

The 2014/15 audit of NHS Highland

Update on 2013/14 financial management issues



Prepared for the Public Audit Committee by the Auditor General for Scotland
Made under section 22 of the Public Finance and Accountability (Scotland) Act 2000

October 2015

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Introduction

1. I have received the audited accounts and the independent auditor's report for NHS Highland for the year ended 31 March 2015. I submit these accounts and the independent auditor's report under section 22(4) of the Public Finance and Accountability (Scotland) Act 2000, together with this report that I have prepared under section 22(3) of the Act.
2. In October 2014, I reported to Parliament about issues relating to financial management at the board and which had been highlighted in the auditor's report for the year ending 31 March 2014.¹ The purpose of this report is to update Parliament on NHS Highland's progress in addressing the issues raised in my report last year. This report also includes information requested by the Public Audit Committee (PAC) in its report on the board's financial management.² My report is based on information provided through the 2014/15 audit of the board and additional work undertaken by the auditor.

Auditor's opinion

3. The auditor gave an unqualified opinion on NHS Highland's financial statements for 2014/15. In his 2014/15 annual audit report, the auditor commented on various actions being taken by the board in the last year to strengthen its financial management arrangements.

Background

4. My report to Parliament on the 2013/14 audit of NHS Highland concluded that there were weaknesses in financial management and reporting to Board members during 2013/14. This led to a request late in the financial year for additional funding from the Scottish Government, known as brokerage. While the amount of brokerage represented a small percentage of the board's total revenue budget (0.3 per cent), the need for brokerage was mainly due to an overspend on the operating costs for Raigmore Hospital. Weaknesses in financial management at the hospital emerged late in the year. Other factors contributing to the need for brokerage were financial pressures in the acute sector from costs associated with hiring agency staff, particularly locum doctors, and meeting national waiting times targets. Throughout most of 2013/14, finance reports to the Board continued to forecast a break-even position at the year-end.³ While these reports highlighted financial difficulties, they did not present sufficiently detailed plans about how these were going to be resolved. In addition, the Board was not formally advised of the need for brokerage until close to the end of the financial year. My report also noted that NHS Highland continued to place a high reliance on non-recurring savings which may not be sustainable in the longer term.

¹ *The 2013/14 audit of NHS Highland: Financial management*, Audit Scotland, October 2014.

² *Report on NHS Highland 2013-14: Financial management*, The Scottish Parliament Public Audit Committee, 17 June 2015.

³ We use the term 'Board' to refer to NHS Highland's board of governance whose members include non-executive and executive directors.

5. After considering my report on the 2013/14 audit of NHS Highland, the PAC carried out an inquiry into the board's financial management and produced its own report in June 2015. The PAC made a number of recommendations for NHS Highland and the Scottish Government. The board and the Scottish Government will respond directly to the PAC on these matters. In its report, the PAC invited me to provide an update on a number of issues by the end of 2015:
- The extent to which NHS Highland uses management reports and performance indicators to reassure itself that Raigmore Hospital has improved the efficiency and effectiveness of its services (paragraph 34 of PAC report). My update is provided at paragraphs 17-20 of this report.
 - The extent to which NHS Highland determines whether the causes of previous overspending at Raigmore Hospital are now being addressed and that robust financial management is now being delivered (paragraph 34). My update is provided at paragraphs 16-20 of this report.
 - The planned annual budget for Raigmore Hospital and the targeted overspend for each of the remaining years of the three-year recovery plan (paragraph 35). My update is provided at paragraph 17 and Exhibit 5 of this report.
 - The action NHS Highland has taken to review the three-year recovery plan for Raigmore Hospital to ensure it remains realistic (paragraph 36). My update is provided at paragraph 17 of this report.
 - The extent to which NHS Highland has used NRAC funding for 2014/15 to support long-term sustainable service redesign (paragraph 114). My update is provided at paragraphs 9 and 10 of this report.

Findings

Financial management

6. NHS Highland had budgeted to break even against its Revenue Resource Limit (RRL) of £624.3 million in 2014/15. It achieved a small surplus of £0.136 million at the year-end (0.02% of its RRL) (Exhibit 1).

Exhibit 1. Financial outturn 2014/15

The board achieved a small surplus of £0.136 million in 2014/15.

	Revenue Resource Limit (RRL) £624.294m	Capital Resource Limit (CRL) £16.243m
Outturn	£624.158m	£16.243m
Surplus	£0.136m	£0.0m

7. In November 2014, NHS Highland developed an in-year financial recovery plan. This detailed how the board expected to address the projected shortfall against its budget and achieve its

planned break-even position at the year-end. The board's Delivering Financial Balance Programme Board monitored progress against the recovery plan.

8. In 2014/15, NHS Highland achieved two key national financial targets, which are to break even against its revenue and capital budgets at the end of the financial year.⁴ It delivered efficiency savings of £22.42 million which was in line with its savings plan. The board achieved 40 per cent of these savings (£9 million) on a recurring basis and 60 per cent (£13.41 million) on a non-recurring basis. The auditor has reported that NHS Highland has struggled to deliver the majority of its savings on a recurring basis for a number of years. This puts pressure on future years' budgets as the board's underlying recurring deficit has to be carried forward and added to the savings requirement for the following year.⁵ During 2014/15, NHS Highland sought to increase the proportion of its recurring savings and achieved an increase of two per cent against the previous year (2013/14: 38%, £6.98 million; 2014/15: 40%, £9 million) (Exhibit 2).

Exhibit 2. Savings achieved, 2011/12 – 2014/15

In 2014/15, the board's proportion of recurring savings grew by two per cent compared to the previous year.

	Total savings £m	Recurring savings £m	Non-recurring savings £m	Underlying recurring deficit £m
2011/12	18.92	8.01	10.91	8.91
2012/13	23.74	9.90	13.84	7.28
2013/14	18.37	6.98	11.39	7.77
2014/15	22.42	9.00	13.41	5.62

9. The Scottish Government uses a formula developed by the National Resource Allocation Committee (NRAC) to allocate funding to territorial NHS boards. The formula has been in place since 2009/10, and the government is aiming for all NHS boards to be within one per cent of their target allocations by 2016/17. NHS Highland has been below its target share and the Scottish Government had planned to provide the board with an increase in funding of £11.5 million in 2015/16 to bring the board closer to its target share. However, the Scottish Government and the board agreed to bring forward £3 million of this allocation to help manage NHS Highland's financial position in 2014/15. The Scottish Government provided this funding in January 2015. This afforded the board the option of not implementing some of the more challenging areas of savings that could have had a more direct impact on patient services.

⁴ The revenue budget is known as the Revenue Resource Limit (RRL) and the capital budget is known as the Capital Resource Limit (CRL). This relates to funding from the Scottish Government.

⁵ An underlying deficit is the difference between recurrent resources and recurrent commitments.

The board reprofiled the targets in its in-year recovery plan following receipt of this additional funding.

10. The board allocated the balance of the additional NRAC funding of £8.5 million in 2015/16 between its two main geographical areas, with £2.1 million allocated to Argyll and Bute and £6.4 million to North Highland. The Argyll and Bute funding helped the board meet its commitment to pay an additional £2 million in 2015/16 to NHS Greater Glasgow and Clyde for the services it provides to NHS Highland patients. In North Highland, £1 million of the additional NRAC funding has been reserved to fund additional capacity including the new deputy directors of operation posts. The board is spending the remaining £5.4 million on a range of programmes and initiatives, most of which (£5 million) relates to adult social care. These programmes and initiatives were agreed in NHS Highland's 2015/16 Local Delivery Plan which was approved by the Board in April 2015.
11. NHS Highland took a number of actions in 2014/15 to improve its financial management arrangements, including:
 - close monitoring of progress on savings trajectories which led to the development of an in-year recovery plan to address the projected shortfall against its 2014/15 budget (see paragraph 7)
 - ongoing monitoring of the savings plans and the recovery plan by the Delivering Financial Balance Programme Board
 - inclusion of a savings table in financial reports showing projections by month, along with actual savings achieved
 - development of a training programme for budget holders at Raigmore Hospital
 - more stringent controls over the use of locums across the operational units (see paragraph 22).
12. During 2014/15, the auditor reviewed the Board's standing financial instructions and standing orders, which are updated annually, and concluded that they provide a clear framework for financial management and are comprehensive and up-to-date. The board's internal auditor also reviewed the content of finance reports to the Board and noted that these now contain more details about the risks involved in achieving savings or reducing the overspend along with a trajectory of savings. The August 2015 finance report to the Board included details on the assumptions applied and risks to achieving forecasts, along with the Director of Finance's view of whether the board can achieve a break-even position at the end of the financial year. The financial reports are now clearer and easier for those without a finance background to understand.
13. Based on his review of the work undertaken by the board during 2014/15, the auditor has concluded that NHS Highland has strengthened its financial management arrangements and scrutiny of financial performance.

Financial sustainability

14. Financial sustainability concerns whether the board has the financial resources to meet the current and future healthcare needs of the communities it serves. NHS Highland has a five-year financial plan covering the period 2015/16 to 2019/20. The plan shows a break-even position in each of these five years. It also draws attention to significant cost pressures, such as staff pay and drugs, and expected demographic pressures. In August 2014, NHS Highland agreed its ten-year strategy, *The Highland Care Strategy: NHS Highland's Improvement and Co-production Plan*, but had still to quantify the financial implications of this plan. NHS Highland is developing a ten-year operational implementation plan to support this strategy and the Board noted the first draft of the operational plan in February 2015.
15. The need to make savings will remain part of the board's approach to financial planning over the next five years. Its five-year financial plan assumes a reduction in the board's reliance on non-recurring savings to an annual level of £3 million by 2016/17 ([Exhibit 3](#)). NHS Highland recognises that service redesign will be essential to deliver on its savings plans and, in the short term, it is focusing on four transformational programmes – adult social care and flow; rural general hospitals; out-of-hours; and transformation of outpatients across Highland. The auditor notes that delivering recurring savings has been a challenge for the board and that it now needs to develop a track record of consistently delivering recurring savings in line with its financial plans.

Exhibit 3. Savings plans for 2015/16 - 2019/20

The board plans to reduce its reliance on non-recurring savings over the next five-year period.

	Total savings £m	Recurring savings £m	Non-recurring savings £m
2015/16	16.044	12.044	4.000
2016/17	23.661	20.661	3.000
2017/18	18.363	15.363	3.000
2018/19	17.243	14.423	3.000
2019/20	16.714	13.714	3.000
Total planned savings over 5- year period	92.205	76.205	16.000

Raigmore Hospital

16. Raigmore Hospital had overspent against its budget in each of the last five years. Management at NHS Highland had rebased the hospital's budget in 2012/13 but weaknesses in budgetary control had contributed to it reporting a £9.65 million overspend in 2013/14 and

the board's need for brokerage from the Scottish Government. While the position improved in 2014/15 with the hospital reducing its budget overspend to £6.9 million, this fell short of the £6 million target and adds pressure to the board's savings target for 2015/16 ([Exhibit 4](#)).

Exhibit 4. Financial position at Raigmore Hospital, 2010/11 – 2014/15

The hospital reduced the overspend against its budget in 2014/15.

	Budget £m	Actual £m	Overspend £m
2010/11	130.0	130.6	0.6
2011/12	130.0	134.8	4.8
2012/13	135.8	137.7	1.9
2013/14	136.2	145.9	9.6
2014/15	138.9	145.8	6.9

17. A three-year recovery plan for Raigmore Hospital, covering 2014/15-2016/17, aims to bring the hospital into financial balance by the end of this period ([Exhibit 5](#)). This projected that the hospital would overspend against its budget in each of the three years (by £6 million, £3 million and £1 million respectively), before delivering a break-even position in 2017/18. There was an overspend on the Year 1 target of £0.9 million and current forecasts for Year 2 (2015/16) show a £2.3 million shortfall on the target position. This was due to more activity across a number of specialties in the hospital. Raigmore's management team is monitoring the position closely and reporting regularly to the Highland Health and Social Care Committee. Although the Raigmore team remains confident that financial balance will be achieved by 2017/18, the auditor considers this will be challenging. The savings programmes outlined at paragraph 19 will be key to the recovery plan being delivered.

Exhibit 5. Planned financial position at Raigmore Hospital, 2014/15 - 2016/17

The hospital's three-year recovery plan aims for financial balance by 2017/18.

	Budget £m	Actual £m	Overspend £m
2014/15	138.9	145.8	6.9
2015/16 (planned)	145.8	150.8 (projected)	5.3 (projected)
2016/17 (planned)	Not available	Not available	1.0 (planned)

Note: The annual budget is prepared at the start of each financial year and so the 2016/17 budget is not available at this time.

18. NHS Highland uses a wide range of performance management reports to monitor the efficiency and quality of the services that it provides. Raigmore's management team meets weekly and considers information on finance, staffing, theatre and bed use, waiting lists and HEAT targets.⁶
19. Raigmore's service managers are tasked with identifying savings and, to facilitate this, the hospital has held process improvement workshops. Topics considered to date include working with GPs to reduce referrals, and redesign of child and adolescent mental health services to reduce the need for hospital intervention.
20. The hospital's performance management arrangements are helping it to analyse how it is delivering services and the causes of its overspending in previous years. For example, it is now getting better information about its theatre utilisation rates through the theatres system and better bed management data from the patient management system. This is enabling the board to be clearer on the reasons for the increase in spending. Action is being taken to deliver further savings through three specific savings programmes for Raigmore on transforming outpatient services, theatre utilisation and unscheduled care.

Temporary staffing

21. My report on the 2013/14 audit of NHS Highland highlighted that the cost of hiring agency staff, mostly locum doctors, had contributed to the board's financial position and its need for brokerage. Using temporary staff provides flexibility in enabling the board to provide cover for vacancies and staff absences. However, this can be expensive and may affect the quality of care provided to patients in terms of a lack of knowledge of the board's systems and processes and in a lack of continuity for patients.
22. In 2014/15, NHS Highland spent £9.859 million on temporary staffing and overtime, an increase of 2.8 per cent compared to 2013/14 (£9.593 million). To strengthen controls around the use of locums, the board's director of operations now approves all requests. This led to a reduction in locum costs at Raigmore Hospital of 31 per cent in the first ten months of

⁶ HEAT targets are national performance targets that are set by the Scottish Government.

2014/15, although locum costs increased across other operational units leading to the overall increase in spending for the board as a whole. The Board approved a workforce plan for 2014/15 in August 2014. This highlighted the ageing workforce within the board which will add to its ongoing difficulty in recruiting staff to remote and rural areas in future years. Whilst controls over locum use have resulted in a reduction in costs, the auditor has commented that recruitment of key medical staff in remote and rural areas continues to be a significant challenge for the board.

23. The auditor's overall conclusion on financial sustainability is that the board's financial position is sustainable in the short term but that this needs to be supported by a more robust longer-term financial plan.

Governance and transparency

24. The auditor reviewed the governance arrangements in place and has concluded that the governance framework is effective. The PAC report commented on the lack of transparency around informal meetings of the Board including board development sessions. Since March 2015, minutes of these informal meetings are now made. An independent review of the Board's governance and committee structure is under way and will be reported to the Board in December 2015. The auditor's overall conclusion is that the board is open and has taken steps to improve transparency during 2014/15.

Performance

25. NHS Highland's performance against national targets and standards is presented to each Board meeting, through an assurance report from the Board's Improvement Committee. This information is presented in the form of a balanced scorecard. Performance against local targets is also included. The Improvement Committee carries out more detailed scrutiny of performance, and reports to this committee are accompanied by a narrative setting out the actions being taken to support the achievement and sustainability of performance against targets. The committee also scrutinises separate reports on waiting times and financial performance. The auditor has concluded that NHS Highland has a well-established performance management framework in place which was supported by good performance monitoring.

Looking forward

26. NHS Highland is predicting a balanced budget in each of the five years from 2015/16 to 2019/20. However, this remains dependent on it achieving significant efficiency savings each year to bridge the gap between available funding and the cost of planned services. NHS Highland continues to rely on non-recurring savings to help it break even although the proportion of this type of savings decreased by two per cent in 2014/15. The board plans to reduce its reliance on non-recurring savings over the next five years. The board's underlying deficit reduced by £2.15 million (22 per cent) in 2014/15.

Conclusion

27. In response to my report on the 2013/14 audit of NHS Highland and the PAC's report of June 2015, the board has put in place a number of measures to strengthen its financial management arrangements, scrutiny of financial performance and transparency. It will be important for the board to continue to build on these improvements given the challenges ahead. Further work is required to develop longer-term financial planning and to reduce reliance on non-recurring savings.
28. The auditor will continue to monitor the board's progress and I will report to the Parliament as necessary.