Audit Committee

6 December 2023

Title:	Fixed Assets – Ownership
Responsible Director:	[redacted], Director of Finance
Author:	[redacted], Head of Financial Accounts

Situation:	The Harrogate and District NHS Foundation Trust (HDFT) in the financial year 2017/18 made the decision to create a subsidiary organisation (private limited company). The subsidiary company was named Harrogate Healthcare Facilities Management Limited (HHFM) and was incorporated on 6 November 2017. HHFM began operationally with effect from 1 March 2018 and became responsible for providing HDFT with a range of services wrapped up in an Operated Healthcare Facility contract between the two organisations. There were a number of drivers around this decision ranging from the improvement to the quality of services, easier recruitment due to being able to offer rates of pay comparable with the private sector and some financial benefits. HDFT was supported in the due diligence process by both Legal and Accounting firms appointed to advise throughout the process. The Legal advisors responsibilities broadly covered support on Employment rights issues, advice around the Lease contract, contract novation and ultimately drafting the Operated Healthcare Facility contract. The Accounting advisors were responsible on advising on the options around ownership of land and buildings, liaising with HMRC for approval of the model adopted and all tax matters.
Background:	There were three options/models tabled by the Accountancy advisors; • Freehold transfer of land and buildings to HHFM. • Leasehold arrangement between HDFT and HHFM. • Licencing option between HDFT and HHFM. All three options could deliver financial benefits to HDFT, however there was a nervousness around the Freehold transfer. The Licencing option was in the advisors view the most likely to be challenged by HMRC. Therefore we proceeded with the Leasehold option. For the Leasehold option to deliver the Financial benefits in terms of VAT savings on capital spend we were advised that all new capital expenditure (land and buildings not equipment) would need to be recognised on the HHFM Balance Sheet. Funded via loans and contract revenue streams. Any capital spend would be included in the Group Balance Sheet but not the HDFT Balance Sheet.

Assessment:	The Group's land and buildings in-line with its Accounting Policies and Accounting Standards are valued annually by the Valuation Office Agency (VOA). Every five years being a "full" valuation, much more detailed with site visits etc. With the years between having a desktop valuation carried out, using Building Indices etc. Receiving a single valuation which incorporates land and buildings for the Harrogate District Hospital site, which is now split across two balance sheets (HDFT and HHFM) is causing numerous practical issues. Then bringing them together for the Group position is another challenging scenario. The Accounting Policies adopted by HHFM are over time deviating from the HDFT/Group policies. For example HHFM now state their Fixed Assets at cost. As a result of this impairments and depreciation consequently vary from the Fixed Asset Register (FAR) values. Another example of a deviation would be HHFM capitalising borrowing costs, this is absolutely permissible under Accounting Standards. However in terms of the Group situation these are eliminated as intercompany transactions. This makes the record keeping on the FAR very complicated to say the least. For clarity the FAR holds the valuation of land and buildings in accordance with the Group Accounting Policies. Adjustments carried out as a result of HHFM Accounting Policies are held on Spreadsheets. Nationally at the inception of HHFM a number of other NHS Foundation Trust were going through the same process. Supported by a range of advisors. This has led to a number of hybrid models coming into existence. We have liaised and shared information with two other Foundation Trusts around the models adopted. Both Trust's that we liaised with have also adopted the Leasehold scenario. However where we differ is that they both own all the land and buildings in the parent organisation rather than the subsidiary. Having read the information shared, they appear to keep the mechanism around this much simpler than our current approach. There is a recharge on a monthly basis from the Subsidiary to the parent organisation. However within the Managed Healthcare Facility contract there is a charging schedule. This schedule includes an "on cost" charge percentage to be added to any capital recharge. Our understanding is that this approach satisfies HMRC in terms of transactions being on an arm's length (allowing VAT reclaim).
Recommendation:	I ask the Committee to consider the contents of this paper, discuss any areas of interest and approve the following recommendations.

	• To move away from the model currently adopted by HDFT and HHFM. • To move towards the model adopted by some other NHS Foundation Trusts (remaining Leasehold). • Seek support from Legal and Accountancy firms to assist in the due diligence required; ensuring the contract is amended appropriately and ensure we are compliant from an HMRC perspective. • To work collaboratively liaising with both HDFT's and HHFM's External Auditors to approve how we might transact change of model/approach. For example is this a disposal of Fixed Assets for HHFM? Doesn't feel like it's an addition to the Group as already included. Addition for HDFT? • Consider setting up a project Team/Group to manage this process. • My final recommendation assuming completion of the above would be for this to be then taken through the Governance processes of both HDFT and HHFM. This is not a recommendation but a comment that this will be a complicated thing to work through and will take both time and resources to complete. For example existing capital loans between the organisations will need extinguishing, and other arrangements will also need unpicking. We may also need to review as part of this the HHFM working capital position, looking at the balance between equity/debt financing.

Freedom of Information:	N/A