Financial overview of the NHS in Scotland 2007/08

AUDIT SCOTLAND

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Auditor General for Scotland

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Note:
Prior to September 2007, the Scottish Administration was generally referred to as the Scottish Executive. It is now called the Scottish Government. When dealing with the earlier period, this report refers to the Scottish Executive. Recommendations for the future refer to the Scottish Government.

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Summary

The financial position of the NHS in Scotland was good in 2007/08 but it will face more challenging times in future years.

Introduction

1. This report provides an overview of the financial performance of the NHS in Scotland in 2007/08 and examines the financial challenges and risks for 2008/09 and beyond. The NHS in Scotland spent £10.1 billion in 2007/08, representing around a third of the total spend in the public sector. It remains Scotland's largest employer with over 155,000 people providing care in community, primary and acute settings throughout the country.[1]

2. Expenditure on the NHS in Scotland increased by 33 per cent in cash terms between 2003/04 and 2007/08, but over the next three years funding is only due to grow by 13 per cent. The Scottish Government has set NHS bodies a target of making two per cent cash efficiency savings annually over the same period. In this context, NHS bodies will find it more challenging to achieve their financial targets.

3. During 2007/08, the NHS continued to face a number of cost pressures, including the costs of implementing the UK-wide pay modernisation agenda; the increasing costs of drugs, fuel and energy; and the cost of introducing changes to the way boards deliver their services. In 2008/09 and beyond, NHS bodies will continue to face these and other cost pressures such as the cost of fully complying with the European Working Time Directive (EWTD) for junior doctors in training.

Our study

4. Our study is based largely on the audited accounts and auditors' reports on the 2007/08 audits of the 14 NHS boards, nine special health boards and the Scottish Government Health Directorates (SGHD).[2] These bodies collectively make up the NHS in Scotland.[3] We also used other sources of information to support our work, including:

- literature review
- national published statistics
- interviews with staff from the SGHD.

5. All NHS bodies submitted their audited accounts by the deadline of 30 June 2008. The majority of auditors reported that the audit process ran smoothly and that draft accounts and supporting schedules were of a good standard. Annual audit reports are available on Audit Scotland's website. The final financial positions in 2007/08 for the NHS boards and special boards are shown at Appendix 1 and forecast financial positions for 2008/09 at Appendix 2. For ease of reference, figures in the main body of the report have been rounded. We have tried to minimise the use of technical terms, but in some places this is unavoidable and we have therefore included a glossary at Appendix 3.

6. The financial performance of the NHS cannot be considered in isolation from its overall performance and service delivery, so this report should be considered alongside our 2007 overview report on the performance of the NHS.[4] Following our 2007 review, the SGHD made a commitment to publish an annual report on the NHS in Scotland, the first of which will cover 2007/08.

7. The rest of this report is organised into four parts:

- Part 1 reports on the financial performance of the NHS in Scotland in 2007/08.
- Part 2 provides details of the cost pressures the NHS in Scotland faced during 2007/08.
- Part 3 examines the NHS in Scotland's financial management and governance arrangements.
- Part 4 considers the future financial outlook for the NHS in Scotland in 2008/09 and beyond.

Summary of key messages

- The financial position of the NHS in Scotland in 2007/08 was good, with an overall underspend of £24 million against its revenue budget and £2 million against its capital budget. The revenue underspend makes up less than 0.3 per cent of the overall budget of the NHS in Scotland. The overall revenue underspend was made up of underspends of around £50 million by NHS boards and £26 million by special boards, balanced by a planned overspend of £50 million by the SGHD. Only NHS Western Isles failed to meet one of its financial targets.
- Most NHS bodies were less reliant on non-recurring funding to achieve their financial targets than they were last year. In total, the underlying recurring deficit for NHS bodies reduced from just over £92 million to around £16 million between 2006/07 and 2007/08.
- Pay modernisation continues to be a significant cost to the NHS and boards have faced particular problems with implementing Agenda for Change. The NHS in Scotland is still unable to quantify the potential costs of equal pay claims. Boards faced other cost pressures in 2007/08

1 This equates to over 130,000 whole-time equivalent staff.
2 Although the Mental Welfare Commission for Scotland is a commission constituted under the Mental Health (Care and Treatment) (Scotland) Act 2003, for the purposes of this report we have included financial information on its 2007/08 accounts with our coverage of special health boards.
3 We use the term 'NHS bodies' in this report to refer collectively to NHS boards and special health boards.
4 *Overview of Scotland's health and NHS performance 2006/07*, Audit Scotland, 2007.

such as rising drugs, fuel and energy costs; reducing waiting times; and service redesign.

- Most NHS bodies have generally sound governance arrangements in place, but some issues arose in relation to senior staff appointments and associated governance arrangements at five NHS bodies. NHS Orkney and NHS Western Isles need to address governance and financial management issues raised by their auditors.

- During 2008/09 and beyond, NHS bodies will continue to face similar cost pressures as in 2007/08 as well as having to deal with other issues, such as the cost of achieving full compliance with the European Working Time Directive. NHS bodies will also face new challenges in meeting their financial targets such as the impact of lower growth in funding allocations.

Part 1. Financial performance in 2007/08

NHS bodies met their financial targets in 2007/08, except NHS Western Isles which failed to meet one of its targets.

Key messages

- The financial position of the NHS in Scotland in 2007/08 was good, with an overall underspend of £24 million against its revenue budget and £2 million against its capital budget. The revenue underspend makes up less than 0.3 per cent of the overall budget of the NHS in Scotland. The overall revenue underspend was made up of underspends of around £50 million by NHS boards and £26 million by special boards, balanced by a planned overspend of £50 million by the SGHD. Only NHS Western Isles failed to meet one of its financial targets.
- Most NHS bodies were less reliant on non-recurring funding to achieve their financial targets. In total, the underlying recurring deficit for NHS bodies reduced from just over £92 million to around £16 million between 2006/07 and 2007/08.
- Capital expenditure has grown from £132.5 million in 2003/04 to £428.8 million in 2007/08 and the trend is expected to continue. By 2010/11, the capital allocation to NHS bodies will reach £598 million.
- Scotland's expenditure on health per head of population remains higher than the rest of the UK. There is no evidence available to show changes in the balance of expenditure on health, despite the policy to shift the balance of care closer to home.
- The NHS in Scotland reported that it achieved its overall Efficient Government savings targets for the three years to 2007/08. The target relating to sickness absence was not met and rates remain high in NHS boards. NHS bodies made efficiency savings that allowed them to meet Efficient Government targets and, in most cases, to break even.

The financial position of the NHS in Scotland was good in 2007/08

8. NHS bodies have three financial targets. These are to stay within their:

- revenue resource limit (RRL) – this is the revenue budget allocated for the day-to-day operation of services
- capital resource limit (CRL) – the funding that a health body has available for capital programmes
- cash requirement – this is the amount of cash drawn down by NHS bodies to fund ongoing operational costs and new capital investment.

9. All NHS bodies met their financial targets for 2007/08 except NHS Western Isles, which failed to meet its RRL target. However, for the first time in five years, the board generated an in-year surplus to set against its cumulative deficit. None of the NHS bodies' accounts had a qualified audit opinion. However, the auditor of NHS Western Isles included an explanatory paragraph relating to the overspend against its RRL.

10. Some NHS boards used capital grants in 2007/08. Capital grants allow NHS boards to provide money to other public sector bodies for buying or improving fixed assets for the benefit of a health board's residents. The criteria for making a capital grant are that the funding should be for specific purposes that meet the definition of capital expenditure and contribute towards the achievement of the board's objectives. These payments count against a board's capital resource limit rather than its RRL, allowing it to fund fixed assets while any associated revenue costs are paid for by the other organisation. Lothian (£13 million), Tayside (£6.7 million), Greater Glasgow and Clyde (£5 million) and Orkney (£1.9 million) all used capital grants during 2007/08.

11. The NHS in Scotland spent £10.1 billion in 2007/08, an increase of £696 million from the previous year. Overall, the NHS in Scotland underspent against its total budget by £26 million. This was made up of a revenue underspend of £24 million and a capital underspend of £2 million (Exhibit 1). The revenue underspend

Exhibit 1

Overall NHS financial position, including the Scottish Government Health Directorates, 2006/07 and 2007/08

The NHS in Scotland spent a total of £10.1 billion in 2007/08. This resulted in an underspend of £26 million against its overall budget.

NHS in Scotland outturn	2006/07 (£ million)	2007/08 (£ million)
Revenue budget	9,109	9,726
Capital budget	391	398
Total budget	**9,500**	**10,124**
Revenue expenditure	9,078	9,702
Capital expenditure	324	396
Total expenditure	**9,402**	**10,098**
Revenue underspend/overspend (-)	31	24
Capital underspend/overspend (-)	67	2
Total	**98**	**26**

Source: Audit Scotland

Exhibit 2

Summary of NHS bodies' performance against their revenue resource limit target for 2007/08

NHS bodies underspent their revenue budgets by £76 million during 2007/08.

	RRL (£ million)	Expenditure (£ million)	2007/08 underspend (£ million)	2006/07 underspend (£ million)
NHS boards	7,900	7,850	50	89
Special boards	1,151	1,125	26	24
Total	9,051	8,975	76	113

Note: Figures are rounded to nearest million.
Source: NHS bodies' annual accounts

makes up less than 0.3 per cent of the overall budget of the NHS in Scotland.

12. The revenue underspend consisted of underspends of around £50 million by NHS boards and £26 million by special boards, balanced by a planned £50 million overspend by the SGHD. The combined underspend of £76 million by NHS boards and special boards against their RRL is lower than the £113 million underspend in 2006/07 (Exhibit 2).

13. Seven NHS boards and six special boards underspent by one per cent or more against their RRL in 2007/08. One of the reasons for these underspends was the inability of NHS bodies to fully use additional funding provided by the SGHD during the year, on top of the allocations given to them at the beginning of the year. Some of this additional funding is earmarked for specific policies and NHS bodies are expected to meet any relevant performance targets. Four NHS boards and one special board reported difficulty spending additional funding provided during the year.[5] In contrast, NHS Orkney relied on an agreement with Orkney Islands Council not to pay a £1.3 million resource transfer in 2007/08 and late funding allocations from the SGHD relating to exceptional cost pressures, in order to meet its RRL.

14. Other reasons for NHS bodies underspending against their RRLs were unfilled staff vacancies and revenue and capital projects that progressed more slowly than expected. NHS Education for Scotland had a significant underspend on its dental action plan and £5 million of this has been returned to the Scottish Government. The National Waiting Times Centre Board had an underspend of around 11 per cent of its RRL which related mainly to delays in the transfer of the heart and lung service from NHS Greater Glasgow and Clyde and NHS Lanarkshire.

NHS bodies were less reliant on non-recurring funding

15. Much of the funding that NHS bodies receive from the SGHD can be classified as recurring income, ie it is funding they receive each year to meet their recurring expenditure, or ongoing running costs. NHS bodies also receive non-recurring, or one-off, funding during the year and will make one-off payments during the year. A sign of good financial health for an NHS body is when its recurring expenditure does not exceed its recurring income. This is known as the NHS body's underlying recurring position. We have commented in previous overview reports that NHS bodies rely on non-recurring funding to achieve financial targets or support their financial position.

16. Non-recurring funding is a normal part of running the NHS in Scotland but it should not be used to sustain day-to-day activities in the long term. Non-recurring funding can include support from the SGHD, such as an additional RRL allocation. Previously NHS bodies also used the proceeds from the sale of assets as a non-recurring source of funding. However, from 2007/08 they were only able to use these proceeds for capital purposes.

17. In 2007/08, most boards were less reliant on non-recurring funding to support their financial position. In total, the underlying recurring deficit for NHS bodies reduced from just over £92 million in 2006/07 to £16.4 million in 2007/08. NHS boards reduced their underlying recurring deficit from £103 million in 2006/07 to almost £35 million in 2007/08. NHS Grampian, NHS Greater Glasgow and Clyde, and NHS Lothian made significant reductions in their underlying recurring deficits and NHS Lanarkshire eliminated its deficit. Special boards made a total underlying recurring surplus of almost £19 million (Exhibit 3, overleaf). We comment on the forecast positions of NHS bodies for 2008/09 in Part 4 of this report.

5 NHS Dumfries and Galloway, NHS Fife, NHS Grampian, NHS Shetland and NHS Health Scotland.

Exhibit 3

NHS bodies recurring deficit/surplus, actual 2007/08, and forecast 2008/09

The three island boards and NHS Highland have the biggest underlying recurring deficits as a percentage of their recurring income.

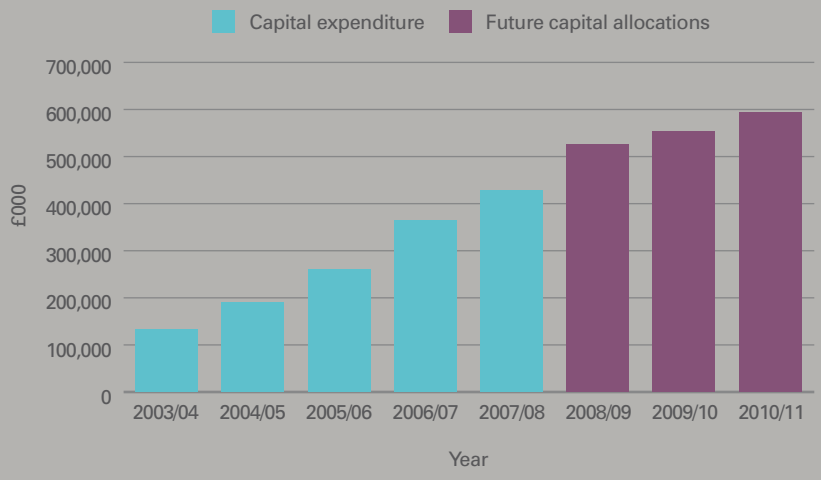
	2007/08 actual		2008/09 forecast	
	Underlying recurring surplus/ deficit ( ) £ million	as a % of recurring income	Underlying recurring surplus/ deficit ( ) £ million	as a % of recurring income
NHS Ayrshire and Arran	1.4	0.2	0	0
NHS Borders	0.9	0.5	-0.9	-0.5
NHS Dumfries and Galloway	2.0	0.8	0.8	0.3
NHS Fife	2.5	0.5	0.2	0
NHS Forth Valley	0	0	0	0
NHS Grampian	-6.1	-0.7	-6.2	-0.7
NHS Greater Glasgow and Clyde	-19.0	-0.7	-0.6	0
NHS Highland	-10.6	-1.9	-8.0	-1.4
NHS Lanarkshire	5.3	0.7	3.7	0.5
NHS Lothian	-5.0	-0.5	0	0
NHS Orkney	-1.0	-2.7	-2.5	-6.7
NHS Shetland	-1.2	-3.5	-1.9	-5.3
NHS Tayside	-1.6	-0.2	0	0
NHS Western Isles	-2.5	-4.7	-1.1	-1.9
Total for NHS boards	**-34.9**	**-0.4**	**-16.5**	**-0.2**
Mental Welfare Commision for Scotland	0.1	2.5	0	0
NHS 24	-0.2	-0.4	0	0
NHS Education for Scotland	7.7	2.1	8.7	2.2
NHS Health Scotland	0	0	0	0
NHS National Services Scotland	9.0	3.8	5.3	2.1
NHS Quality Improvement Scotland	0.1	0.9	0.1	0.6
Scottish Ambulance Service Board	0	0	1.2	0.6
State Hospitals Board for Scotland	0.8	2.2	0.3	0.7
The National Waiting Times Centre Board	1.0	1.5	-2.3	-2.3
Total for special boards	**18.5**	**1.9**	**13.3**	**1.3**
Total for all NHS bodies	**-16.4**	**-0.2**	**-3.2**	**0**

Source: NHS Annual Accounts and unaudited returns from NHS bodies, July 2008

Exhibit 4

Gross capital expenditure and future capital allocations, 2003/04–2010/11

Capital expenditure has increased significantly since 2003/04 and will continue to rise.



Note: This expenditure excludes capital projects funded through Private Finance Initiatives or Public Private Partnerships.
Source: Unified board summaries, Scottish Government

NHS capital expenditure has continued to grow

18. NHS bodies spent £428.8 million on capital during 2007/08. This represents a total underspend of £1.8 million against their total CRL target of £430.6 million.

19. Since 2003/04, capital expenditure has more than trebled in cash terms from £132.5 million to £428.8 million. The Scottish Government has budgeted for further increases in the next three years so that the capital allocation will rise to £598 million by 2010/11 (Exhibit 4).

20. In May 2008, Audit Scotland published a report on major capital projects in the public sector which reported that 11 health and community care major capital projects were completed between 2002 and 2007, costing £258 million.[6,7] A further 28 major capital projects are in progress and are expected to cost £737 million. The report recommended that public bodies carry out post-project evaluations to determine whether projects have delivered the benefits intended.

21. Some of the major capital projects in 2007/08 included:

- a new acute hospital at Larbert (funded through a Private Finance Initiative (PFI)). NHS Forth Valley will have double running costs while it continues providing services from Falkirk and District Royal Infirmary and Stirling Royal Infirmary until the new hospital is fully functional.
- new ambulatory care services at Stobhill and Victoria hospitals (funded through PFIs). NHS Greater Glasgow and Clyde expects both projects to be completed in 2009/10.
- the redevelopment of the State Hospital.

The Scottish Government allocated additional funding of £270 million towards specific workstreams in 2007/08

22. The Scottish Government allocated additional funding of around £270 million to NHS and other public sector bodies towards specific national health-related workstreams in 2007/08 (Exhibit 5, overleaf).[8] This additional funding is provided to support NHS bodies and their partners in implementing local delivery plans and achieving their HEAT targets. For example, the SGHD allocated £44 million to NHS boards for coronary heart disease and delayed discharges to help them achieve their targets in these areas. HEAT targets are the national performance indicators for the NHS in Scotland.

23. NHS bodies monitor and report on the progress of these workstreams through their local delivery plans, but they are not required to report separately on the use of this additional funding. These plans set out how NHS bodies intend to meet the HEAT targets and any other local targets they have in place and these are reported to the Scottish Government as part of the national performance framework for the NHS.

Scotland continues to spend more on health per head of population than the rest of the UK

24. Scotland continues to spend more on health per head of population than other UK countries (Exhibit 6, page 11). In 2007/08, Scotland was forecast to spend £1,919 per head of population, compared to £1,758 in Wales, £1,676 in England and £1,770 in Northern Ireland. In 2006, the Scottish Executive identified the main reasons for higher spending in Scotland as the added costs of being a sparsely populated area and higher death rates from circulatory diseases and cancer.[9] From 2008/09, the gap is projected to narrow.

There is no evidence of a change in the balance of health expenditure to match the move towards more community-based care

25. Shifting the balance of care is a term used to describe change at a number of levels, for example, moving the location of care towards more community-based

6 *Review of major capital projects – How government works*, Audit Scotland, 2008.
7 Major capital projects are defined as any project costing more than £5 million or more than £10 million for NHS Greater Glasgow and Clyde and NHS Lothian.
8 Scottish Government draft budget 2007/08.
9 *Government expenditure and revenue in Scotland 2004–2005*, Scottish Executive, 2006.

Exhibit 5
Additional funding allocated towards national workstreams in 2007/08

An additional £270 million was allocated towards national workstreams in 2007/08

National workstreams	£m
Health improvement[10]	110
Other health services[11]	45
Delayed discharge	29
Centre for change and innovation[12]	24
Community care services[13]	19
Coronary heart disease/stroke	15
Mental health specific grant[14]	14
Audiology services modernisation	6
Clean hospitals	5
Joint Improvement Team	1
Diabetes	1
Autism	1
Total	270

Note: Figures are rounded to nearest million.
Source: Scottish Government budget extract, 2007/08

facilities; shifting the focus of care towards long-term conditions; and changing the roles and responsibilities of patients and professionals. There has been a commitment to shifting the balance of care since the Kerr report in 2005.[15]

26. We would expect the balance of expenditure to change between acute, primary and community care sectors to support the shift in the balance of care. However, *Scottish Health Service Costs* show that there was no change in the split of expenditure between the hospital, community and family health/GP sectors between 2004/05 and 2006/07.[16] The split of expenditure in 2006/07 was:

- hospital sector – 60 per cent
- community sector – 13 per cent
- family health/GP sector – 27 per cent.

27. The hospital sector includes community hospitals but we would, nevertheless, expect to see some change in the balance of the resources going into the community and family health/GP sectors. The SGHD needs to be able to demonstrate that resources are following the shift in the balance of care.

The Scottish Government has reported that it met its Efficient Government savings targets

28. The Scottish Executive launched its Efficient Government Initiative, *Building a Better Scotland*, in June 2004. This set the NHS in Scotland a three-year overall savings target of around £534 million by 2007/08. The SGHD reported that the NHS in Scotland achieved total efficiency savings of around £610 million for the three years to 2007/08 (Exhibit 7, page 11).

29. For some of the individual savings initiatives, there have either been significant developments during 2007/08 or Audit Scotland has made comment on them, including:

- NHS efficiency savings
- sickness absence
- shared services
- increasing consultant productivity.

NHS efficiency savings

30. Under the Efficient Government Initiative, the Scottish Government set NHS bodies a cumulative efficiency savings target of £208 million between 2005/06 and 2007/08, based on one per cent of their revenue budget over this period. The SGHD reported that NHS bodies met this target, achieving total savings of £231 million over the three years.

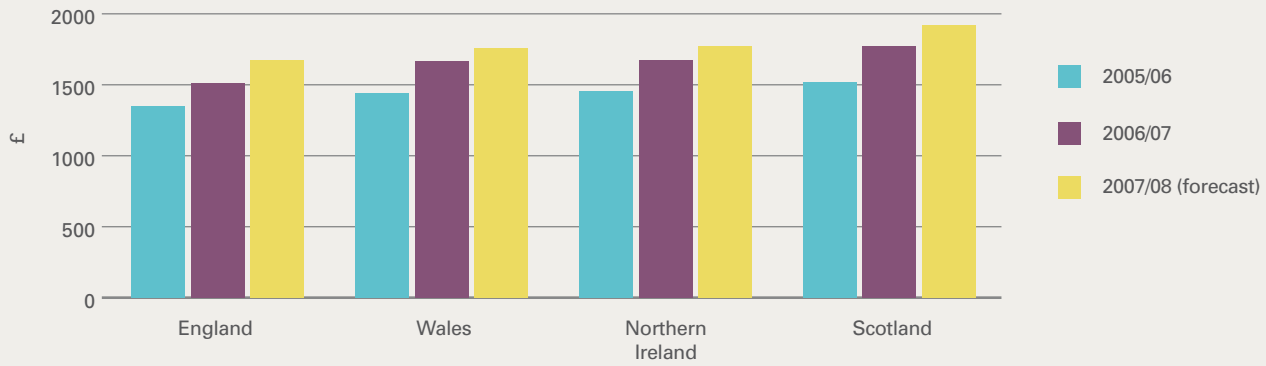
31. NHS bodies produce annual savings plans which set savings targets to meet both their Efficient

10 This funding included: allocations of £29 million for the health improvement strategy; £14 million for tobacco control; £12 million for alcohol misuse; £34 million for public health and workplace health; £6 million for mental well-being and £15 million for welfare foods.
11 This includes funding to boards for community and voluntary sector initiatives.
12 The Centre for Innovation and Change is now known as the Improvement and Support Team (IST). The IST and its predecessor run national improvement programmes that engage with every NHS board.
13 This includes funding to boards for community and voluntary sector initiatives.
14 This includes funding to boards for community and voluntary sector initiatives.
15 *Building a health service fit for the future – A national framework for service change in the NHS in Scotland,* Scottish Executive, May 2005. Also known as the Kerr Report.
16 *Scottish Health Service Costs,* Information Services Division, NHS National Services Scotland.

Exhibit 6

UK expenditure per head of population 2005/06–2007/08

Scotland continues to spend relatively more on health than the rest of the UK.



Source: Public Expenditure Statistical Analyses 2008, HM Treasury

Exhibit 7

Summary of NHS efficient government savings targets and reported performance between 2005/06 and 2007/08

The NHS in Scotland achieved savings of £610 million against its overall target of £534 million.

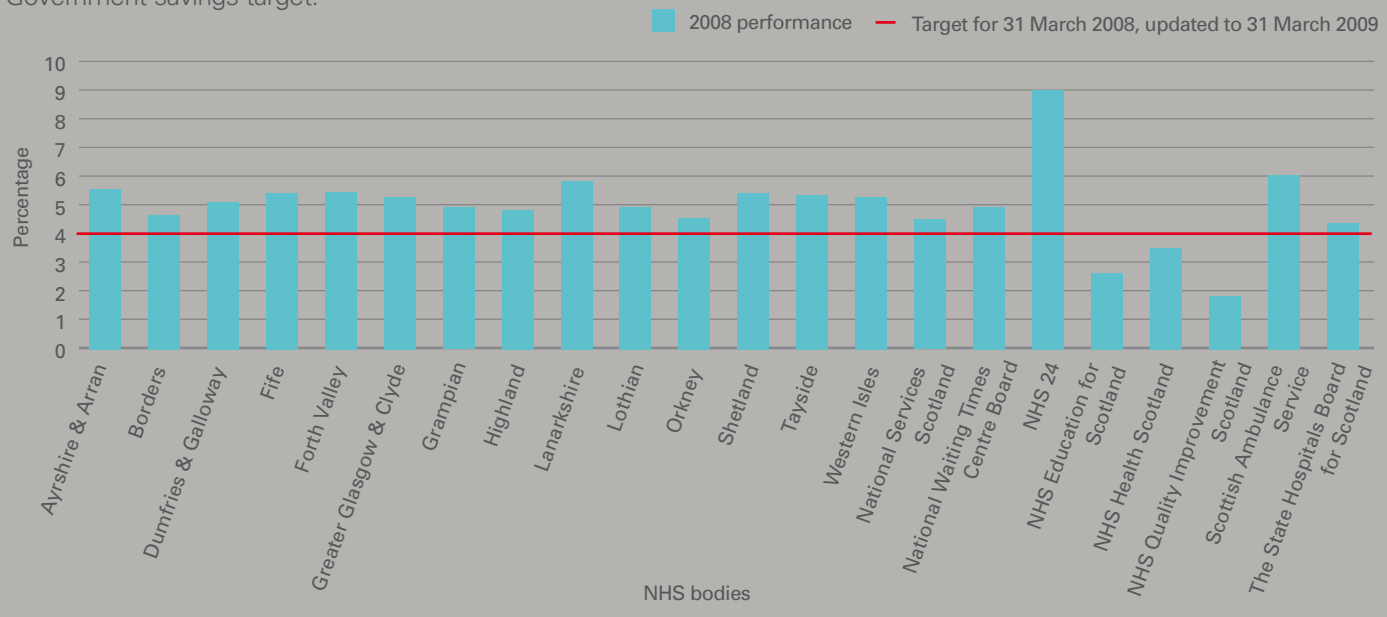
Savings initiative	Target (£ million)	Actual (£ million)
NHS efficiency savings	208	231
Increasing consultant productivity	73	73
NHS procurement	63	73
Reduction in absence	55	42
Drug purchasing	42	74
Digital X-rays/Picture Archiving and Communication System	24	9
Improved prescribing	20	80
Electronic transmission of laboratory results to GPs	12	0
NHS support services reform	10	3
NHS logistics	10	8
Scottish primary care collaborative	7	7
Patient-focused booking	3	1
Countering NHS fraud	3	3
Care Commission efficiency savings	2	3
Specialty redesign projects	1	3
Facilities management systems	1	0
Total savings	**534**	**610**

Source: Scottish Government

Exhibit 8

NHS bodies' sickness absence rates as at 31 March 2008

Only NHS Education for Scotland, NHS Quality Improvement Scotland and NHS Health Scotland met the Efficient Government savings target.



Source: NHS Workforce Statistics, ISD Scotland, June 2008

Government efficiency savings target and to ensure that they break even. In 2007/08, NHS bodies achieved total savings of £145 million against an overall target of £118 million.

32. Savings targets consist of recurring and non-recurring savings. Recurring savings are when permanent changes are made to reduce the cost base such as redesigning a service to make it more efficient. Non-recurring savings are one-off savings that only apply to that financial year, for example, delaying the filling of vacant posts where there is an intention to fill those posts. Recurring savings made by NHS bodies increased from £87 million in 2006/07 to £106 million in 2007/08.

Sickness absence savings targets

33. The Efficient Government sickness absence savings target of £54.8 million was based on NHS bodies reducing their sickness absence levels to four per cent or below by March 2008. This target was not achieved. The target has been extended to March 2009.

34. Sickness absence rates at 31 March 2008 for all NHS bodies were 5.28 per cent compared to 5.55 per cent in the previous year. NHS 24 continued to have the highest rate at 9.06 per cent and only three special boards, NHS Education for Scotland, NHS Quality Improvement Scotland and NHS Health Scotland, reported rates below four per cent (Exhibit 8).

Shared services

35. NHS National Services Scotland (NHS NSS) continues to lead the shared services programme for finance on behalf of the NHS in Scotland. The programme aims to make recurring savings by providing the NHS in Scotland with a single shared service for day-to-day financial transactions, for example, the processing of invoices.

36. The shared services programme has not made the progress anticipated when it was launched so pilot projects were started in 2007/08 to move the programme forward. All NHS bodies will move to a common finance system and 15 bodies have completed this process so far. Other pilots have been taking place to develop shared finance support services. We will continue to review progress in our NHS performance overview report in 2009.

Increasing consultant productivity through improved rates of day surgery

37. As part of the Efficient Government Initiative, the Scottish Government aims to achieve a one per cent improvement in consultant-led productivity. Improving the rate of day surgery is expected to contribute to this target. In September 2008, Audit Scotland reported on progress against day surgery targets.[17] We found that the percentage of surgery undertaken as same-day care continues to rise but that the percentage of surgical procedures carried out as day surgery varies considerably among NHS boards. There is also considerable variation within NHS boards in the performance of different procedures.

17 *Day surgery in Scotland – reviewing progress*, Audit Scotland, 2008.

Part 2. Cost pressures and other financial risks facing the NHS in Scotland in 2007/08

Pay modernisation continues to be a significant cost to the NHS and boards continue to face pressures due to increases in the costs of drugs, fuel and energy.

Key messages

- Pay modernisation continues to be a significant cost to the NHS and boards have faced particular problems with implementing Agenda for Change. The NHS in Scotland is still unable to quantify the potential costs of equal pay claims.
- Boards faced other cost pressures in 2007/08 such as rising drugs, fuel and energy costs; reducing waiting times; and service redesign. Clinical negligence compensation costs increased during the year by £14 million.

Pay modernisation continues to be a significant cost to the NHS

38. Most boards continue to cite pay modernisation as a significant cost pressure. Pay modernisation includes three UK-wide pay contracts – the consultant contract, the new General Medical Services (nGMS) contract and Agenda for Change. Cost pressures arising from these include the need to make provisions for appeals and reviews, and incremental pay claims in relation to Agenda for Change.

39. Audit Scotland published reports on the consultant contract and the nGMS contract in 2006 and 2008 respectively.[18] Both reports found that the costs of implementing these contracts were significantly more than expected and that allocations were insufficient to meet all of the additional costs. The consultant contract report estimated the cumulative additional cost of implementing the contract between 2004/05 and 2006/07 to be around £235 million, increasing to £273 million when inflation and on-costs are included. The nGMS report found that between 2004/05 and 2006/07, NHS boards spent £160.4 million more on general medical services than the specific funding allocated by the then Scottish Executive Health Department.

Agenda for Change is still being implemented

40. Agenda for Change introduces a new pay system and standard terms and conditions for all NHS staff, with the exception of doctors, dentists and most senior managers. NHS bodies have faced particular problems implementing Agenda for Change, such as agreeing job profiles for specialist staff and the high level of review requests in some NHS bodies. The full cost will not be known until the process is complete, although the Scottish Government estimates the additional costs to be £634 million to the end of 2007/08.[19] The target was for full assimilation of all staff into the new pay scales by 31 March 2008 – 93 per cent of staff were assimilated at that date.[20,21] Only four NHS bodies (NHS Orkney, Scottish Ambulance Service, the National Waiting Times Centre Board and NHS Health Scotland) had completed the Agenda for Change assimilation process for all staff. The Scottish Government has estimated that full implementation, including payment of arrears, will be complete by 31 December 2008.[22]

41. By 30 April 2008, 39,745 staff had lodged review requests, with 13,723 so far being accepted and put forward to the formal review process.[23] By June 2008, NHS Orkney was the only board that had completed the review process. Fifty per cent of staff at NHS NSS have requested reviews and more than 80 per cent of those completed have had their pay band adjusted as a result.

42. NHS bodies accrued £210 million in their 2007/08 accounts for back pay and the estimated cost of successful reviews. This includes £191 million by NHS boards and £19 million by special boards.

The NHS in Scotland is still unable to quantify the potential costs of equal pay claims

43. There have been approximately 12,000 equal pay claims raised in Scotland against NHS bodies. There is a gender pay gap in the percentage difference between the median hourly earnings of men and women and the UK Government has introduced legislation to try to eradicate this. Progress with equal pay claims in the NHS in Scotland is not sufficiently advanced to determine the likelihood of their success or failure or to estimate their value. Our 2007 NHS performance overview report raised this as an important issue for the NHS in Scotland. Since then, uncertainty in this area has increased as some recent claims include a challenge to the Agenda for Change system, stating that it perpetuates discrimination rather than resolving it. This allegation has yet to be legally tested. The Equal Pay Unit and the Central Legal Office (CLO), based in NHS National Services Scotland, are still working to resolve this issue.

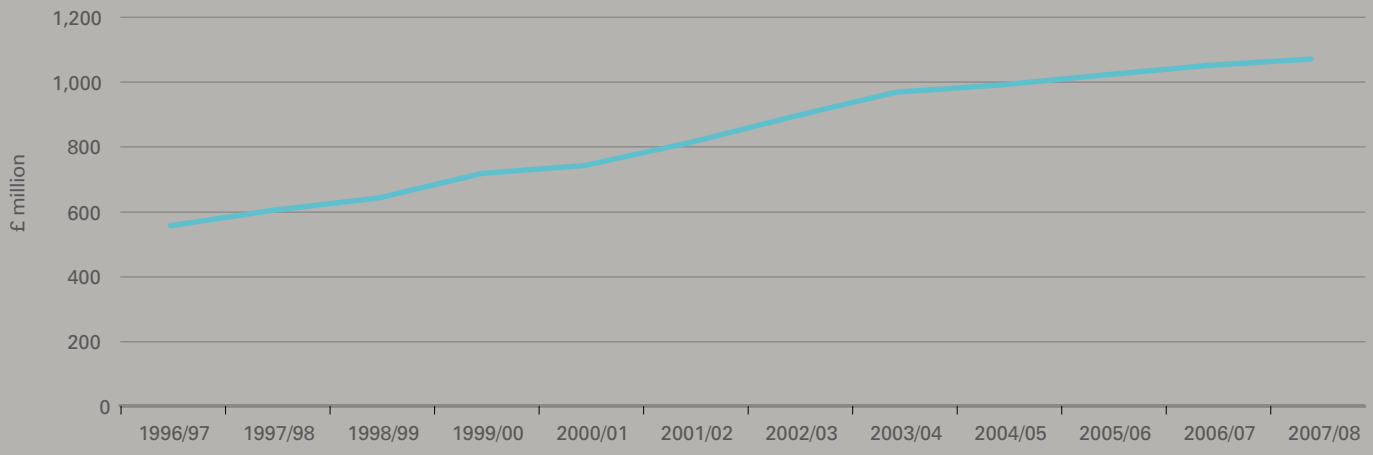
44. This is also an issue for councils, but they have been more successful in estimating the potential value of equal pay claims. In their 2006/07 accounts, councils valued these claims at £233 million, of which around half represents amounts set aside for future payments and outstanding claims. Equal pay claims may represent a considerable cost to the NHS, when they are quantified.

18 *Implementing the NHS consultant contract in Scotland,* Audit Scotland, 2006*; Review of the new General Medical Services contract*, Audit Scotland, 2008.
19 Answer to parliamentary question S3W – 15955.
20 Assimilation means the process of job evaluation and matching staff to their new grade on the Agenda for Change pay scales.
21 ISD workforce newsletter, June 2008.
22 Answer to parliamentary question S3W – 14160.
23 Answer to parliamentary question S3W – 14157.

Exhibit 9

Prescribing costs 1996/97–2007/08

Increases in prescribing costs have begun to level off over the last three years.



Note: These costs exclude drugs dispensed in hospitals.
Source: Prescribing/Dispensing Costs, ISD Scotland, September 2008

NHS bodies continue to face other cost pressures

45. In addition to the costs of implementing the UK-wide pay modernisation agenda, most NHS boards continue to identify similar cost pressures as in 2006/07, such as the increasing costs of drugs, fuel and energy; and the cost of introducing changes to the way boards deliver their services.

46. Between 1996/97 and 2007/08, drugs prescribing costs rose in cash terms by around 93 per cent to just over £1 billion. However, annual increases over the last three years were three per cent in 2005/06 and 2007/07, and two per cent in 2007/08. While drug costs remain a cost pressure, the rate of increase reduced in 2007/08 (Exhibit 9). New medicines and technologies continue to be introduced, making it difficult for boards to forecast expenditure.

47. Audit Scotland will publish a follow-up review of its 2005 baseline report on managing medicines in hospital in 2009.[24]

48. The additional costs of meeting waiting times targets continue to be a cost pressure to the NHS. The Audit Scotland report on diagnostic services found that the Scottish Government allocated an additional £50 million to NHS boards to improve patients' access to diagnostic tests. Boards used this funding to clear the backlog in waiting lists and make longer-term changes to how they manage services.[25] New, more challenging targets have been introduced from 2008/09 under *Better Health, Better Care*.[26]

49. Boards also identified local cost pressures. For example, NHS Western Isles and NHS Orkney identified locum costs as a cost pressure and NHS Western Isles overspent its medical staff budget, including locums, by £765,000.

50. Total energy costs increased by 34 per cent in real terms over the last year to September 2008.[27,28,29] Due to the rising fuel costs, the Scottish Ambulance Service overspent its fuel budget by £400,000 (eight per cent of its fuel budget).

Clinical negligence compensation costs increased by £14 million between 2006/07 and 2007/08

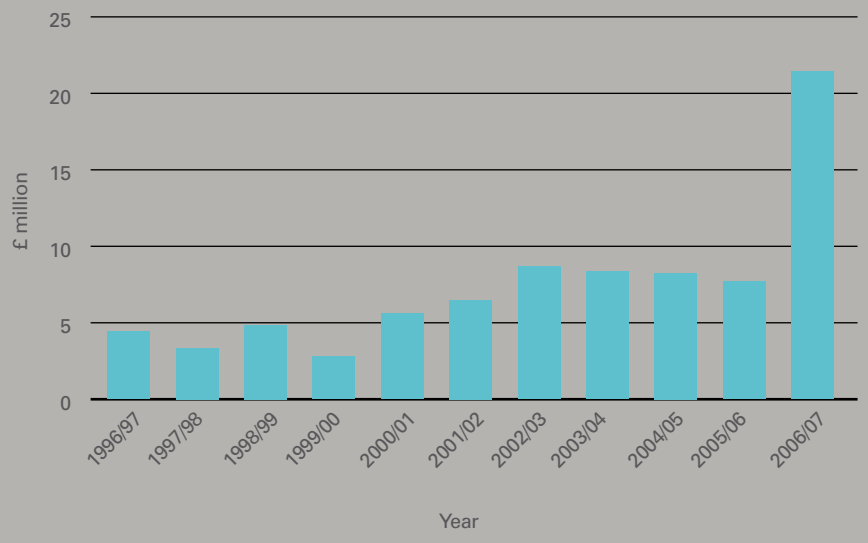
51. The total amount paid out for clinical negligence claims has increased significantly since 2000/01 and there was a £13.7 million increase

24 *A Scottish prescription – Managing the use of medicines in Scotland hospitals,* Audit Scotland, 2005.
25 *Review of NHS diagnostic services,* Audit Scotland, 2008.
26 *Better Health, Better Care,* Scottish Government, 2007.
27 *Quarterly energy prices, national statistics,* Department for Business, Enterprise and Regulatory Reform, September 2008.
28 Total energy costs include coal, heavy fuel oil, gas and electricity.
29 Fuel costs have increased over the last year to September 2008 – diesel prices by 27.8 pence per litre and petrol by 18.1 per cent per litre.

Exhibit 10

Cost of settlement of clinical negligence claims 1996/97–2006/07

The amounts actually paid out to settle negligence claims increased significantly in 2006/07.

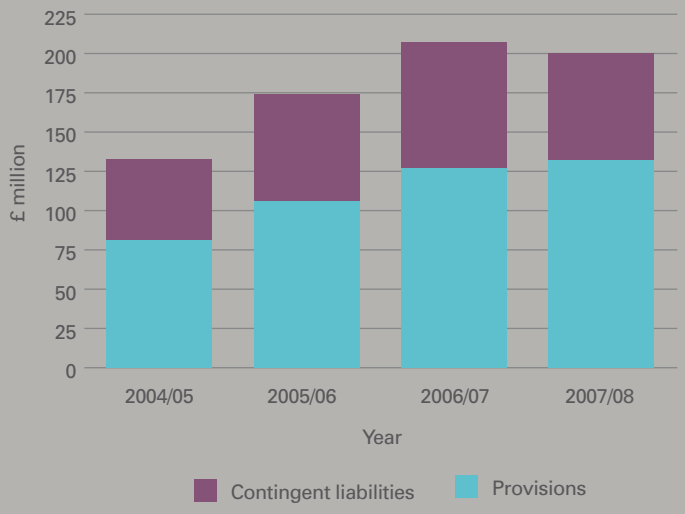


Source: Answer to parliamentary question S3W – 11099

Exhibit 11

Provisions and contingent liabilities for clinical and medical negligence

The amounts included in the accounts for clinical medical negligence claims decreased in 2007/08.



Source: Unified Board Summaries, Scottish Government

between 2005/06 and 2006/07 (Exhibit 10). This increase is partly due to the settlement of a small number of birth-related cases in 2006/07, totalling £6 million.

52. NHS bodies include provisions and contingent liabilities in their accounts for clinical and medical negligence claims. Provisions are the money NHS bodies have set aside in their accounts to cover their estimated settlement of claims raised against them. Contingent liabilities are a statement in the accounts about the potential settlement of existing and potential future claims. These may or may not include an estimate of the costs dependent on whether these can be accurately calculated. The CLO estimates the likelihood of success for clinical negligence claims. NHS bodies then use these estimates to decide whether to account for claims as a provision or a contingent liability.

53. Despite the increase in compensation costs, there has been little change in the provisions and contingent liabilities in NHS bodies' accounts for clinical and medical negligence between 2006/07 and 2007/08 (Exhibit 11). This is because the Scottish Government operates an insurance scheme which covers most of the value of claims that NHS bodies are expected to award for successful claims. Therefore, NHS bodies are not significantly affected by fluctuations in pay-outs as they would have provided money for such claims in previous years.

Part 3. Governance and financial management

Most NHS bodies have generally sound governance arrangements but some issues arose in relation to senior staff appointments and associated governance arrangements at five boards.

Key messages

- Most NHS bodies have generally sound governance arrangements in place but some issues arose in relation to senior staff appointments and associated governance arrangements at five NHS bodies.
- NHS Orkney and NHS Western Isles need to address governance and financial management issues raised by their auditors.
- Some NHS boards are reviewing or restructuring their CHPs. Although CHPs have been in place from 2005, there has been no national evaluation of whether they are efficient and effective in planning and delivering health improvements within their local communities. The Scottish Government announced its plans to carry out a study of CHPs at the end of this year.

Most NHS bodies had generally sound governance arrangements in place

54. Auditors reported no major issues in relation to the governance arrangements at the majority of boards during 2007/08. However, the auditors of five NHS bodies reported concerns around the appointment of, and governance arrangements for, senior staff (Exhibit 12).

55. In July 2008, the auditor of the Mental Health Tribunal for Scotland Administration (MHTSA) reported that the organisation had made significant progress in addressing governance issues raised in a Section 22 report by the Auditor General on the 2006/07 accounts.[31] This included the creation of a board with independent members from March 2008. However, the auditor also recommended that the organisation needs to take further steps to strengthen its financial management arrangements.

Exhibit 12

Summary of audit issues identified in relation to senior staff appointments and governance arrangements

Board	Key issues
NHS 24	NHS 24 completed a reorganisation of its senior management structure during 2007/08 in an attempt to reduce its running costs. The reorganisation has cost the organisation £1 million in compromise agreements and redundancies for staff over the last two years.[30]
NHS National Services Scotland	The board continues to have difficulty recruiting and retaining senior and specialist staff in key posts across the organisation. This is partly the result of the outcomes of the Agenda for Change process and changes to senior manager pay structures.
NHS Orkney	The medical director resigned from the board in May 2007 and by 31 March 2008, NHS Orkney had yet to fill the post on a permanent basis. The board has also been without a permanent finance director since September 2006 when the post-holder was appointed as chief executive. A secondee from NHS Lanarkshire has filled this post on an interim basis since October 2006. The secondment terms mean that the board has had to cover travel and accommodation costs, as well as salary and employers' contributions.
NHS Western Isles	The board has experienced considerable difficulties in recruiting a permanent chief executive. Including interim and acting roles, the board has had five chief executives in the last three years.
Scottish Ambulance Service	The chief executive was appointed in November 2007, but in May 2008, both the chief executive and operations director took voluntary leave of absence pending the outcome of an investigation into claims that they were involved in bullying and harassment. On 14 November, during the process of the investigation, both staff resigned from their posts.

Source: Board annual audit reports for 2007/08

NHS Orkney and NHS Western Isles need to address governance and financial management issues

56. The auditors of NHS Orkney and NHS Western Isles identified that these boards need to improve their

30 Compromise agreements are legally binding agreements following the termination of employment. They usually provide for a severance payment by the employer, in return for which the ex-employee cannot pursue any claim they have to an employment tribunal.

31 The Mental Health Tribunal for Scotland Administration provides administration and support for the judicial work of the Tribunal. It is an executive agency of the Scottish Government and was created under the Mental Health (Care and Treatment) (Scotland) Act 2003.

financial management and governance arrangements. NHS Western Isles failed to meet its RRL target and NHS Orkney only met its target due to an agreement with the council not to pay a £1.3 million resource transfer in 2007/08 and additional late funding allocations from the SGHD relating to exceptional cost pressures. Both boards have experienced difficulties with governance arrangements (Case studies 1 and 2).

57. The Auditor General prepared a Section 22 report on NHS Western Isles in 2006/07.[32] The Scottish Parliament Audit Committee then held an inquiry and published its report in May 2008. The key findings and outcome of the inquiry are summarised in Case study 2.

Boards need to manage their major capital projects better

58. Audit Scotland's 2008 report on major capital projects found that in appraising projects, including those in the NHS, explicit consideration of the effect of whole-life costs (the costs of construction, operation and maintenance for the life of the asset) was relatively scarce.[33] The report also identified some minor risks relating to changes and uncertainty in the timing and cost of a small number of NHS projects.

59. Audit Scotland is currently carrying out a study specifically examining asset management in the NHS in Scotland, which is planned for publication in 2009.

The Scottish Government has announced plans to do a study of Community Health Partnerships

60. All NHS boards now have Community Health Partnerships (CHPs) – or Community Health and Social Care Partnerships (CHSCPs) – in place except NHS Orkney, which still did not have a fully operational CHP at

Case study 1

Governance arrangements in NHS Orkney during 2007/08

In 2006/07, the auditors of NHS Orkney identified a number of areas for improvement in its corporate governance and performance management arrangements. Some improvements were made during 2007/08 but there are still a number of weaknesses.

Progress has been made in strengthening risk management arrangements. The board also facilitated a clinical governance development day to develop an action plan to address clinical governance issues identified by NHS QIS.

Management established a framework of quarterly performance monitoring and reporting to the board but only one performance report was presented to meetings of the board during 2007/08. While it regularly reports the anticipated financial position to board meetings, these reports did not highlight the risks to achieving financial targets or the action needed to achieve these.

The annual audit report included several recommendations in relation to internal control including:

- implementing a programme of review for all governance and operational policies
- introducing annual self-evaluation exercises for the board and its sub-committees to identify areas for development or training
- ensuring minutes of public board and committee meetings provide a comprehensive and accurate record of the discussion by management and non-executives
- establishing a process to document and review the board's internal control framework.

Recent developments

In August 2008, at the NHS Orkney annual review, the Cabinet Secretary for Health and Wellbeing raised concerns over the board's ongoing ability to meet its financial targets, particularly its heavy reliance on non-recurring funding.

In September 2008, NHS Orkney reported on potential governance failings relating to its handling of executive pay and grading, severance payments, executive recruitment and aspects of the proceedings of its Remuneration Committee. The report attributed the potential failures to the lack of an underpinning documented risk and controls based approach to the business of the Remuneration Committee, combined with a number of new or inexperienced staff moving into key roles. The report called for assistance from the SGHD to further strengthen the governance arrangements within the Committee.

Source: Annual audit report to Orkney NHS board and the Auditor General for Scotland 2007/08

32 Section 22 of the Public Finance and Accountability (Scotland) Act 2000 provides the Auditor General for Scotland with statutory powers to produce a report on any audited account sent to him. These reports are laid in Parliament along with the annual accounts.
33 *Review of major capital projects – How government works*, Audit Scotland, 2008.

Case study 2

Summary of the Scottish Parliament Audit Committee report on its inquiry into NHS Western Isles

Focus of the inquiry

The inquiry focused on the following areas:

- governance arrangements and systems of internal control
- leadership and management
- the financial recovery plan
- performance management arrangements.

Key findings

The committee found that the board had built up a deficit due to a combination of factors, including external cost pressures; the pursuit of a clinical strategy that involved investing heavily in acute care services; and serious weaknesses in the board's own internal control systems and financial management. The committee also stated that the Scottish Executive Health Department bore part of the responsibility for the failures as it should have taken further steps to ensure that the board's strategy was financially sustainable. Concern was expressed that progress made by current management would not be maintained without consistency of leadership at the board.

Key recommendations

The committee made a number of recommendations, including:

- the SGHD should review arrangements for the recruitment, training and support provided to health board members, especially in relation to members' audit responsibilities
- the board should work with the SGHD to identify recurrent savings to ensure long-term financial sustainability.

Outcome

In response to the findings of the inquiry, the Scottish Government announced in July 2008 that the three island boards (Western Isles, Orkney and Shetland) will each receive an additional £250,000 annually and each board has agreed to use this funding to develop more formal working partnerships with mainland boards. Formal agreements will be put in place between Western Isles and Highland, and Orkney and Shetland will be partnered with Grampian. The detail of these arrangements will be worked out locally between the partner boards. The Scottish Government anticipates that this will strengthen the island boards' human resources, finance, governance and planning functions. The Scottish Government also announced that it is currently taking forward a board effectiveness project with the aim of improving the performance and working of board members. It also plans to launch a board performance tool to provide boards with the opportunity to measure their performance with a view to introducing a culture of continuous performance improvement.

Update on NHS Western Isles position for 2007/08

While NHS Western Isles' financial position improved in 2007/08, the Auditor General prepared a Section 22 report on the board again this year. This was to report the board's failure to achieve its RRL and to update the Scottish Parliament on the board's progress in addressing the issues raised in previous Section 22 reports.

Source: Report on the 2006/07 Audit of the Western Isles Health Board, Scottish Parliament, 2008 and Annual Report to Western Isles health board and the Auditor General 2007/08

the end of March 2008. It has since begun putting in place management arrangements, although a CHP committee has yet to be formed.

61. In 2007/08, four NHS boards reviewed or restructured their CHP arrangements:

- NHS Ayrshire and Arran reviewed all of its partnership arrangements.
- NHS Borders worked with partners to agree a revised CHCP structure.
- NHS Dumfries and Galloway developed joint working arrangements further through the establishment of a CHSCP board.
- NHS Forth Valley worked with its three partner councils to look at how increased integration can inform the future development of its CHPs.

62. Although all but one NHS board have CHPs in place and some of these have been running for a number of years, their governance and financial management arrangements vary and the running costs of these are unknown. There has been no national evaluation of whether CHPs are efficient and effective in planning and delivering health improvements within their local communities, or whether they are making the best use of their resources.

63. The Scottish Government has stated that CHPs have delivered some benefits to patients, including better management of long-term conditions; more local diagnosis and treatment; improved access to primary care services; and improvements in health through anticipatory care programmes targeted at disadvantaged groups.[34]

64. There are some potential barriers to the effective operation and performance of CHPs. For instance, boards and their council partners have different planning processes, budget cycles and performance management arrangements (including

targets) in place. Boards' HEAT targets and local delivery plan requirements for 2008/09 are linked to the new National Performance Framework and identify the NHS's contribution towards meeting the Scottish Government's national targets and outcomes.[35] Councils' contributions to the national targets are separately agreed as part of their Single Outcome Agreements (SOAs).[36] We understand there are plans for HEAT targets and SOAs to be aligned as the National Performance Framework is developed.

65. From 2008/09, the Scottish Government announced that councils will be required to involve their community planning partners in developing and agreeing their SOAs, which could help to join up arrangements across the sectors. However, in 2007/08, only 16 councils involved or consulted with them in the process.[37]

66. The Scottish Government recently announced its intention to commission a study of CHPs at the end of 2008. There will be three stages to the study. The first will involve all CHPs and build up a picture of how they are progressing overall. The second stage will involve working with a smaller number of CHPs to examine in more depth how they are operating and how they have approached certain key responsibilities and functions. The final stage will involve engagement with a range of stakeholders to discuss and validate the key findings of the study and to see how these compare with their own experience of how CHPs are working. The Scottish Government anticipates that the study will last 12 months and will begin early in 2009.

34 Answer to parliamentary question S3W – 15956.
35 The Scottish Government has put in place a new National Performance Framework outlining the Government's purpose, its five strategic objectives and the 15 national outcomes through which it intends to measure its performance.
36 *Single outcome agreements, SPiCE briefing 08/47*, Scottish Parliament, 16 September 2008.
37 *Single outcome agreements, SPiCE briefing 08/47*, Scottish Parliament, 16 September 2008.

Part 4. The financial outlook for the NHS in Scotland in 2008/09 and beyond

The NHS in Scotland is facing challenging times. Over the next three years, NHS bodies will receive a lower rate of growth in funding and will have to make greater efficiency savings.

Key messages

- Despite an anticipation of relatively lower funding allocations, all boards are predicting a break-even position or better in 2008/09, apart from NHS Western Isles.
- During 2008/09 and beyond, NHS bodies will continue to face similar cost pressures as in 2007/08 as well as having to deal with other issues, such as the cost of achieving full compliance with the European Working Time Directive.
- NHS bodies will also face new challenges in meeting their financial targets such as the impact of lower growth in funding allocations. Boards will also need to be aware of any issues arising as a result of the introduction of single outcome agreements for councils.
- The Scottish Government has announced £1.2 billion to fund specific initiatives set out in its new health strategy.

Funding allocations are expected to reduce in real terms over the next three years

67. In real terms, NHS funding in Scotland has increased by 28 per cent since 2003/04 but will only increase by four per cent between 2007/08 and 2010/11. The Scottish Government has set boards a target of making two per cent cash efficiency savings per year over the next three years. This reduction in funding growth, together with increased efficiency savings targets, means that boards will find it more challenging to achieve their financial targets.

Exhibit 13

Summary of NHS and special board forecast positions against their RRL, 2008/09

NHS bodies are forecasting a total surplus of £64 million in 2008/09.

	RRL (£ million)	Underspend (£ million)
NHS boards	7,095	51
Special boards	957	13
Total	8,052	64

Source: Health board funding allocation news release, Scottish Government, February 2008 and unaudited returns from NHS bodies, July 2008

All boards predict they will break even in 2008/09 apart from NHS Western Isles

68. NHS bodies have predicted that they will underspend their revenue budgets by £64 million in 2008/09. NHS boards are forecasting a £51 million underspend with special boards forecasting a £13 million underspend. NHS Western Isles expects to record an overspend against its RRL of more than £3 million (Exhibit 13 and Appendix 2). The Scottish Government has proposed to provide brokerage to cover the board's cumulative deficit during 2008/09, providing progress with its financial recovery plan is sustained.

69. NHS bodies are forecasting that they will be even less reliant on non-recurring funding in 2008/09. NHS boards are forecasting a total recurring deficit of £16.5 million with special boards forecasting a £13.3 million surplus (Exhibit 3, page 8). The boards that are forecasting a recurring deficit greater than one per cent of their RRL are:

- NHS Highland
- NHS Orkney
- NHS Shetland
- NHS Western Isles.

70. The National Waiting Times Centre Board forecast a short-term recurring deficit of £2.3 million between 2008/09 and 2009/10. This relates specifically to the additional costs of the West of Scotland Heart and Lung Centre. The SGHD has made a commitment to provide funding for this facility for these two years. From 2010/2011, NHS boards in the West of Scotland have agreed to provide recurring funding for the Centre, therefore minimising the financial risk to the board.

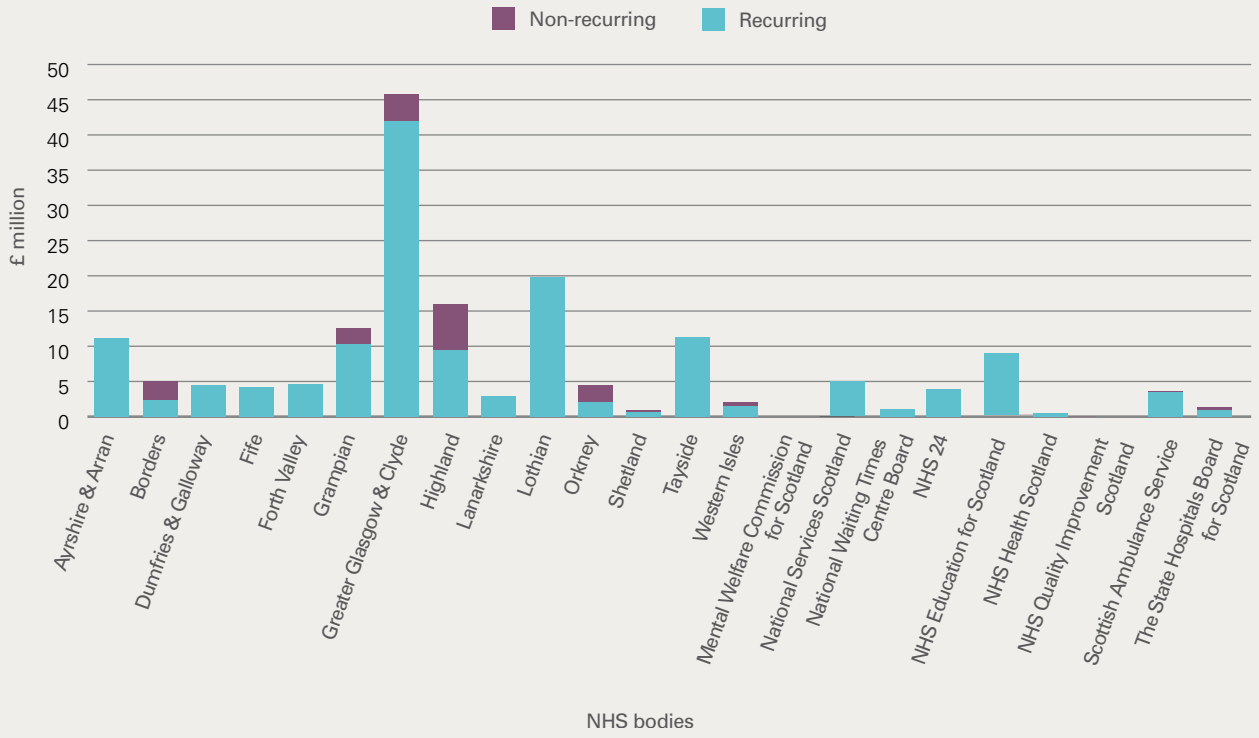
Savings targets

71. In order to achieve their financial positions for 2008/09, NHS bodies plan to make savings of £170 million. Boards have identified £151 million of these savings as recurring and £19 million are considered non-recurring (Exhibit 14, overleaf). Approximately £155 million of these savings will relate to new Efficient Government cash efficiency savings targets for NHS bodies of two per cent of their initial revenue budget allocations.[38]

38 New Efficient Government savings targets have been set for 2008/09–2011/12, including cumulative savings targets of £672 million for the NHS in Scotland. As part of those savings, NHS bodies will be expected to achieve cash releasing efficiency savings of £478 million, which equates to two per cent of their revenue budgets over the three-year period.

Exhibit 14
Analysis of planned savings split between non-recurring and recurring savings for 2008/9

NHS bodies intend to achieve £151 million of recurring savings and £19 million of non-recurring savings in 2008/09.



Source: Unaudited returns from NHS bodies July 2008

Exhibit 15
Challenging savings targets

Six NHS bodies have set themselves significantly higher savings targets for 2008/09.

NHS body	Savings target (£m)	Increase on 2007/08 savings achieved (£m)
NHS Ayrshire and Arran	11.2	5.7
NHS Borders	5.1	3.2
NHS Forth Valley	4.6	3.6
NHS Greater Glasgow and Clyde	46.2	25.8
NHS Orkney	4.4	3.2
Scottish Ambulance Service	3.7	1.9

Source: Unaudited returns from NHS bodies, July 2007 and July 2008

72. Some boards will need to make significant savings in 2008/09 to ensure that they break even. Six boards have set particularly challenging savings targets significantly above the actual savings they achieved in 2007/08 (Exhibit 15).

73. All of the above boards' annual audit reports highlighted the potential failure to achieve planned savings for 2008/09 as a risk. The savings plan for NHS Greater Glasgow and Clyde is outlined in Case study 3, (page 25).

74. Some boards are starting to build up surpluses to pay for forecast increases in expenditure in the future. For example, some NHS boards are building surpluses up to meet the revenue costs of future service redesign projects:

Case study 3

NHS Greater Glasgow and Clyde's financial savings plan for 2008/09–2010/11

NHS Greater Glasgow and Clyde aims to achieve savings of £46 million in 2008/09, of which £42 million will be recurring and £4 million non-recurring. The board has currently identified savings initiatives and plans for £30 million of this target.

This is the second year of a three-year plan to eliminate the £26 million gap between recurring funding and expenditure for the Clyde area which the board inherited when NHS Argyll and Clyde was abolished at the end of 2005/06. The SGHD is providing transitional funding of £8 million in 2008/09 to help fund the shortfall.

The board's auditor has reported that some of the cost pressures that the board will face in 2008/09 include: pay cost increases; growth in prescribing costs of almost six per cent; energy price increases; capital charge increases related to the scale of the current capital programme; and other general inflationary pressures above the funding allocation rates.

Source: NHS Greater Glasgow and Clyde Financial Plan: 2008/09–2010/11

- NHS Fife – costs associated with general hospital and maternity redesign project
- NHS Forth Valley – costs associated with the new acute hospital at Larbert. There will also be some double running costs while the move takes place
- NHS Greater Glasgow and Clyde – costs associated with new hospitals.

Boards will face other cost pressures in 2008/09 and beyond

75. Boards will continue to face cost pressures such as expenditure relating to pay modernisation, rising drug costs and the costs of reducing waiting times and service redesign in 2008/09 and beyond. Emerging cost pressures for 2008/09 and beyond include the cost of abolishing prescription charges; fuel, energy and other general inflationary pressures; and the cost of complying with the European Working Time Directive (ETWD) for junior doctors.

European Working Time Directive

76. Boards must fully comply with the EWTD of a 48-hour working week limit for junior doctors in training by August 2009. Extensions can be given in certain exceptional circumstances up until 2012. The current target for boards is that junior doctors should work less than 56 hours per week. By June 2008, the overall compliance rate in Scotland for this target was 98.4 per cent for doctors in training. Ten boards reported full compliance and NHS Ayrshire and Arran reported the lowest compliance rate of 90.4 per cent.[39]

77. The need to comply fully with the EWTD is a cost pressure to boards as they will need to make other arrangements for covering junior doctors' hours over and above 48 hours or face financial penalties for non-compliance. The Scottish Government requested boards to submit an ETWD compliance plan by June 2008. These plans should set out in detail their plans for achieving compliance with this target. All boards have submitted their plans and the Scottish Government is currently reviewing these.

Car park charges

78. In addition to the cost pressures outlined above, the Scottish Government announced that hospital car park charges are to be abolished from 31 December 2008 at 14 hospitals.[40] Charging will continue at three hospitals where the cost of abolishing the charges would be prohibitive.[41] This will result in a loss of income to the boards affected of approximately £1.4 million during 2008/09, which will be funded by the Scottish Government.[42] In subsequent years, boards will not be compensated for this loss of income.

Boards will also have to deal with new challenges in the coming year

New funding allocation formula

79. The NHSScotland Resource Allocation Committee (NRAC) was established in 2005 to improve the current method used to divide the NHS budget among NHS boards. It published a report in 2008 which set out the new formula. The formula recalculates the percentage share of funding each board will get but it will not be introduced until 2009/10 at the earliest.

39 *Doctors in Training, compliance with new deal,* ISD Scotland, June 2008.
40 The 14 hospitals are NHS Grampian – Aberdeen Royal Infirmary and Dr Gray's Hospital; NHS Greater Glasgow and Clyde – Gartnavel General Hospital and Gartnavel Royal Hospital (one car park for both), Southern General Hospital, Stobhill Hospital, Victoria Infirmary, Western Infirmary and Yorkhill Hospital; NHS Highland – Raigmore Hospital; NHS Lothian – Lauriston Building, Royal Hospital for Sick Children, St John's Hospital and Western General Hospital; and NHS Tayside - Perth Royal Infirmary.
41 The three hospital car parks where charges will still apply after 31 December 2008 are the Royal Infirmary of Edinburgh, Glasgow Royal Infirmary and Ninewells Hospital in Dundee. Parking charges at these hospitals are tied into PFI or contracts with private companies.
42 £1.4 million relates to only part of 2008/09. The full-year effect of the change in policy would be around £5.5 million.

Exhibit 16

Hypothetical example of the impact of the NRAC formula on boards' funding levels for 2007/08

Eight boards would have received less funding in 2007/08 had the new allocation formula been applied.

NHS board	2007/08 funding (£m)	Hypothetical NRAC funding 2007/08 (£m)	Difference
Ayrshire and Arran	530.2	515.2	-15.0
Borders	154.1	143.7	-10.4
Dumfries and Galloway	221.2	210.6	-10.6
Fife	462.4	472.2	9.8
Forth Valley	363.0	375.5	12.5
Greater Glasgow and Clyde	1,737.3	1,701.7	-35.6
Grampian	625.0	639.7	14.7
Highland	445.8	426.5	-19.3
Lanarkshire	735.0	754.6	19.6
Lothian	930.9	989.0	58.1
Tayside	549.4	537.9	-11.5
Orkney	28.7	28.9	0.2
Shetland	33.9	30.7	-3.2
Western Isles	53.6	44.1	-9.5

Source: *Delivering Fair Shares for Health in Scotland: The report of the NHSScotland Resource Allocation Committee*, September 2007

80. The NRAC report gave a hypothetical example of how the formula would have changed the funding allocations for 2007/08 had it been used (Exhibit 16). However, it is important to note that there will be no funding cuts and all NHS boards will continue to receive a minimum growth in their current funding year on year. An additional growth element will be included for those NHS boards which currently receive funding at a level below the NRAC formula percentage. Over time, it is envisaged that NHS boards will gradually move towards receiving the new percentage share of the NHS allocation. The Technical Advisory Group on Resource Allocation has been set up to implement the NRAC recommendations.

National Performance Framework

81. The National Performance Framework includes the adoption of SOAs between the Scottish Government and councils and the abolition of ring-fenced funding for local government. This could present a risk to boards in that they may be accountable for meeting targets for which they do not have financial control. For example, delayed discharge funding will be allocated directly to councils and will no longer be ring-fenced. Some funding streams in the NHS remain earmarked, particularly those allocated during the financial year after the initial funding allocation is made to NHS bodies. NHS bodies are not required to report specifically how they have spent this funding and performance is measured against performance targets.

Cervical screening and the HPV vaccine

82. From September 2008, boards are required to implement routine cervical screening and provide the HPV vaccine for girls aged between 12 and 18 years.[43] The Scottish Government has allocated £64 million to fund the cost of the vaccine and a communications campaign for the next three years. However, boards are required to implement the immunisation programme within existing resources, which some boards may find challenging.

83. The largest resource needed is skilled nurses to implement the programme. However, a 2006 report recommended a new model of community nursing which combines the different nurse disciplines,

43 The Human Papilloma Virus (HPV) vaccine helps to protect against cervical cancer.

Exhibit 17

Funding commitments in *Better Health, Better Care*

The Scottish Government has committed £1.2 billion between 2008/09 and 2010/11.

Policy area	Scottish Government commitment 2008/09 2010/11 (£m)
To tackle poverty deprivation	435
Support to deliver 18-week whole journey standard	270
Increase resilience against a flu pandemic	100
Abolition of prescription charges	97
Drug treatment and rehabilitation services	94.3
Reduce alcohol-related harm	85.3
New measures to tackle hospital associated infection	54
Smoking cessation services	33
Implementation of national sexual health strategy	15.6
Tackling obesity	11.5
Implementation of carer information strategies	9
Smoking prevention action plan	9
Independent sexual health information	1
Pilot carer training	0.3
Development of national young carer forum	0.2
Total	1,215.2

Source: *Better Health, Better Care*, Scottish Government, December 2007

including school nursing, absorbing them into a single community health nursing discipline. This model is currently being tested at four development sites (Borders, Lothian, Tayside and Highland) and testing is due to be completed by March 2009.[44]

The Scottish Government has announced funding for initiatives set out in its health strategy

84. The Scottish Government's health strategy, *Better Health, Better Care*, was launched in December 2007.[45] The strategy sets out the key actions the Scottish Government will take to improve health in Scotland. Some of these included additional funding commitments (Exhibit 17).

85. Boards are not required to report on the use of this additional funding separately. They are required to report on their overall performance through the HEAT targets and their local delivery plans.

The Scottish Futures Trust has been established to coordinate and support investment in public infrastructure

86. The Scottish Government established the Scottish Futures Trust (SFT) in September 2008 to coordinate and support investment in public infrastructure. The Scottish Government intends the SFT to replace the use of PFI, although it is not yet clear how the SFT will work or how the NHS will be able to access capital funding from this source.

87. The Scottish Government has approved a number of new major capital projects from 2008/09, the business cases for which rely on continued public and private investment. It is not yet clear how the SFT intends to secure the private investment for these and future capital projects. Major capital projects being progressed from 2008/09 include:

- the Southern General Hospital in Glasgow, which will be publicly funded, costing around £840 million
- three projects by NHS Grampian, costing around £177 million
- the redevelopment of Dumfries and Galloway Royal Infirmary, costing around £120 million.

88. The UK Government has committed the UK as a whole to move to accounting under the International Financial Reporting Standards (IFRS) from April 2008, although the implementation date for public bodies has been deferred until 2009.[46] These new accounting rules will have significant implications for NHS bodies as it is more likely that they will be required to show PFI assets on their balance sheets. It will also have implications for private investors in their accounting treatment of profits, which could lead to less private investment in some public sector infrastructure projects.

44 *Visible, Accessible and Integrated Care, Report of the Review of Nursing in the Community in Scotland,* Scottish Executive, 2006.
45 *Better Health, Better Care*, Scottish Government, December 2007.
46 The deferral was agreed to minimise the burden on public bodies and give them more time to make the changes to their accounting treatment of PFIs.

Appendix 1.

Financial performance of NHS bodies 2007/08

	Revenue resource limit £000	Revenue resource outturn £000	Variance under/over ( ) £000	Capital resource limit £000	Capital resource outturn £000	Variance under/over ( ) £000
NHS Ayrshire & Arran	596,150	586,189	9,961	30,395	30,395	0
NHS Borders	175,058	174,408	650	5,338	5,294	44
NHS Dumfries & Galloway	257,141	250,134	7,007	11,851	11,774	77
NHS Fife	520,388	514,724	5,664	23,468	23,428	40
NHS Forth Valley	408,081	406,081	2,000	7,778	7,778	0
NHS Grampian	729,245	722,854	6,391	29,163	29,163	0
NHS Greater Glasgow & Clyde	2,014,370	2,013,724	646	122,733	122,333	400
NHS Highland	522,136	516,774	5,362	21,071	21,044	27
NHS Lanarkshire	821,928	810,143	11,785	17,494	17,475	19
NHS Lothian	1,080,060	1,079,696	364	40,254	39,874	380
NHS Orkney	37,978	37,974	4	3,848	3,811	37
NHS Shetland	42,184	41,208	976	3,615	3,457	158
NHS Tayside	634,862	633,061	1,801	42,543	42,520	23
NHS Western Isles	60,324	63,421	-3,097	3,767	3,666	101
Total for NHS boards	**7,899,905**	**7,850,391**	**49,514**	**363,318**	**362,012**	**1,306**
Mental Welfare Commission for Scotland	4,040	3,933	107	177	172	5
National Waiting Times Centre Board	65,846	58,567	7,279	13,768	13,305	463
NHS 24	55,656	55,401	255	6,277	6,276	1
NHS Education for Scotland	390,328	375,149	15,179	764	764	0
NHS Health Scotland	23,091	22,907	184	69	69	0
NHS National Services Scotland	382,116	379,595	2,521	26,449	26,449	0
NHS Quality Improvement Scotland	16,001	15,603	398	294	294	0
Scottish Ambulance Service Board	179,666	179,628	38	10,984	10,973	11
State Hospital Board for Scotland	33,987	33,923	64	8,458	8,447	11
Total for special boards	**1,150,731**	**1,124,706**	**26,025**	**67,240**	**66,749**	**491**
Total for all NHS bodies	**9,050,636**	**8,975,097**	**75,539**	**430,558**	**428,761**	**1,797**

Source: NHS bodies' annual accounts

Appendix 2.

Forecast financial performance of NHS bodies 2008/09

NHS board	Revenue Resource Limit (RRL) £000	Forecast cumulative surplus/deficit ( ) £000
NHS Ayrshire and Arran	546,700	10,000
NHS Borders	158,900	0
NHS Dumfries & Galloway	228,100	4,500
NHS Fife	479,700	1,990
NHS Forth Valley	375,500	3,500
NHS Grampian	646,300	8,000
NHS Greater Glasgow & Clyde	1,790,900	11,400
NHS Highland	459,600	0
NHS Lanarkshire	760,500	14,800
NHS Lothian	963,000	0
NHS Orkney	29,700	0
NHS Shetland	34,900	0
NHS Tayside	566,400	0
NHS Western Isles	55,200	-3,100
Total for NHS boards	**7,095,400**	**51,090**
Mental Welfare Commission for Scotland	4,000	0
National Waiting Time Centre Board	40,000	4,000
NHS 24	53,400	0
NHS Education for Scotland	361,700	8,900
NHS Health Scotland	17,300	0
NHS National Services Scotland	247,100	0
NHS Quality Improvement Scotland	16,200	400
Scottish Ambulance Service Board	183,400	0
State Hospitals Board for Scotland	33,700	0
Total for special boards	**956,800**	**13,300**
Total for all NHS bodies	**8,052,200**	**64,390**

Source: Health board funding allocation news release, Scottish Government, February 2008 and unaudited returns from NHS bodies, July 2008

Appendix 3.

Glossary of terms

Agenda for Change	A UK-wide plan to introduce a new pay system for all NHS staff with the exception of doctors, dentists and most senior managers. The new system aims to standardise conditions of service for staff.
Annual accounts	The annual accounts of an NHS body provide the financial position for a financial year, ie 1 April to 31 March. The format of the annual accounts is set out in NHS accounts manuals and includes financial statements, notes to the accounts and memorandum statements (known as Scottish Financial Returns).
Audit report	A final report by an NHS body's auditor on the findings from the audit process.
Break even	Where income equals expenditure.
Brokerage	A facility where the Scottish Government provides money to a health board to enable them to meet their financial target. This money must be repaid in future years.
Capital resource limit (CRL)	The amount of money an NHS board is allocated to spend on capital schemes in any one financial year.
Cash releasing savings	Where a saving is realised because the organisation or function delivers the same service with less money. For example, by delivering support services differently.
Cash requirement	This is the amount of cash an NHS body needs to support its operational activities during the year.
Clinical governance	Arrangements put in place to ensure safe and effective healthcare.
Community Health Partnership (CHP)	A partnership between health and social care and responsible for the delivery of a wide range of community health provision including GP services, pharmacy, social care and community nursing.
Community Health and Social Care Partnership (CHSCP)/Community Health and Care Partnership (CHCP)	A partnership between health and social care and responsible for the delivery of a wide range of community health provision including GP services, pharmacy, social care and community nursing. Also responsible for many local social care services, provided by social work staff.
Consolidation	Where a group of entities combine (consolidate) their financial statements into one set of accounts. The Scottish Government's consolidated accounts reflect the consolidated assets and liabilities and the results of all entities within the Scottish Government departmental accounting boundary.
Consultant contract	The new pay, terms and conditions negotiated on a UK-wide basis for NHS consultants.

Corporate governance	Arrangements put in place to ensure proper use of management and resources.
Cost base	The cost of providing day-to-day healthcare services in an NHS board area.
Cumulative deficit	The excess of expenditure over income built up over more than one year.
Cumulative surplus	The excess of income over expenditure built up over more than one year.
Efficient Government Initiative	A Scottish Government initiative to increase efficiency across the whole of the public sector in Scotland by delivering the same services with less money or delivering more services with the same money.
Family Health Services (FHS)	Services provided by GPs, dentists, opticians and community pharmacists.
Financial balance	Where income received is equal to expenditure made on an on going basis.
Financial gap	The difference between the income and expenditure that is needed on a recurring basis to pay for operational activities. This excludes any additional one-off funding received from SGHD and any planned savings.
Financial statements	The main statements in annual accounts of an NHS body. These include an operating cost statement, statement of recognised gains and losses, balance sheet and cash flow statement. The format of these statements is specified in NHS accounts manuals.
General Medical Services (GMS) contract	A new contract for general practitioners (GPs) introduced in April 2004 where GPs receive a lump sum based on a contract. Additional payments are made for services provided over and above those specified in the contract or where they are provided to an enhanced specification.
Governance	The framework of accountability to users, stakeholders and the wider community, within which the organisations take decisions, and lead and control their functions, to achieve their objectives.

In-year financial performance	Result of income compared with expenditure, ignoring any impact of the previous years' financial results.
Non-recurring funds	An allocation of funding for projects with a specific lifespan, or one-off receipts. This includes ring-fenced funding and capital receipts.
One-off funding	Funding which is provided for one year only.
Outturn	The final financial position, which could be the actual or forecast position.
Private Finance Initiative (PFI)	The UK Government's initiative to encourage the development of private finance in the public sector. A generic term for projects involving both the public and private sectors. The involvement can be to varying degrees and the partnership can take different forms.
Productivity efficiency savings	Efficiencies which do not release cash but allow frontline services to deliver more or better services with the same money. For example, through reducing sickness absence.
Qualified audit opinion	When an auditor is of the opinion that there is a problem with the annual accounts of an NHS body, they can issue a qualified report on the accounts. The qualification may be on the truth and fairness of the accounts, the regularity of transactions or both.
Revenue resource limit (RRL)	The amount of money an NHS board is allocated to spend on day-to-day operations in any one financial year.
Section 22 report	Reports produced by the Auditor General for Scotland to draw attention to significant issues concerning public sector bodies. Section 22 reports are only produced for bodies where the Auditor General for Scotland is responsible for securing the audit.
True and fair opinion	Auditors provide an opinion as to whether an NHS body's accounts have been prepared in accordance with all relevant accounting standards, legislation and guidance.
Underlying deficit	The underlying deficit is the on going financial gap in the NHS board area between the money received to provide health services and the costs of providing these services.
Unqualified audit opinion	When auditors of NHS bodies are satisfied with the annual accounts they will issue an unqualified audit opinion.

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