



**Scott-Moncrieff**  
business advisers and accountants

# **The State Hospitals Board for Scotland**

2016/17 Annual Audit Report to the State  
Hospitals Board for Scotland and the Auditor  
General for Scotland

**June 2017**

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# Key messages

## Annual accounts

The State Hospitals Board for Scotland's annual report and accounts for the year ended 31 March 2017 were approved by the Board on 29 June 2017.

We reported within our independent auditor's report, unqualified opinions on the financial statements, the regularity of transactions and on other prescribed matters. There were no matters which we were required to report by exception.

We received draft annual report and accounts and supporting papers of a good standard, in line with our agreed audit timetable and document requests. We are pleased to report that the audit process ran smoothly, and our thanks go to management and staff for their assistance with our work.

## Wider Scope

### Financial management

- We concluded that the Board has effective arrangements in place over the management of its finances. Our conclusion is based on a review of the Board's financial performance, underlying financial position, financial reporting and achievement of savings targets.

### Financial sustainability

- The Board has appropriate arrangements in place for short and medium term (3 year) financial planning.
- The Board has, over recent years, delivered a high proportion of its savings on a non-recurring basis. In 2016/17 this equated to 86% of total savings. Delivering non-recurring savings means that a similar level of savings is required in all future years until the underlying cost base is reduced on a recurring basis. We note that, looking forward, the Board is forecasting that the proportion of recurring savings will increase.
- The achievement of future financial targets will depend on continuing tight control of expenditure, delivery of a challenging savings plan and may also require some difficult decisions to be taken in areas such as workforce planning. This will be a key area which the Board will have to monitor very closely.

### Governance & transparency

- Overall we have concluded that the Board's governance arrangements are adequate and appropriate.

### Value for money

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

## Key facts

- All key financial targets were met in 2016/17
- The revenue resource limit was underspent by £50,000
- Capital expenditure of £323,000 was reported, against a revised capital resource allocation of the same amount.
- The savings target of £1.775million was achieved.
- A breakeven position is forecast over each of the next three years, subject to realisation of further planned savings.
- 6 of the Board's 12 reported key performance measures were on target for 2016/17. In comparison to 2015/16, 1 key performance measure had improved, 5 were comparable and in 6 performance had declined.
- The Board is working with other special/national health boards to collectively standardise and share services with a target of reducing operating costs of special boards by £15million in 2017/18.

## Conclusion

This report concludes our audit for 2016/17. Our work has been performed in accordance with the Audit Scotland Code of Audit Practice, International Standards on Auditing (UK and Ireland) and Ethical Standards.

**Scott-Moncrieff**  
**June 2017**

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# Introduction

# Introduction

1. This report summarises the findings from our 2016/17 audit of the State Hospitals Board for Scotland (“the Board”).
2. We outlined the scope of our audit in our External Audit Plan, which we presented to the audit committee in January 2017. The core elements of our audit work in 2016/17 have been:
  - an interim audit concentrating on the key financial systems;
  - an audit of the 2016/17 annual report and accounts;
  - a review of the arrangements for governance and transparency, financial management, financial sustainability and value for money;
  - consideration of the National Fraud Initiative data-matching exercise; and
  - consideration of the local impact of Audit Scotland’s national performance report [The Role of Boards](#).
3. The Board is responsible for preparing an annual report and accounts that show a true and fair view and for implementing appropriate internal control systems. The weaknesses or risks identified are only those that have come to our attention during our normal audit work, and may not be all that exist. Communication in this report of matters arising from the audit of the annual report and accounts or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
4. The report contains an action plan with specific recommendations, responsible officers and dates for implementation. Senior management should assess these recommendations and consider their wider implications before deciding appropriate actions. We give each recommendation a grading to help the Board assess their significance and prioritise the actions required.
5. We discussed and agreed the content of this report with the Finance and Performance Management Director. We would like to thank

all management and staff for their co-operation and assistance during our audit.

## Adding value through the audit

6. All of our clients quite rightly 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.
7. We welcome any comments you may have on the quality of our work and this report via: [www.surveymonkey.co.uk/r/S2SPZBX](http://www.surveymonkey.co.uk/r/S2SPZBX).
8. This report is addressed to both the Board and the Auditor General for Scotland and will be published on Audit Scotland’s website. [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

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# Financial statements

# Financial statements

9. The Board's financial statements are the principal means of accounting for the stewardship of its resources and its performance in the use of those resources. The respective responsibilities of the Board and the auditor in relation to the financial statements are outlined in Appendix 2.
10. In this section we summarise the issues arising from our audit of the 2016/17 annual accounts.

## Overall conclusion

### An unqualified audit opinion on the financial statements

11. The financial statements for the year ended 31 March 2017 were approved by the Board on 29 June 2017. We reported, with our independent auditor's report:
  - an unqualified opinion on the annual accounts;
  - an unqualified audit opinion on regularity; and
  - an unqualified audit opinion on other prescribed matters.
12. We are also satisfied that there were no matters which we were required to report by exception.

### Good administrative processes were in place

13. We received draft financial statements and supporting papers of a good standard, in line with our agreed audit timetable. We are pleased to report that the audit process ran smoothly, and our thanks go to finance management and staff for their assistance.
14. The financial statements were submitted to the Scottish Government and the Auditor General for Scotland by the 30 June 2017.

### Our assessment of risks of material misstatement

15. The assessed risks of material misstatement described 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 financial statements as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the financial statements is not modified with respect to any of the risks described in Exhibit 1 below.

## Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

### 1.1 Treatment of unspent RRL

In 2015/16 the Board deferred income to the value of £560,000 in its annual report and accounts. Of this, £487,000 related to unspent RRL allocation. This should have been presented in the financial statements as an underspend in the year and approval sought from the SGHSCD to carry this forward into 2016/17. This was not adjusted for in the 2015/16 financial statements. The Board agreed to review its accounting treatment in respect of unspent RRL from 2016/17 onwards. There is a risk however that the correct accounting treatment is not adopted which results in a material misstatement in the financial statements.

*Excerpt from the 2016/17 External Audit Plan*

16. Management has reviewed the Board's accounting treatment in respect of unspent RRL. In 2016/17, we noted that no unspent RRL allocation was accounted for as deferred income. Based on our audit work performed we have concluded that the correct accounting treatment was adopted.



## Exhibit 1: Our assessment of risks of material misstatement and how the scope of our audit responded to those risks

### 1.2 Management override

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

*Excerpt from the 2016/17 External Audit Plan*

17. We have not identified any indications of management override in the year. We have reviewed the Board’s accounting records and obtained evidence to ensure that any significant transactions outside the normal course of business were valid and accounted for correctly. We have also reviewed the journal entries processed in the period and around the year end.

### 1.3 Revenue recognition

Under ISA 240 – “*The auditor’s responsibilities relating to fraud in an audit of financial statements*”, there is a presumed risk of fraud in relation to revenue recognition. The presumption is that the Board could adopt accounting policies or recognise income and expenditure transactions in such a way as to lead to a material misstatement in the reported financial position.

*Excerpt from the 2016/17 External Audit Plan*

18. We have gained reasonable assurance on the completeness and occurrence of income and we are satisfied that income is fairly stated in the financial statements. To inform our conclusion we evaluated the Board’s key revenue streams and reviewed the controls in place over revenue accounting. We also carried out testing to confirm that the revenue recognition policy is appropriate and that it was consistently applied throughout the year. We considered the findings from our audit work in respect of the Board’s treatment of unspent RRL (risk 1.1 above) in forming our conclusion. As noted above, we have concluded that the correct accounting treatment was applied.

## Our application of materiality

19. The assessment of what is material is a matter of professional judgement and involves considering both the amount and the nature of the misstatement. This means that different materiality levels will be applied to different elements of the financial statements.
20. Our initial assessment of materiality for the financial statements was £525,000. We revised our assessment, following receipt of the draft annual report and accounts, to £495,000 and it remained at this level throughout our audit. Our assessment of materiality equates to approximately 1.5% of the Board’s Revenue
- Resource Limit (RRL). A key target for the Board is achieving a breakeven position against its RRL. We consider the RRL to be one of the principal considerations for the users of the financial statements when assessing the financial performance of the Board.
21. We set a performance materiality for each area of work based on a risk assessment for the area and percentage application of overall materiality. We then perform audit procedures on all transactions, or groups of transactions, and balances that exceed our performance materiality. This means that we are performing

a greater level of testing on the areas deemed to be of significant risk of material misstatement. Performance testing thresholds used are set out in the table below:

Area risk assessment	Weighting	Performance materiality
High	45%	£222,750
Medium	55%	£272,250
Low	70%	£346,500

22. We agreed with the Audit Committee that we would report to them on all audit differences in excess of 2% of the overall materiality figure, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the annual report and accounts.

### Audit differences

23. We are pleased to report that there were no material adjustments to the draft financial statements that have had an impact on the outturn against the Revenue Resource Limit (RRL). We identified some disclosure and presentational adjustments during our audit, which have been reflected in the final set of financial statements.
24. We identified two audit differences during our work that have not been adjusted for in the financial statements. These two differences are not considered to be material to the financial statements, either individually or in aggregate. Through discussion with the Finance and Performance Management Director the decision was taken not to adjust the financial statements. These unadjusted audit differences are included in the representation letter.

### Board representations

25. We have requested that the Board present a signed representation letter, covering a number of issues, to us at the date of signing the annual report and accounts.

## An overview of the scope of our audit

26. The scope of our audit was detailed in our External Audit Plan, which was presented to the Audit Committee in January 2017. 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.
27. 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.
28. Our standard audit approach is based on performing a review of the key financial systems in place, substantive tests and detailed analytical review. Tailored audit procedures, including those designed to address significant risks, were completed by the audit fieldwork team and the results were reviewed by the audit manager and audit partner. In performing our work, we have applied the concept of materiality, which is explained earlier in this report.

### Regularity

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

### Governance statement

30. We are satisfied that the governance statement complies with the Scottish Ministers' guidance and that the content is consistent with the financial statements.
31. The disclosures in the governance statement reflect internal audit's conclusion for 2016/17: "Significant (with minor improvements) assurance can be given on the overall adequacy and effectiveness of the organisation's framework of risk management, internal control and governance".

### Remuneration report

32. Our independent auditor's report confirms that the part of the remuneration report to be audited has been properly prepared.

## Performance report

33. We are satisfied that the performance report is consistent with the financial statements and has been prepared in line with Scottish Ministers' guidance.

## Follow up of prior year recommendations

34. As part of our audit we have followed up the agreed audit recommendations from prior years which were yet to be implemented. We are pleased to report that all outstanding recommendations, where the completion date has passed, have now been implemented.

## Other matters identified during our audit

35. We have not identified any other matters during our audit which we require to bring to the attention of the Board.

## Qualitative aspects of accounting practices and financial reporting

36. We have considered the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided in the

financial statements. Our findings are summarised below:

Qualitative aspect considered	Audit conclusion
The appropriateness of the accounting policies used.	The accounting policies, which are disclosed in the financial statements, are considered appropriate to the Board.
The timing of the transactions and the period in which they are recorded.	We did not identify any concerns over the timing of transactions or the period in which they were recognised.
The appropriateness of the accounting estimates and judgements used.	The accounting estimates and judgements used by management in preparing the financial statements are considered appropriate. The principal areas of estimates and judgements have been: asset depreciation rates and the valuation of provisions.
The potential effect on the financial statements of any uncertainties, including significant risks and related disclosures that are required.	We have not identified any uncertainties, including any significant risk or required disclosures, which should be included in the financial statements.
The extent to which the financial statements have been affected by unusual transactions during the period and the extent that these transactions are separately disclosed.	From the testing performed, we identified no significant unusual transactions in the period.
Apparent misstatements in the annual report or material inconsistencies with the financial statements.	The annual report contains no material misstatements or inconsistencies with the financial statements.
Any significant financial statements disclosures to bring to your attention.	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.
Disagreement over any accounting treatment or financial statements disclosure.	While some disclosure and presentational adjustments were made during the audit process there was no material disagreement during the course of the audit over any accounting treatment or disclosure.
Difficulties encountered in the audit.	There were no significant difficulties encountered during the audit.

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# Financial management

# Financial management

37. Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. It is the Board's responsibility to ensure that its financial affairs are conducted in a proper manner.

## Overall conclusion

38. We concluded that the Board has effective arrangements in place over the management of its finances. Our conclusion is based on a review of the Board's financial performance,

underlying financial position, financial reporting and achievement of savings targets.

## The Board's financial performance in 2016/17

39. The Board has to work within the resource limits and cash requirements set by the Scottish Government Health and Social Care Directorates (SGHSCD). As shown in the table below, the Board met all of its key financial targets in 2016/17.

### Exhibit 2: Performance against key financial targets

Financial target	Target £'000	Actual £'000	Underspend £'000	Target achieved
Revenue Resource Limit – Core	32,169	32,119	50	
Revenue Resource Limit – Non core	934	934	-	
<b>Revenue Resource Limit</b>	<b>33,103</b>	<b>33,053</b>	<b>50</b>	<b>Yes</b>
<b>Capital Resource Limit</b>	<b>323</b>	<b>323</b>	<b>-</b>	<b>Yes</b>
<b>Cash Requirement</b>	<b>33,224</b>	<b>33,224</b>	<b>-</b>	<b>Yes</b>

Source: Annual Report and Accounts for the year ended 31 March 2017

40. The Board reported a £50,000 under-spend against its revenue resource limit (RRL). This represents 0.16% of the RRL and is therefore in line with the breakeven position forecast at the start of the year. The outturn includes a carry forward of £11,000 from 2015/16, which was received as a non-recurring revenue allocation during 2016/17.

41. During the year over spends occurred against certain budgets. In particular, nursing costs were higher than budgeted with clinical activity and backfill for staff sickness (over and above what had been budgeted for) contributing significantly to the over spends. Reported over spends in respect of nursing costs is consistent with prior years.

42. The most significant over spends occurred within the General Manager directorate, which

is the Board's largest directorate in terms of staffing and budget allocation. At the year end, an over spend of £994,000 was reported against this directorate. This was offset against under spends reported by other directorates, including the corporate functions and medical and nurse non wards, which under spent by £717,000, £224,000 and £129,000 respectively. Corporate functions underspends were due to delays in the delivery of strategic projects, release of deferred income and vacancies in the year. Under spends in medical were largely due to having fewer recharges for doctors in training from other boards and in nursing non wards due to vacancies.

### Exhibit 3: Performance against budget

Function	Annual Budget £'000	Actual £'000	Variance £'000
Corporate functions	5,910	5,193	717
General manager	22,453	23,447	(994)
Medical	2,253	2,029	224
Nursing non-ward	1,016	887	129
Security	1,471	1,497	(26)
<b>Total</b>	<b>33,103</b>	<b>33,053</b>	<b>50</b>

Source: Finance report as at 31 March 2017

43. Within the General Manager directorate, ward nursing costs were approximately £1.313million over budget (£978,000 in 2015/16). Nursing overtime costs continue to be a significant cost pressure for the Board; this is after establishing an overtime budget of £300,000. Due to the nature of the service provided by the Board, all nursing shifts which are scheduled on wards and are then affected by sickness, high levels of clinical intensity and holiday absence are required to be filled in order to reduce risk to staff. As such, the Board incurs higher levels of overtime costs.

#### Savings target met in 2016/17

44. In order to achieve a balanced outturn position, the Board was required to identify £1.775million in efficiency savings. The Board has delivered this savings target. £1.533million of these savings (86%) are non-recurring and are mainly attributable to vacancy management.

### Exhibit 4: Efficiency savings

Source of savings	Target as per LDP £'000	Actual savings £'000	Variance under/(over) achieved £'000
Workforce – pay non-recurring	820	1,191	371
Workforce – pay recurring	382	233	(149)
Non pay non-recurring	504	341	(163)
Non pay recurring	69	10	(59)
<b>Savings as at 31 March 2017</b>	<b>1,775</b>	<b>1,775</b>	<b>0</b>

Source: Finance report as at 31 March 2017

## Capital resource limit

45. The Board's initial capital resource allocation was £269,000. During the year, £54,000 was transferred from revenue to capital as a result of certain eHealth projects requiring a capital resource allocation. Authorisation was received from the Scottish Government for these transfers. The Board reported capital expenditure of £323,000 against its revised capital resource allocation of the same amount.

## Systems of internal control

46. We have evaluated the key financial systems and internal financial controls to determine whether they are adequate to prevent material misstatements in the financial statements. Our approach has included audit testing on the key internal financial controls to confirm that they are operating as intended.

47. As reported in our External Audit Interim Report, we did not identify any significant deficiencies in the operation or design of internal financial controls over the Board's key financial systems. Reliance has been placed on these controls during our 2016/17 audit.

## Internal audit

48. The internal audit service was provided by KPMG. To avoid duplication of effort and to ensure an efficient audit process we have taken cognisance of all of the work of internal audit.

## Fraud and corruption

49. In accordance with the Code of Audit Practice, we have reviewed the arrangements for the prevention and detection of fraud and corruption. Overall, we found the Board's arrangements to be sufficient and appropriate.

## National Fraud Initiative (NFI)

50. The National Fraud Initiative (NFI) is a counter-fraud exercise co-ordinated by Audit Scotland working together with a range of Scottish public bodies, external auditors and overseen by the Cabinet Office for the UK as a whole to identify fraud and error.

51. The NFI exercise produces data matches by comparing a range of information held on various public bodies' systems to identify potential fraud or error. Bodies investigate these matches and record appropriate outcomes based on their investigations.

52. The most recent NFI exercise commenced in October 2016 and as part of our 2016/17 audit we monitored the Board's participation in NFI. Overall we concluded that the Board has actively participated in the NFI exercise.

53. The NFI exercise identified 141 data matches, of which 30 were recommended for investigation. Due to circumstances outwith the Board's control, matches relating to payroll data were not released on a timely basis. These matches account for four of the total matches (none of the recommended matches).

54. All matches have been, or are in the process of being investigated. Reports on the exercise are presented to the Audit Committee.





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# Financial sustainability

# Financial sustainability

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

## Key audit risk

56. As outlined in our External Audit Plan, we considered there to be a significant risk to the wider scope of our audit in relation to financial sustainability:

## Financial sustainability

The Board has produced a local delivery plan (LDP) covering the financial years 2016/17 to 2020/21. The LDP forecasts a breakeven position in each of the next five years. To achieve this, however, the Board is expected to make substantial efficiency savings each year. There is a risk that delivery of the Board's efficiency savings plans are at the detriment of services and/or on-going financial health.

## Overall conclusion

57. The Board has appropriate arrangements in place for short and medium term (3 year) financial planning.
58. The Board has, over recent years, delivered a high proportion of savings on a non-recurring basis, although we note that the Board has forecast that a higher proportion of recurring savings will be delivered in future years.
59. The achievement of future financial targets will depend on continuing tight control of expenditure, delivery of a challenging savings plan and may also require some difficult decisions to be taken in areas such as

workforce planning. This will be a key area which the Board will have to monitor very closely.

## Future financial plans

60. The Board has drafted a Local Delivery Plan (LDP) which outlines its financial plans for the three year period to 2019/20. The Board is forecasting a breakeven position over each of these years although this is dependent on the realisation of its savings plan. The Board expects its core RRL to remain broadly consistent in the short term, as shown below.

## Exhibit 5: Anticipated movements in core RRL

	2017/18	2018/19	2019/20
Core RRL (£'000)	32,128	32,304	32,477
Increase/(decrease) on prior year (%)	0.03%	0.5%	0.5%

Source: The State Hospitals Board for Scotland draft Local Delivery Plan 2017/18 – 2019/20

## Savings

61. Recurring savings are savings that, once achieved, recur year-on-year from that date, for example savings on costs as a result of streamlining services. Non-recurring savings are one-off savings that apply to one financial year, and do not result in ongoing (recurring) savings in future years, for example not filling a

vacancy on a temporary basis. Identifying new recurring savings becomes more difficult for NHS boards each year. Boards that make high levels of non-recurring savings will have to find further savings in future years. Non-recurring savings are typically short-term decisions rather than initiatives to change the way services are provided.

62. The LDP identifies the savings required over the next three years to enable the Board to achieve a breakeven position. Exhibit 6 below highlights the split between recurring and non-recurring savings.
63. The Board has, over recent years, delivered a

high proportion of non-recurring savings. In 2016/17 this equated to 86% of the overall savings (2015/16 67%). We note (Exhibit 6) that, in comparison with previous years, the Board has forecast that the proportion of non-recurring savings will reduce.

## Exhibit 6: Savings split between recurring and non-recurring

Savings by type	2017/18	2018/19	2019/20
Recurring £'000	433	653	711
Recurring unidentified £'000	200	-	-
Non-recurring £'000	769	965	1,115
<b>Total £'000</b>	<b>1,402</b>	<b>1,618</b>	<b>1,826</b>
<b>% ratio (recurring: non-recurring)</b>	<b>45:55</b>	<b>40:60</b>	<b>39:61</b>

Source: The State Hospitals Board for Scotland draft Local Delivery Plan 2017/18 – 2019/20

### Cost pressures

64. The Board has identified a number of pressures over the coming year which will have an impact on meeting its financial plan:
- **Expenditure associated with the Hospital** – this includes, for example, expenditure on repairs essential for health and safety compliance.
  - **Workforce plan numbers and skill mix** – the Board has yet to achieve the planned workforce numbers. The issues relate mainly to nursing costs. The full workforce plan is currently under review.
  - **Payroll costs** – increased payroll costs in respect of pension and national insurance contributions. Additional costs associated with the apprenticeship levy.
  - **Utility costs** – both a price and usage pressure.
65. The achievement of future financial targets will depend on continuing tight control of expenditure, delivery of a challenging savings plan and may also require some difficult decisions to be taken in areas such as workforce planning. This will be a key area which the Board will have to monitor very closely.

### Long term strategic financial planning

66. As part of its 2016/17 audit plan, internal audit carried out a review of long-term strategic financial planning. The objective of this review was to consider the long-term strategic financial planning processes in light of continued financial pressures, and the extent to which long-term strategic and financial plans are aligned and robust.
67. Internal audit concluded that *“in relation to long term financial planning we concluded that “significant assurance with minor improvements required” can be given. This is due to the short term nature of planning at the Board.”*
68. Internal audit noted that the Board’s financial planning process is focussed primarily on the medium term, where targets are met through non-recurring rather than recurring savings. This is in part due to the delivery of savings being achieved by the Board being through vacancy management resulting in savings being achieved on a non-recurring basis.
69. Internal audit’s findings are consistent with those identified during our audit. As noted above, the Board’s LDP covers a three year period, which is standard practice in the NHS. In our view, all NHS boards should develop longer term financial plans on a 5 to 10 year

basis. This would assist the Board in highlighting risks to the financial sustainability of its service model over the longer term, allocating resources to the services with highest demand and identifying opportunities for strategic service redesign.

***Action plan point 1***

## **National priorities – collaborative working**

- 70.** Special/National Health Boards have been tasked by SGHSCD to work together to identify ways to collectively standardise and share services with a target to reduce the operating costs of Special Boards by £15million in 2017/18 so that this can be reinvested in frontline NHS Scotland priorities.
- 71.** Rather than delivering this saving through a pro-rata share of the £15million apportioned in terms of the RRLs of each Board (or other arbitrary allocations); the plan is to deliver it through targeting real change in the way they deliver support services. Four key workstreams have been developed covering; transformation, review of support services, cash releasing efficiency savings and management of non-recurring spend.
- 72.** Each Board has however recognised that they will individually require to contribute non-recurring contributions in 2017/18 as it will take time for any initiatives to impact on a recurring basis. The State Hospitals Board for Scotland is working on an initial assumption of a contribution of £440,000 which will be achieved from the temporary closure of one of its ward and the associated reduction in workforce additional hours costs. These savings are not included in the draft LDP as at the time the Board did not know what contribution may be required.

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# **Governance & transparency**

# Governance and transparency

73. Governance and transparency is concerned with the adequacy of governance arrangements, leadership and decision making, and transparent reporting of financial and performance information. The Board is responsible for ensuring the proper conduct of its affairs including compliance with relevant guidance, the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements.

## Overall conclusion

74. Overall we have concluded that the Board's governance arrangements are adequate and appropriate.

## Governance arrangements

### Board and senior staff changes

75. The Board Chair's second term came to an end in March 2017. The Chair has recently been reappointed for a third, two year term.

76. The Nursing Director retired in January 2016. An appointment to a newly created post (and replacing the Nursing Director post) of Director of Nursing and Allied Health Professions was made in June 2016.

### Standards of conduct

77. In our opinion, the Board's arrangements in relation to standards of conduct and the prevention and detection of bribery and corruption remain adequate and appropriate.

78. To inform our conclusion we have reviewed the arrangements for adopting and reviewing standing orders, financial instructions and schemes of delegation and complying with national and local codes of conduct.

79. We have previously noted that a large number of policies and procedures are out of date and/or not available to staff. The Board has been working towards addressing this issue. We have noted the following progress in relation to this action:

As at March 2017, out of 130 policies:

- 73 were up to date;
- 32 were overdue for review;
- 13 policies were under review

- 5 were under consolidation; and
- 7 were awaiting confirmation, following a consultation period, to circulate.

## Risk management

80. Public sector bodies in Scotland currently face increasing demand for quality services, but also have to face the challenge of tighter financial budgets. Effective risk management encourages effective decision making and better use of resources.

81. The Board's risk management arrangements continue to be developed. A full review of the Corporate Risk Register was undertaken in 2015 by way of a workshop facilitated by KPMG. A report finalising the recommendations from this review was published in January 2016.

82. We have previously noted that the Board's risk management strategy has not been reviewed since 2009 and therefore did not reflect current arrangements. We understand this has since been updated and will be presented to the Board this month (June 2017) for approval.

## Role of boards

83. In September 2010 the Auditor General for Scotland published a report aiming to assess the role and work of boards across 67 public bodies and 39 colleges. The report made a number of recommendations as detailed in Exhibit 7 below.

## Exhibit 7: Key messages from 'Role of Boards' report

All non-executives should receive a formal induction	Boards should review the skills and expertise required on the Board and attract people to plug the gaps	Performance of non-executives should be assessed on a regular basis	Scrutiny efforts should be focused on organisational performance, financial and risk management
Performance information provided to the Board could be improved	Boards should aim to maximise openness and accessibility of papers	Declarations of interests should be considered at every meeting	Boards should review the use of Committees and ensure delegation levels are appropriate

Source: Role of Boards Report (September 2010)

- 84.** As part of our work in 2016/17 we followed up on the issues highlighted by Audit Scotland. Our aim was to identify any causes for concern or areas of good practice. Our detailed findings will be shared with Audit Scotland and are summarised below.

### Arrangements for scrutiny and decision-making are appropriate

- 85.** We consider that arrangements for scrutiny and decision-making at the Board are appropriate.
- 86.** The Board has an induction programme for new non-executive members. This is tailored to the skills and experience of the new non-executive member.
- 87.** Non-executive members are encouraged to attend board and committee meetings of other NHS boards. Board development sessions are held throughout the year. Board members are encouraged to attend NHS-wide training sessions delivered by the Scottish Government.
- 88.** All Board members are subject to an annual appraisal by the Chair (for non-executive members and the Chief Executive) and the Chief Executive (for executive board members).
- 89.** The committees of the Board undertake an annual self-assessment of their performance and report this to the Board.
- 90.** Minutes of Board meetings are published on the Board's website. Declarations of interest are a standing item on the Board and committee meeting agendas.
- 91.** In forming our conclusions we have taken account of the 'effectiveness of committees' review performed by internal audit during the

year. Overall, internal audit concluded that *"governance arrangements are strong, and that the Board and its committees are effective"*.

- 92.** Internal audit noted that a number of improvements have been made by the Chief Executive as part of an on-going review of organisational structure and effectiveness. Internal audit made six recommendations (moderate to low risk) to enhance established practices. These recommendations focussed on:
- Content of the induction programme for new executive board members;
  - Record keeping of non-executive board member training and development;
  - Financial skills of board members;
  - Board approval of committee minutes;
  - Improved clarity of purpose in board agendas; and
  - Strategy development.

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# Value for money



# Value for money

93. 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 consideration of the Board's reported performance and to what extent this demonstrates continuous improvement.

## Overall conclusion

94. We found that the Board has appropriate performance management arrangements in place which support the achievement of value for money.

## Performance management framework

95. The Board has developed a performance management framework and receives reports on organisational performance and finance each quarter. An annual overview of performance is also prepared which is available on the Board's website. Performance reports are based on the Board's local delivery plan (LDP) and its associated targets and measures.

96. The performance and financial information presented to the Board comprises sufficient detail to facilitate scrutiny and challenge. From review of Board papers we found that members are actively scrutinising and challenging the position against targets.

## Performance against non-financial targets in 2016/17

97. The Local Delivery Plan (LDP) sets out the Board's performance expectations against targets. The Board identified 12 performance targets in 2016/17. Progress against these targets has been reported by the Board in its Annual Report and Accounts for the year ended 31 March 2017.

98. Six of the Board's 12 reported key performance measures were on target for 2016/17. In comparison to 2015/16, one key performance measure had improved, five were comparable and in six performance had declined.

99. Performance had declined for the following targets:

- Sickness absence: 8.35% (2015/16 8.03%)

- Review of patients' care and treatment plans at six monthly intervals: 91% (2015/16: 98%)
- Patients engaged in off-hub activity centres: 79.3% (2015/16 81%)
- Patients who had a healthier BMI: 13.6% (2015/16: 15%)
- Personal development plan review completions: 73% (2015/16 82.7%)
- Annual review of clinical risk assessment: 97% (2015/16: 97.3%).

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## Appendices

# Appendix 1: Action plan

Our action plan details the control weaknesses that we have identified during the course of our audit together with the officers responsible for implementing the recommendations and the implementation dates.

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

### Action plan grading structure

To assist the Board in assessing the significance of the issue raised and prioritising the action required to address it, the recommendation has been rated.

The grading structure for our recommendations is as follows;

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

Action plan point	Issue & Recommendation	Management Comments
1. Financial sustainability	<p>The Board's LDP covers a three year period, and is supported by a five year capital plan.</p> <p>In our view, all NHS boards should develop longer term financial plans on a 5 to 10 year basis. This would assist the Board in highlighting risks to the financial sustainability of its service model over the longer term, allocating resources to the services with highest demand and identifying opportunities for strategic service redesign.</p>	<p>A 5-10 year plan will be developed when preparing the 2018/19 LDP.</p> <p><b>Action owner:</b> Finance and Performance Management Director</p> <p><b>Due Date:</b> 31 March 2018</p>
Rating		
Grade 3		
Paragraph ref		
69		

# Appendix 2: Respective responsibilities of the Board and the Auditor

## Responsibility for the preparation of the annual report and accounts

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

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

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

Board members are also responsible for:

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

## Auditor responsibilities

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

- they give a true and fair view in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers of the state of the board's affairs as at 31 March 2017 and of its net expenditure for the year then ended;
- they have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2016/17 FRoM ;
- they have been prepared in accordance with the requirements of the National Health Service

(Scotland) Act 1978 and directions made thereunder by the Scottish Ministers;

- in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers;
- the auditable part of the Remuneration and Staff Report has been properly prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers; and
- the information given in the Performance Report for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers; and
- the information given in the Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the National Health Service (Scotland) Act 1978 and directions made thereunder by the Scottish Ministers.

We are also required to report by exception if, in our opinion

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

## Wider scope of audit

The special accountabilities that attach to the conduct of public business, and the use of public money, mean that public sector audits must be planned and undertaken from a wider perspective than in the private sector. This means providing assurance, not only on the financial statements, but providing audit

judgements and conclusions on the appropriateness, effectiveness and impact of corporate governance and performance management arrangements and financial sustainability.

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

### Independence

We are required by International Standards on Auditing to communicate on a timely basis all facts and matters that may have a bearing on our independence. We can confirm that we have complied with the Financial Reporting Council's Ethical Standards. In our professional judgement the audit process has been independent and our objectivity has not been compromised. In particular, there have been no relationships between Scott-Moncrieff and the Board or senior management that may reasonably be thought to bear on our objectivity and independence.

With regard to our appointment for a second term, we can confirm that we comply with Financial Reporting Council's Ethical Standard which notes that where applicable, once an engagement partner has held this role for a continuous period of ten years, careful consideration is given as to whether it is probable that an objective, reasonable and informed third party would conclude the integrity, objectivity or independence of the firm or covered persons are compromised. Therefore, the new appointment for a second five year term does not contradict the requirement of the FRC. This is in line with guidance from Audit Scotland which states that there is no expectation for the rotation of audit partners for special health board audits.



**Scott-Moncrieff**  
business advisers and accountants

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