully with that review. But there had been no suggestion that this review would consider the role of the auditor.

36 In the light of the emerging information about Croydon PCT, Martin Evans, the Commission's Managing Director, Audit Policy decided, after consulting senior colleagues, to ask his Head of Audit Quality, Keith Douthwaite, to conduct an urgent review of the quality of the 2010/11 audit of Croydon PCT. The aim of the review was to determine whether there was any evidence of non-compliance with the auditor's statutory and professional responsibilities and, if so, what action the Audit Commission should take.

37 To ensure the review was seen to be independent he arranged for Paul Winrow, an experienced Director of Grant Thornton, who is responsible for the firm's quality reviews of its own local public audit work, to join Keith Douthwaite on the review team.

38 In accordance with auditors' statutory terms of appointment, the auditor cooperated fully with the review and responded promptly to the quality review team's questions. The review team also had unfettered access to all the auditor's working papers.

39 On 6 January 2012, Martin Evans wrote to Ann Radmore, Chief Executive of the South West London PCT cluster (the PCT cluster) and Paul Baumann, the Finance Director of NHS London, confirming the terms of the review and promising to keep them informed about the progress of the review and any action arising from it.
On 12 January 2012, Martin Evans and Keith Douthwaite met Paul Baumann and his deputy, Azara Mukhtar, to discuss the scope of the review and its relationship to the Ernst and Young review.

Both Paul Baumann and Ann Radmore welcomed the actions the Audit Commission had taken.

Paul Baumann wrote on 17 January 2012 'I am pleased to hear that the Audit Commission has instigated a review of the Croydon PCT audit'. In his letter he discussed how the results of the Commission's review of the audit could be incorporated or, if the respective timings of the two reviews did not permit this, alluded to in the Ernst and Young report.

Ann Radmore wrote on 6 February 2012, 'I am reassured that the Audit Commission has acted in a prompt manner to look into concerns which have been raised about the quality of the work of one of its auditors'.

The review of the audit was completed in March and on 4 April 2012 a letter summarising the findings of the review was sent to Ann Radmore. The letter was copied to:

- Sian Bates, Chair of the PCT cluster;
- Paul Gallagher, Chair of the Audit Committee of the PCT cluster;
- Jill Robinson, Director of Finance of the PCT cluster;
- Paul Baumann, Director of Finance, NHS London;
- Azara Mukhtar, Deputy Director of Finance, NHS London; and
- Shahida Nasim, the appointed auditor.

A copy of the letter is attached as Appendix 2.

The Ernst and Young report was subsequently made public on 19 June 2012. It draws inferences about the conduct of the audit, despite not having access to the auditor’s working papers. It also did not fully reflect the observations that the appointed auditor made on drafts of the report.
Findings of the Audit Commission's review of the audit of Croydon PCT's 2010/11 accounts

Scope of the review

47 The review addressed specific aspects of the conduct of the 2010/11 audit about which the PCT cluster had expressed concern, in particular that the auditor failed to:
   ■ report a material misstatement in commissioning spending in 2010/11, which was causing serious financial problems in 2011/12; and
   ■ take proper account of the significant organisational changes at the PCT in 2010/11 and reflect these in her risk assessment and resulting audit work.

48 The review assessed these aspects of the audit work against the requirements of the Commission’s statutory Code of Audit Practice and applicable ISAs (UK and Ireland).

49 The quality review team interviewed Shahida Nasim and reviewed the relevant audit working papers. Keith Douthwaite also met Jill Robinson, Director of Finance, and Paul Gallagher, Chair of the Audit Committee, of the PCT cluster, to seek their views on the conduct of the audit.

50 He also sought the views of Caroline Taylor, the Chief Executive; Mark Phillips, the interim Deputy Director of Finance; and David Fitze, the Chair of the Audit Committee, of Croydon PCT during 2010/11, before the establishment of the PCT cluster.

The findings of the review

51 In summary, the review could not find evidence that an inappropriate audit opinion had been issued.

52 With regard to the first of the PCT’s two concerns, the review confirmed that, as required by auditing standards, the auditor sought and got a letter of representation signed by the Chief Executive, Director of Finance and Chair of the Audit Committee of the PCT cluster. The letter confirms among other things that all the transactions had been properly reflected and recorded in the financial statements; and all events requiring additional adjustment or disclosure had been properly dealt with. The statement on internal control approved by those charged with governance at the PCT did not identify any significant control issues.

53 The review team examined the auditor’s work on the commissioning spending and was satisfied that the selection of samples for testing was consistent with the Audit Practice’s audit approach and met the requirements of professional standards. However, some of the documentation on the audit file was not sufficient to support fully the scope
of the work and the conclusions reached on high-risk areas of the financial statements. As a result it was not clear the auditor applied the required degree of professional scepticism in these areas. In the review team’s view the auditor did the minimum required of her, but could have done more testing on aspects of the commissioning spending, including accruals, disputed balances and journals.

54 With regard to the second of the PCT’s concerns, the review confirmed that the auditor was aware of a possible increase in the risk of misstatement or manipulation of the PCT’s financial position. However, there was insufficient documentation on the audit file to support fully the auditor’s consideration of whether she should revise her assessment of these risks in the light of the changing circumstances at the PCT.

55 While individually the indicators of increasing risk may not be material or significant, taken together they could have led the auditor to revisit the initial risk assessment of misstatement or financial manipulation, and/or consider the need for more testing.

**Action taken as a result of the review**

56 In light of the findings of the review, the Audit Practice specified a minimum level of procedures that its auditors were required to carry out in relation to disputed balances as part of their 2011/12 audits of NHS bodies.

57 It also reminded its auditors of the need to ensure that there is sufficient appropriate documentation on the audit file to support the scope of their work and conclusions.
Appendix 1 'Statement of responsibilities of auditors and of audited bodies'

Responsibilities of audited bodies

General

58 The Statement sets out the general responsibilities of audited bodies for the stewardship of public money:

'Those responsible for the conduct of public business and for spending public money are accountable for ensuring that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively' (paragraph 5).

In discharging this accountability, public bodies are responsible for putting in place proper arrangements for the governance of their affairs and the stewardship of the resources at their disposal. They are also required to report on their arrangements in their annual published statement on internal control' (paragraph 6).

'It is the responsibility of the audited body to ensure that proper arrangements are in place, but certain individuals have specific responsibilities. NHS bodies have a unitary board, consisting of a non-executive chairman, non-executive directors and executive directors. The chairman and non-executive directors are responsible for monitoring the executive management of the body and are responsible to the Secretary of State for the discharge of these responsibilities. In addition, there is a requirement for an audit committee, which contributes independently to the board’s overall process for ensuring that an effective internal control and risk management system is maintained. The chief executive is responsible to the board for the day-to-day management of the organisation and, as accountable officer, is also responsible to the Department of Health for the proper stewardship of public money and assets' (paragraph 7).

The financial statements

59 The Statement then specifies audited bodies' responsibilities in relation to the financial statements:

'The financial statements, which comprise the published accounts of the audited body, are an essential means by which it accounts for its stewardship of the resources at its disposal and its financial performance in the use of those resources. It is the responsibility of the audited body to:
- put in place, and review the effectiveness of its system of internal control, including arrangements to ensure the regularity and lawfulness of transactions;
- maintain proper accounting records; and
- prepare financial statements that give a true and fair view of the financial position of the body and its expenditure and income and that are in accordance with applicable laws, regulations and accounting policies' (paragraph 11).

Other information published alongside the financial statements

60 The Statement then goes on to specify audited bodies' responsibilities in relation to other information published alongside the financial statements:

"The audited body is also responsible for preparing and publishing with its financial statements a statement on internal control and an annual report, incorporating a remuneration report' (paragraph 12).

"In preparing their financial statements, audited bodies are responsible for: preparing realistic plans that include clear targets and achievable timetables for the production of the financial statements; assigning responsibilities clearly to staff with the appropriate expertise and experience; providing necessary resources to enable delivery of the plan; maintaining adequate documentation in support of the financial statements and, at the start of the audit, providing a complete set of working papers that provide an adequate explanation of the entries in those financial statements; ensuring that senior management monitors, supervises and reviews work to meet agreed standards and deadlines; and ensuring that a senior individual at top management level personally reviews and approves the financial statements before presentation to the auditor' (paragraph 13).

Responsibilities of appointed auditors

General

61 The Statement sets out the general responsibilities of auditors:

"In carrying out their work auditors will:
- plan and manage the audits in a timely, professional and efficient manner;
- plan to complete work within agreed deadlines;
- maintain close liaison with the audited body; and
- provide appropriate and adequate resources and assign responsibilities to staff with the relevant expertise and experience' (paragraph 8).

"In meeting their responsibilities, auditors obtain representations from management, both orally and in writing, on specific aspects of the audit' (paragraph 9).
The financial statements

62 The Statement then specifies auditors’ responsibilities, and the limitations on those responsibilities, in relation to the financial statements:

‘In carrying out their responsibilities in relation to the financial statements, auditors will have regard to the concept of materiality’ (paragraph 15).

‘Subject to the concept of materiality, auditors provide reasonable assurance that the financial statements:

■ are free from material misstatement, whether caused by fraud or other irregularity or error;
■ comply with statutory and other applicable requirements; and
■ comply with all relevant requirements for accounting presentation and disclosure’ (paragraph 16).

‘Subject to the concept of materiality, auditors of strategic health authorities (SHAs) and primary care trusts (PCTs) also provide reasonable assurance on the regularity of expenditure and income. In carrying out an audit, auditors do not perform detailed tests of all transactions. Therefore the audit process should not be relied upon to disclose all unlawful transactions or events that may have occurred or might occur’ (paragraph 17).

‘Auditors plan and perform their audit on the basis of their assessment of risk. Auditors examine selected transactions and balances on a test basis and assess the significant estimates and judgements made by the audited body in preparing the statements’ (paragraph 18).

‘Auditors evaluate significant financial systems, and the associated internal financial controls, for the purpose of giving their opinion on the financial statements. However, they do not provide assurance to audited bodies on the operational effectiveness of specific systems and controls or their wider system of internal control. Where auditors identify any weaknesses in such systems and controls, they draw them to the attention of the audited body, but they cannot be expected to identify all weaknesses that may exist’ (paragraph 19).

Other information published alongside the financial statements

63 The Statement then goes on to specify the audited bodies’ responsibilities in relation to other information published alongside the financial statements:

‘Auditors review whether the statement on internal control has been presented in accordance with relevant requirements and report if it does not meet these requirements or if it is misleading or inconsistent with other information the auditor is aware of. In doing so, auditors take into account the knowledge of the audited body gained through their work in relation to the financial statements and through their work in relation to the body’s arrangements for securing economy, efficiency and effectiveness in the use of its resources. They also have regard to the work of other regulators, to the extent that it is relevant to auditors’ responsibilities. Auditors are not required to consider whether the statement on internal control covers all
risks and controls, and auditors are not required to express a formal opinion on the effectiveness of the audited body’s corporate governance procedures or risk and control procedures’ (paragraph 20).

64 ‘Auditors also review for consistency other information that is published by the audited body alongside the financial statements, such as an annual report. If auditors have concerns about the consistency of any such information they will report them to those charged with governance (paragraph 21).

Fraud

65 The Statement also sets out the limitations on auditors’ responsibilities in relation to fraud:

66 ‘Audit work in relation to the audited body’s arrangements to ensure it promotes and demonstrates the principles and values of good governance does not remove the possibility that breaches of proper standards of financial conduct, or fraud and corruption, have occurred and remained undetected. Neither is it auditors’ responsibility to prevent or detect breaches of proper standards of financial conduct, or fraud and corruption, although they are alert to the possibility and act promptly if grounds for suspicion come to their notice’ (paragraph 38).

Reporting the results of the audit

67 Finally, the Statement sets out auditors' reporting responsibilities in relation to the financial statements:

‘At the conclusion of the audit of the accounts, auditors give their opinion on the financial statements, including:

■ whether they give a true and fair view of the financial position of the audited body and its expenditure and income for the year in question;
■ whether they have been prepared properly in accordance with relevant legislation and applicable accounting standards;
■ for SHAs and PCTs, on the regularity of their expenditure and income;
and
■ whether the part of the remuneration report to be audited has been properly prepared’ (paragraph 22).

‘Auditors also give their opinion on whether the summarisation schedules and, where prepared, summarised financial statements have been properly prepared’ (paragraph 23).
Appendix 2  Report of the Audit Commission's review of the audit of Croydon PCT's 2010/11 accounts

4 April 2012

Ms A Radmore
Chief Executive
NHS SW London
120 The Broadway
Wimbledon
London
SW19 1RH

Dear Ms Radmore

Review of the 2010/11 audit of Croydon PCT

Further to my letter of 6 January, I am writing to let you know the outcome of our review of the Croydon PCT 2010/11 audit.

The PCT has expressed two concerns about the conduct of the audit by Shahida Nasim (the auditor) of the Audit Commission's Audit Practice:

■ first, she did not report a material misstatement in commissioning spending in 2010/11, which is causing the PCT serious financial problems in 2011/12; and
■ secondly, she did not take proper account of the changes at the PCT in 2010/11 and reflect these in her risk assessment and resulting audit work.

As a result the PCT felt its working relationship with the auditor had broken down irrevocably.

The Commission takes seriously all concerns about the quality of work at audits within its regime, and we set up a special review with particular emphasis on the above aspects of the audit. The review was carried out by Keith Douthwaite (the Commission’s Head of Audit Quality) and, to provide an independent perspective, Paul Winrow (Director, Grant Thornton).

We had access to all audit records and the auditor answered readily all our questions. We assessed aspects of the audit work against the requirements of the Commission’s statutory Code of Audit Practice and applicable professional auditing standards.
With regard to the first of the PCT’s two concerns, we were able to confirm that the auditor sought and got a letter of representation signed by the cluster Chief Executive, Director of Finance and Chair of the Audit Committee. The letter confirms among other things that all the transactions had been properly reflected and recorded in the financial statements; and all events requiring additional adjustment or disclosure had been properly dealt with. We also noted the PCT’s statement of internal control did not identify any significant control issues.

We found it difficult to put a figure on the alleged misstatement of commissioning spending in the 2010/11 financial statements. We understand the PCT is proposing a £27 million adjustment in the 2011/12 financial statements, but the incoming auditor has not yet been able to complete her work to assess the proposed restatement. Therefore we were not able to confirm whether any misstatement exceeded the auditor’s headline materiality figure or tolerance around the accuracy of the audit opinion of £14 million.

Against this background we could not find evidence that an inappropriate audit opinion had been issued.

We examined the auditor’s work on the commissioning spending and are satisfied that the selection of samples for testing was consistent with the Audit Practice’s audit approach and met the requirements of professional standards. However, some of the documentation on the audit file was not sufficient to support fully the scope of the work and the conclusions reached on high-risk areas of the financial statements. As a result it is not clear the auditor applied the required degree of professional scepticism in these areas. In our view the auditor did the minimum required of her, but could have done more testing on aspects of the commissioning spending, including accruals, disputed balances and journals.

In this context, we also feel the concept of materiality, its quantification and the implication for the nature of the audit assurance being provided could have been better explained to the PCT.

With regard to the second of the PCT’s concerns, our review confirmed that the auditor was aware of a possible increase in the risk of misstatement or manipulation of the PCT’s financial position. However, there is insufficient documentation on the audit file to support fully the auditor’s consideration of whether she should revise her assessment of these risks in the light of the changing circumstances at the PCT.

While individually the indicators of increasing risk may not be material or significant, taken together they could have led the auditor to revisit the initial risk assessment of misstatement or financial manipulation, and/or consider the need for more testing.

Finally, we did find indications that effective relationships were not established between the auditor and the PCT following clustering.
In light of the PCT’s views of the working relationship with the auditor, a Director of the Audit Practice met with directors of the PCT in January 2012. Following that meeting and discussions within the Audit Practice, Ms Nasim agreed with the PCT’s view about the working relationship and decided it was not in anybody’s interests for her to continue as the appointed auditor. The Commission has appointed Sue Exton, a current PCT and SHA engagement lead, as the auditor for 2011/12.

I understand that NHS London is finalising and intends to publish shortly the report it commissioned from Ernst and Young (EY) into financial management and governance at the PCT. Extracts from the draft report seen by Ms Nasim make reference to her work, and she has commented directly to EY about the draft. If the final version includes references to the auditor, we would appreciate an early sight of the final report along with any press release, so we can prepare for any subsequent questions to us.

We would like to thank all those involved with our review.

Yours sincerely

Martin Evans
Managing Director, Audit Policy

cc  Ms S Bates, Chair NHS SW London
    Mr P Gallagher, Chair of Audit Committee NHS SW London
    Ms G Robinson, Director of Finance NHS SW London
    Mr P Baumann, Director of Finance NHS London
    Ms A Mukhtar, Deputy Director of Finance, NHS London
    Ms S Nasim, Audit Commission