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# Introduction

## The key messages in this report:

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

We have pleasure in presenting our draft planning report to the Audit Committee for the year ending 31 March 2019 audit. We would like to draw your attention to the key messages of this draft audit plan:

### **Audit Plan**

We have updated our understanding of the Board including discussion with management and review of relevant documentation from across the Board.

We are aware of the planned organisational changes in relation to the forming of a new 'Public Health Scotland' body, although we note the 'go live' date has slipped from 1 April 2019 to 1 December 2019. We will monitor preparations for transition and keep abreast of developments, and consider their implications for the Board, as they arise over the coming year.

Based on these procedures, we have developed this plan in collaboration with the Board to ensure that we provide an effective audit service that meets your expectations and focuses on the most significant areas of importance and risk to the Board.

### **Key Risks**

We have taken an initial view as to the significant audit risks the Board faces. These are presented as a summary dashboard on page 13.

- As with other public sector bodies, NHS Health Scotland continues to face financial challenges, due to uncertainty around future funding.

- As at 30 September 2018, NHS Health Scotland is showing an underspend of £233k but is forecasting to break even with its Revenue Resource Limit (RRL) of £19,790k by year end. The achievement of a breakeven position will be a key focus of our audit.
- Our significant audit risk is pinpointed to accruals and prepayments made at the year-end.
- In accordance with auditing standards, management override of controls has also been identified as a significant audit risk.
- In line with our prior year audits, having considered the risk factors set out in Auditing Standards and the nature of the revenue streams at NHS Health Scotland, we have determined that the presumed risk of fraud arising from revenue recognition can be rebutted. This is based on the fact that there is little incentive or opportunity to manipulate revenue recognition with the majority of revenue being from the Scottish Government which can be agreed to confirmations supplied.

# Introduction (continued)

## The key messages in this report (continued):

### **Audit Dimensions**

The Code of Audit Practice sets our four audit dimensions which set a common framework for all public sector audits in Scotland. These are financial sustainability, financial management, governance and transparency and value for money. Due to the relative size and scale of the functions delivered by NHS Health Scotland, we have concluded that the full wider scope of audit is not appropriate. In accordance with paragraph 53 of the Code, our work in this area will therefore be restricted to concluding on:

- The appropriateness of the disclosures in the governance statement; and
- the financial sustainability of the Board and the services that it delivers over the medium to longer term.

The potential audit risks associated with the wider scope are detailed in pages 16 – 17 .

Our audit work on the audit dimensions incorporates the specific risks highlighted by Audit Scotland, in particular: the impact of EU withdrawal; the changing landscape for public financial management; dependency on key suppliers; and increased focus on openness and transparency.

### **Regulatory Change**

New accounting standards on revenue and financial instruments will apply for 2018/19, and for leases from 2019/20. We recommend that the Board review the impact of IFRS 9 and 15 early in the year, including calculating any adjustments that will be required as at 31 March 2019 for transition. We would suggest that the Audit Committee receive reporting in year from management on the implementation of the new standard, and we will report specifically on the findings from our audit work in this area.

We have reported on other regulatory changes in our sector updates in our separate report.

### **Our Commitment to Quality**

We are committed to providing the highest quality audit, with input from our market leading specialists, sophisticated data analytics and our wealth of experience.

### **Adding value**

Our aim is to add value to the Board through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Board promote improved standards of governance, better management and decision making and more effective use of resources.

**Pat Kenny**  
**Audit Director**

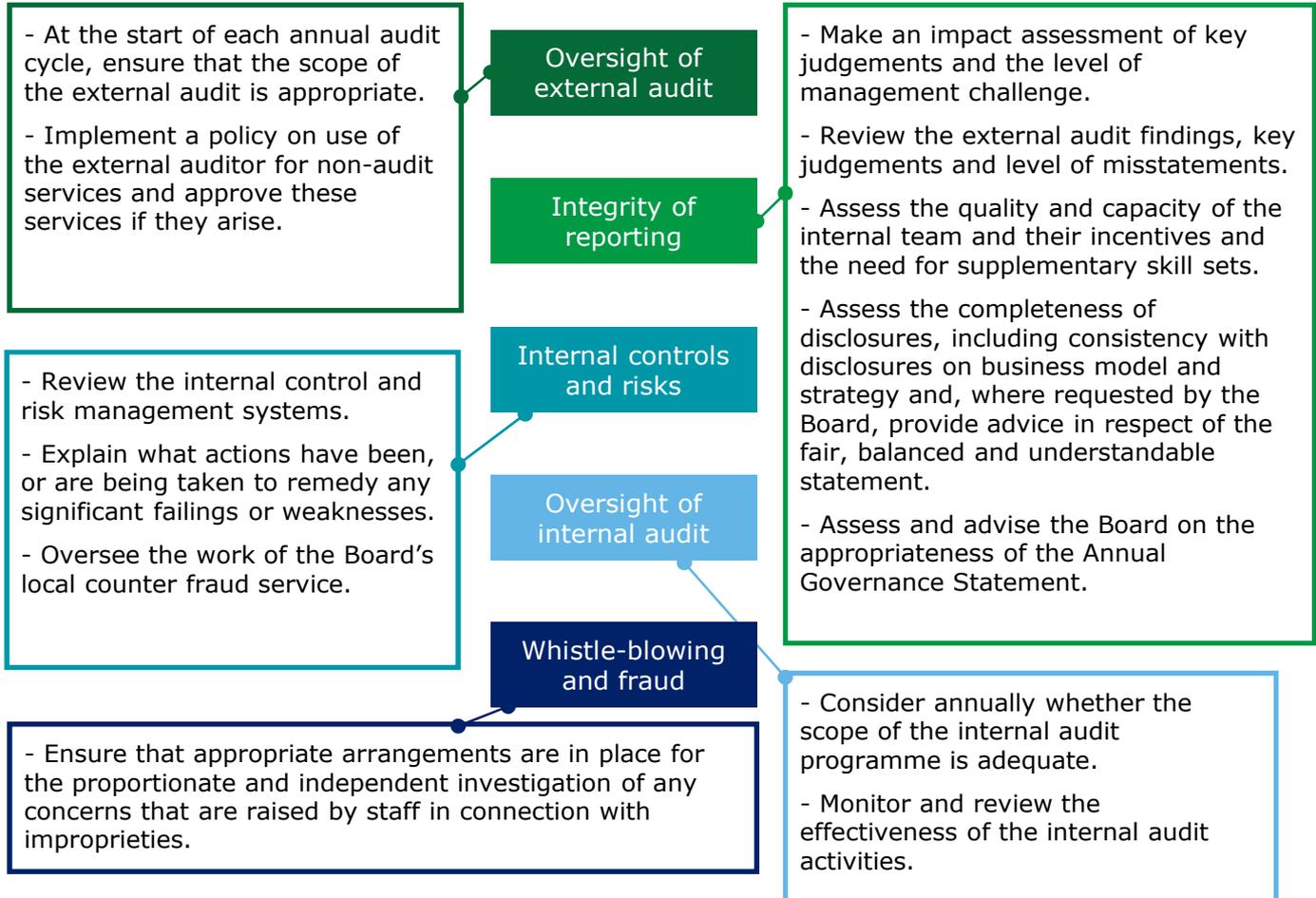
# Responsibilities of the Audit Committee

## Helping you fulfil your responsibilities

The primary purpose of the Auditor's interaction with the Audit Committee:

- Clearly communicate the planned scope of the financial statements audit.
- Provide timely observations arising from the audit that are significant and relevant to the Audit Committee's responsibility to oversee the financial reporting process.
- In addition, we seek to provide the Audit Committee with additional information to help fulfil your broader responsibilities.

As a result of regulatory change in recent years, the role of the Audit Committee has significantly expanded. We set out here a summary of the core areas of Audit Committee responsibility to provide a reference in respect of these broader responsibilities and highlight throughout the document where there is key information which helps the Audit Committee in fulfilling its remit.



# Our audit explained

## We tailor our audit to your Board and your strategy

### Identify changes in your Board and environment

Despite historically underspending against the RRL, as with all NHS bodies, the Board continues to face significant financial pressures, impacting on the achievement of the corporate objectives around reducing health inequalities and improving health. The long term impact on these objectives from the transition to a new Public Health Scotland body are unknown at this stage.

A summary of these considerations is set out on page 8.

### Scoping

Our scope is in line with the Code of Audit Practice issued by the Audit Scotland.

More detail is given on page 10.

### In our final report

In our final report to you we will conclude on the significant risks identified in this paper, report to you our other findings, and detail those items we will be including in our audit report.



### Determine materiality

We have determined a materiality of £387k (2017/18: £394k). This is based on forecasted gross expenditure, consistent with the basis used in the prior year. We have determined a performance materiality of £328k (2017/18: £295k), which is 85% of materiality (2017/18: 75%), increased in the current year due to the low history of error and the risk profile of the Board.

We will report to you any misstatements above £19k (2017/18: £20k). Any errors identified will be considered in the context of meeting the RRL.

### Significant risk assessment

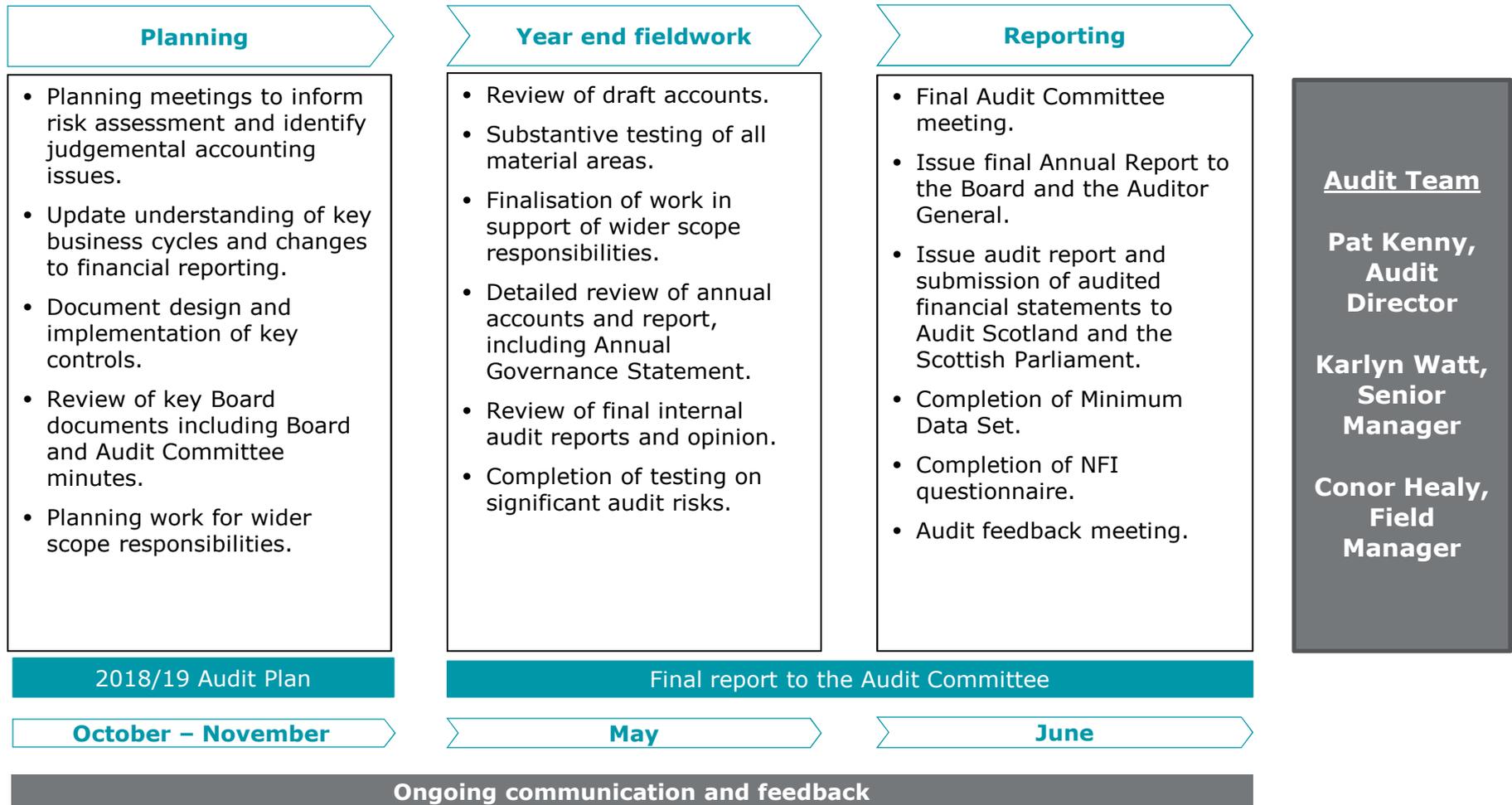
We have identified two significant audit risks in relation to the Board. More detail is given on page 12 to 15. These are consistent with our prior year audit.

### Quality and Independence

We confirm all Deloitte network firms are independent of NHS Health Scotland. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority.

# Continuous communication and reporting

## Planned timing of the audit



# An audit tailored to you

## Focusing on your business and strategy

### Description

### Impact on our audit

Performance against expenditure resource limit



There is a financial duty for NHS Health Scotland to comply with its RRL. As at 30 September 2018, NHS Health Scotland is showing an underspend of £233k (represented by £274k of staff savings, offset by an overspend of £41k on projects) against budget. However, the Board is forecasting to meet its RRL target by year end, given concern that any under utilisation of the funding in the current year could result in longer-term funding reductions. Our significant audit risk has been pinpointed to accruals and prepayments at the year end as these areas have a higher risk of management override as discussed further on page 15.

We will consider the Board's financial sustainability in the medium to longer term and consider whether it is planning effectively to continue to deliver its services on a sustainable basis, including progress towards outcome based planning/budgeting, as discussed further on page 16. This will include consideration of the transition to the new Public Health Scotland body and the impact that this will have on the Board and its services.

We will also monitor the Board's savings plans and its contribution to the national savings plan to assess whether the impact of savings has been fully identified, mitigated and planned for, linking to its achievement of corporate priorities discussed below.

Achievement of corporate priorities



Many of the risks highlighted in the Risk Register that the organisation considers its key risks to be relate to the lack of achievement of its corporate priorities through ineffective organisational performance management. It was highlighted in the Annual Report and Accounts for 2017/18 that the Board achieved 71% (2016/17: 66%) of its corporate objectives. The Board identified that the main cause for not achieving all of the objectives was a lack of staff capacity, with inadequate prioritisation and difficulties recruiting and retaining specialist staff consistently ranking highly on the Board's risk register.

It is a key objective for NHS Health Scotland to review staff capacity and conduct analysis of the causes of project overruns to tackle these issues and fully achieve its corporate priorities in the current financial year. This was also an objective in the prior year and resulted in a marked improvement (from 66% to 71% objectives achieved), with capacity issues accounting for 35% of incomplete objectives (down from 53% in 2016/17). We will consider how this is progressed in the current year as part of our review of the arrangements in place to monitor the impact of savings plans as discussed above.



New significant risk



Continuing significant risk



Considered as part of wider scope audit requirements

# Materiality

## Our approach to materiality

### Basis of our materiality benchmark

- The audit director has determined materiality as £387k (2017/18: £394k) and a performance materiality of £328k (2017/18: £295k), based on professional judgement and risk factors specific to NHS Health Scotland, the requirement of auditing standards and the financial measures most relevant to users of the financial statements.
- We have used 2% of forecasted gross expenditure as the benchmark for determining materiality and applied 85% as performance materiality.
- This approach is consistent with our prior year materiality calculation. We have increased the percentage applied as performance materiality given the low history of error and the level of risk faced by the Board.

### Reporting to those charged with governance

- We will report to you all misstatements found in excess of £19k (2017/18: £20k).
- Any errors identified will be considered in the context of

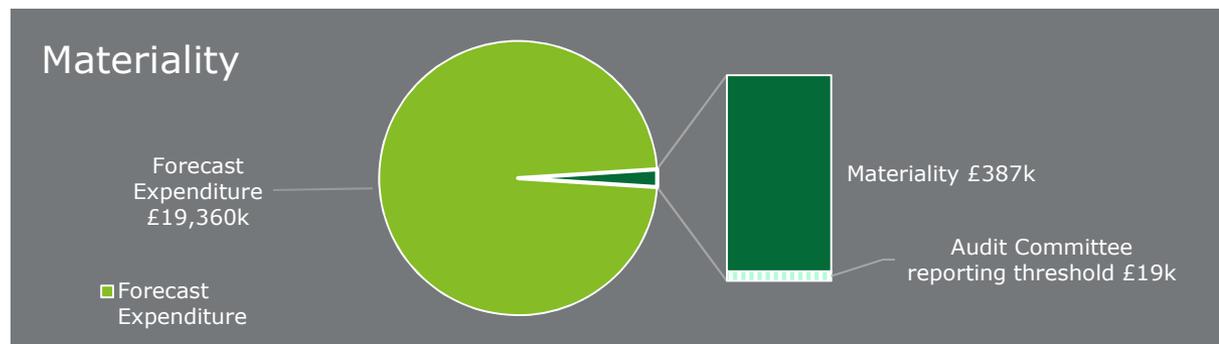
meeting the RRL.

- We will report to you misstatements below this threshold if we consider them to be material by nature.
- Our approach to determining the materiality benchmark is consistent with Audit Scotland guidance, which states that the threshold for clearly trivial above which we should accumulate misstatements for reporting and correction to audit committees must not exceed £250k.

### Our annual audit report

We will:

- Report the materiality benchmark applied in the audit of the Board;
- provide comparative data and explain any changes in materiality, compared to prior year, if appropriate; and
- explain any normalised or adjusted benchmarks we use, if appropriate.



Although materiality is the judgement of the Audit Director, the Audit Committee must satisfy themselves that the level of materiality chosen is appropriate for the scope of the audit.



# Scope of work and approach

## Our key areas of responsibility under the Code of Audit Practice

Core audit work	Planned output	Timeline
Perform an ISA (UK) compliant audit of the annual accounts	<ul style="list-style-type: none"> <li>Annual audit plan</li> <li>Interim report (if required)</li> <li>Independent auditor's report</li> </ul>	<ul style="list-style-type: none"> <li>November 2018</li> <li>March/April 2019</li> <li>June 2019</li> </ul>
Audit and report on the audit dimensions	<ul style="list-style-type: none"> <li>Annual audit plan</li> <li>Annual audit report</li> </ul>	<ul style="list-style-type: none"> <li>November 2018</li> <li>June 2018</li> </ul>
Contribute to performance audits (including performance audit reports, overview reports and impact reports)	<ul style="list-style-type: none"> <li>Minimum datasets</li> <li>Data returns</li> </ul>	<ul style="list-style-type: none"> <li>June 2019</li> <li>As required</li> </ul>
Share intelligence with health and social care national agencies	<ul style="list-style-type: none"> <li>Intelligence template</li> </ul>	<ul style="list-style-type: none"> <li>As required</li> </ul>
Share audit intelligence with Audit Scotland including highlighting potential statutory reports	<ul style="list-style-type: none"> <li>Current issues returns</li> </ul>	<ul style="list-style-type: none"> <li>January 2019</li> </ul>
Carry out preliminary enquiries into referred correspondence	<ul style="list-style-type: none"> <li>None</li> </ul>	<ul style="list-style-type: none"> <li>N/A</li> </ul>
Provide information on cases of money laundering	<ul style="list-style-type: none"> <li>Audit Scotland to advise</li> </ul>	<ul style="list-style-type: none"> <li>As required</li> </ul>
Contribute to National Fraud Initiative (NFI) report	<ul style="list-style-type: none"> <li>NFI audit questionnaire</li> <li>Reference, if necessary, in annual audit report</li> </ul>	<ul style="list-style-type: none"> <li>June 2019</li> </ul>
Contribute to technical guidance notes	<ul style="list-style-type: none"> <li>Consultation comments on draft technical guidance notes</li> </ul>	<ul style="list-style-type: none"> <li>As required</li> </ul>

# Scope of work and approach (continued)

## Our approach

### Liaison with internal audit

The Auditing Standards Board's version of ISA (UK) 610 "Using the work of internal auditors" prohibits use of internal audit to provide "direct assistance" to the audit. Our approach to the use of the work of Internal Audit has been designed to be compatible with these requirements.

We will review their reports and meet with them to discuss their work. We will discuss the work plan for internal audit, and where they have identified specific material deficiencies in the control environment we consider adjusting our testing so that the audit risk is covered by our work.

Using these discussions to inform our risk assessment, we can work together with internal audit to develop an approach that avoids inefficiencies and overlaps, therefore avoiding any unnecessary duplication of audit requirements on the Board's staff.

### Approach to controls testing

Our risk assessment procedures will include obtaining an understanding of controls considered to be 'relevant to the audit'. This involves evaluating the design of the controls and determining whether they have been implemented ("D&I").

The results of our work in obtaining an understanding of controls and any subsequent testing of the operational effectiveness of controls will be collated and the impact on the extent of substantive audit testing required will be considered.

### Promoting high quality reporting to stakeholders

We view the audit role as going beyond reactively checking compliance with requirements: We seek to provide advice on evolving good practice to promote high quality reporting.

We have also designed and continually update International Financial Reporting Standards ("IFRS") disclosure checklists in conjunction with the requirements of the FReM to support the Board in preparing high quality drafts of the Annual Report and Accounts, which we would recommend the Board complete during drafting.

We will continue to review an early draft of the Annual Report ahead of the typical reporting timetable to feedback any comments to management and the Audit Committee.

Audit Scotland has published good practice guides in relation to the Annual Report and the Governance Statement to support the Board in preparing high quality drafts of the Annual Report and Accounts, which we would recommend the Board consider during drafting.

Obtain an understanding of the Board and its environment including the identification of relevant controls.

Identify risks and controls that address those risks.

Carry out D&I work on relevant controls.

If considered necessary, test the operating effectiveness of selected controls

Design and perform a combination of substantive analytical procedures and tests of details that are most responsive to the assessed risks.

# Significant risks

## Our risk assessment process

We consider a number of factors when deciding on the significant audit risks. These factors include:

- The significant risks and uncertainties previously reported in the Annual Report and Accounts;
- the IAS 1 critical accounting estimates previously reported in the Annual Report and Accounts;
- our assessment of materiality;
- the changes that have occurred in the business and the environment it operates in since the last Annual Report and Accounts; and
- the Board's actual and planned performance on financial and other governance metrics compared to its peers.

### Principal risk and uncertainties

- Staffing recruitment and retention.
- Keeping pace with digital and ICT advancements.
- Data loss.
- Regulatory changes.
- Economic environment.
- The impact of EU withdrawal.

### IAS 1 Critical accounting estimates

- Impairment of fixed assets
- Provisions and contingencies

### Changes in your business and environment

- Establishment of 'Public Health Scotland'.
- Potential difficulties retaining key staff through transition.

The next page summarises the significant risks that we will focus on during our audit. All of the risks mentioned in the prior year Audit Committee report are included as significant risks in this year's audit plan.



# Significant risks Dashboard



Risk	Material	Fraud risk	Planned approach to controls testing	Level of management judgement	Page no.
Achievement of expenditure resource limits			Design and implementation		14
Management override of controls			Design and implementation		15



Some degree of management judgement

# Significant risks (continued)

## Risk 1 – Achievement of expenditure resource limits

### Key focus for management

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**Risk identified**

There is a key financial duty for NHS Health Scotland to comply with the Revenue Resource Limit set by the Scottish Government.

The risk is therefore that NHS Health Scotland materially misstates expenditure in relation to year end transactions, in an attempt to align with its tolerance target or achieve a breakeven position. The significant risk is therefore pinpointed to accruals and prepayments made by management at the year end and invoices processed around the year end as this is the area where there is scope to manipulate the final results. Given the financial pressures across the whole of the public sector, there is an inherent fraud risk associated with the recording of accruals and prepayments around year end.

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**Our response**

We will evaluate the results of our audit testing in the context of the achievement of the target set by the Scottish Government.

Our work in this area will include the following:

- Obtain independent confirmation of resource limits allocated to NHS Health Scotland by the Scottish Government;
  - perform design and implementation testing on the key controls which cover this risk;
  - perform focussed testing of accruals and prepayments made at the year end; and
  - perform focussed cut-off testing of invoices received and paid around the year end.
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# Significant risks (continued)

## Risk 2 – Management override of controls

We will use computer assisted audit techniques, including Spotlight, to support our work on the risk of management override

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### **Risk identified**

In accordance with ISA 240 (UK) management override is a significant risk. This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Board's controls for specific transactions.

The key judgments in the financial statements are those which we have selected to be the significant audit risk around expenditure recognition. This is inherently the areas in which management has the potential to use their judgment to influence the financial statements.

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### **Planned audit challenge**

In considering the risk of management override, we plan to perform the following audit procedures that directly address this risk:

#### **Journal testing**

- We will test the design and implementation of controls over journal entry processing;
- we will perform design and implementation testing on the key controls which cover this risk;
- using our Spotlight data analytics tool, we will risk assess journals and select items for detailed follow up testing. The journal entries will be selected using computer-assisted profiling based on areas which we consider to be of increased interest; and
- we will test the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting.

#### **Accounting estimates**

- We will test the design and implementation of controls over key accounting estimates and judgements; and
- we will review accounting estimates for biases that could result in material misstatements due to fraud. This will include both a retrospective review of 31 March 2018 estimates and a review of the corresponding estimates as at 31 March 2019.

#### **Significant and unusual transactions**

- We will obtain an understanding of the business rationale of significant transactions that we become aware of that are outside of the normal course of business for the entity, or that otherwise appear to be unusual, given our understanding of the entity and its environment.

# Wider scope requirements

## Audit Dimensions

The Code of Audit Practice sets our four audit dimensions which set a common framework for all public sector audits in Scotland. These are financial sustainability, financial management, governance and transparency and value for money. Due to the relative size and scale of the functions delivered by NHS Health Scotland, we have concluded that the full wider scope of audit is not appropriate. In accordance with paragraph 53 of the Code, our work in this area will therefore be restricted to concluding following:

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
<p>The appropriateness of the disclosures in the <b>governance statement</b>.</p>	<ul style="list-style-type: none"> <li>• The completeness of the disclosures in meeting the requirements of the essential features, as specified in the Scottish Public Finance Manual (SPFM).</li> <li>• Inconsistencies between the disclosures and financial statements or between the disclosures and audit knowledge.</li> </ul>	<p>We will review the draft governance statement and assess whether there are any inconsistencies or omissions based on other audit evidence obtained throughout the audit.</p> <p><b>Audit Risk:</b> The governance statement is not consistent with the wider direction of the accounts or compliant with the SPFM.</p>

# Wider scope requirements (continued)

## Audit Dimensions (continued)

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
<p><b>Financial sustainability</b> looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.</p>	<ul style="list-style-type: none"> <li>• The financial planning systems in place across the shorter and longer terms.</li> <li>• The arrangements to address any identified funding gaps.</li> <li>• The affordability and effectiveness of funding and investment decisions made.</li> <li>• Workforce planning.</li> </ul>	<p>Given the establishment of 'Public Health Scotland' from 2019/20 and the uncertainty surrounding its remit, we will consider if the Board is appropriately prioritising transition to the new body while protecting delivery of services in the interim. We will also review if the Board has appropriately considered the impact that the transition will have on its ability to achieve its objective as outlined in the corporate and strategic plans.</p> <p><b>Audit Risk:</b> The Board may fail to properly prepare for transition, or it may overly-prioritise transition to the detriment of service delivery. Either of these options could undermine the ability of the Board to achieve its objectives.</p> <p>In view of the Scottish Government's Medium Term Financial Strategy (MTFS) and new budget process (discussed further on page xx), we will consider the extent to which the Board has reviewed the potential implications of the MTFS for its own finances and whether it is taking these into account in its arrangement for financial management and financial sustainability.</p> <p><b>Audit Risk:</b> The Board's long-term financial planning is inconsistent with the Scottish Governments five-year plan.</p> <p>We will also confirm that underling financial performance including any in-year changes to funding agreed with the Scottish Government is transparently presented.</p> <p><b>Audit Risk:</b> The underlying financial performance of the Board is not transparently reported.</p>

# Wider scope requirements (continued)

## Specific risks

As part of the 2018/19 planning guidance, Audit Scotland have identified the following areas as significant risks faced by the public sector. Any specific risks in relation to these areas for NHS Health Scotland have been included in our audit risk under the audit dimensions, discussed on the previous pages. We will continue to monitor these areas as part of our audit work.

Risk	
<b>EU withdrawal</b>	<p>There are uncertainties surrounding the terms of the UK's withdrawal from the European Union in March 2019. Some arrangements have been provisionally agreed, such as a transition period to the end of 2020, although they are dependent on a final deal being reached between the UK Government and the remaining EU countries. The outcome of negotiations should become clearer in the months up to March 2019.</p> <p>Whatever the outcome, EU withdrawal will inevitably have implications for devolved government in Scotland and for audited bodies. Audit Scotland has identified three areas where EU withdrawal may have the most significant impact as summarised below:</p> <ul style="list-style-type: none"><li>• <b>Workforce</b> – Many public services are dependent on workers from EU countries, including health, social care and education. A decline in migration from the EU could potentially result in vacancies and skills gaps in some areas of the public sector. There is a risk that this could impact on some public bodies' ability to deliver 'business as usual' particularly given existing workforce and service pressures.</li><li>• <b>Funding</b> – Funding from the EU makes an important contribution to the Scottish public sector. The main sources of funding provide support to farmers and rural businesses, projects to encourage economic growth and support for research and education. The UK Government has made guarantees to meet some funding commitments to the end of existing programmes, but there are uncertainties about what any replacement funding may look like.</li><li>• <b>Regulation</b> – The EU Withdrawal Bill will transpose existing EU law into UK law immediately after the UK leaves the EU. Legislation in many devolved areas will transfer to the Scottish Parliament. The UK government has identified 24 devolved policy areas where it seeks to retain temporary control until UK-wide common legislative frameworks are developed. This is currently an area of contention between the Scottish and UK Governments and is under consideration by the Supreme Court.</li></ul> <p>In addition, some public bodies may be affected directly by changes to trade and customs rules, which could impact on supply chains and the procurement of goods or services from EU countries. This could influence the availability and cost of supplies and services (e.g. specialist medical equipment or drugs) with potential implications for public bodies' finances and their ability to deliver specific services.</p> <p>While there are considerable uncertainties about the detailed implications of EU withdrawal, at a minimum by the end of 2018/19, we would expect public bodies to have assessed the potential impact of EU withdrawal on their operations and identified any specific risks and how they will respond to them. We will assess how NHS Health Scotland has prepared for EU withdrawal and how it continues to respond to any emerging risk after March 2019.</p>

# Wider scope requirements (continued)

## Specific risks (continued)

Risk	
<p><b>Changing landscape for public financial management</b></p>	<p>Scottish public finances are fundamentally changing, with significant tax-raising powers, new powers over borrowing and reserves, and responsibility for 11 social security benefits worth over £3 billion a year. This provides the Scottish Government with more policy choices but also means that the Scottish budget is subject to greater volatility, uncertainty and complexity.</p> <p>Parliamentary scrutiny of the public finances is increasingly important in this changing landscape. A new Scottish budget process has been introduced, which is based on a year-round continuous cycle of budget setting, scrutiny and evaluation. This involves parliamentary committees looking back to explore what public spending has achieved, looking forward to longer-term objectives and challenges, and considering what this should mean for future budgets.</p> <p>As part of the new budget process, the Scottish Government published an initial five-year Medium Term Financial Strategy (MTFS) in May 2018. This five-year outlook for the Scottish budget provides useful context for audited bodies' financial planning. Alongside the publication of this, the Cabinet Secretary announced recently that NHS boards will no longer be required to break even at the end of each financial year. Instead, they will be required to break even every three years. This should provide NHS Health Scotland with greater flexibility in planning and investing over the medium to longer term. It also makes it even more important that the Board plans its finances over a medium to longer-term period. As part of our wider scope audit work on financial management and financial sustainability (discussed further on page xx), we will consider how NHS Health Scotland have reviewed the potential implications of the MTFS for its own finances, including longer-term financial planning.</p> <p>The new budget process places greater emphasis on assessing outcomes and the impact of spending. There is an expectation that the Scottish Government and public bodies will report on their contributions towards the national outcomes in their published plans and performance reports, including their Annual Reports. Increased complexity and volatility is also likely to mean that the Scottish Government will be increasingly active in managing its overall budget position in-year, engaging with public bodies closely on their anticipated funding requirements. As part of our review of the Annual Report and Accounts we will consider the extent to which NHS Health Scotland's performance report provides an accessible account of the body's overall performance and impact of its public spending. We will also confirm that underlying financial performance, including any in-year changes to funding agreed with the Scottish Government, is transparently presented.</p>

# Wider scope requirements (continued)

## Specific risks (continued)

Risk	
<p><b>Dependency on key suppliers</b></p>	<p>It has become clear that the collapse of Carillion has had a significant impact across the public sector. This has brought into focus the risk of key supplier failure and the risk of underperformance in suppliers that are experiencing difficult trading conditions. The risk exists on two levels:</p> <ul style="list-style-type: none"> <li>• Individual public sector bodies are dependent on key suppliers; and</li> <li>• the Scottish public sector as a whole is subject to significant systematic risk.</li> </ul> <p>We will determine as part of our detailed risk assessment the extent to which NHS Health Scotland is dependent on key supplier relationships. Where dependency is significant, we will consider this as part of our audit work and report back to the Audit Committee.</p> <p>We will also be requested to complete a short questionnaire to establish the extent, value and nature of key supplier dependencies that can inform the national position.</p>
<p><b>Openness and transparency</b></p>	<p>There is an increasing focus on how public money is used and what is achieved. In that regard, openness and transparency supports understanding and scrutiny.</p> <p>We would expect to see public bodies reviewing their approach to openness and transparency to ensure they are keeping pace with public expectations and good practice. Evidence of progress might include:</p> <ul style="list-style-type: none"> <li>• Increased public availability of board papers;</li> <li>• more insight into why some business is conducted in private; and</li> <li>• development of the form and content of the Annual Report.</li> </ul>

# Wider scope requirements (continued)

## Other requirements

### Performance Audits

In accordance with Audit Scotland planning guidance, we will be requested to provide information to support performance audits that Audit Scotland intends to publish during 2018/19 and 2019/20. There are no specific reports planned, other than the overview report, which directly impact on the NHS. We will provide an update to the Audit Committee if there are any changes to this plan.

### Impact reports

We will also be requested to provide information to support assessing the impact of previously published performance audit reports. There are no specific impact reports which directly relate to the NHS. We will provide an update to the Audit Committee if there are any changes to this plan.

### Anti-money laundering

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 came into force on 26 June 2017 and replace the Money Laundering Regulations 2007. The regulations impose an obligation of the Auditor General to inform the National Crime Agency if she knows or suspects that any person has engaged in money laundering or terrorist financing. As part of our audit work, we will ensure we are informed of any instances of money laundering at the Board so that we can advise the Auditor General.

### National Fraud Initiative (NFI)

All health boards, except for the Mental Welfare Commission, are participating in the NFI 2018/19. All data was required to be submitted in October 2018 and Boards will receive matches for investigation in January 2019. Audit Scotland expects bodies to investigate all recommended matches based on findings and the risk of error or fraud. Match investigation work should be largely completed by 30 September 2019 and the results recorded on the NFI system.

We will monitor the Board's participation and progress during 2018/19 and into 2019/20 and, where appropriate, include references to the NFI in our annual audit reports for both years. We will also complete an NFI audit questionnaire and submit to Audit Scotland by 30 June 2019.

# Wider scope requirements (continued)

## Other requirements (continued)

### Audit intelligence and statutory reports

The Auditor General determines whether a statutory report is required under section 22 of the Public Finance and Accountability (Scotland) Act 2000 for the Scottish Parliaments' Public Audit and Post Legislative Scrutiny Committee.

We are responsible for identifying and highlighting any significant issues arising which might prompt the Auditor General to consider preparing a statutory report with issues arising during the year being raised timeously. We are required to provide Audit Scotland with returns summarising current issues. The health sector return deadline is 21 January 2019. We will have early discussions with management of any issues arising.

# Audit Quality

## Our commitment to audit quality



Our objective is to deliver a distinctive, quality audit to you. Every member of the engagement team will contribute, to achieve the highest standard of professional excellence.

In particular, for your audit, we consider that the following steps will contribute to the overall quality.

We will apply professional scepticism on material issues and significant judgements identified, by using our expertise in the health sector and elsewhere to provide robust challenge to management.

Over the two years of our audit relationship we have obtained and will continue to develop further a deep understanding of your business, its environment and of your key processes, enabling us to develop a risk-focused approach tailored to NHS Health Scotland that focuses on your key risk areas.

Our engagement team is selected to ensure that we have the right subject matter expertise and industry knowledge.

In order to deliver a quality audit to you, each member of the core audit team will receive tailored learning to develop their expertise in audit skills, delivered by Pat Kenny and other sector experts. This includes sector specific matters and audit methodology updates.



### **Engagement Quality Control Review**

We have developed a tailored Engagement Quality Control approach. Our dedicated Professional Standards Review (PSR) function will provide a 'hot' review before any audit or other opinion is signed. PSR is operationally independent of the audit team, and supports our high standards of professional scepticism and audit quality by providing a rigorous independent challenge.

# Purpose of our report and responsibility statement

## Our report is designed to help you meet your governance duties

### What we report

Our report is designed to establish our respective responsibilities in relation to the financial statements audit, to agree our audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes:

- Our audit plan, including key audit judgements and the planned scope; and
- key regulatory and corporate governance updates, relevant to you.

### What we don't report

As you will be aware, our audit is not designed to identify all matters that may be relevant to the Board.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, the views on internal controls and business risk assessment in our final report should not be taken as comprehensive or as an opinion on effectiveness since they will be based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

### Other relevant communications

We will update you if there are any significant changes to the audit plan.

This report has been prepared for the Audit Committee, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

We welcome the opportunity to discuss our report with you and receive your feedback.



**Pat Kenny, CPFA**

for and on behalf of Deloitte LLP

Glasgow

2 November 2018

# Appendices



# Prior year audit adjustments

## Uncorrected and disclosure misstatements

### **Uncorrected misstatements**

In our prior year audit, we identified one immaterial uncorrected misstatement. The provision for injury benefit was understated as at 31/3/2018 as the assumptions upon which the provision is based (life expectancy) were not updated for the most recently available information for the UK from the ONS. The error would reduce the net surplus position from £123k to £58k as at 31/3/2018, however it would not change it to a deficit position. The error would correspondingly reduce net assets as at 31 March 2018 by £65k.

### **Disclosure misstatements**

There were no uncorrected disclosure misstatements identified during the course of our prior year audit.

# Fraud responsibilities and representations

## Responsibilities explained



### Your responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.



### Our responsibilities:

- We are required to obtain representations from your management regarding internal controls, assessment of risk and any known or suspected fraud or misstatement.
- As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risks section of this document, we have identified the risk of fraud in achievement of expenditure resource limits and management override of controls as a key audit risk for your organisation.



### Fraud characteristics:

- Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.
- Two types of intentional misstatements are relevant to us as auditors – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

### We will request the following to be stated in the representation letter signed on behalf of the Board:

- We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- We are not aware of any fraud or suspected fraud that affects the entity and involves:
  - (i) Management;
  - (ii) employees who have significant roles in internal control; or
  - (iii) others where the fraud could have a material effect on the financial statements.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.



# Fraud responsibilities and representations

## Inquiries

We will make the following inquiries regarding fraud:



### **Management**

- Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether management has knowledge of any actual, suspected or alleged fraud affecting the entity.

### **Internal audit and Local Counter Fraud Specialist**

- Whether internal audit and the Board's Local Counter Fraud Specialist has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain their views about the risks of fraud.



### **Those charged with governance**

- How those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks.
- Whether those charged with governance have knowledge of any actual, suspected or alleged fraud affecting the entity.
- The views of those charged with governance on the most significant fraud risk factors affecting the entity.



# Independence and fees



As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

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## Independence confirmation

We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Board and will reconfirm our independence and objectivity to the Audit Committee for the year ending 31 March 2019 in our final report to the Audit Committee.

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## Fees

Fee range for the 2018/19 audit to be provided by Audit Scotland in early December 2018 will be discussed and agreed with management and the Audit Committee in early 2019.

There are no non-audit services fees proposed for the period.

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## Non-audit services

In our opinion there are no inconsistencies between the FRC's Ethical Standard and the Board's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.

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## Relationships

We have no other relationships with the Board, its directors, senior managers and affiliates, and have not supplied any services to other known connected parties.

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# Our approach to quality

## AQR team report and findings

We maintain a relentless focus on quality and our quality control procedures and continue to invest in and enhance our overall firm Audit Quality Monitoring and Measuring programme.

In June 2018 the Financial Reporting Council ("FRC") issued individual reports on each of the eight largest firms, including Deloitte, on Audit Quality Inspections which provides a summary of the findings of its Audit Quality Review ("AQR") team for the 2017/18 cycle of reviews.

We take the findings of the AQR seriously and we listen carefully to the views of the AQR and other external audit inspectors. We remediate every finding regardless of its significance and seek to take immediate and effective actions, not just on the individual audits selected but across our entire audit portfolio. We are committed to continuously improving all aspects of audit quality in order to provide consistently high quality audits that underpin the stability of our capital markets.

We have improved the speed by which we communicate potential audit findings, arising from the AQR inspections and our own internal reviews to a wider population, however, we need to do more to ensure these actions are embedded. In order to achieve this we have launched a more detailed risk identification process and our InFlight review programme. This programme is aimed at having a greater impact on the quality of the audit before the audit report is signed. Consistent achievement of quality improvements is our aim as we move towards the AQR's 90% benchmark. All the AQR public reports are available on its website. <https://www.frc.org.uk/auditors/audit-quality-review/audit-firm-specific-reports>

### The AQR's 2017/18 Audit Quality Inspection Report on Deloitte LLP

"The overall results of our reviews of the firm's audits show that 76% were assessed as requiring no more than limited improvements, compared with 78% in 2016/17. Of the FTSE 350 audits we reviewed this year, we assessed 79% as achieving this standard compared with 82% in 2016/17. We are concerned at the lack of improvement in inspection results. The FRC's target is that at least 90% of these audits should meet this standard by 2018/19."

"Where we identified concerns in our inspections, they related principally to aspects of group audit work, audit work on estimates and financial models, and audit work on provisions and contingencies. During the year, the firm has continued to develop the use of "centres of excellence", increasing the involvement of the firm's specialists in key areas of the audit. We have no significant issues to report this year in most of the areas we reported on last year."

"The firm has revised its policies and procedures in response to the revised Ethical and Auditing Standards. We have identified some examples of good practice, as well as certain areas for improvement."

### The firm has enhanced its policies and procedures in the following areas:

- Increased use of centres of excellence ("CoE") involving the firm's specialists, including new CoEs focusing on goodwill impairment (established in response to previous inspection findings) and corporate reporting, to address increasing complexity of financial reporting.
- Further methodology updates and additional guidance issued to the audit practice including the audit approach to pension balances, internal controls, data analytics, group audits and taxation.
- A new staff performance and development system was implemented with additional focus on regular timely feedback on performance, including audit quality.
- Further improvements to the depth and timeliness of root cause analysis on internal and external inspection findings.

### Our key findings in the current year requiring action by the firm:

- Improve the group audit team's oversight and challenge of component auditors.
- Improve the extent of challenge of management's forecasts and the testing of the integrity of financial models supporting key valuations and estimates.
- Strengthen the firm's audit of provisions and contingencies.

### Review of firm-wide procedures. The firm should:

- Enhance certain aspects of its independence systems and procedures.



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