



Scott-Moncrieff
business advisers and accountants

The State Hospitals Board for Scotland

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

June 2018

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Key messages

Annual accounts audit

All key financial targets were met in 2017/18. The Board made a saving against its revenue resource limit of £5,000 and a saving against its capital resource limit of £71,000.

The annual report and accounts were approved by the Board on 28 June 2018. We report within our independent auditor's report an unqualified opinion on the annual accounts, regularity and on other prescribed matters.

Wider scope audit

Financial sustainability

A breakeven position is forecast for 2018/19 subject to achieving savings of £1.983million.

The Board has appropriate arrangements in place to develop a financial framework for achieving long term financial sustainability in partnership with other national health boards.

Financial management

The Board has adequate and effective processes in place for managing its financial position and use of resources.

The Board's savings target was achieved in 2017/18. However, of the Board's total savings in 2017/18 (£1.847million), less than 10% of these were recurring. As a result the Board will find it challenging to continue to deliver this level of savings in future years.

The key financial systems and internal financial controls are adequate to prevent material misstatements in the annual accounts.

Governance & transparency

Governance arrangements are adequate and appropriate.

Effective arrangements are in place regarding financial control, prevention and detection of fraud and irregularity, and standards of conduct.

Value for money

The Board has appropriate performance management processes in place that support the achievement of value for money.

Progress has been made towards achievement of the local priorities and five out of thirteen LDP measures are on target for 2017/18.

However, overspends on nursing overtime continue to present a significant challenge to the Board's financial position.

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) 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 the State Hospitals Board for Scotland 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 the State Hospitals Board for Scotland, the Audit Committee has been designated as "those charged with governance".

Introduction

1. This report summarises the findings from our 2017/18 audit of the State Hospitals Board for Scotland (“the Board”).
2. We outlined the scope of our audit in our External Audit Plan, which we presented to the Audit 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. The Board is responsible for preparing an annual report and accounts that show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the 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. The 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. We give each recommendation a grading to help the Board assess their significance and prioritise the actions required.
5. We discussed and agreed the content of this report with the Finance and Performance Management Director. We would like to thank all management and staff for their co-operation and assistance during our audit.

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 the Financial Reporting Council's (FRC) Ethical Standards. In our professional judgement, the audit process is independent and our objectivity has not been compromised in any way.

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.

Feedback

9. 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
10. 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

The Board's annual report and accounts are 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 report and accounts.

Annual report and accounts

The annual report and accounts for the year ended 31 March 2018 were approved by the Board on 28 June 2018. We report unqualified opinions within our independent auditor's report. We did not identify any significant adjustments to the unaudited annual report and accounts.

The Board has appropriate administrative processes in place to prepare the annual report and accounts and the required supporting working papers.

Our audit identified no material adjustments to the annual accounts.

Overall conclusion

An unqualified audit opinion on the annual report and accounts

11. The annual report and accounts for the year ended 31 March 2018 were considered by the Audit Committee and approved by the Board on 28 June 2018. We report 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.

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

Appropriate administrative processes were in place

13. We received the draft financial statements template and supporting papers of a good standard, in line with our agreed audit timetable.

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

Our assessment of risks of material misstatement

15. 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 report and accounts as a whole, and not to express an opinion on individual accounts or

disclosures. Our opinion on the annual report and 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. Loss of financial expertise

The Head of Financial Accounts is retiring in 2018 resulting in a significant gap in the Board's financial expertise. The Board is currently making arrangements to ensure minimal disruption to the finance function. There remains a risk, however, that arrangements are not put in place on a timely basis resulting in disruption to the finance function, including the preparation of the 2017/18 annual accounts to the standard expected.

Excerpt from the 2017/18 External Audit Plan

16. The Board appointed an interim Head of Financial Accounts in April 2018, prior to the start of our audit. They performed a key role in the preparation of the 2017/18 annual accounts and provided working papers of a good standard in a timely manner. The loss of financial expertise did not disrupt the preparation or audit of the annual accounts and we did not notice any significant disruption to the finance function. The Board will look to appoint a permanent Head of Financial Accounts in 2018/19.

2. 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

17. 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.

3. Revenue recognition

Under ISA (UK) 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

18. At the planning stage of our audit we considered that the risk of fraud in relation to revenue recognition was present in all non-government revenue streams. We evaluated each type of revenue transaction and documented our conclusions.
19. We have gained reasonable assurance on the completeness and occurrence of income and we are satisfied that income is fairly stated in the financial statements. To inform our

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

conclusion we evaluated the Board's key revenue streams and reviewed the controls in place over revenue accounting. We also carried out testing to confirm that the revenue recognition policy is appropriate and that it was applied consistently throughout the year.

4. Risk of fraud in the recognition of expenditure

The FRC published Practice Note 10 which applies to the audit of financial statements 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.

Excerpt from the 2017/18 External Audit Plan

20. We evaluated each type of expenditure transaction and documented our conclusions. We gained reasonable assurance on the completeness and occurrence of expenditure and are satisfied that expenditure is fairly stated in the annual accounts. To inform our conclusion we carried out testing to confirm that the Board's policy for recognising expenditure is appropriate and has been applied consistently throughout the year.

Our application of materiality

21. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the misstatement. This means that different materiality levels will be applied to different elements of the annual accounts.
22. Our initial assessment of materiality for the Board's annual accounts was £520,000 and it remained at this level throughout the audit. This equates to approximately 1.5% of the Board's forecast expenditure. Achieving a breakeven position through the application of both income and government funding is a key target for the Board and one of the principal considerations for the users of the accounts when assessing financial performance.

Performance materiality

23. Performance materiality is the amount set by the auditor at less than overall materiality for the annual accounts 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 annual accounts as a whole.
24. We set a performance (testing) materiality for each area of work which was based on a risk

assessment for the area. We performed audit procedures on all transactions and balances that exceeded our performance materiality. This means that we performed a greater level of testing on the areas deemed to be of significant risk of material misstatement. Performance testing thresholds used are set out in the following table:

Area risk assessment	Weighting	Performance materiality
High	40%	£0.8million
Medium	55%	£1.1million
Low	70%	£1.4million

25. We agreed with the Audit Committee that we would report all material corrected misstatements, uncorrected misstatements with a value in excess of £10,400, as well as other misstatements below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we

identified when assessing the overall presentation of the annual accounts.

Audit differences

26. We are pleased to report that our audit identified no material adjustments or unadjusted errors to the annual accounts. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of annual accounts.

An overview of the scope of our audit

27. The scope of our audit was detailed in our External Audit Plan, which was presented to the Audit Committee at the outset of our audit. 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. Planning is a continuous process and our audit plan is subject to review during the course of the audit to take account of developments that arise.
28. 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.
29. 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.

Other matters identified during our audit

30. During the course of our audit we noted the following:

Revised financial statement format

31. In 2017/18, the presentation of the statement of comprehensive net expenditure (SoCNE) was amended, in line with the NHS Accounts Manual, to improve clarity for the user 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.

Other information in the annual report and accounts

32. "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

33. 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.
34. 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

35. The accountability report is required in order 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.

Governance statement

36. The governance statement details the significant control weaknesses and issues that have arisen, as identified by internal audit. In 2017/18, high risk recommendations were raised in the following internal audit reports:
- The audit report on Cyber Security identified six high risk recommendations. Two recommendations have been completed with the remaining due for completion in 2018/19.
 - The audit report on Effective Rostering and Overtime Management Review identified nine high risk recommendations. Six recommendations have been completed with the remaining due for completion in 2018/19.
 - The audit report on Sickness and Absence Management identified three high risk

recommendations. All of these are outstanding with actions underway.

37. We have concluded that the governance statement has been prepared in accordance with the National Health Service (Scotland) Act 1978 and directions from Scottish Ministers and is consistent with the financial statements.

Remuneration and staff report

38. We have concluded that the audited part of the remuneration and staff report has been prepared in accordance with the National Health Service (Scotland) Act 1978 and directions from Scottish Ministers.

Regularity

39. 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.

Property, Plant and Equipment (PPE)/Intangible Assets

40. During our audit we noted that a number of the Board's PPE and Intangible assets had been fully written down but are still in use. This is a particular issue in respect of the Board's IT assets.
41. As these assets are still in use it would appear unreasonable for them to be fully depreciated and would suggest that the estimated useful life applied is inaccurate.
42. We would encourage the Board to review its asset register and write off any assets no longer in use and re-assess the useful life of those assets still in use but fully depreciated.

Action plan point 1

IT back-ups

43. As part of our audit, we consider the controls the Board has in place in respect of its IT environment. We noted from this review that system back-ups are not subject to formal or regular testing, and are only tested as and when required. As a result, there is a risk that system back-ups cannot be relied upon if any issues were to occur.

Action plan point 2

Qualitative aspects of accounting practices and financial reporting

44. 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.
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.	We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the annual accounts. Significant estimates have been made in relation to the valuation of property, plant and equipment and liabilities related to the Board's membership of the Clinical Negligence and Other Risks Indemnity Scheme (CNORIS). These estimates have been informed by advice from qualified, independent experts. We evaluated the competence, objectivity and capability of management experts in line with the requirements of ISA (UK) 500 and concluded that use of the expert is appropriate.
The appropriateness of the going concern assumption	We have reviewed the detailed financial forecasts for 2018/19. Our understanding of the legislative framework and activities undertaken provides us with sufficient assurance that the Board will continue to operate for at least 12 months from the signing date.
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, including any significant risk or required disclosures, which should be included in the annual accounts.
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 financial statements.	The annual report 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.	There were no significant difficulties encountered during the audit.

3

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



The Board has effective arrangements in place for managing its financial position and the use of resources.

All three key financial targets for the year were met.

The Board's savings target was achieved in 2017/18. However, of the Board's total savings in 2017/18 (£1.847million), less than 10% of these were recurring. As a result, the Board will find it challenging to continue to deliver this level of savings in future years.

Financial performance

45. All Boards have to work within the resource limits and cash requirements set by the Scottish Government.

46. The Board reported a saving against its revenue resource limit (RRL) of £5,000 and a saving against its capital resource limit (CRL) of £71,000. This position was consistent with the breakeven position outlined in the 2017/18 Local Delivery Plan (LDP).

Exhibit 3: Performance against resource limits

Financial Target	Limit £000	Actual £000	Variance £000	Target achieved?
Core revenue resource limit	32,012	32,007	5	Yes
Non-core revenue resource limit	1,384	1,384	0	Yes
Capital resource limit	750	679	71	Yes
Cash requirement	33,292	33,292	0	Yes

Source: The State Hospitals Board for Scotland Annual Report and Accounts 2017/18

47. Nursing overtime costs continued to be a significant financial pressure throughout 2017/18 and threatened the achievement of a break even position.

48. A number of measures were implemented in February and March 2018 to reduce this overspend, and budget holders were closely involved in reviewing remaining spend for efficiencies. This proved to be effective and the Board brought expenditure back in line with the projected breakeven position.

49. As discussed within Section 6 of this report, Value for Money, the level of nursing overtime spend incurred in the first three quarters of

2017/18 is not sustainable and immediate action is required.

50. The underspend against the capital resource limit (£71,000) relates to the timing of work on the Perimeter Security and Enhanced Internal Security System Project (see section 4 of this report, Financial Sustainability). The full business case received Board approval in May 2018 and the majority of spend is expected in 2018/19.

Efficiency savings

51. As part of the 2017/18 LDP, the Board was tasked with achieving £1.402million efficiency savings. In addition, the Board committed to delivering £0.44million savings towards the national savings target.
52. The Board exceeded its savings target by £5,000, predominantly as a result of delivering significant workforce savings. (see Exhibit 4).
53. To ensure continuous improvement and achievement of efficiency savings targets in future years, it is important that the Board is able to identify recurring savings. Of the total savings in 2017/18 (£1.847million), less than 10% were recurring (£176,000), £457,000 below target. Further work is required in 2018/19 to ensure the Board delivers a higher proportion of recurring savings.

Exhibit 4: Efficiency savings

Efficiency savings	Recurring £000	Non-recurring £000	Total £000
LDP target	633	769	1,402
National target	-	440	440
Total target	633	1,209	1,842
Actual	176	1,671	1,847
(Under)/over	(457)	462	5

National working

54. During 2017/18, consistent with the 'Once for Scotland' approach outlined in the Scottish Government's Programme for Scotland 2017-18, national boards worked together to meet a shared target of £15million efficiency savings. The Board delivered £0.44million of the overall total savings, which was reflected in an in-year reduction of £0.44million to the board's funding allocation. Further discussion on national board working is given in the Financial Sustainability section of this report.

Prevention and detection of fraud and irregularity

55. Our audit was planned to provide a reasonable expectation of detecting material misstatements in the financial statements resulting from fraud and irregularity. We found the Board's arrangements for the prevention and detection of fraud and other irregularities to be adequate.
56. Regular updates on fraud related matters (including Counter Fraud Services updates), the National Fraud Initiative (NFI) are presented to the Audit Committee.

National Fraud Initiative

57. The National Fraud Initiative (NFI) is a counter-fraud exercise co-ordinated by Audit Scotland working together with a range of Scottish public bodies to identify fraud and error.
58. We last reviewed the Board's participation in the 2016/17 NFI in February 2018. The exercise identified 144 matches which were recommended for investigation. As at February 2018 the Board had investigated and concluded upon all recommended matches (100%). No issues were noted from that work and we concluded that the Board's participation in the NFI had been satisfactory.

Standards of conduct

59. In our opinion the Board's arrangements in relation to standards of conduct and the prevention and detection of bribery and corruption are 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. We have also considered compliance with the regulatory guidance that is produced by the SGHSCD throughout the year.

Internal audit

60. An effective internal audit service is an important element of a Board's overall governance arrangements. The Board's internal audit service is provided by RSM. During our audit we considered the work of internal audit wherever possible to avoid duplication of effort and make the most efficient use of the Board's total audit resource.

Systems of internal control

61. 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.
62. We did not identify any significant weaknesses in the Board's accounting and internal control systems during our audit.

4

Financial sustainability

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.

Financial sustainability



The Board has appropriate arrangements in place to develop a financial framework that will inform consideration of its long term financial sustainability in partnership with other national and regional health boards.

The Board is forecasting a breakeven position for 2018/19 and is fully engaged in the developing national financial planning processes for the medium and longer term.

Significant audit risk

63. As outlined in our audit plan, we considered there to be a significant risk to the wider scope of our audit in relation to financial sustainability:

Financial sustainability

The Board has produced a local delivery plan (LDP) covering the financial years 2017/18 to 2019/20. The LDP forecasts a breakeven position in each of the next three years. To achieve this, however, the Board is expected to make substantial 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.

The achievement of future financial targets will depend on continuing tight control of expenditure, delivery of a challenging savings plan and may also require some difficult decisions to be taken in areas such as workforce.

Excerpt from the 2017/18 External Audit Plan

64. The Board, in partnership with other national health boards, has begun to develop a financial framework. This framework will inform the Board's long term strategy for financial sustainability. As outlined below we have reviewed the developing arrangements in national planning as well as the Board's own arrangements for managing its financial position and use of resources. We plan to continue to review the Board's input to national planning in detail during our 2018/19 audit.

National Board planning

65. The Scottish Government's Programme for Scotland 2017-18 included the commitment to "supporting national NHS Boards to develop a plan of where improvement in national services should be focused, including where appropriate a 'Once for Scotland' approach."
66. The Board plays a crucial role in collaborating with other national health boards. A National Board Plan 2018-2023 is in development with the intention of being finalised during summer 2018. The Plan will require a supporting financial framework and the Board is fully engaged in the national financial planning process. The general principles underpinning the process are:
- use existing capacity and capability wherever possible;
 - focus on potential impact and added value;
 - focus on priorities where they can achieve most by working together;
 - not limiting the level of ambition; and
 - work in partnership across health and social care.

Operational and financial planning

67. The Board recognises that financial planning is an integral part of the Annual Operational Plan (AOP) process (previously called the Local Delivery Plan). The Board submitted its AOP to the Scottish Government, with an accompanying financial plan, by the 31 March 2018 deadline.
68. Unlike in the 2017/18 LDP, the 2018/19 AOP presents the financial outlook for only one financial year (Exhibit 5), although it includes high level consideration of future financial pressures. The 2018/19 AOP sets out how the Board will achieve financial balance in the coming year and discusses a range of key issues and assumptions made in forming that view.

Exhibit 5: Forecast 2018/19 financial position

Financial plan 2018/19	£million
Expenditure	(36.012)
Income	1.329
Baseline funding allocation	31.230
Anticipated funding allocations	0.693
Non-core RRL	2.760
Forecast outturn position	0

69. The key risks and assumptions within the 2018/19 AOP are set out in Exhibit 6.

Developing planning frameworks

70. The AOP also reflects the developing arrangements in place, and the practical steps being taken by the Board, to ensure full engagement with national planning groups.

¹ The Board has received confirmation that they will receive central funding to meet additional staff costs following the end of the public sector pay cap. As a result, the Board have budgeted to cover the expected annual 1% pay increase in line with previous years, acknowledging that there is still a level of risk surrounding this.

Exhibit 6: Key risks and assumptions

Risk / assumption	Likely cost implication	Risk rating
Unable to deliver savings contributions to national boards	£440k	High
Pay increase is higher than 1% ¹	£329k	High
Potential staff cost relating to 2018/19 capital work which may not be able to be capitalised	£150k	High
Apprenticeship Levy potential charge for 2018/19	£116k	High
Capital works on-going	£58k	High
On-going legal case	Unknown	High

71. Given the timing of these developments at a national level, the Board has not been able to integrate any wider medium and long term financial implications into the current AOP. In preparation of the 2018/19 AOP any investment and redesign plans have been assumed to be cost neutral.

Capital plans

72. The Board's capital plan outlines significant capital investment in its property, plant and equipment over the next three years, totalling £7.2million. This relates to the Board's planned work on the Perimeter Security and Enhanced Internal Security System Project.
73. While the AOP only outlines the forecast revenue position for one year, capital plans extend out to five years (as in previous years).
74. Work has taken place internally to re-examine the security threats to the hospital and establish how they may be mitigated. This work was used to inform the business case.

Efficiency savings

75. The AOP outlines further challenging savings requirements. While the Board has a strong record in delivering efficiency savings to date, it still needs to develop plans in respect of 26% of the required 2018/19 savings target. As noted in the Financial Management section of this report and in the table below, the vast majority of savings achieved in previous years and planned in 2018/19 are non-recurring. Unless additional funding is received and/ or the

Board's underlying cost base is reduced, a similar or greater level of non-recurring savings will have to be achieved every year.

Exhibit 7 – Efficiency savings (£million)		
	Recurring	Non-recurring
Savings required	0.308	1.675
Savings identified	0.308	0.927
Unidentified savings	-	0.440
% savings unidentified	0%	26%

76. As noted in the Financial Management section of this report, during 2017/18 national boards worked together to meet a shared target of £15million efficiency savings. From 2018/19 the same £15million target will be deducted from revenue allocations on a recurring basis, with the State Hospital again expected to contribute £0.44million.

EU withdrawal

77. Senior management have formally considered the potential impact of EU withdrawal with regard to the Board's workforce, funding and regulation. No significant risks to the Board were identified in relation to these areas.

78. The Board do not expect EU withdrawal to have any impact on its workforce as there is a minimal number of EU staff employed. In addition, the Board do not receive any direct EU funding. As a result, EU withdrawal has had minimal impact on workforce and financial plans.

79. There is on-going review of EU regulations for any potential changes. Key areas identified by the Board are; procurement, staff working times and medical regulation. No significant risks have been identified at this stage, but the Board will continue to monitor this position.

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



Governance arrangements at the Board were found to be satisfactory and appropriate.

Effective arrangements are in place regarding financial control, prevention and detection of fraud and irregularity, and standards of conduct.

Governance Arrangements

Board retirements

80. The Chair, Chief Executive, Employee Director and a further Non-Executive Director are expected to retire in March 2019. An early engagement meeting has taken place with the Scottish Government (May 2018) to discuss succession planning. A follow-up meeting is due to take place in September 2018.
81. The Board plans to interview for successors in September 2018 and has acknowledged the need to arrange appropriate inductions in a timely manner. The Board appears to be taking adequate and appropriate action to address this risk area and we will continue to monitor the position throughout 2018/19.

Collaborative working

82. From January 2018, a number of national boards have been trialling a collaborative working set up that sees Directors of Finance taking on the role across multiple Boards. The Finance and Performance Management Director from the State Hospitals Board for Scotland has taken on the same role, two days a week, at the National Waiting Times Centre Board. This collaborative approach is being trialled to facilitate sharing of best practice between Boards.

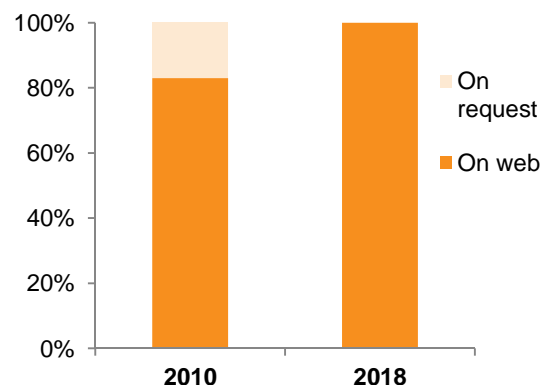
Openness and transparency

83. One of the sector risks identified by Audit Scotland for 2017/18 relates to public sector organisations keeping pace with public expectations relating to openness and transparency.
84. 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. 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.

85. As Exhibit 8 below highlights, our research in 2018 found that the variation that Audit Scotland reported in the availability of Board papers has been addressed.

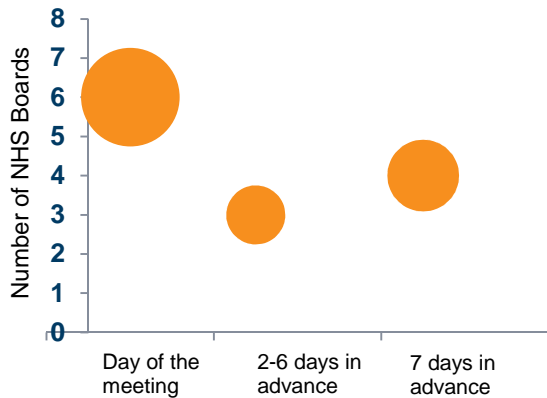
Exhibit 8: Availability of Board papers



In 2010, 17% of NHS Boards made board papers available on request only. By 2018 all NHS Board papers were available on the organisations' websites.

86. 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.
87. However Exhibit 9 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 9: Timing of availability of Board papers



We found only 4 NHS boards in Scotland that committed to making Board papers available a week in advance of their meetings.

Source: Review of NHS Board websites March - May 2018

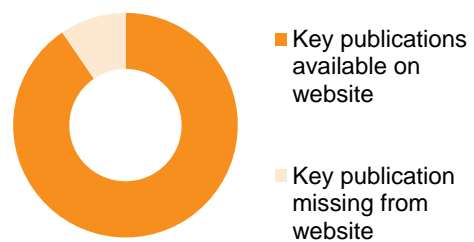
- 88. The Board’s Standing Orders do not specify timetables for publication of agenda items publically, although we note that the schedule of board meetings is available for the full calendar year, and includes location details.
- 89. Audit Scotland’s NHS in Scotland 2017 overview report stressed that 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.
- 90. Our own research highlights that, 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.
- 91. Only two NHS Boards in Scotland make other key committee papers available publicly. We

would support any future review of openness and transparency at the Board, including consideration of the sensitivity of Audit Committee papers, and therefore whether there is scope to make papers available publicly.

Openness Benchmarking

- 92. The following exhibits (Exhibit 10 and 11) highlight the results of our assessment of other key openness indicators, and our commentary on the Board.

Exhibit 10: Availability of key publications



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

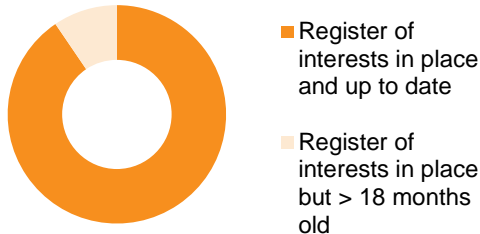
- 93. For all but two NHS Boards in Scotland, we found that all key publications by which the Board can be held to account by the public were found on the website including the annual accounts, results of the annual review and Local Delivery Plan/Annual Operational Plan.

Our assessment of the Board	Green
All key documents were found on the website, and the publications section of the website is helpful and appears to be up to date	

Disclosure of Interests

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

Exhibit 11: Disclosure of interests



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

Our assessment of the Board

Green

The register of interest for executive and non-executive members is updated annually and the 2017/18 register is available on the website. We also note that declarations of interest are required at the start of each Board and Committee meeting.

Risk Management

95. The Board continues to have an appropriate risk management framework in place. During 2017/18, the Board updated their Risk Management Strategy, further strengthening arrangements.

Disclosure of Risks

96. As part of our assessment of Board openness, we reviewed the top risks across NHS Scotland, as disclosed in Boards' annual accounts and risk registers (where publically available). We found that there are a number of strong themes across the NHS in Scotland as Exhibit 12 outlines:

Exhibit 12: 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

Information Governance

Cyber Security

97. 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'.
98. 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.
99. The Board are in the process of implementing all actions outlined within the plan, including finalising the Cyber Incident Response Plan. In the interim, all cyber issues are brought to the attention of the Senior Management Group and IT Sub Group.

General Data Protection Regulations

100. The General Data Protection Regulations 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, the Act has brought in new legislative duties for the Board. The regulations bring significant potential penalties for non-compliance.

- 101.** The Board has used guidance issued by the Information Commissioner's Office to develop an action plan to demonstrate compliance with the new regulations. At the last update, the Board was on track for compliance before the 25 May deadline. The Board's revised privacy policy was published on its website in May 2018.
- 102.** Compliance with the Regulations is an ongoing process, which we will continue to monitor as part of our annual audit procedures in the future. We have not identified any significant risks to compliance with the regulations at this stage.

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 the Board's own reporting of its performance.

Value for money



The Board has appropriate performance management arrangements in place that support the achievement of value for money.

Progress has been made towards achievement of the local priorities and five out of thirteen LDP targets are on target for 2017/18.

Performance management arrangements

103. The Board has developed a performance management framework and receives reports on organisational performance and finance each quarter. An annual overview of performance is also prepared, which is available on the Board's website.

Key Performance Indicators

104. The Board identified 13 local key performance indicators (KPIs) in 2017/18. Progress against these KPIs has been reported in the Annual Report and Accounts for the year ended 31 March 2018.

105. Five of the thirteen reported KPIs were on target for 2017/18. In comparison to 2016/17², four KPIs had improved; four were comparable and in the following four performance had declined:

- Sickness absence: 8.52% (2016/17: 8.35%)
- Patients engaged in psychological treatment: 94.4% (2016/17: 96.4%)
- Patients engaged in off-hub activity: 78.7% (2016/17: 79.3%)
- Patients discharged/transferred using the Care Programme Approach: 97% (2016/17: 100%)

Nursing overtime

106. Nursing overtime costs continue to be a significant cost pressure for the Board. Due to the nature of the service provided by the Board, all nursing shifts which are scheduled and are then affected by either sickness or high levels

of clinical intensity need to be filled in order to maintain safe staff levels. As such, the Board incurs higher levels of overtime costs than territorial health boards.

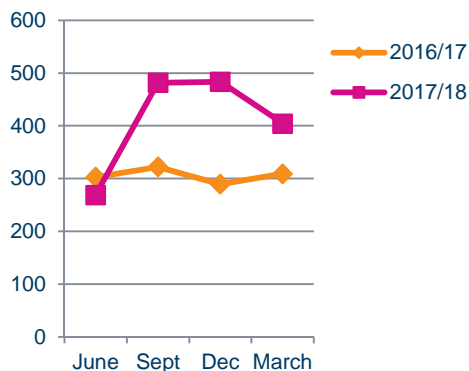
107. As at the end of December 2017, the Board was projecting an overspend of £0.3million in respect of nursing overtime costs. Managing overspends due to nursing overtime continues to be a challenge for the Board and the level of overspend is consistent with the prior year.

108. In February 2018, the Board identified a range of actions in an attempt to reduce the overspends towards the end of the financial year. Actions included, for example, delaying any non-essential training and suspending secondments to the Nursing Practice Development Team for the last two months of 2017/18. These actions were effective and the Board achieved a breakeven position by 31 March 2018.

109. However, the Board do not consider these actions to be sustainable and they only provide a short term solution. In order to reduce overtime costs in the long term, the Board will need to introduce significant changes to the current practices.

110. Whilst overtime levels have reduced since December 2017, costs in the first quarter of 2018/19 are expected to be higher than they were for the same timeframe in 2017/18. The Board have observed that overtime levels are often cyclical, as supported by exhibit 13 and so more meaningful comparisons can be drawn with the prior year.

² In 2016/17 12 key performance measures were in place. Physical activity of patients was also measured in 2017/18.

Exhibit 13: Nursing overtime costs

-
- 111.** As highlighted in exhibit 13 nursing overtime costs have continued to rise., despite closer monitoring taking place at the Board. This suggests that further action is needed as an immediate priority.
- 112.** The Board has acknowledged this and discussed nursing overtime at a Board workshop held in May 2018. Senior Management identified eight areas to look at and deemed half of these to be a priority. A sustainability group will be set up in 2018/19 to plan and implement long term measures, such as changing shift patterns, in the hope to reduce overtime costs. The group, comprising staff from finance, HR and nursing, will also look at immediate measures to manage overtime costs in the short term.
- 113.** The sustainability group should review the data that is available and look to develop an action plan in the immediate future. This should be subject to regular scrutiny by the Board.
- 114.** The Board should identify ways of measuring the effectiveness of these actions. As demonstrated in exhibit 13, costs have continued to rise despite the Board monitoring this as a high risk area and implementing actions to address this. Hence is it essential that the Board monitor the impact of their actions to enable effective management of overtime costs.

Action plan point 3

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 report and 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

We audit the annual report and 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 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 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 by exception 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 the 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 financial statements, but providing audit judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability.

The Code frames a significant part of our wider scope responsibilities in terms of four audit dimensions. As part of our annual audit we consider and report against these four dimensions: financial management; financial sustainability; governance and transparency; and value for money.

Independence

We are required by International Standards on Auditing to communicate on a timely basis all facts and matters that may have a bearing on our independence. We can confirm that we have complied with the Financial Reporting Council's Ethical Standards. In our professional judgement the audit process has been independent and our objectivity has not been compromised. 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.

With regard to our appointment for a second term, we can confirm that we comply with FRC's Revised Ethical Standard which states that careful consideration must be given once an audit engagement partner has held the role for a continuous period of ten years. Therefore, the new appointment for a second five year term does not contradict the requirement of the Revised Ethical Standards. This is in line with guidance from Audit Scotland which states that there is no expectation for the rotation of audit partners for special health board audits.

Appendix 2: Action plan

Our 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, Risk & Recommendation	Management Comments
1. Asset register	<p>Issue</p> <p>During our audit we noted that a number of the Board's PPE and Intangible assets had been fully written down but are still in use. This is a particular issue in respect of the Board's IT assets.</p>	<p>Asset lives will be reviewed in 2018/19 as part of the annual review and this will be considered. However, it should be noted that the current useful lives have been assessed on a prudent basis and that, in certain cases, assets (where still serviceable and where no risk identified) have been used for longer periods due to constraints and prioritisations on capital funding.</p>
Rating		
Grade 2	<p>As these assets are still in use it would appear unreasonable for them to be fully depreciated and would suggest that the estimated useful life applied is inaccurate.</p>	
Paragraph ref		<p>Responsible officer: Finance and Performance Management Director</p>
40	<p>Risk</p> <p>There is a risk that the value of assets held on the balance sheet is understated.</p>	<p>Implementation date: January 2019</p>
	<p>Recommendation</p> <p>The Board should consider the remaining useful life of assets on an annual basis, as part of the verification exercise, and ensure that any changes are correctly reflected in the fixed asset register.</p>	

Action plan point	Issue, Risk & Recommendation	Management Comments
2. Testing of IT back ups	<p>Issue</p> <p>System back-ups are only tested as and when required, and there is no formal testing programme. The system was fully tested in 2016/17 but this was a reactive measure to issues identified during the year.</p>	<p>This is noted and a timetable for back-up testing will be established.</p> <p>Responsible officer: Head of eHealth</p> <p>Implementation date: September 2018</p>
Rating	<p>Risk</p> <p>There is a risk that IT back-ups do not work correctly as they are not subject to regular testing.</p>	
Grade 2	<p>Recommendation</p> <p>IT back-ups should be tested on a regular basis, in line with an established timetable. Evidence should be retained to confirm that this exercise has been completed.</p>	
Paragraph ref		
43		

Action plan point	Issue, Risk & Recommendation	Management Comments
3. Nursing overtime costs	<p>Issue</p> <p>Nursing overtime costs continue to be a pressure for the Board and threatened the achievement of a break even position in 2017/18. Remedial action was taken by the Board however these measures are not considered sustainable.</p>	<p>An action plan is currently under development, following a Board workshop in May 2018. Once complete, reports on these actions will be presented regularly to Board for review.</p> <p>Responsible officer: Nursing and AHP Director</p> <p>Implementation date: August 2018</p>
Rating	<p>The Board has identified this as a key priority for 2018/19 and immediate action is required to address overtime costs in both the short and long term.</p>	
Grade 4	<p>Risk</p> <p>There is a risk that the Board does not achieve its key financial targets, due to the ineffective management of overtime.</p>	
Paragraph ref	<p>Recommendation</p> <p>An action plan should be developed and supported by clear performance measures to assess the impact of the actions. The action plan and supporting measures should be subject to regular review by the Board.</p>	
114		

Appendix 3: Follow up on prior year action plan

	Issue & Recommendation	Management Comments	2018 update
1. Financial Sustainability	<p>The Board's LDP covers a three year period, and is supported by a five year capital plan.</p> <p>In our view, all NHS boards should develop longer term financial plans on a 5 to 10 year basis. This would assist the Board in highlighting risks to the financial sustainability of its service model over the longer term, allocating resources to the services with highest demand and identifying opportunities for strategic service redesign.</p>	<p>A 5-10 year plan will be developed when preparing the 2018/19 LDP.</p> <p>Action owner: Finance and Performance Management Director</p> <p>Due Date: 31 March 2018</p>	<p>The Board have developed a one year AOP.</p> <p>Since we raised this point, effort has been directed into shaping longer term national financial plans rather than at the Board level. While these are in draft at the time of audit, they are expected to be finalised during Summer 2018.</p>
Rating			
Grade 3			



Scott-Moncrieff
business advisers and accountants

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