



The State Hospitals Board for Scotland

**Annual report on the 2013/14
audit to the Board and the
Auditor General for Scotland**

June 2014



Scott-Moncrieff
business advisers and accountants



The State Hospitals Board for Scotland

Annual report on the 2013/14 audit to the Board and the Auditor General for Scotland

Executive summary	1
Introduction	3
Financial statements	4
Use of resources and performance	10
Governance	14
Appendix 1 - action plan	17
Appendix 2 - follow up of 2012/13 recommendations	19
Appendix 3 – recommendations from the McGoldrick review	20

Executive summary

Financial statements

The State Hospitals Board for Scotland annual accounts were approved by the Board on 26 June 2014. Our audit of the annual accounts is complete and our independent auditor's report is unqualified.

We received draft annual accounts and supporting papers of a good standard, in line with our agreed audit timetable and document requests. We are pleased to report that the audit process ran smoothly, and our thanks go to the finance team for their assistance with our work.

The annual accounts will be submitted to the Scottish Government and the Auditor General for Scotland prior to the 30 June 2014 deadline.

Use of resources and performance

The Board met all of its key financial targets in 2013/14, reporting an under spend of £2,000 against its revenue resource limit and a saving of £14,000 against its capital resource limit. In order to achieve a balanced outturn position, the Board was required to identify £1.029 million in efficiency savings. £0.114 million of savings were achieved by a base budget exercise, reducing this target to £0.915 million. Overall, the Board achieved savings of £0.933 million in the year. Taken together with the savings achieved by the base budget exercise, the Board exceeded its savings target by £18,000.

The local delivery plan (2014-2019) sets out the financial plan for the five year period commencing 2014/15. The Board has forecast a breakeven position over each of the next five years although this is dependent on the realisation of further planned savings. For 2014/15, £1.081 million of savings will be required.

For the first month of 2014/15, the Board has reported that overtime costs are higher than the previous year and sickness levels remain the highest in the Scottish NHS sector. These factors have contributed to an over spend against budget to date of £200,000. In May 2014, the interim Chief Executive issued a bulletin to staff outlining the current financial position and proposing actions to address it. These include a review of office accommodation and the temporary closure of one of the twelve wards within the Hospital.

The Board has developed a performance management framework and receives reports on organisational performance and finance at every meeting. Finance and performance reports are based around the local delivery plan and its associated targets and measures.

Governance

We have reviewed the Board's corporate governance arrangements, to ensure effective systems are in place for internal control, the prevention and detection of fraud and irregularity, standards of conduct and the prevention and detection of bribery and corruption. Our audit work identified no issues of concern in these areas.

During 2012/13, the Chair of the Board received three letters, each raising a number of concerns over certain aspects of the organisation's operations. In response to these concerns, the Chair commissioned internal audit to carry out three specific reviews, as well as an independent investigation by an external advisor, Professor Jim McGoldrick. The McGoldrick Review considered the outcome of the internal audit reviews as well as the

other allegations made. The findings of the McGoldrick review were released in December 2013. Six recommendations were made, relating to systems and arrangements for financial and other forms of governance. Work is on-going to address the recommendations and Board members and staff have been updated on the progress made to date. We will continue to monitor progress in implementing these recommendations during 2014/15.

Conclusion

This report concludes our audit for 2013/14. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards.

This report has been agreed with the Finance and Performance Director and we would like to thank all management and staff for their co-operation and assistance during our audit.

Scott Moncrieff
June 2014

Introduction

1. This report summarises the findings from our 2013/14 audit of the State Hospitals Board for Scotland ('the Board'). The scope of our audit was set out in our External Audit Plan, which was previously presented to the Audit Committee.
2. The main elements of our audit work in 2013/14 have been:
 - An audit of the financial statements, including a review of the Governance Statement; and
 - A review of governance arrangements, internal controls and financial systems.
3. As part of our audit, we have also made use of the work of other inspection bodies including the Board's internal audit service and Audit Scotland's Public Reporting Group.
4. The Board is responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
5. This report is addressed to members of the Board and to the Auditor General for Scotland and will be published on Audit Scotland's website, www.audit-scotland.gov.uk.

Financial statements

Introduction

6. The annual financial statements are the principal means of accounting for the stewardship of the resources made available to the Board. In this section we summarise the issues arising from our audit of the 2013/14 financial statements.

Overall conclusion

An unqualified audit opinion on the financial statements

7. The annual accounts for the year ended 31 March 2014 were approved by the Board on 26 June 2014. Our independent auditor's report includes:

- an unqualified opinion on the financial statements;
- an unqualified audit opinion on regularity; and
- an unqualified audit opinion on other prescribed matters.

8. We are also satisfied that there are no matters which we are required to report to you by exception.

Good administrative processes were in place

9. We received draft annual accounts and supporting papers of a good standard, in line with our agreed audit timetable. We are pleased to report that the audit process ran smoothly, and our thanks go to the finance team for their assistance with our work.
10. Arrangements are in place to enable the annual accounts to be submitted to the Scottish Government and the Auditor General for Scotland prior to the 30 June 2014 deadline.

Board members' responsibilities

11. It is the responsibility of the Board and the Chief Executive, as Accountable Officer, to prepare the financial statements in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder. This means:
- applying on a consistent basis the accounting policies and standards approved for NHS Scotland by Scottish Ministers;
 - making judgements and estimates that are reasonable and prudent;
 - stating whether applicable accounting standards as set out in the Financial Reporting Manual (FReM) have been followed, subject to any material departures disclosed and explained in the financial statements; and
 - preparing the accounts on a going concern basis unless it is inappropriate to presume that the Board will continue to operate.
12. Board members are responsible for ensuring that proper accounting records are maintained which disclose with reasonable accuracy at any time the financial position of the Board and enable them to

ensure that the accounts comply with the National Health Service (Scotland) Act 1978 and the requirements of Scottish Ministers. They are also responsible for safeguarding the assets of the Board and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditor responsibilities

13. 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. Specifically in relation to the financial statements, we are required to audit them in accordance with International Standards on Auditing (ISAs) and to give an opinion on:
- whether they give a true and fair view of the financial position of the Board and its net operating cost for the year then ended;
 - whether the financial statements, and the part of the Remuneration Report to be audited, have been prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder;
 - whether expenditure and income has been applied and incurred in accordance with guidance from Scottish Ministers;
 - whether the information given in the Directors Report and Strategic Report for the financial year is consistent with the financial statements;
 - whether the Board has kept proper accounting records, or if we have not received all the information and explanations we require for our audit; and
 - whether the Governance Statement complies with the guidance issued by Scottish Ministers and report if 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.

Independence

14. International Standard on Auditing (UK & Ireland) 260, "communication with those charged with governance" requires us to communicate on a timely basis all facts and matters that may have a bearing on our independence. We can confirm that we have complied with the APB's Ethical Standard 1 – Integrity, Objectivity and Independence. In our professional judgement the audit process has been independent and our objectivity has not been compromised.

Key areas of audit focus and significant findings

15. As noted in our External Audit Plan the following audit risk areas were identified as significant matters and therefore considered in detail during our audit fieldwork.

Financial position

The Board was reporting an over spend against budget during 2013/14. A balanced budget had been set and the Board continued to forecast a breakeven position at the year-end.

A contributing factor to the over spend was nursing overtime. Work was on-going to reduce the number of staff working nightshift. The Board expected that should resources be transferred to the day shift there will be a reduction in overtime costs.

Noted in 2013/14 External Audit Plan

16. The Board met all of its key financial targets in 2013/14, reporting an under spend of £2,000 against its revenue resource limit and a saving of £14,000 against its capital resource limit.
17. During our audit we considered the Board's financial position, related budgets and projections to ensure that they are soundly based. Overall, we found that the Board has adequate arrangements in place for financial management and the use of resources. Our findings are reported more fully in the 'use of resources and performance' section of this report.

Outcome of the independent investigation

During 2012/13, the Chair of the Board received three letters, each raising a number of concerns over certain aspects of the organisation's operations. In response to these concerns, the Chair commissioned internal audit to carry out three specific reviews, as well as an independent investigation by an external advisor, Professor Jim McGoldrick, which considered the outcome of the internal audit reviews as well as the other allegations made. The findings of the McGoldrick Review were released in December 2013. Six recommendations were made relating to systems and arrangements for financial and other forms of governance.

In respect of the Board's financial statements, there was a risk that these circumstances are not adequately reflected in the governance statement.

Noted in 2013/14 External Audit Plan

18. We confirmed during our audit that the information presented in the governance statement is consistent with our understanding of the Board. We have made further commentary on the Board's approach to addressing the recommendations from the independent investigation in the 'governance' section of this report.

Governance changes

Over the last year, there have been four new appointments to the Board. An induction programme is in place for all new board members covering the local delivery plan, the strategic objectives of the Board and introductory meetings with senior management.

The Chief Executive has taken up a new role as NHS Director, Health and Justice, on secondment from the State Hospital. An interim Chief Executive has been appointed and arrangements are being put in place to appoint a permanent successor.

There was a risk that these changes are not completely and accurately reflected in the financial statements, for example, within the governance statements, annual report and remuneration report.

Noted in 2013/14 External Audit Plan

19. We confirmed during our audit that the changes noted above have been accurately reflected in the financial statements.

Revenue recognition

Under International Standard on Auditing (UK & Ireland) 240, “The auditor’s responsibilities relating to fraud in an audit of financial statements” there is a presumed risk of fraud in relation to revenue recognition. The presumption is that the Board could adopt accounting policies or recognise income and expenditure transactions in such a way as to lead to a material misstatement in the reported financial position.

Extract from 2013/14 External Audit Plan

20. We have evaluated each material revenue stream, considered the Board’s revenue recognition policy and carried out testing to ensure this is appropriate and has been applied consistently. Satisfactory assurance has been gained in respect of the completeness and occurrence of revenue transactions in the year.

Management override

In any organisation, there exists a risk that management have the ability to process transactions or make adjustments to the financial records outside the normal financial control processes. Such issues could lead to a material misstatement in the financial statements. This is treated as a presumed risk area in accordance with International Standard on Auditing (UK & Ireland) 240, “The auditor’s responsibilities relating to fraud in an audit of financial statements”.

Extract from 2013/14 External Audit Plan

21. We have reviewed the accounting records and did not identify any significant transactions outside the normal financial control processes. We did not identify any evidence of management override. Satisfactory assurance has been gained in respect of the mitigation of this risk.

Audit issues identified during our audit fieldwork

22. During the course of our audit work we noted the following:

NHS Superannuation Scheme

23. The Board participates in the NHS Superannuation Scheme for Scotland (‘the scheme’). The amount charged to the statement of comprehensive net expenditure represents the Board’s contributions payable to the scheme in the year, determined by an actuarial valuation. However the most recently published actuarial valuation was as at 31 March 2004. Given that the scheme ought to be subject to a full actuarial valuation every five years, a more up to date valuation should have been received by now and reflected in the financial statements. The periodic actuarial valuation is essential to determine the adequacy of employer and employee contributions to the scheme.
24. In common with all health boards in Scotland, the information in relation to the scheme is out of date. There is a risk that, as the level of employers contributions have not recently been revised, the current contribution levels may not be sufficient to meet the future commitments of the pension scheme. The NHS Directors of Finance group has requested an updated valuation for the scheme from the Scottish Public Pensions Agency. We endorse this action and encourage the Board to continue with efforts to obtain an updated valuation in time for the 2014/15 annual accounts.

Follow up of prior year audit recommendations

25. As part of our audit we have followed up the recommendation raised in our 2012/13 Annual Report. Implementation of this recommendation was still outstanding at the time of our 2013/14 audit (appendix 2). The Board still has no approved procedures in place for early departure schemes. The Board is currently drafting a Voluntary Severance and Compromise Agreement Policy which is not due to be finalised and approved until later on in 2014.

Audit adjustments

26. We are pleased to report that there were no material adjustments to the draft financial statements that have had an impact on the outturn against the Revenue Resource Limit (RRL). We identified some minor disclosure and presentational adjustments during our audit, which have been reflected in the final set of accounts.
27. We identified two differences during our audit work that the accounts have not been adjusted for. These two differences are not considered to be material to the financial statements, either individually or in aggregate. Through discussion with the Finance and Performance Director the decision was taken not to adjust the annual accounts. These unadjusted items are included in the representation letter and shown in the table below.

Unadjusted differences

No	Narrative	DR £'000	CR £'000
1	Expenditure – 2013/14 movement on accrual	5	
	General Fund – prior year restatement on accrual	28	
	Accruals		33
	<i>Being the recognition of national insurance and pension contributions in the accumulated paid absences accrual</i>		
2	Provisions	14	
	Other income		14
	<i>Being recognition of amounts to be reimbursed in respect of the Board's provisions</i>		
	Net potential impact on net operating costs (decrease)		9

Board representations

28. We have requested that a signed representation letter, covering a number of issues, be presented to us at the date of signing the financial statements. This letter includes the Board's confirmation that the above unadjusted differences are not considered material to the financial statements.

Qualitative aspects of accounting practices and financial reporting

29. During the course of our audit, we consider the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the financial statements. The following observations have been made:

Qualitative aspect considered	Audit conclusion
The appropriateness of the accounting policies used.	We have reviewed the significant accounting policies, which are disclosed in the financial statements, and we consider these to be appropriate to the Board.
The timing of the transactions and the period in which they are recorded.	We did not identify any significant transactions where we had concerns over the timing or the period in which they were recognised.
The appropriateness of the accounting estimates and judgements used.	The accounting estimates and judgements used by management in the preparation of the financial statements are considered appropriate. The principal areas of estimates and judgements have been: property valuations and asset depreciation rates. Where appropriate, the Board has utilised the work of independent experts or industry practice to support the estimates made.
The potential effect on the financial statements of any uncertainties, including significant risks and disclosures such as pending litigation that are required to be disclosed in the financial statements.	All material areas of uncertainty have been appropriately considered in the preparation of the financial statements.
The extent to which the financial statements have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed in the financial statements.	From our testing performed, we identified no unusual transactions in the period.
Apparent misstatements in the directors' report or material inconsistencies with the financial statements.	There has been no misstatement or material inconsistency between the financial statements and the directors' report and strategic report.
Any significant financial statement disclosures to bring to your attention.	There are no significant financial statement disclosures that we consider should be brought to your attention, other than those mentioned in this report. All disclosures made are required by relevant legislation and applicable accounting standards.
Disagreement over any accounting treatment or financial statement disclosure.	There was no disagreement during the course of the audit over any accounting treatment or disclosure.
Difficulties encountered in the audit.	There were no difficulties encountered in the audit.

Use of resources and performance

30. This section of the report sets out the main findings from our review of how the Board manages its key resources in terms of financial performance. Overall, we have found that the Board has adequate arrangements in place for financial management and the use of resources. Our conclusions are based on a review of the Board's financial performance, underlying financial position, financial plans, financial reporting and achievement of savings targets.

The Board's financial performance in 2013/14

The Board has met its key financial targets in the year

31. The Board is required to work within the resource limits and cash requirements set by the Scottish Government Health and Social Care Directorates (SGHSCD). As shown in the table below, the Board met all of its key financial targets in 2013/14.

Performance against key financial targets

Financial Target	Target £'000	Actual £'000	Underspend £'000	Target achieved
Revenue Resource Limit - Core	32,201	32,199	2	Yes
Revenue Resource Limit – Non core	3,029	3,029	-	Yes
Capital Resource Limit	365	351	14	Yes
Cash Requirement	33,000	32,824	176	Yes

(Source: Annual Report and Accounts for the year ended 31 March 2014)

32. The Board reported a £2,000 under-spend against its revenue resource limit (RRL). At the outset the Board forecast a breakeven position for the year. During the year however the Board reported over spends against budget. The most prominent over spends were reported within the General Manager directorate. At the year-end, an over spend of £1.005 million was reported against this directorate. This was offset against under spends reported by other directorates, including the corporate function. Within this function the Board had contingency reserves of approximately £690,000 which were not utilised fully in the year and could be offset against the over spends reported within the General Manager directorate.

Function	Annual Budget £'000	Actual £'000	Variance £'000
Corporate functions	8,660	7,784	876
General manager	22,469	23,474	(1,005)
Medical	1,596	1,510	86
Nursing non-ward	1,077	1,010	67
Security	1,428	1,450	(22)
Total	35,230	35,228	2

(Source: Board 2013/14 management accounts for period 13)

33. Ward nursing costs were approximately £1.136 million over budget in 2013/14. Within this, nursing overtime costs continue to be a significant cost pressure for the Board. Due to the nature of service provided by the Board, nursing shifts are affected by sickness or holiday absences. In periods of high sickness absence there is an increase in nursing overtime. In 2013/14, the Board reported sickness absence levels for 6.19%. This is 1.19% above the national target and an increase of 1.03% from the prior year. A nursing review, led by the General Manager and Nursing Resources Administration Teams, has identified a number of actions to be taken to reduce nursing staff costs. This includes a reduction to the number of night shift staff required and a review of the current skill mix.
34. In order to achieve a balanced outturn position, the Board was required to identify £1.029 million in efficiency savings. £0.114 million of savings were achieved by a base budget exercise, reducing this target to £0.915 million. Overall, the Board achieved £0.933 million in savings in the year. Taken together with the savings achieved by the base budget exercise, the Board exceeded its savings target by £18,000.

Source of savings	LDP target £'000	Revised target £'000	Actual savings £'000	Variance £'000
Hospital savings - recurring				
Workforce	393	278	7	271
Hand back of savings to Scottish Government	50	50	0	50
Non Pay	86	87	499	(412)
Additional savings	-	-	28	(28)
Total recurring savings	529	415	534	(119)
Non recurring savings (vacancy management)	500	500	399	101
Savings as at March 2014	1,029	915	933	(18)

(Source: Finance report as at 31 March 2014)

Capital Resource Limit

35. The Board reported an under spend against its Capital Resource Limit (CRL) of £14,000. The Board expects to be able to carry this forward to 2014/15. Capital resources have reduced to £300,000 in 2014/15. There is no anticipated resource for property in the three year financial plan. This presents a challenge for the Board in terms of implementing its property and asset management strategy, particularly in areas such as information management and technology and security. The next significant capital item will be the planned security fence replacement in 2016/17 (estimated £5 million).

Future financial plans

36. The Board's local delivery plan (2014-2019) sets out its financial plan for the five year period commencing 2014/15. The Board is forecasting a breakeven position over each of the next five years although this is dependent on the realisation of its savings plan. For 2014/15, £1.081 million of savings are to be achieved. Included within this are £200,000 of, as yet, unidentified savings.

37. The Board has identified several financial pressures over the coming year:
- **Workforce skill mix** – due in part to the fall in staff turnover, the Board has not been able to achieve the planned workforce numbers set out in the Full Business Case (hospital redevelopment). The workforce plan is currently under review, to be concluded in 2014.
 - **Unknown service contract costs and increases** – The new hospital became operational in September 2011. Following a complete year of operation in 2012/13, the Board is now in a position to assess and understand the full costs of running the site. This assessment is now underway.
 - **Utility costs** – these continue to rise, giving both a price and usage pressure in 2014/15.
 - **Furniture and equipment replacement costs** - As part of the hospital redevelopment, new furniture and equipment was provided across the hospital. The Board is now expecting to replace some items of furniture and equipment during 2014/15. The Board is expected to perform a full evaluation of the financial impact of this over the next few years. The capital funding allocation is expected to decrease over the next few years, which could impact on the Board's ability to meet the costs of replacing major equipment.
38. The achievement of future financial targets will depend on continuing tight control of expenditure, delivery of a challenging savings plan and may also require some difficult decisions to be taken in areas such as workforce planning. This will be a key area which the Board will have to monitor very closely.

Financial performance in 2014/15

39. For the first month of 2014/15, the Board has reported that overtime costs are higher than the previous year and sickness levels remain the highest in the Scottish NHS sector. These have contributed to an over spend against budget to date of £200,000. In May 2014, the interim Chief Executive issued a bulletin to staff outlining the current financial position and proposing actions to address this. These include a review of office accommodation and the temporary closure of one of the twelve wards within the Hospital. This would reduce bed capacity from a theoretical 144 to 132. There will be no changes to overall staffing levels. This will allow more flexibility in staffing across the remaining eleven wards.
40. In prior years, directorates have been allocated budgets which in total were in excess of the funds available to the Board, with the understanding that, during the year, savings would require to be identified through the finance function and regular budget meetings. This strategy has changed in 2014/15 to ensure that overall budgets are set with the financial allocation and directorates are clear what must be achieved from their individual savings. The savings targets have been reduced to 1.7% for ward nursing, security and some facilities budgets with all other budgets given a target to achieve 4.8% savings.

Performance management framework

41. The Board has developed a performance management framework and receives reports on organisational performance and finance at every meeting. Performance reports are based on the Board's local delivery plan (LDP) and its associated targets and measures.

42. Performance is reported on a 'priority-ordered' exceptions basis with a red, amber and green system in place to identify performance levels. In addition the performance reports set out progress against local delivery plan (LDP) targets. The LDP performance measures are aligned with the ministerial objectives of; Health improvement for people in Scotland; Efficiency/governance improvements; Access more quickly to service; and Treatment appropriate for patient (HEAT). The Board identified 17 key performance indicators in 2013/14. Progress against key performance indicators has been reported by the Board in its Annual Report and Accounts for the year ended 31 March 2014.
43. The Board also receives regular and detailed performance and financial information which facilitates scrutiny and challenge. Key risk factors which may impact on achievement of financial and non-financial outcomes are identified and discussed.

Governance

44. Corporate Governance is concerned with the structures and processes for decision-making, accountability, control and behaviour at the upper levels of organisations. Through the Accountable Officer, the Board is responsible for ensuring the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements.
45. We have found that the Board has appropriate governance arrangements in place. Our work has involved reviewed the Board's arrangements for:
- systems of internal control;
 - the prevention and detection of fraud and irregularity; and
 - standards of conduct and the prevention and detection of bribery and corruption.

Governance arrangements

46. During the year, the Board reviewed the remit and function of committees and working groups. This was in response to concerns over low attendance at certain meetings. It was also acknowledged that a significant number of groups and committees were in existence and the effectiveness of those arrangements was challenged. As part of the review, all directors, heads of service and the general managers were asked to comment on the committees and groups they attended, and comment if the committees and groups remained relevant and integral to the governance and performance management framework for the Board. At a Senior Management Team meeting in March 2014, it was agreed that two committees should be discontinued, with the responsibilities assigned to other committees. The 'Communications Review Group' and the 'Risk and Governance Committee' were agreed to be discontinued.
47. Over the last year, there have been four new appointments to the Board. An induction programme is in place for all new board members covering the local delivery plan, the strategic objectives of the Board and introductory meetings with senior management. All board members are subject to an annual appraisal by the Chair. The Chair is currently exploring training opportunities for board members with other Health bodies.
48. The Committees of the Board undertake an annual self-assessment of their performance and report this to the Board. The Board has recently carried out a self-assessment on its effectiveness. The findings are due to be presented to the Board during the next cycle of committee meetings.

Systems of internal control

49. In line with International Standards on Auditing, we have considered the internal controls in place over the Board's key financial systems. As reported in our interim management report, we identified no significant deficiencies in the operation or design of internal financial controls over the Board's key financial systems. We found the internal financial controls to be well designed and operating effectively.
50. The governance statement included within the Board's 2013/14 annual accounts discloses no material internal control weaknesses. Reference is however made to the letters that the Chair received in

2012/13 raising concerns over the governance of the Board (see below) and the work on-going in response to these. Our audit identified no additional issues which we consider need to be disclosed in the governance statement.

McGoldrick report

51. As noted above, during 2012/13, the Chair of the Board received three letters, each raising a number of concerns over the governance of the Board. In response to these concerns, the Chair commissioned the internal auditors to carry out three specific reviews, as well as an independent investigation by an external advisor, Professor Jim McGoldrick, which considered the outcome of the internal audit reviews as well as the other allegations made.
52. A redacted version of the McGoldrick report was published in December 2013 (the full report was issued in September 2013). The report contains six recommendations that are intended to strengthen the Board's governance arrangements. In February 2014, a board seminar was held at which board members discussed the conclusions and recommendations and discussed what further action would be needed. One such action was to provide an update to staff. In April 2014, a bulletin was issued to staff which set out progress to date on implementing the six recommendations.
53. From review of the minutes from the board seminar and the staff bulletin, it is evident that work has been, and continues to be, carried out to address the recommendations. A summary of this work is included in Appendix 3. We did however note that no formal action plan has been developed, with responsible individuals and timescales, to address the recommendations. Monitoring arrangements should also be agreed to ensure that the actions are on track to be implemented by the agreed timescales.

Action Plan Point 1

Internal audit

54. An effective internal audit service is an important element of the Board's governance arrangements. The Board's internal audit service is provided by KPMG. In accordance with International Standards on Auditing we have considered the function provided by KPMG and have concluded that the service is fit for purpose. To avoid duplication of effort and to ensure an efficient audit process, we have taken cognisance of internal audit work where appropriate and we are grateful to the KPMG internal audit team for their assistance during the course of our audit work.

Prevention and detection of fraud and irregularity

55. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. During the year we have found the Board's arrangements for the prevention and detection of fraud and other irregularities to be adequate.

National Fraud Initiative

56. The National Fraud Initiative (NFI) is a counter-fraud exercise co-ordinated by Audit Scotland working together with a range of Scottish public bodies, external auditors and the Audit Commission to identify fraud and error. We are required to consider the Board's participation in the NFI exercise. In our interim audit we reported that the Board's approach to the most recent NFI exercise (2012/13) was satisfactory.

Standards of conduct and arrangements for the prevention and detection of bribery and corruption

57. We have reviewed the arrangements for adopting and reviewing standing orders, financial instructions and schemes of delegation and complying with national and local codes of conduct. We also considered controls over register of interests. We are pleased to report that our audit identified no significant issues of concern in relation to standards of conduct and the prevention and detection of bribery and corruption. We did note in 2012/13 that some of the Board's existing policies and procedures are out of date and should be refreshed. Work is currently underway by the Board to address this.

Appendix 1 - action plan

Our action plan details the control weakness that we have identified during the course of our audit together with the officers responsible for implementing the recommendations and the implementation dates.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist. Our communication of these matters does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

Grading

The grading structure for our recommendations is as follows:

Grade	Explanation
Grade 5	Very high risk exposure - Major concerns requiring Board attention.
Grade 4	High risk exposure - Material observations requiring management attention.
Grade 3	Moderate risk exposure - Significant observations requiring management attention.
Grade 2	Limited risk exposure - Minor observations requiring management attention
Grade 1	Efficiency / housekeeping point.

Action Plan Point	Issue Identified	Risk and Recommendation	Management Response
1 (para. 53)	<p>McGoldrick recommendations</p> <p>Although it is evident that work is being done to address the recommendations from the McGoldrick review, we noted that no formal action plan has been developed, with responsible individuals and timescales, to address the recommendations. Monitoring arrangements should also be agreed to ensure that the actions are on progress to be implemented by the agreed timescales.</p>	<p>There is a risk that insufficient information is provided to the Board to allow it to monitor and challenge progress made in implementing the recommendations.</p> <p>The Board should develop a formal action plan, which includes the specific actions required to implement each of the recommendations, along with the officer responsible for each action and the timescale for completion.</p> <p>The Board should also ensure that formal monitoring arrangements are in place to allow the Board to monitor and challenge progress in implementing those actions.</p> <p>Risk Rating 3</p>	<p>A report updating progress on each specific recommendation made by Professor McGoldrick will be formally submitted to the private session of the June 2014 Board meeting. Thereafter, progress will be continuously monitored on a formal basis by the same means at future meetings.</p>

Appendix 2 - follow up of 2012/13 recommendations

As part of our audit we have followed up the recommendation raised in our 2012/13 Annual Report. Implementation of this recommendation was still outstanding at the time of our 2013/14 audit.

Issue Identified	Risk and Recommendation	Update
<p>The Board does not currently have a policy in place for early departure schemes.</p> <p>The Board uses compromise agreements to protect the organisation from future legal claims in respect of the termination of employment, severance payment (where applicable) and any potential breaches in confidentiality.</p>	<p>There is a risk that the Board has not complied with the Scottish Public Finance Manual and is not currently following best practice guidelines.</p> <p>The Board should develop a policy for early departures and ensure this is approved by the Board and the Scottish Government and circulated to all staff.</p> <p>We would encourage the Board to review these principles and ensure that they are being complied with.</p> <p>Risk Rating 4</p>	<p>Outstanding</p> <p>The Board still has no approved procedures in place for early departure schemes. The Board is currently drafting a Voluntary Severance and Compromise Agreement Policy which is not due to be finalised and approved until later on in 2014.</p>

Appendix 3 – recommendations from the McGoldrick review

A redacted version of the McGoldrick report was published in December 2013 (the full report was issued in September 2013). The report contains six recommendations that are intended to strengthen the Board's governance arrangements. From review of the minutes of the board seminar and the staff bulletin, it is evident that significant work has been carried out to address the recommendations. The table below summarises our understanding of the actions to be taken or completed by the Board to address the recommendations.

Recommendation as per McGoldrick Review	Action to be taken or completed to date
Recommendation 1 Alongside the review of the human resources records system currently underway following on from the audit recommendations, the Remuneration Committee should also develop a Governance Protocol regarding MHO status	<p>Human resources are carrying out a full review of employee information held to ensure all relevant documentation is in place for all employees.</p> <p>A review of existing long term secondments has been carried out and the Secondment Policy has been revised.</p> <p>A new HR system is currently being implemented.</p> <p>No Governance Protocol on MHO status will be implemented. The Board has confirmed that existing clauses within employment contracts are sufficient.</p> <p>The Remuneration Committee will consider cases where a MHO status is contentious. When a staff member moves from one post to another then any resultant likely impact on MHO status will be confirmed in writing.</p>
Recommendation 2 The Board should urgently examine what further actions it may wish to take to ensure that tighter corporate governance is given greater priority in the Board.	<p>The Chairs of each Governance Committee are considering ways of introducing good practice which they can identify e.g. from own experience or other NHS Boards.</p> <p>A new Code of Corporate Governance has been approved by the Board.</p> <p>The terms of reference for the Remuneration Committee have been extended to encourage the Committee to provide further scrutiny on pay related issues.</p>

Recommendation as per McGoldrick Review	Action to be taken or completed to date
<p>Recommendation 3</p> <p>It is recommended that the Board give serious consideration to the need for any further investigation or action.</p>	<p>This related to one set of personnel issues; the Board has concluded that there is no need for further investigation or action.</p>
<p>Recommendation 4</p> <p>It is recommended that the Board urgently look to set out a corporate development programme to address the Staff Governance and Partnership issues raised in the report.</p>	<p>The Partnership Forum will meet more regularly than was previously the case. The Forum is now engaging with member of the national Partnership Staff Associates team to develop ways of strengthening partnership working.</p> <p>A key issue for the Partnership Forum is how issues raised in the Staff Survey are addressed.</p> <p>The Board has implemented procedures to engage more with staff, this includes the introduction of an 'anonymous mailbox' where staff can raise concerns confidentially.</p> <p>The Board are working alongside ACAS for the preparation of the Partnership Policy and changes to the arrangements in partnership working.</p>
<p>Recommendation 5</p> <p>It is recommended that the Board gives strong and visible leadership and support to the initiatives on the Board's response to NHS Scotland '20:20 vision' and the Boards 'Culture, Values and Behaviours Group'.</p>	<p>The Board set up the <i>Cultures, Values and Behaviours Group</i> to discuss the approach to improving upon the objectives raised in the 2020 Workforce Vision. This Group has met once to date. The Board are currently waiting on the position of Organisation Development Manager being filled before further action is taken.</p> <p>The Board is also looking to develop a set of culture and behavioural values.</p>
<p>Recommendation 6</p> <p>It is recommended that the Board considers existing management structures and arrangements.</p>	<p>The Interim Chief Executive is not planning any changes to management structures.</p>

© Scott-Moncrieff Chartered Accountants 2014. All rights reserved. "Scott-Moncrieff" refers to Scott-Moncrieff Chartered Accountants, a member of Moore Stephens International Limited, a worldwide network of independent firms.

Scott-Moncrieff Chartered Accountants is registered to carry on audit work and regulated for a range of investment business activities by the Institute of Chartered Accountants of Scotland.