

# NHS Shetland

## Annual Report to Members and the Auditor General for Scotland 2008/09

For Discussion at the Audit Committee on 26 June 2009



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

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

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

# 1. Introduction

## Purpose of this report

The Annual Report which follows is primarily designed to direct your attention to matters of significance that have arisen out of the 2008/09 audit process and to confirm what action is planned by management to address the more significant matters identified for improvement.

## Scope of the Audit

Our overall responsibility as external auditor of NHS Shetland is to undertake our audit in accordance with the principles contained in the Code of Audit Practice issued by Audit Scotland in March 2007.

In this regard, the Code sets out the need for public sector audits to be planned and undertaken from a wider perspective than in the private sector involving not only assurance on the financial statements but also consideration of areas such as regularity, propriety, performance and the use of resources.

It also sets out the need to recognise that the overall audit process is a co-ordinated approach involving the “appointed auditor”, the Auditor General for Scotland and other auditors such as Audit Scotland’s Health Performance and Public Reporting Group.

Our audit has been planned and conducted to take account of these wider perspectives.

Under the requirements of International Standard on Auditing (UK and Ireland) (‘ISA (UK&I)’) 260: “Communication of audit matters to those charged with governance”, we are required to communicate audit matters of governance interest arising from the audit of financial statements to those charged with governance of an entity.

This Annual Report to Members, together with previous reports to the Audit Committee throughout the year, discharges the requirements of ISA (UK&I) 260.

## Acknowledgment

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

PricewaterhouseCoopers LLP  
Kintyre House  
209 West George Street  
Glasgow

26 June 2009

## 2. Executive Summary

### Audit Opinion and Accounting Issues (Section 3)

Our audit opinion addresses both the true and fair statement of the Board's financial results and balances for the year ended 31 March 2009 (2008/09) and the regularity of its income and expenditure in the year.

We are pleased to report that our opinion on the true and fair view on the financial statements is **unqualified**.

Our regularity opinion on income and expenditure is also **unqualified**.

We also provide a view as to whether those parts of the Remuneration Report subject to audit have been properly prepared. Our opinion on the Remuneration Report is **unqualified**.

Our audit opinion does not extend to any other part of the Directors' Report.

We did encounter significant issues with the efficiency and robustness of the financial statements preparation process which had a knock-on impact on the efficiency and related costs of our audit process. In particular, working papers were not of an appropriate standard in terms of completeness and accuracy. Working papers were revised on a number of occasions during our audit fieldwork, requiring us to revisit work already completed.

In addition, the financial statements presented for audit were incomplete in most respects.

A number of specific accounting issues were discussed with management during the audit. The most significant of these related to the accrual for prescribing expenditure. However, we noted a wider issue in relation to the robustness of the process for all Family Health Service income and expenditure, resulting in an audit adjustment of £0.574 million.

Our concerns over the process used to prepare the financial statements and the specific accounting issues we encountered are discussed further in section 3.

### Financial Management and 2008/09 Performance (Section 4)

The Board is reporting a surplus for the year of £0.390 million. A significant factor in this overall surplus is the abatement of the Revenue Resource Transfer by Shetland Islands Council of £0.775 million, along with the carry forward of a £0.976 million surplus from 2007/08. As a result, the Board achieved all 3 of its key financial targets (Revenue Resource Limit, Capital Resource Limit and Cash Requirement). Financial performance is discussed in further detail with Section 4.

### Financial Forecasts for 2009/10 (Section 5)

The Board has prepared detailed financial forecasts as part of its long term five year financial planning. The financial forecasts for 2009/10 include a projected breakeven position which relies on a significant non-recurring surplus and continued abatement of the Resource Transfer. More significant savings are required to achieve recurring balance. Further details are included in section 5.

## Governance and Business Risks (Section 6)

As part of our Annual Audit Plan, we have performed work in the year in relation to the Board's Governance arrangements. Our findings were presented in our 2008/09 Interim Management Letter. In overall terms, the Board has in place established arrangements, although needs to take steps to further enhance the governance environment, including in relation to financial management, budgetary control, accounts preparation and reconciliations.

## Systems of Internal Control (Section 7)

The Code of Audit Practice requires us to review and report on the Board's Statement on Internal Control. Based on our normal audit procedures, we do not disagree with the disclosures contained within the Statement of Internal Control. Section 6 includes a summary of recent developments in relation to corporate governance and risk management.

Corrective management action on previously reported weaknesses in control has been slower than anticipated, requiring more concerted effort to be made to improve the control environment.

## Recommendations

Where appropriate, we have made recommendations for improvement. These are summarised in Appendix A along with management's responses.

# 3. Audit Opinion and Accounting Issues

## Audit opinion

Our audit opinion concerns both the true and fair statement of the Board's financial results for the year ended 31 March 2009 and the regularity of its income and expenditure in the year.

We are pleased to report that our opinion on the true and fair view on the financial statements is **unqualified**.

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## Audit Process

In response to a recommendation made in our 2007/08 Annual Report, the Board committed to put in place more effective arrangements for the accounts closure and preparation process for 2008/09. However, during our final audit visit of 2008/09, we found that the level of improvement was significantly lower than had been agreed.

We received a set of financial statements at the start of our audit fieldwork. However, only the section on Cash was complete in full. Fixed Assets and Debtors were partially complete. Other areas were incomplete. Furthermore, relative to other NHS organisations which we audit, the supporting working

papers were lacking in completeness and detail.

Also, by example, several financial statement areas were only finalised and presented to us for audit during the third and final week of our visit. In addition, finance staff did not complete reconciliations of Family Health Services (FHS) Income until after our audit fieldwork had been completed.

In several financial statement areas, we found that the working papers provided to us did not match the underlying accounting records. It appears that management had not spent sufficient time reviewing working papers prior to presenting them to us for audit. Consequently, we were forced to spend time investigating differences between the financial statements, working papers and accounting records before starting our actual audit work. Our normal audit role had to be expanded to inform finance staff of completion changes required to finalise the financial statements. These were not categorised as normal audit adjustments.

This led to abortive audit work and significant inefficiency in the process. The Director of Finance was personally required to intervene in the financial statement completion process on a number of occasions when we feel issues could and should have been resolved by the Finance team.

### **ACTION 1**

As a result of these matters, we have incurred additional costs and would normally require additional audit fees to be paid. However, as a sign of goodwill, we are not proposing any additional fees. Nevertheless, should a significant improvement not take place in 2009/10, we would be forced to require additional audit fees to be paid.

Despite these unnecessary pressures, we believe a professional working relationship was maintained with your officers and we again intend to work closely with management to enable you to develop a more effective accounts closure and preparation process for 2009/10.

## Preparation and Approval

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

The financial statements were submitted to the Board's Audit Committee on 26 June 2009 and approved and adopted at the Board meeting on 26 June 2009.

## Unadjusted misstatements

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

As a result of our work, we proposed a number of audit adjustments and all of these have been processed by management in the finalised version of the 2008/09 financial statements.

## Accounting Issues

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

### Prescribing Accrual

Dispensing doctors and chemists are reimbursed initially by Practitioner Services Division (PSD), which makes payments on behalf of NHS

Shetland. NHS Shetland then reimburses PSD, with this payment being made two months in arrears.

In order to monitor this expenditure and ensure that NHS Shetland has accurate information on payments made by PSD, monthly reconciliations need to be carried out between PSD reports and the Board's general ledger position. However, this process is not currently being carried out for all categories of FHS income and expenditure.

As a result, management had considerable difficulty at the year end in providing explanations for the reconciling differences between the values contained in the NHS Shetland general ledger and those supplied by PSD. While management did eventually manage to complete reconciliations to our satisfaction, this was not done until three days after our audit fieldwork had been concluded and after several interventions by ourselves.

### **ACTION 2**

As part of our review of the FHS reconciliations, we found that the value of the accrual relating to prescribing expenditure had been understated by £0.574 million in the draft financial statements. The expenditure and hence accrual balance had been omitted from the financial statements because of an error in working papers which was not picked up due to weaknesses in NHS Shetland's reconciliation process as outlined above.

The required adjustment to reflect the correct accrual balance would have had the effect of putting the Board in a deficit position for the 2008/09 financial year. However, to offset the impact, the Board reached agreement with Shetland Islands Council (SIC) to return to the Board £0.575 million of the total £1 million payment that had been made by the Board to the Council during the year in respect of Resource Transfer.

In substance, the Board's final surplus position has only been achieved as a result of SIC agreeing to adjust the Resource Transfer payment post-year end.

### **ACTION 3**



## Treatment of Equal Pay Contingent Liability

Following recent developments in the cases against the NHS in relation to Equal Pay and Agenda for Change, the CLO Equal Pay Unit and Audit Scotland have agreed wording which should be included within the notes to the financial statements regarding the contingent liability for Equal Pay claims. The Board has received no formal claims in relation to Equal Pay in the financial year to 31 March 2009. However, the Board has reflected its potential liability by complying fully with the prescribed contingent liability wording.

## International Financial Reporting Standards (IFRS)

Government bodies, including NHS Boards, are required to adopt IFRS for 2009/10, including the restatement of 2008/09 comparatives. The objective is to bring the public sector into line with the private sector and to introduce greater comparability and consistency across public sector accounting.

In order to prepare IFRS compliant accounts in 2009/10, NHS Shetland will need to revise its accounting policies, change the format of its financial statements and include a significant number of additional disclosures. It will need to restate its 2008/09 comparative figures and report these together with its 2009/10 figures on an IFRS basis.

In order to restate the 2008/09 closing balances under IFRS, NHS Shetland was required to recalculate its opening balance sheet as at 1 April 2008 on an IFRS basis and submit it to the Scottish Government Health Directorates by 28 November 2008.

We were required to report on the processes adopted by management to prepare the IFRS opening balance sheet as at 1 April 2008. The results of our findings have been reported separately in a letter to the Director of Finance.

We found during our review of Land and Buildings within the IFRS opening balance sheet that GP Surgeries had been written down by £3.035 million from their UK GAAP valuation, based on an estimate given by an Independent Valuer, where a more formal valuation could have produced an

amount materially different to the estimation. A formal valuation was carried out subsequently.

We also found that the holiday pay accrual of £0.350 million was calculated based on an average salary and five days leave for all staff. This method of calculation lacks reliability and may lead to misstatement. The holiday accrual should be calculated based on a sample of actual data which is extrapolated to estimate the total holiday accrual.

In addition, we noted that two Dental Equipment leases should be treated as finance leases instead of operating leases.

The next stage of the process is that a full set of IFRS accounts need to be prepared for 2008/09 by the end of September 2009. These will be subject to audit by end November 2009.

The Board will need to apply the same degree of rigour to the preparation of the IFRS accounts as to the year end financial statements.

**ACTION 1**



## 4. Financial Management and 2008/09 Performance

	£ million	£ million
Recurring income	34.870	
Recurring expenditure (before savings)	(37.360)	
Recurring savings	<u>0.640</u>	
<b>Underlying recurring surplus / (deficit)</b>		<b><u>(1.850)</u></b>
Non-recurring income	10.060	
Non-recurring expenditure (before savings)	(8.060)	
Non-recurring savings	<u>0.240</u>	
<b>Non-recurring surplus/(deficit)</b>		<b><u>2.240</u></b>
<b>Financial surplus/(deficit) for the year</b>		<b><u>0.390</u></b>
<b>Underlying recurring surplus / (deficit) as a percentage of recurring income</b>		<b>(5.3%)</b>

Figures provided by Nick Kenton, Director of Finance

### Performance against Key Financial Targets

The Board is required to meet three targets each year as set by the Scottish Government Health Directorates (SGHD). The performance of the organisation is as follows:

	Limit set by SGHD £ million	Actual Outturn £ million	Variance (over)/under £ million
Revenue Resource Limit	44.924	44.534	0.390
Capital Resource Limit	4.023	4.013	0.010
Cash Requirement	49.622	49.553	0.069

A significant reason for the achievement of the £0.390 million surplus by the Board in 2008/09 was a non-recurring agreement with SIC not to pay the full Revenue Resource Transfer amount. The Board made a payment of £0.425 million.

It must be emphasised that the Board is not in recurring balance and that the financial outturn was underpinned by a carry forward surplus of £0.976 million from 2007/08, together with the lower Resource Transfer payment noted above.

## Performance against Budget 2008/09

The table and narrative below set out in summary form the main under and overspends against budget for the year to 31 March 2009.

Actual Out-turn versus Original Plan	£ million	£ million
<b>Projected breakeven for 31 March 2009</b>		<b>0</b>
Underspends:		
Health Promotion & Community Dental	0.200	
Reserves & Contingencies	0.900	
Non-Recurring Funding Increases	<u>0.700</u>	
<b>Total Underspend</b>		<b><u>1.800</u></b>
Overspends:		
Facilities Management	(0.200)	
Estates	(0.500)	
Non-SLA NHS Activity	(0.200)	
Agenda for Change	(0.200)	
Other	<u>(0.310)</u>	
<b>Total Overspend</b>		<b><u>(1.410)</u></b>
Actual Surplus Reported 31 March 2009		<b><u>0.390</u></b>
<b>Agreed carry forward to 2009/10</b>		<b><u>0.390</u></b>

## Underspends

A key underspend arose from increases in non-recurring funding of £0.700 million. This contributed to the substantial overall non-recurring surplus position.

In addition, the Board maintains a number of budgetary reserves and contingencies to off-set the impact of unforeseen expenditure in functional budget areas. A total underspend of £0.900 million was reported against these reserves in 2008/09.

Other underspends totalling £0.200 million were also noted across Health Promotion and Community Dental expenditure.

## Overspends

The key overspends arose from Facilities Management and Estates, amounting to £0.700 million in total. The Board has acknowledged the need to address overspends in this area and has commissioned a review of financial control to be overseen by the Estates Improvement Project Board.

A key component in robust financial monitoring is good quality management accounting information. This should allow budget holders to identify and address the causes of overspends promptly. We have previously noted concerns with the quality and timeliness of the information being provided to budget holders.

### **ACTION 4**

Non-SLA NHS activity also showed a significant overspend. This expenditure related to treatment for Shetland residents by other NHS bodies for which there is no Service Level Agreement (SLA). The overspend emerged post year end when several large and unexpected invoices were received from other NHS Boards.

Agenda for Change has continued to have a financial impact on the Board. However, the 2008/09 overspend of £0.200m relates to back-pay and is not expected to create significant pressure on the Board's recurring position in future years.

## Capital Programme Performance

NHS Shetland reported total expenditure of £4.013 million against its 2008/09 Capital Resource Limit. Whilst the full Capital Programme covers numerous projects, a significant proportion of total expenditure was incurred on a small number:

- Gilbert Bain Hospital – a major project is underway, covering redevelopment, refurbishment and major maintenance. Total expenditure in 2008/09 was £2.266 million.
- Montfield Accommodation – project involves refurbishment to exterior of accommodation at Montfield, with total expenditure of £0.208 million.
- Whalsay Health Centre – relocation of dental services from Whalsay Junior High School to Whalsay Health Centre and the redevelopment of the Health Centre to provide additional space and improved access. Total spend in 2008/09 was £0.204 million.

As in previous years, NHS Shetland continues to make significant capital grants to fund improvements in health infrastructure across the islands. Total grants made in 2008/09 amounted to £0.802 million. An element of this (£0.350 million) related to Montfield Care Home for which the Board has approved a total capital grant to the Council of £2.417 million. The purpose is to extend the level of care that can be provided in Shetland.

The Board intends to continue to make capital grants in 2009/10 and has kept us apprised of its plans in this regard throughout the year.

# 5. Financial Forecast for 2009/10

	£ million	£ million
Recurring income	35.900	
Recurring expenditure (before savings)	(38.900)	
Recurring savings	<u>1.500</u>	
<b>Underlying recurring surplus / (deficit)</b>		<b><u>(1.500)</u></b>
Non-recurring income	8.900	
Non-recurring expenditure (before savings)	(7.400)	
Non-recurring savings	<u>0.000</u>	
<b>Non-recurring surplus/(deficit)</b>		<b><u>1.500</u></b>
<b>Financial surplus/(deficit) for the year</b>		<b><u>0.000</u></b>
<b>Underlying recurring surplus / (deficit) as a percentage of recurring income</b>		<b>(4.2%)</b>

## 2009/10 Projected Outturn

NHS Shetland is forecasting a breakeven position in 2009/10. This is expected to arise from an underlying recurring deficit of £1.500 million which will be off-set by the same level of non-recurring surplus.

The Board is aware of the underlying risks arising from its planning assumptions and the need to restore underlying financial balance. In particular, the Board has noted its exposure to the Revenue Transfer abatement, potential for impairment of the Gilbert Bain Hospital redevelopment and expenditure on locum staff.

In view of the risks associated with the forecast and the reliance on the non-recurring surplus and informal arrangement with SIC leading to the Resource Transfer reduction, the Board needs to refresh efforts to identify further recurring savings.

### **ACTION 3**

## Recurring deficit

In preparing its budget for the 2009/10 financial year, the Board has identified and quantified a series of recurring cost pressures. These include the effects of inflation, investment to meet national targets and local service developments.

Key cost pressures are summarised in the table on the next page:

Figures provided by Nick Kenton, Director of Finance

Pressure area	Cost £ million
Pay Awards & Increments	0.586
Inflation on Service Level Agreements	0.264
Capital charges arising from Capital Programme	0.200
Secondary care drugs	0.105
Estates maintenance programme & departmental restructuring	0.238
Additional GP in Lerwick	0.100
<b>Recurring Pressure</b>	<b><u>1.493</u></b>

In order to respond to these cost pressures, NHS Shetland has identified total savings of approximately £1.5 million for 2009/10, with a particular focus on a range of areas including Primary Care prescribing, the National Tariff initiative, the SLA with NHS Grampian and hospital nursing.

The Board also has a lease agreement with SIC for space at Montfield Hospital, from which it expects to generate income of £0.100 million. This extra income will be used in conjunction with efficiency savings to off-set the impact of the additional cost pressures identified above.

However, we note that even with this target level of savings and additional income, the Board is still projecting a substantial underlying recurring deficit of £1.500m, representing 4.2% of recurring income.

### Non-recurring surplus

The recurring deficit is off-set by a significant non-recurring surplus of £1.500 million, largely due to the carried forward surplus of £0.390 million from 2008/09 and an assumption by management that it will continue to be able to negotiate non-recurring reductions in the amount paid to SIC in relation to the Resource Transfer.

We note that the proportion of income and expenditure that the Board has identified as non-recurring is approximately 20% of its total income which is high in comparison to other NHS Boards which we audit. The impact of a withdrawal of this funding is therefore potentially greater for NHS Shetland, particularly given that the non-recurring surplus is supporting the overall breakeven forecast.

The pressing need for the Board to identify recurring savings and decrease its reliance on this non-recurring surplus is discussed further within 'Financial Plan' below.

### Financial Plan

The Board has acknowledged the need to reduce the level of recurring deficit in order to achieve medium to long-term financial sustainability. In this regard, we have been informed that the Board has agreed a three-year financial plan with the Scottish Government Health Directorates that would see the underlying deficit being reduced to around £1 million by 2011/12.

However, the UK pre-budget report indicated that an additional £5 billion of savings would be required from the public sector in 2010/11. There still remains significant uncertainty across the sector how this will translate into targets for individual Boards, although the probability is that there will be a significant increase in savings requirements from 2010/11 in comparison to those previously anticipated. This matter will also likely have an impact on SIC, potentially impacting its ability to continue to reduce Resource Transfer payments due from the Board.

These additional savings requirements will place significant increased financial pressure on NHS Shetland. Existing financial planning and efficiency savings targets do not take account of the savings requirements resulting from the expected pressures on public sector budgets in future.

The Board should therefore commence planning for this likelihood at the soonest opportunity to ensure that it is able to react effectively to the significant financial constraints which will be placed upon it from 2010/11 and beyond.

### **ACTION 3**

# 6. Governance and Business Risks

We comment on the following areas throughout this section of the report:

- Overall Governance Arrangements
- Partnership Working
- Service Sustainability
- Performance Management
- Financial Management and Performance
- People Management
- Information Management
- e-Health Plans

We have also reported in detail on a number of these areas in our Interim Management Letter (IML) for 2008/09 submitted to the Audit Committee on 26 March 2009.

## Overall Governance Arrangements

Through good governance, NHS Boards are able to improve services for patients and the working lives of those staff that care from them. In order to discharge this function, NHS Shetland must have in place a full executive management team to ensure that the organisation's vision and strategy can be delivered.

The post of Director of Service Improvement post was vacant between April and October 2008 and is again vacant, having been so since March 2009. The Director of Pharmacy covered the post on an acting basis during these vacant periods. We have been informed that the Board disbanded the post in May 2009 and has transferred responsibilities to other members of the Senior Management Team. However, it is important to ensure that the Board still retains sufficient senior management capability, particularly in view of the financial pressures it will face in the short to medium term future.

### **ACTION 5**

NHS Shetland has an established committee framework, with Audit, Staff Governance, Remuneration, Clinical Governance, Service Redesign and Community Health Partnership Committees in place.

A specific plan has been compiled which sets out how objectives and actions will be taken forward to develop the Clinical Governance and Risk Management framework across the organisation.

The objectives set out in the plan are based on locally defined Key Performance Indicators as well as recommendations from the formal NHS

Quality Improvement Scotland (NHS QIS) review, which took place in May 2007.

## Partnership Working

NHS Shetland and SIC work in collaboration through the Community Health and Care Partnership (CHCP). The CHCP Agreement sets out agreed joint aims, targets, governance arrangements and financial resources.

The CHCP does not currently make use of a pooled budget. During 2008/09, both NHS Shetland and SIC provided funds for specific areas of the budget. Funding streams for agreed joint priorities across the CHCP are aligned. All funding previously available through specific funding allocations and now included in the Council's revenue streams are allocated to community health and care services.

Both SIC and NHS Shetland must ratify the annual objectives set for the CHCP. An annual plan and a three year plan are maintained, with both documents being set within the context of the Terms of Reference agreed between the two partners.

Performance against annual objectives is monitored quarterly at the CHCP committee. This includes a number of HEAT targets, for example, relating to delayed discharges. The number of targets is expected to increase for the 2009/10 financial year.

## Service Sustainability

NHS Shetland was among the first wave of boards in Scotland to adopt the strategic introduction of LEAN methodology in Service Redesign. This methodology focuses on process flow and the removal of activities identified as not directly benefiting service delivery to patients.

We have been informed that NHS Shetland has taken a number of steps during 2008/09 to improve service delivery, including:

- Creating a Gynaecology special interest training role to speed up treatment and remove the need for patients to see a consultant;

- Implementing new technical level roles in ENT/Audiology to assist care pathway throughput;
- Examining pathways of care within community-based services; and
- Joining the Ayrshire & Arran consortium to access the Cedar general ledger system. This has created additional functionality for management accounting.

In addition to service redesign, investment in facilities is a major part of the long-term vision, as set out in NHS Shetland's "2020 Vision". In this regard, the Gilbert Bain Hospital redevelopment continues to be a central part of the Board's investment in infrastructure. The work on outpatients (including new dental surgeries) has been completed and the rooms are now operational.

Other projects include the extension of the Theatre Suite, including extension and refurbishment of staff accommodation and offices, refurbishment of the endoscope room, provision of a temporary car park at the Brevik House site and refurbishment of the Maternity Unit.

The Board is working to improve the Medical Records and Reception Services through the development of procedures and policy for health records management e.g. access to health records procedure. In addition, the Information and IM&T departments have been reviewed and restructured to improve support for service delivery.

## Performance Management

Performance management is carried out through monitoring against the Local Delivery Plan (LDP) which is agreed on an annual basis by the Board and is based upon the nationally prescribed HEAT targets. The LDP includes trajectories to indicate how national targets will be reached by March 2011.

The delivery of the waiting times targets has been supported by the establishment of a performance management framework and organisation plan (known as the 09/10 Plan) which focuses on capacity, financial balance, service development and performance.



## Financial Management

Management receive financial information each month to help manage performance against budgets and control expenditure. Management accounts are prepared on a monthly basis. Management accountants liaise with budget holders to analyse the management reports to understand key variances against budgets. The outcomes of the monthly reviews are consolidated into monthly financial management reports that are considered by the Board and senior management. The information produced and frequency of reporting aims to ensure decision makers have appropriate information on which to base decisions.

However, following a review of budget monitoring arrangements, we noted concerns with the quality and timeliness of budget monitoring information. This has already been reported in our Interim Management Letter submitted to the Audit Committee on 27 February 2009.

### **ACTION 4**

## People Management

### Staff Governance Action Plan

During the year we carried out a short review with the objective of ensuring that staff governance action plans included reference to matters arising from:

- Staff survey results;
- Mandatory SWISS statistics on people management; and
- Outstanding issues from the previous year's action plan.

We also ascertained whether the current staff governance action plan included timescales, identified who was responsible and set out measurable actions.

Our work revealed that issues had been included in the staff governance action plan where:

- A significant portion of staff survey respondents had not provided a positive response to a question within the survey; and

- Mandatory SWISS statistics indicated action needed to be taken.

There were no outstanding items from the 2007/08 staff governance action plan to be carried forward into the 2008/09 action plan.

All actions noted in the staff governance action plan had clearly assigned responsibilities and where an action was not complete, a timescale for completion was recorded in the action plan.

Based on these findings, we did not recommend that any changes to the staff governance action plan were required.

## Pay Modernisation

We have been informed that all staff at NHS Shetland now have a Personal Development Programme in place. The Board has a benefit realisation plan in place for pay modernisation covering the Board, line managers and staff.

## Agenda for Change

All Agenda for Change (AFC) review requests are now complete. There were 101 initial requests, of which 54 resulted in a higher banding outcome. 5 staff members who have appealed their AFC band are awaiting review. All other appeals have now been dealt with.

The AFC accrual of £0.206 million as at 31 March 2009 covers bank staff, leavers and staff who appealed their bands.

## Equal Pay

The National Health Service in Scotland has received a number of claims for equal pay including related back pay. The NHS Central Legal Office (CLO) has been instructed by the Management Steering Group of the NHS Scotland in this regard and is co-ordinating the legal response of NHS Scotland with this issue.

By the end of May 2009 no formal claims had been registered against NHS Shetland. However, the Board is aware of a number of individuals who may submit claims in future.

During the year there has been a significant development in the legal environment in relation to Equal Pay and Agenda for Change. A test case (Hartley vs. Northumbria Healthcare NHS Foundation) which had been brought claiming that the AFC pay system did not address pay inequalities in the NHS has concluded in the favour of the NHS Foundation. Although this decision may be appealed in future, NHS Shetland believes it has reduced the likelihood of any further Equal Pay claims in respect of Agenda for Change.

In recognition of the Board's potential liability in respect of Equal Pay claims, the financial statements contain a contingent liability disclosure. The wording for this note has been agreed by the CLO Equal Pay Unit and Audit Scotland.

### Sickness Absence

The Scottish Government Health Directorates set a sickness absence target of 4% as at the end of March 2009.

Sickness absence became a standing agenda item for both the Local Partnership Forum and Staff Governance Committee during 2008/09. In addition, the Board monitors sickness absence on a monthly basis with the ability to drill down to individual level. Monthly reports are provided to Senior Management Team and all line managers have a performance objective in this area.

During the course of 2008/09, the Board fell below the target 4% on three occasions. The annual figure for 2008/09 is 4.28%.

### Information Management

Best Value audits are being carried out across the public sector to help protect taxpayers' interests by examining the use of resources and to report on the delivery of outcomes for people who use services. The Best Value

audits are being carried out in a cycle focusing on distinct areas each year. In 2008/09 the Use of Resources Best Value audit focused on Information Management. The Audit of Best Value involved a detailed toolkit drafted by Audit Scotland.

The conclusions from the toolkit provide an assessment of current performance as well as assisting a judgement on the capacity of the service to improve.

A summary of the Board assessment against the 5 key areas of the toolkit is summarised below:

Information Management Toolkit Module	Evaluation
Information Governance and Leadership	Basic Practices
Information for Decision Making	Basic Practices
Service Delivery	Basic Practices
Compliance and Control	Basic Practices
Knowledge Management	Basic Practices

The evaluations for each module are attributed to one of four levels: does not meet basic requirements; basic practices; better practices; and advanced practices.

We identified a series of areas in which the Board's current processes do not yet meet basic practices:

- Senior management do not hold qualifications or an equivalent level of experience in Information Management;
- Benchmarking is not used to measure performance of the service provided by the Information Management & Technology (IM&T) Department;
- Tactical plans are not developed from the information strategy to drive business decisions;
- Information System Investment Programmes are not actively managed to achieve specific business objectives taking into account resources

- and risks;
- A benefits realisation monitoring system is not currently in operation for IM&T projects; and
- The cost of the process of producing information is not calculated.

While the Board has not achieved any areas of advanced practice, we did note a series of areas where the Board is demonstrating better practices.

For example, the Board is working to improve its practices and processes in respect of:

- Senior management's understanding of information risks;
- The Board's leadership in identifying opportunities for sharing information / data and processing systems with other public sector bodies;
- Staff access to training to develop skills in response to new Information Management requirements;
- Collaboration between the Information Management function and service sections of the organisation;
- Senior management's challenge of IM&T strategies;
- Communication between heads of service and the Information Management function to determine the information strategy;
- Quality control checks in information processes;
- Alignment of information processes with the information strategy; and
- Compliance reviews with respect to legislation and standards.

## E-Health Plan

The Board has an approved e-Health plan. The purpose of the plan is to describe the key priority areas for e-health across NHS Shetland and the CHCP for 2009/10. The plan also sets the direction for medium term planning for 2010/2012.

The plan forms part of the e-Health Strategy for NHS Shetland and is aligned to a number of other key policy areas including the LDP which describes the actions put in place to achieve government targets, including the HEAT framework and the national strategic direction for e-health planning.

NHS Shetland intends to use the plan to support an application to the national e-Health team for funding for nationally and locally mandated projects which support the delivery of healthcare services.

# 7. Systems of Internal Control

## Systems of Internal Control

We are required under ISA 260 to report to you any material weaknesses in the accounting and internal control systems, including general computer controls identified during the audit. The results of our work on systems of internal control were communicated to the Audit Committee in our Interim Management Letter.

The report contained 6 recommendations to improve controls, 1 of which was graded as higher risk. This related to authorisation of new users on the NHS Shetland system. However, no risks were identified that could be considered material in nature to the financial statements.

The Board has completed an action plan detailing those individuals responsible for implementing our recommendations and the timetable for completion. We will follow up this action plan during our 2009/10 audit.

## Statement on Internal Control

The Code of Audit Practice requires us to review and report on the Board's Statement on Internal Control.

The Board has used the correct format for its Statement and has outlined the processes it has employed to identify and evaluate risks. In addition, key elements of the Board's control framework have been highlighted.

The Statement also outlines areas where the Board plans to take further action. These include:

- Implement electronic risk management, complaints and incident reporting system by the end of September 2009;
- Increase investment in IM&T which will support improved clinical services;
- Take forward recommendations from the IM&T service review and ensure action is taken to meet information governance standards regarding information security and policy and procedure for systems implementation and business continuity;
- Roll out the encryption process underway on laptops to other mobile devices and desktops;
- Develop performance reporting for individual departments; and
- Develop an enhanced option appraisal methodology particularly in relation to capital projects.

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

## Audit Issues

During our final audit visit, we noted a number of control issues. These related to Service Level Agreement charges, theatre stock valuations and Fixed Asset Register reconciliations.

These issues will be reported to management in a separate Final Management Letter.

## Follow up of outstanding recommendations

We followed up the Board's progress in implementing recommendations made in the prior year. Our Follow Up Report was considered at the Audit Committee meeting on 26 March 2009.

At the time of reporting, of the 32 agreed actions, progress was as follows:

Status	Annual Report to Members 2007/08	Interim/Final Management Report 2007/08	Follow Up Report 2007/08	Total
Action Implemented	1	6	6	<b>13</b>
Action in Progress	2	4	3	<b>9</b>
Limited/Little Progress to Date	2	0	3	<b>5</b>
No Longer Applicable	0	0	2	<b>2</b>
Not yet due	0	2	1	<b>3</b>
<b>Total</b>	<b>5</b>	<b>12</b>	<b>15</b>	<b>32</b>

Overall, the Board had fully implemented 13 recommendations from the reports issued in 2007/08. While some action had been taken on a further 9 of the 29 recommendations due, a total of 17 recommendations remained outstanding at the time of reporting to the March Audit Committee. Progress is therefore considered to be slower than anticipated. While progress has been made in some areas, a large amount of work is required in order to fully implement all audit recommendations. We intend to bring forward our planned full review of progress; we have agreed with management that we will now report on the findings from this in November 2009, rather than March 2010 as originally planned.

### ACTION 6

## National Fraud Initiative

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

A total of 113 matches were identified by NFI for review by the Board. At the date of reporting, it was noted that only one match relating to a Payroll to UK Visa match had been opened and investigated. This relates to an individual who left the Board's employment in December 2008. We have been informed that the NFI team has agreed to undertake investigation into this issue on the Board's behalf. This was the only recommended match.

Investigations into other matches have yet to commence. As the Board has been in possession of this data for some time, we would expect more than one match to have been investigated and we will continue to liaise with the NFI Key Contact at the Board throughout the year in order to ensure that the matches are investigated appropriately. The outcomes of the NFI exercise will be reported in 2010.

### ACTION 7

## Internal audit

The role of internal auditing is determined by management and therefore its objectives differ from ours. It is part of our approach to gain an understanding of the internal audit function to determine if it would be effective and efficient to use their work.

Deloitte took up their role as the Board's internal auditors in 2008/09. We have reviewed the work of internal audit and have, where appropriate, placed reliance on their work.

# Appendix A – Action Plan

Ref	Issue and Recommendation	Management Response
1	<p><b>Finding:</b></p> <p>While we did receive a draft set of financial statements at the start of our audit fieldwork, the majority of areas were not complete and therefore required further amendments by management before our audit work could commence. Additions and changes to the statements continued throughout our final audit visit, even during the third and final week of our visit.</p> <p>In addition, almost all areas of the draft financial statements could not be agreed to underlying accounting records or working papers and supporting working papers were not of an appropriate standard.</p> <p><b>Recommendation:</b></p> <p>NHS Shetland should put in place effective arrangements relating to its accounts closure and preparation process for 2009/10. In particular, management should ensure that working papers accurately reflect underlying accounting records and that clear details are provided to explain the composition of the disclosures in each lead schedule.</p> <p>In order to ensure accuracy of lead schedules and supporting papers, management should carry out a thorough review prior to presenting these to us for audit.</p> <p>Accurate and complete financial statements should be available when agreed and any adjustments should be made in a logical and controlled manner.</p>	<p><b>Management Response:</b></p> <p>The Finance staff worked extremely hard to produce accounts in difficult circumstances and to a tighter schedule than previous years.</p> <p>We have changed our ledger twice in the space of ten months (across two financial years). The second change involved a change in working practices (moving to a consortium-led system) which also required a full rewrite of all cost centres and several account codes. At the same time we have restructured the Finance Team and experienced significant staff turnover. Two of the key staff for the final accounts process were in new roles. The errors that occurred during the process were a product of the extent of the changes in staff and systems in the department coupled with time pressures arising from the changes. In turn, these errors led to a need for amendments to the financial statements and lead schedules during the audit. This is clearly regrettable and we acknowledge the impact this would have had on audit – however, it should be recognised that we had three weeks fewer to produce a first draft compared with last year. Accounts were completed in time for them to be issued a week before the Board meeting – which is a significant improvement on previous years. We would anticipate fewer errors next year with a more settled system and hopefully more settled team who now have a more thorough</p>

Ref	Issue and Recommendation	Management Response
		<p>understanding of the year-end process. We acknowledge the need for improved working papers and a more thorough review of these. We would welcome some advice from audit as to the standard they expect (preferably based on real-life examples from another NHS Board). The time pressures felt from changing systems should alleviate for next year's accounts, giving more time for review.</p> <p>We will liaise closely with audit regarding the timing of next year's visit. Our view is that consideration should be given to audit arriving one week later than this year to allow more time for a management review of the first draft and therefore fewer alterations to subsequent drafts.</p> <p>The Director of Finance will conduct a post-accounts review of the process in liaison with external audit to identify what could have been done better and lessons to be learnt. Any necessary actions will be built into the Finance Manager's objectives. This will include a training needs analysis of the Finance Team to identify any gaps in knowledge that need addressing. We will seek advice from external audit regarding other Boards viewed as 'good examples' to potentially learn from.</p> <p><b>Responsible Officer:</b> DoF will conduct the review by Sep 2009 Finance Manager will implement agreed actions</p> <p><b>Due Date:</b> For 2009/10 accounts – including preparatory dialogue with external audit</p>
2	<p><b>Finding:</b> Practitioner Services Division (PSD) reports on Family Health Services (FHS) income and expenditure. The NHS Shetland general ledger is not currently being reconciled to this information on a regular monthly basis. As a result, management had difficulty in explaining all differences in the year end reconciliations leading to delays and errors in</p>	<p><b>Management Response:</b> Agreed. We have already put steps in place to ensure that these are reconciled monthly. Last year, due to staff changes and</p>



Ref	Issue and Recommendation	Management Response
	<p>the financial statements.</p> <p><b>Recommendation:</b></p> <p>NHS Shetland should ensure that all FHS reconciliations are completed on a monthly basis. The reconciliations should be reviewed by an appropriate member of management on a timely basis to ensure the information in the ledger is accurate and up to date. This will reduce the likelihood of encountering unexplained differences in year end reconciliations or expenditure being omitted from the financial statements, as was the case in 2008/09.</p>	<p>then system changes, the reconciliations were delayed. We sought help from another Board during the year but unfortunately this did not produce an effective result. We have transferred this task to the Management Accounts section who are closer to the detail and in regular contact with budget holders.</p> <p><b>Responsible Officer:</b></p> <p>Finance Manager</p> <p><b>Due Date:</b></p> <p>Reconciliations will be done on a monthly basis. Aim to do April and May by end June and then build this into the regular monthly management accounting work.</p>
3	<p><b>Finding:</b></p> <p>The Board's year end surplus position of £0.390 million has been largely achieved because of the agreement of Shetland Islands Council to reduce £0.775 million of the planned Resource Transfer amount and through the carry forward from the previous year of a £0.976 million surplus. It should be noted that the Board had paid £1 million during 2008/09 but post year end agreed with the Council that £0.575m of this could be returned to off-set the impact of an audit adjustment to the expenditure position and accruals balance in the draft 2008/09 financial statements.</p> <p>Without the agreement of the Council to abate the Resource Transfer, the Board would be in deficit against its Revenue Resource Limit target as set by SGHD.</p> <p>In addition, the Board is forecasting that it will continue to be in an underlying recurring deficit position for 2009/10.</p> <p><b>Recommendation:</b></p> <p>NHS Shetland has acknowledged the need to return the underlying financial position to one of recurring surplus. In order to achieve this, the Board should consider widening the scope of existing efficiency and savings plans significantly. This would allow the Board to reduce its reliance on its non-recurring surplus in general and the abatement of the Resource Transfer in particular in order to achieve an overall surplus position.</p>	<p><b>Management Response:</b></p> <p>Agreed.</p> <p>Audit identify in this report that the Board's non-recurring funding represents around 20% of the total and that this is high compared with other Boards. It is important to point out that the non-recurring funding includes around £1.9m for the Highland &amp; Islands Travel Scheme. This is technically non-recurring as it is not part of the recurring baseline. However, in reality this funding is recurring in nature. Taking this into account would reduce the percentage of non-recurring funding to around 16%. In addition, the funding for primary medical services has been treated as non-recurring. Again this is technically not part of the recurring baseline although it is recurring in nature. It is possible that other Boards may have treated this as recurring when analysing their funding - therefore comparisons need to be made with care. Nevertheless the Board fully accepts a need to reduce its reliance on non-recurring measures.</p> <p>The Board had agreed in principle with SIC that the £1.2m</p>

Ref	Issue and Recommendation	Management Response
		<p>would be fully abated in 2008/09. However, as the financial outturn was forecast to better than expected the Board was able to make a payment of £1m during 2008/09. Clearly, the discovery of the error in relation to prescribing changed the Board's draft outturn and therefore required a renegotiation of the payment made to SIC in 2008/09. The Board is fully aware that the reliance on this arrangement represents a significant risk to its financial plans.</p> <p>The Board has a balanced plan for 2009/10 although it is acknowledged that this continues to rely on non-recurring measures.</p> <p>Preliminary work has already begun on a savings plan for 2010/11. This has been discussed by Senior Management Team and at a Board Information session. It is intended to discuss this with the Local Partnership Forum on 25/06/09 and then report to the SGHD by 30/06/09. At the moment the Board is working towards the savings target agreed with the SGHD as part of its Local Delivery Plan (LDP). It is acknowledged that there is a risk that savings requirements may increase in 2010/11 as a result of the overall economic position – however, the initial task facing the Board is to identify savings sufficient to meet the LDP requirements. So far, we have identified in principle around £0.350 million of the £1 million savings required by the LDP in 2010/11. As regards widening the range – the Board is already looking across the whole range of its services and all departmental heads have been charged with identifying savings in their areas. The Board is becoming an early adopter of LEAN and aims to apply this across the Board. To deliver additional savings therefore requires looking 'deeper' rather than 'wider'.</p> <p><b>Responsible Officer:</b> Director of Finance</p>

Ref	Issue and Recommendation	Management Response
		<b>Due Date:</b> Ongoing throughout 2009/10
4	<p><b>Finding:</b></p> <p>Budget monitoring reports are not produced in a high level of detail and are not always received by budget holders on time. Furthermore, training has not been provided to all budget holders to ensure that they can interpret the information being provided to them. In the absence of good quality budget monitoring information, it is difficult for management to identify and address the causes of overspends.</p> <p><b>Recommendation:</b></p> <p>The quality of information and training provided to budget holders has a critical role to play in the budget monitoring process. The level of detail contained in budget monitoring reports should therefore be reconsidered and an effort should be made to ensure reports are available on a timely basis. Documented procedures should be established for budget monitoring and used to meet budget holders' training requirements.</p>	<p><b>Management Response:</b></p> <p>Agreed.</p> <p>A new Management Accounting Manager has been recruited and is due to start September 2009. The Management Accountant and temporary staff employed have been ensuring that budget statements do go out on time and they are working on redesigning reports. Since the interim audit (when this was checked), training has been given to heads of departments and their staff and procedures will be developed. The new system allows a great deal of information to be provided and in fact some of the feedback we have had from budget holders is that we are providing too much detail – hence the need to redesign reports. Budget reports are much more timely than in previous years and we will continue to work to improve on this. We are sending out the first statements of the new year on 22 June compared with the end of July in previous years. Reports to the Board are now generally comprising information that is one month more up to date when compared with the equivalent meeting in the previous year.</p> <p>As part of the redesign process we will engage with budget holders in order to understand their requirements.</p> <p><b>Responsible Officer:</b>  Finance Manager</p> <p><b>Due Date:</b>  September 2009</p>
5	<p><b>Finding:</b></p> <p>The Board has taken the decision to disband the post of Director of Service Improvement (DSI) which has been vacant since March 2009. Responsibilities will be</p>	<p><b>Management Response:</b></p> <p>Agreed. Responsibilities have been transferred from May 2009 and this will be kept under review.</p>

Ref	Issue and Recommendation	Management Response
	<p>transferred to other members of the Senior Management Team.</p> <p><b>Recommendation:</b> A complete and stable executive management team is an essential component of NHS Shetland's ability to deliver a robust governance framework. The Board should therefore ensure that the Senior Management Team has sufficient capability to discharge all responsibilities and to meet future challenges around service delivery without the post of DSI.</p>	<p><b>Responsible Officer:</b> Chief Executive</p> <p><b>Due Date:</b> Ongoing</p>
6	<p><b>Finding:</b> A total of 17 external audit recommendations remain outstanding from previous year reports, including 6 high risk recommendations as follows:</p> <ul style="list-style-type: none"> <li>• The user lockout facility should be utilised for all desktops;</li> <li>• NHS Shetland should put in place more effective arrangements relating to its accounts closure and preparation process;</li> <li>• The Revenue Transfer abatement from Shetland Islands Council should be secured on a more formal and recurring basis;</li> <li>• Any known trends or spikes in expenditure e.g. winter pressures should be included in budgets to enhance their precision and hence the accuracy of the budgetary control statements;</li> <li>• Staff within the Payroll department should consider beginning to draw up procedures to cover the key processes. These should be documented and stored on the shared Finance drive so that they can be referred to by any temporary members of staff who may be drafted in as cover; and</li> <li>• The Authorised Signatory Listing should be updated by the Payroll Department to reflect all those who have delegated authority to sign off timesheets.</li> </ul> <p><b>Recommendation:</b> Management should take more concerted action against previously raised recommendations, particularly in relation to those noted as high risk, to ensure that all actions are achieved in line with original timescales.</p>	<p><b>Management Response:</b> Agreed.</p> <p>This issue was discussed at the Audit Committee meetings in March and May. We had agreed with audit that a verbal update would be given to the May Committee meeting (which was done). We have agreed that a further written update on progress should be provided to the November Committee meeting.</p> <p>Progress against the recommendations is being monitored at Senior Mgt Team meetings.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Due Date:</b> Due date – varies depending on the recommendation but aiming for a full update on progress to November Audit Committee.</p>
7	<p><b>Finding:</b> The National Fraud Initiative (NFI) has identified a total of 113 matches were identified</p>	<p><b>Management Response:</b> Agreed.</p>

Ref	Issue and Recommendation	Management Response
	<p>for review by the Board. The majority of these are payroll to payroll matches. However, only one of these matches has been fully investigated, despite the Board having been in possession of the information for some time.</p> <p><b>Recommendation:</b></p> <p>If prompt action is not taken to investigate all NFI matches, it is possible for fraud to persist, even though the Board has in its possession information to prevent it. The Board should therefore ensure that all matches are investigated in order to understand the level of exposure to payroll-related fraud.</p>	<p>We had explained to audit the background to this and we have produced an update for the Audit Committee on 26 June. We aim to have finished the preliminary investigation of all matches by end of July. Detailed investigations may take longer depending on the nature of the issue to follow up. The delay in exploring matches is due to the fact that all but one of the matches requires payroll input and the payroll team have been prioritising Agenda for Change processing as well as carrying a vacancy until very recently. All matches have already been reviewed by the Director of Finance but it is acknowledged that a more formal review is required as soon as possible.</p> <p>The one high risk match (relating to an individual who left the Board in December 2008) has now been referred to the Home Office on the advice of the NFI Team.</p> <p><b>Responsible Officer:</b></p> <p>Director of Finance</p> <p><b>Due Date:</b></p> <p>Initial findings by end of July. Detailed investigations by end September depending on the complications arising from the need to comply with the Data Protection Act.</p>

# Appendix B – Communications to Management

International Standard on Auditing (“ISA”) (UK&I) 260 – Reporting to those charged with Governance, requires that the External Auditor communicates certain matters to those charged with governance.

Those charged with Governance is taken to be the Members of the Audit Committee with responsibility discharged through the regular meetings of the Audit Committee during the year. Summarised below are the requirements set out within ISA 260 together with reference to the relevant communication with you during 2008/09 or comments as appropriate.

Communication Required under ISA 260	Reference/Comment
Engagement letters	Signed Engagement Letter with Audit Scotland at the start of our 5 year appointment and updated annually.
Independence	Audit Planning document reported to 26 March 2009 Audit Committee and confirmed no member of audit team has any direct interest, financial or otherwise, in NHS Shetland.
Audit Approach and Scope	Audit Planning document (reported to Audit Committee 26 March 2009).
Accounting Policies/Practices with a Material Effect on the Financial Statements	Section 3 of our Annual Report to Board Members and the Auditor General for Scotland.
Potential Effects of Material Risks and Exposures	Audit Planning document (26 March 2009).
Audit Adjustments	Section 3 of our Annual Report to Board Members and the Auditor General for Scotland.
Material Uncertainties relating to Going Concern	None identified.
Disagreement with Management about Matters	Not applicable.

Communication Required under ISA 260	Reference/Comment
that could be Significant to the Financial Statements	
Expected Modifications to the Auditor's Report	No modifications identified. A true and fair opinion provided.
Letter of Representation	Signed by Management June 2009.
Material Weaknesses in Internal Control	Internal Controls findings reported separately in our Interim Management Letter (26 March 2009), Section 7 of our Annual Report to Board Members and the Auditor General for Scotland and
Fraud	Discussed fraud arrangements with the Chair of the Audit Committee (26 March 2009), Management throughout audit process.
Laws and Regulations	We have not identified any material breaches of laws and regulations in the period which impact on the 2008/09 Financial Statements.
Audit Materiality	Audit Planning document – presented to Audit Committee in 26 March 2009
Fair Value Measurement and Disclosure	Included in representation letter, signed by management dated June 2009
Related Parties	Other than those transactions disclosed in the financial statements we have not identified any further transactions requiring disclosure.

### Formal Reporting to Management during 2008/09

During the year we have presented a number of formal reports to Management and the Audit Committee and produced certain outputs. Our principal outputs during 2008/09 are summarised below:



Formal Output	Timing								
Audit Plan	March 2009								
Interim Accounts – Audit Opinion	March 2009								
Detailed Timetable for 2008/09 Financial Audit	March 2009								
IFRS Opening Balance Sheet Letter	February 2009								
Follow-up of 2007/08 Recommendations	March 2009								
Interim Management Letter	March 2009								
Letter to Director of Workforce regarding the process for preparation of the Staff Governance Action Plan	April 2009								
Annual Report to Board Members and the Auditor General for Scotland	June 2009								
<p>Audit Opinions</p> <table border="0"> <tr> <td data-bbox="188 879 772 911">1. True and fair view on the financial statements</td> <td data-bbox="817 879 851 903">✓</td> <td data-bbox="862 879 929 1007" rowspan="3" style="font-size: 3em; vertical-align: middle;">}</td> <td data-bbox="952 911 1093 1007" rowspan="3">Unqualified Audit Opinions</td> </tr> <tr> <td data-bbox="188 927 683 959">2. Regularity of income and expenditure</td> <td data-bbox="817 927 851 951">✓</td> </tr> <tr> <td data-bbox="188 975 616 1007">3. Remuneration Report (sections)</td> <td data-bbox="817 975 851 999">✓</td> </tr> </table>	1. True and fair view on the financial statements	✓	}	Unqualified Audit Opinions	2. Regularity of income and expenditure	✓	3. Remuneration Report (sections)	✓	June 2009
1. True and fair view on the financial statements	✓	}			Unqualified Audit Opinions				
2. Regularity of income and expenditure	✓								
3. Remuneration Report (sections)	✓								

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

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

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