



NHS Highland

External Audit Plan for the financial year ending 31 March 2018

Audit Committee 19 December 2017 and finalised February 2018

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Our audit at a glance



Performance materiality is set at 75% and trivial is 5% of materiality. This reflects minimal audit adjustments in prior year and our understanding of NHS Highland in a year 2 audit cycle.



Materiality is set at 1% of gross expenditure based on 2016/17 audited information (£8.7 million). This is consistent with the prior year.



We have identified a significant risks of management override of controls and revenue and expenditure recognition as set out in International Auditing Standards (ISAs UK) and the FRC's Practice Note 10.

An audit
underpinned by
quality and adding
value to you



We fulfil our responsibilities per International Standards of Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice throughout our work.



At the planning stage we have identified other inherent audit risks over the valuation of defined benefit pension scheme liabilities and the valuation of land and buildings.



Our audit is undertaken in accordance with the Code of Audit Practice and reflects the wider scope nature of public audit. Our wider scope risks identified are: Financial management, Financial sustainability over the medium term and governance and transparency.

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Overarching principles of our audit

Our audit is risk based and undertaken in accordance with the relevant International Auditing Standards (ISAs) (UK and Ireland) and the Audit Scotland Code of Audit Practice 2016.

Our overall objective is a robust, quality-focused external audit which adds value through wider insights and challenge. Our audit foundations are:

- professional scepticism
- a focus on audit risks and key areas of management judgement
- sharing our wider insights across the sector (Scotland and UK)
- use of specialists to support our work where relevant
- using IDEA our data analytical software to effectively and efficiently test your balances
- clear and upfront communications, with regular communication during the year
- Reporting with focused actions which will support you in improving your controls/operations
- We will aim to not duplicate the work of your internal auditors. We will consider the internal audit plan for 2017/18 and identify any particular areas of risks that we either need to reflect in our approach or are relevant to our wider scope audit work. We will continue to review internal audit work throughout the year and maintain an ongoing, open, dialogue with internal audit.

Specific areas we will look to add value to NHS Highland ("NHS Highland") during 2017/18, identified as part of our planning work and reflection on prior year include:

- We will actively share relevant Audit Scotland and Grant Thornton publications with Senior Management and the Audit Committee, identifying particular areas for consideration.
- Should any new accounting changes or governance updates emerge during the year we will be providing a briefing for the Audit Committee. We will also pro-actively work with management during the year to discuss any emerging matters and seek to reach agreement on the treatment of these in advance of year-end.
- We will share the Scottish Public Sector Transparency report we produced for Audit Scotland at the end of December 2017, alongside our UK Grant Thornton Transparency Report.



External Audit deliverables for 2017/18 – Audit Committee

- External Audit Plan (this document)
- Governance and Transparency report and audit quality briefing (March - Committee Members)
- Audit progress report on interim testing and control walkthroughs – including where relying on controls (March 2018)
- Annual Report to those Charged with Governance and the Auditor General (June 2018)
- Audit opinion (June 2018)
- Management letter of representation (June 2018)
- Submit accounts and electronic version by end of June 2018
- Submission of NHS Minimum data set (2 July 2018)



2017/18 Deliverables as set out in the Audit Scotland planning guidance (October 2017)

- Confirmation of agreed fee by end of March 2018
- National Fraud Initiative - completed Auditor checklist (February 2018)
- Current Issues returns to Audit Scotland covering matters of ministerial or Auditor General interest and best value elements (January and July 2018)
- Submission of fraud returns to Audit Scotland – 27 April 2018



Planned Audit Scotland publications which may be relevant to NHS Highland

- Digital developments and projects – risks and issues
- Supporting Scotland's economic growth (Spring 2018)
- Changing models of health and social care (Autumn 2018)

Audit approach and materiality



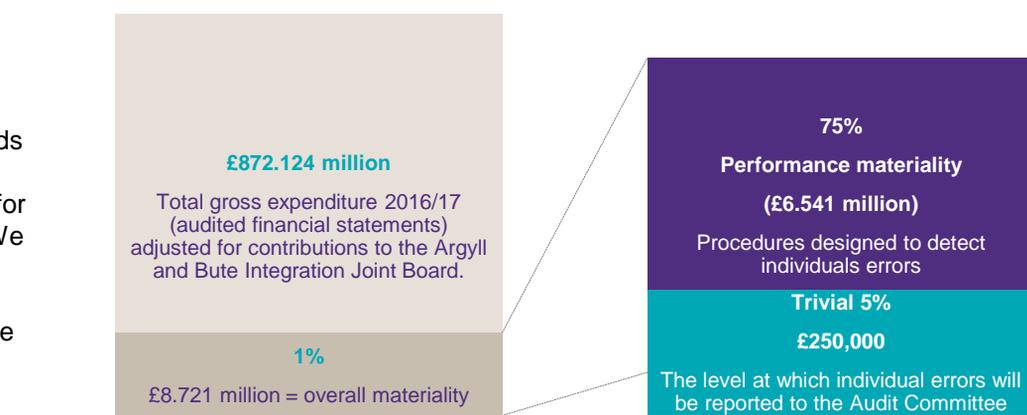
We undertake your audit in accordance with International Standards in Auditing (UK) (ISAs) and the Audit Scotland Code of Audit Practice (May 2016). On an annual basis we are required to give an opinion as to whether the Financial Statements:

- give a true and fair view
- have been properly prepared in accordance with relevant legislation and standards
- the wider information contained in the annual report and accounts e.g. Performance Report, the Accountability report including the Corporate Governance Report and Governance Statement, management commentary, that are consistent with the disclosures in the financial statements
- regularity of expenditure
- audited parts of the remuneration and staff report have been prepared in accordance with the guidance

Materiality

In performing our audit we apply International Standards on Auditing (UK) 320:

Materiality. Our materiality for 2017/18 is shown below. We will revise this on receipt of the unaudited financial statements for 2017/18 once received.



Overall materiality

We have calculated overall materiality in line with gross expenditure, as is recognised as a common measure in the public sector. We have removed contributions to the Argyll and Bute Integration Joint Board to ensure the base expenditure reflects actual costs incurred. In the context of NHS Highland's activities we feel it is appropriate to keep our overall materiality consistent with the prior year at 1%. Under our audit methodology we typically set materiality within the benchmark range of 0.5% up to 2%.

Performance materiality

Performance materiality represents the amount set for the financial statements as a whole to reduce the probability that the aggregate of uncorrected and undetected misstatements exceed materiality. Based on our audit experience in 2016/17 we have increased this for 2017/18 to 75% (65% in prior year). This does not impact on the financial statement balances we undertake substantive testing on, as all balances are in scope per prior year, but will impact on sample sizes.

Trivial

Under ISA 540 we are required to set an amount below which we consider misstatements would be clearly trivial, and therefore when accumulated we would not expect that they would have a material impact on the financial statements. The Code of Audit Practice requires auditors to report at no more than £250,000. We have therefore set our reporting threshold in accordance with the Code.

Misstatements above trivial (corrected and uncorrected) will be reported to the Audit and Risk Committee in our Annual Report to those charged with governance.

Going concern considerations

As auditors, we are required to "obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern" (ISA (UK) 570).

We will review management's assessment of the going concern assumption and evaluate the disclosures in the financial statements.

A risk based audit methodology

Our understanding of NHS Highland

This is our second year as the external auditors of NHS Highland appointed under the Audit Scotland framework. In 2016/17 NHS Highland received funding of £701,282 million, consisting of £664.5 million of core funding and £36.769 million of non-core funding, and delivered a saving of £111,000 against core revenue resource limits. This was achieved through the delivery of in year savings of £28.8 million. Management reported that this had operational detriment of some patients, through outpatient appointments and surgery exceeding the governments waiting time guarantees. Furthermore, savings were achieved through £6 million of non-recurring savings as well as a one-off £2.5 million transfer from capital to revenue approved by the Scottish Government.

NHS Highland continues to face significant financial and operational challenges. The Local Delivery Plan identified that savings of £47million were required for 2017/18 and over the next three years approximately £100 million of savings being required. This predominantly reflects cost significant cost pressures including prescriptions and staffing costs.

The focus for NHS Highland is to deliver sustainable recurrent savings through service re-design and transformational change. However, there is a significant risk that the planned service re-design may be a lengthy, complicated process and will not therefore deliver financial savings to the exact value or timing anticipated within NHS Highland's plans.

Overview of our audit risks identified at planning and our proposed approach

	Risk of fraud in revenue	Risk of fraud in expenditure	Management override of controls
The Risk	<p>As set out in ISA 240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In 2016/17, NHS Highland's income included £198.829 million of income commissioned by the IJB. This is formally agreed at the start of the year and not considered judgemental. We therefore do not consider this revenue stream as a significant risk. We consider the risk to be most prevalent in transactions and balances at the year end. We focus our testing on other material revenue streams including non-IJB hospital and community income, family health income, and other operating income.</p>	<p>Operating expenditure is understated or not treated in the correct period (risk of fraud in expenditure). As set out in Practice note 10 (revised) which applies to public sector entities. The risk is focused on transactions and balances at the year end.</p>	<p>As set out in ISA 240, across all entities there is a presumed risk of fraud being perpetrated by management through its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. override of controls is present in all entities.</p>
Our planned response	<ul style="list-style-type: none"> Walkthroughs of the controls and procedures around material income streams and validation of key controls where appropriate Consider income cut off procedures and substantive testing over pre and post year end balances A focus on recoverability of balances at the year end 	<ul style="list-style-type: none"> Perform cut off at year end on pre and post year end transactions and recording Walkthrough of the key expenditure controls in place A focus on year-end accruals Regularity – Expenditure incurred in accordance with the type/nature of NHS Highland as an organisation 	<ul style="list-style-type: none"> A focus on understanding how/where management override of controls may occur Review of the controls over journal entries Understanding key areas of judgement and estimation within the financial statements and the basis for these judgements and the application of accounting policies Reviewing unusual and/or significant transactions

Other areas of audit focus.

Through our audit planning process we identify areas and accounts that due to the nature of a transaction, disclosure or account balance in the financial statements are inherently more at risk of material misstatement within the financial statements.

Overview of other areas of audit focus identified at planning and our proposed approach

	Accounting for the defined benefit pension scheme	Valuation of land and buildings
The Risk	<p>NHS Highland participates in the Local Government Pension Scheme for those employees who transferred from Highland Council. The Council recognises the liability of the Pension Fund as at 31 March 2012 within the Council accounts. On an annual basis, NHS Highland recognises the net gain or loss in the fund, attributable for these individuals. The movement on the fund is derived through actuarial valuation of the fair value of the NHS Highland's share of the scheme assets and present value of the scheme liabilities.</p> <p>Given the level of judgement and subjectivity in the assumptions used in the actuarial valuation, there is therefore a risk that the pension fund net liability measurements are not materially correct.</p>	<p>In accordance with the Government Financial Reporting Manual (FRoM), NHS Highland holds property, plant and equipment and fair value. Valuations of land and buildings are reassessed by professional valuers under a five-year programme, with adjustments in intervening years to reflect valuation movements since the last full valuation.</p> <p>As at 31 March 2017, NHS Highland held land and buildings of over £300 million. While we have no underlying concerns around the basis of valuation, given the value of assets held and level of estimation in the valuation applied, this is considered a inherently higher risk area.</p>
Our planned response	<ul style="list-style-type: none"> • We will review the competence, expertise and objectivity of the actuary who carried the pension fund valuation • Assessment of the reasonableness of the actuarial assumptions made • Testing of the underlying data used to support the pension valuation • We will review the consistency of pension fund disclosures in the financial statements to the actuarial report. 	<ul style="list-style-type: none"> • We will review the valuations undertaken in year by the independent valuer including the basis of the valuation • We will review managements assessment of impairment risk • We will review the classification of PPE to ensure this is appropriate, depreciated in line with NHS Highland policies and complies with the FRoM.

Specific areas of focus – applying a lower materiality

During the course of our audit we may apply a lower level of materiality to specific balances or transactions in the financial statements. This reflects areas where there is a greater degree of interest or sensitivity on the amounts reported in the financial statements. Examples include the Remuneration and Staff Reports where due to the nature of the amounts reported we will apply a lower level of materiality.

Wider scope – what this means for the 2017/18 external audit

Financial sustainability

NHS Highland continues to face significant financial and operational challenges. The LDP identified that savings of £47million were required for 2017/18 and approximately £100 million over the next three years. This reflects demand lead pressures including prescriptions and staffing costs. Furthermore, the uncertainty around the potential impact of Brexit on future finances and workforce creates additional challenges.

Management recognise that significant transformational change is critical to the financial sustainability of the board.

Our Response: We will continue to discuss financial sustainability with NHS Highland Management. We will review the financial plans in place, including the scenarios set out, the governance of the plans and regular reporting on future financial scenarios.

Financial management

The Health Board achieved its financial targets in 2016/17. However, this was achieved through non-recurring savings of £6 million and a one-off approved transfer of capital to revenue funding of £2.5 million. With the level of savings required in 2017/18 being even more challenging than previous years, it is essential that robust financial management arrangements are in place to ensure that it can continue to meet patients needs.

Our Response: We will review NHS Highland's financial management arrangements informed through the work of internal audit and the high level financial framework of policies and procedures. This will include financial planning and monitoring arrangements in place.



Governance and transparency

NHS Highland Board and officers are responsible for establishing robust governance arrangements. During 2016 the board commissioned an independent review of governance arrangements which identified a number of recommendation including enhancing the leadership and scrutiny role of the Board.

During 2017 we identified opportunities for the Board to strengthen its governance arrangements including filling the vacant Non-Executive posts.

Our Response: As part of our overall assessment of governance, we will consider the progress made by NHS Highland in implementing agreed actions to enhance governance arrangements. This includes effective scrutiny and challenge of financial and non-financial performance.

Value for money

No specific risks were identified in relation to NHS Highlands arrangements for effectively utilising its resources and arrangements in place to continually improve services. NHS Highland has a clear strategic framework in place which aligns the organisation's vision and values to supporting strategy and quality framework.

NHS Highland recognise that financial and demand pressures puts significant challenge on the delivery of performance targets with two areas in particular: waiting times and delayed discharges, requiring focus.

We will consider NHS Highland's performance management framework and how they capture and measure performance and outcomes. We will also consider progress against the key strategic objectives.

Our planned work, like our financial statements work, is risk based and proportionate. We will continue to develop our understanding over the four dimensions and conclude on these in our final report, based on the work we have undertaken during the year.

Appendices

Key audit deliverables and our team

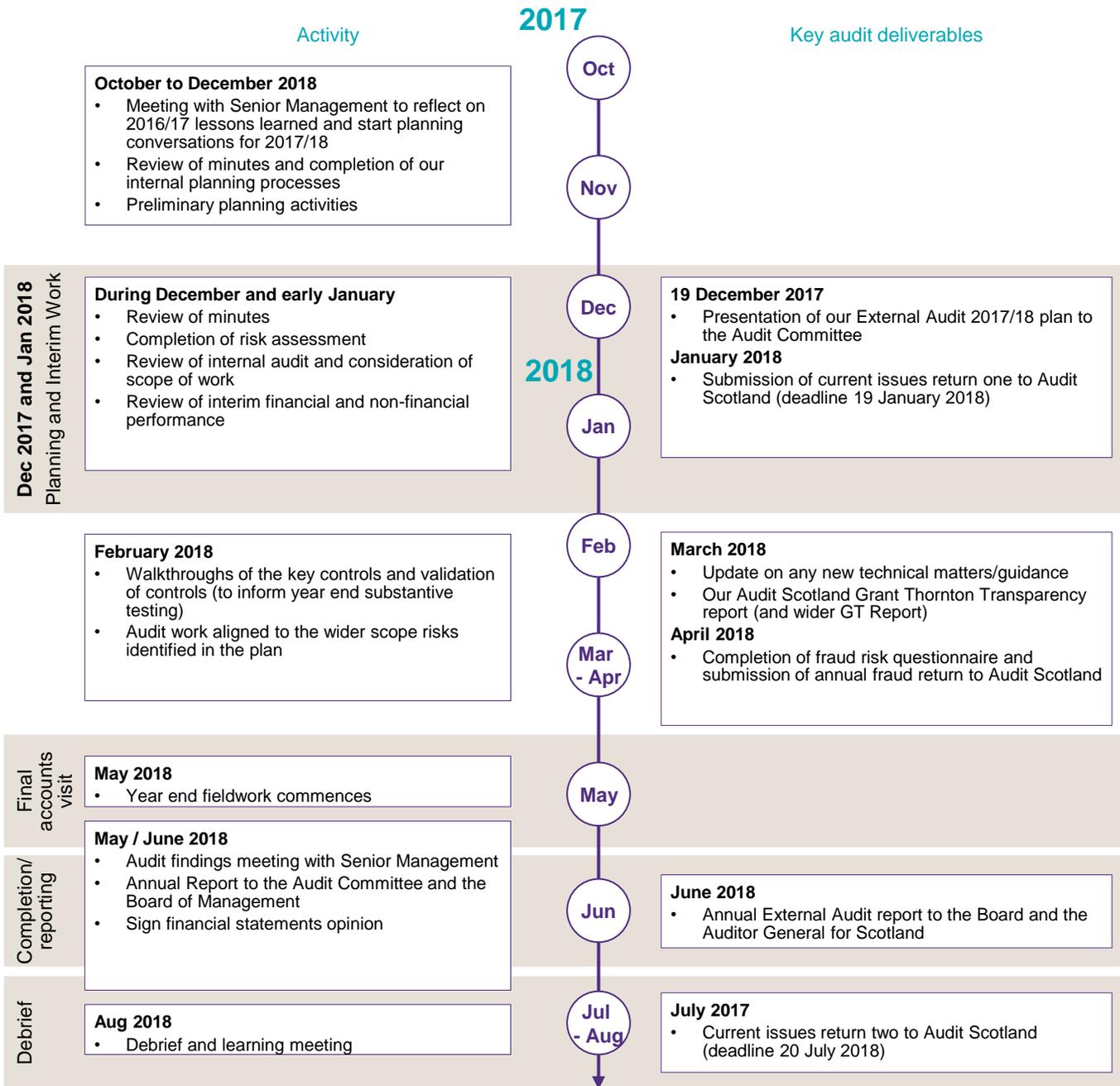
Independence and fees

Fraud arrangements

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Key audit deliverables and our team



Our team

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In addition we will use our Accounting technical team as required

Fees and independence

External Audit Fee

Service	Fees £
External Auditor Remuneration	141,600
Pooled Costs	20,460
Contribution to Audit Scotland costs	8,540
Contribution to Performance Audit and Best Value	0
2017-18 Fee	170,600

Fees for other services

Service	Fees £
At planning stage we confirm there are no non-audit fees	Nil

The audit fee is calculated in accordance with guidance issued by Audit Scotland. In accordance with the Audit Scotland guidance we can increase the fee by up to 10% from the base fee set by Audit Scotland, depending on risk factors identified by us as your external auditors. We cannot reduce the fee from the baseline set out by Audit Scotland. Our agreed fee is as set out, which is the baseline position. Typically our fee assumptions include:

- supporting schedules to all figures in the accounts are supplied by the agreed dates and in accordance with the agreed upon information request list
- the scope of the audit, and NHS Highland activities will not change significantly from planned
- NHS Highland will make available management and accounting staff to help us locate information and to provide explanations. We reserve the right to charge an additional fee for any additional work.
- We will only receive (and audit) 3 sets of accounts (1st draft; amended draft and final)
- Specific balances such as pensions and valuations of assets are supported by an independent specialist

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw your attention.

We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

Full details of all fees charged for audit and non-audit services will be included in our Annual Report to those charged with governance at the conclusion of the audit.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

We are required by auditing and ethical standards to communicate any relationships that may affect the independence and objectivity of the audit team.

We can confirm no independence concerns have been identified.

Fraud arrangements

The term fraud refers to intentional acts of one or more individuals amongst management, those charged with governance, employees or third parties involving the use of deception that result in a material misstatement of the financial statements. In assessing risks, the audit team is alert to the possibility of fraud at NHS Highland.

As part of our audit work we are responsible for:

- identifying and assessing the risks of material misstatement of the financial statements due to fraud in particular in relations to management override of controls.
- Leading a discussion with those charged of governance (for NHS Highland this is assumed to be the Audit Committee) on their view of fraud. Typically we do this when presenting our audit plan and in the form of management and those charged with governance questionnaires.
- designing and implementing appropriate audit testing to gain assurance over our assessed risks of fraud
- responding appropriately to any fraud or suspected fraud identified during the audit.

As auditors we obtain reasonable but not absolute assurance the financial statements as a whole are free from material misstatement, whether due to fraud or error.

We will obtain annual representation from management regarding managements assessment of fraud risk, including internal controls, and any known or suspected fraud or misstatement.

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

It is NHS Highland responsibility to establish arrangements to prevent and detect fraud and other irregularity. This includes:

- developing, promoting and monitoring compliance with standing orders and financial instructions
- developing and implementing strategies to prevent and detect fraud and other irregularity
- receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity.

Throughout the audit we work with NHS Highland to review specific areas of fraud risk, including the operation of key financial controls. We also examine the policies in place, strategies, standing orders and financial instructions to ensure that they provide a strong framework of internal control.

In addition, as set out in the Audit Scotland Code of Audit Practice we have a role in reviewing NHS Highland arrangements in response to the national fraud initiative exercise.

All suspected frauds and/or irregularities over £5,000 are reported to Audit Scotland by us as your auditors on an annual basis (no later than end of April 2018)

Respective responsibilities

As set out in the Code of Audit Practice (pages 10 to 16) there are a number of key responsibilities you as an organisation are responsible for, and others, as appointed auditors we are responsible for. These are summarised below:

Area	NHS Highland Responsibilities
Corporate governance	<ul style="list-style-type: none"> Establishing arrangements for proper conduct of its affairs Legality of activities and transactions Monitoring adequacy and effectiveness of arrangements (inc role of those charged with governance)
Financial statements	<ul style="list-style-type: none"> Preparing financial statements which give a true and fair view of their financial position Maintaining accounting records and working papers Putting in place systems of Internal Control Maintaining proper accounting records Preparing and publishing an annual governance statement, management commentary and remuneration report Effective systems of internal control as well as financial, operational and compliance controls – supporting achievement of objectives and secure value for money
Financial position	<ul style="list-style-type: none"> Proper arrangements to ensure financial position is soundly based and responsibility to ensure arrangements secure best value
Fraud and error	<ul style="list-style-type: none"> Establishing appropriate arrangements for prevention and detection of fraud, error, irregularities, bribery and corruption and affairs are properly managed

Our responsibilities



- Undertake statutory duties and comply with professional engagement and ethical standards
- Provide an opinion on financial statements
- Review and report on, as appropriate, other information eg annual governance statements, management commentary, remuneration reports
- Notify the Auditor General when circumstances indicate a statutory report may be required
- Demonstrate compliance with wider public audit scope

How do we do this in practice



- By reviewing and providing judgements and conclusions on NHS Highland arrangements including those across the wider scope of audit dimensions.
- Consideration of the effectiveness of performance management arrangements
- Suitability and effectiveness of corporate governance arrangements in year
- Financial position and arrangements for ensuring financial sustainability in the medium to longer term
- Review of other information in line with our knowledge and understanding of NHS Highland
- Ongoing dialogue and engagement with Audit Scotland during the year

Weaknesses and risks identified by us as your auditors 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 us 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.

Communication of audit matters with those charged with governance

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	•	
Overview of the planned scope and timing of the audit, including planning assessment of audit risks and wider scope risks	•	
Confirmation of independence and objectivity	•	•
A statement that we have complied with relevant ethical requirements regarding independence. Relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged. Details of safeguards applied to threats to independence	•	•
Significant matters in relation to going concern	•	•
Views about the qualitative aspects of NHS Highland accounting and financial reporting practices, including accounting policies, accounting estimates and financial statement disclosures		•
Significant findings from the audit		•
Significant matters and issues arising during the audit and written representations that have been sought		•
Significant difficulties encountered during the audit		•
Significant deficiencies in internal control identified during the audit		•
Significant matters arising in connection with related parties		•
Identification or suspicion of fraud involving management and/or which results in material misstatement of the financial statements		•
Non-compliance with laws and regulations		•
Unadjusted misstatements and material disclosure omissions		•
Expected modifications to the auditor's report, or emphasis of matter		•

International Standards on Auditing (UK) (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table above.

This document, The Audit Plan, outlines our audit strategy and plan to deliver the audit, while our Annual Report to those Charged with Governance will be issued prior to approval of the financial statements and will present key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

We will communicate any adverse or unexpected findings affecting the audit on a timely basis, either informally or via a report to NHS Highland Management and the Audit Committee.



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