6 The governors and the NHS foundation trust's auditor

The auditor of an NHS foundation trust has important duties in relation to the foundation trust's annual accounts. This chapter sets out the governors' role in relation to the auditor. Note that this chapter relates to the NHS foundation trust's external, not internal, auditor.

Issues that we will look at in this chapter include:

- what the auditor does;
- who the auditor can be; and
- appointing and removing the auditor.

The role of the audit committee

The audit committee is responsible for monitoring and reviewing matters such as the integrity of financial statements of the NHS foundation trust, the NHS foundation trust's internal financial controls and the internal audit function.

The audit committee must consist of non-executive directors. The *Code of Governance* states that the committee should have at least three independent non-executive directors and that at least one member of the audit committee should have recent and relevant financial experience.

What other responsibilities are there?

In order to support the underlying statutory duty, the *Code of Governance* states that the audit committee should report to the board of governors, identifying any matters where it considers that action or improvement is needed.

The report should also make recommendations as to the steps to be taken. The governors will need to consider such reports closely, particularly with regards to holding directors to account for trust performance.

The governors will also want to look at *The Audit Code for NHS Foundation Trusts* ("*Audit Code*") and, in particular, the criteria for auditors set out in the code.

The *Audit Code* is guidance that must be followed, as per the terms of authorisation for every NHS foundation trust.

Have you considered?

If governors attending the audit committee during the auditor selection process would help build skills and experience in this area.

What does the auditor do?

The auditor has statutory duties in auditing the accounts of an NHS foundation trust. These involve ensuring that:

- the accounts are prepared in accordance with all relevant directions set by Monitor and any other statutory provisions;
- proper practices have been observed in the compilation of the accounts; and
- the NHS foundation trust has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

Further details on the auditor's role are set out in Monitor's document, the *Audit Code*.

Who can be the auditor?

On authorisation as an NHS foundation trust, the auditor appointed by the Audit Commission to the predecessor NHS trust will continue to be appointed until the board of governors has had an opportunity to discuss the matter.

An engagement letter must therefore be agreed between the NHS foundation trust and the incumbent auditors for that interim period so that there is not a period during which the NHS foundation trust has no auditor in place. Thereafter, the NHS foundation trust is free to appoint whichever auditor it considers to be the most appropriate.

The auditor can either be an individual, from a firm of auditors or an officer of the Audit Commission. However, the auditor (or in the case of a firm, each of its members) must be a member of one of a list of specified professional bodies set out in legislation. This is included in the box on the left.

Specified professional bodies

(a) the Institute of Chartered Accountants in England and Wales;

(b) the Institute of Chartered Accountants of Scotland;

(c) the Association of Certified Accountants;

(d) the Chartered Institute of Public Finance and Accountancy;

(e) the Institute of Chartered Accountants in Ireland; and

(f) any other body of accountants established in the United Kingdom and for the time being approved by the Secretary of State for the purposes of this section.

In addition, the *Audit Code* includes particular criteria that the auditor must be able to demonstrate that it meets, not only on appointment but throughout its term as auditor. The auditor must:

- have an established and demonstrable standing within the healthcare sector and be able to show a high level of experience and expertise. The work is of a specialised nature, and so general audit experience is not sufficient;
- comply with the *Audit Code*; and
- subject the audit to internal quality control procedures that are sufficiently robust to monitor the compliance of the audit work with the *Audit Code*.

If the auditor fails to meet, or has cause to believe that it will not be able to comply with, the criteria set out in the *Audit Code* at any point during its appointment, the auditor must resign.

Consideration should be given to whether the team at the auditor's firm should be changed. A team that has been in place for too long may no longer be able to perform its role to the requisite standard of independence from the NHS foundation trust. To assist governors in determining rotation criteria, advice could be sought from the Audit Practices Board (APB).

The APB Ethical Standard 3 requires audit firms to put in place arrangements to ensure that:

- no individual acts as audit partner or quality review partner for more than seven years. Where an individual remains in this position for more than five years the reasons for this must be clearly stated to the Board of Governors; and
- staff in senior positions do not work on the audit team for more than seven years.

Annual process

The audit committee should make a report to the board of governors in relation to the auditor.

Such a report should be made after the completion of the annual audit and should assess the auditor's work and fees to ensure that the work is of a sufficiently high standard and the fees are reasonable.

The audit committee must make a recommendation to the board of governors with respect to the retention of the auditor. The board of governors should then consider whether it may be appropriate to remove the auditor.

Section one: appointing the auditor

What is the trigger for action?

The most common trigger for action will be the impending expiry of the existing auditor's contract term. With this, a new appointment process will need to be undertaken, whether or not the existing auditor is seeking re-appointment.

Governors also have the power to remove an existing auditor and, in certain situations, an auditor can or should resign. If either event occurs, then a new appointment will need to be made.

What are the over-arching principles?

As with all appointments, the procedure for appointment (or re-appointment) must be formal, rigorous and transparent. The appointment must be based on merit and objective criteria and the process should be described in the NHS foundation trust's annual report.

Deciding on a process

The board of governors should take the lead in agreeing with the audit committee the criteria for appointing, re-appointing or removing auditors.

Initial steps

Once the criteria have been established, the audit committee will drive the process in the first instance. However, the final decision on any appointment rests with the board of governors.

The audit committee should agree with the board of governors a clear process for the nomination of a new auditor or the re-appointment of an existing one. The board of governors should set up an audit working group made up of governors to liaise with the audit committee.

The audit committee should then prepare a specification defining the role and capabilities required. This should be agreed with the governors' audit working group.

Have you considered?

What additional training can be provided to governors charged with leading on this statutory duty.

Procurement process

Once the audit committee (in consultation with the board of governors or the working group) has decided on the qualifications, skills and experience required of the auditor, it should run a formal procurement process to obtain the best candidate in the most fair and transparent manner possible.

The exact form of the procurement process will vary depending on the NHS foundation trust. It will be in accordance with the NHS foundation trust's own procurement rules and must be within procurement law. Procurement law is complex and the audit committee and the governors' audit working group are likely to need legal advice before embarking on a new procurement process.

Even if the existing auditor is seeking re-appointment, they must be treated in the same way as all other candidates for the role. The same criteria should be applied to all those that express an interest in becoming the auditor of the NHS foundation trust.

Shortlist

The audit committee should decide on a shortlist of at least two appointable candidates. This shortlist should be considered in conjunction with the governors' audit working group.

Re-appointment

Provided the correct process is followed and the appropriate criteria are met, the existing auditor may be on the final shortlist of candidates.

Presentation by the audit committee

The audit committee and the governors' audit working group should present to the board of governors, setting out:

- the procurement process that it has followed;
- the results of the procurement process; and
- recommendations.

The recommendations should include a full description of the shortlisted candidates and an assessment of the relative strengths and weaknesses of those candidates.

In addition, as part of its recommendations, there should be proposals in respect of the terms of engagement of the external auditor.

How will the final decision be made?

The board of governors should then make a decision in accordance with its statutory obligations.

If the board of governors makes an appointment, the terms of engagement of the auditor will need to be approved by the audit committee. In particular, the board of governors and the audit committee should consider for how long the appointment should last. Best practice is to appoint an auditor for a period which allows it to develop a strong understanding of the NHS foundation trust. The norm will be a three to five year appointment.

In the event that the board of governors does not feel able to make an appointment, for example because it is not willing to accept the recommendations made to it or it believes that the procurement process was flawed or otherwise, then the matter will revert back for further consideration and action by the audit committee and the governors' audit working group. The NHS foundation trust must have an auditor. As such, the speed of the process must reflect this statutory requirement and therefore the timelines of the particular appointment process should be adhered to. Consideration may be required as to extending the incumbent auditor's contract in order to ensure that the NHS foundation trust does have an auditor at all times.

In all cases, the full process must be set out in the NHS foundation trust's annual report. In particular, if the board of governors does not accept the audit committee's recommendation, the board of directors should include in the annual report a statement from the audit committee explaining the recommendation and the reasons why the board of governors took a different position.