

FIFE HEALTH BOARD

**Report to the Board Members
and the Auditor General for Scotland**

Audit Year to 31 March 2005

External Audit Report No: 2005/10

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Henderson Loggie
Chartered Accountants
Royal Exchange
Panmure Street
Dundee, DD1 1DZ

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1. EXECUTIVE SUMMARY

1.1 Introduction

- 1.1.1 This report summarises our main responsibilities and duties and draws attention of members to the key matters emerging from the audit of Fife Health Board for the year to 31 March 2005.

1.2 Respective responsibilities

- 1.2.1 Board members' responsibilities are set out on page 2 of the financial statements. As auditors of the Board our responsibilities derive from Part 2 of the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice. An outline of our responsibilities and duties is provided in Section 2.4 Scope of the Audit.

1.3 Audit findings and conclusions

Financial statements

- 1.3.1 Our overall conclusion is that the financial stewardship of Fife Health Board was of a satisfactory standard. In particular in addition to staying within the prescribed Revenue Resource Limit, Capital Resource Limit and Cash Requirement we were able to report that:
- The financial statements give a true and fair view of the state of affairs of Fife Health Board as at 31 March 2005.
 - In all material respects, the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.
 - Appropriate disclosures have been made by the Chief Executive in the Statement on Internal Control (SIC). The content of the statement was not inconsistent with information arising from our audit work and accordingly our opinion on the SIC was unqualified.
 - The Summarisation Spreadsheet was consistent with the financial statements.
 - The financial statements of the Fife Health Council were unqualified.
- 1.3.2 In compliance with Statement of Auditing Standard 610 on 14 July 2005 we issued to those charged with governance, the Board's Audit Committee, our audit report, *Year-End Management Letter 2004/05*. The report provides audit comment on the key issues, accounts adjustments and audit opinions arising from the audit of the financial statements and of the Board's system of internal control.

1.3 Audit findings and conclusions (Cont'd)

Corporate governance

- 1.3.3 Last year we reported that while there were a number of governance areas progressing reasonably well there were weaknesses in others and it was imperative that steps were taken to establish a sound governance framework that staff and stakeholders could have confidence in.
- 1.3.4 This year there has been progress towards strengthening the arrangements in place. In particular there has been improvement in corporate and financial governance and in developments to improve risk management. As noted in the SIC there are still some significant areas to be addressed. We believe further improvement is needed in a number of areas in order to establish a sound governance framework. These areas include the finalisation of corporate governance arrangements, implementation of the Risk Management Strategy, taking forward workforce planning, further development of single-system frameworks in a number of areas and ensuring effective project management arrangements are in place to provide the timely delivery of single-system working and the creation of a robust performance management framework.
- 1.3.5 Our audit report, *Overall Arrangements 2004/05*, was issued on 14 July 2005 for consideration by the Board's Audit Committee to allow it to complete its governance role and to report appropriately to the Board ahead of the formal adoption of the annual accounts and other assurance statement.

Financial Governance

- 1.3.6 There has been improvement in the Board's governance arrangements during the year. The introduction of a Finance and Resources Committee has helped ensure greater awareness and consideration of the financial affairs by Board members. The greater focus and accountability of the financial affairs of the Board has provided a form of greater support to the finance function.
- 1.3.7 There are further improvements that can be made in the area of financial planning. Greater clarity of the Board's recurring income and expenditure profile would help establish the level of the Board's recurring funding gap and make easier the understanding of the action, and timing of action, necessary to generate internal cost and efficiency savings. The recurring funding gap is the difference between the recurring funding available and the recurring expenditure for operational activities. This excludes any additional one-off funding received from the Health Department, any planned savings or additional non-recurring expenditure not required for operating activities. The Board receives funds, awarded annually on a non-recurring basis, to cover certain recurring service expenditure. In our opinion these funds would have to be separately identified in arriving at the underlying recurring funding gap.
- 1.3.8 Savings initiatives were identified and considered by the Board's Challenge Group during 2004/05 however the achievement or otherwise of in-year and future year savings cannot be readily identified in the regular financial reports. It is important that the initiatives identified for 2005/06 are taken forward proactively and are regularly measured and reported to the Challenge Group. We believe the Board's Finance and Resources Committee should take an active oversight role in reviewing the work of the Challenge Group during the year. This greater understanding of the potential and achieved savings by the members of the Committee will aid future revenue and capital planning.

1.3 Audit findings and conclusions (Cont'd)

Planning and Performance Management

- 1.3.9 There is a need to further develop SMART objectives for the Local Health Plan and ensure appropriate coverage for national, local and regional issues. Further there has been delay to date in addressing the Board's performance management arrangements in regard to the Plan, with a lack of reporting to the Board evident during 2004/05.
- 1.3.10 The Board's intended performance management and reporting arrangements through the use of a balanced scorecard approach needs to be finalised, approved and implemented without further delay.

IM&T Strategy

- 1.3.11 There is an urgent need to continually update and drive forward the implementation of the Board's IM&T Strategy taking account of the developing eHealth agenda at both national and local levels.

Capital Planning

- 1.3.12 There has been improvement made in this area of the Board's activity during 2004/05. Internal audit have reported the need for further improvement around the availability of appropriate capital planning and investment control guidelines and project management guidelines.

Audit Recommendations

- 1.3.13 We have made eight recommendations for the attention of Board members throughout this report. These cover financial planning, governance arrangements, planning and performance management, IM&T and capital planning. The recommendations, and management comment, are included in the action plan at Section 9 on pages 24 to 26. We will review progress against the action plan during our 2005/06 audit.

2. INTRODUCTION

2.1 Introduction

- 2.1.1 We are pleased to submit our fourth annual report covering significant matters arising during the course of our audit of Fife Health Board for the year-ended 31 March 2005.
- 2.1.2 The responsibility of procuring the external audit of all health bodies in Scotland rests with the Auditor General for Scotland. Following a procurement process during early 2001 the Auditor General appointed us as external auditors to the Board for the audit of the accounts for a five-year period from 2001/02 to 2005/06. In accordance with the terms of our appointment copies of the Board's annual accounts and this report are submitted to the Auditor General.
- 2.1.3 We would like to take this opportunity to thank the Director of Finance and his staff, together with those members of staff of other directorates who assisted in our work.

2.2 Purpose of the Report

- 2.2.1 Our purpose in preparing this report is two-fold. Our aim is to provide a summary of the results of our audit for Fife Health Board (the Board) for Board members. Additionally, our report is designed to provide information to the Auditor General for Scotland on the main issues arising from our audit, a summary of the results of our audit, and comment on a number of issues we have specifically been asked to include in this report to provide information for the "Overview Report on NHS Scotland".

2.3 Respective Responsibilities of Auditors and Board Members

- 2.3.1 Each public sector body is accountable for the way in which it has discharged its stewardship of public funds. Stewardship is a function of both executive and non-executive management and, therefore, responsibility for effective stewardship rests upon both members and officers of a public sector body.
- 2.3.2 That responsibility is discharged primarily by the establishment of sound arrangements and systems for the planning, appraisal, authorisation and control over the use of resources and by the preparation, maintenance and reporting of accurate and informative accounts.
- 2.3.3 It is our responsibility to undertake an independent appraisal of the discharge by management of its stewardship responsibilities, to enable us to give an assurance that those responsibilities have been reasonably discharged.
- 2.3.4 Board members' responsibilities for the Statement of Accounts are set out on page 2 of the accounts. Our responsibility is to form an independent opinion, based on our audit, on the abstract of accounts and report that opinion to you. We are also required to provide assurance regarding the regularity of income and expenditure included in the Board's annual accounts. We are further required to review the Board's Statement on Internal Control and, where in our opinion full disclosure has not been given, then for us to report accordingly. Additionally we are required to review and confirm the accuracy of the Board's Summarisation Spreadsheet prior to its submission to the Scottish Executive Health Department (SEHD) and certify the expenditure of the Local Health Council.

2.4 Scope of the Audit

2.4.1 We audited the accounts under the National Health Service (Scotland) Act 1978. We have conducted our audit in accordance with the requirements of Part 2 of the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice approved by the Auditor General for Scotland, which requires consideration of relevant auditing standards.

2.4.2 Our audit objectives were to consider and assess the following: -

- whether the statement of accounts presents a true and fair view of the financial position of the Health Board;
- the adequacy of the main financial systems;
- the adequacy of the arrangement in place for the prevention and detection of fraud and corruption;
- the performance of particular services and activities;
- the effectiveness of overall management arrangements.

2.4.3 Our audit scope therefore includes wider responsibilities and duties than would be expected of external auditors in the private sector.

2.4.4 Our audit comprises: -

Audit opinion

The scope of the work required to audit the accounts takes various forms. It includes detailed testing of account balances to substantiate their material accuracy and completeness, and to ensure that the financial out-turn is presented in accordance with approved accounting standards. It also encompasses an assessment of the integrity of the fundamental financial control systems operating during the year, responsibility for the effective maintenance of which rests with management. Our findings are noted in Section 3.

Performance Audit

The performance audit programme undertaken this year was devised by Audit Scotland and included studies on staff governance and Priorities and Risk Framework. We have also carried out a locally determined joint study on the development of Joint Future arrangements at the Board and Fife Council. We will report separately on our work on Joint Future. We have also followed up on the implementation of audit recommendations from our earlier work on the national studies on waste management and community equipment and adaptations. Separate reports have been issued for these projects. We have also followed up on the implementation of recommendations from our work on resource transfer. Comments on resource transfer were reported in our *Overall Arrangements Report 2005/07* on 14 July 2005.

Overall Arrangements

We have undertaken an overall review of the effectiveness of management arrangements within the Health Board to secure economy, efficiency and effectiveness in the discharge of its functions. Our work included a review of the Board's development of its corporate and financial governance arrangements, single system working, performance management, risk management, workforce planning, development of Community Health Partnerships (CHPs) and internal audit. Our findings have been reported in our *Overall Arrangements Report 2005/07* on 14 July 2005

Legality, Regularity, fraud and corruption

We have also undertaken a review of the procedures implemented to prevent instances of fraud and corruption. Our work also includes specific consideration of the regularity of transactions included in the Board's accounts. Our findings are noted in Sections 3 and 8.

3. AUDIT COMPLETION AND CERTIFICATION

3.1 Audit Completion

3.1.1 The target date set by The Scottish Executive Health Department (SEHD) for submission of the 2004/05 audited accounts of the Board was 31 July 2005. We are pleased to report that the target date for the audit completion and certification of the annual accounts was met. The Board approved the accounts for the financial year ended 31 March 2005 on 26 July 2005. We signed our audit reports on the same day.

3.2 Accounts Certification

3.2.1 Our Management Letter, *2004/05 Year-End Audit Key Issues Report 2005/09*, was presented at the Audit Committee meeting on 22 July 2005 at which the financial statements of the Board were considered and recommended for Board approval. The Management Letter set out commentary on audit certification issues, including those relating to the financial statements, the regularity of transactions, the Statement on Internal Control, the Board's Summarisation Spreadsheet and the accounts of the Local Health Council. We set out below a summary of the audit certification issues:

- The financial statements give a true and fair view of the state of affairs of Fife Health Board as at 31 March 2005.
- In all material respects, the expenditure and income shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.
- The Statement on Internal Control was unqualified and the Chief Executive had made appropriate disclosures and the content of the statement was not inconsistent with information arising from our audit work.
- The Summarisation Spreadsheet was consistent with the financial statements.
- The financial statements of the Fife Health Council were unqualified.

3.2.2 Members wishing further information on audit certification issues should refer to our Management Letter Report 2005/09 issued on 14 July 2005.

4. ANNUAL RESULTS AND FINANCIAL PERFORMANCE

4.1 Introduction

4.1.1 The purpose behind this section is to provide information on the annual results and financial performance of Fife Health Board for the year to 31 March 2005.

4.1.2 The accounts preparation and audit process was much improved on the previous year. We commend the finance staff for the high standard of working papers created in support of the draft financial statements and their positive contribution towards the accounts and audit closure process. The move in 2005/06 to an accounts and audit closure deadline of 30 June will remain a challenge, however, with the advances made during 2004/05 and with further planning we are confident that the earlier deadline next year is capable of being met.

4.2 Financial Targets

4.2.1 Boards are now set three limits by the Scottish Executive:

- a Revenue Resource Limit;
- a Capital Resource Limit;
- a Cash Requirement.

4.3 Financial Out-turn

4.3.1 In 2004/05 the Board stayed within all three targets. Details of the actual outturns against the three targets are given on page 12 of the accounts.

Table 1 – Financial Targets

<i>Financial Target</i>	<i>Objective</i>	<i>Actual 2004/05</i>
Revenue Resource Limit	£426.864m	£421.464m
Capital Resource Limit	£6.807m	£6.200m
Cash Requirement	£417.671m	£404.158m

4.3.2 The achievement of the Revenue Resource Limit was again met this year through a mix of non-recurring monies and other measures, including late allocation of funds from SEHD to meet in-year cost pressures, capital to revenue transfer, the use of carry forward funding, other expenditure deferred into 2005/06, slippage in the use of ring-fenced monies and the achievement of some recurring and non-recurring savings.

4.3 Financial Out-turn (Cont'd)

4.3.3 The Capital Resource Limit was originally set at £12.407 million but was later revised to £6.807 million. There was an underspend of £0.607 million against the revised target. With the permission of SEHD the Board has carried forward a facility of £5.600 million from the 2004/05 limit for use in the capital budget in 2005/06.

4.3.4 The Board fell within its cash limit for 2004/05.

4.4 Financial Performance

4.4.1 Financial performance in one sense can be measured by securing financial balance in year and in that regard the Board met its financial targets while also reporting an overall underspend of £5.4 million. As stated above the achievement of the underspend came about through various means.

4.4.2 In terms of performance against the approved financial plan, initial calculations, without allowing for further income or the impact of savings efforts, projected a potential maximum overspend of £7.521m. This figure shifted over the year, with changing circumstances in both of those aspects and through slippage in expenditure, to an underspend of £5.4m at the year end, a movement of £12.921 million. As required the financial plan reported to the SEHD did not change throughout the year. The plan reported a projected excess against RRL of £6.687 million. Financial reporting to the Finance and Resources Committee and the Board throughout the year highlighted on-going changes in projected year-end forecasts. The reported position to the Board on 25 January 2005, representing the position at 31 December 2004, highlighted a year-end forecast of £0.5 million overspend. The last three months of the financial saw the overspend move to an overall underspend of £5.4 million by 31 March 2005.

4.4.3 The performance against the reported financial plan is set out below:

Table 2 – Financial Performance against plan

Revenue Resource Analysis	Actual £m	Plan £m	Variance £m
Clinical Service Costs	450.898	429.098	21.800
Non-Clinical Costs	24.935	30.414	(5.479)
Total Gross Expenditure	475.833	459.512	16.321
Miscellaneous Income	35.321	25.135	(10.186)
Net Operating Costs	440.512	434.377	6.135
FHS and LHC	19.048	18.484	(0.564)
Net Resource Outturn	421.464	415.893	5.571
Revenue Resource Limit	426.864	409.206	17.658
Savings/(excess) against RRL	5.400	(6.687)	12.087

4.4.4 The outturn underspend includes £1.025 million of unutilised capital to revenue allocation as a result of the cancellation of a proposed relocation of services provided by Forth Park Hospital, Kirkcaldy. This underspend has been carried forward to 2005/06 with the approval of the SEHD. Other ring fenced allocations suffered slippage in expenditure in 2004/05 resulting in unutilised expenditure of £2.126 million. Corporate directorates were also underspent during the year creating an overall underspend of £5.4 million. Additions to the initial RRL facilitated additional clinical spend however clinical services were overspent against budget for the year.

4.5 Financial Planning for 2004/05

- 4.5.1 Financial planning for 2004/05 identified the potential for a financial imbalance within the Fife NHS system. The main issues were highlighted in the 2004/05 Resource Allocation and Financial Framework paper that went to the Board on 25 May 2004. The Framework identified that despite a substantial uplift in funding for 2004/05, if all assumptions made at that time were borne out there would be a need to generate internal savings of up to £7.521 million to cover the impact of anticipated expenditure in 2004/05.
- 4.5.2 The Board approved specific corporate, resource transfer, voluntary sector, NHS Lothian and NHS Tayside allocations and endorsed the proposed savings approach set out in the Framework. No clear route was offered around the setting of the operational budgets; however the Board were advised of three possible options. The Board remitted to the Chief Executive, the Divisional Chief Executives and the Divisional Boards to agree the detailed sums allocated to the operational budgets.
- 4.5.3 The Challenge Group, a sub-group of the Board's Strategic Management Team, identified the potential for cost reductions across five broad areas of procurement, estate, managerial/staffing, clinical and miscellaneous. These areas were concerned with strategic and system-wide opportunities and would be taken forward in addition to the normal savings actions taken as part of budget management at both Divisions.
- 4.5.4 The Challenge Group, chaired by the Board's Director of Finance, met throughout 2004/05 and considered various savings initiatives and the scope for in-year and recurring savings. In total 36 savings schemes were identified and by March 2005, 32 schemes had agreed templates setting out the scope for savings, the lead officer(s), the expected date for implementation and the targets for in-year and recurring savings.
- 4.5.5 By March 2005 a summary of the overall savings target position was as follows:

Table 3 - Summary of savings schemes and targets

Status at 3 March 2005					
Scheme Details	No. of Scheme Elements	Templates Done	Templates O/S	2004/05 £m	2005/06 £m
Total General Issues	3	3	0	1.398	1.398
Total Procurement	11	10	1	0.234	0.816
Total Estate and Facilities	12	12	0	0.053	1.269
Total Organisational Change	3	1	2	0	0
Total Clinical	5	4	1	2.400	1.550
Total Miscellaneous	2	2	0	0.028	0.044
Total savings targets	36	32	4	4.113	5.077

4.5 Financial Planning for 2004/05 (Cont'd)

Audit comment

- 4.5.6 We welcome the approach now being taken by the Board in investigating opportunities for internally generated efficiency and cash releasing savings. The pace of developing and implementing strategic and system-wide initiatives has perhaps been influenced in some part by the evolving nature of single system working and the wider agenda for the development and implementation of the new corporate governance and operational structures.
- 4.5.7 Progress around the initiatives has been taken forward at various levels and to different timeframes. While the summary of savings status report at March 2005 identifies savings targets it is not clear from the financial reporting arrangements at the Board the scale to which the targets have been met during 2004/05 and whether the targets for future years will be achieved.
- 4.5.8 Routine budget management during 2004/05 at Board and Operating Divisions levels included on-going review by senior management of progress in the achievement of savings. While an overall saving of £5.4 million against the RRL was achieved by 31 March 2005 the Operating Divisions were £2.6 million overspent indicating a recurring funding gap that has not been addressed through savings initiatives at strategic or operational level. The bridging of the overspend has been made largely through non-recurring means.
- 4.5.9 We believe it is now imperative that the Board ensures that savings initiatives are taken forward to agreed timescales and that progress is monitored and reported appropriately. We believe that without the achievement of internally generated efficiency savings the Board will have to fully address key decisions on the range and level of services Fife NHS can afford to deliver. Robust information is key to this process. In our view there is a need for greater clarity of information on the level of the Board's recurring funding gap and the scope for the realistic achievement of recurring internally delivered savings.

4.6 Financial Planning for 2005/06

4.6.1 For the purposes of this report we have summarised the projected 2005/06 financial position for NHS Fife in the table below:

Table 4: Financial Framework 2005/06

	£m	£m	£m
Expenditure			
Clinical Services - Local			
Operating Division	134.2		
Community Health Partnerships	106.2		
Primary Care Services/ PMS	134.3		
Depreciation of buildings	10.9		
Clinical Services – Other		385.6	
		67.4	
Total Clinical Services			453.0
Non-Clinical Costs			
Administration		19.6	
Other		12.7	
Specific reserves and contingencies		15.1	
Total Non-Clinical Costs			47.4
Total Forecast Expenditure			500.4
Income			
Carry forward underspends (estimate)		4.0	
Carry forward capital to revenue underspend		1.0	
2005/06 capital to revenue transfer		2.4	
Allocations		486.4	
			493.8
Shortfall against Income			(6.6)
Reinvestment target			6.9
Excess against RRL			0.3

4.6.2 In approving the financial framework the Board has built in a reinvestment target of 1.9% (£6.954m) of the forecast expenditure excluding Primary Care Services/PMS to be achieved in order to help fund service enhancements, new pressures, and the development reserve.

4.6 Financial Planning for 2005/06 (Cont'd)

4.6.3 To ensure longer term financial sustainability the Board has recognised the need for improved efficiencies around four principal areas of the service. These cover costs associated with “Did not attend” (DNAs), locum, bank and agency staff costs, delayed discharges and absence levels. The quantum of resources tied up in these areas is estimated at:

	£m
DNAs	2.0
Locum, bank and agency staff costs	4.0
Delayed Discharges	5.0
	<hr/>
Potential savings	11.0
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In addition, the Board recognises the potential for significant efficiency savings through tackling absence levels. The Board estimate current absence levels average out at 6.5%, on a pay bill of nearly £200 million.

4.6.4 While it is recognised that there will never be a position where these resources can be fully released there is considerable scope for improvement in the management arrangements covering these areas and that appropriate action could generate significant recurring savings.

4.6.5 Targets for the achievement of savings for these areas are to be set and thereafter monitored by the Board’s Challenge Group.

Audit comment

4.6.6 It is not clear from the financial framework or other finance papers submitted to the Board or its Finance and Resources Committee the extent of the Board’s expenditure and income that are of a recurring nature. While the Board has approved the setting of a reinvestment target of £6.954 million for 2005/06 it is unclear whether the Board is fully aware of the scale by which NHS Fife requires to deliver recurring savings in order to achieve recurrent balance.

4.6.7 There continues to be an expectation that for future years non-recurring measures will assist in securing in-year financial balance.

4.6.8 The ability to deliver the reinvestment target of £6.954 million will depend upon active and focussed budget management at operational level and the achievement of savings from the four identified strategic and NHS Fife-wide initiatives. The approved financial framework for 2005/06 highlights the reinvestment target across clinical and non-clinical services however it is not clear how much is to be met from routine budget management and from the four initiatives. Further it is not clear how much of the reinvestment target is to be achieved from recurring savings.

4.6.9 The work of the Challenge Group will be critical in ensuring that sufficient and timely resource will be given to develop, approve and implement the strategic and NHS Fife-wide initiatives.

4.6.10 *The Board, through its Finance & Resources Committee, should seek greater clarity as to the underlying financial position on recurring and non-recurring income and expenditure to allow it to identify more precisely the Board’s recurring funding gap. This then would allow the Board to understand more fully the funding issues and the scale of the required level and timing of corporate and operational savings and efficiency improvements.*

4.6 Financial Planning for 2005/06 (Cont'd)

- 4.6.11** *A breakdown of the reinvestment target of £6.954 million for 2005/06 between operational savings and those expected from the four strategic and NHS Fife-wide initiatives should be provided to, and monitored by, the Finance & Resources Committee and thereafter reported to the Board.*
- 4.6.12** *The Finance and Resources Committee should take an active role in reviewing the work of the Challenge Group charged with the delivery of the Board's reinvestment target of £6.954 million for 2005/06.*

5. SIGNIFICANT MATTERS

5.1 Governance Arrangements

- 5.1.1 Following the commitment given by the Board's Chairman and the Chair of the Board's Audit Committee at the Board meeting on 30 July 2004 steps have been taken to improve the governance arrangements during 2004/05. There remain areas to be addressed and these were highlighted in the Board's 2004/05 SIC. The approach taken has been to evolve the governance arrangements.
- 5.1.2 Further improvements have taken place since March 2005 and more are planned, in particular these areas include the finalisation of corporate governance arrangements, implementation of the Risk Management Strategy, taking forward workforce planning, further development of single-system frameworks in a number of areas and the creation of a robust performance management framework. In our view the Board needs to ensure effective project management arrangements are in place to provide the timely delivery of single system working.
- 5.1.3 Issues in our Report 2005/07; *Overall Arrangements 2004/05*, will be followed up and reported as part of our 2005/06 audit.
- 5.1.4 ***The Board should agree an action plan to ensure that the areas of internal control, governance and risk management that were highlighted for improvement in the 2004/05 SIC are taken forward to an agreed timetable. Periodic reporting of progress towards the action plan should be taken to the Board through the Audit and Clinical Governance Committees.***

5.2 Financial Governance

- 5.2.1 In past years we have highlighted the need for improvement in the financial governance arrangements at the Board. A number of improvements have been implemented during 2004/05 including the formation of the Board's Finance and Resources Committee, the inclusion in the Local Health Plan of a resource allocation and financial framework, Board development sessions on financial matters, and a Challenge Group responsible for driving savings targets. A new financial ledger system came into operation on 1 April 2004, and from the results of our work and work undertaken by NHS Fife internal audit services we have concluded that the new system is operating satisfactorily.
- 5.2.2 The creation of the Board's Finance & Resources Committee has generally been well received by executive and non-executive members of the Board and by the Board's wider executive team. Board and non-executive member awareness of the financial issues faced by the Board has improved; this greater understanding has allowed the Committee to play its part in the development of an improved financial governance culture within the Board. Financial matters are considered in greater depth and analysis with the Committee challenging key assumptions underpinning financial and investment plans.
- 5.2.3 The financial reporting to the Finance & Resources Committee and then to the Board does however vary in style and content making it difficult to fully map across the considerations and decisions of the Committee to that presented to the Board. This point was raised by the Chair of the Committee who went on to suggest that it would be useful if presentations could be kept the same to compare differences. The point was noted by Board members.

5.2 Financial Governance (Cont'd)

- 5.2.4 Internal audit arrangements within the Board were through the agency arrangement with FTF Audit and Management Services (FTF). The Board hosts this agency. Our review of the arrangements at FTF confirmed that, while there were areas for further improvement, including a more timely delivery of audit outputs, FTF demonstrated general compliance with many of the areas laid down in the code of good practice and the NHS Standards.

5.3 Planning and Performance Management

- 5.3.1 The Board approved its Local Health Plan for 2004/05 on 25 May 2004. Internal Audit carried out a review of the Plan and while identifying improvement over previous years around national commitments and the setting of SMART objectives they expressed disappointment with the lack of SMART objectives having been set for local and regional commitments, staffing and finance resource issues.
- 5.3.2 The agreed implementation of quarterly reporting to the Board of progress with the Plan was not actioned during 2004/05. There has been no specific or comprehensive Plan monitoring reports provided to the Board during the year although certain elements of performance reporting has been made to Board members through other means. NHS QIS while noting the evolving nature of the Board's performance management process commented on the absence of a robust performance management framework and that it is recognised that performance management reporting to the Board lacked a coherent approach to key drivers and targets. The NHS QIS report noted an ad-hoc nature to regional planning.
- 5.3.3 The Board Statement on Internal Control stated that in 2005/06 a balanced scorecard technique will be used to ensure that performance against objectives is regularly reported to the Board. Initial discussions on the use and possible style of the balanced scorecard were led by the Chief Executive and considered by the Board at its meeting on 25 January 2005 and were followed up in meetings of the Executive officers during early 2005. The intention is to share the balanced scorecard with the Remuneration Sub-Committee as part of determining individual director objectives for 2005/06. It was planned that the Board receive the balanced scorecard at its May or July 2005 meetings for consideration and approval. The balanced scorecard has not yet been finalised and taken to the Board.
- 5.3.4 The Board's Strategic Implementation Groups were established to enhance the planning process across the Fife NHS system covering differing disciplines. These Groups are at differing stages of development and are to be further developed during 2005/06. These Groups are expected to play a significant role in the service redesign agenda and in the allocation of change and innovation monies.

Audit Comment

- 5.3.5 The Board has recognised the need for robust and timely performance management arrangements to be implemented and see the introduction of the balanced scorecard as the appropriate means of recording objectives and the measured progress towards their achievement. As an area of adverse comment by external audit, internal audit and NHS QIS it is imperative that the balanced scorecard is finalised for consideration and approval of the Board as a matter of urgency.

5.3 Planning and Performance Management (Cont'd)

Audit comment (Cont'd)

- 5.3.6 Despite previous commitments to report progress quarterly to the Board no such reporting took place during 2004/05. Following approval of the balanced scorecard, progress reporting to the Board must be implemented
- 5.3.7 The involvement of the Board's Remuneration Sub-Committee in seeking to link the Plan objectives to the individual objectives of the executive directors is important to ensure clarity of responsibilities and allow the means by which performance can be more directly measured to the achievement of corporate objectives.
- 5.3.8 *The Board's performance management and reporting arrangements through the use of a balanced scorecard approach must be finalised, approved and implemented without further delay.*
- 5.3.9 *The Board should ensure that the use of the balanced scorecard approach is appropriately applied and recorded by its Remuneration Sub-Committee in carrying out its role of assessing the performance of the executive director group.*

5.4 IM&T Strategy

- 5.4.1 Internal Audit reported concerns with the lack of an explicit link between the Board's IM&T Strategy to the local operational aims and objectives, especially the Local Health Plan. Further they commented upon a number of deficiencies in the strategy and its implementation. The strategy, approved by the Board in July 2003, was due for renewal by 31 March 2005 however no new strategy had been prepared and presented to the Board by the end of the financial year.
- 5.4.2 In July 2005 the Board received a paper; eHealth Strategy 2005-2007, that proposed a refreshing of the IM&T Strategy to take account of the national agenda for the development of a standard set of clinical products that will facilitate data collection and data sharing. While aimed at broadening the IM&T agenda the Board requested that further work on the IM&T /eHealth Strategies be carried out.

Audit Comment

- 5.4.3 The development and effectiveness of IM&T strategies in the NHS has been subject to previous adverse audit comment representing an area of the NHS that requires further improvement. The Board has not fully achieved the successful implementation of its previous IM&T Strategy leading to the necessary disclosure in the 2004/05 Statement on Internal Control. This may in part be due to IM&T being a fast-moving field where the target keeps moving. While developing its new IM&T/eHealth Strategies the Board must take account of the developing national eHealth agenda together with the operational needs of NHS Fife. Once approved the Board must ensure improvement in the arrangements for and timeliness of the implementation of the strategies.

5.4 IM&T Strategy (Cont'd)

Audit Comment (Cont'd)

5.4.4 It is likely that separate disclosure on IM&T/eHealth issues will again be required in the Board's Statement on Internal Controls for 2005/06.

5.4.5 *The Board must ensure the early development, approval and successful implementation of its revised IM&T/eHealth Strategies taking account of national and local needs*

5.5 Capital Planning

5.5.1 Capital planning within the Fife NHS system will need to be considered in light of the developments that flow from the Right for Fife Strategies and the development and implementation of the Joint Future agenda. Ongoing consideration of the estate planning within Fife NHS will be important to ensure appropriate short and long-term requirements are accommodated in a cost effective manner. In this regard the Director of Finance has developed for submission to the Finance & Resources Committee and the Board a formal capital plan showing the current and next three years' proposed capital programme. The Committee continues to consider and monitor capital planning issues.

5.5.2 Internal audit reported that while separate disclosure of capital planning weaknesses was required in the Statement on Internal Control in 2003/04 improvement in the capital planning arrangements have been made during 2004/05 removing the need for disclosure in 2004/05. However internal audit state that there continues to be a lack of NHS Fife capital planning and investment control guidelines and a lack of project management guidelines increasing the risk faced by the organisation in this aspect of its affairs.

5.5.3 *The Board, through its Finance & Resources and/or Audit Committees should continue to seek assurance that steps to address reported weaknesses in the capital management arrangements have been taken.*

5.6 Primary Care

5.6.1 While there has been an improvement in the control environment at National Services Scotland (NSS), formerly Common Services Agency (CSA), there remain weaknesses that present risk to the payment of primary care contractors. The Service Auditors found no "business critical" weaknesses and of the 55 control weaknesses 2 were regarded as high priority. These related to security and access issues. There remain 5 high priority issues unresolved from the previous year. These relate to security standards and monitoring, access controls, prior approval reconciliations and system validation. Based on the evidence available we were able to confirm no qualification of our opinion in relation to the regularity of FHS expenditure.

5.6.2 Our Management Letter; Report 2005/09; *2004/05 Year-End Audit Issues*, highlighted the results of the work carried out by the Counter Fraud Service around patient exemption checking. The results indicate a degree of ineligible claims and a potential loss of income to the NHS in Fife and to the NHS in Scotland. (Section 7 refers)

5.7 Joint Working and Joint Future

- 5.7.1 Our audit work in 2004/05 on the progress of the development of Joint Future arrangements is underway and will be reported to both the Board and Fife Council following receipt of information awaited from the Council. The main issue going forward is to ensure that CHP development is fully considered and that the development of Joint Future and CHPs move forward together to achieve local and national priorities.
- 5.7.2 We will continue to carry out an overview of the developing arrangements as part of our 2005/06 audit.

5.8 Financial Plans

- 5.8.1 As identified previously there remains the potential for financial imbalance within the Fife NHS system. Our comments at section 4 of this report highlight the expectation that the use of non-recurring monies and measures will again be necessary in 2005/06. The delivery of internally generated savings from the identified initiatives will be key in ensuring financial balance while facilitating the funding for service enhancements, new cost pressures and development.

5.9 Pay Modernisation

General Medical Services Contract

- 5.9.1 The new contract for General Medical Services (GMS) was introduced on 1 April 2004. Contracts with all Fife GP practices were signed by 2 April 2004. All of the practices in Fife opted out of providing Out of Hours Service and the Board took over the responsibility for the provision from 12 July 2004. The contract has introduced a major financial burden on the Board not fully matched by specific funding.
- 5.9.2 NHS Fife Internal Audit Service undertook two reviews related to GMS contracts during the year relating to quality payments and enhanced services. We have reviewed the work and have taken assurance on the operation of the GMS contract in this first year. The results from both reviews were assessed as broadly satisfactory.

New Consultants' Contracts

- 5.9.3 The new contract was offered to consultants from 1 April 2004. NHS Fife internal audit services reviewed the processes used in implementing the contracts and assessed whether these had complied with SEHD national standards. The overall assessment was broadly satisfactory. Implementation was in line with national guidance and, while the process of implementation had taken longer than the originally recommended timescale the outcome was satisfactory, with contracts and job plans meeting the required Service Redesign expectations.

5.9 Pay Modernisation (Cont'd)

Agenda for Change

Job Evaluation and Appeals

- 5.9.4 The job evaluation sub-group of the NHS Fife Agenda for Change Steering Group has worked in partnership to develop a framework and process to support staff and managers through the job evaluation process. Awareness sessions were held throughout NHS Fife to cover all three aspects of Agenda for Change including job evaluation. The appeals procedure is currently under discussion and we have been advised that this will be concluded shortly. It was noted that national clarification around some elements of the appeals process is required to define which elements can be determined at a local level as opposed to nationally.

Job Description – Matching Panels

- 5.9.5 The original national timetable specified that all posts were to be matched by 31 July 2005. However, due to the delay nationally in reaching a formal agreement this timetable has been revised to 30th September 2005. We have been advised that progress to date in relation to job matching is satisfactory with NHS Fife being a leading mainland Board in implementing Agenda for Change within NHS Scotland (as at 31 July 2005). Job matching progress is constantly monitored in relation to meeting the national timetable.

Terms and Conditions of Service

- 5.9.6 The terms and conditions sub-group of the NHS Fife Agenda for Change Steering Group is working in partnership to consider all of the issues arising from the implementations of the new terms and conditions of service contained within the Agenda for Change agreement. An internal system has been established to provide managers and staff with expanded guidance with ten specific topics addressed to date. Any issues arising from the new terms and conditions of service which are common across NHS Scotland are being addressed via national networking events, the Scottish Pay Reference and Implementation Group (SPRIG) and NHS Staff Council as appropriate.

Costing Model

- 5.9.7 A costing model has been developed and scrutinised which assesses the likely impact of assimilation on members of staff. This has allowed an additional cost to be calculated, including best estimates for backfill as appropriate. As the matching process progresses, groups of staff can be put forward to obtain the necessary national agreement to allow the Board to pay these staff under the revised arrangements. Work on obtaining the relevant national approval is progressing in line with the outcomes of the job matching process outlined above.

6. REGULARITY WORK

6.1 Introduction

- 6.1.1 In November 2004, we issued our Report 2005/01; *Strategic Plan 2001/06 and Operational Plan for 2004/05*. These original plans prepared in 2001 have annually been updated and revised to take account of emerging issues within the Board, dissolution of the Fife NHS Trusts, implementation of the new financial ledger and move to shared financial services, changes in our original assessment of the audit risk scores arising from our 2003/04 interim and year-end reviews, our work across all areas of our remit, changes in regulations and accounting practices and our review of the plans for and findings of internal audit work. We also considered if specific systems require to be revisited and if planned reviews should be brought forward in order to inform our overall opinion on the Board's system of internal control for the current year.
- 6.1.2 Our updated audit needs assessment, revised Strategic and Operational Plans were discussed and agreed with the Director of Finance. The plans were discussed with members of the Board's Audit Committee on 19 January 2005 and our proposed fees agreed.

6.2 Overall Conclusion

- 6.2.1 From our regularity work and from audit assurances received in respect of shared arrangements, we were satisfied that there were no material matters arising, which adversely affected our audit reports for the year to 31 March 2005.
- 6.2.2 Separate management reports detailing our regularity audit have been issued and discussed with the Director of Finance and considered by the Audit Committee. Action plans to address issues raised have been agreed as necessary.

7. LEGALITY, FRAUD AND CORRUPTION

7.1 Legality

Responsibilities

7.1.1 External auditors have a duty to give an independent assessment of the audited body's arrangements for ensuring the legality of transactions that might have a financial consequence. As discussed in section 3 we now have an extra responsibility placed on us by the Public Finance and Accountability (Scotland) Act 2000 to certify on the regularity of transactions included in the Board's accounts.

7.1.2 It is the responsibility of audited bodies and their officers to act within the law. It is the auditor's responsibility to bear in mind the question of legality and to take reasonable steps to inform themselves of significant financial transactions or events that are unusual or of questionable legality, for example by:

- reviewing the arrangements in place within the audited body for ensuring the legality of financial transactions;
- reviewing the minutes of committee and board meetings;
- holding discussions with officers;
- having regard to the audited body's implementation of significant new legislation, significant statutory requirements, and SEHD circulars;
- reviewing the local applicability of relevant national issues;
- taking account of advice issued by Audit Scotland;
- reviewing statutory requirements concerning the financial statements;
- having regard to matters which come to our attention where legality, losses or deficiencies may be an issue.

7.1.3 Where it is believed that a decision by an audited body or officer has incurred, or would involve, unlawful expenditure, or that some action has been, or would be, unlawful and likely to cause a loss or deficiency, then auditors must report the matter. In addition as stated above we are required to report our audit opinion on the regularity of transactions in the audit report placed on the annual accounts.

Findings

7.1.4 We are able to confirm that arising from our review of the legality of transactions there are no issues that we are aware of, or which have been brought to our attention, which require to be reported for 2004/05. Issues arising from our consideration of the regularity of transactions are discussed in our Management Letter; Report 2005/09. Our audit report for the Board included unqualified opinions.

7.2 Fraud and Corruption

Responsibilities

- 7.2.1 The primary responsibility for the prevention, detection and investigation of irregularities including fraud and corruption rests with management who should institute an appropriate system of internal control including segregation of duties, proper authorisation and approval processes, reconciliation procedures and an effective internal audit function.
- 7.2.2 In accordance with the Code of Audit Practice our responsibility is to assess the adequacy of the systems and arrangements made by management to prevent and detect fraud and corruption, and to plan our audit so that we have a reasonable expectation of detecting material mis-statement in the relevant financial statements resulting from fraud or irregularity.

Findings

- 7.2.3 As an interim measure ahead of the CFS partnership agreement coming into force the Board's Audit Committee approved in January 2005 an Anti-fraud, Theft and Corruption Policy and Response Plan as part of the revised Financial Operating Procedures (FOPs). For the earlier part of 2004/05 the Board operated with the former fraud policy and investigation procedures of the Board and the Fife NHS Trusts. Internal Audit commented on the lack of widespread awareness of the new FOPs and that there had been no anti-fraud messages issued to staff during 2004/05. Management have recognised the need for further work to be undertaken during 2005/06 to raise awareness with staff on this issue.
- 7.2.4 As in past years Patient Exemption Checking (PECS) was carried out by the Counter Fraud Service (CFS) across Scotland. The work carried out by CFS revealed a potential understatement of income in the Board and across Scotland for 2004. For Fife, the potential understatement was £1.08 million (2003 - £1.71 million). A comprehensive review of the periodic NSS reports for NHS Fife and of the activities of Fife NHS in this area was carried out and reported by management to the Board's Audit Committee. Our review of the report and other supporting evidence confirms that the Board has taken appropriate steps in assessing the level of potential exemption fraud and its potential impact on the regularity of income. We formed the view that the potential understatement of income was not material and accordingly our opinion was unqualified in relation to the regularity of FHS income.
- 7.2.5 One first tier fraud report has been issued to Audit Scotland. This case involved the loss of IT equipment with an estimated value of £10,000. A second tier fraud report was also issued to Audit Scotland. This identified six individual cases of reported fraud below £2,000 per case. In total the estimated loss is £1,912.

8. OVERALL ARRANGEMENTS

8.1 Introduction

8.1.1 We are required, as external auditors, to satisfy ourselves that the Board has made adequate and appropriate arrangements to secure economy, efficiency and effectiveness in the discharge of its functions. In order to do this we consider a wide range of issues and information gained in all areas of the audit. These include consideration of the organisation's management structure, the roles and responsibilities of the management team, and the recording, monitoring and reporting mechanisms both from an operational and strategic viewpoint. Studies that are centrally directed by the Audit Scotland may also form part of this work.

8.2 Management Arrangements

8.2.1 Management arrangements cover a wide range of procedures designed to allow both executive and non-executive management to discharge their responsibilities with regard to the stewardship of public funds. They should cover planning, appraisal, authorisation and control over the use of resources. Good internal and external communication and adherence to sound corporate governance principles are essential to the operation of the arrangements.

8.2.2 Our work on this aspect of the Board's affairs was summarised in Report 2005/07; *Overall Arrangements 2004/2005*, issued on 14 July 2005 and presented to the Audit Committee at its meeting on 22 July 2005.

8.2.3 Our work covered single system working, corporate governance, financial governance, performance management, risk management, workforce planning, Community Health Partnerships and Joint Future and Joint Working. We carried out follow up reviews on waste management, community equipment and adaptations, resource transfer and internal audit. We also carried out a national study on staff governance.

8.2.4 Progress has been made during 2004/05 however further improvement is needed in order to establish a sound governance framework. In our opinion areas for improvement include the finalisation of corporate governance arrangements, implementation of the risk management strategy, taking forward workforce planning, further development of single-system frameworks in a number of areas and ensuring effective project management arrangements are in place to provide the timely delivery of single system working and the creation of a robust performance management framework.

8.2.5 While we have not qualified our audit opinion, there remain a number of issues that relate to the adequacy and appropriateness of the Board's arrangements to secure economy, efficiency and effectiveness in the discharge of its functions that require to be addressed. It is important that further progress is made during 2005/06.

ACTION PLAN

Para Ref.	Recommendation	Comments	Agreed	Responsible Officer	Agreed Completion Date
4.6.10	<p>Financial Planning for 2005/06</p> <p>R1 The Board, through its Finance & Resources Committee, should seek greater clarity as to the underlying financial position on recurring and non-recurring income and expenditure to allow it to identify more precisely the Board's recurring funding gap. This then would allow the Board to understand more fully the funding issues and the scale of the required level and timing of corporate and operational savings and efficiency improvements.</p>	The role of the Finance & Resources Committee, and the style and content of information it considers, is an evolutionary process.	YES	Director of Finance	Ongoing during 2005/06
4.6.11	<p>R2 A breakdown of the reinvestment target of £6.954 million for 2005/06 between operational savings and those expected from the four strategic and NHS Fife-wide initiatives should be provided to, and monitored by, the Finance & Resources Committee and thereafter reported to the Board.</p>	Comment as above.	YES	Director of Finance	Ongoing during 2005/06
4.6.12	<p>R3 The Finance and Resources Committee should take an active role in reviewing the work of the Challenge Group charged with the delivery of the Board's reinvestment target of £6.954 million for 2005/06</p>	Comment as above.	YES	Chair of Finance and Resources Committee	Ongoing during 2005/06

ACTION PLAN

Para Ref.	Recommendation	Comments	Agreed	Responsible Officer	Agreed Completion Date
5.1.4	<p>Governance Arrangements</p> <p>R4 The Board should agree an action plan to ensure that the areas of internal control, governance and risk management that were highlighted for improvement in the 2004/05 SIC are taken forward to an agreed timetable. Periodic reporting of progress towards the action plan should be taken to the Board through the Audit and Clinical Governance Committees.</p>	This is already recognised as a necessary step.	YES	Chief Executive	30 September 2005
5.3.8	<p>Planning and Performance Management</p> <p>R5 The Board's performance management and reporting arrangements through the use of a balanced scorecard approach must be finalised, approved and implemented without further delay.</p>	This process is already under way.	YES	Chief Executive	30 November 2005
5.3.9	<p>R6 The Board should ensure that the use of the balanced scorecard approach is appropriately applied and recorded by its Remuneration Sub-Committee in carrying out its role of assessing the performance of the executive director group.</p>	As above.	YES	Chair of Sub-Committee	Post 31 March 2006
5.4.5	<p>IM&T Strategy</p> <p>R7 The Board must ensure the early development, approval and successful implementation of its revised IM&T/eHealth Strategies taking account of national and local needs</p>		YES	Executive Lead for IM&T	30 November 2005

ACTION PLAN

Para Ref.	Recommendation	Comments	Agreed	Responsible Officer	Agreed Completion Date
5.5.3	<p>Capital Planning</p> <p>R8 The Board, through its Finance & Resources and/or Audit Committees should continue to seek assurance that steps to address reported weaknesses in the capital management arrangements have been taken.</p>	Already in the work programme for the Audit Committee.	YES	Director of Finance <u>and</u> Director of Operations	31 December 2005