



Scott-Moncrieff
business advisers and accountants

NHS Lothian

Audit Committee Progress Report

April 2018

Introduction

Purpose

This progress report is presented to NHS Lothian's Audit and Risk Committee to update the committee on our progress in delivering our responsibilities as external auditors.

We also use the paper to provide an update on key sector developments, including recent Audit Scotland reports.

We welcome any feedback on the content and format of this report.

Chris Brown

Partner and Engagement Lead

April 2018

This paper is structured as follows:

1

Progress against annual plan

A summary of our progress to date, including an updated assessment of significant audit risks.

2

Assessing impact

Our assessment of the progress and impact of audit recommendations made within our 2016-17 reports.

3

Sector update

Our summary of key developments and relevant national publications in the period October 2017 – March 2018:

- NHS Tayside: Section 22 report on financial sustainability
- Audit Scotland's Good Practice Note on Improving the quality of NHS annual accounts – reporting financial performance
- NHS Tayside: Scottish Government Investigation on use of eHealth funds
- Scotland's Cyber Resilience Strategy and Action Plan

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Our progress to
31 March 2018

Progress against our plan

The table below summarises our progress against the external audit plan.

2017-18 area of work	Complete	Date planned	Comments
<p>Annual audit plan A detailed audit plan to those charged with governance, setting out our proposed approach and identification of key audit risks.</p>	✓		The External Audit Plan was approved by the Audit and Risk Committee on 26 February 2018. This set out the various strands of our work in detail and the related timetable for delivery.
<p>Interim audit work Review of key systems and processes to underpin the financial statements and planning/initial work on wider scope dimensions.</p>	✓		We undertook preparatory work for our final accounts audit, bringing forward some aspects of testing to help the efficiency and effectiveness at the final audit visit. Our initial work on wider scope dimensions identified no reportable issues and will continue up to and including June 2018.
<p>National Fraud Initiative 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 overseen by the Cabinet Office, to identify fraud and error. NFI produces 'matches' by using data matching to compare a range of information held on bodies' systems to identify potential fraud or error. Bodies investigate these matches and record appropriate outcomes based on their investigations.</p> <p>The most recent NFI exercise commenced in October 2016 and as part of our 2016/17 audit we monitored the Board's participation in NFI, with further review performed in February 2018.</p>	✓		<p>We found the arrangements for participation in the NFI were satisfactory. In February 2018, 970 recommended matches had been actioned (94% of the total) and plans were in place to complete all investigations by end March 2018. No areas of concern have been highlighted in any of the matches identified. We also noted that Board has control processes over duplicate payments out with the NFI process. The Accounts Payable department run a "duplicate payment" report every day using Business Objects.</p> <p>Every potential duplicate is investigated and (where necessary) corrective action is taken immediately, and in many cases before the actual payment is made to the supplier. As a result of this control, we note that the Board has not found a true duplicate payment through the NFI process.</p>
<p>Review of cyber security The Scottish Government is developing a Cyber Resilience Framework for Scottish Public Bodies and published a Cyber Resilience Action Plan in November 2017. This includes a number of actions for public bodies to ensure they meet the baseline level of cyber security standards (Refer to Section 3 of this report for further detail).</p>		May 2018	<p>Our Specialist IT auditors will review the Board's cyber security arrangements including the steps they have taken to ensure compliance with the Scottish Government's cyber resilience framework.</p> <p>The results of this work will be reported within our annual audit report output.</p>
<p>Internal Audit Each year we reflect on the work of internal audit and consider any implications for our external audit work.</p>		Ongoing	We will take cognisance of internal audit to ensure efficient use of total audit resources. This includes review of reports relevant to the 2017-18 financial statements audit, including Fixed Assets and Financial Ledger.
<p>Final audit / annual accounts The audit of the annual accounts of NHS Lothian 2017/18, leading to the overall annual audit opinion.</p>		May & June 2018	Detailed audit of the financial statements and review of the wider annual accounts of NHS Lothian. We will also conclude our work on the wider dimensions of audit scope, in line with Audit Scotland's Code of Audit Practice.

Key financial systems: Our risk assessment

The External Audit Plan was approved by the Audit and Risk Committee on 26 February 2018. We have used our interim fieldwork to gain a detailed understanding of the key financial systems. We have identified no additional significant risks as a result of this work.

Audit area	Linked to area of significant risk in our plan?	Our assessment
Nominal ledger	✓	We have considered the key accounting and internal financial controls over the nominal ledger. We consider these to be appropriately designed and operating effectively. We will also consider national assurance reports over this area, once produced.
Income and receivables	✓	We have documented the key accounting and internal financial controls for the Board's material income streams. Walkthrough testing has been performed to ensure that the controls are operating as expected. Our work did not identify any significant deficiencies in the adequacy or design.
Payroll		Year to date controls testing has been performed on payroll including starters, leavers, amendments to the payroll masterfile and the payment of expenses. We consider these to be appropriately designed and operating effectively.
Expenditure and payables	✓	We have documented the key accounting and internal financial controls over non-pay expenditure and payables, including procurement. We consider the controls to be appropriately designed, with no reportable weaknesses identified.
Family Health Services		We have considered the key accounting and internal financial controls over family health services income and expenditure including: <ul style="list-style-type: none"> • General Medical Services (GMS) • General Pharmaceutical Services (GPS) • General Dental Services (GDS) • General Ophthalmic Services (GOS) We consider these to be appropriately designed with no reportable issues arising.
Property, Plant and Equipment	✓	NHS Lothian uses the Real Asset Management (RAM) system to record all assets in the Balance Sheet. We have considered the key controls over property, plant and equipment, including the Property and Asset Management Implementation Plan, and supporting detailed list of approved projects. Our controls testing has considered additions, disposals and the monthly reconciliation process. We consider these to be appropriately designed and operating effectively. The revaluation and asset verification processes will be reviewed in May 2018 to support our opinion, as these are annual processes.
Compliance with Scottish Government Circulars		We have documented the key controls in place to ensure the Board promptly identifies and implements relevant circulars. No concerns were highlighted as a result of this review.

Update against Significant Audit Risks

This section provides an updated position against the Significant Audit Risks identified in the External Audit Plan. We have not identified any new significant audit risks, although we note and will maintain a watching brief in relation to the Board's work to respond to challenges in Unscheduled Care pressures.

Significant risk within Annual Audit Plan	Our progress to date
<p>1. Capital Transactions</p> <p>The Board holds a significant amount of high value estate (net book value of land and buildings was £688.557million at 31 March 2017). The Board values its assets on a five year cycle, with an element of the estate being subject to valuation each year. In addition, the Board expects to make significant capital additions during 2017/18. Additions are expected through traditional procurement routes (£50.087million) as well as through Hub projects (£25.057million as outlined in significant risk 2 below).</p> <p>Given the value of assets held, and the scale of the in-year capital transactions expected, any misstatement in the accounting for assets could potentially result in a material misstatement in the financial statements.</p>	<p>We have met with the capital accounting team to gain an understanding of the expected capital transactions during 2017/18.</p> <p>We have documented our understanding of the key controls with respect of capital transactions and have not identified any significant deficiencies.</p> <p>Internal audit has also conducted a review of fixed assets during the year and identified only one low risk finding.</p> <p>We will complete our testing on these areas as part of our final audit work, to ensure sufficient and appropriate coverage from across the entire financial year.</p>
<p>2. PFI and related assets</p> <p>The Board has a range of legacy facilities which were delivered through the Public-Private Partnerships (PPP) / Private Finance Initiatives (PFI), including The Royal Infirmary of Edinburgh, Midlothian Community Hospital, Ellens Glen and Findlay House. The cumulative estimated base capital value of these agreements is in excess of £200million.</p> <p>The Royal Edinburgh Hospital (REH) Phase 1 new Hub facilities became operational in 2016/17 at a value of £38.382 million. The contract agreed over this Hub asset runs until December 2041 at which point ownership of the facilities will transfer to the Board. The Board expects further Hub developments at REH in 2017/18 along with a number of other Hub developments delivered through the Partnership Centre Bundle. Total capital additions on Hub projects are expected to be £25.057million during the year.</p> <p>Due to the complexity of accounting and the high value of the transactions, there is a risk that the Board's financial statements do not show the correct accounting entries and related commitments, and that the unitary payments in relation to these facilities are not correctly accounted for.</p>	<p>We have also undertaken assets systems work and found no reportable issues, as noted in the previous section.</p>
<p>3. Revenue Recognition</p> <p>Under ISA 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 in a way that materially misstates the Board's financial performance.</p>	<p>We have documented the key accounting and internal financial controls for the Board's material income streams. Our work did not identify any significant deficiencies in the adequacy or design of these controls.</p>


Significant risk within Annual Audit Plan	Our progress to date
<p>4. Risk of Fraud in the recognition of expenditure</p> <p>The FRC published a revised Practice Note 10 which applies to the audit of financial statements of public sector bodies in the UK, for periods commencing after June 2016. The Practice Note recognises that most public sector bodies are net spending bodies and notes that there is an increased risk of material misstatement due to improper recognition of expenditure. In line with the practice note, our presumption is that the Board could adopt accounting policies or recognise expenditure in a way that materially misstates the Board's financial performance.</p>	<p>We have documented the key accounting and internal financial controls over the Board's expenditure. We have also reviewed the investigation and reporting of matches identified as part of the National Fraud Initiative.</p> <p>Our work did not identify any significant deficiencies in the adequacy or design of these controls.</p>
<p>5. Management Override</p> <p>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 ISA 240.</p>	<p>We have documented the key accounting and internal financial controls for the Board's financial ledger. Our work did not identify any significant deficiencies in the adequacy or design of these controls.</p>
<p>6. Financial Sustainability</p> <p>The Board's Local Delivery Plan sets out a very challenging outlook for the Board's financial position and the Board is expected to make substantial recurring efficiency savings each year. There is a risk that delivery of the Board's efficiency savings plans are at the detriment of services and/or on-going financial health.</p> <p>Projections for 2018-19, as part of the five year financial outlook, highlight a financial gap (before recovery actions) of £48.3million. Financial recovery actions of £20.5million have been identified, leaving a gap after recovery actions of £27.8million. The Board recognises that given the scale of the remaining gap, and the increasing reliance on non-recurring resources, it will be necessary to develop scenarios regarding the choices the Board may be required to make in order to achieve a balanced position for 2018/19.</p>	<p>The most recent update to the Board's Finance and Resources Committee in March 2018 outlines an improving financial position, but an outstanding projected financial gap after recovery actions of £21.4 million in 2018-19, rising to £131 million in 2022-23.</p> <p>The financial outlook does not yet include scenario plans. We also note that while national and regional planning is underway to deliver a financial framework for the medium to long term, there is not yet a clear approach to deliver sustainability across the sector.</p>
<p>7. Waiting Times</p> <p>The Board received a report on the Emergency Access Standard: Review of Performance Reporting Compliance at its meeting on 6 December 2017. The report provided an update on progress with the investigation into specific concerns raised under the Board's whistleblowing arrangements about the alleged mismanagement of waiting times reporting.</p> <p>The report noted that NHS Lothian was not consistently complying with the guidance set out in the A&E Data Recording reference manual (2013), the Scottish Government clarification guidance on ambulance waits (2015) and the Board's own standard operating procedures. The Cabinet Secretary for Health and Wellbeing has commissioned an external investigation into the concerns, which we anticipate will be available in April 2018.</p>	<p>The independent review by the Scottish Academy of Medical Royal Colleges, Chaired by Professor Derek Bell, was expected to be considered by the Board at its April meeting, but the report was not finalised. We will therefore review the findings, and the Board's response, as part of our final accounts visit in May 2018.</p> <p>We note that the Board's work to implement internal audit recommendations, and the organisational development programme to support individual behaviours, is ongoing.</p>

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Audit impact

Follow up of prior year recommendations

We have used our interim visit to follow up the progress against our recommendations from 2016-17, and our assessment of the impact on the effectiveness the Board's governance, risk and control arrangements.

2016-17 recommendation	Original Management Response	Comments	Audit Update
<p>Observation A medium term financial strategy is essential to demonstrate how financial sustainability can be achieved. The Board faces a significant recurring deficit position in the period to 2021-22, with no clear and detailed plans yet in place to bridge the financial gap.</p> <p>Recommendation The Board should continue to work with its partners to identify a clear approach to financial sustainability over the medium term.</p>	<p>The Board recognises the critical importance of its financial planning strategy and will continue to work with all relevant partners.</p> <p>Responsible officer: Director of Finance</p>	<p>In progress</p> 	<p>An outline financial strategy was presented to the Finance and Resources Committee in May 2017. Updates have subsequently been reported at each meeting.</p> <p>The latest projections as reported in March 2018 show the Board having a financial gap of £131m by 2022/23.</p> <p>A four-tiered approach has been developed to help achieve financial sustainability. This approach reflects the cross-sector work required at both regional and national levels.</p> <p>A Sustainability and Value group has been established to review progress on all programmes supporting financial sustainability and recovery.</p>

Follow up of prior year recommendations

2016-17 recommendation	Original Management Response	Comments	Audit Update
<p>Observation We identified four non-financial interests which had not been disclosed in the register of interests during 2016/17 (three charity trusteeships and one appointment resulting from another public sector role).</p> <p>We are not aware of any indication that there has been an actual conflict during the year in relation to these interests.</p> <p>Recommendation To ensure that the Board is seen to avoid even the perception of a conflict of interests, all members' interests must be disclosed in full. To support full disclosure the Board should ensure that all relevant members and officers understand the full range of interests that must be declared and the timeliness of this disclosure.</p>	<p>A detailed section on Declaration of Interest will be included in the Interactive Board Member Induction pack being updated and prepared for new Board Members. The cover letter will draw specific attention to requirements around declaration of interest. The Induction pack will be issued to existing as well as new Board Members. Issues around declaration of interest will also be covered in the more formal Induction process that is being prepared for new Board Members.</p> <p>Responsible officer: Corporate Services Manager</p>	<p>In progress</p> 	<p>The Head of Corporate Governance reorganised the Board Members Handbook to make it more accessible and understandable. Guidance has also been published on the Board's website that contains links to relevant internal documents and external sources where appropriate. In addition, the induction process for new board members has been updated to highlight the importance of declaring interests.</p> <p>We reviewed controls over related party transactions as part of our interim audit and found them to be reasonable and appropriate. We will review declarations of interest, and any related party transactions there have been, in detail as part of our final audit.</p>

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Sector update

In this section we present our summary of recent sector reports and developments including:

- NHS Tayside: Section 22 report on financial sustainability
- Audit Scotland's Good Practice Note on Improving the quality of NHS annual accounts – reporting financial performance
- NHS Tayside: Scottish Government Investigation on use of eHealth funds
- Scotland's Cyber Resilience Strategy and Action Plan

NHS Tayside: Financial Sustainability

Audit Scotland issued a Section 22 report on NHS Tayside to the Scottish Parliament in October 2017 to draw attention to the scale of the challenge that NHS Tayside continues to face in meeting its financial targets. NHS Tayside has needed financial assistance for five successive years in order to achieve in-year financial balance.

The Board is projecting a funding gap of £49.8 million in 2017-18. The Board plans to achieve efficiency savings of £45.8 million, with the balance of £4 million funded through additional brokerage. The Board has a total of £33.2 million of outstanding brokerage to repay.

In April 2017, the Scottish Government appointed an independent Assurance and Advisory Group to provide scrutiny and challenge on the delivery of the operational plan for 2017-18 and the five year transformation programme. In June 2017, the Group's Staging report highlighted that it was not confident that the board can return to financial balance within 5 years, and that the £4 million brokerage is likely to be an underestimate.

The Staging Report also highlighted the results of benchmarking with other Scottish territorial Health Boards and found that NHS Tayside's total staff complement is high - representing 9.3% of the NHS Scotland total - compared with its NRAC target share of 7.85%. This finding is consistent across most staff groups, clinical and non-clinical, hospital and community based.

A benchmarking review was also undertaken recently by NHS Tayside based on information for 2015/16 provided by the NHS Scotland Information Services Division (ISD). The report compared the cost of service provision within NHS Tayside with the other teaching boards (NHS Greater Glasgow and Clyde, NHS Grampian and NHS Lothian) and highlighted a number of areas where the operating costs of NHS Tayside were higher than the peer group.

For example, in 2015-16, in terms of financial performance:

- NHS Tayside's costs per in-patient week of £4,677 were 19% higher than the lowest of the teaching boards and 14% above the second highest board
- At 9.7% of NHS Scotland's total spend on energy, NHS Tayside energy cost was 27% higher than its share of funding, highlighting the challenges regarding operating from many dispersed sites
- Of the four teaching boards, NHS Tayside was the only Board to incur expenditure on primary care prescribing in excess of available resources.

The report noted that savings of £4 million could have been achieved if expenditure had been contained within its NRAC population share of funding.

The Section 22 report is available on Audit Scotland's website at <http://www.audit-scotland.gov.uk/report/the-201617-audit-of-nhs-tayside-financial-sustainability>

Financial Reporting in the NHS

Audit Scotland's Professional Support Unit issued a good practice note in November 2017 to help NHS boards improve the reporting of financial performance and outturn in their performance reports. The guidance is based on review of all Scottish boards' 2016/17 disclosures to identify instances of good practice and areas for improvement.

The report highlighted NHS Lothian's approach to disclosing the impact of resource limits on cash as an area of good practice, but included an improvement checklist for all boards to consider, including:

- Reporting the cumulative under/overspend as part of the memorandum for in year outturn to provide the user with a clear link back to the financial performance?
- Provide a clear explanation of the financial performance resource limits and the purpose of the memorandum for in year outturn
- Ensure narrative descriptions are consistent with the amounts being described.

The Good Practice Note is available on Audit Scotland's website at the link below:

http://www.audit-scotland.gov.uk/uploads/docs/um/gp_improving_quality_nhs_accounts_reporting.pdf

NHS Tayside: eHealth Funding

In March 2018, the Scottish Government published the results of an independent review into eHealth Funding between eHealth, NHS National Services Scotland and NHS Tayside between 2012 and 2018.

The investigation related to the eHealth programme resource allocation transactions from NSS to NHS Tayside through the Scottish Government's revenue allocation process, and ranged in value from £0.538 million to £2.582 million over the time period. In 2017/18 the financial impact on NHS Tayside is £5.3million (the unreturned balance in 2016/17 and the 2017/18 funds).

The review found a lack of openness, governance and wider transparency over the use and reporting of eHealth funds.

From 2012, NHS Tayside were "holding" money related to future eHealth programme activity, which was given to NHS Tayside by the Scottish Government. From 2012 to 2015 the money "held" by NHS Tayside was returned the following year through RRL transactions. From 2016/17 larger sums were involved and NHS Tayside were informed they did not need to pay back the 2016/17 monies during 2017/18 due to overall eHealth slippage. In 2017/18 NHS Tayside requested a further sum of 2.7million, in addition to the sum they were still "holding".

In 2016/17 NHS Tayside effectively used the money they were holding (around £2 million) to offset general expenditure in year, which supported them in showing a more favourable financial position. As a result this misrepresented NHS Tayside's financial position.

In 2017/18 the £5.3 million of eHealth funding was required in order for NHS Tayside to achieve the forecasted £5 million deficit in year, which was being reported to Scottish Government.

Ultimately this arrangement supported NHS Tayside given their financial challenges but also the eHealth programme administered by NSS, as slippage could then be carried forward for future use eHealth programme use.

Scotland's Cyber Resilience Strategy

Cyber incidents pose an increasing threat to all public sector organisations. Incidents over the last year have shown that they can significantly disrupt services. As public bodies embrace the opportunities that digital technologies bring it is increasingly important that actions are taken to manage and protect services from the threats and vulnerabilities that these technologies can also bring.

In light of the recent cyber incidents the Scottish Government has produced new guidance for public bodies. This builds on Scotland's cyber resilience strategy (Safe, Secure and Prosperous) and provides more concrete actions for bodies to take, and develops a monitoring framework for the Scottish Government.

The Scottish Government guidance can be found here:

[Public Sector Action Plan 2017-18](#)

[Implementation toolkit](#)

Appendix A of the implementation toolkit sets out how the action plan applies to public bodies. The action plan sets out a number of requirements for public bodies, with the intention to develop a Scottish Public Sector Cyber Resilience Framework by end June 2018. It is expected that the requirements will be written into the Scottish Public Finance Manual once finalised in the framework.

The Scottish Government guidance highlights that the National Cyber Resilience Leaders Board consider cyber resilience to be as much a cultural issue as a technical one. They view it as vital that Scotland's public bodies understand and manage the cyber threat at Board/Senior management level, and take action to promote a culture of cyber security and awareness at all levels of the organisation.

The Scottish Government has also established a Public Sector Cyber Catalyst Scheme. A number of public bodies, including NHS Lothian, have committed to acting as leaders in respect of cyber resilience. They will help 'catalyse' learning and action by other public sector organisations over time.

During 2017-18, each public sector organisation needs to take significant action to prepare and confirm compliance to the Scottish Government. We have committed to reviewing NHS Lothian's progress against the action plan in May 2018, and will report the findings within our annual report.



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