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Reports and letters prepared by the auditor and addressed to the CCG are prepared for the sole use of the CCG and we take no responsibility to any member or officer in their individual capacity or to any third party.
Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor for NHS East Riding of Yorkshire CCG (the CCG) for the year ended 31 March 2018. Although this letter is addressed to the CCG, it is designed to be read by a wider audience including members of the public and other external stakeholders.

Our responsibilities are defined by the Local Audit and Accountability Act 2014 (the 2014 Act) and the Code of Audit Practice issued by the National Audit Office (the NAO). The detailed sections of this letter provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

<table>
<thead>
<tr>
<th>Area of responsibility</th>
<th>Summary</th>
</tr>
</thead>
</table>
| Audit of the financial statements | Our audit report issued on 25 May 2018 included our opinion that:  
  • the financial statements give a true and fair view of the CCG’s financial position as at 31 March 2018 and of its financial performance for the year then ended; and  
  • income and expenditure has, in all material respects, been applied for the purposes intended by Parliament except for the failure to meet the statutory duty for expenditure not to exceed income in year. |
| Value for Money conclusion | Our audit report stated that we had no matters to report in respect of the CCG’s arrangements to secure economy, efficiency and effectiveness in its use of resources except for planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions. |
| Reporting to the group auditor | In line with group audit instructions issued by the NAO, on 25 May 2018 we reported that the CCG’s consolidation schedules were consistent with the audited financial statements. |
| Statutory reporting | Our report also outlined that we made a referral to the Secretary of State under s30 of the 2014 Act, in relation to the breech of financial duties. |
The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the relevant financial reporting framework and whether they give a true and fair view of the CCG’s financial position as at 31 March 2018 and financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by the NAO, and International Standards on Auditing (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the CCG’s circumstances and have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and
- the overall presentation of the financial statements provides a true and fair view.

The Code of Audit Practice also requires us to form and express an opinion on whether the CCG’s expenditure has been, in all material respects, applied for the purposes intended by Parliament (our regularity opinion).

Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider the concept of materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for specific items of account (specific materiality) because of the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Audit and Integrated Governance Committee. We call this our trivial threshold.

The table below provides details of the levels applied in the audit of the financial statements for the year ended 31 March 2018:

<table>
<thead>
<tr>
<th>Financial statement materiality</th>
<th>Our financial statement materiality is based on 1.5% of gross revenue expenditure.</th>
<th>£5.959 million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trivial threshold</td>
<td>Our trivial threshold is based on 3% of financial statement materiality.</td>
<td>£178,000</td>
</tr>
<tr>
<td>Specific materiality</td>
<td>We have applied a lower level of materiality to the following areas of the accounts:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- exit packages</td>
<td>£10,000</td>
</tr>
<tr>
<td></td>
<td>- senior officer remuneration</td>
<td>£150,000</td>
</tr>
</tbody>
</table>
## 2. AUDIT OF THE FINANCIAL STATEMENTS

### Our response to significant risks

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the CCG’s financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit and Integrated Governance Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report. The table below outlines the identified significant risks, the work we carried out on those risks and our conclusions.

<table>
<thead>
<tr>
<th>Identified significant risk</th>
<th>Our response</th>
<th>Our findings and conclusions</th>
</tr>
</thead>
</table>
| **Management override of controls**             | We addressed this risk by performing audit work in the following areas:  
• accounting estimates impacting on amounts included in the financial statements;  
• consideration of identified significant transactions outside the normal course of business; and  
• journals recorded in the general ledger and other adjustments made in preparation of the financial statements. | Our work provided us with the assurance we sought and did not highlight any issues to bring to your attention. |
| In all entities, management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Because of the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits. |                                                                                                                                                  |                                                                                              |
| **Revenue recognition**                         | We addressed this risk by:  
• undertaking cut-off testing of receipts around the year-end;  
• reviewing inter-NHS reconciliations and data matches provided by the NHSE (income and receivables); and  
• if necessary, seeking direct confirmation from third parties or their external auditors.  
This work also informs our conclusion on the regulatory element of our audit opinion. | Our work provided us with the assurance we sought and did not highlight any issues to bring to your attention. |
| In all entities, there is a risk of fraud in financial reporting relating to revenue recognition as there is potential to inappropriately record income in the wrong period. This is not to imply we suspect actual fraud, but that we approach our audit maintaining due professional scepticism. |                                                                                                                                                  |                                                                                              |
| **Related party transactions**                  | We addressed this risk by:  
• reviewing the CCG’s arrangements for identifying and recording potential related party transactions;  
• reviewing a range of documents including minutes of meetings and declarations of interest for evidence of potential related party transactions; and  
• testing disclosures in the financial statements. | Our work provided us with the assurance we sought and did not highlight any issues to bring to your attention. |
| GPs are members of the Governing Body and also potential service providers. |                                                                                                                                                  |                                                                                              |
3. VALUE FOR MONEY CONCLUSION

Audit approach
We are required to consider whether the CCG has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider. We are only required to report if we conclude that the CCG has not made proper arrangements.

The overall criterion is that, ‘in all significant respects, the CCG had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.’ To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- informed decision making;
- sustainable resource deployment; and
- working with partners and other third parties.

Our auditor’s report, issued to the CCG on 25 May 2018 outlined our qualified conclusion on the CCG’s arrangements to secure economy, efficiency and effectiveness in its use of resources.

<table>
<thead>
<tr>
<th>Sub-criteria</th>
<th>Commentary</th>
<th>Matters to report</th>
</tr>
</thead>
<tbody>
<tr>
<td>Informed decision making</td>
<td>The CCG has governance arrangements in place and takes regular reports to members. Financial data is presented alongside activity data and reports are presented at sufficient regularity allowing the CCG time to deal with issues that arise. There is evidence that the CCG manages risks effectively and maintains a sound system of internal control. The Governing Body has set the risk appetite through the Risk Management Strategy and the supporting Board Assurance Framework (BAF).</td>
<td>No</td>
</tr>
<tr>
<td>Sustainable resource deployment</td>
<td>The CCG has a brought forward deficit of £1.999 million and set an in-year deficit budget of £2.773 million for 2017/18 (and recorded an in-year deficit of £0.385 million). The medium term financial plan indicates that the CCG is forecast to break even in 2018/19 and achieve an in-year surplus position in subsequent years. This would result in the CCG returning to overall surplus by no later than 2020/21. The 2018/19 plan includes QIPP targets of £11.9 million. The CCG is rated green for financial planning by NHS England.</td>
<td>Yes. Deficits are evidence of weaknesses in proper arrangements for planning finances effectively to support the sustainable delivery of strategic priorities.</td>
</tr>
<tr>
<td>Working with partners and other third parties</td>
<td>Our audit work has confirmed there is evidence the CCG works with third parties to deliver strategic priorities. A number of policies and frameworks for partnership working are on the publications section of the external website including the Commissioning plan. The CCG works closely with the local acute trusts and other providers. The contract with the main hospital services provider is on an aligned incentive basis. The aim is to ensure the whole health economy shares responsible for managing demand and keeping costs within the financial envelope available.</td>
<td>No</td>
</tr>
</tbody>
</table>
Significant audit risks
The NAO’s guidance requires us to carry out work to identify whether or not a risk to our value for money conclusion exists. Risk, in the context of our value for money work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the CCG being inadequate. In our Audit Strategy Memorandum, we reported that we had identified one significant audit risk. The work we carried out is outlined below.

<table>
<thead>
<tr>
<th>Risk</th>
<th>Work undertaken</th>
<th>Conclusion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial position</td>
<td>We addressed this risk by monitoring the progress the CCG made in delivering its financial plan as the year progressed.</td>
<td>The CCG set an in-year deficit budget of £2.773 million for 2017/18 and delivered an in-year deficit of £0.385 million. As financial duties were not met for 2017/18 we made a referral to the Secretary of State in March 2018 and qualified our statutory conclusion.</td>
</tr>
</tbody>
</table>

In 2016/17 the CCG reported a deficit of £1.999 million.

The CCG continued to face several financial challenges in 2017/18, including the need to achieve significant savings in-year. In addition, the CCG was working with Hull CCG, Hull and East Yorkshire hospitals and the NHS England Area Team to achieve the local control total but recognised that the planned measures alone would be insufficient to address the underlying overspend. The CCG was forecasting that it would not meet the requirement, under section 223H (1) of the NHS Act 2006 (as amended), to ensure expenditure in a financial year does not exceed income.

When a CCG breaches this statutory duty, even if this is agreed with NHS England, we are under a duty to make a report to the Secretary of State for Health under Section 30 of the Local Audit and Accountability Act 2014.
The NAO’s Code of Audit Practice and the 2014 Act place wider reporting responsibilities on us, as the CCG’s external auditor. We set out below, the context of these reporting responsibilities and our findings for each.

Matters which we report by exception

The 2014 Act provides us with specific powers where matters come to our attention that, in our judgement, require reporting action to be taken. We have the power to:

- issue a report in the public interest;
- make a referral to the Secretary of State where we believe that as decision has led to, or would lead to, unlawful expenditure, or an action has been, or would be unlawful and likely to cause a loss or deficiency; and
- make written recommendations to the CCG which must be responded to publically.

We have a duty under the Local Audit and Accountability Act 2014 to refer the matter to the Secretary of State if we have a reason to believe that the CCG, or an officer of the CCG, is about to make, or has made, a decision involving unlawful expenditure, or is about to take, or has taken, unlawful action likely to cause a loss or deficiency.

On 9 March 2018, we issued a report to the Secretary of State for Health under section 30(a) of the Local Audit and Accountability Act 2014, for the breach of financial duties under:

- section 223H(1) of the NHS Act 2006 (as amended) to ensure expenditure did not exceed income in 2017/18; and
- section 223I(3) of the NHS Act 2006 (as amended) to ensure revenue resource use does not exceed the amount specified in the Direction.

We are also required to report if, in our opinion, the governance statement does not comply with the guidance issued by NHS England or is inconsistent with our knowledge and understanding of the CCG. We did not identify any matters to report in this regard.

Reporting to the NAO in respect of consolidation data

The NAO, as group auditor, requires us to report to them whether consolidation data that the CCG has submitted is consistent with the audited financial statements. We have concluded and reported that the consolidation data is consistent with the audited financial statements.

Other information published alongside the financial statements

The Code of Audit Practice requires us to consider whether information published alongside the financial statements is consistent with those statements and our knowledge and understanding of the CCG. In our opinion, the information in the Annual Report is consistent with the audited financial statements.
5. OUR FEES

Fees for work as the CCG’s auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to Audit and Integrated Governance Committee in September 2017.

Having completed our work for the 2017/18 financial year, we can confirm that our final fees are as follows:

<table>
<thead>
<tr>
<th>Area of work</th>
<th>2017/18 proposed fee</th>
<th>2017/18 final fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Delivery of audit work under the NAO Code of Audit Practice</td>
<td>£39,555</td>
<td>£39,555</td>
</tr>
</tbody>
</table>

Fees for other work

We confirm that we have not undertaken any non-audit services for the CCG in the year.
Financial outlook

The CCG has a brought forward deficit of £1.999 million and set an in-year deficit budget of £2.773 million for 2017/18 (and recorded an in-year deficit of £0.385 million). The medium term financial plan indicates that the CCG is forecast to break even in 2018/19 and achieve an in-year surplus position in subsequent years. This would result in the CCG returning to overall surplus by no later than 2020/21.

The 2018/19 financial plan reflects the second year of two year contracts with service providers. The CCG agreed an aligned incentives contract (AIC) in 2017 with its main acute services provider which focuses on a whole system approach to improving care pathways and delivering efficiencies. It is hoped similar contracts will be developed with the other acute service providers.

The 2018/19 plan includes QIPP targets of £11.9 million which have been subject to external scrutiny on behalf of NHSE, the outcome of the review is to risk rate the majority of QIPP schemes as green, low risk. The most recent feedback from NHS England continues to rate the CCG green for financial planning.

Challenges

There is evidence that the CCG commissions and procures services to support the delivery of the financial plan. The aim is to ensure the whole health economy shares responsibility for managing demand and keeping costs within the financial envelope available. There are clear plans being developed under the new contractual arrangements to change pathways and deliver savings across all organisations.

As part of the Humber Coast and Vale Sustainability and Transformation Plan and the development of the East Riding of Yorkshire Plan with East Riding of Yorkshire Council, the CCG is looking towards integrating commissioning across organisations. To ensure sufficient activity is commissioned to meet population needs while providers have sufficient resources to meet demand, the CCG and providers all need to agree affordable demand and capacity solutions. While overseeing the collaboration needed and setting the direction for financial recovery, the Governing Body will require assurance on the basis and progress of the changes to activity plans and pathways that need to be made to achieve financial sustainability.

Future actions

The CCG has a good grasp of the issues facing it including the financial pressures. Senior management take the lead locally to drive improvements and promote joined up working so that patient care is improved whilst continuing to meet financial responsibilities.

The CCG will need to maintain focus on systemic change including challenging current behaviours that lead to over performance by hospital service providers and make difficult decisions around the range and level of services provided.

How we will work with the CCG

We are grateful to the CCG, its Members and officers for the cooperation and open dialogue during the year and look forward to continuing to work closely with the CCG in delivering our Code of Audit Practice responsibilities.
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