



cutting through complexity

East Lothian Integration Joint Board

Annual audit report to the Members of East Lothian
Integration Joint Board and the Controller of Audit

For the year period 31 March 2016

30 September 2016

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About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the Code").

This report is for the benefit of East Lothian Integration Joint Board ("the IJB") and is made available to Audit Scotland and the Controller of Audit (together "the Beneficiaries"). This report has not been designed to be of benefit to anyone except the Beneficiaries. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we may have been aware that others might read this report.

We have prepared this report for the benefit of the Beneficiaries alone.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the introduction and responsibilities section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk.

To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries.

Complaints

If at any time you would like to discuss with us how our services can be improved or if you have a complaint about them, you are invited to contact Andy Shaw who is the engagement leader for our services to East Lothian Integration Joint Board, telephone 0131 527 6673, email: andrew.shaw@kpmg.co.uk who will try to resolve your complaint. If your problem is not resolved, you should contact Alex Sanderson, our Head of Audit in Scotland, either by writing to him at Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2EG or by telephoning 0131 527 6720 or email to alex.sanderson@kpmg.co.uk. We will investigate any complaint promptly and do what we can to resolve the difficulties. After this, if you are still dissatisfied with how your complaint has been handled you can refer the matter to Russell Frith, Assistant Auditor General, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN.

Audit conclusions

- We have issued an unqualified audit opinion on the financial statements of East Lothian Integration Joint Board (“the IJB”).
- There are no adjusted or unadjusted audit differences. A small number of minor presentational adjustments were required to some of the financial statement notes. The Chief Officer’s remuneration was updated to correctly reflect information from NHS Lothian. Page 13
- The IJB is required to prepare its financial statements in accordance with International Financial Reporting Standards, as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom (“the Local Authority Code”). Additional guidance on accounting for the integration of the health and social care was created by the Local Authority (Scotland) Accounts Advisory Committee (“LASAAC”). Our audit confirmed that the financial statements have been prepared in accordance with the LASAAC guidance and relevant legislation. Page 5
- We did not encounter any significant difficulties during the audit. There were no other significant matters arising from the audit that were discussed, or subject to correspondence with management that have not been included within this report. There are no other matters arising from the audit, that, in our professional judgement, are significant to the oversight of the financial reporting process. Page 13

Financial position

- The notional financial resources expended to support the IJB in 2015-16 have been identified and disclosed within the financial statements. However, these costs were borne in their entirety by either East Lothian Council or NHS Lothian and the IJB was not charged for these services. Page 7

Financial statements and related reports

- We have concluded satisfactorily in respect of each significant risk and audit focus area identified in the audit strategy. We concur with management’s accounting treatment and judgements, including going concern. We have no matters to highlight in respect of: unadjusted audit differences; independence; and changes to management representations. Page 4

Wider scope matters

- We considered the wider scope audit dimensions and concluded positively in respect of financial management, value for money and governance and transparency. Page 6
- We highlighted some risk areas in relation to financial sustainability.

Purpose of this report

The Accounts Commission has appointed KPMG LLP as auditor of the East Lothian Health and Social Care Integration Joint Board (“the IJB”) under the Local Government (Scotland) Act 1973 (“the Act”). This document summarises our opinion and conclusions on significant issues arising from our audit. The scope and nature of our audit were set out in the audit strategy document which was presented to the audit and risk committee at the outset of the audit.

Audit Scotland’s Code of Audit Practice (“the Code”) sets out the wider dimensions of public sector audit which involves not only the audit of the financial statements but also consideration of areas such as financial management and sustainability, governance and transparency and value for money.

Accountable officer responsibilities

The Code sets out the IJB’s responsibilities in respect of:

- preparation of financial statements that show a true and fair view;
- systems of internal control;
- prevention and detection of fraud and irregularities;
- standards of conduct and arrangements for the prevention and detection of bribery and corruption;
- financial position; and
- Best Value.

Auditor responsibilities

This report reflects our overall responsibility to carry out an audit in accordance with our statutory responsibilities under the Act and in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board and the Code. Appendix five sets out how we have met each of the responsibilities set out in the Code

Scope

An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. Management of the audited body is responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems.

Weaknesses or risks identified are only those which have come to our attention during our normal audit work in accordance with the Code, and may not be all that exist.

Communication by auditors of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

Under the requirements of International Standard on Auditing (UK and Ireland) (‘ISA’) 260 *Communication with 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 the Board, together with previous reports to the audit and risk committee throughout the year, discharges the requirements of ISA 260.

International Standard on Auditing (UK and Ireland) 315: *Identifying and assessing risks of material misstatement through understanding the entity and its environment* requires the auditor to determine whether any of the risks identified as part of risk assessment are significant risks and therefore requiring specific audit consideration.

Professional standards require us to make a rebuttable presumption that the fraud risk from income recognition is a significant risk. As the IJB was not directing services in 2015-16, it did not receive income for operations and therefore we do not consider fraud risk from revenue recognition to be significant. We provide an update of our assessment of significant risks below, along with other audit focus areas.

SIGNIFICANT RISK	OUR RESPONSE	AUDIT CONCLUSION
Fraud risk from management override of controls	Professional standards require us to communicate the fraud risk from management override of controls as a significant risk; as management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.	We have no changes to the risk or our approach to addressing the assumed ISA risk of fraud in management override of controls. We do not have findings to bring to your attention in relation to these matters. No control overrides were identified.
FOCUS AREA	OUR RESPONSE	AUDIT CONCLUSION
First year financial statements preparation	<ul style="list-style-type: none"> ■ As 2015-16 is the first period of the preparation of the IJB's financial statements we reviewed the disclosures in the financial statements against the Local Authority Code, the Local Authority Accounts (Scotland) Regulations 2014 and LASAAC guidance. ■ The remuneration report was reviewed to check the officers disclosed are appropriate and that the amounts are accurate by agreeing to supporting documentation. 	The accounts have been prepared in accordance with the relevant legislation and guidance.

Overview

In March 2014 the Public Bodies (Joint Working) (Scotland) Act was passed by the Scottish Government. This required all Councils and NHS Boards to formally and legally establish integration of health and social care by April 2016. The integration scheme for East Lothian was approved by Scottish Government in September 2015. The IJB was formally established on 1 July 2015.

Whilst there was no transfer of functions until 1 April 2016, the IJB was required to prepare financial statements for 2015-16, following the 2015-16 Code. Guidance was issued by The Local Authority (Scotland) Accounts Advisory Committee ("LASAAC") in September 2015 on the expected content of the IJB accounts. The LASAAC guidance states that IJBs should comply with the Local Authority Accounts (Scotland) Regulations 2014, which includes the preparation of a remuneration report. The IJB appointed a Chief Officer and Chief Finance Officer in July 2015.

Financial position

CIES	£'000
Income	52
Expenditure	(52)
Net expenditure	-
Balance Sheet	£'000
Current assets	-
Current liabilities	-
Net assets	-

The IJB produced a break even position for 2015-16 which incorporated running costs, the Chief Officer and Chief Finance Officer salaries, audit and insurance fees. The IJB received contributions from East Lothian Council and NHS Lothian as income.

The remuneration report is appropriately produced to include the Chief Officer as this position is deemed to be a 'relevant position'. Per LASAAC guidance the Chief Officer costs should be allocated to the IJB from its establishment date.

The Balance Sheet shows the value as of the assets and liabilities recognised by the board. The net assets of the Board are matched by the reserves held by the Board and are currently nil.

We summarise below the work we have undertaken in the year to obtain assurances over the arrangements for each audit dimension and our conclusions on the effectiveness and appropriateness of these arrangements.

Financial sustainability

Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

Our conclusion below is derived from the following audit tests, carried to determine the effectiveness of the financial sustainability arrangements.

Framework for planning and agreeing the annual funding arrangements

The framework for planning and agreeing annual funding arrangements was discussed at previous Audit and Risk Committee meetings. The IJB must operate within the budgetary timelines for local government and the NHS, which are not aligned. Currently there is no formal funding agreement process in place. The IJB should ensure that the process for financial planning for 2017-18 and onwards starts timeously and that the IJB engages with the Scottish Government to review the national health financial planning process.

Recommendation one

Development and approval of 2016-17 budget

No formal 2016-17 budget has been approved, as it was not possible in advance of the start of the year due to NHS Lothian's own budget not being finalised. An indicative position was established, and an offer received from NHS Lothian. This is due to be discussed at the next Audit and Risk Committee meeting.

Medium to long term forecasting and planning

There is no formalised medium to long term forecasting and planning at the IJB. There is also no financial risk sharing agreement with East Lothian Council and NHS Lothian in the medium to long term.

Recommendation one

Conclusion:

Management continues to work closely with the two partners and the Scottish Government to anticipate the impact of future local government budget and NHS allocations. We consider that the IJB is a going concern however there are risks around the uncertainty of future funding.

Value for money

Value for money is concerned with using resources effectively and continually improving services.

We consider value for money and Best Value throughout our testing. Areas where we had a specific focus on value for money and Best Value are:

- *reviewing amounts disclosed in the of the IJB's financial statements to ensure they were in relation to the IJB.* The IJB had no income and expenditure in 2015-16. The remuneration of the Chief Officer is included within the remuneration report. We are satisfied that this relates to the operations of the IJB, however this was initially disclosed incorrectly; and
- *reviewing the draft Strategic and Joint Commissioning plans;* ensuring the focus is delivering quality service to meet increasing demand with a clear focus on value for money.

Conclusion:

The IJB has evidenced using its resources for the purposes of initial set up and running costs of the IJB. One presentational adjustment was made to the financial statements to correctly reflect the remuneration of the Chief Officer.

Financial management

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

Our conclusion below is derived from the following audit tests, carried out to determine the effectiveness of the financial management arrangements. This included:

- *consideration of the finance function and financial capacity within the IJB.* We noted that the chief financial officer has the appropriate skills, capacity and experience to support the IJB and effectively manage the organisation. This post is shared with Midlothian IJB to create efficiencies; and
- *reviewing the IJB's financial regulations.* The financial regulations are available to relevant staff. These were created in 2016-17 and approved by the Board. We found them to be suitably comprehensive.

Conclusion:

The IJB has appropriate financial capacity for current operations. This is supported by approved financial regulations and scrutiny by senior management and IJB members.

Governance and transparency

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

In considering governance and transparency we performed the following work:

- *reviewing the organisational structure, development of strategy and governance reporting lines within the setup of the IJB.* The IJB demonstrates effective scrutiny, challenge and transparency on decision making in the board minutes reviewed. IJB papers and minutes are available online through the East Lothian Council website;
- *reviewing arrangements for the creation of an audit committee.* An Audit and Risk Committee with a detailed remit, powers, and with the membership clearly defined has been created. This supports a solid governance framework to support challenge and scrutiny of the organisation. The IJB and Audit and Risk Committees are sufficiently balanced to ensure appropriate expertise; and
- *reading the annual governance statement;* we are satisfied that this is prepared in line with relevant guidance and is consistent with the governance framework.

Conclusion:

Governance controls were found to be operating effectively and we consider the governance framework to be appropriate for IJB. Transparency is achieved through the online publication of IJB papers and minutes.

Appendices

To the Integration Joint Board members

Assessment of our objectivity and independence as auditor of East Lothian Integration Joint Board (the IJB)

Professional ethical standards require us to provide to you at the conclusion of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- General procedures to safeguard independence and objectivity;
- Independence and objectivity considerations relating to the provision of non-audit services; and
- Independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the APB Ethical Standards. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Communications
- Internal accountability
- Risk management

- Independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

Independence and objectivity considerations relating to the provision of non-audit services

We have considered the fees charged by us to the IJB for professional services provided by us during the reporting period.

The audit fee charged by us for the period ended 31 March 2016 was £3,950 (excl VAT). No other fees were charged in the period. No non-audit services were provided to the IJB and no future services have been contracted or had a written proposal submitted.

Independence and objectivity considerations relating to other matters

There are no other matters that, in our professional judgment, bear on our independence which need to be disclosed to the IJB.

Confirmation of audit independence

We confirm that as of the date of this letter, in our professional judgment, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the partner and audit staff is not impaired.

This report is intended solely for the information of the IJB and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

Yours faithfully

KPMG LLP

Appendix two

Appointed auditors responsibilities

Area	Appointed auditors responsibilities	How we've met our responsibilities
Corporate governance	Review and come to a conclusion on the effectiveness and appropriateness of arrangements to ensure the proper conduct of the bodies affairs including legality of activities and transactions, Conclude on whether the monitoring arrangements are operating in line with recommended best practice.	Page eight sets out our conclusion on these arrangements.
Financial statements and related reports	Provide an opinion on audited bodies' financial statements on whether financial statements give a true and fair view of the financial position of audited bodies and their expenditure and income Provide an opinion on whether financial statements have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements	Page two summarises the opinion we expect to provide.
Financial statements and related reports	Review and report on, as appropriate, other information such as annual governance statements, management commentaries, remuneration reports, grant claims and whole of government returns.	Page two reports on the other information contained in the financial statements, covering the annual governance statement, management commentary and remuneration report. We have not reported on any grant claims.
Financial statements and related reports	Notify the Auditor General or Controller of Audit when circumstances indicate that a statutory report may be required.	No notifications to Controller of Audit required.
Financial statements and related reports	Review and conclude on the effectiveness and appropriateness of arrangements and systems of internal control, including risk management, internal audit, financial, operational and compliance controls.	Pages two sets out our conclusion on these arrangements.
WGA returns and grant claims	Examine and report on WGA returns Examine and report on approved grant claims and other returns submitted by local authorities.	The IJB is below the threshold for the completion of audit work on the WGA return.

Appendix two

Appointed auditors responsibilities (continued)

Area	Appointed auditors responsibilities	How we've met our responsibilities
Standards of conduct – prevention and detection of fraud and error	Review and conclude on the effectiveness and appropriateness of arrangements for the prevention and detection of fraud and irregularities, bribery and corruption and arrangements to ensure the bodies affairs are managed in accordance with proper standards of conduct. Review National Fraud Initiative participation and conclude on the effectiveness of bodies engagement.	Not applicable for 2015-16 for the IJB.
Financial position	Review and conclude on the effectiveness and appropriateness of arrangements to ensure that the bodies financial position is soundly based.	Pages six and seven set out our conclusion on these arrangements.
Financial position	Review performance against targets	Not applicable as no targets have been set in the IJB's first year.
Financial position	Review and conclude on financial position including reserves balances and strategies and longer term financial sustainability.	Pages two and seven set out our conclusion on the IJB's financial position.
Best Value	Be satisfied that proper arrangements have been made for securing Best Value and complied with responsibilities relating to community planning.	Page seven sets out our conclusion on these arrangements.
Performance information	Review and conclude on the effectiveness and appropriateness of arrangements to prepare and publish performance information in accordance with Accounts Commission directions.	The Annual Performance Report for 2015-16 has not yet been published.

The action plan summarises specific recommendations arising from our work, together with related risks and management’s responses.

We present the identified findings across four audit dimensions:

- financial sustainability;
- financial management;
- governance and transparency; and
- value for money.

Priority rating for recommendations

Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the organisation or systems under consideration. The weaknesses may therefore give rise to loss or error.

Grade two (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.

Grade three (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the control to meet their objectives in any significant way. These are less significant observations than grades one or two, but we still consider they merit attention.

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
<p>Framework for planning <i>Audit dimension: financial sustainability</i></p> <p>The IJB does not have a formalised process for financial planning for 2017-18 onwards. Additionally, there is no formalised medium to long term forecasting and planning. There is no financial risk sharing agreement with East Lothian Council and NHS Lothian in the medium to long term.</p> <p>There is a risk that appropriate strategic decisions cannot be made where budgets are not agreed in advance of the start of the year and where there is no medium to long term visibility.</p>	<p>We recommend that the IJB develops a medium to long term financial forecast with collaboration of both NHS Lothian and East Lothian Council. Whilst we acknowledge that the budget setting timetable is outwith the IJB’s direct control, a process to enable longer term planning should be established.</p> <p>The financial risk sharing agreement should be agreed with the partners.</p>	<p style="text-align: center;">Grade two</p> <p>The recommendation is accepted. The matter of financial planning was discussed with the IJB as part of a report presented to its May 2016 meeting. The financial assurance report also reflects this need .</p> <p>Responsible officer: Chief Finance Officer</p> <p>Implementation date: December 2016</p>



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