



Year-end issues 2022/23

24 March 2023 at 13:30

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Year-end 2022/23 accounting and auditing issues

Presenters:
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Agenda

IFRS 16

Changes to the GAM

Other continuing matters

What your auditor needs and why



IFRS 16

- Accounting reminders
- Scenarios
- Transition
- Disclosures
- Audit evidence



What is a lease?

Expanded for the public sector – includes agreements between public sector bodies that may not be enforceable by law

The right to obtain substantially all of the economic benefits from use of the asset
and
the right to direct the use of the asset

A contract that conveys the right to control the use of an identified asset for a period of time in exchange for consideration

Explicit or implicit in the contract and supplier does not have substantive substitution rights

Expanded for the public sector – includes peppercorn leases

Exemptions and deferrals

Exemptions:

- Short term <12m
- Low value asset <£5k
- Intangible assets

Deferral:

- PFI – implementation deferred until 2023/24

Is it a lease?

An NHS body has an arrangement with NHS Property Services to occupy a building, but there is no agreed contract. The NHS body has sole use of, and the right to operate the asset as it wants, throughout its period of use.

Is this a lease under IFRS 16?



Is it a lease?

An NHS Trust has entered into a contract with a medical equipment supplier for sole use of equipment and can use it as it wants. The Trust pays nothing for the equipment provided it guarantees to buy a certain quantity of an associated reagent for three years. There would be no economic benefit to the supplier in substituting the equipment.

Is this a lease under IFRS 16?



Accounting by lessees under IFRS 16

Right of use asset

Lease liability

Lease liability

Present value of the lease payments that are unpaid

Fixed payments,
less any lease incentives

Amounts payable under residual
value guarantees

Variable payments that depend
on an index or a rate

Excluding
irrecoverable
VAT

Price of a purchase option
if reasonably certain to be
exercised

Penalties for terminating lease if
the term reflects the lessee
exercising an option to terminate

Calculating the lease term

An NHS Trust leases a building. There is no fixed lease term as the lease rolls forward each year with no significant penalty for either party if the lease is terminated.

How might the lease term be calculated?



Calculating the lease term



An ICB has entered into a lease for a building. The lease is for 25 years, with a break clause which allows the ICB to terminate the lease after 15 years.

How might the lease term be calculated?

Right of use asset

Initially measured at cost

Initial lease liability

Any lease payments before the commencement date, less incentives received

Initial direct costs

An estimate of costs to be incurred dismantling or restoring the asset to the condition required by the lease

Subsequently measured in line with the class of property, plant and equipment or investment property as appropriate

Peppercorn rentals

An NHS Trust agrees to lease a building from the council for nil consideration.

Current value of the building is £500k at the commencement date. The building will be used for its service potential.

How might this be accounted for?

ROU asset - £500k

Lease liability - £0

Income - £500k

IFRS 16 and group accounts

- Alignment of accounting policies
 - Subsidiaries not applying IFRS 16
 - GAM adaptations/interpretations
- Intragroup leases
 - Asymmetrical accounting treatment – both lessor and lessee recognising assets



Accounting by lessors

Transfers risks and rewards incidental to ownership –
finance lease

Derecognise asset
Recognise receivable

Does not transfer risks and rewards incidental to
ownership – operating lease

Recognise lease payments as
income

Consideration of a sublease needs to be in relation to the head lease not the
underlying asset

Transition

Grandfathering - an arrangement that was identified as a lease under IAS 17 or IFRIC 4 at the date of transition is treated as a lease under IFRS 16

However... misapplication of IAS 17 or IFRIC 4 may need to be corrected via a PPA

Exclude leases for which underlying asset is low value

Exclude leases for which lease term ends within 12 months of date of initial application

Use hindsight to determine the lease term if the contract contains options to extend or terminate the lease

Accounting on transition

Previous OL (lessee)

Recognise lease liability - PV of outstanding lease payments discounted at lessee's incremental borrowing rate

Recognise RoU asset - amount equal to lease liability adjusted for prepayments and accruals immediately preceding transition

Peppercorn leases (lessee)

Recognise lease liability - PV of outstanding lease payments discounted at lessee's incremental borrowing rate

Recognise RoU asset - at current value if operational

Previous FL (lessee)

No change to asset or liability values

Lessors

Assess any arrangements as intermediate lessor

Cumulative effect recognised as an adjustment to opening balances

Disclosures - lessees

RoU asset and lease liability each shown separately in SOFP or notes

Depreciation, additions and carrying value by class of asset, interest expense, expenses for low value leases and variable lease payments, income from subleasing, total cash outflow.

Interest on lease liability and depreciation charge on RoU asset presented separately

Disclosures - lessors

Operating leases: lease income, variable income not depending on index/rate

Finance leases: finance income (both included and excluded from net investment in lease)

IAS 16 disclosures for assets subject to operating leases disclosed separately from owned assets

Disclosures – all leases

Maturity analyses by date of
lease liabilities of lessee,
finance lease receivables by
lessor

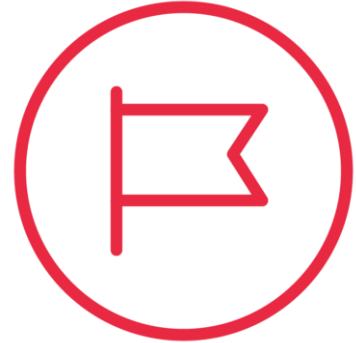
Other disclosures
needed to meet
disclosure objectives

Preparing for audit

- Processes in place to ensure accuracy and completeness
- Reconciliation between operating leases (IAS 17) and those recognised on transition to IFRS 16
- Working papers
- Significant judgements
- Year end valuations

Have you thought about ...

- Peppercorn rentals
- Short term/low value
- Variable payments
- Non-lease components of a contract
- Adjustment to opening reserve balances
- Intermediate lessors
- Intragroup leases, accounting policy alignment
- Completeness of disclosures



Other changes



Changes to the GAM



Department
of Health &
Social Care

**Department of Health and Social
Care**

Group Accounting Manual 2022-23

Published June 2022

FAQs 1-3

- FAQ 1 – discount rates for provisions, pensions, financial instruments
- FAQ 2 – injury cost revenue probability of non recovery 24.86%
- FAQ 3 – adding ICBs; additional performance reporting for NHS trusts; ICB annual reporting requirements

Further guidance expected

Clarity on reporting against new financial duty:

Each integrated care board and its partner NHS trusts and NHS foundation trusts must exercise their functions with a view to ensuring that, in respect of each financial year

(a) local capital resource use does not exceed the limit specified in a direction by NHS England;

(b) local revenue resource use does not exceed the limit specified in a direction by NHS England

Changes to contracts

- Signed contracts
- Consider IFRS 15
- Variable elements higher risk
- Incomplete spells?

Other continuing matters



Other reminders from 2021/22 audits (1)

- AOB mismatches
- Deferred income / receipts in advance
- Impact of unadjusted errors
- Accumulated depreciation on formal revaluation

Other reminders from 2021/22 audits (2)

- Assets under construction
- Assets not yet in your possession
- Work as a system but account as statutory entity
- Tailoring of templates

Judgements/Estimation Uncertainty


Are of the accounts

Significant Judgment : judgements that have the **most significant effect** on the amounts recognised in the financial statements (IAS1. 122-124)

Estimation uncertainty – Estimates that have a **significant risk** of resulting in a **material adjustment** to the carrying amounts of assets and liabilities within the **next financial year?** (IAS1.125-129)

What your auditor needs

- Judgements - accounting papers referenced to standards, clearly articulated
- Estimates – specific not generic, clear understanding of assumptions
- Evidence of challenging your own management expert
- Evidence of ‘stand back’ review



**Increased
professional
scepticism
and challenge**

Valuation questions

Which assets are deemed specialised and why?

Why is depreciated historic cost equivalent to current value?

Any individual assets that need special attention?

Any impairment triggers?

What information or source data is provided?


Do you understand the movements and why they have occurred?

Which assumptions are used and why? (eg build indices, obsolescence rates)

What alternative assumptions have been rejected?

Any significant changes in assumptions or approach?

Using management experts



Increased
professional
scepticism and
challenge

What can go wrong

- Errors in source data completeness and/or accuracy
- Inappropriate valuation bases
- Inappropriate assumptions
- Errors in accounting

What can help prevent issues

- Clear **instructions** to the expert
- Providing **specific context** to the expert
- Ensuring **completeness and accuracy** of information provided to the expert
- **Reviewing the outputs** from the expert and **challenge** when values are unusual
- **Stand back** review of the accounts

What your auditor needs and why



Changes to auditing Standards

There are significant changes to the following ISA (UK):

- ISA (UK) 315 (Revised July 2020) 'Identifying and Assessing the Risks of Material Misstatement'
- ISA (UK) 240 (Revised May 2021) 'The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements'


The changes will impact the level and nature of audit work for audits of your 22/23 financial statements.

Changes to auditing standards – ISA (UK) 315

Key Elements of ISA (UK) 315


Impact on audit

IT environment	More information required about IT infrastructure and processes – liaison likely to be needed with IT staff
Considering IT risks related to internal controls relevant to the audit.	Additional walkthrough testing of IT general controls that address risks arising from use of IT
Relevant Journal Entry Controls	Additional walkthrough testing of IT general controls relating to journals
Understanding the entity's information system & business process understanding	Potential for additional business processes to require documentation
Control reliance	Potential for increased sample sizes in some areas



**Increased Risk
Assessment
Procedures**

Changes to auditing standards – ISA (UK) 240



Increased
professional
scepticism and
challenge

Key Changes to ISA (UK) 240

Additional audit evidence

Fraud

The design, nature timing and extent of audit procedures performed in support of the audit opinion will **change** due to:

- clarification of the requirements relating to **understanding fraud risk factors**
- additional focus on the **authenticity** of information used as audit evidence
- requirement to consider whether to **involve specialists** including forensics to identify and respond to risks of material misstatements due to fraud
- **additional communications** with management or those charged with governance

Audit report

Specific reporting requires specific additional audit evidence

Changes to audit profession

Increased external regulations - monitoring and scrutiny of quality of audit

High profile corporate failures

Accountability, governance and public confidence

Penalties and fines

Sustainable fees and specialist resources



What we have covered

Changes to the GAM – IFRS 16

Other changes and continuing matters

What your auditor needs and why



Any more questions



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