

NHS Highland

Annual Audit Plan 2022/23



 AUDIT SCOTLAND

Prepared for NHS Highland

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Introduction

Summary of planned audit work

1. This document summarises the work plan for our 2022/23 external audit of NHS Highland. The main elements of our work include:

- evaluation of the key controls within the main accounting systems
- an audit of the annual report and accounts, and provision of an Independent Auditor's Report
- audit opinions on regularity and other statutory information published within the annual report and accounts including the Performance Report, the Governance Statement and the Remuneration and Staff Report
- consideration of arrangements in relation to wider scope areas: financial management; financial sustainability; vision, leadership and governance; and use of resources to improve outcomes
- consideration of Best Value arrangements.

Audit Appointment

2. We are pleased to be appointed as the external auditor of NHS Highland for the period 2022/23 to 2026/27 inclusive. You can find a brief biography of your audit team at [Appendix 1](#).

3. In the first year of the audit appointment, we invest significant time gaining an understanding of your business and identifying and assessing the risks of material misstatement to the financial statements. While we use our initial assessment of risk to inform our planned audit approach, we keep our assessment of risks under review as the audit progresses. We will inform you of any significant changes in assessed risks and any resulting changes in our planned audit work.

4. The audit team will actively engage with you over the course of the audit to ensure our audit work continues to be focused on risk.

Adding value

5. We aim to add value to NHS Highland through our external audit work by being constructive and forward looking, by attending meetings of the Audit Committee and by recommending and encouraging good practice. In so doing, we will help NHS Highland promote improved standards of governance, better management and decision making and more effective use of resources.

Respective responsibilities of the auditor and Audited Body

6. The [Code of Audit Practice 2021](#) sets out in detail the respective responsibilities of the auditor and NHS Highland. Key responsibilities are summarised below.

Auditor responsibilities

7. Our responsibilities as independent auditors are established by the Public Finance and Accountability (Scotland) Act 2000 and the [Code of Audit Practice](#) (including [supplementary guidance](#)) and guided by the Financial Reporting Council's Ethical Standard.

8. Auditors in the public sector give an independent opinion on the financial statements and other information within the annual report and accounts. We also review and report on the wider scope arrangements in place at NHS Highland. In doing this, we aim to support improvement and accountability.

NHS Highland responsibilities

9. NHS Highland is responsible for maintaining accounting records and preparing financial statements that give a true and fair view.

10. NHS Highland has the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to deliver their objectives.

Communication of fraud or suspected fraud

11. In line with auditing standards, in presenting this plan to the Audit Committee, we seek confirmation from those charged with governance of any instances of actual, suspected, or alleged fraud that should be brought to our attention. Should members of the committee have any such knowledge or concerns relating to the risk of fraud within NHS Highland, we invite them to communicate this to the appointed auditor for consideration.

Financial statements audit planning

Introduction

12. The annual report and accounts are an essential part of demonstrating NHS Highland's stewardship of resources and its performance in the use of those resources.

13. We focus our work on the areas of highest risk. As part of our planning process, we prepare a risk assessment highlighting the audit risks relating to each of the main financial systems relevant to the production of the financial statements.

Materiality

14. The concept of materiality is applied by auditors in planning and performing the audit, and in evaluating the effect of any uncorrected misstatements on the financial statements. We are required to plan our audit to obtain reasonable assurance that the financial statements are free from material misstatement. The assessment of what is material is a matter of professional judgement over both the amount and the nature of the misstatement.

Materiality levels for the 2022/23 audit

15. We assess materiality at different levels as described in [Exhibit 1](#) along with the materiality values for NHS Highland and its group.

Exhibit 1

2022/23 Materiality levels for NHS Highland and its group

Materiality	Amount
<p>Planning materiality – This is the figure we calculate to assess the overall impact of audit adjustments on the financial statements. Materiality has been set based on our assessment of the needs of the users of the financial statements and the nature of NHS Highland's operations. For the year ended 31 March 2023 we have set our materiality at 1.5% of gross expenditure based on the audited financial statements for 2021/22.</p>	£21.0 million
<p>Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality, this could indicate that further audit procedures should be considered. Using our professional judgement, we have assessed performance materiality at 60% of planning materiality.</p>	£12.6 million

Materiality	Amount
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount.	£250,000

Source: Audit Scotland

Significant risks of material misstatement to the financial statements

16. Our risk assessment draws on our cumulative knowledge of NHS Highland, its major transaction streams, key systems of internal control and risk management processes. It is informed by our discussions with management, meetings with internal audit, attendance at committees and a review of supporting information.

17. Audit risk assessment is an iterative and dynamic process. Our assessment of risks set out in this plan may change as more information and evidence becomes available during the progress of the audit. Where such changes occur, we will advise management and where relevant, report them to those charged with governance.

18. Based on our risk assessment process, we identified the following significant risks of material misstatement to the financial statements. These are risks which have the greatest impact on our planned audit procedures. [Exhibit 2](#) summarises the nature of the risk, the sources of assurance from management arrangements and the further audit procedures we plan to perform to gain assurance over the risk.

Exhibit 2

2022/23 Significant risks of material misstatement to the financial statements

Significant risk of material misstatement	Sources of assurance	Planned audit response
<p>1. Risk of material misstatement due to fraud caused by management override of controls</p> <p>As stated in International Standard on Auditing (UK) 240, management is in a unique position to perpetrate fraud because of management's ability to override controls that</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance</p>	<ul style="list-style-type: none"> Assess the design and implementation of controls over journal entry processing. Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments. Test journals at the year-end and post-closing entries and focus on significant risk areas.

Significant risk of material misstatement	Sources of assurance	Planned audit response
otherwise appear to be operating effectively.		<ul style="list-style-type: none"> • Consider the need to test journal entries and other adjustments during the period. • Evaluate significant transactions outside the normal course of business. • Assess the adequacy of controls in place for identifying and disclosing related party relationship and transactions in the financial statements. • Assess any changes to the methods and underlying assumptions used to prepare accounting estimates compared to the prior year. • Substantively test income and expenditure transactions around the year-end to confirm they are accounted for in the correct financial year. • Perform focussed testing of accounting accruals and prepayments.

Source: Audit Scotland

19. As set out in International Standard on Auditing (UK) 240: *The auditor's responsibilities relating to fraud in an audit of financial statements*, there is a presumed risk of fraud over the recognition of revenue. There is a risk that revenue may be misstated resulting in a material misstatement in the financial statements. We have rebutted this risk as most income is provided by the Scottish Government and other public bodies and is easily verified.

20. In line with Practice Note 10: *Audit of financial statements and regularity of public sector bodies in the United Kingdom*, as most public-sector bodies are net spending bodies, the risk of material misstatement due to fraud related to expenditure recognition may in some cases be greater than the risk relating to revenue recognition. We have rebutted this risk as the main expenditure streams of NHS Highland are in low-risk areas (for example salaried staff costs in a well-defined grading system) and individual transactions are relatively small in scale.

21. We have not incorporated specific work into our audit plan in these areas over and above our standard audit procedures.

Other areas of audit focus

22. As part of our assessment of audit risks, we have identified other areas where we consider there are also risks of material misstatement to the financial statements. Based on our assessment of the likelihood and magnitude of the risk,

we do not consider these to represent significant risks. We will keep these areas under review as our audit progresses.

23. The areas of specific audit focus are:

- **Estimation in the valuation of other land and buildings - NHS**
Highland hold land and buildings with a NBV of £383 million as at 31 March 2022. These assets are revaluated on a five-year rolling basis by external valuers. Valuations are based on specialist and management assumptions and changes in these can result in material changes to valuations. We will review the arrangements in place to satisfy the board that the annual revaluation process is complete and is free from material misstatement. There is also the risk, for those assets not subject to revaluation in-year, that the carrying value does not reflect current value.
- **Pension liabilities**
 - **Accounting treatment:** NHS Highland has a pension fund liability of £16 million as at 31 March 2022 in respect of NHS Highland Council social care staff who transferred to NHS Highland in 2012. Accounting for the Local Government Pension Scheme within NHS Highland financial statements departs from the requirements of IAS 19 as there is no net pension liability recognised within the Statement of financial position, instead the impact of the liability is removed to other reserves. We will liaise with the client to ensure a formal agreement of this accounting treatment is obtained from Scottish Government.
 - **Valuation:** The liability requires the use of an actuarial methodology based on a range of assumptions including financial and demographic assumptions. This is an area of audit focus because the methodology applied could have a material impact on the net pension liability accounted for in the financial statements. The basis of the assumptions should also be derived on a consistent basis year to year. We will assess the scope, independence and competence of the professionals engaged in providing estimates for pensions and review appropriateness of actuarial assumptions and results including comparison with other councils. We will establish officer's arrangements for ensuring the reasonableness of professional estimations and the accuracy of information provided to the actuary by Highland Council.

Group Consideration

24. As group auditors, we are required under International Standard on Auditing (ISA) (UK) 600: *Audits of group financial statements (including the work of component auditors)* to obtain sufficient appropriate audit evidence on which to base our audit opinion on the group financial statements.

25. NHS Highland has a group which comprises component entities, including Highland Health Board Endowment Funds and Argyll and Bute IJB as a joint

venture. The audits of the financial information of the components are performed by other auditors.

26. We will obtain sufficient appropriate audit evidence in relation to the consolidation process and the financial information of the components on which to base our group audit opinion.

Wider Scope and Best Value

Introduction

27. The [Code of Audit Practice](#) sets out the four areas that frame the wider scope of public sector audit. The Code of Audit Practice requires auditors to consider the adequacy of the arrangements in place for the wider scope areas in audited bodies.

28. In summary, the four wider scope areas cover the following:

- **Financial management** - means having sound budgetary processes. We will consider the arrangements to secure sound financial management including the strength of the financial management culture, accountability and arrangements to prevent and detect fraud, error and other irregularities, including bribery and corruption.
- **Financial sustainability** - means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs. We will consider the extent to which audited bodies have shown regard to financial sustainability and are planning ahead effectively. We look at planning for the medium term (two to five years) and longer term (longer than five years). The audit will include consideration of the use of the going concern basis of accounting as part of the annual audit. We will also comment on financial sustainability in the longer term.
- **Vision, leadership and governance** - audited bodies must have a clear vision and strategy, and work together with partners and communities to improve outcomes and set priorities for improvement. We will consider the arrangements in place to deliver the vision, strategy and priorities adopted by NHS Highland, including plans to address workforce capacity issues in medical services and finance and corporate services. We will also consider the effectiveness of the governance arrangements to support delivery.
- **Use of resources to improve outcomes** - audited bodies must make best use of their resources to meet stated outcomes and improvement objectives. We will consider how NHS Highland demonstrates economy, efficiency and effectiveness through the use of financial and other resources.

Wider scope risks

29. We have identified wider scope audit risks in the areas set out in [Exhibit 3](#). This exhibit sets out the risks, sources of assurance from management and the further audit procedures we plan to perform to gain assurances over the risks.

Exhibit 3

2022/23 wider scope risks

Description of risk	Sources of assurance	Planned audit response
<p>Financial Management and Sustainability</p> <p>The most recent financial monitoring report prepared by NHS Highland is projecting a year-end overspend position of £20 million. This represents an increase of £4 million on the approved budgeted overspend.</p> <p>There is a risk that the Board does not receive the final allocation letter to enable audit sign off by 30 June 2023. There is also a risk that NHS Highland cannot deliver services over the medium term within budget.</p>	<ul style="list-style-type: none"> • Internal audit reports. • Board monitoring reports and minutes. • Committee (FRP) reports and minutes. • Monthly budget holder reporting and monitoring. • Quarterly review meetings. • Annual financial plans. • SG interim allocation letters. • Counter Fraud bulletin and updates/ training. 	<ul style="list-style-type: none"> • Monitor the board's financial position as reported to the board / relevant committees. • Review the board's financial plans and transformation plans on an ongoing basis and consider whether appropriate arrangements are in place to address the underlying recurring deficit. • Attendance and observations at board and relevant committee meetings

Source: Audit Scotland

30. Our planned work on our wider scope responsibilities is risk based and proportionate and in addition to local risks we consider challenges which are impacting the public sector as a whole. In 2022/23 we will consider tackling climate change and responding to cyber security threats.

Climate Change

31. Tackling climate change is one of the greatest global challenges. The Scottish Parliament has set a legally binding target of becoming net zero by 2045 and has interim targets including a 75% reduction in greenhouse gas emissions by 2030. The public sector in Scotland has a key role to play in ensuring these targets are met and in adapting to the impacts of climate change.

32. The Auditor General and Accounts Commission are developing a programme of work on climate change. In 2022/23, we will gather information on NHS Highland's arrangements for responding to climate change covering areas such as the development of climate change strategies and the monitoring and reporting of progress against targets for reducing emissions.

Cyber Security

33. There continues to be a significant risk of cyber-attacks to public bodies, and it is important that they have appropriate cyber security arrangements in place. A number of recent incidents have demonstrated the significant impact that a cyber-attack can have on both the finances and operation of an organisation. In 2022/23, we will consider NHS Highland's arrangements for managing and mitigating cyber security risks.

Duty of Best Value

34. [Ministerial Guidance to Accountable Officers](#) for public bodies and the [Scottish Public Finance Manual](#) (SPFM) explain that accountable officers have a specific responsibility to ensure that arrangements have been made to secure Best Value. We will be carrying out a high-level review to confirm that such arrangements are in place within NHS Highland.

Reporting arrangements, timetable, and audit fee

Reporting arrangements

35. Audit reporting is the visible output for the annual audit. All Annual Audit Plans and the outputs, as detailed in [Exhibit 4](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

36. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

37. We will provide an independent auditor's report to NHS Highland, the Scottish Parliament and the Auditor General for Scotland setting out our opinions on the annual report and accounts. We will provide NHS Highland and the Auditor General for Scotland with an annual report on the audit containing observations and recommendations on significant matters which have arisen during the audit.

38. [Exhibit 4](#) outlines the target dates for our audit outputs. We are aiming to issue the independent auditor's report by the statutory deadline of 30 June 2023 which will be challenging. We will continue to liaise with management over the timelines and adjust our plans accordingly should there be slippage in the agreed timetable.

Exhibit 4

2022/23 Audit outputs

Audit Output	Target date	Audit Committee Date
Annual Audit Plan	31 March 2023	2 May 2023
Independent Auditor's Report	30 June 2023	20 June 2023
Annual Audit Report	30 June 2023	20 June 2023

Source: Audit Scotland

Timetable



39. To support an efficient audit, it is critical that the timetable for producing the annual report and accounts for audit is achieved. We have included a proposed timetable for the audit at [Exhibit 5](#) that has been discussed with management.

40. Covid-19 has had a considerable impact on the conduct and timeliness of the audit. We recognise that it is in the best interests of public accountability to get the reporting of audited accounts back to pre-pandemic timelines. We are identifying ways to work more efficiently to expedite the 2022/23 audits whilst at the same time maintaining high standards of quality.

41. We intend to take a hybrid approach to the 2022/23 audit with a blend of onsite and remote working. We will continue to work closely with management to identify the most efficient approach as appropriate and will keep timeframes and logistics for the completion of the audit under review. Progress will be discussed with management and finance officers over the course of the audit.

Exhibit 5

Proposed annual report and accounts timetable

 Key stage	 Provisional Date
Latest submission date for the receipt of the unaudited annual report and accounts with complete working papers package	9 May 2023
Latest date for final clearance meeting with the Director of Finance	9 June 2023
Issue of draft Annual Audit Report, draft Letter of Representation and proposed Independent Auditor's Report	13 June 2023
Agreement of audited and unsigned annual report and accounts	13 June 2023
Issue of final Annual Audit Report to those charged with governance.	27 June 2023
Signed Independent Auditor's Report	27 June 2023

Source: Audit Scotland

Audit fee

42. In determining the audit fee, we have taken account of the risk exposure of NHS Highland and the planned management assurances in place. The proposed audit fee for 2022/23 is £224,840 (2021/22: £190,150).

43. Our fees have increased in 2022/23 and this is a reflection of the current audit market and the rising costs in delivering high quality audit work. There are increased regulatory expectations and risks placed on audit and its quality, as well as a widening in the scope of work audit must cover.

44. In setting the fee for 2022/23 we have assumed that NHS Highland has effective governance arrangements and will prepare comprehensive and accurate accounts for audit in line with the agreed timetable for the audit. The audit fee assumes there will be no major change in respect of the scope of the audit during

the year and where our audit cannot proceed as planned, a supplementary fee may be levied.

Other matters

Internal audit

45. It is the responsibility of NHS Highland to establish adequate internal audit arrangements. We will review the internal audit plan and the results of internal audit's work.

46. While we are not planning to place formal reliance on the work of internal audit in 2022/23, we will review internal audit reports and assess the impact of the findings on our financial statements and wider scope audit responsibilities.

Independence and objectivity

47. Auditors appointed by the Auditor General for Scotland or Accounts Commission must comply with the [Code of Audit Practice](#) and relevant supporting guidance. When auditing the financial statements, auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors.

48. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual '*fit and proper*' declaration for all members of staff. The arrangements are overseen by the Executive Director of Innovation and Quality, who serves as Audit Scotland's Ethics Partner.

49. The appointed auditor for NHS Highland is Claire Gardiner, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of NHS Highland.

Audit Quality

50. Quality is at the core of public audit in Scotland and is the foundation for building consistency and confidence across all audit work. High quality audits provide assurance, add value and can support public bodies to achieve their objectives.

51. Until 2021/22, the applicable audit quality standard was International Standard on Quality Control 1 (ISQC (UK) 1). This set out an audit practice's responsibilities for its system of quality control for audits.

52. ISQC(UK) 1 has been replaced by two new audit quality standards: Internal Standards on Quality Management (ISQM (UK) 1) applicable from 15 December 2022 and (ISQM(UK) 2) effective for the 2023/24 audits. Work is underway at Audit Scotland to meet the requirements of these quality standards.

53. Audit Scotland is committed to delivering high quality audits. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the [Code of Audit Practice](#) (and supplementary guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards, Audit Scotland conducts peer reviews and internal quality reviews. Additionally, the Institute of Chartered Accountants of England and Wales (ICAEW) have been commissioned to carry out external quality reviews.

54. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time, and this may be directed to the engagement lead.

Appendix 1: Your audit team

55. The audit team involved in the audit of NHS Highland have significant experience in public sector audit.

<p>Claire Gardiner Audit Director cgardiner@audit-scotland.gov.uk</p>	<p>Claire has over 18 years of public sector auditing experience. Claire has worked across the breadth of the public sector on financial audits.</p>
<p>Patricia Fraser Senior Audit Manager pfraser@audit-scotland.gov.uk</p>	<p>Patricia has over 25 years of public sector audit experience and has delivered external audit services to a range of bodies including local authorities, health boards and central government bodies.</p>
<p>Kay Jenks Senior Auditor kjenks@audit-scotland.gov.uk</p>	<p>Kay has considerable experience in planning and delivering audits and will manage the team and work alongside the Senior Audit Manager and Audit Director to deliver the audit.</p>

56. The local audit team is supported by a specialist technical accounting team, all of whom have significant experience of public bodies and work with accounting regulatory bodies.

57. Where possible and appropriate, we use our data analytics team to enable us to capture whole populations of your financial data. This analysis allows us to identify specific exceptions and anomalies within populations to enhance the focus of audit testing and support efficiency.

NHS Highland

Annual Audit Plan 2022/23

Audit Scotland's published material is available for download on the website in a number of formats. For information on our accessibility principles, please visit:

www.audit-scotland.gov.uk/accessibility

For the latest news follow us on social media or [subscribe to our email alerts.](#)



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