
NHS Shetland

Annual Report to Members and the
Auditor General for Scotland

2010/11

June 2011

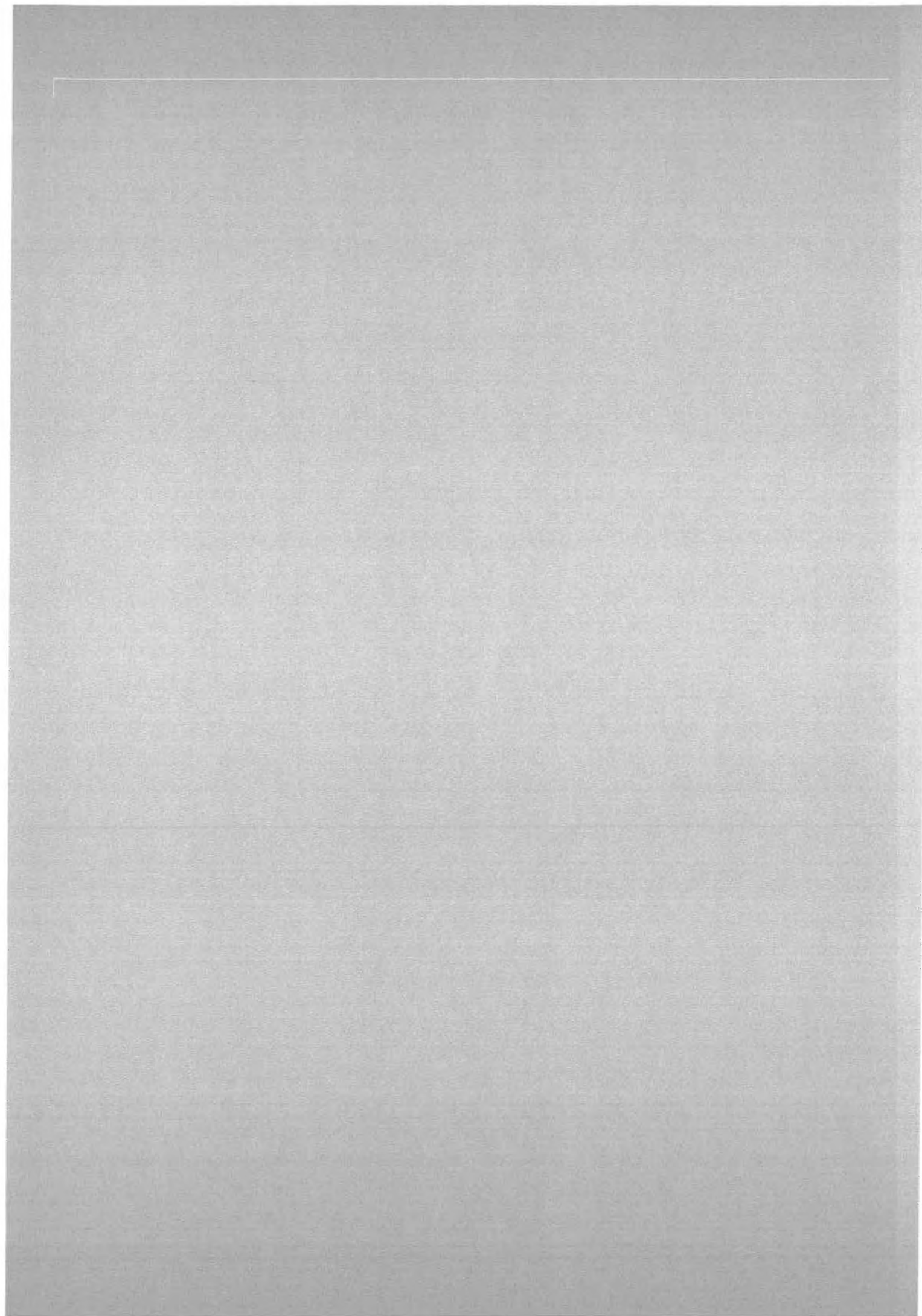
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The principal objective of our audit procedures is to enable us to express our opinion, in line with the requirements of the Audit Scotland Code of Audit Practice, on the financial statements as a whole. Our audit opinion does not guarantee that the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

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

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



1. *Executive Commentary*

Introduction - Section 2

Our overall responsibility as external auditor of NHS Shetland (“the Board”) is to undertake our audit in accordance with the principles contained in the Audit Scotland Code of Audit Practice (“the Code”), revised and published in March 2007. We have a dual reporting responsibility for the audit: to the Board Members of NHS Shetland and to the Auditor General for Scotland.

Financial Statements and Audit Opinions - Section 3

The financial statements of NHS Shetland for the year ended 31 March 2011 have been prepared to comply with accounting requirements contained in the NHS Board Accounts Manual for Directors’ Report and Accounts of NHS Boards and for Scottish Financial Returns, and supplementary guidance, as issued by the Scottish Government Health Directorates (SGHD) and approved by the Scottish Ministers. We are pleased to report that our opinion on the financial statements for the year ended 31 March 2011 is **unqualified**.

We also provide a view as to whether those parts of the Remuneration Report subject to audit have been properly prepared. Our opinion on the Remuneration Report is **unqualified**. Our audit opinion does not extend to any other part of the Directors’ Report.

As a result of our work, we proposed a number of disclosure adjustments, none of which were financial. All of these have been processed by management in the finalised version of the 2010/11 financial statements.

Four significant accounting issues were noted during the 2010/11 financial statement audit. These include the change in accounting policy in relation to the cost of capital and the revision of asset useful lives. The accounting treatment of these changes has been confirmed in the preparation of the 2010/11 financial statements, with no unadjusted misstatements remaining. However, there are a few issues that require further action from NHS Shetland management to resolve.

2010/11 Performance - Section 4

NHS Shetland budgeted for a break even position for the year to 31 March 2011. The final outturn was a surplus against the core Revenue Resource limit of £0.461 million.

Capital expenditure was under spent by £0.115 million against a core capital resource limit of £2.111 million, representing an overall net surplus of £0.576 million.

In year performance included savings of £1.3 million which was essential in allowing the Board to achieve their budgeted break-even position.

In addition to their financial targets NHS Shetland also made progress towards the achievement of its non-financial performance targets.

Looking Forward - 2011/12 - Section 5

A break even budget has been approved for 2011/12. The Board requires £1.675 million of cash releasing savings to achieve the break even position reflecting the increased cost pressures that are expected to exceed the SGHD funding package with a budgeted 1% uplift from 2010/11. Achievement of this internal savings target exceeds the SGHD requirement of £1.1 million cash release savings.

The Board has agreed a challenging savings target of £1.675 million. At the time of this report, £1.265 million has been identified, leaving £0.41 million as yet unidentified.

Governance and Control - Section 6

We have assessed the Board's overall governance arrangements including a review of Board and key Committee structures and minutes, financial reporting to the Board, and risk management. We consider that appropriate arrangements and reporting appear to be in place. We have also considered key areas of risk to the Board including partnership working; service sustainability; performance management; and people management. Appropriate evidence of activity has been provided by NHS Shetland.

The Code of Audit Practice requires us to review and report on NHS Shetland's Statement on Internal Control. NHS Shetland has used the correct format for its Statement and has outlined the processes it had employed to identify and evaluate risks. In addition, key elements of NHS Shetland's control framework have been highlighted.

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

2. Introduction

Purpose of this report

Our Annual Audit Report which follows is designed to set out the scope, nature and extent of our audit, and to summarise our opinion and conclusions on issues arising. Specifically this will direct your attention to matters of significance that have arisen out of the 2010/11 audit process and to confirm what action is planned by management to address the more significant matters identified for improvement.

Scope, nature and extent of our audit

Our overall responsibility as external auditor of the Board is to undertake our audit in accordance with the principles contained in the Code of Audit Practice issued by Audit Scotland in March 2007. In this regard, the Code sets out the need for public sector audits to be planned and undertaken from a wider perspective than in the private sector involving not only assurance on the financial statements but also consideration of areas such as regularity, propriety, performance and the use of resources. It also sets out the need to recognise that the overall audit process is a co-ordinated approach involving the “appointed auditor”, the Auditor General for Scotland and other auditors such as Audit Scotland’s Health Performance and Public Reporting Group.

Our audit has been planned and conducted to take account of these wider perspectives. Under the requirements of International Standard on Auditing (UK and Ireland) (‘ISA’) 260: “Communication of audit matters to those charged with governance”, we are required to communicate audit matters arising from the audit of financial statements to those charged with governance of an entity. This Annual Audit Report to Members, together with previous reports to the Audit Committee throughout the year, discharges the requirements of ISA 260.

Acknowledgement

We would like to formally extend our thanks to NHS Shetland’s managers and staff for the assistance they have given us during this year’s audit process and over the last five years.

PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP
Glasgow
24 June 2011

3. *Audit Opinion and Financial Statements*

Audit Opinion

Our audit opinion concerns the true and fair statement of NHS Shetland's financial results for the year ended 31 March 2011 and the regularity of its income and expenditure for the year.

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

We also provide a view as to whether those parts of the Remuneration Report subject to audit have been properly prepared. Our opinion on the Remuneration Report is **unqualified**. Our audit opinion does not extend to any other part of the Directors' Report.

Audit Process

The financial statements and supporting schedules were presented to us for audit within the agreed timetable and the quality of working papers provided by management was of a high standard. This demonstrates a marked improvement on previous years. It is clear Management responded to our previously reported comments and actions have been taken which resulted in a more efficient audit process, including a more effective working relationship with your staff.

Basis of Preparation

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

Approval

The Financial Statements will be submitted to the Audit Committee on the 24 June 2011 and are to be approved and adopted at the Board meeting on 24 June 2011.

Unadjusted Misstatements

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

As a result of our work, we proposed a number of disclosure adjustments and all of these have been processed by management in the finalised version of the 2010/11 financial statements. No financial adjustments were identified and all adjustments proposed were accepted by management.

Accounting Issues

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

Bad Debts in the CDF

Through our audit work, it was identified that the current practice within the Board is to net off bad debts against income when they should be treated as a write-off through expenditure. Although the amounts are immaterial, the current accounting treatment should be revised going forward.

Action 1

Asset Useful Lives and Residual Value

International Financial Reporting Standards (IFRS) were introduced into the Public Sector in 2008, with the NHS in Scotland preparing fully IFRS compliant accounts for the first time in March 2010. One of the key elements of the introduction of IFRS accounting into the public sector has been the requirement to comply with International Accounting Standard (IAS) 16 – Property, Plant and Equipment.

One of the key elements of IAS 16 is the requirement to separately identify and depreciate assets (building) elements that have different expected lives e.g roof, lifts, electrics, etc. The elements making up the asset (building) are separated into two categories based on the past pattern of consumption and future maintenance and capital expenditure. The methodology then takes account of the fact that regular maintenance/preservation (revenue) expenditure is made on the “shorter-life” elements, e.g. internal doors, floor coverings, wall finishings. Due to this maintenance/preservation expenditure, these “shorter life” elements, which in the past reduced the life of the building, can now be assumed to last as long as the building itself – assumed by the professional valuers to be 70 or 80 years, and can also be depreciated over this period.

One of the outcomes of adopting the revised methodology is a reduced recurring annual depreciation charge. The relating reduction in the depreciation charge for the year ended 31 March 2011 for the Board was almost £180,000.

Equal Pay

The National Health Service in Scotland has received a number of claims for equal pay including related back pay. By the end of May 2011 there were claims registered against the Board, with over 11,000 registered across the country. The NHS Central Legal Office (CLO) has been instructed by the Management Steering Group of NHS Scotland in this regard and is co-ordinating the legal response of NHS Scotland to this issue.

The CLO has co-ordinated the legal response to all claims. The CLO has confirmed that the cases in Scotland are at too early a stage to allow any assessment of the potential financial exposure to be included in the financial statements. The Board has included a Contingent Liability Note in its financial statements, setting out this matter. The wording used within this note reflects guidance issued by Audit Scotland.

Removal of Capital Charge from 1st April 2010

The financial regime of health bodies has been amended to remove the Cost of Capital from 1st April 2010. This is considered to be a voluntary change in accounting policy and therefore a prior year restatement has been made. As a result, a £0.970 million charge has been removed from the 2009/10 figures in the Statement of Comprehensive Net Expenditure, Balance Sheet, Cash Flow Statement and Statement of Changes in Taxpayers Equity together with Notes 3, 4, and 6. This prior year restatement is being made by all NHS Scotland Boards.

Fixed Asset Register

An asset verification exercise was undertaken by the Board during the year 2010/11. On review of the Fixed Asset Register as part of our audit work, it was identified that some assets remained on the register when they had been disposed of. Management should seek to review the Fixed Asset Register to ensure it accurately reflects the actual fixed assets held by the Board.

Action 2

4. 2010/11 Financial Performance

<i>NHS Shetland</i>	<i>£m</i>
Recurring income	35.6
Recurring expenditure	(38.1)
Recurring savings	1.2
Underlying recurring surplus/(deficit)	(1.3)
Non-recurring income	9.1
Non-recurring expenditure	(7.4)
Non-recurring savings	0.1
Non-recurring surplus/(deficit)	1.8
Financial surplus/(deficit)	0.5
Underlying recurring surplus/(deficit) as a percentage of recurring income	3.65%

Confirmed by the Director of Finance on 10 June 2011

NHS Shetland budgeted for a break even position for the year to 31 March 2011. The final outturn was a surplus of £0.461 million.

In achieving the surplus, NHS Shetland encountered a number of other variations from budget as follows:

Clinical Services (overspend £0.558 million)

Variations on Clinical Services were principally due to both pay and non-pay factors. Locum doctor overspends occurred across the organisation, particularly within the Community Health Partnership principally due to locum doctors in Whalsay.

An over spend on nursing was mainly due to non-pay (chiefly the increasing requirement for single-use items to comply with infection control policies). There was also an over spend on pay but this was partly due to the fact that the budgets did not accurately reflect enhancement payments. Both of these issues have been addressed in the budget-setting for 2011/12.

Public Health (overspend £0.285 million)

The budget for Extra Contractual Referrals (ECRs refer to episodes of care provided to Shetland residents by providers with which the Board has no Service Level Agreement and therefore are bought on a 'cost-per-case' basis) has been showing an overspend for many years – although it is true to say that it experienced particular pressures in 2010/11.

'Cost-per case' episodes include specialist planned care such as eating disorders, child and adolescent mental health, alcohol and drug detox. Single cases can cost in excess of £100k which has a huge % impact on the budget. This will partly be resolved by the budget-setting process for 2011/12, which sought to reflect recent expenditure trends and produce more aligned budgets.

Estates & Facilities (overspend £0.496 million)

The over spend on Estates and Facilities was despite non-recurring revenue of £250,000 being made available to the budget. The £250,000 was designed to cover planned additional work and this was spent as planned. In addition, Estates and Facilities experienced significant pressure on utilities costs. Also, significant overtime costs and contractors costs were incurred, these were partly a knock-on consequence of the significant capital programme in the hospital.

The over spend did show a late deterioration due to items that had originally been budgeted as capital in nature being charged to revenue as a result of a review during the year-end financial statements process. The Board has seen a return on the investment made in Estates, with a more robust infrastructure and an increase in its SCART (Statutory Compliance Audit and Risk) score.

The capital resource limit of £2.111 million saw an under spend of £0.115 million due to items which had initially been treated as capital being reclassified as revenue expenditure towards the year end.

Finance (under spend of £0.681 million)

An under spend on Service Level Agreements (SLAs) reflected a reversal of the expected increase in usage of acute and mental health services provided by Grampian NHS Board. Activity fell in the final quarter of 2009/10 and continued to fall in 2010/11. The Board had projected forward an upward trend to December 2009 when in fact this was reversed hence the large underspend.

Management are continuing to monitor the trends and patterns within the SLA spend which will assist in producing budgets going forward that are more aligned with actual spend.

Human Resources & Support Services (under spent £0.069 million)

The budget for Computing over spent by almost £100,000 despite £250,000 of non-recurring funding being made available. Programmes for IT upgrades ran into difficulties causing a number of them to significantly overspend. This was exacerbated by the turnover of staff and consequential high costs of agency staff. An interim Head of IT is now in place, charged with stabilising the IT team and the IT infrastructure.

The over spend of £100,000 was in effect absorbed by under spends in other parts of the Directorate of Human Resources & Support Services budget, most significantly Personnel non-pay underspent by £97,000. This was due to recruitment costs and interview expenses as posts have been held open across budgets.

Reserves

There was an underspend on reserves in year as management decided not to allocate the Contingency and Risk Reserves to cover in-year pressures. This was due to a conscious decision to retain these two reserves at a corporate level and manage in-year pressures through underspends on other budgets, so as to achieve the planned underspend to be carried forward.

Budgets

It has been recognised that Management have taken steps to monitor, assess and report on budgets going forward. Reviewing actual spend against budget on an ongoing basis will assist the Board in ensuring budgets are more aligned with the actual patterns of care and spend. This will be essential in helping the board achieve its savings targets going forward.

Action 3

Savings Programme 2010/11

A detailed listing of the recurring and non-recurring savings plans has been included in Appendix 2. The larger individual savings Programmes, from the total of £1.3 million have been highlighted below for information;

Description	Recurring Savings £,000	Non-recurring Savings £,000
Completion of Nursing Service Redesign	101.0	0.0
Medicines Waste	172.0	0.0
Grampian (2%)	100.0	0.0
Interim Placement Service	381.0	0.0
Total	754.0	0.0

Of the above plans, the most significant relates to the following;

Interim Placement Service

The unit has had no patients for over a year now and the Board have been utilising the staff in other areas who have gradually been obtaining permanent jobs in other clinical posts. Management anticipate going to consultation to formally close the unit in 2011/12. Most of the savings have in effect already been reinvested into Community Services (the fact that there are no patients in the unit has implications for supporting them in the community)

Managing Financial Performance

Management receives detailed financial information to help manage performance against budgets and control expenditure. Detailed management accounts are prepared on a monthly basis, while management accountants liaise with directors and senior management to analyse the management reports and understand key variances against budgets. Directors receive responses from budget-holders within their directorates regarding variances, which they feed through to management accountants. The outcomes of the monthly reviews are consolidated into financial monitoring reports for consideration by the Board and senior management. The information produced and frequency of reporting ensures decision makers have appropriate information on which to base decisions.

The reporting arrangements were considered during the year and summarised in the Interim Management Letter, as reported to the Audit Committee on 14 April 2011. We note that management has made some progress towards implementing our recommendations since this date.

Performance against Key Financial Targets

NHS Shetland has achieved all four of its financial targets in the year, as follows:

	Limit set by SGHD £m	Actual Outturn £m	Variance (over)/under £m
Core Revenue Resource Limit	44.784	44.323	0.461
Non Core Revenue Resource Limit	7.467	7.467	0.0
Capital Resource Limit	2.111	1.996	0.115
Cash Requirement	52.310	52.310	0.0

Managing Performance and non financial performance targets

An assessment of the Board's performance management arrangements is detailed in full within the Interim Management Letter. However, the key points and a year-end update is summarised below:

- Performance is reported to the Board on a monthly basis. The reports expand on issues that are highlighted by the performance measures.
- The information reported and monitored focuses on the achievement of Local Delivery Plan (LDP) national HEAT targets and local KPIs, as well as a range of other measures including Community, Health & Care Partnership (CHCP) performance.
- Performance measures are refreshed annually, following the publication of the LDP.

The Board continues to actively manage the challenges in relation to cancer targets and is working closely with colleagues in NHS Grampian in order to reduce delays and improve access to diagnostic and treatment services for patients with cancer.

Pay Modernisation

NHS Boards are required to ensure that at least 80% of staff covered by Agenda for Change have their annual Knowledge and Skills Framework (KSF) development reviews completed and recorded on the e-KSF system by March 2011.

NHS Shetland has achieved this target with 93.7% of staff completing their reviews prior to 31 March 2011.

National Performance Audits

Procurement

As reported in our Interim Management Letter, at the request of Audit Scotland we have undertaken targeted follow up on the Board's response to *Improving public sector purchasing* (published July 2009).

The findings of this review will be reported to management in a separate letter.

Improving Efficiencies

In addition to the above and also at the request of Audit Scotland we have undertaken a review on the Board's response to *Scotland's Public Finances: planning for challenges ahead*.

The findings of this review have also been reported to management in a separate letter.

High Earnings

The Cabinet Secretary for Health and Wellbeing issued a letter to all Health Board Chairs on 12 November 2010 asking them to undertake a detailed review of their boards' pay policies for all staff earning over £100,000 to ensure they have been properly applied. The letter also requested that external auditors provide 'specific reassurance' that Boards had complied with national policies and guidance.

We reviewed the work undertaken by the Board. The findings of our work were subject to a separate letter issued to the Board during March 2011. No matters of significant concern were identified or reported.

5. Looking forward - 2011/12

<i>NHS Shetland</i>	<i>£m</i>
Recurring income	36.7
Recurring expenditure	(39.8)
Recurring savings	1.7
Underlying recurring surplus/(deficit)	(1.4)
Non-recurring income	7.7
Non-recurring expenditure	(6.3)
Non-recurring savings	0.0
Non-recurring surplus/(deficit)	1.4
Financial surplus/(deficit)	0.0
Underlying recurring surplus/(deficit) as a percentage of recurring income	3.81%

Confirmed by the Director of Finance on 10 June 2011

Financial Plan and Service Sustainability

The Board has completed its revised 2011/12 financial plan. Financial projections have also been considered over the period 2011/12 to 2016/17, although the degree of uncertainty remaining in the economic environment and regarding UK and Scottish Government budgets over this period will clearly impact on the assumptions made.

Financial Challenges

The 2011/12 budget includes a number of financial challenges and is dependent on a range of efficiencies and savings targets being met. The budget has been based on a SGHD uplift of 1%.

The 2011/12 Financial Plan, approved by the Board in March 2011 is based on recurring income of £36.7 million (£35.6 million 2010/11) and recurring expenditure of £39.8 million (£38.1 million 2010/11). Non-recurring income is projected £7.7 million (£9.1 million 2010/11) and non-recurring expenditure at £6.3 million (£7.4 million 2010/11).

Savings targets have been set at £1.675 million for recurring savings in the year 2011/12.

Savings Plans

The 2011/12 budget, reflecting the cost pressures outlined above, includes a savings target of £1.675 million (£1.2 million 2010/11) to achieve a break even position. £1.1 million of cash releasing savings (as required by the SGHD) will be required to address this shortfall and savings plans have been developed and agreed to address this gap.

A detailed listing of these planned savings Programmes, as presented to the Board as part of the 2011/12 Financial Plan, has been included in Appendix 3.

As detailed in previous sections, the Interim Placement Service savings target remains significant, as does the saving incurred through the revision of asset useful lives.

£0.410 million remains unidentified in the 2011/12 savings proposals. Management should seek to identify the required savings as soon as possible.

Action 4

2011/12 Cost Pressures

The cost pressures facing NHS Shetland in 2011/12 have been calculated as £1.5 million (this has been included in the £39.8 million expenditure forecast).

Savings plans, continual cost reduction and maximisation of resource utilisation have been highlighted as vital to cover these cost pressures and achieve a break even budget over this period.

Action 5

Pay costs are budgeted to inflate by around £0.358 million due to the low pay award to staff earning under £21,000, annual incremental progression for Agenda for Change staff and increased 0.5% National Insurance contributions from April 2011.

The table below details the projected cost pressures facing NHS Shetland in 2011/12

	£,000
Anticipated pay awards for staff earning below £21,000	44
Incremental drift (estimate)	250
National Insurance increases	64
Hotel Services inflation	35
Primary Care Inflation	40
VAT increase	100
Increases in prescribing and drugs costs	234

	£,000
Capital charge increases	116
Inflation on Service Level Agreements with other NHS providers	232
National systems and top-slices	71
Regional Developments	30
Anticipated increase in cost of services provided by Grampian	100
Other Non-pay	187
Total	1,503

In addition to the amounts estimated above, the following pressures should also be noted;

- Agreement of the annual abatement of Revenue Resource Transfer to Shetland Island Council of £1.2 million is ongoing.
- The Board's notified Capital Resource Limit is currently £0.2m (excluding capital grants). This is insufficient to address the statutory compliance issues identified. The Board is aware that there will be an island Board uplift and should work closely with Scottish Government to manage the risks involved.

6. Governance and Control

Overall Governance Arrangements

The established Committee framework at the Board remains in place, incorporating Audit, Clinical Governance, Staff Governance, Remuneration, Service Redesign and Community Health Partnership (CHP) Committees. Each of the Committees meets regularly and has at least one non-executive director present. The Board also has a Controls Assurance Group (chaired by the Director of Human Resources and Support Services) which has overall responsibility for risk management and for reporting any risk issues to the Board.

Significant changes in senior positions at the Board during the year include the appointments of the new Chief Executive, new Director of Nursing, the new board appointment of the Director of Human Resources and Support Services and the standing down of the Medical Director. This position is currently being filled on an interim basis, however, the Board intend to fill the role on a substantive basis in the near future. A change in the Chair of the Audit committee was also made in June 2010.

The NHS Quality Improvement Scotland (QIS) Standards for Clinical Governance, Patient Safety and Risk Management cover all aspects of clinical governance and risk management from the perspective of patient outcomes. A QIS Clinical Governance and Risk Management monitoring visit was carried out at the Board in April 2010 in addition to various evaluations and the Scottish Health Council Participation Standards Review in March 2011. Findings from these reviews have been reported to the Board.

Partnership working and Shared Services

The Board's partnership working arrangements are characterised by SLAs with other NHS bodies, membership of the NHS Tayside Consortium for a shared payroll system, membership of the NHS Ayrshire & Arran Consortium for shared Cedar e-financials systems and the CHP with SIC.

We noted that the Board is behind schedule with the implementation of the SSTS payroll system. However, the additional option of sharing the payroll service with NHS Grampian will be discussed and a decision taken at the July 2011 Board Meeting. The ongoing objective of implementing the Cedar Fixed Asset Module (once it is ready to go live) is being monitored by the Finance team. We understand that the Board intends to implement the module by the end of August 2011.

A number of performance measures exist to monitor the CHP's performance against its objectives. The performance measures and targets apply to a single financial year and are monitored by the CHP Committee quarterly. This Committee's minutes are, in turn, approved by the Board, providing it with direct oversight of the activities of the CHP. The CHP action plan includes referenced links to both the Board's LDP and to the Council's Service Plan. A small number of Single Outcome Agreement performance measures have been included in NHS Shetland's Performance Measurement framework e.g. health improvement, efficiency and access to treatment.

Statement on Internal Control

The Code of Audit Practice requires us to review and report on the Board's Statement on Internal Control. The Board has used the correct format for its Statement and has outlined the processes it has employed to identify and evaluate risks. In addition, key elements of the Board's control framework have been highlighted. Based on our normal audit procedures, we do not disagree with the disclosures contained in the Statement.

Systems of Internal Control

The results of our work on systems of internal control were communicated to the Audit Committee in our Interim Management Letter on 14 April 2011. The report contained seven recommendations to improve controls, none of which were considered high risk. Management has completed an action plan detailing those individuals responsible for implementing our recommendations and the timetable for completion.

Follow up of outstanding recommendations

We followed up NHS Shetland's progress in implementing recommendations made in the prior year during our interim visit. Our Follow Up of Prior Year Recommendations Report was considered at the Audit Committee meeting on 14 April 2011.

Of the agreed recommendations made in the reports issued to 2009/10, progress is now as follows:

Status	Total
Action implemented	5
Partially implemented	6
Little action to date	-
Not yet due for implementation / No longer applicable	2
	13

Since our interim visit, five recommendations have moved from the 'Partially implemented' category into the 'Action implemented' category representing good ongoing progress by the Board to put in place improvements identified by external audit.

Information Technology General Controls

ISA (UK&I) 315.93 requires auditors to "... obtain an understanding of how the entity has responded to risks arising from IT". IT General Controls (ITGCs) are controls put in place by management to mitigate those risks. ITGCs help ensure the continued proper operation of information systems to maintain the integrity of information and security of data.

Several of the Board's IT operations are outsourced to service organisations such as NSS, NHS Ayrshire & Arran Consortium and the Tayside Consortium. As a result, we are able to gain assurance over the Family Health Service and General Ledger systems through the receipt and review of service organisation auditor reports, such as a SAS 70. Our review of these reports did not uncover any instances whereby we were unable to place reliance upon the outsourced key financial systems. In other areas, we perform our own ITGC procedures.

From our own ITGC work, seven control weaknesses were noted in respect of the Board's IT control environment, six of these are outstanding from 2009/10. All of these issues were reported in the Interim Management Letter and none were noted as high risk or as having an impact on the level of reliance that could be placed on the key financial system outputs.

Internal Audit

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

During 2010/11, the Board continued to outsource its internal audit function to Deloitte. We have reviewed the work of internal audit and have, where appropriate, placed reliance on their work.

National Fraud Initiative

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

NHS Shetland chose to investigate all matches rather than focusing on recommended matches or a particular type of match only. To 31 May 2011 all matches had been reviewed to determine a suitable course of action and to investigate and conclude on the reason for the match. This includes reviewing payroll records, liaising with the Human Resources Department or other Boards and Local Authorities.

The majority of the matches NHS Shetland received related to employees working on multiple jobs. The Human Resources Department is contacted to ensure the individual has formally applied for permission to work on a secondary job and received the appropriate authorisation. Checks are also performed on individuals with long term sickness absence to ensure they are not working for other Boards or Local Authorities.

As at 31 May 2011 no frauds have been identified through the 2010/11 NFI exercise.

Appendices

Action Plan

Ref	Recommendation	Management Response
1	<p>Bad Debt Write-off</p> <p>Bad Debt write-offs are currently not treated correctly. Write-offs should be treated as expenditure and not netted off against income as is current practice.</p>	<p>This change will be implemented for financial year 2011/12.</p> <p>Management Response: Agreed Responsible Officer: Financial Accounting Manager Due Date: April 2011</p>
2	<p>Fixed Asset Register</p> <p>An asset verification exercise was undertaken by the Board in the year. When looking at the Fixed Asset Register during our audit work, it was identified that some assets remained on the register when they had been disposed of. Management should seek to review the Fixed Asset Register to ensure it accurately reflects the fixed assets held by the Board.</p>	<p>Fixed asset register will be updated during 2011/12 to reflect all disposals and an annual verification exercise will be carried out going forward. A new Fixed Asset procedure document was implemented and made available on the Board's Intranet in January 2011 which should ensure all disposals are reported to Finance in a timely manner.</p> <p>Management Response: Agreed Responsible Officer: Head of Finance & Procurement Due Date: July 2011</p>
3	<p>Budgets</p> <p>We recognise that work within the Board is ongoing to ensure budgets are aligned with changing trends, current economic conditions and changing patterns of patient care. Management should continue to re-assess and monitor budgets to ensure they reflect the continually changing environment.</p>	<p>We recognise that work within the Board is ongoing to ensure budgets are aligned with changing trends, current economic conditions and changing patterns of patient care. Management should continue to re-assess and monitor budgets to ensure they reflect the continually changing environment.</p> <p>Management Response: Agreed Responsible Officer: Director of Finance Due Date: Ongoing</p>

<p>4</p>	<p>Efficiency Targets</p> <p>NHS Shetland is required to identify a further £0.41 million to meet the 2011/12 savings target. Management should complete its review of potential savings options to ensure specific areas have been identified to generate all required efficiencies.</p>	<p>NHS Shetland is required to identify a further £0.41 million to meet the 2011/12 savings target. Management should complete its review of potential savings options to ensure specific areas have been identified to generate all required efficiencies.</p> <p>Management Response: Agreed. Further progress has been made – there is now around £150k still to identify.</p> <p>Responsible Officer: Director of Finance</p> <p>Due Date: 31 July 2011</p>
<p>5</p>	<p>Savings Challenge</p> <p>NHS Shetland has a challenging savings target of £1.675 million in order to break-even in 2011/12. Management should continually monitor and report on progress against savings plans, taking early action to avoid slippage within the savings schemes identified.</p>	<p>NHS Shetland has a challenging savings target of £1.675 million in order to break-even in 2011/12. Management should continually monitor and report on progress against savings plans, taking early action to avoid slippage within the savings schemes identified.</p> <p>Management Response: Agreed. A review has already taken place based on Apr-May figures. There is some slippage identified but this looks manageable within the overall position.</p> <p>Responsible Officer: Director of Finance</p> <p>Due Date: Ongoing throughout 2011/12</p>

Savings Programmes in 2010/11

The following table details the savings Programmes implemented during 2010/11 by the Board

Description	Recurring Savings	Non-recurring Savings
	£,000	£,000
Occupational Health Income	0.0	17.0
Completion of Nursing Service Redesign	101.0	0.0
Travel	10.0	0.0
Psychology Redesign	25.0	0.0
Primary Care	30.0	0.0
Medicines Waste	172.0	0.0
Grampian (2%)	100.0	0.0
Sodexo (2%)	35.0	0.0
Interim Placement Service	381.0	0.0
Procurement 5%	90.0	0.0
Clinical Governance redesign	40.0	0.0
Clinical Services Admin	29.0	0.0
Public Health Overhead	20.0	0.0
Primary Care Efficiency	30.0	0.0
Finance Non Pay	10.0	0.0
CEO dept	20.0	0.0
Facilities / Utilities	20.0	0.0
Vacancy Savings	0.0	50.0
Human Resources Savings	0.0	20.0
Lerwick Health Centre	7.0	0.0
Podiatry	20.0	0.0
Midwife Training	10.0	0.0
Midwife Post	8.0	0.0
Community Nursing	18.0	0.0
Total	1,176.0	87.0

Savings Programmes for 2011/12

The following table details the savings plans as presented to the Board in the 2011/12 Financial Plan;

Directorate	Detail	Identified in Principle £,000	Target £,000	Unidentified £,000
Public Health	Band 6/7 Health Promotion	22.3		
	Sub Total	22.3	35.6	13.3
Finance	Band 7	18.1		
	Sub Total	18.1	52.2	34.1
Estates	Sodexo	30.0		
	Utilities	6.5		
	Procurement	5.0		
	Retail Unit	1.1		
	Sub Total	52.5	189.2	136.7
Clinical Services	Podiatry – lease car	2.3		
	Medical Physics – contract	3.7		
	Occupation Therapy – non pay	5.6		
	Primary Care – to be negotiated	100.0		
	Primary Care prescribing	100.0		
	Information Dept – skill mix	5.0		
	Nursing – Interim Placement	207.0		
	Workforce Re-design of Band 5's	75.3		
	Nursing – Maternity	8.0		
	Lerwick Practice	51.8		
	Podiatry – balance of full year effect	7.0		
	Physio – balance of full year effect	11.0		
	Child Health – backfill costs TBC	17.1		
	Consultant Psychiatrist	22.6		
Sub Total	616.4	786.8	170.4	
HR & Support Services	Health & Safety (TBC)	3.4		

Directorate	Detail	Identified in Principle £,000	Target £,000	Unidentified £,000
	Computing (TBC)	20.0		
	Personnel	4.4		
	Occupational Health	8.3		
	Education & Training	5.2		
	Sub Total	41.3	96.7	55.4
Chief Executive	Communications Manager	28.9	28.9	
Pan-Directorate TBC	Asset-related savings	200.0		
	Crown Cars	8.0		
	Travel	100.0		
	Sub Total	308.00	308.00	
	SLA's	177.0	177.0	
TOTAL		1,264.5	1,674.4	409.9

Communication to Management

International Standards on Auditing (“ISA”) (UK&I) 260 – Reporting to those charged with Governance, requires that the External Auditor communicates certain matters to those charged with governance. Those charged with Governance is taken to be the Members of the Audit Committee with responsibility discharged through the regular meetings of the Audit Committee during the year. Summarised below are the requirements set out within ISA 260 together with reference to the relevant communication with you during 2010/11 or comments as appropriate.

Communication Required under ISA 260	Reference/Comment
Engagement Letters	Signed Engagements Letter with Audit Scotland at the start of our 5 year appointment and updated annually.
Independence	Audit Planning document report to 14 April 2011 Audit Committee confirmed no member of audit team has any direct interest, financial or otherwise, in NHS Shetland.
Audit Approach and Scope	Audit Planning document (reported to Audit Committee 14 April 2011).
Form and Timing of Communications	Audit Planning document (reported to Audit Committee 14 April 2011).
Accounting Policies/Estimates/Disclosures	Reviewed throughout audit process. No outstanding issues identified.
Correspondence with management on significant matters	Discussed and resolved matters arising with management throughout audit process.
Letter of Representation	Signed by management 24 th June 2011.
Other matters significant to the oversight of financial reporting process	None identified.
Material Uncertainties relating to Going Concern	None identified.
Related Parties	Other than those transactions disclosed in the financial statements we have not identified any further transactions requiring disclosure.
Fraud	Discussed fraud arrangements with the Audit Committee (14 April 2011) and management throughout audit process.
Material Weaknesses in Internal Controls	Internal Controls findings reported separately in our Interim Management Letter (14 April 2011)

This report has been prepared for and only for NHS Shetland in accordance with the terms of our engagement letter and for no other purpose. We do not accept or assume any liability or duty of care for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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