

NHS Health Scotland  
Annual Report to Members and the Auditor General for Scotland  
2009/10



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The principal objective of our audit procedures is to enable us to express our opinion, in line with the requirements of the Audit Scotland Code of Audit Practice, on the financial statements as a whole. Our audit opinion does not guarantee that the financial statements are free from misstatement. Our audit responsibilities, and their limitations are explained in our letter of appointment.

Any oral comments made in discussions with you relating to this report are not intended to have any greater significance than explanations of matters contained in the report. Any oral comments that we make do not constitute oral advice unless we confirm any such advice formally in writing.

The matters raised in this and other reports that will flow from the audit are only those which have come to our attention arising from or relevant to our audit that we believe need to be brought to your attention. They are not a comprehensive record of all the matters arising, and in particular we cannot be held responsible for reporting all risks at NHS Health Scotland or all internal control weaknesses. This report has been prepared solely for your use and should not be quoted in whole or in part without our prior written consent. No responsibility to any third party is accepted as the report has not been prepared for, and is not intended for, any other purpose.

# 1. Executive Commentary

## Introduction – Section 2

Our overall responsibility as external auditor of NHS Health Scotland (Health Scotland) is to undertake our audit in accordance with the principles contained in the Audit Scotland Code of Audit Practice (“the Code”), revised and published in March 2007. We have a dual reporting responsibility for the audit: to the Board Members of Health Scotland and to the Auditor General for Scotland.

## Financial Statements and Audit Opinion – Section 3

The financial statements of Health Scotland for the year ended 31 March 2010 have been prepared to comply with accounting requirements contained in the NHS Board Accounts Manual and supplementary guidance, as issued by the Scottish Government Health Directorates (SGHD) and approved by the Scottish Ministers. We are pleased to report that our **opinions** on the financial statements and regularity of income and expenditure for the year ended 31 March 2010 are **unqualified**.

In order to prepare financial statements which are International Financial Reporting Standards (IFRS) compliant, Health Scotland has been required to change the format of its financial statements and include a considerable number of additional disclosures. Significant work has been undertaken (in consultation with the PricewaterhouseCoopers’ technical support team) to achieve this objective. Over the last 18 months this has required a significant time commitment by the Director of Resource Management and the Finance Team and it is to their credit that this first full set of accounts under IFRS has been completed.

Following discussion with management, 4 adjustments remain unadjusted in the final accounts for 2009/10 due to their immaterial nature. Details have been provided in Section 3.

The Financial Statements at 31 March 2010 report a decrease in creditor payment days to 11 days, down from 35 days in 2008/09. Government guidance, issued in 2008/09 as a result of the economic downturn, states that good practice is for suppliers to be paid within 10 days. Health Scotland has made good progress in moving towards this target and is significantly ahead of other NHS bodies.

## 2009/10 Performance – Section 4

Health Scotland budgeted for a saving of £276,000 for the year to 31 March 2010. The final outturn was a surplus of £334,000

The Capital Resource Limit and Cash Requirement targets were achieved in the year. In addition efficiency savings in line with the 2% Scottish Government target were reported.

An additional target exists in relation to Knowledge and Skills Framework development reviews. NHS Boards have been set the target of at least 80 per cent of staff covered by Agenda for Change to have their annual Knowledge Skills Framework development reviews completed and recorded by e-KSF by March 2011. As of 31 March 2010, 93% of Health Scotland staff had a KSF outline, 48% of staff had a PDP, and 25% of staff had a review completed and recorded on e-KSF (with a further 30% in progress).

Health Scotland continues to out-perform the target of 4% in relation to sickness absence. The Board's 2009/10 sickness absence rate was 2.5%, a slight increase of 0.4% from the prior year but still well below the national target.

## **Governance and Control – Section 5**

We have reviewed Health Scotland's overall governance arrangements including a review of Board and key Committee structures and minutes, financial reporting to the Board, and risk management. Appropriate arrangements and reporting were noted. We have also considered key areas of risk to Health Scotland including partnership working; service sustainability; performance management; and people management, where clearly defined arrangements and reporting were noted.

In particular, Health Scotland devotes time and resources to achieve effective partnership working. As a special health board, Health Scotland has a close working relationship with all territorial Health Boards to ensure services are delivered effectively.

## **Managing in Uncertain Times – Section 6**

Despite entering the downturn from a relatively strong financial position, the NHS in Scotland currently faces a period of uncertainty. Impending tightening of public expenditure will impact the sector at a time when the cost base of many NHS bodies will rise.

While some NHS bodies will be more vulnerable than others, all NHS bodies, including Health Scotland, will be affected. Regardless of whether an NHS body is in a relatively stronger or weaker financial position, difficult decisions are going to have to be made. We recommend looking at six key areas which our experience in other sectors has shown may be relevant to addressing the challenges ahead:

- Honesty and awareness of the size of the challenge
- Strong leadership
- Need to engage with the whole organisation and external stakeholders
- Realistic and detailed plans to resolve the situation
- Rigorous implementation (programme management arrangements)
- Financial control and discipline

Health Scotland is already considering how best to respond to the existing drive for efficiencies by undertaking scenario modelling to assess the impact of budgets being frozen and a reduction in non core funding. Forecasts for the next four years should include "downside" scenarios and challenge from zero and priority based budgeting. Tough decisions on which spending plans take priority are likely to be faced by Health Scotland in the coming months and years.

## 2. Introduction

### **Purpose of this report**

The Annual Audit Report which follows is designed to set out the scope, nature and extent of our audit, and to summarise our opinion and conclusions on issues arising. Specifically this will direct your attention to matters of significance that have arisen out of the 2009/10 audit process and to confirm what action is planned by management to address the more significant matters identified for improvement.

### **Scope, nature and extent of our audit**

Our overall responsibility as external auditor of NHS Health Scotland (Health Scotland) is to undertake our audit in accordance with the principles contained in the Code of Audit Practice issued by Audit Scotland in March 2007. In this regard, the Code sets out the need for public sector audits to be planned and undertaken from a wider perspective than in the private sector involving not only assurance on the financial statements but also consideration of areas such as regularity, propriety, performance and the use of resources. It also sets out the need to recognise that the overall audit process is a co-ordinated approach involving the “appointed auditor”, the Auditor General for Scotland and other auditors such as Audit Scotland’s Health Performance and Public Reporting Group. Our audit has been planned and conducted to take account of these wider perspectives. Under the requirements of International Standard on Auditing (UK and Ireland) (‘ISA’) 260: “*Communication of audit matters to those charged with governance*”, we are required to communicate audit matters arising from the audit of financial statements to those charged with governance of an entity. This Annual Report to Members, together with previous reports to the Audit Committee throughout the year, discharges the requirements of ISA 260.

### **Acknowledgment**

We would like to formally extend our thanks to all Health Scotland managers and staff for the assistance they have given us during the audit process.

PricewaterhouseCoopers LLP  
Edinburgh

25 June 2010

## 3. Financial Statements and Audit Opinion

### Audit opinion

Our audit opinions concern the true and fair statement of Health Scotland's financial results for the year ended 31 March 2010 and the regularity of its income and expenditure for the year.

We are pleased to report that our opinions on the true and fair view on the financial statements and on the regularity of income and expenditure are **unqualified**.

We also provide a view as to whether those parts of the Remuneration Report subject to audit have been properly prepared. Our opinion on the Remuneration Report is **unqualified**. Our audit opinion does not extend to any other part of the Directors' Report.

### Audit Process

There were delays in the receipt of the financial statements and supporting schedules presented to us for audit and these were not delivered within the agreed timetable. However, once received, the quality of working papers provided by management was generally of a very high standard. Overall the achievement of an efficient audit process was hampered by the delays in receiving information and the number of revisions which were subsequently required to complete the information provided. An effective working relationship with your staff has enabled the audit to be completed on time. However, the process could be significantly improved.

Health Scotland completed the accounts preparation process several weeks later than many of the larger NHS Boards. The main reason for this was to allow amounts to be accrued manually after the system closed on 31 March each year. The volume of manual accruals required after the year end was significant. This was due to the high levels of spend and budget commitment in the last quarter of the year. Management had made some progress in increasing spending earlier in the financial year. However, more needs to be done in this area both from an ongoing operational perspective but also to ensure annual reporting timescales can continue to be met more readily.

#### **ACTION POINT 1**

The current accounts preparation process places a considerable burden on a small number of individuals within the finance team. In 2010 this has resulted in the accounts preparation and audit process being more time pressured than necessary. There are several recently recruited new staff members within the finance team which should alleviate delays in 2011. Management should reconsider the duties performed by each member of the finance team in the coming year in order to make the year end accounts process achievable in a shorter timeframe.

#### **ACTION POINT 2**

## **Basis of Preparation**

The financial statements were prepared in accordance with the accounting requirements contained in the NHS Board Accounts Manual for Directors' Report and Accounts of NHS Boards and for Scottish Financial Returns, and supplementary guidance, as issued by the Scottish Government Health Directorates (SGHD) and approved by the Scottish Ministers.

Government bodies, including NHS Boards, have been required to adopt International Financial Reporting Standards (IFRS) from 2009/10 onwards. This included a restatement of 2008/09 comparatives. The objective is to bring the public sector into line with the private sector, and to introduce greater comparability and consistency across public sector accounting.

In order to prepare financial statements which are IFRS compliant, Health Scotland has been required to change the format of its financial statements and include a considerable number of additional disclosures. Significant work has been undertaken (in consultation with the PricewaterhouseCoopers' technical support team) to achieve this objective.

Over the last 18 months this has required a significant time commitment by the Director of Resource Management and the Finance Team and it is to their credit that this first full set of accounts under IFRS has now been completed.

## **Approval**

The Financial Statements are to be submitted to the Health Scotland Audit Committee on the 25 June 2010 and are to be approved and adopted at the Board meeting on the same date.

## **Unadjusted misstatements**

Under ISA 260 - "Communication of audit matters to those charged with governance", we are required to report to you all unadjusted misstatements which we have identified during the course of our audit, other than those which we deem to be of a trivial nature.

As a result of our work, we proposed a number of minor audit adjustments, which following discussion with management have not been processed in the finalised version of the 2009/10 financial statements. We, therefore, have the following 2009/10 unadjusted misstatements to report:

Ref	Description	Operating Cost Statement		Balance Sheet	
		Dr	Cr	Dr	Cr
SUD 1	Being an adjustment to recognise a liability for the £14,000 of charitable donations held within Health Scotland's trust fund account, which will be spent in 2010/11.			Bank £14,000	Creditors £14,000
SUD 2	Being an adjustment to correct a sales invoice incorrectly posted as £7820 rather than £782, a difference of £7,038	Income £7,038			Debtors £7,038
SUD 3	Being an adjustment to correct the allocation of £15,970 of prepayments made in 2009/10 for 2010/11 as expenditure.		Expenditure £15,970	Prepayments £15,970	
SUD 4	Being an adjustment to correct the Cost of Capital figure, which was incorrectly calculated as £7,000. The actual Cost of Capital was calculated as £17,500, a difference of £10,500.	Expenditure £10,500			General Fund £10,500

The net effect on the Operating Cost Statement of SUDs 2 to 4 is an immaterial amount of £1,568. The impact of these adjustments on the balance sheet is wholly immaterial.

### Accounting Issues

A number of accounting issues were discussed with management during the audit. The most significant of these are set out below:

#### Balance Sheet Position

Health Scotland is currently disclosing net current liabilities of £902,000 on its balance sheet as at 31 March 2010 (2009: £569,000).

Under the current accounting arrangements as set out in the Financial Reporting Manual (FReM), Health Boards must show liabilities on the balance sheet without drawing down the equivalent cash to fund them. However, as the liabilities fall due, the cash will be requested from the SGHD to meet the payments.

We are satisfied that the accounts have been correctly prepared on a going concern basis.

#### Bank and Cash - Treatment of Endowment Fund

Health Scotland holds £14,000 of charitable donations and interest in a separate trust fund bank account. Following receipt of the initial donation a number of years ago, Health Scotland was instructed by the Scottish Government Health Department to keep the funds at 'arms length' and the trust fund account has not



been previously included within the Board's cash balance within the financial statements. Following discussion with management, it was noted that Health Scotland intends to utilise the funds in 2010/11 and a number of possible uses are being considered. A balance sheet adjustment was, therefore, proposed to recognise the £14,000 as cash held and an equal £14,000 liability for the payment of the funds in 2010/11. We consider this to be an immaterial balance sheet adjustment and, therefore, it has not been processed by management. It is included in the listing of unadjusted misstatements listed on page 6.

### ***Cost of Capital Calculation***

The Cost of Capital had been calculated incorrectly as £7,000. The true Cost of Capital was recalculated as £17,500, a difference of £10,500. An issue with the Cost of Capital calculation was also noted and adjusted for in the prior year. This, when taken collectively with the other expenditure adjustments, has an immaterial impact on the accounts and, therefore, has not been processed by management. It is included in the listing of unadjusted misstatements listed on page 6. The cost of capital calculation will not be required in future years.

### ***Recognition of Income/Expenditure***

Some immaterial errors were noted during income and expenditure testing. A sales invoice had been incorrectly keyed during posting, to overstate income by £7,038. It was also identified that two invoices which related to prepayments for 2010/11 had been incorrectly classified as expenditure in 2009/10. Expenditure in the year was, therefore, overstated by £15,970. This, when taken collectively with the other expenditure adjustments, has an immaterial impact on the accounts and, therefore, has not been processed by management. It is included in the listing of unadjusted misstatements listed on page 6.

### ***Creditors – Creditors Payment Days***

The Financial Statements at 31 March 2010 report a decrease in overall creditor payment days to 11 days, down from 35 days in 2008/09. Government guidance, issued in 2008/09 as a result of the economic downturn, stated that it is good practice for suppliers to be paid within 10 days. Health Scotland processes invoices and releases them for payment as soon as they are matched to purchase orders and goods received notes. Health Scotland has made good progress in moving towards this target and is significantly ahead of other NHS bodies, having resolved the initial problems experienced following the introduction of Cedar.

### ***IFRS – Breakdown of Revaluation Reserve***

Following our review of Health Scotland's 2008/09 IFRS shadow accounts, it was identified that Health Scotland does not have a breakdown of the Revaluation Reserve to individual asset level. A recommendation to complete this exercise was reported to the Audit Committee in November 2009. This was not required for our audit of the 2009/10 financial statements and had not been completed at the time of our visit. As the unresolved amount is not material to the financial statements, we have not insisted in any adjustment. However, management should aim to complete this exercise before the next interim audit visit.

## **ACTION POINT 3**

## 4. 2009/10 Performance

### Financial Results 2009/10

	£m	£m
Recurring income	24.423	
Recurring expenditure (before savings)	(24.361)	
Recurring savings	<u>0.230</u>	
<b>Underlying recurring surplus / (deficit)</b>		0.292
Non-recurring income	2.766	
Non-recurring expenditure (before savings)	(2.851)	
Non-recurring savings	<u>0.127</u>	
<b>Non-recurring surplus/(deficit)</b>		0.042
<b>Financial surplus/(deficit) for the year</b>		<u>0.334</u>
<b>Underlying recurring surplus / deficit as a percentage of recurring income</b>		<u>1.20%</u>

Health Scotland budgeted for a surplus of £0.276 million for the year to 31 March 2010. The final outturn was a surplus of £0.334 million

In achieving this surplus, Health Scotland encountered a variation from budget as follows:

#### *Income Generation*

Health Scotland's income was higher than anticipated in 2009/10. £60,000 of income was generated from the mental health initiative, "Choose Life". This is Scotland's national strategy and action plan to prevent suicide. Income was generated from the sale of Health Scotland training course materials.

#### *Capital Resource Limit*

Health Scotland secured an initial Capital Resource Limit of £0.75 million in 2009/10 to embark upon a Business Improvement Programme, a project to modernise Health Scotland's business systems. It was confirmed at a Board meeting in March 2010 that all of the 2009/10 Business Improvement Plan expenditure had been converted to revenue and, accordingly, the Capital Resource Limit had been reduced to £0.055 million. £0.052 million of the final Capital Resource Limit was utilised.

Figures confirmed by Alan Crawford, Director of Resource Management,  
21 June 2010

## Performance against Key Financial Targets

Health Scotland has achieved all three of its financial targets in the year, as follows:

	Limit set by SGHD £m	Actual Outturn £m	Variance (over)/under £m
Revenue Resource Limit	27,189	26,855	0.334
Capital Resource Limit	0.055	0.052	0.003
Cash Requirement	26,500	26,443	0.057

Health Scotland also reported efficiency savings in the year in line with the 2% Scottish Government target. Health Scotland had a target of £0.358 million in 2009/10 and achieved savings of £0.357 million.

## Managing Financial Performance

The Board receives detailed financial information each month to help manage performance against budgets and control expenditure. Detailed budget reports are prepared on a monthly basis. Finance liaise with Budget Holders to analyse the management reports and understand key variances against budgets. The information produced and frequency of reporting ensures decision makers have appropriate information on which to base decisions. The reporting arrangements were considered during the year and reported in our Interim Management Letter reported to the Audit Committee on 30 April 2010.

## Managing Performance and non financial performance targets

Operational performance is monitored regularly at Board level. Detailed reports are provided for HEAT targets showing results against targets. The reports are scrutinised by the Board and actions developed where targets are not being achieved.

For the year to 31 March 2010, 14 HEAT targets were relevant to Health Scotland per the 2009/10 Business Plan. We note from the Quarter 4 Board Report that a new method of reporting against HEAT targets will be introduced in 2010/11 to follow a more succinct layout and remove the level of narrative within the reports.

## Pay Modernisation

NHS Boards are required to ensure that at least 80% of staff covered by Agenda for Change have their annual Knowledge and Skills Framework development reviews completed and recorded on e-KSF by March 2011. Progress was reported in the Staff Governance Committee 2009/10 Annual Report. As of 31 March 2010, 93% of Health Scotland staff had a KSF outline, 48% of staff had a PDP, and 25% of staff had a review completed and recorded on e-KSF (with a further 30% in progress). This shows some progress towards achieving the March 2011 deadline.

This area remains a focus for Health Scotland.

## Sickness Absence

The Staff Governance Action Plan includes steps to reduce sickness absence levels and is an essential part of the improvement process as Health Scotland continues to record levels of sickness absence below agreed national targets. The average sickness absence rate for the 12 months to March 2010 was 2.5% against a national target level of 4%. This is 0.4% higher than the prior year.

## Best Value

Best Value audits are being carried out across the public sector to help protect taxpayers' interests by examining the use of resources and to report on the delivery of outcomes for people who use services. The Best Value audits are being carried out in a cycle focusing on distinct areas each year. In 2009/10 Audit Scotland issued eighteen toolkits with instructions that one was to be performed and validated by the auditors of each NHS Board.

In agreement with management the Customer Focus toolkit was selected for completion in 2009/10. The evaluation for each module is classed as: does not meet basic requirements; basic practices; better practices; or advanced practices.

Module	Evaluation
Corporate and Strategic Leadership	Better Practices
Approach to Customer Service	Better Practices
Customer Service Standards	Basic Practices
Accessibility of Customer Services	Better Practices

The aim of the Customer Focus Toolkit was to provide a structured, evidence based assessment of Health Scotland's approach to Customer Focus and its achievement of Best Value in this area. It is broken down into the four component elements and posed questions as to the extent to which good practice had been embedded across Health Scotland. The achievement of better practice in all but one area shows the commitment that Health Scotland has made in this important area. Three recommendations for improvements were made (one medium risk and two low risk).

Following discussion at the June 2010 Corporate Management Team meeting, Health Scotland requested an opportunity to submit additional evidence in support of one category 'Accessibility of Customer Services'. The detailed findings of the review will be presented to the Audit Committee in August 2010 to provide an opportunity for this additional evidence to be evaluated.

## 5. Governance and Control

### Overall Governance Arrangements

The established Committee framework at Health Scotland, incorporating Audit, Staff Governance, Remuneration, and Health Governance Committees remains in place. As reported in our Interim Management Letter (reported 30 April 2010), the terms of reference for the Board and each Committee were approved by the Board in December 2009.

The current Chief Executive has communicated his intention to stand down from the position in July 2010 and a replacement has now been secured. It is expected that the new Chief Executive will take up post in September 2010. This is a change in key personnel, in addition to the recent review of the organisational structure, and may lead to changes to the governance structure of Health Scotland over the coming months.

Further comment on governance arrangements was included in our Interim Management Letter (reported 30 April 2010).

### Partnership Working

Health Scotland devotes time and resources to achieve effective partnership working. As a special health board, Health Scotland has a close working relationship with all territorial Health Boards. Health Scotland continues to participate in and contribute to a number of partnership agreements including being part of the NHS Ayrshire and Arran Consortium for shared payroll and Cedar efinancials. The selection of Customer Focus as the most applicable best value toolkit this year (see Section 4) continues Health Scotland's dedication to meeting partner expectations. Further comment on governance arrangements was included in our Interim Management Letter (reported 30 April 2010).

### Systems of Internal Control

The results of our work on systems of internal control were communicated to the Audit Committee in our Interim Management Letter on 30 April 2010. The report contained 4 recommendations to improve controls, none of which was graded as higher risk or business critical in nature. Health Scotland has completed an action plan detailing those individuals responsible for implementing our recommendations and the timetable for completion. We will follow up this action plan during our 2010/11 audit process.

### Statement on Internal Control

The Code of Audit Practice requires us to review and report on Health Scotland's Statement on Internal Control. Health Scotland has used the correct format for its Statement and has outlined the processes it has employed to identify and evaluate risks. In addition, key elements of Health Scotland's control framework

have been highlighted. Based on our normal audit procedures, we do not disagree with the disclosures contained in the Statement.

### Follow up of outstanding recommendations

We followed up Health Scotland's progress in implementing recommendations made in the prior year. Our Follow Up Report was considered at the Audit Committee meeting on 30 April 2010. At the time of reporting, of the 16 agreed actions, progress was as follows:

Status	Follow Up Report 2007/08	Interim Management Letter 2007/08	Annual Report to Board Members 2007/08	Interim Management Letter 2008/09	Final Management Letter 2008/09	Best Value Audit 2008/09	Total
Action Implemented	1	2	2	2	2	-	9
Partially Implemented	1	-	-	3	-	-	4
Little Action to Date	-	-	1	-	-	-	1
Not Yet Due	-	-	-	-	-	1	1
No Longer Applicable	-	-	-	1	-	-	1
<b>Total</b>	<b>2</b>	<b>2</b>	<b>3</b>	<b>6</b>	<b>2</b>	<b>1</b>	<b>16</b>

Overall, Health Scotland has fully implemented nine of the recommendations from the reports issued in 2007/08 and 2008/09 with action taken on a further four of the recommendations. This represents progress towards improving the standards of internal control within the organisation. None of the recommendations made in prior reports was categorised as being higher risk.

### National Fraud Initiative

The National Fraud Initiative (NFI) brings together data from health bodies, councils, police and fire rescue bodies and other agencies, to help identify and prevent a wide range of frauds against the public sector. These include housing benefit fraud, occupational pension fraud and payroll fraud.

Health Scotland met its mandatory requirements in 2008/09 with regard to the submission of payroll data sets and subsequent investigation of matches. As reported in our Interim Management Letter (reported 30 April 2010), no exceptions were noted to our review of this area during the Interim Audit process.

## 6. Managing in Uncertain Times

The UK economy went into recession in mid-2008 for the first time since 1991. By summer 2009, UK economic output had fallen for five consecutive quarters. Significant financial pressures remain and the future economic position is uncertain and difficult to predict.

In response to the recession the UK Government almost doubled its level of borrowing to £175 billion in 2009/10 to allow it to increase public spending to support the economy. This level of borrowing means that the UK Government will need to pay higher debt interest payments, which in turn reduces the amount left for spending on the public sector. The recent Westminster General Election has resulted in a change of Government and this has led to a change in the plans for repaying the national debt with the new coalition government planning to halve the deficit by 2013/14. In order to achieve this ambitious target, significant reductions in public sector spending will be required. A recent paper by the Scottish Government Chief Economist predicts that public sector spending in Scotland may fall in real terms by 3% every year to 2014/15 and will take a total of 12 to 15 years to get back to 2009/10 levels.

Further details of this challenge may become clearer after the 22 June 2010 UK emergency budget, although the impact this will have on the NHS in Scotland may take some time to become apparent.

In April 2009, the UK Government also announced that Public Sector **capital budgets would fall**.

Taken together, these factors will have **serious consequences** for the Scottish budget. As a result of the current financial position, Audit Scotland has issued a number of reports on the matter. Key reporting themes from two of these reports are highlighted below.

### The NHS Health Scotland Perspective

Despite entering the downturn from a relatively strong financial position the NHS in Scotland currently faces a period of uncertainty. Impending tightening of public expenditure will impact the sector at a time when the cost base of many NHS bodies will rise.

Health Scotland is already considering how best to respond to the existing drive for efficiencies. We suspect that much of the relatively easier savings will already have been achieved so that the ability of Health Scotland to respond to a prolonged wave of revenue reduction arising from the re-assessment of public spending levels and priorities is likely to be more difficult. Forecasts for the next four years should include “downside” scenarios and challenge from zero and priority based budgeting. In addition, there are lessons to be learned from other organisations that have already weathered financial challenge and crisis. Tough decisions on which spending plans take priority are likely to be faced by all NHS boards in the coming months and years.

While some NHS bodies will be more vulnerable than others, all NHS bodies, including Health Scotland, will be affected. Regardless of whether an NHS body is in a relatively stronger or weaker financial position, difficult decisions are going to have to be made. We recommend looking at six key areas that our experience in other sectors has shown may be relevant to addressing the challenges ahead:



- Honesty and awareness of the size of the challenge
- Strong leadership
- Need to engage with the whole organisation and external stakeholders
- Realistic and detailed plans to resolve the situation
- Rigorous implementation (programme management arrangements)
- Financial control and discipline

#### ACTION POINT 4

#### Audit Scotland - Scotland's Public Finances: Preparing for the Future

In November 2009 Audit Scotland published their report: 'Scotland's Public Finances: Preparing for the Future'. This report highlighted the fact that the Scottish Government budget is likely to have peaked in 2009/10 for the foreseeable future. This means that individual public bodies will have **smaller budgets** in future years. It highlighted that in addition, **other public sector income is likely to be less than previously forecast** – in particular, NHS capital funding.

The report concluded that we are at a real **historical breakpoint** in public finances.

#### Audit Scotland - Improving Public Sector Efficiencies

Following on from the Scotland's Public Finances report, Audit Scotland published a further report in February 2010: 'Improving public sector efficiency'. It provided a position statement on the first year (2008/09) of the Efficient Government Programme (the Programme), which aims to deliver £1.6 billion efficiency savings over the three years to 2010/11. It also gave an update on how the Scottish Government and public bodies have addressed the recommendations made in a 2006 Audit Scotland report about the previous efficiency programme.

The report noted that Scottish public bodies had reported more efficiency savings than the Government's two per cent target. However, there were serious financial challenges ahead – the biggest since devolution – and making the required savings simply through efficiency will become increasingly difficult.

The report recommends that to deal with reduced future funding, public bodies need to consider fresh approaches to improving efficiency and productivity. They must take a more fundamental approach to identifying priorities, improving the productivity of public services, and to improving collaboration and joint working.

To support these high-level recommendations, Audit Scotland, the Northern Ireland Audit Office and the Wales Audit Office have drawn on their combined experience to develop a detailed good practice checklist. The checklist is intended to promote detailed review and reflection and, if necessary, a basis for improvement. We recommend that those responsible for leading efficiency and improvement work at Health Scotland should formally assess themselves against each question.

These Audit Scotland reports have been presented previously to the Board for consideration.

## The Health Scotland Action Plan

Health Scotland is required to achieve efficiency savings of 2%, as outlined in the NHS Scotland Efficiency and Productivity Programme: Delivery Framework, published in June 2009. Cash and productivity efficiency savings are required to enable Health Scotland to produce a break-even budget. Health Scotland has identified the key areas for 2010/11 to achieve the 2% three year target and generate £0.316 million of savings towards the annual budget.

Figures confirmed by Alan Crawford, Director of Resource Management,  
23 June 2010

2010/11 Projected Outturn	£m	£m
Recurring income	21.467	
Recurring expenditure (before savings)	( 21.449)	
Recurring savings	<u>0.252</u>	
<b>Underlying recurring surplus</b>		0.270
Non-recurring income	5.453	
Non-recurring expenditure (before savings)	( 5.517)	
Non-recurring savings	<u>0.064</u>	
<b>Non-recurring surplus</b>		<b><u>( 0.000 )</u></b>
<b>Financial break even for the year</b>		<b><u>0.270</u></b>
<b>Underlying recurring surplus as a percentage of recurring income</b>		<b><u>1.26%</u></b>

## Financial Plan

The Board has completed its revised three year financial plan and this is included within the Local Delivery Plan 2009/10 to 2011/12 submitted to the SGHD for approval.

## Service Sustainability

During 2009/10 Health Scotland performed a review of their organisational structure with a view to developing the most effective structure to support their business activities. This resulted in some changes after the end of the 2009/10 financial year. The main changes affected the corporate communications function which became part of the Directorate of Programme Design and Delivery, and the Human Resources function which became part of the re-titled Directorate of Equality, People and Performance.

Health Scotland has been proactive in considering the impact of the current and future economic climate on their service provision. To ensure that services are sustainable, management has undertaken financial planning to assess the effect of budget cuts on service provision and to inform future planning based on various scenarios such as budget freezes and budget reductions.

## Overall

In overall terms the uncertainties concerning future funding levels will place significant pressure on Health Scotland meaning that existing strategies and approaches may need to be re-prioritised and flexed over the next few years.

# Appendices

# Appendix A – Action Plan

Ref	Issue and Recommendation	Management Response
1	<p>The volume of manual accruals required after the year end was significant. This was due to the high levels of spend and budget commitment in the last quarter of the year. Management had made some progress in increasing spending earlier in the financial year. However, more needs to be done in this area both from an ongoing operational perspective but also to ensure annual reporting timescales can continue to be met more readily.</p>	<p><b>Management Response:</b>            Recommendation accepted. The need to build on improvements made is recognised. Actions will be taken during 2010/11 to scrutinise expenditure plans and action necessary changes. In addition, work will be undertaken to identify and rectify any underlying issues in relation to budgeting, planning, reporting and accountability systems.</p> <p><b>Responsible Officer:</b>            Chief Executive (and executive directors)</p> <p><b>Due Date:</b>            31 December 2010</p>
2	<p>The current accounts preparation process places a considerable burden on a small number of individuals within the finance team. In 2010 this has resulted in the accounts preparation and audit process being more time pressured than necessary. There are several recently recruited new staff members within the finance team which should alleviate delays in 2011. Management should reconsider the duties performed by each member of the finance team in the coming year in order to make the year end accounts process achievable in a shorter timeframe.</p>	<p><b>Management Response:</b>            Recommendation accepted. Year end accounts processes including staff responsibilities will be reviewed and improvements made prior to preparation of 2010/11 Annual Accounts.</p> <p><b>Responsible Officer:</b>            Director of Resource Management</p> <p><b>Due Date:</b>            28 February 2011</p>

Ref	Issue and Recommendation	Management Response
3	<p>Following our review of Health Scotland's 2008/09 IFRS shadow accounts, it was identified that Health Scotland does not have a breakdown of the Revaluation Reserve to individual asset level. A recommendation to complete this exercise was reported to the Audit Committee in November 2009. This was not required for our audit of the 2009/10 financial statements and had not been completed at the time of our visit. As the unresolved amount is not material to the financial statements, we have not insisted in any adjustment. However, management should aim to complete this exercise before the next interim audit visit.</p>	<p><b>Management Response:</b>  Recommendation accepted. The exercise referred to will be completed before the next interim audit visit.</p> <p><b>Responsible Officer:</b>  Director of Resource Management</p> <p><b>Due Date:</b>  31 October 2010</p>
4	<p>The NHS in Scotland faces a period of uncertainty and impending tightening of public expenditure will impact the sector at a time when the cost of providing services is likely to rise. Forecasts for the next four years should include "downside" scenarios and challenge from zero and priority based budgeting. Tough decisions on which spending plans take priority are likely to be faced by all NHS boards in the coming months and years and this requires to be an area of primary focus by the Board and Management.</p>	<p><b>Management Response:</b>  Recommendation accepted. Initial contingency financial planning projections will be updated as appropriate to reflect the latest available data and brought forward for consideration by the Corporate Management Team, Audit Committee and Board.</p> <p><b>Responsible Officer:</b>  Chief Executive/Director of Resource Management</p> <p><b>Due Date:</b>  30 September 2010</p>

# Appendix B – Communications to Management

International Standards on Auditing (“ISA”) (UK&I) 260 – Reporting to those charged with Governance, requires that the External Auditor communicates certain matters to those charged with Governance. Those charged with Governance is taken to be the Members of the Audit Committee with responsibility discharged through the regular meetings of the Audit Committee during the year. Summarised below are the requirements set out within ISA 260 together with reference to the relevant communication with you during 2009/10 or comments as appropriate.

Communication Required under ISA 260	Reference/Comment
Engagement Letters	Signed Engagements Letter with Audit Scotland at the start of our 5 year appointment and updated annually.
Independence	Audit Planning document report to 15 January 2010 Audit Committee and confirmed no member of audit team has any direct interest, financial or otherwise, in NHS Health Scotland.
Audit Approach and Scope	Audit Planning document (reported to Audit Committee 15 January 2010)
Accounting Policies/Practices with a Material Effect on the Financial Statements	Sections 3 and 4 of our Annual Report to Board Members and the Auditor General for Scotland.
Potential Effects of Material Risks and Exposures	Audit Planning document (15 January 2010).
Audit Adjustments	Section 3 of our Annual Report to Board Members and the Auditor General for Scotland.
Material Uncertainties relating to Going Concern	None identified.
Disagreement with Management about Matters that could be Significant to the Financial Statements	Not applicable.
Expected Modifications to the Auditor’s Report	No modifications identified. A true and fair opinion provided
Letter of Representation	Signed by Management 25 June 2010.
Material Weaknesses in Internal Control	Internal Controls findings reported separately in our Interim Management Letter (30 April 2010), Section 5 of our Annual Report to Board Members and the Auditor General for Scotland.
Fraud	Discussed fraud arrangements with the Chair of the Audit Committee (15 January 2010), Management throughout audit process.

Communication Required under ISA 260	Reference/Comment
Laws and Regulations	We have not identified any material breaches of laws and regulations in the period which impact on the 2009/10 Financial Statements.
Audit Materiality	Audit Planning document – presented to Audit Committee on 15 January 2010.
Fair Value Measurement and Disclosure	Included in representation letter, signed by management dated 25 June 2010.
Related Parties	Other than those transactions disclosed in the financial statements we have not identified any further transactions requiring disclosure.

### Formal Reporting to Management during 2009/10

During the year we have presented a number of formal reports to Management and the Audit Committee and produced certain outputs. Our principal outputs during 2009/10 are summarised below:

Formal Output	Timing	
Letter outlining work undertaken in relation to our review of Health Scotland's 2008/09 shadow IFRS based financial statements	15 January 2010	
Audit Plan	15 January 2010	
Detailed Timetable for 2009/10 Financial Audit	30 April 2010	
Follow-up of 2008/09 Recommendations	30 April 2010	
Interim Management Letter	30 April 2010	
Annual Report to Board Members and the Auditor General for Scotland	25 June 2010	
Audit Opinions	25 June 2010 Board Meeting	
1. True and fair view on the financial statements and regularity of income and expenditure ✓		} Unqualified Audit Opinions
2. Remuneration Report (parts only) ✓		

### **Freedom of Information Act (Scotland) 2002**

*In the event that, pursuant to a request which the institution has received under the Freedom of Information Act (Scotland) 2002 or the Environmental Information Regulations 2004 (as the same may be amended or re-enacted from time to time) or any subordinate legislation made thereunder (collectively, the "Legislation"), Health Scotland is required to disclose any information contained in this report, it will notify PwC promptly and will consult with PwC prior to disclosing such report. Health Scotland agrees to pay due regard to any representations which PwC may make in connection with such disclosure and to apply any relevant exemptions which may exist under the Legislation to such report. If, following consultation with PwC, Health Scotland discloses any of this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.*

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