

### Financial Review

- The Board achieved all three of their financial performance targets.(see 2.1)
- The Board have prepared a balanced budget for 2005/06 following a rigorous review of developments and risks. (see 2.4)
- Late discovery of an error in the 2004/05 budget process caused difficulties in agreeing the 2005/06 budget. (see 2.2)

### Financial Statements

- Our opinion on the financial statements is qualified in respect of the accounting treatment of the Easter Ross Resource Centre. (see 3.1)
- Our opinion on regularity is unqualified. (see 3.3)
- The budgeting error caused major delays in the preparation of the accounts. (see 3.2)

### Corporate Governance

- Our opinion on the Statement of Internal Control is unqualified. (see 4.1)
- A new "Priorities and Risks Framework" audit planning tool was introduced this year. A summary of our "position statement" report is at 4.3.

### Performance Audit

One study was completed in the year:

- Staff Governance – our report concluded that the self-assessment process had not been as robust as in the previous year, but that collection of monitoring information had improved. (see 5.3)

### Action Plan

Five recommendations are made:-

- The Board should continue to monitor the risks associated with the financial plan for 2005/2006
- The Board should demonstrate the planned efficiencies from the integration of the three NHS Highland bodies and plan towards the achievement of these efficiencies.
- The Board should ensure that appropriate measures are introduced to ensure that errors in the budget and monitoring process do not recur.
- The Board should progress the review of their financial planning process to address the underlying deficit.
- The Board should monitor progress in each of the key risk areas highlighted in the Priorities and Risks Framework report.

### Acknowledgement

We take this opportunity to thank the Board Members and staff of the Board for assisting and co-operating with us during the course of our work.

We also thank the Audit Committee for assisting in the completion of the Action Plan.

*The purpose of the financial review is to consider the general financial standing of the Board by looking back at financial performance in 2004/05 and to look ahead to the future financial position. Our review is aimed at helping Board members understand the financial position of the Board at a particular point in time. It should not be regarded as definitive or comprehensive and the Board should not seek to rely on this summary in isolation.*

### Contents:

- **Financial Objectives 2004/05**
- **Performance against budget 2004/05**
- **Underlying Financial position 2004/05**
- **Financial Plan 2005/06**

**2.1 Financial Objectives 2004/05**

The Board is required to stay within three financial performance targets:

- the Revenue Resource Limit (RRL)
- the Capital Resource Limit (CRL)
- the Cash Requirement

The RRL is the total funding in-year which has been allocated by the Scottish Executive for patient services. The CRL applies to in-year capital expenditure, and is set by the Scottish Executive.

The Cash Requirement is a financing requirement to fund the cash consequences of the ongoing operations and the new capital investment.

The table below summarises the Board's performance and shows that the Board achieved all three targets.

	Target £'000	Outturn £'000	Achievement
To remain within the RRL	302,818	300,980	Yes
To remain within the CRL	5,547	5,335	Yes
To remain within the Cash Requirement	297,866	297,866	Yes

**2.1 Financial Objectives 2004/05 (cont'd)**

**Revenue Resource Limit (RRL)**

The Board is aware that the above was achieved with the use of significant non-recurring resources (see the table at 2.3).

**Capital Resource Limit**

The Capital Resource Limit, as originally advised by the Scottish Executive was £8.1m. Additional allocations of £2.2m were received for various projects during the year. Of this the Board sought and received approval to transfer £1.5m to support the revenue resource limit. These changes revised the allocations to £8.8m.

Slippage in capital programmes caused £3.3m of the allocations to be returned, leaving a final allocation of £5.5m.

These schemes have been carried forward and are included in Capital Plans for 2005/06 and 2006/07.

**Cash Requirements**

This target was met after the agreement of a revised target with the Scottish Executive on 21 July.

## 2.2 Performance against budget

The Board set a budget of £319m in April 2004.

This figure was amended during the year as further developments and actions were funded from SEHD, resulting in a "final" budget of £331m at March 2005.

At the end of April 2005, as work was ongoing to finalise the accounts for the year ended 31 March 2005 and update the financial plans for future years, a significant error was discovered in the 2004/05 budget. Income in respect of Out of Area Treatment (OATS) of £1.4m had been included both as part of the funding allocation from the Scottish Executive and as "other income" within the operating division of the Board. This, together with adverse unpredicted year end costs of £0.75m, and an unexpected write-off on a stock control account of £0.4m, contributed to a reduction in the forecast surplus for the year from £4m to £1.2m.

This had a cumulative effect in the financial plan for 2005/06, as the budget error in respect of the OATS income had been repeated. Taken together with the lower than anticipated carry-forward of surplus from 2004/05 this meant a further £4.2m of savings having to be found for 2005/06.

Clearly this error, and its impact, has overshadowed the Board's achievement of containing expenditure within budget.

The Chairman and Chief Executive of the Board asked the Chairman of the Audit Committee to lead a review of the issues which caused the error, to identify the causes and ensure that appropriate action was put in place to avoid a repetition. The draft report was presented to the June Audit Committee. A further report will be presented to the Board.

## 2.2 Performance against budget (cont'd)

It is clear that a more robust process of checks and reconciliations would have either prevented the errors, or detected them at an earlier stage. Actions have been implemented to prevent these errors recurring.

### Recommendations

***The Board should ensure that appropriate measures are introduced to ensure that errors in the budget and monitoring process do not recur.***

## 2.3 Underlying Financial Position

One of the major challenges in managing the financial position of the Board is having the flexibility to adapt to different national and local initiatives. National initiatives, in particular, are often subject to specific funding ("ring-fenced") which is for a prescribed period.

Some areas of expenditure are effectively fully funded by the SEHD, based on the actual spend (referred to as "non-discretionary"). This primarily relates to elements of Family Health Service (FHS) expenditure.

These are generally referred to as non-recurring, in the sense that they are not part of the core funding, although this type of funding can stretch over two or three financial years, and does occur on an annual basis.

The following table illustrates this by analysing the funding and expenditure for 2004/05. For the purpose of the table we have separately identified the non-recurring income and expenditure which is expected to be available over a longer period than in one financial year (long-term), from "one off" non-recurring items.

### 2.3 Underlying Financial Position (cont'd)

Highland NHS Board	£'000	£'000
Recurring income	328,360	
Recurring expenditure	338,826	
<b>Underlying recurring (deficit)</b>		<b>(10,466)</b>
Non-recurring income (long-term)	2,646	
Non-recurring expenditure (long-term)	6,002	
Balance of non-recurring (long-term)		(3,356)
<b>2004/05 funding gap</b>		<b>(13,822)</b>
Other income sources		
Non-recurring SEHD income	10,600	
Corporate savings programme	5,060	
<b>Total other income</b>		<b>15,660</b>
<b>Financial surplus for 2004/05</b>		<b>1,838</b>

This illustrates that the Board faced a recurring funding gap of £13.8m, and only balanced the books from supplementary allocations from SEHD, and a savings programme.

### 2.4 Financial Plan 2005/06

The anticipated final resource limit revenue allocation for 2005/06 is £332m, an increase of £17m from the final position in 2004/05.

An initial summary financial plan for 2005/06 was submitted to the Board in March 2005. This informed the Board of the initial revenue resource allocation and anticipated that this would be augmented by a £4m underspend from 2004/05, and a transfer from Capital to Revenue of £2m.

However, the Head of Financial Planning highlighted a number of financial pressures for 2005/06 including:-

- Pay uplift – £4.2m
- Full year effect of agenda for change – £6.7m
- Prescribing and hospital drugs – £3m
- GMS Contract - £8.8m
- Waiting Times initiatives - £1.5m

The Head of Financial Planning, at that stage forecast a shortfall of approximately £5m, to be met from a savings programme. This subsequently had to be revised following discovery of the error in the 2004/05 budget, and finalisation of the 2004/05 accounts (see 2.2).

This reliance on non-recurring funding was highlighted to the Board by the Head of Financial Planning in April 2005. Work is underway to develop a revised financial planning model, which seeks to address this issue.

2.4 Financial Plan 2005/06 (cont'd)

Highland NHS Board	£'000	£'000
Recurring income	355,371	
Recurring expenditure	365,020	
<b>Underlying recurring (deficit)</b>		<b>(9,649)</b>
Non-recurring income (long-term)	2,655	
Non-recurring expenditure (long-term)	6,086	
Balance of non-recurring (long-term)		<b>(3,431)</b>
<b>2005/06 funding gap</b>		<b>(13,080)</b>
Other income sources		
Non-recurring SEHD income	5,874	
Corporate savings programme	7,306	
<b>Total other income</b>		<b>13,180</b>
<b>Projected financial surplus/(deficit) for 2005/06</b>		<b>100</b>

2.4 Financial Plan 2005/06 (cont'd)

A further report to the Board in June 2005 confirmed that following the errors discovered in the 2004/05 budget process, further reductions of approximately £3.9m would require to be made to balance the budget for 2005/06. The Director of Finance reported that plans were in place to meet this target. This comprised a further Capital to Revenue transfer of £0.5m, a reduction in the expenditure of £1m and savings of £2.4m.

Of this total of £7.3m of savings £2.3m is considered to be non recurring.

**Recommendation**

- *The Board should continue to monitor the risks associated with the financial plan for 2005/06.*
- *The Board should progress the review of their financial planning process to address the underlying deficit.*

*The respective responsibilities of the Board, and Tenon Audit Limited are summarised in Appendix 2. The purpose of this section of our report is to highlight and explain our formal opinion on the financial statements, and to comment on the main issues arising from our audit of the financial statements.*

### Contents:

- **Audit Opinion**
- **Timetable and Procedures**
- **Regularity Opinion**
- **Issues for this year**
  - **Indexation and Revaluation of Fixed Assets**
  - **Agenda for Change**
  - **Medical and Clinical Negligence**
  - **Prior Year Adjustment**
- **Local Health Council**

### 3.1 Audit Opinion

We have issued a qualified audit opinion and report on the accounts of Highland Health Board for the year ended 31 March 2005.

A copy of our audit report is attached to this report as Appendix I.

In March 2003, as auditors of the Highland Primary Care Trust (HPCT), we were asked for our preliminary view on the proposed accounting treatment of a "PFI" contract to provide a Primary Care Centre at Easter Ross. The principal source of guidance on the accounting treatment of PFI transactions is Financial Reporting Standard 5 – "Reporting the Substance of Transactions". Guidance on the application of this to PFI deals is contained in an appendix to the FRS by way of "application note G", which deals specifically with PFI transactions. In the Public Sector this is supplemented by "Treasury Taskforce Technical note 1", which offers practical guidance on specific areas of the application note to FRS5.

The Trust's proposal, based on advice from their financial advisors to the project, was to treat the transaction as similar to an operating lease, in that the asset, and the related liability, would not appear on the Trust's balance sheet. The basis for this, was to identify and where possible quantify, where the relative risks and rewards of ownership of the asset primarily lay. This followed the appropriate guidance referred to above, principally the Treasury Taskforce Technical Note 1.

After a lengthy process of review of evidence, meetings and discussions, we issued our report in July 2003.

### 3.1 Audit Opinion (cont'd)

An extract from our report appears below:

*We do not consider that this represents a conclusive argument in favour of the proposed accounting treatment.*

#### **Unavailability Risk**

*The single largest item pointing to an off balance sheet treatment in AB Consulting's analysis is unavailability risk. Blueprint Audit noted that the assumptions underpinning estimates in this area are unsupported by any independent data and are entirely a matter of judgement. We consider that use should have been made of the experience of Highland Primary Care NHS Trust's existing PFI project at New Craigs, to inform this risk assessment.*

*We have reservations concerning the outcome of the risk analysis because of the uncertainty underpinning the key assumptions and the lack of statistical data to support the risk estimates.*

*References in FRS 5 Application Note F24 and F44, indicate that demand risk and residual value risk, where they are significant, will give clear evidence of who should record an asset of the property. Both of the risks remain with the Trust, although the Trust contends that they are not significant.*

*Given these reservations concerning the outcome of the risk analysis and that the risk analysis adjusted spread of risk outcome (above) is not in our view compellingly persuasive, the principles of prudence and transparency would support treating the property as an asset of the Trust and therefore recording this on the Trust's balance sheet.*



### 3.1 Audit Opinion (cont'd)

*However, we understand that Robertson Health (Easter Ross) Ltd has indicated that it intends to account for the property as an asset on its balance sheet, providing additional assurance that the property can be seen as off balance sheet from Highland Primary Care NHS Trust's viewpoint. In our view this is a key factor in shifting the balance in favour of the Trust's proposed accounting treatment.*

In August 2003 the NHS Highland Board approved the business case for the provision of the Primary Care Centre. The contract was signed in November 2003, and the facility was opened in February 2005. The 2004/05 accounts are therefore the first accounts that reflect the concluded transaction.

When reviewing the final contract and related documentation to update our assessment of the accounting treatment, we discovered that, contrary to previous written assurances from them, the operating company had decided, also on the basis of FRS5, that the asset should not appear on their balance sheet, as "substantially all of the risks and rewards of ownership" had been transferred to the Highland Primary Care NHS Trust.

The Board did not place any reliance on the proposed accounting treatment by Robertson Health (Easter Ross) Ltd, and have therefore not altered their view.

Given this reversal of what we considered to be a key factor in our original view of the Board's accounting treatment, we have now concluded that there was insufficient evidence to support that accounting treatment and have qualified our opinion on the accounts.

### 3.2 Timetable and Procedures

The deadline for submission of audited accounts of the Board to the Scottish Executive Health Department (SEHD) is 31 July.

The deadline for the submission of the previous NHS Highland Trust accounts was 30 June. The Board took the view, some time ago, to work towards a 30 June target for the preparation, and audit of their accounts. In discussions we pointed to the risks of not being able to achieve that in the first year of the new organisation; with movement of key staff; a new ledger; and a new accounts manual. However, the Board were confident of meeting their timescale for preparation of accounts by 9 May. We agreed to this accelerated deadline and prepared our plans accordingly.

However, the Board's timetable was significantly disrupted by staff being diverted to investigate the budget error referred to at 2.2. As a result the first incomplete draft of accounts was not received until 24 May. The first complete set of draft accounts was received on 6 June. This in turn disrupted our own plans.

The first draft of the published accounts including all narrative statements, was received on 19 July 2005.

### 3.2 Timetable and Procedures (cont'd)

Our audit was substantially completed by 22 July and a closedown meeting was held with the Director of Finance on 25 July.

A copy of the final version of the summarisation spreadsheet was received by us on 28 July 2005.

The accounts were approved by the Audit Committee and NHS Board on 27 July. Our audit was formally concluded on 29 July, within the SEHD deadline.

### 3.3 Regularity Opinion

The Public Finance and Accountability (Scotland) Act 2000 requires us to give an opinion on the regularity of expenditure and receipts.

Auditors are now required to confirm that "in all material respects, expenditure and income shown in the accounts were incurred or applied in accordance with applicable enactments and guidance issued by the Scottish Ministers".

To meet this requirement we need to:-

- Have a sufficient understanding of such laws, regulations and guidance as are applicable.
- Test compliance with such provisions.
- Review the audited body's arrangements for implementing new legislation or statutory requirements which may have significant financial consequences.
- Consider the applicability to the audited body of relevant national issues which may have financial consequences.
- Consider transactions that are unusual or of questionable legality and which may have significant financial implications.

We discharge this responsibility by reviewing the Board's system for ensuring that guidance issued by Scottish Ministers is appropriately acted upon, and where necessary, amendments to Standing Orders, Financial Instructions and procedures are introduced. We were satisfied that this system was appropriate. We test for compliance against Standing Orders and Financial Instructions and procedures as part of our annual audit work.

### 3.3 Regularity Opinion (cont'd)

Difficulties in respect of regularity have been experienced in the past, principally relating to Primary Care Income and Expenditure.

Guidance on verification of aspects of the new General Medical Services (GMS) contract was not issued until March 2005. Informal guidance was issued in October 2004 and the Board followed this in their practice visits. As a result we have issued an unqualified opinion on regularity.

### 3.4 Issues for this year

#### *Indexation and Revaluation of Fixed Assets*

The complete NHS Estate in Scotland was revalued at 31 March 2004.

In order to avoid the difficulties experienced last year the SEHD have decided on a rolling five year programme of revaluations. This means that 20% of the NHS Estate in Scotland will be revalued each year. Indices from this will be used to estimate the effect each year on the remaining 80%.

This produced an increase of £13.5m at 31 March 2005,.

#### *Agenda for Change*

The new terms and conditions package for most NHS Scotland employees (known as 'Agenda for Change') was ratified by the Staff Council in November 2004. 'Agenda for Change' relates to all employees other than medical and dental practitioners and executive/senior managers covered by other arrangements.

The new terms and conditions began from 1 December 2004, with an effective date of 1 October 2004.

The process of introducing the new terms and conditions includes matching jobs into an appropriate placing on the new pay scale. In order to achieve this, a job description for the existing role has to be agreed and 'matched' into one of the new job profiles. This is a lengthy process and is still ongoing.

**3.4 Issues for this year (cont'd)**

***Agenda for Change (cont'd)***

The Board have estimated a cost of £1.8m for the period 1 October 2004 to 31 March 2005 and this figure is included in the accounts.

***Medical and Clinical Negligence***

From 1 April 2000, new financial risk sharing arrangements for clinical negligence awards and certain non-clinical risk categories came into operation – Clinical Negligence and Other Risks (Non-Clinical) Indemnity Scheme (CNORIS). In essence, the financial risks are managed within a single pool, with separate arrangements for incidents occurring or reported from 1 April 2000, and for pre 1 April 2000 losses.

The provision in the accounts for Medical and Clinical Negligence claims has been reduced from £0.859m to £0.6m.

A contingent liability of £1.2m is disclosed in respect of claims lodged, which the Board consider requires no provision. This is based on advice from the Central Legal Office.

**3.4 Issues for this year (cont'd)**

***Prior Year Adjustment***

Following the merger of the three separate NHS bodies in the Highlands into one, the comparative year's figures for the accounts for the year ended 31 March 2005 have had to be produced from an amalgamation of the three previous bodies accounts. This involves eliminating the inter NHS body transactions and have resulted in a prior year adjustment as disclosed in Note 27 to the accounts.

In the year ended 31 March 2005, the new Primary Care Resource Centre at Easter Ross opened and was brought into use for the first time. Costs incurred in setting up the PFI agreement and in decanting and relocating patients during the construction process had been charged to assets under construction in the two years ended 31 March 2004. However, the Board considered that the property did not represent an asset of the Board and that the transactions should be accounted for as an operating lease, meaning that the property would not be reflected in their balance sheet. This meant that the costs incurred, which had totalled just over £1m, could not be shown as an asset in the balance sheet. A prior year adjustment was therefore necessary to remove these costs from fixed assets and transfer them to long term pre-payments. The intention is that these costs be written off over the period of the lease (i.e. 25 years).

### 3.4 Issues for this year (cont'd)

However, these costs include principally:

- Professional Fees paid to advisers of the PFI project (approximately £0.5m)
- Construction and decanting costs incurred relocating patients during the construction phase of the project (approximately £0.35m)
- In-house salaries (approximately £0.09m)

FRS5 Application Note G provides for a situation where contributions to a PFI Project which reduce the rental can be treated as a pre-payment.

It could be argued that the construction and decanting costs, if not incurred by the Board, would have been incurred by the operator and re-charged to the Board through the rental mechanism. In this case it seems appropriate to account for this as a prepayment.

However, in our view, the same argument cannot be put for professional fees and in-house salaries. Accounting guidance (UITF24) indicates that "start-up costs" should be written off in the accounting period in which they are incurred. The Board do not share this view and have included the total costs incurred, including professional fees and in-house salaries as a pre-payment.

### 3.5 Local Health Council

The Accounts of the Highland Health Council are included as note 8 of the Highland Health Board Accounts and show total expenditure of £178,000. We are required to attach a separate audit certificate on these accounts. There are no qualifications to our opinion.

*Corporate Governance is concerned with structures and processes for decision making, accountability, control and behaviour at the upper levels of the organisation. The respective responsibilities of Highland Health Board and Tenon Audit are summarised in Appendix 2.*

*This section of our report comments on the main aspects of our work, and highlights particular issues which arose.*

### **Contents:**

- **Statement of Directors' Responsibility in respect of Internal Control**
- **New Organisation**
- **Priorities and Risks Framework**
- **Primary Care Income and Expenditure**
- **Internal Audit**
- **Management Letters**
- **Other Governance responsibilities**

**4.1 Statement of Directors' Responsibility in Respect of Internal Control**

Scottish Executive Health Department requirements in respect of this statement require a comprehensive and structured annual review of internal controls. This requires the Board to:

- Acknowledge their responsibility for ensuring that an effective system of Internal Control is maintained and operated
- State the main components of the system of Internal Control
- Review the effectiveness of the system
- Detail action taken or proposals to correct weaknesses.

The overall system of internal control consists of the following components:

- Financial
- Operational
- Compliance
- Clinical Governance

This statement and guidance is based on the outcome of the Turnbull Report on Corporate Governance (Internal Control: Guidance for Directors on the Combined Code). The Turnbull Report states that a sound system of internal control *"depends on a thorough investigation on the nature and extent of the risks to which the company is exposed"*. It goes on to say that the purpose of internal control *"is to help manage and control risk, rather than to eliminate it"*.

**4.1 Statement of Directors' Responsibility in Respect of Internal Control (cont'd)**

Risk Assessment and Management has therefore become a critical element of planning, managing and control.

In the period of integration the existing Risk Management arrangements for the three organisations continued at operational level, although there was a lack of overall reporting as the Risk Management Groups did not continue. Internal Audit reported on this in December 2004. Following this a Risk Management Workshop was held, a combined Risk Register prepared, and a Board Risk Group established.

As auditors of the Board, our role is to review the statement for:

- Compliance with Scottish Executive Health Department directions (in HDL(2002)11) and the Code of Audit Practice
- Consistency with our findings from our normal audit work

We are required to provide an opinion on the statement within our Audit Report.

Following discussion with the Director of Finance, we were able to issue an unqualified opinion, a copy of which is attached to this report in Appendix 1.

### 4.2 New Organisation

On 31 March 2004 the two Highland NHS Trusts were dissolved and integrated with Highland Health Board with effect from 1 April 2005. A single operating division was established entitled Direct Health Services. A Direct Health Services Committee was established and met during the year.

Beneath the Direct Health Services were three area Community Health Partnership (CHPs) and one Specialist Services Unit (SSU) centred on the Raigmore Hospital site.

A scheme of establishment for the CHPs was approved in December 2004 and CHPs became fully operational from 1 April 2005.

We reported last year on our concerns that planned efficiencies from the integration of non-clinical support services had not been demonstrated.

We made a recommendation that this should be undertaken and the Board agreed that an exercise would be carried out comparing the old and new structures by September 2004.

Savings of £0.334m were reported for 2004/05 (against a target of £0.349m), and further savings of £0.612m have been targeted for 2005/06, but no full formal review has been performed.

This agreed action, therefore, has not been implemented. We have therefore repeated this recommendation in the Action Plan on page 27.

### 4.3 Priorities and Risks Framework

#### *Introduction*

The Priorities and Risks Framework "PRF" is a national tool, produced by Audit Scotland, for Auditors to use when planning audits of NHS bodies in Scotland. This tool was piloted in 2003/04 at a number of sites then refined and issued to all auditors in November 2004 for use on the 2004/05 audit.

The PRF is a comprehensive document identifying approximately seventy risks and a similar number of audit issues over a range of eight topics. The PRF will be refined and revised and used to plan future audits commencing 2005/06.

#### *Audit Approach*

We met with the Chief Executive and the Director of Finance, to discuss the full PRF document and obtain senior management's view of the key risks and issues. We also sought their assessment of where Highland Health Board stood in relation to the issues, recognising that these were in the main, emerging issues and it was not therefore expected that completed action would be in place in all cases.

We also reviewed a range of evidence and supporting documentation in order to assist in our own assessment. For 2004/05 we considered that it would make best use of the tool to identify the key risks for Highland Health Board from the document and agree with the senior management team a position statement in respect of those risks which will enable future monitoring. A commentary on each of the eight key themes appears overleaf.



4.3 Priorities and Risks Framework (cont'd)	
Priorities and Risks Framework (PRF)	Commentary
Governance	A Governance structure for the integrated organisation has been in operation throughout the year although remits were not formally approved by the Board. Roles and responsibilities continue to evolve and a review of the Governance arrangements in light of this is underway.
Service Sustainability	Work in "underway on preparing a vision document for the Board that will take into account the recent "Kerr" report, and also the proposed merger with part of the Argyll and Clyde board area. This should enable the Board to prepare an overall modernisation strategy, which will in turn inform subsequent
Financial Management	Health plans. Financial management was weakened during the integration period. A financial review is now underway. The Board recognise the further risks involved with the proposed merger with part of the Argyll and Clyde board area.

4.3 Priorities and Risks Framework (cont'd)	
Priorities and Risks Framework (PRF)	Commentary
Performance Management	Corporate objectives were established and performance against key deliverables has been reported to the Board throughout the year. This process has been undergoing development in the first year of the new organisation. The Board has recently approved measureable corporate objectives that should help in this area.
Pay Modernisation	There is an expectation that Pay Modernisation will enable service redesign – the Board's main focus to date has been on successful implementation, which has been achieved within overall budget for the Consultants contract and GMS contract in 2004/05. A review of the potential opportunities for using the new arrangements in modernising services is planned by the Pay Modernisation Board.
Workforce Management	A "baseline" assessment has recently been completed. The Board has a Director of Pay Modernisation and a workforce planning officer has recently been appointed. This should pave the way for the development of workforce planning.

4.3 Priorities and Risks Framework (cont'd)		4.3 Priorities and Risks Framework (cont'd)	
Priorities and Risks Framework (PRF)	Commentary	<p>A report expanding on specific risks in each area has been submitted to the Chief Executive.</p> <p>We would recommend that the Board use this to monitor their progress in each of these areas.</p> <p><b>Recommendation</b></p> <p><b><i>The Board should monitor progress in each of the key risk areas highlighted in the Priorities and Risks Framework report.</i></b></p>	
Joint Futures	Processes in support of this area continue to evolve and the Board has progressed well against SEHD criteria for 2003/04. Outcome focussed performance measures are to be introduced from April 2005.		
Information Management	The e-health strategic plan will be considered by the August Board. Separate allocations for e-health have been ring-fenced in both the revenue and capital plans. Business continuity plans require further development.		

### 4.4 Primary Care Income and Expenditure

The Practitioners Services Division (PSD) of the Common Services Agency (CSA) have responsibility for calculating and making payments to primary care contractors on behalf of Primary Care Trusts (PCTs) and Island Health Boards.

This expenditure, and related income, is also reflected in the accounts of Highland Health Board.

Within Highland Health Board this accounts for approximately £76m of expenditure (approximately 28% of gross operating costs). We have reported in previous years on the difficulties in implementing an effective payment verification procedure in respect of this expenditure, and potential income.

The payment verification protocol, agreed between the PSD and PCTs identifies five different categories of transactions:

- Patient Exemption Income
- General Medical Services
- Ophthalmology Services
- Dental Services
- Pharmacy Services

Work on the payment schemes is largely covered by a combination of reconciling forecast expenditure against actual, following up exception reports produced from analytical review, and detailed checking by PSD staff.

### 4.4 Primary Care Income and Expenditure (cont'd)

A new GP contract was introduced in 2004/05. This was designed to simplify the system for payments, and also provide incentives and rewards for GP practices to provide enhanced levels and quality of service.

A quality payment system was introduced, the Quality and Outcomes Framework (QOF), which relies on a national software system (QMAS) to calculate the quality "score" for each practice on which payments are based.

The Payment Verification Protocol was revised to take account of the new method of payments for GPs but this was not issued to Boards until March 2005, although interim guidance had been issued in October 2004. This protocol states, "The principal method of validating payments made under the QOF is via an annual practice visit". Board staff have carried out practice visits, and this guidance has been followed.

The CSA service auditors (Internal Auditors) produce a comprehensive report on the controls in operation over Primary Care expenditure made on behalf of Boards. However, for 2004/05 this did not include the QMAS system (we understand that this is included in the 2005/06 programme of work).

Assurances in respect of QMAS were obtained through various additional working groups set up to review the probity of the new GMS contract.

### 4.4 Primary Care Income and Expenditure (cont'd)

#### Patient Exemption Fraud / Error

The results of the patient exemption checks for the Highland area for the 12 months ended 31 December 2004 were made available to Directors of Finance in February 2005. Patients can claim exemption from charges in respect of three service streams.

- Dental
- Ophthalmic
- Pharmaceutical

Patient Exemption checks are carried out by the Counter Fraud Service of the CSA. The results of their findings have been reported to the Board analysed by exemption category (44 in all) and by the number of cases investigated, the number where repayment has been made, and the number where the result has been inconclusive and the amounts involved have been written off. The CFS extrapolate the results to project the number and value of fraud claims for the Highland area. This is summarised in the table below. As can be seen, this extrapolation suggests that the loss of income due to fraud or error in the Highland area is in the region of £344,000. (2003 - £512,000).

### 4.4 Primary Care Income and Expenditure (cont'd)

#### Patient Exemption Fraud / Error (cont'd)

This extrapolation in Highland, however, should be viewed with caution. In pharmacy for example there are fifteen different exemption categories and the CFS sample included twelve of these categories. However, in one category (Disabled Persons Tax Credit) forty two cases were examined and twenty were found to be fraudulent. This is therefore extrapolated into an error rate of 47% resulting in an extrapolated error value of £37,500.

This is the highest percentage value in this category in Scotland. In general fraud rates in Highlands are lower than the Scottish average.

Our overall conclusion is that the level of the extrapolated error is not sufficient to cause us to qualify our opinion on regularity of Primary Care income and expenditure.

#### EXTRAPOLATED LOSS OF INCOME

	Highland %	£	All Scotland %	£
Dental	3.4%	68,208	4.3%	2,750,012
Ophthalmic	1.9%	22,550	2.7%	969,137
Pharmaceutical	1.5%	253,397	2.0%	8,987,141
		<b>344,155</b>		<b>12,706,290</b>

### 4.5 Internal Audit

Our relationship with Internal Audit is governed by the Auditing Practices Board Statement SAS 500 "Considering the work of Internal Audit".

It is the responsibility of management to determine the extent of the internal control system required. Internal Audit is an important element of the internal control system.

Whenever possible we use the work of the internal auditor to assist us in our assessment of the effectiveness of the internal controls in the Board's main financial systems. However, to enable us to rely on the work of Internal Audit, we need to be satisfied that the audit work has been properly planned, controlled, performed, recorded and reviewed in accordance with the NHS Internal Audit Manual and SAS 500.

We are pleased to confirm that we were able to derive the planned assurance in the areas examined and that the Internal Audit Service was carried out in accordance with NHS Internal Audit Standards.

In 2004/05 we placed reliance on assignments carried out by Internal Audit in the following areas:-

- In-Year Reporting
- Payroll
- Cash and Bank
- General Ledger and Control Accounts
- Treasury Management
- Creditor Payments
- Debtors

### 4.6 Management Letters

It is our practice to send interim management letters to the Board's management during the audit year which report, principally, on weakness in internal control. Our recommendations have been responded to positively and appropriate action has been taken by the Board. Other matters arising in the later stages of our audit, are consolidated into an annual management letter, which is issued as soon after the conclusion of our audit as possible.

Our first draft interim management letter was submitted to the Board on 28 February 2005, and agreed on 15 March 2005. Our second draft interim management letter was submitted to the Board on 13 May 2005 and was agreed on 22 June 2005.

A further management letter will be issued as part of our final audit.

We expect the Audit Committee to monitor implementation of the Action Plans which form part of the management letters.

#### 4.7 Other Governance responsibilities

##### *Prevention and Detection of Fraud and Irregularities*

The respective responsibilities of the Board and ourselves as auditors as set out in Appendix 2. During the year, we reviewed the Board's overall arrangements and Control Environment and made a recommendation in our Interim Management Letter for improvements.

In overall terms, we are satisfied that these arrangements are adequate.

##### *Legality*

Again, the respective responsibilities of the Board and ourselves as auditors are set out in Appendix 2.

Our review of the Board's transactions and arrangements has revealed no areas of concern.

##### *Standards of Conduct, Integrity and Openness*

We reviewed the Board arrangements in 2004/05 which included:

- Complaints procedures
- Openness
- Freedom of Information (Scotland) Act 2002

We are satisfied that these arrangements are satisfactory.

#### 4.7 Other Governance responsibilities (cont'd)

##### *Financial Position*

An overall financial strategy and long-term plan is approved for NHS Highland and the Board agrees its annual revenue budget and Capital Programme within this framework. We report on the error that was made in the 2004/05 budget process at section 2.2.

Regular monitoring reports are submitted to the Board, which reflect actual expenditure to date; revisions to the original plan to take account of changes during the year; and the projected year-end position.

Except for the error referred to at section 2.2 we are satisfied that these arrangements are generally satisfactory.

*The wider dimension of the public sector audit requires that the audit process gives consideration to the way in which the Board secures economy, efficiency and effectiveness in its use of resources. These terms are frequently referred to under the generic term Value for Money. Achievement of Value for Money depends on the existence of sound management arrangements, including procedures for planning, appraisal, authorisation and control, accountability and evaluation of the use of resources.*

*The Public Finance and Accountability (Scotland) Act 2000 gives the Auditor General the right to initiate examinations into the economy, efficiency and effectiveness in the use of resources.*

### Contents:

- Introduction
- 2004/05 Performance Audit Programme
- Staff Governance

### 5.1 Introduction

To comply with our requirements under the Code of Audit Practice we have reviewed the effectiveness of management arrangements at the Board over a range of activities. The aim of this exercise is to ensure that the Board has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. Many of these arrangements can also be described as governance arrangements. We comment on Corporate Governance arrangements in section four of this report.

In general terms we were able to conclude that the Board has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources although we have made recommendations as appropriate where we considered procedures could be improved.

### 5.2 2004/05 Performance Audit Programme

As part of his statutory responsibilities the Auditor General will procure through Audit Scotland examinations of the use of resources and publish reports or guidance. These performance audit reviews promote good management practice and the best use of public money in service delivery. Depending on the nature of the review this work may be carried out by us, as external auditor.

Each National Health Study Report is now laid before the Audit Committee of the Scottish Parliament. This changed environment in which performance audit is now conducted has raised the profile of Health Studies considerably.

The strategy for reporting on Health Performance Audit is:

- to establish a baseline report with data and key performance indicators for tracking change
- after 18-24 months, a national follow-up study will be conducted which will name individual bodies (i.e. the "Name and Shame" policy).

It is essential therefore that when data is being collected for performance audit studies, it is based on high quality data and a consistent standard has been applied in collecting evidence. We have agreed the factual content of our reports with you.



### 5.2 2004/05 Performance Audit Programme (cont'd)

These national reports undergo a lengthy clearance procedure at national level, and are required to be submitted to the Audit Committee in accordance with the agreed timescale. Local reports form the main source of the national reports. It is particularly important, therefore, that an agreed local report is delivered within the agreed timescale.

This year, a number of studies have been conducted nationally with no local audit involvement. These include:

- Using medicines in hospital
- Review of colorectal cancer services
- Whole systems approach to discharge
- Review of bowel cancer services

Audit Scotland also design a number of performance audit studies which are conducted across Boards nationally by the local auditors. This year the only study which fell into that category was Staff Governance.

Although these studies are organised nationally it is important, in our view, that they are tailored to your Board's specific needs. To this end we develop a project brief for each study which lays out terms of reference and which is discussed with management before the studies are undertaken.

### 5.3 Staff Governance

The NHS in Scotland Staff Governance Standard was launched in 2002. It introduced the third component of governance, combining with financial and clinical governance to complete the governance framework within which NHS Boards and Special Health Boards are required to operate.

The aim was to raise the profile of people management in the NHS in Scotland, and improve accountability by putting the spotlight on how staff are managed and how they feel they are managed in the largest employing organisation in Scotland.

This involved audited bodies reviewing their own HR practice to ensure that it met the requirements of the standard. The output from the original self-assessment process was an agreed, credible action plan. This year's study revisited the action plan and validated the actions taken to date. It also reviewed the current year's self assessment process and actions identified for the 2004/05 action plan. There was also a requirement to provide Audit Scotland with various sets of Mandatory Statistical Information (MSI) for benchmarking purposes.

Our assessment indicated that:

- Last year's action plan is being delivered in part.
- These actions, where completed, are resulting in the desired outcomes.
- This year's self assessment process was not robust. However, following review of the SAAT by the Staff Governance sub-group, the assessment was supported by the evidence.
- The SAAT Area Summary Action Plan is credible and owned.
- The specified statistics are not all available for the period, but those that are have been produced in accordance with SEHD instructions.

<p><b>5.3 Staff Governance (cont'd)</b></p> <p>The information required for the six sets of MSI was not collected on a consistent basis throughout NHS Highland, and difficulties were experienced in providing the information for the time periods requested. However, improvements had been made in this area from the previous year.</p> <p>The local report was issued on 31 March 2005.</p>	
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Para Ref	Recommendation	Responsible Officer	Agreed Action	Timescale
2.3	The Board should ensure that appropriate measures are introduced to ensure that errors in the budget and monitoring process do not recur.	Director of Finance	Assurances on budgets and ledger monitoring provided and system introduced.	July 2005
2.4	The Board should continue to monitor the risks associated with the financial plan for 2005/2006.	Head of Area Accounting	Monthly Monitoring of expenditure and forecasting will identify risk areas within the overall financial plan for the year. Reporting monthly to the Board.	Ongoing
Nov. 2005	The Board should progress the review of their financial planning process to address the underlying deficit.	Head of Financial Planning	Review of the financial planning process for 2006/07 will be developed and take account of the underlying deficit.	
4.2	The Board should demonstrate the planned efficiencies from the integration of the three NHS Highland bodies and plan towards the achievement of these efficiencies.	Head of Financial Management	Formal Review to report to Audit Committee. Monitoring of achievement of the planned savings from integration of the NHS bodies to be reported, including achievement of the revised CRS targets for each department reporting monthly to the Board.	
4.3 Quarterly	The Board should monitor progress in each of the key risk areas highlighted in the Priorities and Risks Framework report.	Director of Finance	Progress to be monitored at the Risk Steering group and reported to the Audit Committee.	

**Independent Auditors' Report to the members of Highland Health Board, the Scottish Parliament and the Auditor General for Scotland**

We have audited the financial statements on pages 16 to 37 and 39 to 58 under the National Health Service (Scotland) Act 1978. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain fixed assets, and in accordance with the accounting policies set out on pages 22 to 27.

This report is made solely to the parties to whom it is addressed in accordance with the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice approved by the Auditor General for Scotland and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by Audit Scotland, dated July 2001.

**Respective responsibilities of the Board, Accountable Officer and Auditor**

As described on pages 9 and 10 the Board and the Accountable Officer of the Highland Health Board are responsible for the preparation of the financial statements in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder. The Accountable Officer is also responsible for ensuring the regularity of expenditure and income. The Board and Accountable Officer are also responsible for the preparation of the Directors' Foreword. Our responsibilities, as independent auditors, are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice approved by the Auditor General for Scotland, and guided by the auditing profession's ethical guidance.

We report our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder and whether, in all material respects, the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers. We also report if, in our opinion, the NHS Board has not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

We review whether the statement on pages 11 and 12 complies with the guidance issued by the Scottish Executive Health Department 'Corporate governance: Statement on Internal Control'. We report if, in our opinion, the statement does not comply with the guidance or if it is misleading or inconsistent with other information we are aware of from our audit. We are not required to consider whether the statement covers all risks and controls, or form an opinion on the effectiveness of the NHS Board's corporate governance procedures or its risk and control procedures.

We read the other information published with the financial statements and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

**Basis of audit opinions**

We conducted our audit in accordance with the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice, which requires compliance with relevant United Kingdom Auditing Standards issued by the Auditing Practices Board.

An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of expenditure and income shown in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Board of the Highland Health Board and the Accountable Officer in the preparation of the financial statements and of whether the accounting policies are appropriate to the NHS Board's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error, and that, in all material respects, the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers. As is disclosed in note 26 to the accounts, the Board have entered into an agreement with a contractor to provide and service a Primary Care Resource centre in Invergordon. The Board have accounted for the property concerned as an operating lease and therefore there is no related asset or liability included on the Balance Sheet. In our opinion, the Board should have accounted for this asset as a finance lease and included a fixed asset and a related liability on the Balance Sheet. Had the Board adopted this treatment it would have increased the fixed assets by £8.8m and long-term liabilities by a similar amount.

In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

**Opinions**

*Financial statements*

Except for the omission of the fixed asset and related liability referred to above, in our opinion, the financial statements give a true and fair view of the state of affairs of the Highland Health Board as at 31 March 2005 and of its net operating cost, total recognised gains and losses and cash flows for the year then ended and have been properly prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder.

*Regularity*

In our opinion, in all material respects, the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

Tenon Audit Limited  
10 Ardross Street  
Inverness

July 2005

### Risk Assessment

#### *The Board's Responsibility*

It is the responsibility of the Board to identify and address its operational and financial risks and to develop and implement proper arrangements to manage them, including adequate and effective systems of Internal Control.

This includes:

- Completion of a Statement on Internal Control (see 4.1)
- Management of exposure to Medical and Clinical negligence claims (see 3.4)
- Maintenance of systems of internal control

#### *The Role of Tenon Audit Limited*

In planning our audit, we consider and assess your risk management arrangements as part of our assessment of audit risk. This helps us to tailor our audit plans so that they are both appropriate to your circumstances and directed to the areas of greatest risk. We also complete a review of these arrangements as part of our final accounts audit work relating to the Internal Control Statement (see 4.1).

### Systems of Internal Control

#### *The Board's Responsibility*

The Board has a responsibility to develop and implement systems of internal control, including risk management, and systems of financial, operational and compliance controls. For all NHS bodies, it is mandatory to at least annually conduct a review of the effectiveness of the systems of internal control and report publicly that they have done so. This review should take account of the work of Internal Audit and should usually be carried out through the Audit Committee.

Three components of the system of risk management are:

- Timely identification of key business risks
- Consideration of the likelihood of the risks crystallising and the significance of the consequential financial or other impact
- Establishment of priorities for the allocation of resources to control risk and the setting and communicating of key objectives.

The monitoring of controls provide assurance that managers are assessing the existence of risk and the effectiveness of controls over the risks. The internal audit arrangements form an important part of management's monitoring and review of internal control arrangements, and in ensuring that appropriate monitoring or risks and controls takes place.

**Systems of Internal Control (cont'd)**

*The Role of Tenon Audit Limited*

In broad terms the external auditor is expected to assess the internal controls in the Board's main financial systems and report on any significant control weaknesses identified. This does not absolve management from its responsibility for the maintenance of an adequate internal control system.

Through the results of our own testing, and our reliance on areas examined by Internal Audit, we have concluded that the fundamental key financial systems of the Board are generally operating satisfactorily.

We have made suggestions for improvements to procedures where appropriate, in management letters (see section 4.6).

The systems reviewed were as follows:

- Control Environment
- Regularity
- Fraud and Corruption Procedures
- In-Year Reporting (IA)
- General Ledger and Control Accounts (IA)
- IT Arrangements
- Cash, Income and Banking Arrangements (IA)
- Accounts Payable (IA)
- Payroll (IA)
- Debtors (IA)
- Code of Practice on Openness
- Freedom of Information (Scotland) Act 2002
- Treasury Management (IA)
- Evaluation of Internal Audit

(IA) indicates where we were able to place reliance on work performed by Internal Audit.



**Prevention and Detection of Fraud and Irregularities**

*The Board's Responsibility*

It is the responsibility of the Board to establish arrangements to prevent and detect fraud and other irregularity. It therefore needs to put in place proper arrangements for:

- Developing, promoting and monitoring compliance with standing orders and financial instructions
- Developing and implementing strategies to prevent and detect fraud and other irregularity
- Receiving and investigating allegations of breaches of proper standards of financial conduct or fraud and irregularity.

*The Role of Tenon Audit Limited*

External audit is required to review the adequacy of the measures taken by the Board, to test compliance, and to draw the attention of management to any weaknesses or omissions.

**Legality**

The responsibility for ensuring the legality of all activities and transactions rests with the Board.

The responsibility of the external auditor is to review the legality of the Board's transactions and to be aware of the requirements of statutory provisions.

**Standards of Conduct, Integrity and Openness**

*The Board's Responsibility*

It is the responsibility of the Board to ensure that its affairs are managed in accordance with proper standards of conduct. It needs therefore to put in place proper arrangements for:

- Implementing and monitoring compliance with appropriate guidance on standards of conduct
- Expressing and promoting appropriate values in standards across the authority
- Developing, promoting and monitoring compliance with Codes of Conduct that advise Members, Officers or Managers of their personal responsibilities and expected standards of behaviour
- Developing, promoting and monitoring compliance with standing orders and financial instructions.

*The Role of Tenon Audit Limited*

It is our role to consider whether the Board has put in place adequate arrangements to maintain and promote proper standards of financial conduct and to prevent and detect corruption. We discharge this duty by reviewing and where appropriate examining evidence that is relevant to these arrangements.

**Financial Position**

*The Board's Responsibility*

It is the responsibility of the Board to conduct its affairs and put in place proper arrangements to ensure that the financial position is soundly based having regard to:

- Financial monitoring and reporting arrangements
- Compliance with statutory financial requirements and achievement of financial targets
- Levels of balances and reserves
- The impact of planned future policies and known or foreseeable future developments

*The Role of Tenon Audit Limited*

It is our role to consider whether the Board has established adequate arrangements. We are also required to have regard to going concern as part of the audit of the financial statements. In carrying out this responsibility we consider:

- Financial performance in the year
- Compliance with statutory financial requirements and financial targets
- Ability to meet known statutory and other financial obligations, actual or contingent
- Responses to known developments which may have an impact on the Board's financial position

**Financial Statements**

It is the responsibility of the Highland Health Board to:

- Ensure the regularity of transactions by putting in place systems of internal control.
- Maintain proper accounting records.
- Prepare financial statements which present a True and Fair view of the state of affairs of the Board and its net operating cost, total recognised gains and losses, and cash flows in accordance with the Accounts Manual.

We are required to give an opinion on:

- whether the accounts present a True and Fair view of the state of affairs of the Board and its net operating cost, total recognised gains and losses, and cash flows for the period.
- whether the accounts have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.
- the regularity of expenditure and income.

In carrying out this responsibility we provide reasonable assurance that, subject to the concept of materiality, the financial statements:

- Are free from material misstatement.
- Comply with the statutory and other requirements applicable.
- Comply with relevant requirements for accounting presentation and disclosure.

### Corporate Governance

Corporate Governance is concerned with structures and processes for decision making, accountability, control and behaviour at the upper levels of the organisation. The three fundamental principles apply:-

- Openness
- Integrity
- Accountability

Highland Health Board has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions, and to monitor the adequacy and effectiveness of these arrangements.

We have a responsibility to review and, where appropriate, report findings on the Board's corporate governance arrangements as they relate to:-

- The Board's review of its systems of internal control including its reporting arrangements.
- The prevention and detection of fraud and irregularity.
- Standards of conduct and arrangements in relation to the prevention and detection of corruption.
- The financial position of the Board.

Our work has focused upon our review of the Board's Risk Management arrangements, systems of internal control, Internal Audit, consideration of the controls to prevent and detect fraud and corruption, and the audit of the final accounts.

In giving an opinion on the accounts our audit strategy requires us to ensure that the fundamental financial systems are adequately covered each year. Whenever possible, to avoid duplication of effort, we seek to rely on the work of Internal Audit.

However, our work cannot cover every financial activity and accounting procedure. We plan and perform our audit to give reasonable assurance that the statements are free from material misstatement and that they comply with statutory and other requirements.

***HIGHLAND HEALTH BOARD***

**YEAR ENDED 31 MARCH 2005  
FINAL REPORT OF THE EXTERNAL AUDITORS  
TO THE MEMBERS OF HIGHLAND HEALTH BOARD AND THE  
AUDITOR GENERAL FOR SCOTLAND**

**JULY 2005**

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# Tenon audit

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*The purpose of this report is to give a summary of our audit activity. It includes details of the more significant matters arising from the audit, sets out the respective responsibilities of Management and external audit, and reports what action has been taken or is necessary by Board members or executive management.*

*Our audit of Highland Health Board for the year ended 31 March 2005 has been carried out in accordance with statutory requirements and follows the practices prescribed by the Code of Audit Practice. The Code of Audit Practice sets out fully the responsibilities of the Board and its officers in relation to financial probity, control, preparation of accounts and the achievement of value for money in the provision of services. We are required under the Code to give an independent assessment of how the Board has discharged its stewardship of public funds. A summary of our responsibilities is contained in Appendix 2.*

*This report is part of a continuing dialogue between the Board and ourselves and is not, therefore, intended to cover every matter which came to our attention. For this reason we do not accept responsibility for any reliance that third parties may place upon it.*

*We have summarised the Key Issues arising from our audit in Section One. In providing the summary, it can be difficult to strike a balance between recognising good performance when achieved and highlighting scope for improvement. The items referred to represent Key Issues for management attention and should not be taken out of the context of the remainder of this report, or the detailed reports covering individual reviews. Our responsibilities are explained in our separate "Audit Responsibilities" document and are summarised in Appendix 2.*

- We invite Highland Health Board to receive this report and consider the recommendations we have made.*
- We would be grateful to receive the Board's response to the issues we have raised.*

Tenon audit

Summary of how we have discharged our audit responsibilities

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Audit Responsibilities	Summary for Members
To give an opinion on: <ul style="list-style-type: none"><li>whether the financial statements present a true and fair view of the financial position of the Board.</li><li>whether the financial statements have been properly prepared in accordance with the National Health Service (Scotland) Act and directions made thereunder.</li></ul>	Our opinion is based on our: <ul style="list-style-type: none"><li>review of certain financial systems;</li><li>year end regularity audit of the Board's financial statements and;</li><li>assessment of Internal Audit and review of their examination of the Board's financial systems.</li></ul> A qualified audit opinion was given on the Board's financial statements. <i>See details at Section 3 &amp; 4</i>
To give an opinion on the regularity of the income and expenditure shown in the accounts.	An unqualified opinion has been given in respect of regularity. <i>See details in Section 3</i>
To review the Statement of Directors Responsibility in respect of Internal Control	We have reviewed information provided by the Board in support of the Statement. Our opinion on the content of the Statement is unqualified.
To consider whether the Board has achieved its financial targets, and draw attention, in our report, to instances where they are not achieved.	All three of the financial targets have been achieved.  <i>See details in Section 2</i>
To review the summarisation spreadsheet package for consistency with the final audited accounts.	We have reviewed the summarisation spreadsheet package, and have issued an unqualified report.  <i>See details in Section 3</i>
To consider and assess the Corporate Governance arrangements of the Board.	We have reviewed the Board's Corporate Governance arrangements and have concluded that they are satisfactory.  <i>See details in Section 4</i>
To review and report on the arrangements to manage performance designed to secure economy, efficiency and effectiveness in the use of resources.	In general the Board's arrangements are satisfactory.  <i>See details in Section 5</i>

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Section	Page
1. Executive Summary	1
2. Financial Review	2
3. Financial Statements	7
4. Corporate Governance	14
5. Performance Audit	23
6. Action Plan	27
Appendices - Audit Report	28
- Our Respective Responsibilities	31