



Scott-Moncrieff
business advisers and accountants

NHS Lothian

**2017-18 Annual Audit Report to the Board
and the Auditor General for Scotland**

June 2018

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Key messages

Annual accounts

The annual accounts for the year ended 31 March 2018 were approved by the Board on 27 June 2018. We have reported within our independent auditor's report an unqualified opinion on the annual accounts, regularity and on other prescribed matters.

The annual accounts and supporting schedules were of a generally good standard. Our thanks go to staff at NHS Lothian for their assistance with our work.

Wider scope audit

Financial Sustainability

NHS Lothian has made progress to develop an approach to achieve financial sustainability in 2017-18, including greater regional working. However, the Finance and Resources Committee has only been able to take limited assurance on the long term financial sustainability of the Board.

The Annual Operational Plan outlines the potential impact on operational performance of different financial scenarios but more work is needed to provide the Board with options on how the required level of savings can be delivered.

Financial management

All key financial targets were met in 2017-18. The revenue resource limit was underspent by £0.279m (0.02%) and a breakeven position was reported against the capital resource limit.

Savings of over £23m were delivered during 2017-18, but the Board increasingly relied on non-recurring savings, which is not sustainable in the longer term.

Financial management is effective but we identified opportunities to enhance the clarity of financial monitoring reports.

Governance & transparency

The Board has good governance arrangements in place and we found that openness arrangements compare well against the sector.

The Board responded quickly to a significant whistleblowing allegation relating to waiting times at emergency departments. Scottish Government published the results of an independent external review on 26 June 2018. We will review the Board's progress against the recommendations during our 2018-19 audit.

Value for money

Performance against targets deteriorated in 2017-18, in the context of significant financial and demographic challenges.

The Board has a strong focus on the Quality Management System and can point to significant improvements in patient outcomes and the reduction of future demand.

Conclusion

This report concludes our audit for 2017-18. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK) (ISA(UK)) and Ethical Standards.

Scott-Moncrieff, June 2018

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Introduction

This report is presented to those charged with governance and the Auditor General for Scotland and concludes our audit of NHS Lothian for 2017/18.

We carry out our audit in accordance with Audit Scotland's Code of Audit Practice (May 2016). This report also fulfils the requirements of International Standards on Auditing (UK) 260: Communication with those charged with governance.

At NHS Lothian, we have designated the Audit and Risk Committee as "those charged with governance".

Introduction

1. Audit Scotland appointed Scott-Moncrieff as auditor to NHS Lothian for the five year period 2016-17 to 2020-21.
2. The scope of the audit was set out in our External Audit Annual Plan, which was presented to the Audit and Risk Committee at the outset of our audit. The core elements of our work include:
 - an audit of the 2017-18 financial statements and related matters;
 - consideration of the wider dimensions of public audit work, as set out in Exhibit 1; and
 - any other work requested by Audit Scotland (for example, input into performance audit work).

Exhibit 1: Audit Dimensions within the Code of Audit Practice



Source: Audit Scotland Code of Audit Practice, May 2016

3. NHS Lothian is responsible for preparing an annual report and accounts which show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the annual report and accounts or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
 4. This report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding appropriate actions. Each recommendation has been given a grading to help the Board assess its significance and prioritise the actions required.
 5. We discussed and agreed the content of this report with the Director of Finance. We would like to thank all members of the Board's management and staff who have been involved in our work for their co-operation and assistance during our audit work.
- ### Confirmation of independence
6. International Standards on Auditing in the UK (ISAs (UK)) require us to communicate on a timely basis all facts and matters that may have a bearing on our independence.
 7. We confirm that we have complied with Financial Reporting Council's (FRC) Revised Ethical Standard (June 2016). In our

professional judgement, the audit process is independent and our objectivity has not been compromised in any way. In particular, there have been no relationships between Scott-Moncrieff and the Board or senior management that may reasonably be thought to bear on our objectivity and independence.

Adding value through the audit

8. All of our clients demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the Board through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Board promote improved standards of governance, better management and decision making and more effective use of resources.
9. As part of our 2017-18 audit we added value to the Board and Audit Scotland in a range of ways:

Regular contact and liaison with the Board

- We invest senior time to ensure that we keep up to date with significant issues, in part through our membership of the NHS Technical Accounting Group and Sub group, and we share that knowledge across our team and with the Board.
- We maintain regular dialogue with the Director of Finance and her team, including early discussion on potential audit and accounting issues.
- We support the Board's finance team through open discussion of technical accounting matters (such as asset and

provisions accounting) and the sharing of best practice from across the sector.

Providing assurance to the Board and Audit Scotland

- We will meet the deadlines set out in Audit Scotland's annual planning guidance in respect of the delivery of audit plans, independent auditor reports and annual reports.

Feedback

10. Any comments you may have on the service we provide, the quality of our work and our reports would be greatly appreciated at any time. Comments can be reported directly to the audit team or through our online survey: www.surveymonkey.co.uk/r/S2SPZBX
11. While this plan is addressed to the Board, it will be published on Audit Scotland's website www.audit-scotland.gov.uk



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Annual report and accounts

NHS Lothian's annual report and accounts is the principal means of accounting for the stewardship of its resources and its performance in the use of those resources.

In this section we summarise the findings from our audit of the 2017/18 annual accounts.

Annual report and accounts

The annual report and accounts for the year ended 31 March 2018 were approved by the Board on 27 June 2018. We have reported unqualified opinions within our independent auditor's report. We did not identify any significant adjustments to the unaudited annual report and accounts. The Board reported a small surplus in 2017-18 of £0.279 million.

NHS Lothian has good administrative processes in place to prepare the annual report and accounts and the required supporting working papers.

Overall conclusion

An unqualified audit opinion on the annual accounts

12. The annual report and accounts for the year ended 31 March 2018 were considered and approved by the Audit and Risk Committee on 18 June 2018 and thereafter by the Board on 27 June 2018. We have reported within our independent auditor's report:

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

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

Good administrative processes were in place

14. We received unaudited annual accounts and supporting papers for the majority of expected

areas in line with our agreed audit timetable. Our thanks go to the team at NHS Lothian for their assistance.

15. The annual report and accounts will be submitted to the Scottish Government and Auditor General for Scotland by the 30 June 2018 deadline.

Our assessment of risks of material misstatement

16. The assessed risks of material misstatement described in Exhibit 2 are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the audit team. Our audit procedures relating to these matters were designed in the context of our audit of the annual accounts as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the annual accounts is not modified with respect to any of the risks described in Exhibit 2.

Exhibit 2: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

1. Capital transactions

The Board holds a significant amount of high value estate (net book value of land and buildings was £688.557 million 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. At time of writing, additions are expected through traditional procurement routes (£50.087million) as well as through Hub projects (£25.057 million as outlined in significant risk 2 below).

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.

Excerpt from the 2017-18 External Audit Plan

17. We have reviewed capital transactions to ensure that they have been accounted for in line with the FReM and the Board's accounting policies. We have gained assurance over the completeness and accuracy of these transactions and are satisfied that the carrying value of the Board's estate in the financial statements is materially correct.

2. PFI and related assets

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.

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. Total capital additions on Hub projects are expected to be £25.057million during the year (at time of writing).

In practice, the accounting arrangements for the REH development, and the other Hub developments, are generally consistent with those used for the Board's legacy PPP/PFI assets. 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.

Excerpt from the 2017-18 External Audit Plan

18. We have reviewed the Board's PPP/PFI accounting and related commitment disclosures against the requirements of the FReM, the Manual and against supporting contracts. We have also reviewed relevant aspects of the transactions against the NHS Scotland Capital Accounting Manual.
19. During 2017-18 phases 1 & 2 of the East Lothian Community Hospital project were brought into operation in addition to three other PFI projects at a capital value of £32million. Through our work we are satisfied that the accounting entries for these and existing projects present a true and fair view of the PFI assets and related commitments.

3. Revenue recognition

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.

Excerpt from the 2017-18 External Audit Plan

20. At the planning stage of our audit, we reported that we did not believe the risk of fraud in revenue recognition was material to the annual accounts and we therefore rebutted this risk. This position has been reviewed throughout the audit and this conclusion has remained appropriate. Our audit work has gained assurance over revenue recognised by the Board.

4. Risk of fraud in the recognition of expenditure

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.

Excerpt from the 2017-18 External Audit Plan

21. We evaluated each material type of expenditure stream and documented our conclusions. We have gained reasonable assurance on the completeness and occurrence of expenditure and are satisfied that expenditure is fairly stated in the financial statements. To inform our conclusion we carried out testing to confirm that NHS Lothian's policy for recognising expenditure is appropriate and has been applied consistently throughout the year.

5. Management Override

In any organisation, there exists a risk that management have the ability to process transactions or make adjustments to the financial records outside the normal financial control processes. Such issues could lead to a material misstatement in the annual accounts. This is treated as a presumed risk area in accordance with ISA (UK) 240 – *The auditor's responsibilities relating to fraud in an audit of financial statements*.

Excerpt from the 2017-18 External Audit Plan

22. We have not identified any indications of management override in the year. We have reviewed the Board's accounting records and obtained evidence to ensure that transactions outside the normal course of business were valid and accounted for correctly. We have also reviewed management estimates and the journal entries processed in the period and around the year end. We did not identify any areas of bias in key judgements made by management and judgements were consistent with prior years.

Other risk factors

23. In 2017-18, the presentation of the statement of comprehensive net expenditure (SoCNE) was

amended, in line with the NHS Accounts Manual. This was done to improve clarity for the users of the accounts and ensure compliance with the HM Treasury Government

Financial Reporting Manual (the FReM) and accounting standards. The comparative information in respect of 2016-17 is presented in the new format in the SoCNE. No further retrospective restatements were required.

Our application of materiality

24. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the item. This means that different materiality levels will be applied to different elements of the annual accounts.
25. Our initial assessment of materiality was £22 million. On receipt of the 2017-18 draft accounts, we reassessed materiality and increased this threshold to £24 million. Our assessment of materiality is set with reference to the RRL (1.5% of RRL). We consider this to be the principal consideration for the users of the accounts when assessing the financial performance of NHS Lothian. We consider that our updated assessment has remained appropriate throughout the audit.

Performance materiality

26. Performance materiality is the amount set by the auditor at less than overall materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of the uncorrected and undetected misstatements exceed materiality for the financial statements as a whole.
27. We set a performance (testing) materiality for each area of work which was based on a risk assessment for the area. We perform audit procedures on all transactions and balances that exceed our performance materiality. This means that we perform a greater level of testing on the areas deemed to be of significant risk of material misstatement. Performance testing thresholds used are as set out below:

| Area risk assessment | Weighting | Performance materiality |
|----------------------|-----------|-------------------------|
| High | 40% | £9.6million |
| Medium | 55% | £13.2million |
| Low | 75% | £18million |

28. We agreed to report on all material misstatements and uncorrected misstatements with a value in excess of £230,000, as well as other misstatements below that threshold that, in our view, warranted reporting on qualitative grounds.

Audit differences

29. We are pleased to report that there were no material adjustments to the unaudited annual accounts. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual accounts.
30. We also identified an unadjusted error which is not considered material to the annual accounts. This relates to accruals against Scottish Government allocations where expenditure is spread over more than one year. The issue therefore spans and has impact over different accounting periods. This is set out further in Appendix 2. This has been reported to the Director of Finance and is included as an appendix to the letter of representation and this report. The letter covers a number of issues and we have requested that it be presented to us at the date of signing the annual accounts.

An overview of the scope of our audit

31. The scope of our audit was detailed in our External Audit Plan, which was presented to the Audit and Risk Committee in February 2018. The plan explained that we follow a risk-based approach to audit planning that reflects our overall assessment of the relevant risks that apply to the Board. This ensures that our audit focuses on the areas of highest risk.
32. At the planning stage we identified the significant risks that had the greatest effect on our audit. Audit procedures were then designed to mitigate these risks.
33. Our standard audit approach is based on performing a review of the key financial systems in place, substantive tests and detailed analytical review. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit manager and audit partner. In performing our work we have applied the concept of

materiality, which is explained earlier in this report.

Group accounts

34. The Board prepares its annual report and accounts on a group basis. The group consists of the Board, the Lothian Health Board Endowment Fund and the four integration joint boards (Edinburgh, West Lothian, Midlothian and East Lothian).
35. The Endowment fund is fully consolidated. The joint boards are deemed joint ventures with the respective local authority and accounted for under the equity method. We do not consider the consolidated entities to be of individual financial significance to the group or, due to their specific nature or circumstances, likely to include significant risks of material misstatement of the group financial statements.
36. In line with our annual audit plan we performed analytical procedures at the group level and testing sufficient to give us assurance over the valuation of endowment fund investments. We reviewed the consolidation entries made within the group accounts and confirmed those entries back to audited financial statements (the endowment fund) and external confirmations (from integration joint boards). We also discussed and agreed with the board some narrative to explain the basis of IJB transactions and the flow of funding, including in response to IJB draft accounts returns received.
37. In addition, we have reviewed the outcomes of the endowment fund audit and concluded that there are no issues to raise with regard to recent Scottish Government correspondence on the use of endowment funds.

Other matters identified during our audit

38. "Other information" in the annual report and accounts comprises any information other than the financial statements and our independent auditor's report. We do not express any form of assurance conclusion on the "other information" except as specifically stated below.

The performance report

39. The performance report provides information on the entity, its main objectives and strategies and the principal risks that it faces. It comprises an overview of the organisation and a detailed summary of how the entity measures performance.
40. We have concluded that the performance report has been prepared in accordance with directions from Scottish Ministers and is consistent with the financial statements.

The accountability report

41. The accountability report is required to meet key parliamentary accountability requirements and comprises three sections: a corporate governance report (including the governance statement), a remuneration and staff report; and a parliamentary accountability report.
42. We consider the Governance Statement to be in compliance with directions made by the Scottish Ministers and the content is consistent with the information gathered during our audit work. This includes specific disclosures in relation to waiting times reporting problems.
43. We have obtained adequate evidence that the information provided in the remuneration and staff report is in agreement with accounting records and has been prepared in line with ministerial guidance.

Regularity

44. We have planned and performed our audit recognising that non-compliance with statute or regulations may materially impact on the annual report and accounts. We did not identify any instances of irregular activity.

Qualitative aspects of accounting practices and financial reporting

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

| Qualitative aspect considered | Audit conclusion |
|---|---|
| The appropriateness of the accounting policies used. | The accounting policies, which are disclosed in the annual accounts, are in line with the NHS Accounts Manual and are considered appropriate to NHS Lothian. |
| The timing of the transactions and the period in which they are recorded. | We did not identify any concerns over the timing of transactions or the period in which they were recognised. |
| The appropriateness of the accounting estimates and judgements used. | The accounting estimates and judgements used in preparing the financial statements are considered appropriate. The principal areas of estimates and judgements have been: property valuations, asset depreciation rates and the valuation of provisions. Where appropriate, the Board has utilised the work of independent experts or industry practice to support the estimates made. We have had extensive and ongoing discussions to challenge management in these judgements. |
| The appropriateness of the going concern assumption | We have not identified any uncertainties, including any significant risk or required disclosures, which should be included within the financial statements. |
| The potential effect on the annual accounts of any uncertainties, including significant risks and related disclosures that are required. | We have not identified any uncertainties, significant risk or required disclosures, which should be included in the financial statements. |
| The extent to which the annual accounts have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed. | From the testing performed, we identified no significant, unusual transactions in the period. |
| Apparent misstatements in the annual report or material inconsistencies with the accounts. | The management commentary contains no material misstatements or inconsistencies with the financial statements. |
| Any significant annual accounts disclosures to bring to your attention. | There are no significant annual accounts disclosures that we consider should be brought to your attention. All the disclosures required by relevant legislation and applicable accounting standards have been made appropriately. |
| Disagreement over any accounting treatment or annual accounts disclosure. | While disclosure and presentational adjustments were made during the audit there was no material disagreement during the course of the audit over any accounting treatment or disclosure. |
| Difficulties encountered in the audit. | No significant difficulties were encountered during the audit. |



3

Financial sustainability

Financial sustainability looks forward to the medium and longer term to consider whether NHS Lothian is planning effectively to continue to deliver its services or the way in which they should be delivered.

Financial sustainability



NHS Lothian has made good progress in developing a medium to long term financial strategy, including working with regional partners, but now needs to set out clearer plans for where and how savings will be generated.

The Annual Operational Plan for 2018-19 sets out a remaining funding gap of £21.4 million. The plan also makes effective use of scenario planning and options to model the financial impact on operational performance.

Introduction

46. Financial sustainability looks forward to the medium and longer term to consider whether the Board is planning effectively to continue to deliver its services or the way in which they should be delivered.

Significant audit risk

47. Our audit plan identified a significant risk in relation to financial sustainability under our wider scope responsibilities:

Brokerage and financial sustainability

The Board's Local Delivery Plan covers a three year period, and is supported by a five year capital plan. The LDP 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.

At time of writing, 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.

Excerpt from the 2017-18 External Audit Plan

48. For 2018-19, the Board is required to produce an Annual Operational Plan, replacing the LDP. The Financial Plan presented to the Finance and Resources Committee and the Board, in April 2018, outlines an updated financial gap of £21.4 million. Our work on the financial projections from 2018-19 onwards is set out below and notes ongoing challenges in achieving the recurring savings targets and medium to longer term financial stability. We have therefore concluded that financial sustainability remains a significant risk for 2018-19.

Strategic Planning

49. NHS Lothian published its Strategic Plan *Our Health, Our Care, Our Future* in 2014. The Strategic Plan set out some of the significant challenges of responding to the health needs of a growing and ageing population.
50. The Scottish Government's Health and Social Care Delivery Plan was published in December 2016 and emphasises the need for greater regional working in order to improve performance and the sustainability of healthcare provision in Scotland. During 2017-18, work has been undertaken to develop a national Medium Term Financial Framework for Health and Social Care.
51. NHS Lothian has played a key role in delivering regional planning to support the financial framework across the East of Scotland. The Chief Executive and Director of Finance were appointed as Regional Leads and chair a Programme Board for the East of Scotland region.
52. We anticipate that the Medium Term Financial Framework, and Regional Plans, will be published in June 2018. Benchmarking with other NHS Boards highlights a number of the challenges for NHS Lothian, including:
 - Ongoing challenges associated with funding (NRAC funding, described below);
 - Costs are already lower than most other boards so there is less scope to make more efficiency savings; and
 - The significant impact of demography associated with anticipated population growth in Lothian.

Funding has not kept pace with demand for a number of years

53. Since 2009-10, the Scottish Government has used a formula developed by the National Resource Allocation Committee (NRAC) to allocate the majority of budgets for each territorial board, based on demography and factors such as deprivation. Population projections for 2015-2025 showed an estimated increase of 9% in the total Lothian population. This will place significant additional demand on health resources in Lothian.
54. Since the formula was introduced, NHS Lothian's actual allocation has fallen considerably below the target level of funding. In 2018/19 all Boards, including NHS Lothian, have moved to within 0.8% of NRAC parity. NHS Lothian has estimated that the value of this shortfall will be £14m at the end of 2018/19.

Financial Strategy

Development of a strategic and tactical approach to achieving financial sustainability is progressing

55. The approach to developing a financial strategy was presented to the Finance and Resources Committee in November 2017. The strategy outlines a four tiered approach to achieving financial sustainability. The four tiered approach recognises the limits that NHS Lothian can achieve on its own.

Exhibit 3: NHS Lothian has identified a four tiered approach to achieving sustainability



56. There are a range of workstreams in development to deliver savings, which will be consolidated in a network office to monitor progress during 2018-19. The bottom tier, Financial Recovery Plans, is the most developed to date with evidence of ongoing strong financial management, including the development of Grip and Control checklists for business units. A Sustainability and Value Group has been established by the Director of Finance as a mechanism for reviewing programmes aimed at supporting financial sustainability and recovery and for monitoring return on investment.

57. Given the scale of financial pressures impacting the NHS in Scotland, NHS Lothian has recognised the importance of collaborative working at both national and regional levels. This is being taken forward through the East of Scotland regional delivery plan. Current areas for joint working include a programme to reduce the incidence of Type 2 diabetes, and efficiencies in laboratories.

58. Work is ongoing to develop detailed savings plans and the governance to support reporting on savings to the Finance and Resources Committee and the Board.

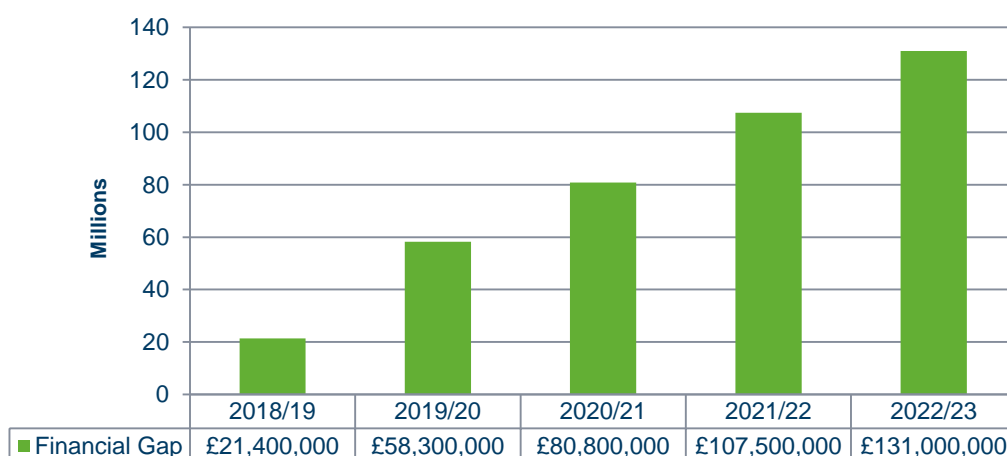
Action plan point 1

Medium-term financial outlook

59. NHS Lothian has recognised the significance of financial risk within the Corporate Risk Register. The risk that the scale or quality of the Board's services is reduced in the future due to failure to respond to the financial challenge is monitored by the Finance and Resources Committee. The risk is currently rated as very high, and is above the Board's target risk level.

60. The 5 year projection presents a daunting financial challenge with the financial gap estimated to reach £131 million by 2022-23, as illustrated in Exhibit 4 below.

Exhibit 4: The financial gap is estimated to reach £131 million by 2022-23



Financial Projections

The Board's Operational Plan sets out a very challenging financial outlook with no clear plans to deliver recurring financial balance

61. The Scottish Government required NHS boards to develop an Annual Operational Plan for 2018-19, replacing the Local Delivery Plan. This required financial projections for one year, rather than the three year forecast previously required.
62. The 2018-19 Operational Plan describes a gap of £21.475 million after taking account of financial recovery plans of £27.671million.
63. This is the third consecutive year that NHS Lothian has forecast a substantial financial gap at the start of the year. While financial balance has been achieved in recent years, the outlook remains challenging and relies on non-recurring savings being achieved.
64. The Finance and Resources Committee has only been able to take limited assurance on the long-term financial sustainability of the Board. The Committee has highlighted that it would like to see more work on assumptions and scenario planning used in development of the financial strategy.

Key assumptions and risks in the Operational Plan

65. The Operational Plan assumptions and risks are largely consistent with prior years. The most significant change to the assumptions applied for 2018-19 relate to the ending of the public sector pay cap. Pay increases had been held at 1% for the past seven years and this change creates a significant new budget pressure for NHS Lothian. While the costs of the pay award (£24.7million) are fully funded in 2018-19, there remains uncertainty around future funding of these costs adding to financial risk in subsequent years.
66. The Operational Plan template requires Boards to identify the key risks to delivering their financial operational plan. NHS Lothian identified a total of 12 risks with 50% (6) being classified as high risk, 5 (42%) as medium risk and 1(8%) as low risk.

Exhibit 5: Financial Risks outlined in the Annual Operational Plan

- Integration
- Delayed Discharges
- Winter Pressures
- Pay Terms and Conditions
- SGHD allocations
- Capital Programme
- New GP Contract
- GP Prescribing
- Acute Medicines
- Outcomes Framework
- Pay funding
- PPRS

National workforce plans are under development

67. The Scottish Government is developing a national Health and Social Care Workforce Plan. A single, integrated national workforce plan is due to be published later in 2018. During 2017-18, three stages have been published:
 - Part I – NHS Workforce
 - Part II – Social Care Workforce
 - Part III – Primary Care Workforce.
68. An effective national workforce plan is dependent on data gathered by individual health boards and integration authorities. At a local level, NHS Lothian developed an updated workforce plan in 2017-18 which takes into account the ongoing national and regional developments.
69. The Workforce plan reflects the projected population growth in the Lothian region and how this will lead to an increased healthcare requirement. The plan then demonstrates the current workforce profile and the gaps that exist. An action plan has been developed and taken forward with the Workforce Planning and Development Programme Board reviewing progress against the plan.

4

Financial management

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

Financial management



NHS Lothian has effective arrangements in place for financial management and the use of resources. The Board met its key financial targets in the year, delivering small underspends against revenue resource limits and meeting capital resource limits.

NHS Lothian delivered over £23m in savings, but this was less than planned and the Board relied on non-recurrent savings to deliver financial balance in 2017-18.

We believe there is scope to further improve financial reporting to aid understanding of complex financial arrangements.

Financial performance in 2017-18

- 70.** As Exhibit 6 shows, NHS Lothian met all of its key financial targets in 2017-18.
- 71.** NHS Lothian has to work within the resource limits and cash requirements set by the Scottish Government. In 2017-18, the Board's final cash requirement was £1.635 billion (2016-17: £1.618 billion).

Exhibit 6: NHS Lothian performance against resource limits

| Financial Target | Limit £000 | Actual £000 | Variance £000 | Target achieved? |
|---------------------------------|---------------|----------------|------------------|---------------------|
| Core revenue resource limit | 1,512,516 | 1,512,237 | 279 | Yes |
| Non-core revenue resource limit | 91,141 | 91,141 | - | Yes |
| Core Capital resource limit | 50,373 | 50,373 | - | Yes |
| Non-core capital resource limit | 23,657 | 23,657 | - | Yes |
| Cash requirement | 1,635,042 | 1,635,042 | 0 | Yes |

Source: NHS Lothian Annual Report and Accounts 2017-18

Delivering financial balance

- 72.** The Local Delivery Plan was based on NHS Lothian managing a funding gap of £47.916 million (3.1% of the recurring budget) to achieve financial balance.
- 73.** Financial pressures in 2017-18 reflected the impact of pay changes, the growing demographic challenge caused by the growth and nature of the population in Lothian, strategic investments and the implementation of national policies.

74. The Local Delivery Plan 2017-18 included £25.5 million of identified financial recovery plans, of which 75% were classified as medium or high risk. The financial plan gap after these recovery actions was £22.377 million. The table below illustrates that a number of actions were required to ensure the Board achieved financial balance:

| | 2017-18 £m |
|--|---------------|
| Projected Financial Plan Deficit | 22.377 |
| Improvement in operational position | 3.892 |
| Financial recovery actions shortfall in delivery | 5.921 |
| Depreciation Benefit | 5.159 |
| CNORIS Benefit | 2.714 |
| Slippage in RHSC Investment | 2.778 |
| In year Flexibility | 14.034 |
| Underspend | 279 |

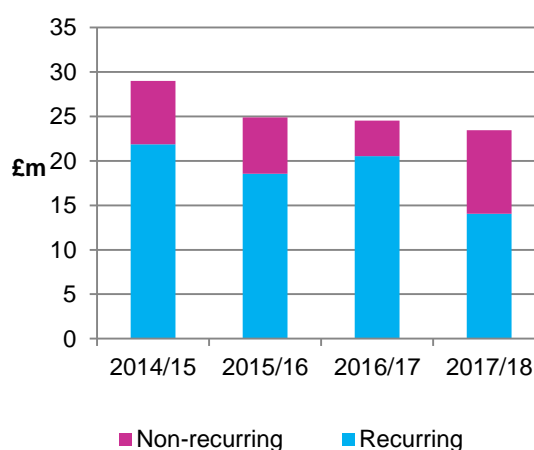
75. NHS Lothian achieved an underspend position against the RRL. However during 2017-18, NHS Lothian reported a cumulative overspend against budget of £7.456 million, primarily as a result of overspends against pay of £8.6 million, junior doctors of £5.6 million and a medical supplies overspend of £5.8 million. These were offset by underspends in a number of areas, including CNORIS costs and one-off savings as a result of asset sales and delays to the opening of the Royal Hospital for Sick Children.

Efficiency savings

NHS Lothian did not achieve all of the savings planned in 2017-18

76. As part of the revised 2017-18 financial plan, a total of £29.373 million of savings were required to achieve financial balance. NHS Lothian delivered £23.452 million of savings. As Exhibit 7 (below) demonstrates, around £9.389 million (40%) of the savings achieved were on a non-recurring basis. This is a significant increase from 2016-17 where £3.879million (16%) of savings were delivered non-recurrently. Reliance on non-recurring savings places pressure on future financial years.

Exhibit 7: NHS Lothian relied on increasing non-recurring savings to deliver financial balance in 2017-18



Source: NHS Lothian Financial Monitoring Reports to Finance and Resources Committee

77. We note that the savings identified to date in the 2018-19 Annual Operational Plan include non-recurring savings of £10.618 million.

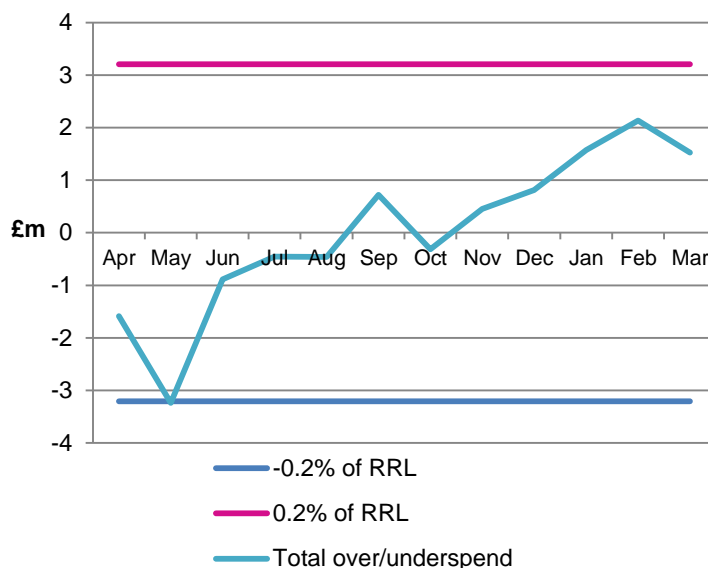
NHS Lothian has effective overall operational budget setting and monitoring arrangements in place, within a challenging financial environment

- 78. We have considered NHS Lothian's system of budgetary control and financial management and did not identify any significant deficiencies, whilst acknowledging the difficult financial situation. Comprehensive financial regulations and policies are in place which are subject to regular review and are available on the Board's Finance Online intranet site.
- 79. Financial monitoring reports are submitted to all meetings of NHS Lothian, the Finance and Resources Committee and Corporate Management Team. The reports include forecast outturn positions, and explanations of key movements in the year.
- 80. As part of their annual development programme, members of the Finance and Resources Committee highlighted the need to improve understanding of NHS finance and sector-specific terminology such as reserves and flexibility. Often these terms are used within finance reports with limited explanations. Recent reports on NHS Tayside highlight the need for clarity in financial reporting, and we therefore believe that the financial monitoring reports could be enhanced by providing greater detail on sources of flexibility, and focusing on in-year performance.

Action plan point 2

- 81. The Finance and Resources Committee was able to provide significant assurance within the governance framework that the Board is operating within its revenue budget and the limits of the Board's expressed risk appetite and tolerance.
- 82. As highlighted in Exhibit 8, NHS Lothian demonstrated strong financial management and was able to manage expenditure against the RRL to within around 0.2% of the budget throughout the year.

Exhibit 8: NHS Lothian managed its budget to within around 0.2% of RRL throughout the year



Substantial progress was made against the Property and Asset Management Investment Programme

- 83. The Property and Asset Management Programme underpins the vision for the estate based on the four "stakes" within the Board's Strategic Plan. NHS Lothian invested £74.03 million in capital and donated estate projects in 2017-18. Key developments included:
 - Patients moved into the Royal Edinburgh Building in summer 2017. A business case is under development for the next phases of the campus.
 - Construction of the new £150 million Royal Hospital for Sick Children and Department of Clinical Neurosciences has continued. Handover of the building is planned for 2018. This represents a delay of at least 12 months from the planned opening date of May 2017.
 - Progress was made in delivering the health and social care capital investment programme with three partnership centres becoming operational in December 2017.
 - The first and second phases of the new East Lothian Community Hospital opened in March 2018. Subsequent phases will be completed by 2021.

Prevention and detection of fraud and irregularity

84. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. We identified no issues in this respect. We found NHS Lothian's arrangements for the prevention and detection of fraud and other irregularities to be satisfactory.
85. The Fraud Liaison Officer provides an annual report to the Audit and Risk Committee outlining any cases that have been referred to Counter Fraud Services, and the progress of any investigations. The Audit and Risk Committee also receive updates on current counter fraud activity from the Fraud Liaison Officer at each meeting.
86. In addition, the Counter Fraud Service's estimates of potential fraud relating to claims for exemptions from patient charges for dental and ophthalmic services are monitored. NHS Lothian has a lower rate than the Scottish average for both dental and ophthalmic potential fraud.

National fraud initiative

87. 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 for the UK as a whole to identify fraud and error.
88. The most recent NFI exercise commenced in October 2016 and as part of our 2017-18 audit we monitored the Board's participation in NFI. We found the arrangements for participation in the NFI to be satisfactory at the time of reporting in February 2018.
89. The NFI uses data matching to compare a range of information held on bodies' systems to identify potential fraud or error. Bodies investigate these data matches and record appropriate outcomes based on their investigations.

90. Our review in February 2018 concluded that good progress was being made with investigating recommended matches. Over 94% of recommended matches had been concluded upon with no frauds or errors identified.

Systems of internal control

91. We have evaluated the Board's key financial systems and internal financial controls to determine whether they are adequate to prevent material misstatements in the annual accounts. Our approach has included documenting the key internal financial controls and performing walkthroughs to confirm that they are operating as intended. We found no issues in this regard.
92. We did not identify any material weaknesses in the Board's accounting and internal control systems during our final audit.

Exhibit 9: Key financial systems evaluated in 2017-18

| | | |
|-------------------------------|----------------------------|---------------------------|
| Non-pay expenditure | Income | Cash receipts and banking |
| Property, Plant and Equipment | Financial Ledger | Payroll |
| ICT Environment | FHS Income and Expenditure | Provisions |

5

Governance and transparency

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

Governance and transparency



Our audit planning identified a significant risk in relation to the Board's response to the alleged mismanagement of waiting times reporting. We concluded that the Board has responded quickly and openly to findings to date.

The Board has a well-developed overall governance framework in place, which includes a clear assurance framework for committees.

We found that the Board has considered its arrangements to secure openness and transparency and compares well against other health boards.

Introduction

93. NHS Lothian is responsible for ensuring the proper conduct of its affairs including compliance with relevant guidance, the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements.

Governance arrangements

94. NHS Lothian has well-established governance arrangements to support the Governance Statement within the Annual Report and Accounts. The Statement reflects the work of the Board's committees, including risk management arrangements, key improvements achieved during 2017-18 and areas of ongoing risk.
95. The Annual Report notes that the Board membership was renewed during the year. In 2017-18 eleven of the non-executives left the Board, and eight new members joined. In September 2017, an updated induction programme for Board members was developed, which was informed by Scottish Government guidance. The programme includes the mandatory completion of electronic training programmes.
96. NHS Lothian has also developed a Board Members Handbook to support all members, which is available on the Board's website. This ensures that key information is publicly available, including explanations on the role of each committee and standing orders.

Waiting Times Significant Risk

97. One of the sector risks identified by Audit Scotland related to public sector organisations keeping pace with public expectations on openness and transparency.
98. Our annual audit plan identified a significant audit risk specifically relating to NHS Lothian's response to a whistleblowing report, as set out below.

Waiting times

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 an investigation into concerns raised under the Board's whistleblowing arrangements about the alleged mismanagement of waiting times reporting.

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 commissioned an investigation into the concerns, which we anticipate will be available in April 2018.

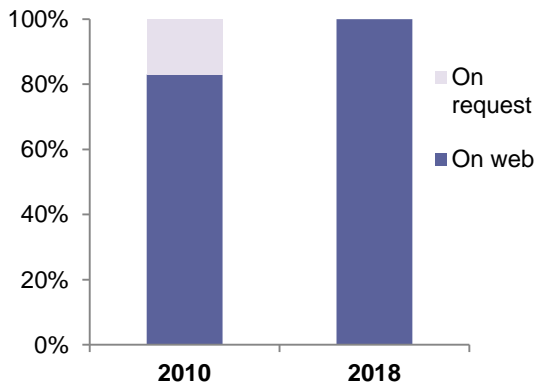
Excerpt from the 2017-18 External Audit Plan



- 99.** We are satisfied that the Board has responded clearly and openly to the allegations, as described below. We will continue to review the implementation of the improvement action plan during 2018-19.
- 100.** NHS Lothian first became aware of concerns relating to the culture and management of the 4 hour emergency care standard in the Emergency Department in October 2017. It was agreed that there was ambiguity in the NHS Lothian 4 hour emergency care standard operating procedure (SOP) and that this required to be reviewed and revised.
- 101.** On 11 October 2017, the Chief Executive received an email containing allegations of misconduct and wrongdoing in relation to the management of the 4 hour emergency care standard in the Emergency Department at St John's hospital. An investigation was launched in compliance with the Board's whistleblowing arrangements led by the Board's Non-Executive Whistleblowing champion.
- 102.** The Board's internal auditors then carried out an investigation process, with oversight from a non-executive board member. The scope of the investigation was extended to all four emergency departments.
- 103.** The internal auditor's report was presented to the Board in December 2017 and highlighted a number of findings and contributing factors which indicated 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.
- 104.** The report set out an action plan to address procedural, cultural and governance issues identified, and was accepted in full by the Board.
- 105.** On 26 June 2018, the Scottish Government published the independent report from the Academy of Royal Medical Colleges on the reporting of A&E waiting times against the 4 Hour Emergency Access Standard. The report underpins a range of findings and actions from the earlier reviews and identifies a number of additional, prioritised recommendations which will be used to inform and enhance the existing improvement plan.
- 106.** The Chief Executive has drawn attention to the weaknesses identified and the implications for the organisation within the Board's Annual Report. We were also satisfied that the issue was disclosed appropriately within the Board's Annual Governance Statement.
- Openness and transparency**
- 107.** One of the sector risks identified by Audit Scotland for 2017-18 relates to public sector organisations keeping pace with public expectations on openness and transparency. Audit Scotland's Role of Boards report, published in September 2010, found that there was wide variation in the openness and transparency of boards of public bodies.
- 108.** NHS organisations were the most open of public boards in 2010, with 100% holding board meetings in public, against an average of 41%

across the public sector. As Exhibit 10 (below) highlights, our research in 2018 found that the variation that Audit Scotland reported in the availability of Board papers has been addressed.

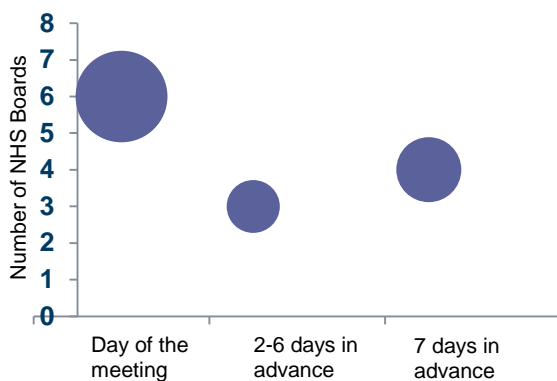
Exhibit 10: In 2010, 17% of NHS Boards made board papers available on request only. By 2018 all board papers were available on the website.



109. We also found that all NHS bodies were clear that members of the public could attend the board meetings as observers, and that agendas were generally available in advance. NHS Lothian publicises the meetings on its website.

110. However, Exhibit 11 highlights that, of the NHS bodies that specify when Boards papers will be available, almost half do not make papers available until the day of the meeting. In one case, the papers are only available after the meeting has begun

Exhibit 11: We found only 4 NHS boards in Scotland that committed to making Board papers available a week in advance of their meetings. Most were available on the day.



111. At NHS Lothian, the Standing Orders commit to making board papers public at least 3 days in advance of the meeting.

112. Audit Scotland's NHS in Scotland 2017 overview report stressed that more information in the public domain would help to involve staff and communities in developing the future of healthcare. Audit Scotland noted that it is important that the public, staff, and elected officials are able to easily access information about how the NHS and integration authorities are performing so that they can get involved with and hold these bodies to account. The report identified a range of areas where transparency could improve, including allowing the public to attend committee meetings and publishing all committee meeting papers and minutes on the organisation's website.

113. Our own research highlights that only two NHS Boards make audit committee papers publicly available on their website. While all NHS boards publish audit committee minutes on their websites, they are often only available through board papers. The timing of meetings meant that in some instances the most recently available minutes were over 6 months old.

NHS Lothian: Better Practice

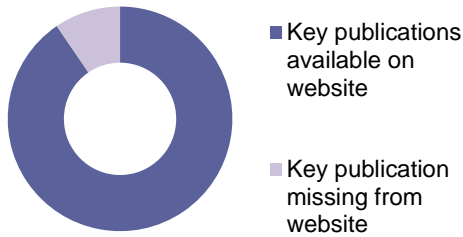
Like most NHS Boards, NHS Lothian makes Audit Committee minutes publicly available through the Board papers. In recognition of the public interest, the Board also makes internal audit reports available on the website once they have been accepted by the Audit and Risk Committee.

We also note that the Board Members Handbook has been updated and published on the website. This includes explanation of how the Board operates, the values and signposting to key governance documents.

Openness Benchmarking

114. The following charts highlight the results of our assessment of other key openness indicators, and our commentary on NHS Lothian.

Exhibit 12: Availability of key publications



Source: Review of NHS Boards' websites March – May 2018

115. For all but two NHS Boards in Scotland, we found that the key publications we selected were found on the website, including the annual accounts, results of the annual review and Local Delivery Plan.

| | |
|--|-------|
| Our assessment of the Board | Green |
| <p>All key documents were found on the website, although we note that the Key Documents section of the website was out of date. The LDP for 2017-18 was available in board papers.</p> | |

116. All NHS Boards have a Register of Interests in place and available on the website, but in two cases we noted that the register is out of date.

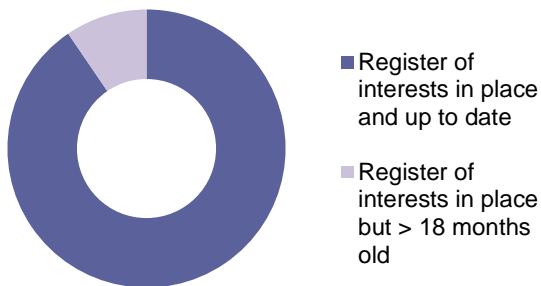
| | |
|---|-------|
| Our assessment of the Board | Green |
| <p>NHS Lothian's register of interests is easily accessible on the website, and was last updated in March 2018. We also note that members are asked to disclose any interests at the start of each Board and Committee meeting.</p> | |

Risk Management

117. Public sector bodies face increasing demand for quality services at a time of significant financial pressure. Well-developed risk management arrangements help boards to make effective decisions and secure better use of resources.

118. NHS Lothian's corporate risk register is directly linked to the corporate objectives. The Board receives regular reports on the corporate risk register, which provide updates on action taken by the corporate management team to mitigate risks. A development session has recently been held with the Board to ensure that the arrangements remain fit for purpose and allow the approach to risk to be further refined.

Exhibit 13: Disclosure of Interests



Source: Review of NHS Boards' websites December 2017 – February 2018

Disclosure of Risks

119. As part of our assessment of Board openness, we reviewed the top risks across NHS Scotland, as disclosed in Board's Financial Statements and risk registers (where publically available). We found that there are a number of strong themes across the NHS in Scotland as Exhibit 13 outlines below.

Exhibit 14: Top NHS Scotland Risks

- Workforce sustainability: Including the impact of factors such as Brexit, GP Sustainability and the new GP contract
- Financial sustainability: Including the inability to deliver efficiency savings and specific risks about failing to meet financial targets
- Partnership working: Risks were often linked to structural change related to the delivery of Health and Social Care Integration or the creation of the new public health body, but 7 boards mentioned stakeholder engagement.

- ICT: Including the implementation of new systems, cyber security threats, ageing ICT infrastructure and lack of funding to implement an effective ICT strategy.
- Targets: Performance targets were mentioned 7 times by 5 NHS boards – often linked to other risks such as delayed discharges, or funding and management of waiting times.

Source: Review of NHS Annual Reports 2016-17, December 2017-February 2018

120. During our review of the Annual Report for 2017-18, we noted that NHS Lothian discloses all corporate risks, and that the Performance Report includes commentary on how key risks have been managed during the year.

Impact of EU Withdrawal

121. Audit Scotland has identified EU withdrawal as an emerging significant risk facing public bodies across Scotland. Three streams of potential impact were identified:

- Workforce
- Funding
- Regulation

122. NHS Lothian's Corporate Management Team has considered a paper on the key areas of potential impact from Brexit. To date, NHS Lothian has recognised that the most significant risk is the impact on workforce and has started to consider the potential implications for workforce planning, but planning is at an early stage. As part of this work, the Board's HR team is developing a webpage for EU citizens to provide information and signposting to further advice. Employee communications are being used to encourage EU citizens to register with HR using a central email address to ensure that advice can be targeted directly.

123. At a national level, discussions around implications for workforce across NHS Scotland have been taken forward through the HR Executive Forum.

Information Governance

Cyber Security

124. In May 2017, a number of health boards across NHS Scotland were affected by the Wannacry

global ransomware attack. In response to this the Scottish Government launched 'A Cyber Resilience Strategy for Scotland: Public Sector Action Plan, 2017-18.

125. The action plan outlines a number of requirements that public bodies should be taking forward. This includes an action for public bodies to achieve a Cyber Essentials Plus certification by the end of October 2018.

126. Planning guidance issued by Audit Scotland for 2017-18 highlighted cyber security as a significant risk that all auditors should consider when scoping, planning, performing and reporting their work.

127. We undertook a review of cyber security at the Board as informed by the Audit Scotland guidance. Through this work we identified areas of good practice at the Board including the existence of an Information Governance Committee to oversee progress on the development of cyber security controls. We fully endorse the two areas identified for further development, as follows:

- The Board anticipates that it will not qualify for Cyber Essentials Plus accreditation. This is part of a national issue across NHS Scotland Boards due to the use of legacy Microsoft operating systems which host service-critical operations. Projects are currently underway to upgrade these operating systems and the Board hopes to achieve accreditation by November 2018.
- The Board's procurement team has also been working in consultation with the Scottish Government to develop a standard policy for all third parties with the aim of establishing a set of minimum security requirements for all suppliers. This remains a work in progress.

General Data Protection Regulation

128. The General Data Protection Regulation came into force in the UK on 25 May 2018. The regulations replace the Data Protection Act 1998 and, as well as strengthening existing regulations, has brought in new legislative duties for the Board. The regulations bring significant potential penalties for non-compliance.

129. NHS Lothian has used guidance issued by the Information Commissioner's Office to develop an action plan to ensure compliance with the new regulations. NHS Lothian's revised privacy

policy was published on the website in May 2018.

- 130.** Compliance with the regulations is an ongoing process, which we will monitor as part of our annual audit procedures. We have not identified any significant risks to compliance with the regulations at this stage.

Internal Audit

- 131.** An effective internal audit service is an important element of NHS Lothian's governance arrangements. NHS Lothian has a compliant and appropriate internal audit service provided through a co-sourced arrangement with Grant Thornton.

- 132.** During our audit we took cognisance of the work of internal audit to ensure the most efficient use of NHS Lothian's total audit resource. In particular we considered the findings of internal audit in relation to:

- The waiting times whistleblowing investigation;
- IJB Directions;
- Performance reporting and targets;
- Fixed assets; and
- Information governance.

Standards of conduct

- 133.** In our opinion, NHS Lothian's arrangements in relation to standards of conduct and the prevention and detection of bribery and corruption are generally adequate. Our conclusion has been informed by a review of the arrangements for adopting and reviewing standing orders, financial instructions and schemes of delegation and for complying with national and local codes of conduct. The Code of Conduct is available on the Board's website through the Board members handbook.

- 134.** We have also considered the controls in place to ensure compliance with the regulatory guidance that is produced by the SGHSCD throughout the year and identified no reportable issues.

6

Value for money

Value for money is concerned with using resources effectively and continually improving services. In this section we report on our audit work as it relates to NHS Lothian's own reporting of its performance.

Value for money



The Board has a well-established performance management framework in place, but more could be done to report progress on key priorities and corporate objectives.

Performance against the indicators that are reported publicly has fallen in 2017-18, although this is in the context of significant and ongoing financial challenges.

The Board's quality improvement programme continues to lead to improved outcomes but there is a risk of the programme being undermined without a clear evidence base for planned savings.

Performance Framework

- 135.** The Board has a well-established performance management framework in place. During 2016-17, the Board delegated scrutiny of performance indicators to relevant committees. A range of 48 indicators are considered by Committees. The indicators include key nationally reported LDP targets and quality indicators.
- 136.** A summary Quality and Performance Improvement Report, with supporting data pack, is considered at each Board meeting. This report is also one of the key mechanisms the Board uses to report to the public on performance during the financial year.
- 137.** The Board is considering improvements to the performance reports, including providing Board members with access to a performance dashboard. However, we consider that there is scope to review the context and coverage of the indicators to better reflect the complexity and priorities of the Board. There are currently nine corporate objectives, but we were unable to link a number of the objectives to current performance reporting, for example relating to Shift the Balance of Care from Hospital to a Community Setting and the use of Innovation and Technology to support transformational change.
- 138.** We also note that limited use is made of contextual information, for example to describe the importance of indicators and, where relevant, the reasons for deteriorating performance and priorities for action.

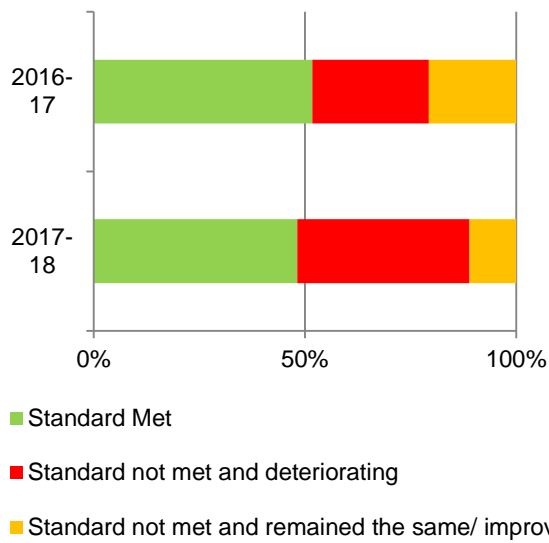
- 139.** The most recent performance report highlights that the scrutiny committees have taken moderate or significant assurance on the relevant indicator in only 30% of cases. It is therefore difficult for the Board to have overall assurance on the accuracy of the indicators and the plans and financial implications for improvement.

Performance during 2017-18

- 140.** The Board uses the Annual Report and Accounts to report on performance against 29 key indicators included within the Local Delivery Plan. Of the 27 indicators where targets were set, during 2017-18 the Board achieved only 48% (compared to 52% in 2016-17).

Action plan point 3

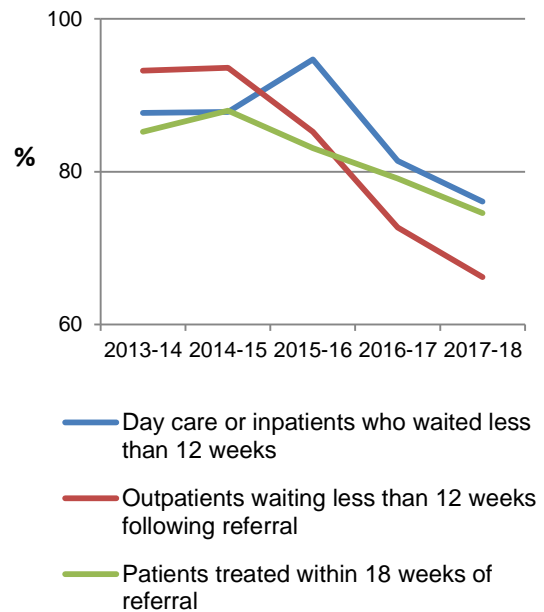
Exhibit 15: The relative performance reported in the Annual Report has fallen during 2017-18



Source: NHS Lothian Annual Report and Accounts

141. The Board acknowledged the challenges associated with a number of targets for scheduled care within the Local Delivery Plan, particularly in light of the financial position. The Board identified that it would be unable to provide additional funding in 2017-18 for Independent Sector Capacity. This additional external capacity supported previous years' performance.
142. Exhibit 16 highlights the relative performance against scheduled care targets, and therefore the impact of this financial decision on capacity in 2017-18.

Exhibit 16: Waiting time performance has significantly deteriorated in recent years, partly as a result of financial decisions



Source: NHS Lothian Annual Report/ISD

143. The timeliness of receiving care continues to be a challenge against a number of expected standards. A number of areas have deteriorated since 2016-17:
- Only 90.4% of patients diagnosed with cancer were treated within 31 days (target: 95%; 2016-17: 96.3%)
 - Only 85.9% of patients referred with suspicion of cancer received treatment within 62 days
 - 66.2% of outpatients waited less than 12 weeks (target: 95%, 2016-17: 72.7%)
 - Only 58.6% of Child and Adolescent Mental Health patients were treated within 18 weeks (target: 90%, but represents an improvement on 2016-17: 51.4%)
 - 74.6% of patients were treated within 18 weeks of referral (target: 90%; 2016-17: 79.1%).

Quality Improvement

- 144. One of the Board's key strategies for delivering continuous improvement and for meeting the scale of the financial challenge is a focus on the Quality Management System.
- 145. The Chief Quality Officer leads a Clinical Quality Academy to build and support the understanding, capability and capacity of NHS Lothian staff in aspects of quality planning, improvement and control of processes relating to health and care.
- 146. Individual clinicians and teams are enabled and empowered to test new approaches to deliver improvements in patient outcomes, patient experiences and use of resources.
- 147. The programmes currently focus on improving outcomes in mental health, stroke, disease, cancer, outpatient endoscopy and hip fractures. NHS Lothian reports that, as a result of the delivery model, significant sustained improvements have been achieved, alongside a high level of staff engagement. The programme has a dedicated website to report on achievements and share good practice and knowledge.
- 148. A five year plan is in development to allow the Board to monitor progress and make investment decisions.

7

Appendices

Appendix 1: Respective responsibilities of the Board and the Auditor

Responsibility for the preparation of the annual accounts

It is the responsibility of the Board and the Chief Executive, as Accountable Officer, to prepare financial statements in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder.

In preparing the annual report and accounts, the Board and the Chief Executive, as Accountable Officer are required to:

- apply on a consistent basis the accounting policies and standards approved for the NHS Scotland by Scottish Ministers;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards as set out in the Financial Reporting Manual have not been followed where the effect of the departure is material;
- prepare the accounts on a going concern basis unless it is inappropriate to presume that the Board will continue to operate; and
- ensure the regularity of expenditure and income.

Board members are also responsible for:

- keeping proper accounting records which are up to date; and
- taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditor responsibilities

We audit the annual accounts and give an opinion on whether:

- they give a true and fair view in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers of the state of the board's affairs as at 31 March 2018 and of its net expenditure for the year then ended;
- they have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017-18 FReM ;
- they have been prepared in accordance with the requirements of the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers;
- in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers;
- the auditable part of the Remuneration and Staff Report has been properly prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers; and
- the information given in the Performance Report for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the

We audit the annual accounts and give an opinion on whether:

- National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers; and
- the information given in the Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers.

We are also required to report, if in our opinion:

- adequate accounting records have not been kept; or
- the annual accounts and the part of the Remuneration and Staff Report to be audited are not in agreement with accounting records; or
- we have not received all the information and explanations we require for our audit; or
- there has been a failure to achieve a prescribed financial objective.

Wider scope of audit

The special accountabilities that attach to the conduct of public business, and the use of public money, mean that public sector audits must be planned and undertaken from a wider perspective than in the private sector. This means providing assurance, not only on the annual report and accounts, but providing audit judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability.

The Code of Audit Practice frames a significant part of our wider scope responsibilities in terms of four audit dimensions: financial sustainability; financial management; governance and transparency; and value for money.

Appendix 2: Action plan

The action plan details the weaknesses and opportunities for improvement that we have identified during our audit.

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

Action plan grading structure

To assist the Board in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated.

The rating structure is summarised as follows:

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

| Action plan point | Issue & Recommendation | Management Comments |
|------------------------------------|---|---|
| 1. Financial sustainability | <p>Issue</p> <p>The Board has made significant progress in 2017-18 to develop a framework to deliver financial sustainability, including regional and national planning. There are currently 22 work streams in NHS Lothian is involved to address the Board's savings gap. However, there is currently limited information presented to committee on specific projects and no breakdown of how the total savings, within each work stream, will be achieved and therefore how this specifically supports NHS Lothian's financial position.</p> <p>Recommendation</p> <p>NHS Lothian should ensure that the Board is presented with clear plans and options for where savings will be achieved.</p> | <p>Responsible officer:</p> <p>NHS Lothian will continue to provide information to its committees on the achievement of savings against plan.</p> <p>As the Sustainability and Value programme as part of Lothian's financial strategy, a more formal process for ensuring a robust prioritisation of savings opportunities will be developed.</p> <p>Implementation date:</p> <p>December 2018</p> |
| Rating | | |
| Grade 3 | | |
| Paragraph ref | | |
| 58 | | |

| Action plan point | Issue & Recommendation | Management Comments |
|--------------------------------|---|--|
| 2. Financial monitoring | Observation The NHS financial framework that the Board operates under is complex and reporting on this in a way that is clear and understandable is a challenge. | Responsible officer: NHS Lothian has agreed to remove legacy LRP gaps following discussion with the F&R committee. |
| Rating | Recommendation We believe that there is scope to further clarify financial monitoring reports by: <ul style="list-style-type: none"> • Providing greater explanation and analysis of flexibility • Removing reference to legacy efficiency savings gaps to allow Board members to focus on in-year performance. | The presentation of financial flexibility information will be discussed with the F&R committee Implementation date: December 2018 |
| Grade 2 | | |
| Paragraph ref | | |
| 80 | | |

| Action plan point | Issue & Recommendation | Management Comments |
|---------------------------------|--|---|
| 3. Performance reporting | Issue The Board is presented with a Quality and Performance Improvement Report, with supporting data pack, at each Board meeting. While we acknowledge that this report legitimately focuses on the key targets that the Board will be assessed on, we believe that there is scope to develop performance reporting to consider the achievement of wider corporate objectives. | Responsible officer: Chief Quality Officer As part of its next review of content in Quality and Performance Improvement NHS Lothian has committed to conduct a comprehensive review of the report specifically including the views of key users on format and content to reflect broader organisational priorities informed by the recommendations arising from the Scottish Parliament's Health and Sports Committee consideration of Scrutiny of NHS Health Boards. |
| Rating | Recommendation The Board should review performance reporting arrangements to ensure that reports provide a balanced and comprehensive commentary across each of the organisation's priorities, including, for example, improvement work and efficiency savings. | Implementation date: 31 March 2019 |
| Grade 3 | | |
| Paragraph ref | | |
| 138 | | |

Follow up on prior year action plan

| | Issue & Recommendation | Management Comments | 2018 update |
|------------------------------------|---|--|---|
| 1. Declaration of interests | <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>Action owner: Douglas Weir</p> <p>Due Date: 31 July 2017</p> | <p>Action complete We have not identified any issues in regard to the declaration of interests through our 2017-18 audit work. We have confirmed that adequate guidance is given to new and existing Board members in this regard.</p> |
| Rating | | | |
| Grade 3 | | | |

Appendix 3: Unadjusted Errors

We identified the following adjustments during the audit. We have discussed these with management and have agreed that they would not be incorporated into the financial statements on the basis of immaterial impact.

| Adjusted difference | SoCNE | | Balance Sheet | |
|---|-------------|----------|---------------|----------|
| | DR £m | CR £m | DR £m | CR £m |
| Accruals | | | 12.5 | |
| Expenditure | | 12.5 | | |
| <p><i>Being the correction of overstated accruals</i></p> <p>This figure is made up of:</p> <ul style="list-style-type: none"> (i) £1.6million of aged automated accruals, and (ii) £10.9million of SGHSCD funding allocations accrued as at 31 March 2018 but for which no accounting obligation existed. This relates to allocations where expenditure is spread over more than one year. The issue therefore spans and has impact over different accounting periods. This situation arises from the NHS funding context. | | | | |
| Net impact on income / expenditure | 12.5 | | | |



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