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# Director introduction

## The key messages in this report

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

I have pleasure in presenting our final report to the Audit Committee for the 2017 audit.

As detailed in our plan presented to the Audit Committee on 28 March 2017, the new Code of Audit Practice, which came into force for the 2016/17 audits, sets out our responsibilities under core audit and wider scope requirements. A reminder of the requirements is set out below.

- *Opinion on the financial statements and regularity*
- *National performance audits and Best Value audits*



- *Opinion on management commentaries, remuneration reports and governance statements*

- *Public reporting and audit findings*
- *Wider scope reporting*

# Director introduction (continued)

## The key messages in this report (continued)

I would like to draw your attention to the key messages of this paper:

### Statutory audit

#### Conclusions from our testing

- The significant risks, as identified in our audit plan, related to:
  - Compliance with expenditure resource limits;
  - Valuation of property assets; and
  - Management override of controls.
- A summary of our work on the significant risks is provided in the dashboard on page 12.
- No material audit adjustments have been identified from our procedures. One immaterial misstatement has been noted in the Appendix to this report.
- Based on the current status of our audit work, we envisage issuing an unmodified audit opinion.

#### Insight

- We have utilised Spotlight, Deloitte's patented analytics tool, to perform analytics on the journal entries posted in the year and insights have been noted for management consideration on page 17.
- We have recommended that each year a review is performed for each Board Member's registered interests to ensure proper disclosure of related party transactions.

#### Status of the audit

- The audit is substantially complete subject to the completion of the following principal matters:
  - Receipt of signed management representation letter; and
  - Our review of events since 31 March 2017.

# Director introduction (continued)

## The key messages in this report (continued)

### Best Practice

#### Overall conclusion

- We have reviewed the annual report with reference to the format and content set out in the Government Financial Reporting Manual (FReM), confirming that the annual report and accounts comprise a performance report, an accountability report (which includes the remuneration and staff report, the governance statement and the parliamentary accountability report) and the financial statements.
- As a new requirement in 2016/17, we are required to provide an opinion on whether:
  - the performance report has been prepared in accordance with the accounts direction;
  - the information given in the governance statement is consistent with the financial statements; and
  - the governance statement has been prepared in accordance with the accounts direction.
- Based on the current status of our audit work, we envisage issuing unmodified opinions on the above.
- In addition to the opinions, we have read the performance report and accountability report (including the governance statement) and confirmed that the information contained within both is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.
- We have also audited the auditable parts of the remuneration and staff report and confirmed that it has been prepared in accordance with the accounts direction.
- We have made a number of recommendations on pages 18 and 19 to align the performance report and accountability report with best practice. None of these recommendations impact on our opinions.

# Director introduction (continued)

## The key messages in this report (continued)

### Adds Value

#### **Financial Sustainability**

NHS Shetland delivered an underspend of £312k in 2016/17 against its Core Revenue Resource Limit. Actual Outturn in the year was £54.8 million. This compares with an underspend in 2015/16 of £396k. NHS Shetland has met its three financial targets in the year.

The 2016/17 Financial Plan included a savings target of £3.713 million, equivalent to 7% of the Board's baseline resource allocation. The savings target was met in the year when including non-recurring savings. Recurring savings achieved in the year was £1.805 million, which is below the original target of £2.311 million.

There are plans to make efficiency savings of £12.6 million over the next 5 years. Historically recurring savings targets have not been met with savings targets being met through non-recurring savings. It is critical NHS Shetland focus on implementing recurring saving schemes to ensure long term financial sustainability. NHS Shetland faces some unique challenges being a small island Board therefore finds it is difficult to make savings. We recognise that a Transformational Change Board has been set up to implement and be held accountable for implementing savings plans. The Change Board needs to be supported by very robust benefits realisation processes, including tools and templates, and programme management methodologies. A supporting people Change Management Strategy will also be critical if the Board is to achieve recurring savings targets.

NHS Shetland has a 3 year Local Delivery Plan (LDP) in place. The LDP focuses on improvement in key areas, is aligned with the strategic direction of the Board and includes a financial plan. It sets out current progress and performance against key NHS targets and details challenges in meeting these targets.

NHS Shetland has a 10 year Capital Programme. This is rolled forward and updated on an annual basis and prepared alongside the revenue budget each year. The LDP includes the expected Capital Resource Limits for the next 3 years and includes specific funded projects and Scottish Government Health and Social Care Directorates (SGHSCD) allocation.

The Board is pro-active in respect of financial planning and is expected to achieve short term financial balance. However to achieve financial balance in the long-term it is crucial recurring savings are identified and implemented (see recommendation on page 40).

# Director introduction (continued)

## The key messages in this report (continued)

### Adds Value

#### **Financial Management**

We have reviewed internal audit reports issued in the year and from our testing throughout the audit we note that NHS Shetland has adequate systems of internal controls in place.

NHS Shetland has a priority based approach to budget setting. Heads of Departments are sent a template detailing continuing funding, they will document where they think cost savings cannot be made and where they think potential savings can be made. The Executive Management Team (EMT) will compare expenditure requirements to anticipated funding and will decide what pressures need funding and then how much savings each Directorate is required to make. The EMT will look at the pressures identified by the Heads of Department.

The budget is updated occasionally throughout the year, to reflect additional funding that has been confirmed by SGHSCD. Forecasting is reasonably accurate in NHS Shetland, evidenced by being marginally underspent in the past two years.

The Finance Team is lead by Colin Marsland (Director of Finance) who has worked for NHS Shetland for 5 years. Colin is supported by Karl Williamson (Head of Finance and Procurement) who has worked for NHS Shetland for 7 years. We are satisfied that they have a strong and in depth understanding of the Board.

NHS Shetland has a Fraud and Corruption Plan, which details the steps to follow in the event of a fraud. They also participate in the NFI. NHS Shetland has appropriate arrangements in place for the prevention and detection of fraud and corruption.

NHS Shetland has historically always met its financial targets and broken even which supports the view that management can effectively forecast and has sound financial management procedures in place.

# Director introduction (continued)

## The key messages in this report (continued)

### Adds Value

#### **Governance and transparency**

NHS Shetland has governance arrangements that are appropriate and operating effectively.

NHS Shetland is transparent in its decision making with reports discussed at Board meetings being made available on-line along with the minutes of the meetings.

The Board meets once every two months to review the performance (both financial and non-financial) of NHS Shetland. From review of the board meeting minutes we note there is scrutiny and challenge by both executive and non-executive members of NHS Shetland.

From our attendance at Audit Committee meetings we note that the meetings were not always well attended, with only two members meeting on several occasions. We would also recommend that the Committee perform an annual review of its effectiveness based on best practice.

Internal audit is outsourced to Scott-Moncrieff. The internal audit plan for the year is agreed by the Audit Committee, and reviewed by the Board, with the aim of providing assurance over the adequacy, efficiency and effectiveness of the local governance, risk management and internal control framework.

Internal Audit concluded that proper arrangements are in place, in the areas they reviewed, to promote value for money, deliver best value and secure regularity and propriety in the administration and operation of the organisation.

We note it can take up to two months from the month end for the Financial Monitoring Report to be reviewed by the Board. We have recommended that the timeline be reviewed to increase the quality and effectiveness of the scrutiny performed.

In the year there has been eight changes to non-executive members and the vice-chair position. There has been no changes in the Executive members.

NHS Shetland has appropriate and transparent governance arrangements. To improve scrutiny and comply with best practice it is recommended that attendance at the Audit Committee is improved and an annual review of its effectiveness is performed.



# Director introduction (continued)

## The key messages in this report (continued)

### Adds Value

#### **Value for money**

A Quality Report is reviewed by the Board every two months which details performance against a number of quality indicators for user satisfaction, treatment time and waiting time targets, some which are set by the Scottish Government and the Board.

Comparing 2016/17 performance to 2015/16 we noted improvement in the performance targets of Treatment and Efficiency and a slight decline in the performance of Health improvement targets. In 2017/18 NHS Shetland is updating its performance management system, to allow a greater focus on outcomes.

NHS Shetland is in a challenging context, where it needs to balance delivery of quality services with ambitious improvement targets and standards whilst also living within the financial realities facing the public sector.

NHS Shetland are focused on improving the quality of the services whilst achieving financial balance. The Board routinely reviews performance and will challenge any changes in results.

**Pat Kenny**  
**Audit Director**

# Responsibilities of the Audit Committee

## Helping you fulfil your responsibilities

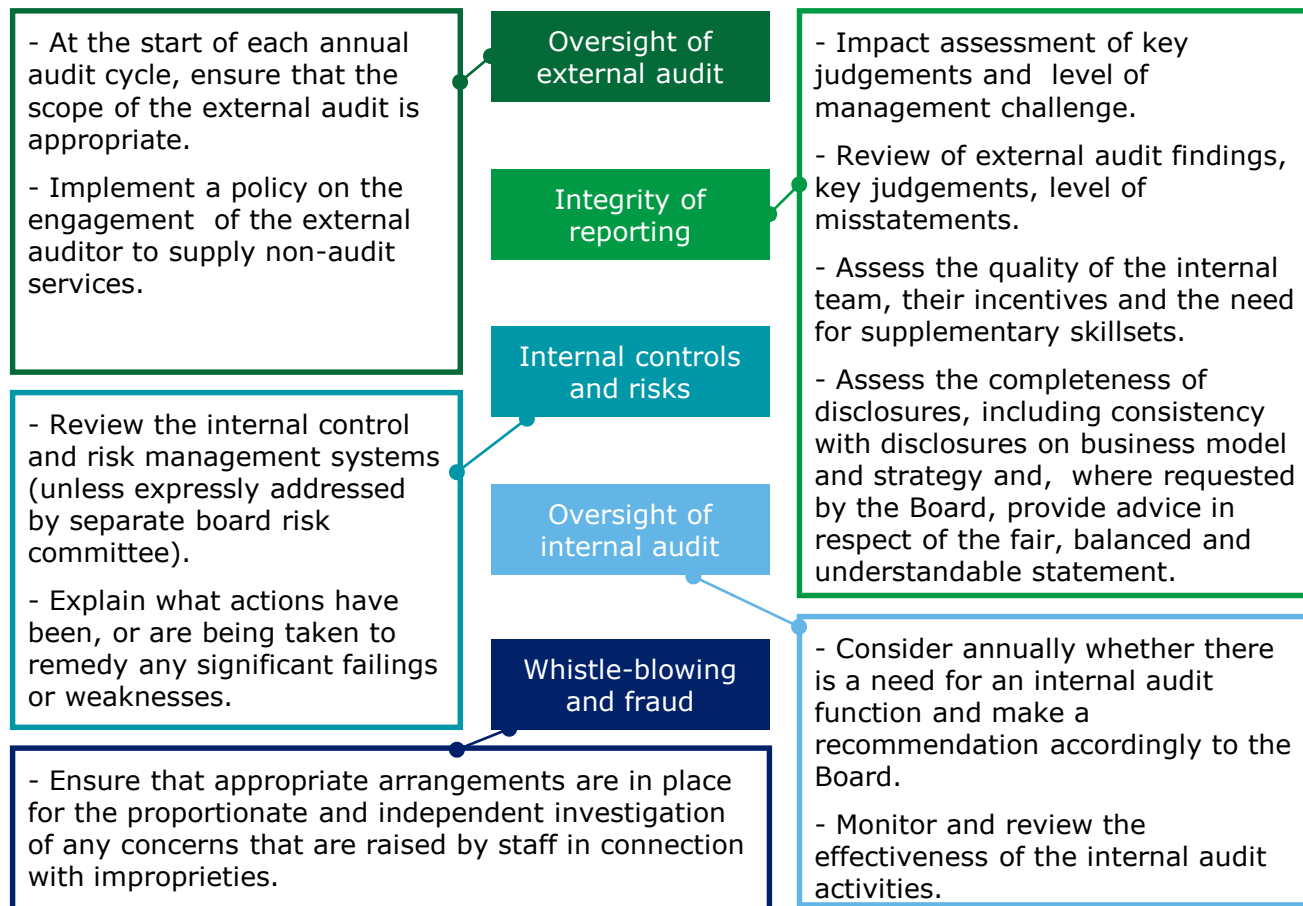
The primary purpose of the Auditor's interaction with the Audit Committee:

- Clearly communicate the planned scope of the financial statements audit
- Provide timely observations arising from the audit that are significant and relevant to the Audit Committee's responsibility to oversee the financial reporting process
- In addition, we seek to provide the Audit Committee with additional information to help them fulfil their broader responsibilities

We use this symbol throughout this document to highlight areas of our audit where the Audit Committee need to focus their attentions.



As a result of regulatory change in recent years, the role of the Audit Committee has significantly expanded. We set out here a summary of the core areas of Audit Committee responsibility to provide a reference in respect of these broader responsibilities and highlight throughout the document where there is key information which helps the Audit Committee in fulfilling its remit.



# Our audit explained

## Area dimensions

In accordance with the 2016 Code of Audit Practice, we have considered how you are addressing the four audit dimensions, being:

- Financial sustainability
- Financial management
- Governance and transparency
- Value for money

## Significant risks

Our risk assessment process is a continuous cycle throughout the year. Page 12 provides a summary of our risk assessment of your significant risks.

## Final audit report

In this report we have concluded on the audit risks identified in our planning report and any other key findings from the audit.

## Key developments in your business

As noted in our planning report, the Board continues to face significant financial pressures due to an increase in costs whilst facing increased demand for services.

The integration of health and social care continues to be a challenge.

## Materiality

The materiality of £1.19 million and performance materiality of £890k has been based on the benchmark of gross expenditure. Materiality is slightly less than the materiality reported in our planning paper of £1.2 million due to updated results. We have used these as the basis for our scoping exercise and initial risk assessment. We have reported to you all uncorrected misstatements greater than £11,900.

## Scope of the audit

We have audit the financial statements for the year ended 31 March 2017 of NHS Shetland group, which includes the consolidated results of Shetland Integration Joint Board.



## Timeline 2017

**November 2016 – February 2017**

Meetings with management and other staff to understand the processes and controls.

**May 2017**

Review of draft accounts, testing of significant risk and performance of substantive testing of results.

**March 2017**

Year end

**26 May 2017**

Audit close meeting

**13 June 2017**

Audit committee meeting










**23 June 2017**

Accounts sign off

## Quality and Independence

We confirm we are independent of NHS Shetland. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority.

# Significant risks Dashboard

Risk	Material	Fraud risk	Planned approach to controls testing	Controls testing conclusion	Consistency of judgements with Deloitte's expectations	Comments	Page no.
Core expenditure resource limits			D+I	Satisfactory		£312k saving achieved	13
Valuation of property assets			D+I	Satisfactory		£3,572k upwards revaluation in year	14
Management override of controls			D+I	Satisfactory		No issues identified	15



Overly prudent, likely to lead to future credit



Overly optimistic, likely to lead to future debit.

**D+I:** Testing of the design and implementation of key controls

# Significant risks (continued)

## Core expenditure resource limits

### Risk identified

The key financial duty for NHS Shetland is to comply with the Revenue Resource Limit, Capital Resource Limit and cash requirements set by the Scottish Government. Given the current budget position for the Board and the pressures across the whole of the public sector, there is an inherent fraud risk associated with the recording of expenditure within these limits.



### Key judgements and our challenge of them

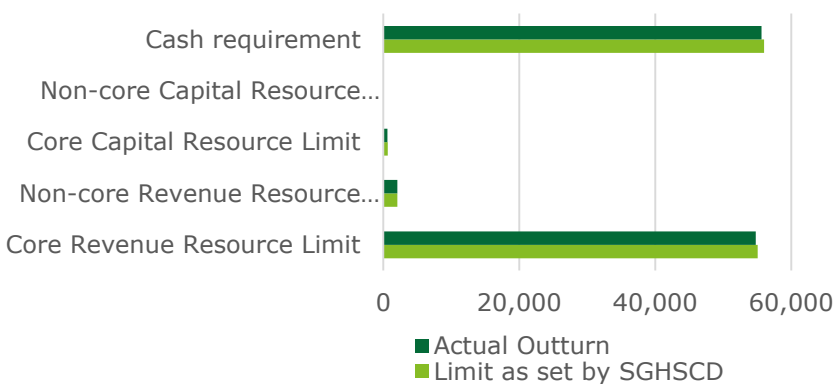
We must provide an opinion on regularity, to the effect that expenditure and receipts were incurred or applied in line with guidance. We have evaluated the results of our audit testing in the context of the achievement of the targets set by the Scottish Government.



### Deloitte response

- We performed design and implementation testing around the controls NHS Shetland has in place to ensure expenditure is within budget;
- We assessed whether expenditure was correctly classified between revenue and capital and whether it has been incurred in accordance with Scottish Government's guidance;
- We performed focused cut-off testing;
- We reviewed and challenged the assumptions made in estimating the prescribing accrual to assess completeness of recorded expenditure; and
- We obtaining independent confirmation of the resource limits allocated to NHS Shetland by the Scottish Government.

Core Expenditure Resource Limits £'000



### Deloitte view

- We have concluded through the performance of our year end procedures that the expenditure and receipts were incurred or applied in accordance with the applicable enactments and guidance issued by the Scottish Ministers and the expenditure is valid and correctly classified between revenue and capital.
- We confirm that NHS Shetland has performed within the limits set by the Scottish Government Health and Social Care Directorate (SGHSCD) and therefore in compliance with the financial targets in the year.

# Significant risks (continued)

## Valuation of property assets

### Risk identified

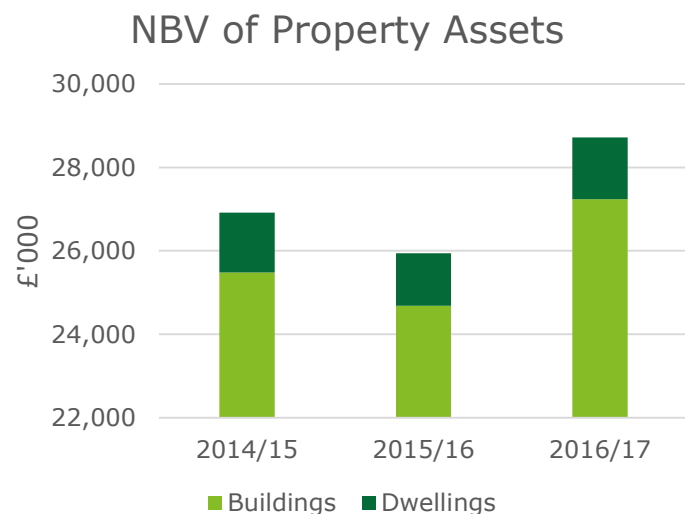
The Board is required to hold NHS Estate property assets (land and building) within Property, Plant and Equipment at a modern equivalent use valuation. The valuations are by nature significant estimates which are based on specialist and management assumptions and which can be subject to material changes in value.



### Key judgements and our challenge of them

The Board held £29.3 million of property assets at 31 March 2017. Revaluation is performed on a 3 year cycle by the Board's appointed Valuer. In the year to 31 March 2017 100% of the portfolio was revalued by Gerald Eve.

The net book value of property has increased by £3.572 million in the year, due to increases in building value.



### Deloitte response

- We reviewed the external revaluations performed in the year and assessed whether they have been performed in a reasonable manner, on a timely basis and by suitably qualified independent individuals;
- We reviewed the information provided to the Valuer to assess completeness;
- We tested a sample of revalued assets and re-performed the calculation assessing whether the movement has been recorded through the correct line of the accounts;
- We involved the use of our internal property specialists, Deloitte Real Estate, to review and challenge the assumptions and methodology adopted;
- As a result of early discussion between NHS Shetland, Gerald Eve and Deloitte property specialists, the Valuer took on board our initial comments and reflected these in the reports which helped the audit to run smoothly; and
- We performed design and implementation testing on the controls in place around the review of the Valuer's report.

### Deloitte view

We have concluded that the net book value is not materially misstated. The Board's valuation assumptions are in line with other Boards and fall within the expected range highlighted by Deloitte Real Estate.

# Significant risks (continued)

## Management override of controls

### Risk identified

International Standards on Auditing requires auditors to identify a presumed risk of management override of control. This presumed risk cannot be rebutted by the auditor. This recognises that management may be able to override controls that are in place to prevent inaccurate or even fraudulent financial reports.



### Deloitte response

We have considered the overall sensitivity of judgements made in preparation of the financial statements, and note that:

- the Board's results throughout the year were projecting overspends in operational areas but this was closely monitored with confidence that the board would be able to meet its overall financial targets; and
- senior management's remuneration is not tied to particular financial results.

We have considered these factors and other potential sensitivities in evaluating the judgements made in the preparation of the financial statements.

### Deloitte view

- We have not identified any significant bias in the key judgements made by management.
- The control environment is appropriate for the size and complexity of the Board.
- See page 17 for insights identified through use of Spotlight, Deloitte's bespoke analytics software.

### Journals

We have made inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments. We have used Spotlight data analytics tools to test a sample of journals, based upon identification of items of potential audit interest. Our analysis covered the 80,472 journals posted in the year. No issues noted from our testing

### Accounting estimates

In addition to our work on key accounting estimates discussed above, our retrospective review of management's judgements and assumptions relating to significant estimates reflected in last year's financial statements completed with no issues noted.

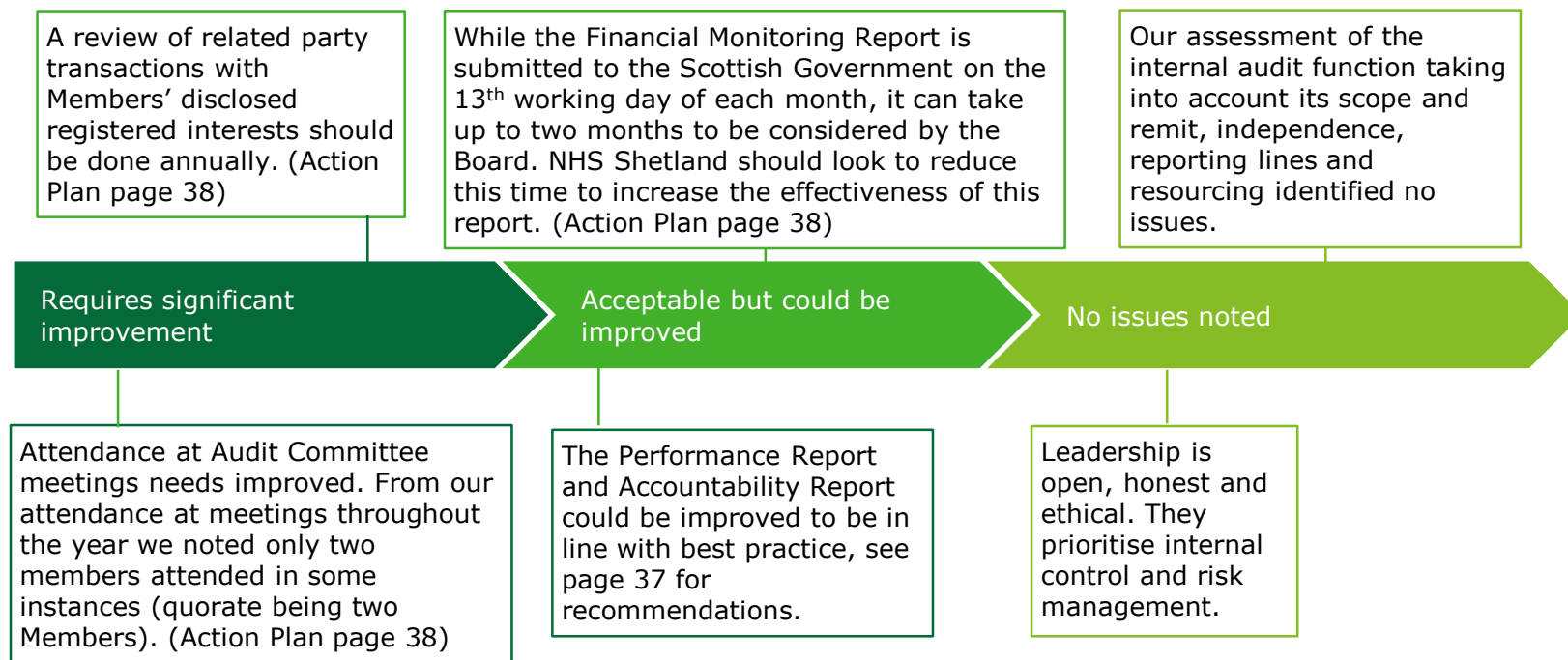
### Significant transactions

We did not identify any significant transactions outside the normal course of business or transactions where the business rationale was not clear.

# Other significant findings

## Internal control and risk management

ISA 315.12 (UK and Ireland) requires we obtain an understanding of internal control relevant to the audit. It is a matter of the auditor's professional judgment whether a control, individually or in combination with others, is relevant to the audit. We do not test those controls we do not consider relevant to the audit. Below we provide a view, based on our audit procedures, on the effectiveness of your system of internal control relevant to the audit risks that we have identified.



### Deloitte view

In our view, a review should be performed annually of Member's registered interests to determine whether there are any related party transactions which should be disclosed.

NHS Shetland also need to improve the quality of its Performance Report in light of best practice in this area and the timeliness of reviewing the financial monitoring report by the Board.



# Other significant findings (continued)

## Insights delivered

Key Statistics	2016/17
Number of journals	80,472
Dr value of largest journal	4,000,000
Total Dr value of journals	388,343,174
Avg absolute value of journals	9,652
Number of zero Dr value journals	147
Number of users posting in the period	28

We have utilised **Spotlight** to perform analytics on all of the journal entries processed during the year. We have highlighted some key themes arising from this work for your consideration.

### Management commentary:

The highest volume users are consistent with the transactional nature of the workload generated in the Finance team and in line with our understanding of NHS Shetland with most journals posted being automated. Two of the top users are NHS Grampian employees who are responsible for invoice processing.

The analysis of journals posted at weekends has been extremely useful. In most cases the transactional activity is consistent with periodic peaks in workload where staff are working weekends in order to meet key deadlines.

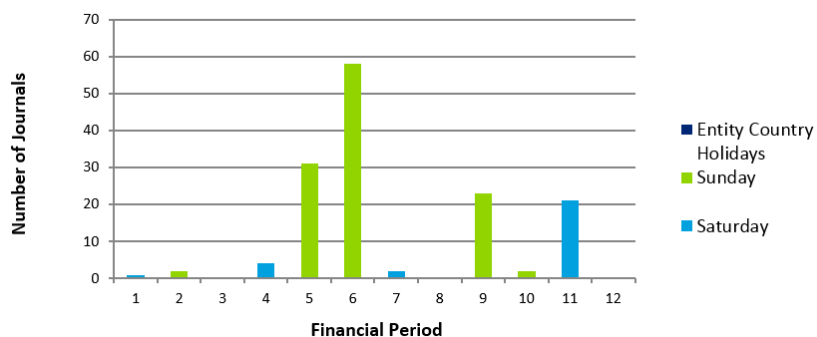
Top 5 Users by Volume			
Current Year Users		New Users	
Username	Total Number of Journals	Username	Total Number of Journals
AUTO	55,669	AUTO	55,669
ZKG1	8,773	ZKG1	8,773
ZDR1	3,796	ZDR1	3,796
ZLS3	3,115	ZLS3	3,115
ZKK1	1,192	ZKK1	1,192

### Deloitte view

70% of journals posted are automated (AUTO being automated journals in Top Users chart). Maintaining high automation levels will help ensure efficiencies within the Finance Team.

Going forward Spotlight will be a useful tool to identify trends and any irregularities over the 5 years of our audit appointment.

Journals entered on a non-business day



# Your annual report

We welcome this opportunity to set out for the Audit Committee our observations on the annual report. We are required to provide an opinion on the remuneration report, the annual governance statement and whether the management commentaries are consistent with the disclosures in the accounts.

	Management response	Deloitte response
The Performance Report	<p>The report outlines NHS Shetland's performance, both financial and non-financial. It outlines its vision, supported by a set of strategic objectives, to deliver its 10 year Public Health Strategy. It also sets out the key risks and uncertainty as set out in the Local Delivery Plan.</p>	<p>We have assessed whether the performance report has been prepared in accordance with the accounts direction. No exceptions noted.</p> <p>We have also read the performance report and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.</p> <p>Audit Scotland published a good Practice note on 9 May 2017 for Performance Reports. NHS Shetland should consider this best practice report and in particular consider the following recommendations:</p> <ul style="list-style-type: none"><li>• Link risks to strategic objective, include mitigating actions and how the risk has changed over time.</li><li>• Include a Governance Chart to show the governance arrangements in place.</li><li>• Tabularise/graph non-financial performance statistics.</li><li>• Include a pie chart which depicts the different types of expenditure in the year.</li><li>• Include employee satisfaction statistic.</li><li>• Include a glossary of commonly abbreviated terms.</li><li>• The Overview should provide sufficient information so that lay users have no need to go further to understand the Board and its performance.</li></ul> <p>(Action Plan – page 37)</p>

# Your annual report (continued)

	Management response	Deloitte response
The Accountability Report	Management have ensured that the accountability report meets the requirements of the FReM, comprising the governance statement, remuneration and staff report and the parliamentary accountability report.	<p>We have assessed whether the information given in the governance statement is consistent with the financial statements and has been prepared in accordance with the accounts direction. No exceptions noted.</p> <p>We have also read the accountability report and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.</p> <p>We have also audited the auditable parts of the remuneration and staff report and confirmed that it has been prepared in accordance with the accounts direction.</p> <p>To be in line with Scottish Public Finance Manual (SPFM) best practice, we recommend the following updates to the governance statement:</p> <ul style="list-style-type: none"><li>• Provide a link to the 5 year plan, strategic documents and whistle blowing policy.</li><li>• Include tables, diagrams and graphs.</li></ul> <p>(Action Plan – Page 37)</p>
Going Concern	Management has made appropriate disclosure relating to Going Concern matters.	We have confirmed that the 2017/18 Local Delivery Plan was approved by the Board on 18 April 2017 and included draft budgets for 2018/19 to 2019/20. We have concluded that the plan is sufficiently robust to demonstrate that NHS Shetland will be a going concern for 12 months from signing the accounts.

# Wider scope requirements

## Financial sustainability

### Audit dimension

As part of the annual audit of the financial statements, we have considered the appropriateness of the use of the going concern basis of accounting. Going concern is a relatively short-term concept looking forward 12 to 18 months from the end of the financial year. Financial sustainability interprets the requirements and looks forward to the medium (two to five years) and longer term (longer than five years) to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

### Areas considered



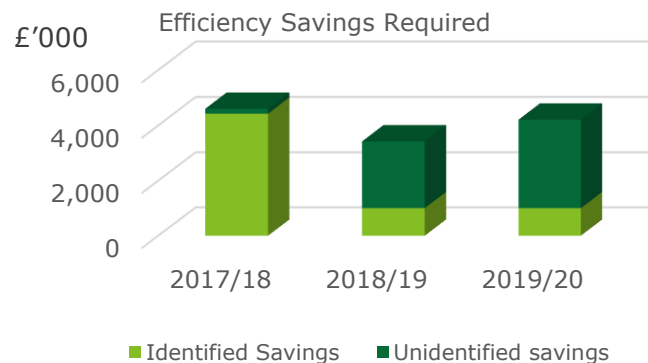
- The financial planning systems in place across the shorter and longer terms
- The arrangements to address any identified funding gaps
- The affordability and effectiveness of funding and investment decisions made

### Deloitte response



We have reviewed NHS Shetland's 3 year financial plan and the arrangements to address the funding gap and planned investment.

The 2017/18 revenue budget and capital programme were agreed by the Board on 18 April 2017. The budget outlines how NHS Shetland will meet its key revenue targets over the next 3 years, and in doing so, it must achieve recurring cost reductions/ productivity improvements in each of these years, which the Board recognises will be challenging. The value of saving is shown below.



It is good practice to identify savings in full in advance of the start of the year to ensure that sufficient time is set aside to have fully developed implementation plans.

# Wider scope requirements (continued)

## Financial sustainability (continued)

NHS Shetland has an approved budget for 2017/18 of £56.5 million, compared to a budget in 2016/17 of £54.8 million. NHS Shetland has agreed the total funds to be allocated to the IJB in 2017/18 is £23.1 million. The IJB has an approved budget for 2017/18 of £42.366 million, compared to a budget of £42.82 million in 2016/17.

In 2016/17, NHS Shetland delivered an underspend of £312k against its core Revenue Resource Limit, an underspend of £2k against its non-core Revenue Resource Limit and an underspend of £50k against its core Capital Resource Limit.

Below is the forecasted increased costs in 2017/18 which highlights the additional cost pressures for 2017/18. We note some of these cost pressures will be covered by the increased budget and the remaining will be met through efficiency savings. The targeted investment tables shows the planned capital investments for the next 3 years for which specific capital funding will be received.

2017/18 Increased Costs	£'000	2017/18-2020/21 Targeted Investment	£'000
Pay awards	741	Ambulatory Care	1,364
Non-pay inflation and Utilities	314	X Ray Room 2 Fluoroscopy	800
SLA Inflation	469	Acute Ward Redesign	6,000
Commissioning and Investments	511	CT Scanner	1,200
Prescribing and Hospital Drugs	573	<b>Total</b>	<b>9,364</b>
Cost Pressures	162		
Social Care Funding (to IJB)	420		
Additional Capacity funding (non-recurring)	250		
Additional Contingency (non-recurring)	500		
<b>Total</b>	<b>3,941</b>		

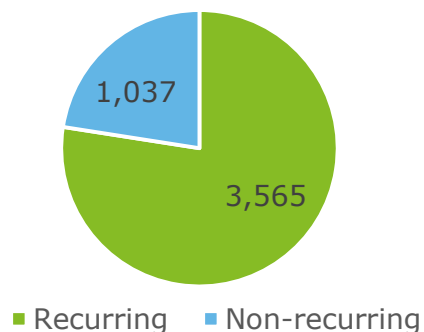
# Wider scope requirements (continued)

## Financial sustainability (continued)

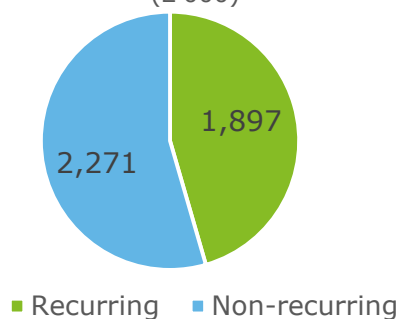
### Overall financial performance

The pie charts below illustrates how the Board's performance is split between recurring and non-recurring savings

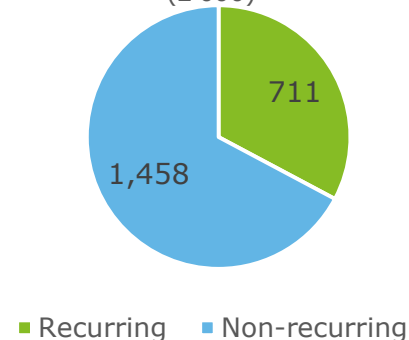
Forecast Savings 2017/18 (£'000)



Achieved Savings in 2016/17 (£'000)



Achieved Savings in 2015/16 (£'000)



The 2016/17 Financial Plan included savings targets of £3,713k, equivalent to 7% of the Board's baseline resource allocation.

At the close of 2016/17 there was a recurring deficit of £1,805k increasing from £1,462k in 2015/16.

This recurring deficit has been included in the 2017/18 financial plan. The Local Development Plan has an efficiency saving target of £12,600k over the next 3 years.

NHS Shetland plans to make £4.6 million savings in 2017/18, £3,565k of this comprising of recurring savings. This represents a 10% savings against baseline expenditure.

Historically recurring savings targets have not been achieved by NHS Shetland. Savings targets have been met through non-recurring savings.

# Wider scope requirements (continued)

## Financial sustainability (continued)

### Workforce planning

To achieve its long term vision detailed within 2020 Healthcare Vision, managing its workforce is key and staff development, training and education is key to creating and maintaining a robust and pro-active workforce and remains a high priority for NHS Shetland.

We have confirmed that NHS Shetland has both an organisation-wide and departmental workforce plans in place informed by the Workforce 2020 vision, which are consistent across the organisation. Succession planning is considered but only for the short-medium term, as required by the Scottish Government guidance.

In its LDP for 2016/17, the board has noted that workforce issues are proving challenging, particularly with regard to recruitment and retention of GPs and junior doctors. A workforce strategy is being created and is to be approved in 2017 and will take forward various initiatives to support the workforce of the future.

### Deloitte view

As with all NHS Boards, NHS Shetland has challenging savings targets to meet moving forward to continue to be financially sustainable. Historically, NHS Shetland has achieved its savings targets, however, this is largely as a result of reliance on non-recurring savings. We recommend that NHS Shetland focuses on identifying and implementing recurring savings in 2017/18 and therefore reduce the savings deficit. (Action Plan – page 40)

The Board is implementing a strategic change programme for 2017/18 which focuses on recurring savings. However future years are more uncertain and detailed plans to realise these savings in each area need to be agreed as soon as possible to ensure that NHS Shetland can achieve these targets. The Transformation Change Board needs to be supported by very robust benefits realisation processes, including tools and templates, and programme management methodologies. A supporting people change management strategy will also be critical if the Board is to achieve recurring savings targets. (Action Plan – page 40)

Further scenario planning and sensitivity analysis should be performed by the Board to assess the impact of these issues. See case studies in page 24 for recommendations and also page 40.

There is currently a risk that the £4.6 million of efficiency savings required in 2017/18 may not be achieved.

We recommend that NHS Shetland considers the case studies on page 24, which highlights the lessons learned from our wider health transformation work in the sector including our work on increasing productivity, demand management and cost reduction.

# Wider scope requirements (continued)

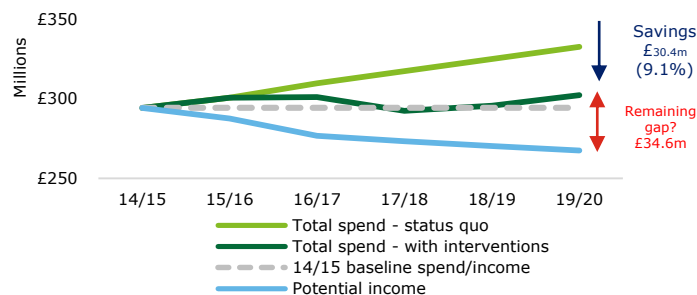
## Financial sustainability (continued)

### Best Practice Case Studies

Deloitte has been involved in cost reduction work with a number of NHS bodies. We recommend that the Board reviews these case studies and considers the opportunities for cost reduction going forward, in line with our recommendation on page 23. We would be happy to provide further details if required.

#### Early Intervention

A case study was carried out on an organisation which had an early intervention programme and assisted living service within local communities. We estimated the benefits that might be possible from the programme, looking forward at the financial position on a “do nothing” baseline and then applying assumptions around reductions in activity based on best practice evidence available. We were then able to advise on the make up of the programme and make recommendations on the best approach to delivering the projects and on the governance structures and resourcing required to enable the programme to achieve its ambitions.



From this work we estimated that the programme could deliver £30m in savings as illustrated in the following diagram, which should at the same time improve outcomes.

We recommend that NHS Shetland consider applying a similar analysis to help identify how best to target its work on interventions and to deliver better outcomes from the new pooled budgets.

#### Agency Cost Reduction

We undertook a review of nurse rostering practices for an NHS client with the aim of reducing premium agency use as well as bank expenditure. This involved a ward by ward review of rostering protocols working with all lead nurses which highlighted a range of issues for the Board to address, including how best to use data from rostering systems, issues associated with ward performance statistics as well as opportunities to tighten up internal cost controls. The work was delivered by a team with both nursing and operational management experience to make sure our recommendations and insight were relevant and bespoke to the NHS.

#### Cost Reduction

Working alongside an NHS client we used a range of internal data and external benchmarks to help the Board identify priority programmes for improvement, in particular looking at length of stay and theatres data which identified opportunities for improving value for money. We used tableau dashboards to identify down to an individual consultant, anaesthetist and surgeon level variation in performance which helped us identify opportunities for improvement and potential cost savings. The aim was to link concepts including data analytics, process variation and cost reduction to complement the establishment of its Quality Programme.



# Wider scope requirements (continued)

## Financial management

### Audit dimension

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

### Areas considered



- Systems of internal control
- Budgetary control system
- Financial capacity and skills
- Arrangements for the prevention and detection of fraud

### Deloitte response



We have reviewed internal audit reports in relation to their work on the key financial controls.

We have reviewed the budget and monitoring reporting to the Board during the year to assess whether financial management and budget setting is effective.

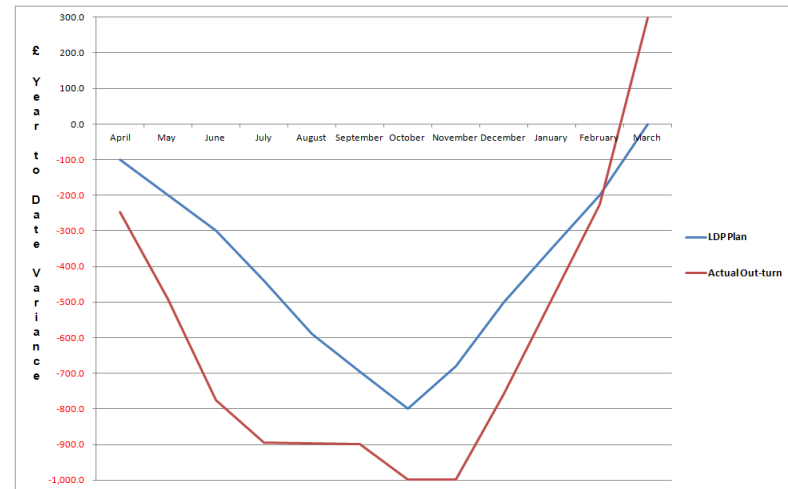
We recommend that the Deloitte Benchmarking survey is completed, to allow assessment of NHS Shetland's financial capacity and skills.

Our fraud responsibilities and representations are detailed on page 41. Ongoing potential fraud investigations have been reported to each Audit Committee and are included in SFR 18 (Summary of Losses and Special Payments) submitted to the Scottish Government.

NHS Shetland budgeted a breakeven position for the year to 31 March 2017. The final out-turn was an underspend of £312k against the core revenue resource limit.

During the year the Board reported overspends each month, which were higher than the trajectory forecasted in the Local Delivery Plan, this peaked at £1 million in December, due to unachieved efficiency savings and the use of locums to fill staffing gaps. To manage the position the Board implemented non-recurring savings to manage the break-even position.

NHS 2016/17 Financial Plan Trajectory



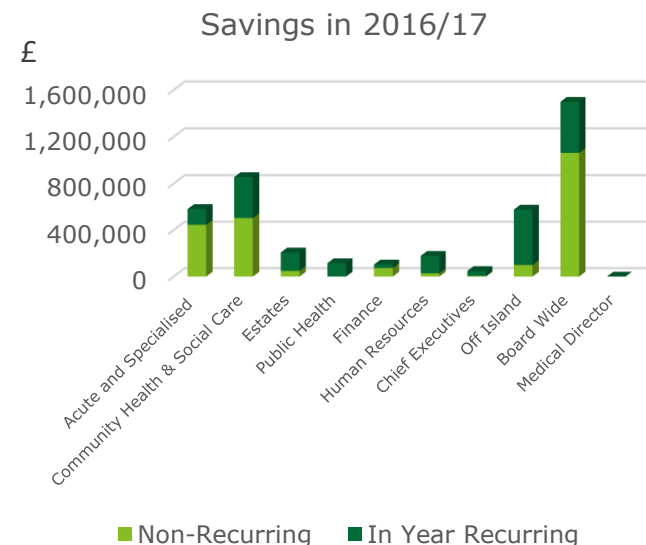
# Wider scope requirements (continued)

## Financial management (continued)

### Revenue expenditure

Financial balance was achieved through a combination of delivery of productivity and efficiency savings. See chart below which shows where savings were achieved in the year.

Looking forward, the Board has recognised within the Local Delivery Plan for 2017/18 a requirement to continue to manage any dependency on non-recurring resources. See consideration of forecasted savings on page 23.



### Capital expenditure

The Board's Capital expenditure in the year was £736k, which is £50k below the approved capital resource limit. The funding of the capital expenditure was also financed by the sale of 2 residential houses for £125k in the year. Capital expenditure has slightly increased from prior year where expenditure was £687k. One of the properties was sold in December 2016 and one just prior to the year-end.

The main areas of spend in the year were:

- Anaesthetics Machines
- Scopes
- Electronic Document Management System
- A&E Trolleys
- Roof Insulation for Health Centres

#### Deloitte view

NHS Shetland has historically always met its financial targets and broken even which evidences that management can effectively forecast and has sound financial management procedures in place.

We are comfortable with the fraud arrangements in place. Ongoing potential fraud investigations have been reported to each Audit Committee and are included in SFR 18 (Summary of Losses and Special Payments) submitted to the Scottish Government.

# Wider scope requirements (continued)

## Governance and transparency

### Audit dimension

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information.

#### Areas considered



- Governance arrangements
- Scrutiny, challenge and transparency on decision making and financial and performance reports
- Quality and timeliness of financial and performance reporting

#### Deloitte response



We have reviewed the financial and performance reporting to the Board during the year as well as minutes of all Board meetings to assess the effectiveness of the governance arrangements. Our attendance at Audit Committees has also informed our work in this area.

We have reviewed the governance of transformation and benefits realisation process and consider the arrangements in place for securing effective clinical governance and engagement. See page 28 for case study on clinical governance which the Board should consider.

From our attendance at Audit Committee meetings we note that on occasions there were only two members in attendance. This will limit the scale of challenge and scrutiny the committee can perform. We recommend the Audit Committee refers to the Audit Committee Effectiveness report issued by Deloitte which has previously been shared with the Director of Finance to perform an annual assessment of its effectiveness in accordance with best practice.

While the Financial Monitoring Report is submitted to the Scottish Government on the 13<sup>th</sup> working day of each month, it can take up to two months to be considered by the Board. NHS Shetland should look to reduce this time to increase the effectiveness of this report. (Action Plan page 38)

# Wider scope requirements (continued)

## Governance and transparency (continued)

In 2016/17 there was a number of changes in leadership, this has the potential for causing a lack of consistency in the year. Three people took the role of Vice Chair in the year. Additionally there was only two Non-Executive Members (including the Chairman) that held office for the whole financial year. Drew Ratter retired in the year. Daisy Leask held office briefly for 2 months in the middle of the year. Thomas Morton and Andrew Glen both started part way through the year. There were no changes in Executive members in the year.

Deloitte recommend the Board consider the Case Study below, which highlights the impact poor governance arrangements can have

Internal Audit has completed its annual plan in accordance with what was agreed with the Audit Committee and has reported its findings from each area to the Audit Committee throughout the year. It is noted that seven high risk recommendation was made in relation to IT Healthcheck, we note that management has taken on Board the recommendations from Internal Audit and responded to the risks.

Management have implemented a number of improvements to its strategic planning and performance management during the year following a review by internal audit.

### Clinical Governance Case Study

Deloitte has recently performed a review of the Clinical Governance arrangements within an NHS client, which was undertaken when the client was undergoing a change in leadership.

It was identified there was a lack of clarity in relation to roles and responsibilities, inadequate papers being presented to the Committee and that standardisation across divisions in the Acute Sector could be implemented to improve effectiveness.

### Deloitte view

We confirm that we have reviewed the governance arrangements, the level of scrutiny, challenge and transparency of decision making and the quality and timeliness of financial and performance reporting and have identified no issues in this regard. We have, however, recommended that the timeliness of financial monitoring to the Board could be improved.

We have no concerns around the arrangements with internal audit. We have reviewed the reports issues by internal audit and considered impact on our audit approach.

# Wider scope requirements (continued)

## Value for money

### Audit dimension

Value for money is concerned with using resources effectively and continually improving services.

### Areas considered



- Value for money in the use of resources
- Link between money spent and outputs and the outcomes delivered
- Improvement of outcomes
- Focus on and pace of improvement

### Deloitte response



We have gained an understanding of the Boards self-evaluation arrangements to assess how it demonstrates value for money in the use of resources and the linkage between money spent and outputs and outcomes delivered.

We have also consider the arrangements the Board has in place to monitor how it is achieving its Local Delivery Plan targets and addressing areas of poor performance.

### Performance management

The performance of NHS Shetland is monitored by the Scottish Government against a number of targets and standards which support the delivery of the Scottish Government's national performance framework. These targets and their trajectories are set out in the Board's 2017/18 Local Delivery Plan (LDP).

Performance against LDP targets and standards is presented to each Board meeting.

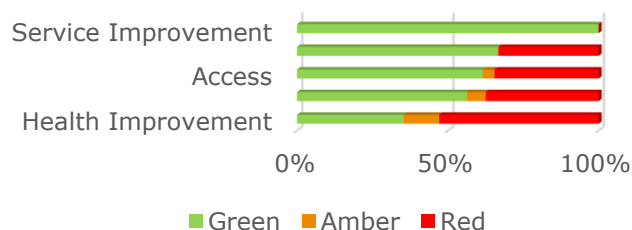
# Wider scope requirements (continued)

## Value for money (continued)

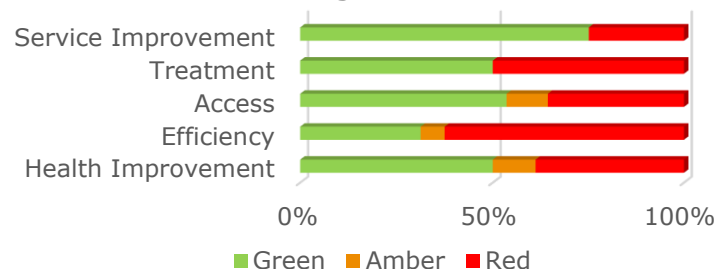
### Overview of performance targets in 2016/17

The board's performance against its LDP targets and standards as reported in the April 2017 Performance Report is compared against 2015/16 results and is summarised below:

Performance against national and local targets 2016/17



Performance against national and local targets 2015/16



Compared to the prior year it is noted there is an improvement in Service Improvement, Treatment and Efficiency. There is a higher incidence of 'red' status on health improvement, this is indicative of the challenges facing the Board in the current financial climate.

NHS Shetland are part of the NHS Benchmarking Club, however they do not participate in the benchmarking exercise as they are an outlier. Given the lack of people that go through the hospital, compared to other hospitals they are seen as being very inefficient.

With the implementation of the Strategic Change Programme in 2017/18, there will be a new reporting system with local targets being updated to better reflect user satisfaction.

#### Deloitte view

The overall approach adopted is that performance management is integral to the delivery of quality and effective management, governance and accountability. The need for transparent and explicit links of performance management and reporting within the organisational structure at all levels is critical. There is a framework of measures at directorate and service level.

The Board had a well established performance management framework in place, with performance regularly considered by management, and the Board. Overall the Board has reported a high number of areas at risk or not on track against local or national indicators, however, a slightly improved position is noted when benchmarked against prior year. A number of actions are in place to address areas where performance is either at risk or not on track.

We are satisfied that the performance is appropriately discussed within the Performance Report in the Annual Accounts and management have introduced plans to address areas where progress has not been satisfactory.

# Wider scope requirements (continued)

## National Fraud Initiative

In accordance with Audit Scotland planning guidance, we are required to monitor the Board's participation in the National Fraud Initiative (NFI) and progress during 2016/17 and completed an NFI audit questionnaire by 30 June 2017. A summary of the matches reported in the NFI system is provided below:

	Payroll	Creditors	Total
Total matches flagged	25	1,798	<b>1,823</b>
Total recommended matches to be investigated	5	46	<b>51</b>

### Deloitte view

The results of investigations have still to be recorded in the NFI system. The review of all matches has not been fully completed as resources were being prioritised to the annual accounts process, however plans are in place to complete this work.

We concluded that NHS Shetland is fully engaged in the NFI exercise.

# Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

## What we report

Our report is designed to help the Audit Committee and the Board discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA 260 (UK and Ireland) to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements and our observations on the quality of your Annual Report.
- Our internal control observations
- Other insights we have identified from our audit

## What we don't report

As you will be aware, our audit was not designed to identify all matters that may be relevant to the board.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

We welcome the opportunity to discuss our report with you and receive your feedback.

## The scope of our work

Our observations are developed in the context of our audit of the financial statements.

We described the scope of our work in our audit plan and the supplementary "Briefing on audit matters" circulated to you on 28 February 2017.

This report has been prepared for the Audit Committee and Board, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.



**Deloitte LLP**

Glasgow 23 June 2017



# Summary of national reports



# National performance reports

## Summary of reports issued over the past year

### **NHS Scotland 2016**

Published October 2016

#### **Headline messages**

A combination of increasing costs, staffing pressures and unprecedented savings targets mean that Scotland's NHS boards are finding it difficult to balance demand for hospital care with investing in community-based services to meet future need.

#### **Impact on NHS Shetland**

In partnership with the IJB, NHS Shetland should take ownership of changing and improving services in their local area, working with relevant partner organisations.

They should also develop long-term workforce plans (more than 5 years) to address problems with recruitment, retention and succession planning and to ensure high quality care.

Finally, they should work with the public about the need for change in how they access, use and receive services and to take more responsibility for looking after their own health and managing their long-term conditions.

### **Scotland's NHS workforce**

Published February 2017

#### **Headline messages**

Audit Scotland has pulled together published statistics on Scotland's NHS workforce in a new data briefing. The document sets out the challenges being explored by the public spending watchdog in a new two part audit of the NHS workforce. Audit Scotland will publish its first report, focuses on staffing in acute services, in summer 2017.

#### **Impact on NHS Shetland**

The following specific areas have been highlighted in relation to NHS Shetland:

- Vacancies – NHS Shetland has high vacancies rates along with high spending on agency staff.
- Turnover – turnover rates have increased slightly over the last few years.
- Ageing – there is a trend towards an increasingly ageing workforce.



# Appendices



# Audit adjustments

We note there were no material unadjusted misstatements or disclosure deficiencies identified up to the date of this report.



One immaterial uncorrected adjustment was noted. From our testing of accruals, we identified an under accrual of £7,133. As it is not possible to confirm that this was an isolated error, we have extrapolated this over the accruals population, which results in a judgemental misstatement of £63,272. As the amount is immaterial, no adjustment has been made to the financial statements.

There was one adjusted disclosure misstatement identified:

Disclosure	Summary of disclosure requirement	Quantitative or qualitative consideration
Staff report	Staff Numbers and WTE	Head count numbers were found to be inconsistent with underlying data. Disclosure has been updated.

# Action plan

## Recommendations for improvement

Area	Recommendation	Management Response	Responsible person	Target Date	Priority
Performance report	<p>To improve users understanding of NHS Shetland's performance in the year, we recommend including the following:</p> <ul style="list-style-type: none"> <li>• Link risks to strategic objective, include mitigating actions and how the risk has changed over time</li> <li>• Include a Governance Chart to show the governance arrangements in place</li> <li>• Tabularise/graph non-financial performance statistics</li> <li>• Include a pie chart which depicts the different types of expenditure in the year</li> <li>• Include employee satisfaction statistic</li> <li>• Include a glossary of commonly abbreviated terms</li> <li>• The Overview should provides sufficient information so that lay users have no need to go further to understand the Board and its performance</li> </ul>	Will look to improve next years performance report	Colin Marsland (Director of Finance)	31 March 2018	
Accountability Report	<p>To be in line with SPFM best practice, Deloitte recommend making the following updates to the Annual Governance Statement:</p> <ul style="list-style-type: none"> <li>• Provide a link to the 5 year plan, strategic documents and whistle blowing policy</li> <li>• Include tables, diagrams and graphs</li> </ul>	Will look to improve next years Accountability Report	Colin Marsland (Director of Finance)	31 March 2018	

### Key:



High Priority






Medium Priority



Low Priority

# Action plan

## Recommendations for improvement (continued)

Area	Recommendation	Management Response	Responsible person	Target Date	Priority
Related Parties	We recommend that the Board perform an annual review of Member's registered interests to determine whether there were any transactions with NHS Shetland, to ensure full disclosure of Related Party Transactions.	Will look to perform in 2017/18	Karl Williamson (Head of Finance)	31 March 2018	
Financial Reporting Period	We recommend that NHS Shetland look to reduce their Financial Close Period, and additionally the time it takes for the Financial Monitoring Report to be reviewed by the Board to increase the effectiveness of the Report.	Board meetings are not aligned to the Financial close. EMT meet every 2 weeks to discuss financial results.	Karl Williamson (Head of Finance)	31 March 2018	
Audit Committee Attendance	We recommend there are increased efforts within the Audit Committee to improve attendance to improve scrutiny and oversight.	There are four non executive members of the Board appointed to the Audit Committee. A review of non executive director appointments to the Governance Committee will occur in August 2017. Once the new committee is confirmed the current meeting schedule will be reviewed in September to minimise the potential risk of non attendance.	Colin Marsland (Director of Finance)	31 March 2018	

**Key:**



High Priority




Medium Priority



Low Priority

# Action plan

## Recommendations for improvement (continued)

Area	Recommendation	Management Response	Responsible person	Target Date	Priority
Audit Committee Effectiveness	We recommend that the Audit Committee refers to the Audit Committee effectiveness report issued by Deloitte which has previously been shared with the Director of Finance to perform an annual assessment of its effectiveness in accordance with best practice.	<p>With the changes in audit committee membership in 2016-17 and further changes in 2017-18 anticipated it has been identified that there is a training gap to address in the Audit Committee members in partnership with their independent advisers. Initial discussions have taken place for Internal Audit to deliver a training session to Board members.</p> <p>The Board currently has no non executive Board Member that has at least one competence in accounting or auditing, or both. Unless the current recruitment for two non executive directors selects an individual with those skills it is a continuing risk management issue for the Board. However some member of the Audit Committee do run their own successful local private business.</p>	Colin Marsland (Director of Finance)	31 Dec 2017	

**Key:**



High Priority





Medium Priority



Low Priority

# Action plan

## Recommendations for improvement (continued)

Area	Recommendation	Management Response	Responsible person	Target Date	Priority
Recurring Savings	NHS Shetland should focus on identifying and implementing recurring saving opportunities, to reduce its savings deficit and become a more cost effective organisation	A Transformational Change Board has been set up to co-ordinate delivery of the 2017/18 Strategic Programme	Transformational Change Group	Ongoing	
Transformational Change Board	The Transformational Change Board needs to be supported by very robust benefits realisation processes, including tools and templates, and programme management methodologies. A supporting people change management strategy will also be critical if the Board is to achieve recurring savings targets.	The terms of reference for the Transformational Change Board has been agreed and strategic projects will be managed by individual project boards using the Prince 2 methodology. In setting the 2017-18 budget for the Board a specific transformational change fund was established with a budget of £250,000 that will be managed by the Transformational Change Board to allocate non recurrent change funding to address identified critical capacity or equipment to take projects forward in-line with their identified critical pathways. Organisational change policies will apply to the projects including partnership working with key external partners, the public and staff groups	Transformational Change Group	Ongoing	

**Key:**



High Priority



Medium Priority



Low Priority



# Fraud responsibilities and representations

## Responsibilities explained



### Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.



### Required representations:

We have asked the Board to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the entity or group.

We have also asked the Board to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.



### Audit work performed:

In our planning we identified the risk of fraud in complying with expenditure resource limits and management override of controls as a key audit risk for your organisation.

During course of our audit, we have had discussions with management and those charged with governance.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the financial statements

We have reviewed the paper prepared by management for the audit committee on the process for identifying, evaluating and managing the system of internal financial control.

### Concerns:

Deloitte note no areas of concern from review of the whistle blowing procedures and from our above audit procedures



# Independence and fees

As part of our obligations under International Standards on Auditing (UK and Ireland), we are required to report to you on the matters listed below:

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**Independence confirmation** We confirm that we comply with APB Ethical Standards for Auditors and that, in our professional judgement, we and, where applicable, all Deloitte network firms are independent and our objectivity is not compromised.

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**Fees** The audit fee for 2016/17 is £74,501 as discussed with management.

No non-audit services fees have been charged by Deloitte in the period.

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**Non-audit services** In our opinion there are no inconsistencies between APB Ethical Standards for Auditors and the company's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.

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**Relationships** We are required to provide written details of all relationships (including the provision of non-audit services) between us and the organisation, its board and senior management and its affiliates, including all services provided by us and the DTTL network to the audited entity, its board and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.

We are not aware of any relationships which are required to be disclosed.

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# Events and publications

## Our events and publications to support the Board

### Sharing our informed perspective

We believe we have a duty to share our perspectives and insights with our stakeholders and other interested parties including policymakers, business leaders, regulators and investors. These are informed through our daily engagement with companies large and small, across all industries and in the private and public sectors.

Recent publications relevant to the NHS are shared opposite:

### Perspectives: Health & Social Care - The great integration challenge

Bringing health and social care closer together has been a policy ambition for decades, yet it continues to be a challenge. This new piece discusses some of the key factors that affect integration and what can realistically be achieved. Read the full blog post here:

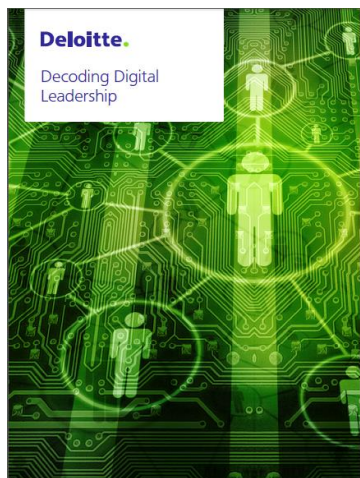
<http://www2.deloitte.com/uk/en/pages/public-sector/articles/the-great-integration-challenge.html>

### Perspectives: The public sector's talent retention challenge – How can a talent drain be avoided?

Although global governments are increasingly conscious of the value of skills, the UK's public sector workforce has been hit hard by austerity. Job losses, low morale and pay freezes have all fuelled concerns of a potential drain. Read the full blog here:

<http://www2.deloitte.com/uk/en/pages/public-sector/articles/public-sectors-talent-retention-challenge.html>

### Publications



### Decoding Digital Leadership Surviving Digital Transformation

Digital transformation is a hot topic in government. The 2010 Spending Review mentioned the word 'digital' only four times in its reform plans, while the 2015 Review mentioned it 58 times. With that context, are senior leaders across government setting their organisations up for digital success?

Digital transformation requires top to bottom organisational transformation, which requires leaders who are willing and able to leverage digital to innovate, fail fast and drive value in an ambiguous context. Are your leaders equipped to drive digital transformation?

Download a copy of our publication here:

<http://www2.deloitte.com/uk/en/pages/public-sector/articles/decoding-digital-leadership.html>



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