



## NHS Lothian

2020/21 Annual Audit Report to the Board  
and the Auditor General for Scotland

July 2021



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# Key messages








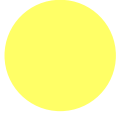
This report concludes our audit of NHS Lothian for 2020/21, with unqualified audit opinions.

This section summarises the key findings and conclusions from our audit.

## Financial statements audit

<b>Audit opinion</b>	<p>Our independent auditor's report includes:</p> <ul style="list-style-type: none"><li>• An unqualified opinion on the financial statements;</li><li>• An unqualified opinion on regularity; and</li><li>• An unqualified opinion on other prescribed matters.</li></ul>
<b>Key findings on audit risks and other matters</b>	<p>COVID-19 continues to present unprecedented challenges to the operation, financial management and governance of organisations, including public sector bodies. In response to the pandemic we considered potential areas of increased risk of misstatement to the financial statements and/or our audit opinion. Our work in all these areas produced satisfactory results.</p> <p>We identified no material adjustments to the unaudited annual accounts.</p> <p>The Board had appropriate administrative processes in place to prepare the annual report and accounts and the required supporting working papers.</p>
<b>Accounting systems and internal controls</b>	<p>We have applied our risk-based methodology to the audit. This approach requires us to document, evaluate and assess the Board's processes and internal controls relating to the financial reporting process.</p> <p>Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we have included these in this report. No material weaknesses or significant deficiencies were noted.</p>

## Wider scope audit

 <p><b>Financial Sustainability</b></p>	<p><b>Auditor judgement</b></p>	
<p>Whilst acknowledging the uncertainty and significant impact of COVID-19, NHS Lothian still needs clearer plans for financial sustainability (including where and how savings will be delivered in response to increasingly significant medium-term challenges). The April 2021 Financial Outlook &amp; Financial Plan paints a stark picture over the next five years, with significantly increased funding shortfalls, underlining the challenge to balance performance and available resources.</p>		
 <p><b>Financial Management</b></p>	<p><b>Auditor judgement</b></p>	
<p>NHS Lothian has effective overall arrangements in place for financial management and the use of resources, albeit it continues to face significant resource pressures. The impact of COVID-19 on 2021/22 and beyond is a significant uncertainty.</p>		
 <p><b>Governance &amp; Transparency</b></p>	<p><b>Auditor judgement</b></p>	
<p>We are satisfied that there has been effective scrutiny, challenge and informed decision making throughout 2020/21 in this area.</p>		
 <p><b>Value for Money</b></p>	<p><b>Auditor judgement</b></p>	
<p>An established and appropriate performance management framework is in place at NHS Lothian. However, COVID-19 has significantly disrupted core service delivery and the challenge facing NHS Lothian as it looks to fully remobilise services and improve against the wide range of performance metrics in the medium term has never been more demanding.</p>		

## Definition

We have used the following grading structure to provide an overall assessment of the arrangements in place as they relate to the four dimensions of the wider scope audit.



# Introduction



We carried out our audit in accordance with Audit Scotland's Code of Audit Practice and maintained auditor independence



## Scope

1. We outlined the scope of our audit in our External Audit Plan, which we presented to the Audit and Risk Committee at the outset of our audit. The core elements of our work included:
  - an audit of the 2020/21 annual report and accounts and related matters;
  - consideration of the wider dimensions of public audit work, as set out below;
  - monitoring the Board's participation in the National Fraud Initiative (NFI); and
  - any other work requested by Audit Scotland.

## Audit dimensions within the Code of Audit Practice



## Responsibilities

2. The Board 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 in this report 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 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.
3. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.
4. We would like to thank all management and staff for their co-operation and assistance during our audit.



## Auditor independence

5. 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.
6. We confirm that we complied with the Financial Reporting Council's (FRC) Ethical Standard. In our professional judgement, we remained independent and our objectivity has not been compromised in any way.
7. We set out in Appendix 1 our assessment and confirmation of independence.

## Openness and transparency

10. This report will be published on Audit Scotland's website [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

## 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 any member of your audit team.

# Financial statements audit

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The Board's annual report and accounts are a principal means of accounting for the stewardship of its resources and its performance in the use of those resources.

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## Overall conclusion

11. Our independent auditor's report includes:

- 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.

## Our audit opinions

Opinion	Basis for opinion	Conclusions
Financial statements	<p>We conduct our audit in accordance with applicable law and International Standards on Auditing.</p> <p>Our findings / conclusion to inform our opinion are set out in this section of our annual report.</p>	<p>We have issued unqualified audit opinions.</p>
Regularity	<p>We plan and perform our audit recognising that non-compliance with statute or regulations may materially impact on the annual report and accounts.</p>	<p>We did not identify any instances of irregular activity.</p> <p>In our opinion in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with applicable enactments and guidance issued by the Scottish Ministers.</p>
Going concern basis of accounting	<p>In the public sector when assessing whether the going concern basis of accounting is appropriate, the anticipated provision of services is more relevant to the assessment than the continued existence of a particular public body.</p>	<p>We reviewed the financial forecasts for 2021/22. Our understanding of the legislative framework and activities undertaken provides us with sufficient assurance that there are no material uncertainties relating to going concern and management's use of the going</p>

Opinion	Basis for opinion	Conclusions
	<p>We assess whether there are plans to discontinue or privatise the board's functions.</p> <p>Our wider scope audit work considers the financial sustainability of the board.</p>	<p>concern basis of accounting is appropriate.</p>
<p>Matters prescribed by the Auditor General for Scotland:</p> <ul style="list-style-type: none"> <li>• Remuneration and Staff Report</li> <li>• Performance Report</li> <li>• Governance Statement</li> </ul>	<p>We read all the financial and non-financial information in the annual report and accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us while performing the audit.</p> <p>We plan and perform audit procedures to gain assurance that the statutory other information has been prepared in accordance with directions from Scottish Ministers.</p>	<p>The annual report contains no material misstatements or inconsistencies with the financial statements.</p> <p>We have concluded that:</p> <ul style="list-style-type: none"> <li>• 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.</li> <li>• the information given in the performance report has been prepared in accordance with directions from Scottish Ministers and is consistent with the financial statements.</li> <li>• the information given in 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.</li> </ul>
<p>Matters reported by exception</p>	<p>We are required to report on whether:</p> <ul style="list-style-type: none"> <li>• adequate accounting records have not been kept; or</li> <li>• the financial statements and the audited part of the</li> </ul>	<p>We have no matters to report.</p>

Opinion	Basis for opinion	Conclusions
	<p>Remuneration and Staff Report are not in agreement with the accounting records; or</p> <ul style="list-style-type: none"> <li>we have not received all the information and explanations we require for our audit; or</li> <li>there has been a failure to achieve a prescribed financial objective.</li> </ul>	

## An overview of the scope of our audit

- The scope of our audit was detailed in our External Audit Plan, which was presented to the Audit and Risk 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.
- 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.
- In our audit, we test and examine information using sampling and other audit techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain evidence through reviewing the significant accounting systems, substantive

procedures and detailed analytical procedures.

## Significant risk areas

- Significant risks are defined by professional standards as risks that, in the judgement of the auditor, require special audit consideration. In identifying risks, we consider the nature of the risk, the potential magnitude of misstatement, and its likelihood. Significant risks are those risks that have a higher risk of material misstatement.
- The significant risk areas described in the table below 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 below.

## Significant risk areas

### 1. Management override

#### Significant risk description

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

**Risk assessment: High**

#### How the scope of our audit responded to the significant risk

##### Key judgement

There is the potential for management to use their judgement to influence the financial statements as well as the potential to override the board's controls for specific transactions.

##### Audit procedures

- Review of the board's accounting records and audit testing on transactions.
- Adoption of data analytics techniques in carrying out testing.
- Review of judgements and assumptions made in determining accounting estimates as set out in the financial statements to determine whether they are indicative of potential bias. This included consideration of the prior year estimates against the current year estimates.

#### Key observations

We have not identified any indication of management override in the year leading to material misstatement or significant concern. We have reviewed the Board's accounting records and obtained evidence to ensure that transactions outside normal processes 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.

## Significant risk areas

### 2. Revenue recognition

**Significant risk description** 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 and expenditure transactions in such a way as to lead to a material misstatement in the reported financial position.

**Risk assessment: High**

**How the scope of our audit responded to the significant risk**

#### Key judgements

Given the financial pressures facing the public sector as a whole, there is an inherent fraud risk associated with the recording of accruals and prepayments around the year end.

#### Audit procedures

- Evaluate each material revenue stream and review controls over revenue accounting.
- Substantive testing on all material revenue streams.
- Audit testing over the revenue recognition policy to ensure it is appropriate and applied consistently throughout the year.

**Key observations**

We have gained reasonable and appropriate assurance on the completeness and occurrence of income, including the board's revenue resource allocation from Scottish Government. To inform our conclusion, we have evaluated the type and extent of revenue transactions and reviewed the controls in place over revenue accounting. We carried out substantive testing to confirm that the board's revenue recognition policy is appropriate and has been applied consistently throughout the year.

We have gained reasonable and appropriate assurance that this area is free from material misstatement, however we have raised a management action point to revise the current approach to how research and development income, which is pertinent to commercial contracts, is recognised in line with IFRS 15. We do not deem this to be material to the financial statements and have noted an unadjusted difference in relation to this (Appendix 2).

**Action plan point 1**

## Significant risk areas

### 3. Expenditure recognition

**Significant risk description** As most public sector bodies are net spending bodies, the risk of fraud is more likely to occur in expenditure. There is a risk that expenditure may be misstated resulting in a material misstatement in the financial statements.

**Risk assessment: High**

**How the scope of our audit responded to the significant risk**

#### Key judgements

Given the financial pressures facing the public sector as a whole, there is an inherent fraud risk associated with the recording of accruals around the year end.

#### Audit procedures

- Evaluate the significant non-pay expenditure streams and review the controls in place over accounting for expenditure. (Payroll is subject to separate tailored testing).
- Consider the board's key areas of expenditure and obtain evidence that expenditure is recorded in line with appropriate accounting policies and the policies have been applied consistently across the year.
- Review of accruals around the year end to identify any indication of understatement of balances held through consideration of accounting estimates.

**Key observations**

We have evaluated each type of expenditure transaction and documented our conclusions. We gained reasonable assurance over 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 the board's policy for recognising expenditure is appropriate and has been applied consistently throughout the year.



## Significant risk areas

### 4. Capital transactions

#### Significant risk description

The board holds a significant level of high value estate. The estate is valued on a five-year cycle, with an element being subject to valuation each year. In the prior year, the valuation recognised a material uncertainty, indicating that lower confidence could be attached to the valuation than otherwise would be the case given the unprecedented impact of COVID-19 on global markets. We included an emphasis of matter paragraph in our independent auditor's report on the 2019/20 financial statements to draw attention to this.

**Risk assessment: High**

#### How the scope of our audit responded to the significant risk

##### Key judgements

Boards are required to ensure properties are held at a carrying amount that does not differ materially from the current value at 31 March, including taking cognisance of changes in the asset base.

##### Audit procedures

Review capital transactions and balances, and assess their quantum and nature against accounting standards, the Government Financial Reporting Manual ('the FReM'), the NHS Capital Accounting Manual, and the Board's accounting policies. Include external experts (eg valuation experts) and assess their work and outcomes as part of this audit assessment.

#### Key observations

##### Additions and completed assets

During 2020/21, the board reported capital additions of £83.609million and completions of £73.752 million. We have reviewed these capital transactions and gained assurance that they have been accounted for in line with the FReM, the NHS Capital Accounting Manual and the Board's accounting policies.

In 2019/20, we noted £8.7million of brought forward assets under construction which should have been recognised as a completion under the appropriate asset category. NHS Lothian committed to reviewing balances as part of internal year end procedures, to identify all completions and enhancements to ensure appropriate accounting treatment in 2020/21. Due to resourcing constraints and the impact of COVID-19 this exercise was not fully completed, with resource focused on reviewing higher value projects. From our audit work, we have identified £2.7million of assets under construction that

## Significant risk areas

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should have been recognised as completions in 2020/21. We have noted an unadjusted difference in relation to the classification of these assets.

### **Prior Year Action Plan – Appendix 4**

We identified a capital accrual for £508k that relates to a disputed transaction with a public sector partner. This transaction dates back to 2014. No recent action has been taken to resolve this dispute. The initial value of the transaction was £342k, with the Board annually accruing interest to reflect a potential late payment charge. We recommend that NHS Lothian takes appropriate steps to resolve this dispute to ensure the transaction is appropriately accounted for.

### **Action Plan Point 2**

#### **Valuation**

We have gained assurance that the carrying value of the Board's estate in the financial statements is in line with the valuer's report received from the external valuers (Avison Young). In accordance with ISA (UK) 500 "Audit Evidence" we have considered the competence, capability and objectivity of the professional valuer and did not identify any items which gave us cause for concern over the suitability of the valuer. We confirmed that the basis of valuation for assets is appropriate based on their usage and reviewed the reasonableness of valuation assumptions applied. Overall, the valuation movements were in line with our expectation.

The valuation report provides assurance that, whilst the pandemic continues to affect economies and global markets, property markets have started to function again and, as a result, the valuation as at 31 March 2021 is not subject to a material valuation uncertainty. This is consistent with the latest guidance issued by the Royal Institution of Chartered Surveyors.

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## Significant risk areas

### 5. PFI and related assets

#### Significant risk description

NHS Lothian 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. More recently, a Non-Profit Distributing Model (NPD) agreement has been entered into and commenced. The cumulative estimated base capital value of these agreements is in excess of £390 million.

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.

**Risk assessment: High**

#### How the scope of our audit responded to the significant risk

##### Key judgements

Given the financial pressures facing the public sector as a whole, there is an inherent fraud risk associated with the recording of provisions around the year end.

##### Audit procedures

- Review and update understand of the board's range of such agreements.
- Consider compliance with the requirements of the FReM and NHS Manual for Accounts.

#### Key observations

We have reviewed the board's PPP/PFI/NPD accounting and related commitment disclosures against the requirements of the FReM, the Manual and against the supporting contracts. We have also reviewed relevant aspects of the transactions against the NHS Scotland Capital Accounting Manual. A disclosure adjustment was identified and corrected in relation to the Royal Infirmary Edinburgh, but no further exceptions were identified.

## 6. Provisions - CNORIS (significant accounting estimate)

### Significant risk description

The Board in its financial statements includes provisions for legal obligations, for example in respect of clinical and medical obligations and participation in CNORIS (Clinical Negligence and Other Risks Indemnity Scheme).

There is a significant degree of subjectivity in the measurement and valuation of provisions. This subjectivity represents an increased risk of misstatement in the financial statements.

**Risk assessment: High**

### How the scope of our audit responded to the significant risk

#### Key judgements

Given the financial pressures facing the public sector as a whole, there is an inherent fraud risk associated with the recording of provisions around the year end.

#### Audit procedures

- Review management's estimation for the provision and related disclosures
- Consider compliance with the requirements of the FReM and NHS Manual for Accounts.
- Consider the competence, capability and objectiveness of the management expert in line with ISA (UK) 500 Audit Evidence.

### Key observations

We are satisfied that the amount recognised as a provision appropriately reflects the amounts notified by the Central Legal Office (CLO). We have reviewed management's estimation of the provision and related disclosures, and are satisfied that these comply with the requirements of the FReM and NHS Manual for Accounts.

Audit Scotland undertake an annual review of the work carried out by the CLO to establish the extent to which the information they provide as a management expert can be used as audit evidence under ISA (UK) 500 and evaluate the appropriateness of the methodology adopted by Scottish Government to estimate the total national obligation. Audit Scotland has concluded that the CLO is objective, has sufficient expertise and the capability, time and resource to deliver reliable information. Their review did not identify any issues in the methodology used by Scottish Government, however noted that due to the impact of COVID-19 a simplified methodology had been used which they deemed reasonable in the circumstances.

## Other risk factors

### COVID-19 and personal protective equipment and testing kits

18. Personal protective equipment (PPE) and testing kits were purchased nationally by NHS National Services Scotland (NSS) during 2020/21 and distributed to NHS Boards at nil cost to each board. Each health board is deemed to be acting as principal in its use of PPE and testing kits for its own frontline staff and therefore should recognise the costs and corresponding funding allocations in its financial statements.
19. NSS has provided the Board with estimates of the costs of equipment provided (£21.397million). The Scottish Government has provided an amended funding allocation letter to reflect the cost of equipment funded by the Scottish Government. The cost of equipment supplied by the UK Government has been recognised as a donation. As all of the PPE was fully funded there is no net effect on the Board's resource outturn.
20. There were significant delays in agreeing the accounting treatment

with Scottish Government and the provision of relevant cost estimates.

21. Audit Scotland, as the external auditor of NSS, has reviewed the methodology and systems used to arrive at the estimated costs to provide assurances to the recipient health boards and their auditors on the accuracy of the estimates. There were no issues identified.

### Other impacts of COVID-19 on the annual accounts

22. COVID-19 continues to present unprecedented challenges to the operation, financial management and governance of organisations, including public sector bodies. In response to the pandemic we identified potential areas of increased risk of material misstatement to the financial statements and/or our audit opinion. Our summary conclusions are set out in the table below.

Area considered	Description	Conclusion
<p><b>Content of the annual report and accounts</b></p>	<p>In response to the continuing impact of COVID-19 HM Treasury has issued an addendum to the Government Financial Reporting Manual 2020/21 which sets out the minimum reporting requirements in respect of the performance report and accountability report.</p> <ul style="list-style-type: none"> <li>• The addendum permits, but does not require, bodies to omit the performance analysis section from the Performance Report. Where relevant performance information has already been published elsewhere, bodies are encouraged to refer to the relevant publication.</li> <li>• Where unaudited information otherwise required to be included in the Accountability Report is already published elsewhere, bodies are permitted to refer to the relevant publication rather than including the information in their Accountability Report.</li> </ul>	<p>The Board has included a range of relevant and appropriate performance information in the accounts.</p>
<p><b>Access to audit evidence</b></p>	<p>Our audit this year has, in the main, been carried out remotely. As a consequence, we identified a risk that access to and provision of sufficient, appropriate audit evidence in support of our audit opinion may be impacted by the inherent nature of carrying out our audit remotely.</p>	<p>We have employed a greater use of technology to examine evidence, but only where we have assessed both the sufficiency and appropriateness of the audit evidence produced.</p> <p>We stayed in close contact with board finance colleagues right up until the point of accounts signing, to ensure all relevant issues were satisfactorily addressed.</p>

Area considered	Description	Conclusion
Timescales / administrative processes	<p>In Scotland, the administrative deadline for the submission of audited accounts of health boards and agencies is usually 30 June but this has been extended by three months to 30 September. The legislative deadline for laying accounts in the Scottish Parliament remains 31 December.</p>	<p>The Board decided to continue with the original timescales (ie 30 June), however due to the national accounting issue regarding PPE, the approval of the annual report and accounts was delayed, but was still within the deadlines.</p> <p>We worked closely with management throughout the audit to put us in the best position to adhere to this timetable.</p>

## Estimates and judgements

- 23. We are satisfied with the appropriateness of the accounting estimates and judgements used in the preparation of the financial statements.
- 24. As part of audit planning we identified all accounting estimates made by management and determined which of those are key to the overall financial statements. Consideration was given to asset valuations, impairment, depreciation and amortisation rates, aspects of leases, provisions for legal obligations and doubtful debts, and

accruals. Other than asset valuations and provisions for legal obligations, we have not determined the accounting estimates to be significant. We revisited this assessment during the fieldwork and completion stages of our audit and concluded that our assessment remained appropriate.

- 25. Our audit work consisted of reviewing these keys areas for any indication of bias and assessing whether the judgements used by management are reasonable. We have summarised our assessment of this below, categorising each area as either Prudent, Balanced or Optimistic.

## Estimates and judgements

### Asset valuations

Balanced

Asset valuations are carried out by external valuers on an annual basis.

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 experts was appropriate.

### Provisions

Balanced

Significant estimates were made in relation to the valuation of liabilities related to the Board's membership of the Clinical Negligence and Other Risks Indemnity Scheme (CNORIS). These estimates were 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 experts was appropriate.

## Materiality

26. Materiality is an expression of the relative significance of a matter in the context of the financial statements as a whole. A matter is material if its omission or misstatement would reasonably influence the decisions of an addressee of the auditor's report. The assessment of what is material is a matter of professional judgement and is affected by our assessment of the risk profile of the organisation and the needs of users. We review our assessment of materiality throughout the audit.

27. Whilst our audit procedures are designed to identify misstatements

which are material to our audit opinion, we also report to the Board and management any uncorrected misstatements of lower value errors to the extent that our audit identifies these.

28. Our initial assessment of materiality for the financial statements was £25.5million. On receipt of the 2020/21 draft accounts, we reassessed materiality and updated it to £30million. We consider that our updated assessment has remained appropriate throughout our audit.



## Materiality

### Overall materiality

£30million



100%

Accounts materially misstated where total errors exceed this value

### Performance materiality

£19.5million



65%

Work performed to capture individual errors at this level

### Trivial threshold

£250,000



De minimis

All errors greater than this level are reported

### Materiality

Our assessment is made with reference to the Board's Revenue Resource Limit (RRL). Achieving a breakeven position against RRL is a key target for the Board and one of the principal considerations for the users of the financial statements when assessing financial performance.

### Performance materiality

Performance materiality is the working level of materiality used throughout the audit. We use performance materiality to determine the nature, timing and extent of audit procedures carried out. We perform audit procedures on all transactions, or groups of transactions, and balances that exceed our performance materiality. This means that we perform a greater level of testing on the areas deemed to be at significant risk of material misstatement.

Performance materiality is set at a value 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 overall materiality. Using our professional judgement we have calculated performance materiality at approximately 65% of overall materiality.

### Trivial misstatements

Clearly trivial misstatements are matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

We noted within our External Audit Plan that we would report to the Board all audit differences in excess of £250,000, as well as differences below that threshold which, in our view, warranted reporting on qualitative grounds. We also report on disclosure matters that we identify when assessing the overall presentation of the annual accounts.

## Group audit

29. 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).
30. As group auditors under ISA (UK) 600 we are required to obtain sufficient appropriate audit evidence regarding the financial information of the components and regarding the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.
31. The Endowment Fund is fully consolidated. The integration 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, circumstances and basis of accounting, likely to include significant risks of material misstatement of the group financial statements.
32. As part of our audit we reviewed the consolidation entries made within the group accounts for the Endowment Fund and confirmed those entries back to the financial statements.
33. Azets Audit Services conducted the audit of the Endowment Fund. During our audit we liaised with the separate Endowment Fund audit team to confirm that their programme of work is adequate for our purposes, including to ensure this considers COVID-19 risks and impact.
34. We have nothing to report in respect of the following matters:
  - No significant deficiencies in the system of internal control or instances of fraud were identified by the Endowment Fund auditor; and
  - There were no limitations on the group audit.

## Audit differences

35. We identified no material adjustments to the unaudited annual accounts.
36. We identified two unadjusted differences which are considered immaterial and are outlined in Appendix 2. These relate to (i) adjustment of £1.7m in relation to timing of recognition of research income, and (ii) £2.7m of assets under construction that should have been recognised as a completion.
37. We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of accounts. This included updates and additional disclosures in relation to the remuneration report,

accounting policies, and in the staff report/fair pay disclosure.

## Internal controls

38. As part of our work we considered internal controls relevant to the preparation of the financial statements such that we were able to design appropriate audit procedures. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we report these to the Board. These matters are limited to those which we have concluded are of sufficient importance to merit being reported.

Area	Assessment	Comment
Control and process environment	<b>Satisfactory</b>	We consider the control environment within the board to be satisfactory.
Quality of supporting schedules	<b>Satisfactory</b>	The supporting schedules received during the course of the fieldwork were sufficient for our audit purposes.
Responses to audit queries	<b>Satisfactory</b>	Management's responses to our audit queries were appropriate and generally received on a timely basis.

## Service auditor reports

39. The Board utilises a number of shared IT systems, IT applications and processes with other Scottish Health

Boards. Assurance reports are prepared by service auditors in the health sector under ISA (UK) 402 covering the national systems/arrangements.

Shared service	Service assurance
<p><b>National Practitioner and Counter Fraud Services</b></p> <p>This contract supports accurate payments and patient registration for NHS services to Scotland's GPs, dentists, pharmacists, and optometrists.</p>	<p>NHS National Services Scotland (NSS) procures a service auditor report from KPMG. In May 2021 KPMG reported a qualified audit opinion. We considered the findings of the report and are satisfied that this does not have a material impact on our audit approach or conclusions reached. We have taken part in and considered national discussions across the service in relation to the audit report outcomes in reaching our conclusions.</p>
<p><b>National IT contract</b></p> <p>This contract covers the services provided by ATOS Origin Alliance e.g. controls over the server supporting eFinancials.</p>	<p>NHS National Services Scotland (NSS) procures a service auditor report from KPMG. In May 2021 KPMG reported an unqualified audit opinion. We have considered the findings of the report and are satisfied that the findings do not have a material impact on our audit approach or conclusions reached.</p>
<p><b>National Single Instance (NSI) eFinancials</b></p> <p>NHS Ayrshire &amp; Arran host this eFinancials service including the Real Asset Management system on behalf of all Scottish Health Boards.</p>	<p>NHS Ayrshire and Arran procure a service auditor report from BDO. The service auditor highlighted no critical or significant risk findings and reported an unqualified opinion.</p>
<p><b>Follow up of prior year recommendations</b></p> <p>40. We followed up on progress in implementing actions raised in the prior year as they relate to the audit of the financial statements. Full details of our findings are included in Appendix 4.</p>	<p>financial statements and consideration of the appropriateness of the accounting policies adopted by the Board.</p> <p>42. The accounting policies, which are disclosed in the annual accounts, are in line with the NHS Accounts Manual and are considered appropriate.</p>
<p><b>Other communications</b></p> <p><b>Accounting policies, presentation and disclosures</b></p> <p>41. Our work included a review of the adequacy of disclosures in the</p>	<p>43. There are no significant financial statements 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.</p>

44. Overall we found the disclosed accounting policies, and the overall disclosures and presentation, to be appropriate.

#### **Fraud and suspected fraud**

45. We have previously discussed the risk of fraud with management. We have not been made aware of any incidents in the period nor have any incidents come to our attention as a result of our audit testing.
46. Our work as auditor is not intended to identify any instances of fraud of a non-material nature and should not be relied upon for this purpose.

#### **Non-compliance with laws and regulations**

47. As part of our standard audit testing, we have reviewed the laws and regulations impacting the Board. There are no indications from this work of any significant incidences of non-compliance or material breaches of laws and regulations that would necessitate a provision or contingent liability.

#### **Written representations**

48. The letter of representation covers a number of issues which we asked the board to confirm to us. This letter was signed on behalf of the board as part of the process of approving the financial statements.

#### **Related parties**

49. We are not aware of any related party transactions which have not been disclosed.

#### **Confirmations from third parties**

50. All requested third party confirmations in respect of bank and legal confirmations have been received.

# 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 and the way in which they should be delivered.



## Auditor judgement



The Financial Outlook & Plan presented to the board in April 2021 paints a stark picture over the next five years with substantial funding gaps beyond anything ever seen in NHS Lothian; £143million in 2022/23, increasing to £177million in 2025/26. These gaps represent 8-9% of full year recurring expenditure budgets, underlining the scale and challenge facing the board as it looks to balance service performance with available resources.

NHS Lothian needs clearer plans for financial sustainability, including where and how savings will be delivered in response to increasingly significant medium-term challenges.

## Significant audit risk

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

### Financial sustainability

In April 2020, the Board and Finance & Resource Committee considered a Financial Plan to support the Annual Operational Plan. The paper outlined a financial gap of £10.8 million in 2020/21 with significant and pronounced increases in the deficit in future years.

COVID-19 has had a fundamental impact on finances and financial planning for 2020/21 and beyond. The Board estimates that it has incurred additional COVID-19 related costs of £53.3million up to the end of October 2020. The achievement of financial balance is dependent on receiving full financial support from the Scottish Government to meet these costs.

The Board continues to face challenges in achieving savings targets, including recurrent savings, in amongst a challenging performance management landscape and unprecedented challenges of responding to COVID-19. The emerging and uncertain impact on the Board's finances and ability to deliver services in a sustainable manner remains a significant challenge and risk.

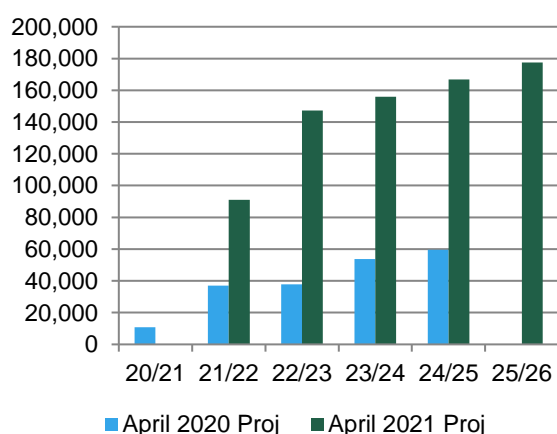
*Noted in the 2020/21 External Audit Plan*

52. We considered how NHS Lothian balances the management of its medium and longer-term financial position with demand and performance targets, and the ongoing work to reflect the impact of COVID-19. We assessed the development and update of financially sustainable operating plans to support the delivery of the Board's statutory functions and strategic objectives.
53. We reviewed NHS Lothian's achievement of the outturn position as part of our work on financial management and the financial statements. This work highlighted that an already difficult balance between the financial resourcing and performance management landscape is expected to become even more challenging and complex, exacerbated by COVID-19 and the simultaneous need to pursue pandemic and wider remobilisation.
54. The board achieved the underspend in 2020/21 due to a combination of close financial management, some reliance on one-off savings, but most particularly the extra funding provided by Scottish Government to cover COVID-19 implications.
55. Our detailed findings on the Board's financial framework for achieving long term financial sustainability are set out below.

## Financial projections

56. NHS Lothian's Financial Outlook & Plan projects a core financial gap of £25.07million in 2021/22 (plus £66million additional COVID-19 costs – funding expected from Scottish Government), with pronounced increases in the deficits in the years thereafter. The two graphs below show the five year outlook, as at April 2021 and 2020 (note: no comparator in 2025/26, given the time horizon of the 2020 outlook). The more-recently updated position is far more significant in terms of size of projected deficit; for example, the gap in 2022/23 has gone from just under £38million to £143million.

### Financial Gap (£'000s) – April 2020 and 2021



Source: 2021/22 and 2020/21 NHS Lothian Financial Outlook & Plan

57. While there are a range of factors underlying these projections, key elements include (i) a £44million baseline gap, (ii) £72million in-year (non-Covid) revised cost growth assumptions, (iii) wider COVID-19

impact, and (iv) minimal efficiency/financial recovery plans in 2022/23 onwards. (The efficiency savings plans reflect only 5%-12.5% of previous levels of savings; indexing 2018/19's £27.1million efficiency savings for 2023/24 would reduce the gap by c.19.2%. Whilst substantial, this still leaves a significant gap and reflects the evolving impact of savings within the range of responses to strategic financial challenges).

58. There are various funding assumptions and recurring/non-recurring funding projections within the Plan which have a net impact of notably increasing future deficit projections.

59. Delivery of savings is a fundamental component of achieving financial balance. For 2021/22, the board has a £25.9m savings plan, with an expected c£19million (73%) being recurring. The savings are as categorised below:

- Acute Services Division: £13.3m
- Corporate Services: £2.1m
- Four IJB/Partnerships: £6.6m
- Facilities & Consort: £2.37m
- Other: £1.54m

60. With delivery of efficiency savings being categorised as "high risk" in the 2021/22 Financial Outlook and the pressures of dealing with COVID-19 alongside remobilisation, this remains a key area of pressure for NHS Lothian.

61. In line with previous financial years, the Finance and Resources Committee has only been able to take limited assurance that the board will achieve financial balance in 2021-22. At this stage, there are no clear plans



to close the financial gap on a recurring basis, and this is exacerbated by the difficult mix of COVID-19 pressures and remobilisation of a range of non-COVID services.

62. NHS Lothian management have reported through the governance structure of the need to keep the financial plan under review and the potential for significant updates as circumstances change or new information emerges. This reflects the complex and increasingly uncertain environment.

### Key assumptions and risks in the Financial Plan

63. There are nine “high risk” items on the Financial Outlook Risk Register (out of a total of twenty risks), including:

- SG COVID-19 allocations (assumed support/cover, but confirmation awaited at time of drafting the Financial Outlook);
- COVID-19 activity;
- Brexit (no cost impact factored in/quantified, but potential pay and non-pay pressure);
- NRAC funding model (0.8% below parity / £14million annual impact);
- Escalation framework (reduced rating reduces funding/additional support);
- Winter Costs (general/per previous practice and COVID-19 related);
- Efficiency savings (risk directorate management cannot devote sufficient focus, including due to COVID-19).

64. The cost pressures identified include the following areas of recurring

expenditure funded from non-recurring sources:

- £15.7m for Hospital Drugs (re the New Medicines Fund);
- £7.1m unscheduled care pressures;
- £2.4m in relation to national services/national distribution centre;
- £2m eHealth investment;
- £1.4m diagnostics, critical care and theatre activity.

65. Pay is identified as the single largest additional cost pressure in 2021/22. The board’s Financial Plan notes that the assumed pay award is measured at 1% for Agenda for Change and other staff. This reflects an additional cost estimated at £16million, but further potential pressures are arising from national proposals for a 4% award (depending on how this is to be funded). £10.2million is also noted as a result of the 2021/22 impact of prior period adjustments to certain pay scale bandings. Other general cost pressures include:

- Acute Prescribing - £14.5m;
- GP Prescribing - £5.5m;
- Lifecycle and PFI costs - £5.3m;
- General non-pay cost inflation of 2% - £4.7m;
- Energy costs - £1.5m.

66. From our review of the financial plans, evolving reviews and updates, and presentations made to the Finance & Resources Committee and NHS Board, it is positive to see the detailed analysis along with clear articulation of the significant risks and uncertainties. The overall projected financial gaps and outturns make for a clear and unambiguous message around the strategic finance risks facing NHS Lothian.

### COVID-19 – a significant and ongoing area of financial risk, challenge and uncertainty

67. COVID-19 is, in itself, an unprecedented challenge and brings significant uncertainty. 2020/21 will have provided insight, experience and data on which to make plans and better understand pandemic pressures. However, NHS Lothian is now facing up to dealing with continued COVID-19 pressures and potentially further pandemic “waves” (of uncertain magnitude) whilst simultaneously addressing the need and expectation to fully remobilise non-COVID services. The pace of this remobilisation creates a near perfect storm of internal and external financial, operational, workforce, political and performance pressures. Keeping all such variables in balance will be extremely challenging and will bring extraordinary strain.
68. As with last year and the outbreak of the pandemic, we expect this is likely to substantially impact financial management actions and may have other adverse impacts such as impairing the ability to deliver savings targets and programmes and using up Finance resource focus, thereby constraining the ability of NHS Lothian to bridge projected deficits. Hitherto, the board has achieved breakeven even with, at times, significant reliance on one-off savings. Whilst the funding gap is not of unprecedented magnitude in 2021/22 compared to previous years, the variables, risks and range of assumptions now seem more complex and significant. Looking ahead to 2022/23 and beyond, it is unclear how financial sustainability can be achieved without a fundamental review of operations and related service redesign.
69. NHS Lothian forecasts additional costs of £66million in 2021/22 associated with COVID-19. This includes:
- £4.5m for a Regional Lab Hub for testing capacity;
  - £5.2m in Test & Protect cost;
  - £6m across East, West and Midlothian partnerships for hospital wards/beds and response teams;
  - Domestic, Portering and Logistics costs of £5m;
  - Vaccinations costs - £9m;
  - £5m GP Prescribing Impact;
  - Extended flu campaign - £2.4m;
  - Income reduction impact of £5m.
70. There is clear evidence of cross-partnership working in resourcing the response to COVID-19 challenges. NHS Lothian has worked with and shared funding with all four IJB partners and, by extension, partner local authorities. We expect this to continue going forward, reflecting a good practice “whole system” approach to proactive and reactive measures in relation to the pandemic.
71. Further, the inclusion of detailed, categorised 2021/22 IJB projections within the NHS Lothian five year financial outlook supports more holistic scrutiny. This includes information on areas/quantum of baseline pressures, recurring/non-recurring resource analysis, financial recovery plan values, and additional IJB COVID-19 cost pressures.

# Financial management

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



## Auditor judgement



NHS Lothian has effective overall arrangements in place for financial management and the use of resources, albeit it continues to face significant resource pressures. 2020/21 saw a “full year” impact of COVID-19, which has brought unprecedented strain and challenge to financial management.

The board met its key financial targets once again in 2020/21, delivering an underspend against its RRL and a breakeven position against its CRL. This was achieved despite the impact of COVID-19 (£111million on a net basis) through close working with Scottish Government and receipt of additional funding to cover the additional COVID-19 costs.

## Financial performance

72. All boards have to work within the resource limits and cash requirements set by the Scottish Government. 2020/21, which represents an underspend of 0.067%. This was in line with the breakeven position targeted and projected by the board.
73. The board delivered an underspend against its RRL of £1.328million in

### Performance against resource limits

Financial target	Limit £000	Actual £000	Variance £000	Target achieved?
Core revenue resource limit	1,983,910	1,982,582	1,328	Yes
Non-core revenue resource limit	94,050	94,050	-	Yes
Capital resource limit	74,771	74,771	-	Yes
Cash requirement	2,053,463	2,053,463	-	Yes

### Delivering financial balance

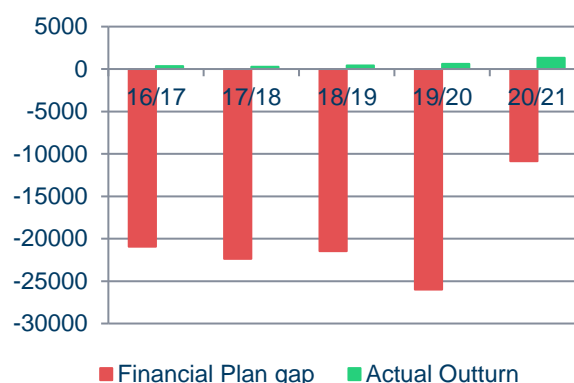
74. The 2020/21 Financial Plan presented to the Board in April 2020 outlined a projected deficit of £10.86million. At the time, the COVID-19 financial implications were still being understood, revised and factored in given the evolving nature of the pandemic. The position was as illustrated:

2020/21 Budget (£000)	
<b>Full year recurring budget</b>	<b>1,703,694</b>
Baseline pressures	(46,562)
Projected expenditure uplifts and commitments	(80,212)
Additional resources:	
Specific pressures	76,367
Overall position	20,995
Financial Recovery Plans	18,552
<b>Financial Plan Gap</b>	<b>(10,860)</b>

75. The financial plan gap represented 0.64% of the full year recurring budget (compared to 1.6% in 2019/20). In line with previous years, limited assurance was given to the Board and the Finance and Resources Committee on achieving a breakeven outturn during early 2020/21. This continued up until the November 2020 meetings. Moderate assurance was then reported in January 2021, and significant assurance was only being provided in March 2021 to the Finance and Resource Committee (based on the financial reporting to the end of January 2021).

76. NHS Lothian has not been able to set a breakeven budget for the past five years. Despite the challenging financial position, NHS Lothian has continued to deliver against financial targets in each year, with COVID-19 funding being a fundamental aspect to delivering this outcome in 2020/21. The board is facing a significant COVID-19 challenge into 2021/22 and beyond, and continues to highlight the adverse impact of the cumulative NRAC funding position in exacerbating this challenge.

### Analysis of outturn against financial plan gaps (£'000)



Source: Annual audit reports & financial statements

77. NHS Lothian has been able to deliver financial targets in recent times in the context of increasing financial pressures from pay changes, growing demographic challenges in Lothian, strategic investment and the implementation of national policies.

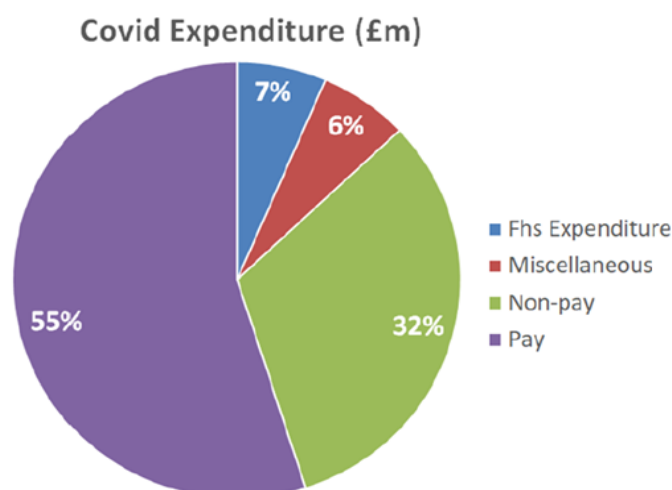
78. The 2020/21 year-end report to the Finance & Resources Committee identified the main areas of saving in pay budgets as being in Administrative Services (£7.3million), Nursing (£1.7million) and Management (£1.18million), and £19million in Administration non-pay budgets. Pay costs overspends relate to Medical (£7.86million) and Support Services (£6.29million), with non-pay overspends in areas including Maintenance (£8.9million), Equipment (£10.5million) and Patient Services Service Agreements (£12.47million).

79. In summary, whilst NHS Lothian achieved an overall underspend against the RRL in 2020/21, the baseline operational overspend was £14.55million which was offset by the net release of reserves flexibility of £15.88million.

## COVID-19 financial analysis

80. NHS Lothian has assessed the net additional costs of COVID-19 in 2020/21 as £111million (£146.4million gross costs, with estimated offset of £35.4million due to activity reductions).
81. Funding received from Scottish Government covered these costs in full, with just over £49million to local authorities and £20.3million to support IJB finances.
82. The pie chart and accompanying breakdown was prepared by NHS Lothian management and shared with the Finance and Resources Committee, to support analysis and scrutiny of COVID-19 spend in 2020/21. We are pleased to note the detail and extent of analysis undertaken by the board, and the way this was reported through the governance framework to aid understanding and challenge on the financial dimensions of dealing with the pandemic.

Total Covid Costs	£m
Medical & Dental	£13.71
Nursing	£40.34
Support Services	£7.31
Administration Services	£10.15
Other Pay	£8.95
<b>Total Pay Costs</b>	<b>£80.45</b>
Payment to GPs	£3.36
Prescribing	£6.14
Equipment	£6.32
Medical Supplies	£1.53
IT Kit & Equipment	£2.57
RHSC Lost Receipt	£9.00
Annual Leave Adjustment	£4.50
Other Non-pay	£16.50
<b>Total Non-Pay</b>	<b>£49.93</b>
<b>Lost Income</b>	<b>£13.01</b>
<b>Lost Efficiencies</b>	<b>£2.97</b>
<b>Total Covid Costs</b>	<b>£146.35</b>



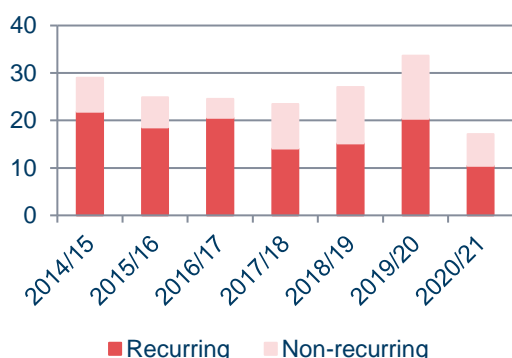
## Efficiency savings

### NHS Lothian is showing signs of improvement in delivering savings on a recurring basis

83. The June 2021 Finance & Resources Committee report set out £17.13million of savings delivered in 2020/21. This was 85% of the £20.1million planned (revised up from £18.55m in the initial overall financial plan for 2020/21).
84. The level of overall savings achieved is notably lower than the levels in previous years. It is just over half of the 2019/20 equivalent. It reflects the extent of savings required to break even, alongside the net effect of COVID-19 funding and activity in 2020/21. COVID-19 has impacted in terms of savings opportunities and resources available to pursue and optimise them.

85. The proportion of savings achieved on a recurring basis is the same as in 2019/20, which itself tackled an increasing proportional reliance on non-recurring savings (from 2017/18). The chart below outlines the historical position.

### Historic analysis of savings achieved (£m)



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

86. Reliance on non-recurring savings places additional pressures on the future financial position of the board and therefore requires careful management. NHS Lothian's efforts to reduce reliance on non-recurring savings is positive and we will monitor this situation going forward, to assess future recurring/non-recurring split and how this sits within wider, ongoing trends.
87. All but one category of savings fell short against planned levels. Facilities and Consort was over £1million short (achieving just 58% of target and most of this on a non-recurring basis), and Royal Edinburgh Hospital and Associated Services (REAS) was £0.478million below target (34%), with all delivered savings being non-recurring.

## Budget monitoring and control

88. As part of our audit, we considered NHS Lothian's system of budgetary control and financial management and did not identify any significant deficiencies, whilst acknowledging the challenging financial situation and the need for the board to be flexible in how it ultimately delivers financial balance. Comprehensive financial regulations and policies remain in place which are subject to regular review and are available on the board's Finance Online intranet site.
89. During 2020/21 there was a strong emphasis on monitoring the financial impact of COVID-19. Reports were submitted to meetings of the Board, the Finance and Resources Committee, and Corporate Management Team. The reports included forecasts to the year end and explanations of key movements in the year. COVID-19 financial reporting has been regularly reviewed and updated, to help the various stakeholders understand, analyse and manage the implications on finances of the pandemic.

## Prevention and detection of fraud and irregularity

90. Our audit was planned to provide a reasonable expectation of detecting material misstatement 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 and appropriate.
91. 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 receives updates on current counter fraud activity from the Fraud Liaison Officer at each meeting.

92. During 2020/21, the Board reported five personal data related incidents to the Information Commissioner's Office (ICO) for review. In addition, the Board experienced a significant data breach in relation to the access of certain patient data. We are satisfied that the Board took appropriate actions, including timely notification to the ICO and the police.
93. The ICO concluded that no further ICO involvement was necessary in their report on the matter (June 2021). However, they recommended that the board investigates the cause of the incident to understand how it occurred and ensure steps are taken to prevent it from happening again.

### National Fraud Initiative

94. 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.
95. The exercise produces data matches by comparing a range of information held on various public sector bodies' systems to identify potential fraud and error. Bodies are required to investigate these matches and record appropriate outcomes based on their investigations.
96. The most recent exercise commenced in January 2021 with matches to be investigated by 30 September 2021. With investigation ongoing, we will continue to monitor NHS Lothian's participation in the NFI scheme and

provide an update in our Annual Report on the Audit. We have no issues or concerns at this stage.

### Standards of conduct

97. In our opinion, NHS Lothian'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 scheme of delegation and for complying with national and local codes of conduct. We have also considered compliance with the regulatory guidance produced by the SGHSCD throughout the year.



## Accounting systems and internal control

98. During our audit of the financial statements we examined the principal internal controls that enable the organisation to ensure, as far as possible, the accuracy and reliability of accounting records and to safeguard assets.
99. It should be noted that our audit was planned to allow us to provide an opinion on the financial statements and it should not be relied upon to reveal all errors and weaknesses that may exist.
100. We are pleased to report we have not identified any significant system weaknesses.

### Asset verification

101. NHS Lothian has a large asset base (net book value of £1,078 million as at 31 March 2021) that is varied in both nature and location.
102. A complete asset verification exercise was finalised in 2018/19, confirming the existence of 100% of assets held by the Board. Thereafter, an annual plan of asset verification was established, implementing a risk assessed sample approach.
103. However, due to resource pressures and the impact of the COVID-19 pandemic, this plan has not been implemented and NHS Lothian has not undertaken any asset verification checks in 2019/20 or 2020/21 (other than for assets provided as part of the COVID response, which amounts to 1% of plant and machinery held at the year end).
104. We appreciate the risk and impact of this will vary depending on the nature

and class of the asset (eg recognising the role and context of land & buildings and related valuations). However, regular asset verification is vital to ensure asset registers remain accurate, up to date and reliable. Due to alternative audit testing completed and evidence obtained, we do not deem the lack of asset verification to have a material impact on the financial statements. However, this poses a risk to asset control and the accuracy of the financial statements. NHS Lothian intends to undertake a verification exercise in 2021/22.

### Action Plan Point 3

## Internal audit

105. An effective internal audit service is an important element of NHS Lothian's governance arrangements and supports the system of internal control. The NHS Lothian internal audit service is provided through a co-sourced arrangement with Grant Thornton. The service operates in line with Public Sector Internal Audit Standards. During our audit we considered the work of internal audit wherever possible to avoid duplication of effort and make the most efficient use of NHS Lothian's audit resource.

# 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.



## Auditor judgement



The NHS Lothian Board made minimal changes to its governance arrangements as a result of COVID-19, seeking to maintain efficient and effective governance during the pandemic.

The Board and its key committees met frequently during 2020/21 to provide effective scrutiny, challenge and oversight and receive assurance on the management of risk.

## Audit risks

106. Our audit plan identified no significant risks in relation to governance and transparency under our wider scope responsibilities. However, we paid particular attention in the current year to COVID-19 governance arrangements and remobilisation planning.

## COVID-19 governance

107. The Scottish Government wrote to all health boards in March 2020 providing guidance on COVID-19 governance arrangements. The guidance emphasised the primary concern of ensuring a focus on responding to the pandemic, and supporting the chief executive and the executive team in this regard, while maintaining effective governance.

108. The Scottish Government guidance recognised that no single approach would fit all boards but each board should ensure the model they adopt “enables agile and effective decision making, places staff and their resilience at the centre and builds important links with the public and the community at this time. Boards should also continue to operate in an open and transparent manner”.

109. The Board made minimal changes to its governance arrangements as a result of COVID-19, seeking to maintain efficient and effective governance during the pandemic.

110. The most significant changes were more regular board and committee meetings, reflecting the increased risk environment, and a temporary cessation of public board meetings between April and December 2020.

From December 2020 onwards, the board put in place a facility to allow the public to observe board meetings online.

111. At its meeting on 8 April 2020 to approve the revised arrangements, the board raised the importance of staff governance and agreed that the Staff Governance Committee would need to meet to focus on COVID issues such as the workload of clinical staff, any whistleblowing issues and to ensure oversight of health and safety.

112. The Staff Governance Committee met regularly during the year and covered all of the above issues. Key areas considered by the committee included staff health and safety issues such as personal protective equipment (PPE) and virus testing, partnership working with care homes, staff resourcing levels and recruitment initiatives, staff well-being services and tools, staff absence, whistleblowing monitoring and overseeing the establishment of four staff networks representing Black and Minority Ethnic, LGBT+, Disability and Youth groups, each of which worked to develop their own Equality Action Plan. The committee agreed to accept a significant level of assurance that NHS Lothian had put staff wellbeing at the forefront of activity and had robust plans in place.

113. Likewise, the Finance and Resources Committee, Healthcare Governance Committee, Audit and Risk Committee and the Board itself met frequently during 2020/21 to provide scrutiny and oversight and receive assurance on the management of risk, including progress on the vaccination programme.

114. The internal auditors carried out a review of governance arrangements

and related response to COVID-19 and provided positive assurance to the Audit & Risk Committee in this regard.

## Remobilisation planning

115. During 2020/21, the board revised its governance structure by creating a Planning, Performance and Development Committee to replace the Strategic Planning Committee and informal board development sessions. Membership of this committee includes all non-executive board members.
116. One of the first activities of the new committee was to review the approach for developing a new NHS Lothian Strategic Development Framework. Work on this framework will be progressed during 2021/22 in collaboration with all partners, in particular the four Integration Joint Boards, and overseen by the Planning, Performance and Development Committee.
117. The Planning, Performance and Development Committee also considered the draft Remobilisation Plan 3 (“RMP3” – the third iteration of remobilisation planning) in May 2021, which was then noted and approved by the Board in late June 2021. This sets out the latest developments and forward plans as NHS Lothian remobilises services.
118. The Board’s three overarching remobilisation objectives are:
  - Managing the pandemic;
  - Delivering essential services;
  - Supporting the workforce.
119. There is clear acknowledgement of the direct interplay between these areas, along with more detailed assertion of

what these mean in strategic and operational terms. The plan covers a wide range of areas, right across NHS Lothian’s acute, primary care and other lines of service and with overt cognisance taken of the important role of partners and stakeholders in achievement of outcomes. Many of the risks, challenges and issues referred to earlier in this report are also recorded in RMP3, setting context and helping to inform the reader and direct scrutiny of the plan and the related options/actions.

120. RMP3 reinforces extant NHS Lothian strategic plans and strategies, noting that, against a background of rising quality aspiration, major demographic challenges and resource constraints, delivery will not be achieved without radical change, accelerating innovation and changing mindsets. As COVID-19 has progressed and the impact, duration and outlook has become more visible since our last annual audit report (even if the specifics and outcomes are still not certain), this has further accelerated the opportunity for, drive towards, and need to achieve such change.
121. RMP4 is expected to cover the second half of 2021/22, including the latest developments in relation to winter planning. RMP3 cites the crucial nature of the vaccination programme roll out and latest virus response/suppression measures as being key to the nature, focus and impact of this pending plan. We will continue to review developments in this area as part of our audit work in 2021/22.

## Overall conclusion

122. Through our review of board and committee papers, governance statement disclosures and other evidence gathered during our audit,

we are satisfied that there has been effective scrutiny, challenge and informed decision making throughout 2020/21.

# 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 reporting of its performance.



## Auditor judgement



An established and appropriate performance management framework is in place at NHS Lothian. COVID-19 has caused substantial disruption in wider service delivery and the challenge facing NHS Lothian as it looks to continuously improve against the wide range of performance metrics in the medium term has never been greater.

The Royal Hospital for Children and Young People, Department of Clinical Neurosciences and Child and Adolescent Mental Health Services hospital fully opened to service users on 23 March 2021. This followed completion of service migration plans, satisfactory progress against project management milestones/actions, appropriate resolution of outstanding rectification works and further testing and inspection of the facility. This came after various internal and external reviews and scrutiny into the significant delays in opening the new facility. Lord Brodie is Chairing the ongoing Public Inquiry into a range of matters in relation to this project.

## Significant audit risks

123. Our audit plan identified significant risks to value for money under our wider scope responsibilities. These related to (i) Royal Hospital for Children and Young People project, and (ii) general performance issues.

### **Value for Money: Developments in relation to Royal Hospital for Children and Young People, Department of Clinical Neurosciences and Child and Adolescent Mental Health Services**

We previously carried out a high-level review of value for money and governance aspects of the settlement agreement made for the development of the new hospital. There have been subsequent reviews by a range of scrutiny bodies and functions into aspects of the new hospital, including (i) KPMG report (to establish what decisions were made in relation to the air ventilation issues and any other material issues that led to project delays), (ii) NHS National Services Scotland (a two phased review, checking that relevant technical specifications and guidance applicable to the new hospital were being implemented), and (iii) by Internal Audit (to review project governance and controls, to better understand the root causes of the ventilation issues). We summarised the key findings and conclusions from these reviews in our 2019/20 annual report.

The Cabinet Secretary commissioned a public inquiry (“Scottish Hospitals Inquiry”) into the issues experienced at the new Royal Hospital for Children and Young People in Edinburgh and the Queen Elizabeth University Hospital in Glasgow. This inquiry, which is being led by the Right Honourable Lord Brodie, commenced in August 2020.

All remaining remedial and enhancement works, including changes to the ventilation system, were expected to be completed by the end of January 2021, with the migration of the remaining children's services being taken forward thereafter.

*Noted in the 2020/21 External Audit Plan*

124. The hospital fully opened to service users on 23 March 2021. This followed completion of service migration plans, satisfactory progress against project management milestones/actions, appropriate resolution of outstanding rectification works, and further testing and inspection of the facility. Reporting through the management and oversight structure in March 2021 confirmed completion of the major works, “snagging” and final commissioning works progressing, and related update on costings. Further update was then provided to the Board as part of the established governance cycle and ongoing reporting. June 2021 reporting to the Board highlighted the “incredibly positive” initial feedback from patients, families, carers and staff on the facility, along with update on advanced plans for disposal of the old Sick Children’s site. The deal for this disposal was subsequently signed off at the end of June 2021.

- 
125. The Board, its Committees and the Executive Team have all been involved in regular reporting and scrutiny of developments over the year. A post-occupancy review remains outstanding, and the public inquiry is in progress. Oversight and executive scrutiny groups have focussed efforts – in a difficult wider operating environment given COVID-19 pressures – to bring the project to this stage. On 8 April 2021, the Oversight Board met and agreed to step down given successful completion and opening of the hospital. The previous day, the Board agreed to remove the specific hospital risk from the Corporate Risk Register.
126. The public inquiry led by Lord Brodie is well underway, and in late June 2021 it held a Procedural Hearing. This was streamed via social media platforms and is still available for viewing at time of writing along with previous broadcasts. This reflected work to date, the planned way forward, and set out the hearings to take place from September 2021 onwards (primarily focussing on the Queen Elizabeth University Hospital in Glasgow) and in May 2022 (expected to have a more specific focus on the Royal Hospital for Children and Young People project). The Inquiry website and related public-facing media for the Inquiry has been providing regular news and updates, along with a range of contextual and background documentation. This includes reports on Lord Brodie visiting the site of the new hospitals, practical arrangements for witness hearings and related protocols (with emphasis on access and inclusivity), and technical directions as to conduct of hearings and evidence. We note the positive progress made to date, and will continue to monitor developments into our 2021/22 audit.




## Performance

In our 2019/20 audit we noted that NHS Lothian met just 20% of performance indicators, a deterioration from the 50% reported in 2018/19. There had been an initial, substantial adverse impact due to COVID-19 in 2019/20 and it is expected that this will continue to impact 2020/21 metrics across a range of areas.

Performance against targets has been an area of challenge for the Board, particularly due to the ongoing financial and operational pressures. During 2019/20, the Scottish Government placed NHS Lothian on Level 3 of its Performance Escalation Framework for general performance issues. The Board put a formal recovery plan in place, increased the frequency of its meetings and retained direct oversight of the recovery plan. Whilst the Board did take clear and proactive steps in 2019/20 to progress with the recovery plan, this has been effectively set aside in the run up to and during the ongoing pandemic response.

*Noted in the 2020/21 External Audit Plan*

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127. Performance metrics (where available and comparable) show a range of areas of deterioration in performance standards compared to prior year, primarily due to COVID-19. The pandemic will continue to impact metrics across a range of areas.
  128. We have seen evidence of senior commitment to making progress in performance, whilst it is widely acknowledged that both focus and resources has been reprioritised to the COVID-19 pandemic response. The “waves” of pressure and activity related to COVID-19 have also impacted (and often impaired) the ability to take wider system actions with confidence and in a way that any such actions could embed and deliver as effectively as possible.
  129. The unique circumstances arising from COVID-19 make it difficult to make comparisons across years, and we acknowledge that the NHS Lothian remobilisation plan has been an area of focus and organisational effort, balancing COVID-19 and wider system pressures. We will look into the further impact and progress made by NHS Lothian in this area in our 2021/22 audit.

## Performance summary

130. The key areas of focus for NHS Lothian during 2020/21 have been adapting to COVID-19 related pressures, remobilisation and recovery and supporting Scottish Government

priorities in relation to mental health and waiting times.

131. In our work in this section, performance for 2020/21 has been compared to the prior two years to confirm the reported movements. Changes to the performance

management and reporting landscape due to COVID-19 and remobilisation mean that it has not been possible to conduct a comparative analysis of the full range of delivery targets which were initially set out in the NHS Lothian Annual Operational Plan. Our analysis has therefore focused on the key metrics relating to waiting time standards and remobilisation and recovery. It has not been possible to conduct a comparative analysis for all of these measures against previous years, as in 2020/21 NHS Lothian moved away from reporting against focused targets to tracking activity levels for recovery and remobilisation.

132. Following the initial adverse impact of COVID-19 at the end of 2019/20, COVID pressures continued to impact upon performance in NHS Lothian throughout 2020/21. Performance declined with a deterioration in standards relating to access performance and scheduled and unscheduled care. Mental health waiting times standards were not met, however performance improved compared with the prior year. Although the majority of waiting time targets were not achieved, improvements on the prior year were seen in the 31 day cancer treatment standard, mental health waiting times and the 18 week referral to treatment standard. Action to improve performance against the national waiting times standards continues as part of the Remobilisation, Recovery and Renew Programme.

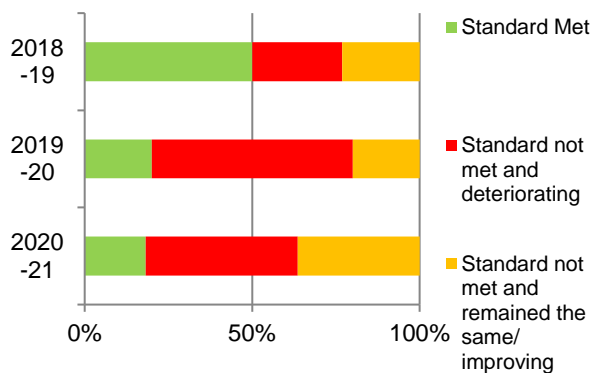
## Performance framework

133. The Board monitors its performance against a range of high level key performance metrics which are set out in the NHS Lothian recovery and

remobilisation plans. A range of quality and safety metrics are also considered by the Healthcare Governance Committee.

134. In 2019/20 we confirmed that there was an established and appropriate performance management framework in place to monitor progress against the Annual Operational Plan. In response to COVID-19 and recovery and remobilisation plans, NHS Lothian has made changes to the performance governance, reporting and monitoring arrangements. An Executive-led Performance Oversight Group has been formed which includes an escalation process to address emerging performance issues relating to key services. The Performance Oversight Group ensures there is regular performance monitoring and that a rapid response is taken to address areas of deteriorating performance. The Planning, Performance and Development Committee will manage the wider performance metrics and report progress to the Board. The metrics managed by the Planning Performance and Development Committee are to be aligned with the NHS Lothian board priorities. The 2020/21 framework amendments and resultant arrangements appear to provide a robust basis on which to report and monitor performance, taking cognisance of the COVID-19 operating environment.

**Relative performance declined slightly during 2020-21, but with fewer “reds”**



Source: NHS Lothian Performance Reports & ISD

135. 2018-19 was NHS Lothian's first Annual Operational Plan in which there were 16 delivery standards in total. For 2020/21 the number of key metrics is fewer with 11 areas of performance included in our analysis as opposed to the full suite of delivery standards. Performance data relating to safety & quality improvement for 2020/21 is not included in our analysis as the annual data was not published at the time of this report.

136. In 2020/21, performance in relation to national standards declined slightly compared with the prior year. Standards were not met and deteriorated in the following areas:

- 95% of cancer patients referred with suspicion of cancer within 62 days
- 95% of outpatients waiting no more than 12 weeks
- 100% inpatient and day case treatment time guarantee patients to be seen within 12 weeks
- 6 weeks following referral for key diagnostic tests
- 95% 4 hours emergency access standard

137. Standards were not met but with improvement compared to the prior year in the following areas:

- 18 weeks referral to treatment
- Waiting times in relation to psychological therapies and CAMHS
- Escherichia Coli Bacteraemia (ECB) healthcare associated infection cases.

138. Standards were met in the following areas:

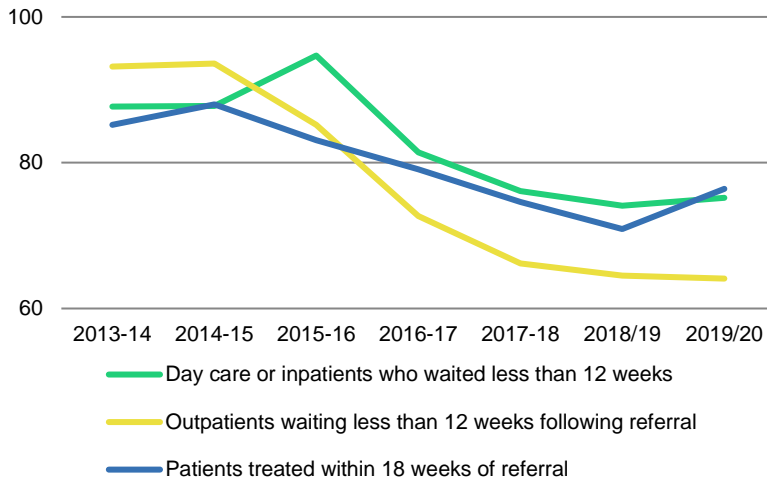
- 95% of cancer patients being treated within 31 days
- Staphylococcus Aureus Bacteraemia (including MRSA) healthcare associated infection cases.

139. For the 31 day cancer standard, NHS Lothian's performance as at March 2021 was 97.9%. This is in the context of 151 (13.4%) fewer patients being treated in the first three quarters of 2020/21 than the same period in 2019/20.

## Performance Against Key Waiting Time Standards

Target/standard	Performance at March 2021		Mar-20	Mar-19
At least 95% of patients referred with suspicion with cancer to be treated with 62 days	82.8%	Standard not met and deteriorating performance	83.5%	94.9%
At least 95% of patients diagnosed with cancer to be treated with 31 days	97.9%	Standard met and improving performance	95.2%	79.4%
At least 90% of patients to be treated within 18 weeks of Referral	77.3%	Standard not met and improving performance	76.4%	70.9%
100% of Inpatient and Day cases covered under the Treatment Time Guarantee to be seen in 12 weeks	67.3%	Standard not met and deteriorating performance	75.2%	73.6%
Outpatients waiting less than 12 weeks	% data not available for comparison. In March 2021 the monthly average for end of month breaches (outpatients waiting >12 weeks) was 37,123 compared with a monthly average of 22,414 in March 2020 and 20,777 in 2018-19.	Standard not met and deteriorating performance	64.1%	64.5%
At least 95%, with an ambition of 98%, of unscheduled care patients to be admitted, treated or discharged within 4 hours	84.8%	Standard not met and deteriorating performance	86.3%	87.7%
At least 90% of Psychological Therapy patients to be treated within 18 Weeks	79.2%	Standard not met and improving performance	78.0%	77.2%
At least 90% of Child and Adolescent Mental Health Patients to be treated within 18 weeks of referral	57.1%	Standard not met and improving performance	53.9%	58.6%

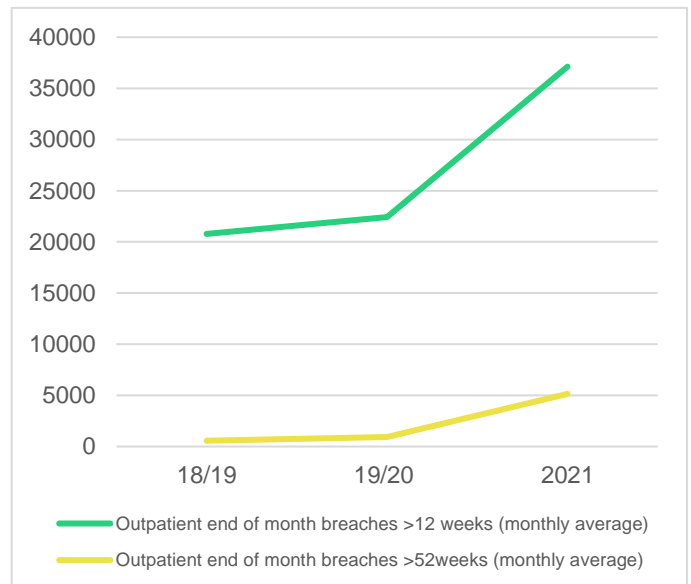
### Longer term waiting time performance



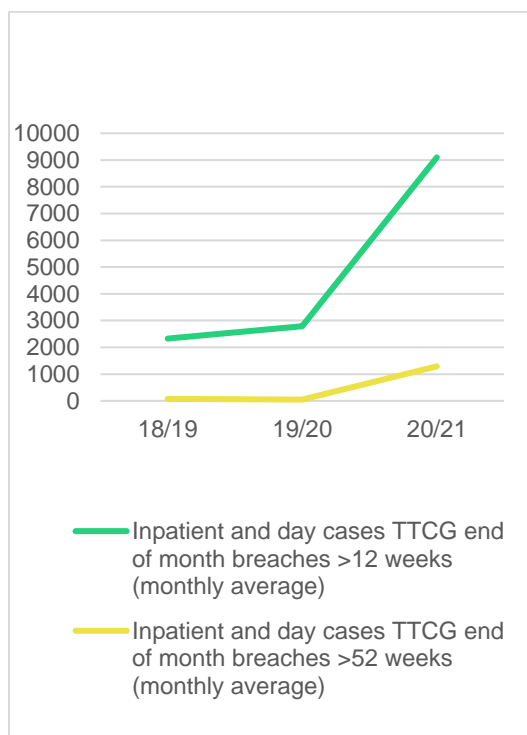
Source: NHS Lothian Performance Reports & ISD

140. There has been a long term deterioration in waiting time performance - impacted by interlinked factors such as finances, resourcing and capacity - with performance deteriorating substantially over the last 5 years. The COVID-19 pandemic has further exacerbated these pre-existing performance issues.
141. In 2020-21 activity levels on the number of breaches were reported in NHS Lothian performance data. The following graph depicts the figures for average monthly breaches for outpatients in 2021/22 compared with the average monthly breaches in 2019/20 and 2018/19. The subsequent graph depicts the average monthly breaches for inpatient and day case TTG breaches.

### Outpatient breaches 2018-19 to 2020-21



### Inpatient and day case TTG breaches 2018-19 to 2020-21



142. As can be seen, the number of inpatient, outpatient and day case breaches in NHS Lothian increased sharply in 2020/21. Issues related to the pandemic such as staff self-isolation, social distancing, enhanced infection control measures alongside a growing demand for secondary care caused staff capacity and service delivery challenges. This included periods of service cancellations.
143. In addition to the key waiting times targets that were not met, the ESB standard was also not met: ECB - Escherichia Coli 32.5 or below (fewer than 330 episodes). The rate of ECB as at March 2021 was reported as 33.7.

### Unscheduled Care

144. There were 73,579 (25.9%) fewer attendances at NHS Lothian emergency departments in 2020/21 compared to 2019/20. In March 2020,

the COVID-19 pandemic led to a significant decline in unscheduled care attendances, and the emergency access standard performance improved significantly in subsequent weeks with the target being achieved at the start of 2020-21. However, following the summer of 2020, performance declined month on month until February 2021. This was followed by an increase in performance in March 2021, however performance was still sitting below target at 84.9%. NHS Lothian's Annual Report for 2020-21 states that this was due to a reduction in the number of people self-presenting at emergency departments and those who did attend having higher severity of illness. This resulted in longer treatment times and is not an indicator of decline in the quality of care.

145. The Royal Hospital for Children and Young People performed relatively well against this standard, however performance is less positive at Western General Hospital (WGH) and the Royal Infirmary of Edinburgh (RIE). The RIE has been escalated to the weekly Executive-led Performance Oversight Group for detailed review and performance support.

### Delayed Discharges

146. In 2020/21 the number of delayed discharges in NHS Lothian were at an all-time low. Delayed discharges have continued to decrease during 2020/21 due to measures put in place to manage COVID-19 pressures, including an increase in the number of community beds and a focus on Home First. In 2020/21 there were 132 delays (across all censuses) compared with 249 and 331 in 2019/20 and 2018/9 respectively. The key reasons for delays include patient

delays related to care required to live in their own home or nursing/residential home and community workforce capacity issues.

## COVID-19, wider performance context, and future outlook

147. The board has acknowledged the dramatic impact that the COVID-19 pandemic has had on the performance of the organisation, including the outturn position at year end. As at 30 March 2020 there had been 208 confirmed COVID-19 cases in Lothian; by 27 April 2021 there had been 31,342 confirmed cases.
148. NHS Lothian's annual report notes that before the pandemic it was on Level 3 of the Scottish Government's Performance Escalation Framework and, with Scottish Government support, had developed a recovery plan to improve various aspects of its performance. Scottish Government then stated that NHS Lothian would remain on Level 3 whilst acknowledging that priorities would change considering the severe impact of COVID-19.
149. With routine inpatient, day case treatment and face-to-face outpatient appointments from 16 March 2020 cancelled, the repercussions have been felt across 2020/21 and will continue for some time. The NHS Lothian performance recovery plan was put on hold and has been significantly impacted given focus on remobilisation plans.
150. NHS Lothian has highlighted the following priority areas in its Remobilisation Plan:
- Diagnostics and treatment for cancer
  - Urgent treatment for cardiac disease, transplants, renal failure.
  - Support and treatment for mental health difficulties.
  - Routine treatments where additional delays caused by the pandemic may have made the clinical picture an urgent one.
  - Services for children, where the impact on a child's development could be disproportionate.
  - Dental and ophthalmic services where significant underlying disease may have built up.
  - General Medical Practice capacity to see patients with non-urgent but significant health problems that will worsen over time.
151. Transformational service redesign and the effective use of resources will be essential, but the operational and financial context of the board exacerbates the difficulty in achieving this.
152. April 2021 brought confirmation from Scottish Government of lowering NHS Lothian's level on the Performance Escalation Framework for scheduled and unscheduled care. The impact of COVID-19, the legacy of shortfall in NRAC funding share, and the reduction in the level of funding due to the revised performance framework level are combining such that the challenge facing NHS Lothian as it looks to continuously improve performance metrics in the medium term has never been greater.

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## Appendix 1: Respective responsibilities of the Board and the Auditor

The Audit Scotland Code of Audit Practice (2016) sets out the responsibilities of both the Board and the auditor and these are detailed below.

### Board responsibilities

The Board has primary responsibility for ensuring the proper financial stewardship of public funds, complying with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

Area	Board responsibilities
<b>Corporate governance</b>	<p>The Board, through its chief executive (as accountable officer) is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Those charged with governance should be involved in monitoring these arrangements.</p>
<b>Financial statements.</b>	<p>The Board has responsibility for:</p> <ul style="list-style-type: none"> <li>• preparing financial statements which give a true and fair view of its financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation;</li> <li>• maintaining accounting records and working papers that have been prepared to an acceptable professional standard and that support its financial statements and related reports disclosures;</li> <li>• ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority;</li> <li>• maintaining proper accounting records; and</li> <li>• preparing and publishing, along with the financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that is consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also address the longer term financial sustainability of the Board.</li> </ul> <p>Management is responsible, with the oversight of those charged with governance, for communicating relevant information to users about the</p>

Area	Board responsibilities
	<p>entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework. The relevant information should be communicated clearly and concisely.</p> <p>The Board is responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of its objectives and safeguard and secure value for money from the public funds at its disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.</p>
<p><b>Standards of conduct for prevention and detection of fraud and error</b></p>	<p>The Board is responsible for establishing arrangements to prevent and detect fraud, error and irregularities, bribery and corruption and also to ensure that its affairs are managed in accordance with proper standards of conduct.</p>
<p><b>Financial position</b></p>	<p>The Board is responsible for putting in place proper arrangements to ensure the financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> <li>• Such financial monitoring and reporting arrangements as may be specified;</li> <li>• Compliance with statutory financial requirements and achievement of financial targets;</li> <li>• Balances and reserves, including strategies about levels and their future use;</li> <li>• Plans to deal with uncertainty in the medium and long term; and</li> <li>• The impact of planned future policies and foreseeable developments on the financial position.</li> </ul>
<p><b>Best value</b></p>	<p>Accountable officers have a specific responsibility to ensure that arrangements have been made to secure best value.</p>

## Auditor responsibilities

Auditor responsibilities are derived from statute, the Code of Audit Practice, International Standards on Auditing (UK), professional requirements and best practice. These are to:

- undertake statutory duties, and comply with professional engagement and ethical standards;
- provide an opinion on the financial statements and the regularity of transactions;
- review and report on, as appropriate, other information such as annual governance statements, management commentaries and remuneration reports;
- notify the Auditor General when circumstances indicate that a statutory report may be required; and
- demonstrate compliance with the wider scope of public audit.

### 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 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.

## Independence

In accordance with our profession's ethical guidance and further to our External Audit Annual Plan confirming audit arrangements, there are no matters to bring to your attention in relation to our integrity, objectivity and independence.

We confirm that Azets Audit Services and the engagement team complied with the FRC's Ethical Standard. We confirm that all threats to our independence have been properly addressed through appropriate safeguards and that we are independent and able to express an objective opinion on the financial statements.

### Audit and non-audit services

In addition to our work on the board we are also responsible for the review of the abstract of receipts and payments of patients' private funds. The non-audit fee for this work in 2020/21 is expected to be around £7,200. This work is undertaken as approved by the firm's ethics partner and Audit Scotland.

## Audit quality

The Auditor General and the Accounts Commission require assurance on the quality of public audit in Scotland through comprehensive audit quality arrangements that apply to all audit work and providers. The audit quality arrangements recognise the importance of audit quality to the Auditor General and the Accounts Commission and provide regular reporting on audit quality and performance.

Audit Scotland maintains and delivers an [Audit Quality Framework](#).

The most recent audit quality report which covers our work at the Board since appointment can be found at <https://www.audit-scotland.gov.uk/report/quality-of-public-audit-in-scotland-annual-report-202021>

## Appendix 2: Unadjusted differences identified during the audit

### Uncorrected misstatements

Our summary of unadjusted audit differences is presented below. We have discussed these with management and confirmed that all unadjusted differences are collectively and individually immaterial.

No	Detail	Assets	Liabilities	Reserves	SoCNE
Details of unadjusted audit differences		Dr / (Cr)	Dr / (Cr)	Dr / (Cr)	Dr / (Cr)
		£m	£m	£m	£m
1.	Transfer of completed assets out of assets under construction and into use	2.7 (2.7)			
2.	Release of R&D income to the SOCNE in line with IFRS 15		1.7		(1.7)
Total					(1.7)

## Appendix 3: Action plan

Our action plan details the weaknesses and opportunities for improvement identified during our audit.

The recommendations are categorised into three risk ratings:

**Key:**

**Significant deficiency**

**Other deficiency**

**Other observation**

### Action Plan

#### 1. Research and development (R&D) income

**Other deficiency**

<b>Observation</b>	The Board is not recognising R&D income from commercial contracts in line with IFRS 15 Revenue from Contracts with Customers, but is instead recognising income in relation to expenditure incurred.
<b>Implication</b>	Non-compliance with accounting standards.
<b>Recommendation</b>	Management should revise the current approach to recognising R&D income in line with IFRS 15.
<b>Management response</b>	<p>Management accepts this recommendation, although we would note that the full technical application of IFRS15 in this context may have implications for the broader support for commercial research in the future. The Board will work with the Technical Accounting Group (TAG) to establish a sustainable way forward, which also will ensure compliance with IFRS 15.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Implementation Date:</b> March 2022</p>

## 2. Disputed capital accrual

Other deficiency

<b>Observation</b>	We identified a capital accrual for £508k that relates to a disputed transaction with a public sector partner that occurred in 2014. No recent action has been taken to resolve this dispute.
<b>Implication</b>	Failure to resolve the dispute may lead to the board being subject to legal action or late payment fees. Additionally, accruals may be overstated if the board continues to recognise a liability when it is inappropriate to do so.
<b>Recommendation</b>	Management should ensure appropriate action is taken to resolve the disputed transaction and ensure it is appropriately accounted for.
<b>Management response</b>	<p>Management accepts this recommendation and will work with the public sector partner to conclude on the outstanding issue and realise any payments required.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Implementation Date:</b> March 2022</p>

## 3. Asset verification

Other deficiency

<b>Observation</b>	Minimal asset verification has been undertaken by management since 2018/19. A plan had been established to undertake the exercise annually on a risk assessed sample basis; however, due to COVID - 19 restricting access and resourcing constraints, this has not been followed in 2019/20 or 2020/21.
<b>Implication</b>	Asset registers may not accurately reflect the quantity or condition of assets held by the Board without regular asset verification.
<b>Recommendation</b>	Management should ensure appropriate and sufficient asset verification is undertaken on an annual basis.
<b>Management response</b>	<p>Management accepts this recommendation and will focus on verification of assets in 21/22. Management will utilise additional verification resources such as the Medusa medical equipment database to minimise the requirement for physical verification in light of the risks presented by the ongoing COVID-19 pandemic.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Implementation Date:</b> March 2022</p>

## Appendix 4: Follow up of prior year recommendations

We have followed up on progress in implementing the outstanding actions raised in prior periods.

### Journal testing

**Recommendation** Management should ensure appropriate controls are in place to prevent or detect where a journal has been posted and authorised by the same individual, and reinforce NHS Lothian procedures to all relevant staff.

Rating	Other deficiency	Implementation date	Immediate
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<b>Closed</b>	We have confirmed that journal authorisation functions have been updated. Our journal testing confirmed that journals were appropriately authorised and appropriate segregation of duties was in place.		
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### Year-end asset procedures

**Recommendation** We encourage NHS Lothian to complete a review of assets under construction and the useful life of revalued assets to ensure appropriate accounting treatment in 2020/21. Going forward, a review for completed assets should be undertaken as part of the accounts preparation process to ensure the correct treatment is applied.

Rating	Other deficiency	Implementation date	31 March 2021
--------	------------------	---------------------	---------------

<b>Ongoing</b>	NHS Lothian has undertaken a review of asset under construction balances as at year end. However, due to resourcing pressures, this exercise was not fully completed.  Revised date: March 2022		
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### Out of date policies

**Recommendation** NHS Lothian should ensure out of date polices are reviewed and updated in a timely manner.

**Rating** **Other deficiency** **Implementation date** 1 April 2021

**Closed** We have confirmed that the relevant policies (Employee Code of Conduct and Whistleblowing Policy) have been updated.

### Invoice management

**Recommendation** Invoices should be actioned and returned to Finance in a timely manner. Any non-compliance should be escalated appropriately.

**Rating** **Other deficiency** **Implementation date** 31 March 2021

**Closed** Our expenditure testing did not identify any reportable delays in passing invoices to Accounts Payable in 2020/21.

### Board meetings

**Recommendation** Given that Board meetings have been successfully held by videoconference, which poses no risk to public safety, NHS Lothian may wish to consider opening these up for public viewing so that board meetings can be held in public.

**Rating** **Other observation** **Implementation date** Dec 2020

**Closed** There is now a link on the NHS Lothian website to view meetings remotely.

RHCYP et al

**Recommendation** The Royal Hospital for Children and Young People post project evaluation should include an element specifically focused on the whole-project contracting, monitoring/timetabling and related “lessons-learned”. This should go beyond what may have otherwise been standard on more straightforward projects which have gone closer to plan. The key outcomes should be shared within NHS Lothian and with other NHS bodies in Scotland (as appropriate) to help with cumulative understanding of the issues arising, and to help with both preventative and reactive measures to mitigate the likelihood and impact in future projects.

Rating	Other observation	Implementation date	Now 31 March 2022
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<b>Not yet due</b>	The post project evaluation will be delayed until after the hospital has been fully occupied. The Board will build on a number of reviews that have already taken place to ensure lessons are learned and disseminated.		
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**Accounting | Tax | Audit | Advisory | Technology**

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