Public Audit Committee

Report on NHS Highland 2013-14: Financial management
Members who would like a printed copy of this *Numbered Report* to be forwarded to them should give notice at the Document Supply Centre.
# Contents

## Introduction

<table>
<thead>
<tr>
<th>Financial management at NHS Highland in 2013/14</th>
<th>2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overspending at Raigmore Hospital, Inverness</td>
<td>3</td>
</tr>
<tr>
<td>Weaknesses in financial management and reporting</td>
<td>7</td>
</tr>
<tr>
<td>The role of the NHS Highland Board</td>
<td>11</td>
</tr>
<tr>
<td>The role of the Scottish Government</td>
<td>13</td>
</tr>
</tbody>
</table>

## Financial management in 2014/15 and beyond

<table>
<thead>
<tr>
<th>Non-recurring savings</th>
<th>15</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vacancy management</td>
<td>16</td>
</tr>
<tr>
<td>NHS Scotland National Resource Allocation Committee (NRAC) funding</td>
<td>17</td>
</tr>
</tbody>
</table>

## Concluding remarks

### Annexe A

| EXTRACT FROM THE MINUTES OF THE PUBLIC AUDIT COMMITTEE | 23 |

### Annexe B

| ORAL EVIDENCE AND ASSOCIATED WRITTEN EVIDENCE | 25 |
| WRITTEN EVIDENCE                              | 25 |
The remit of the Public Audit Committee is to consider and report on—

a. any accounts laid before the Parliament;

b. any report laid before or made to the Parliament by the Auditor General for Scotland; and

c. any other document laid before the Parliament, or referred to it by the Parliamentary Bureau or by the Auditor General for Scotland, concerning financial control, accounting and auditing in relation to public expenditure.
Committee Membership

Convener
Paul Martin
Scottish Labour

Deputy Convener
Mary Scanlon
Scottish Conservative and Unionist Party

Colin Beattie
Scottish National Party

Nigel Don
Scottish National Party

Colin Keir
Scottish National Party

Stuart McMillan
Scottish National Party

Tavish Scott
Scottish Liberal Democrats

Drew Smith
Scottish Labour

David Torrance
Scottish National Party
Introduction

1. On 24 October 2014, the Auditor General for Scotland (AGS) laid in the Scottish Parliament a Section 22 report entitled *The 2013/14 audit of NHS Highland: Financial Management*. In that report the AGS concluded that—

> There were weaknesses in financial management and reporting to Board members in NHS Highland during 2013/14. This led to a request late in the financial year for additional funding from the Scottish Government.

2. The Committee explored this conclusion in evidence with the AGS and Audit Scotland at its meeting on 5 November 2014 and received written evidence from the Scottish Government and NHS Highland. The Committee also took evidence from NHS Highland at its meeting in Inverness on 2 February 2015 and at its meeting on 13 May, held at the Scottish Parliament.

3. This report sets out the key observations, conclusions and recommendations of the Committee on the issues identified within the AGS report.

4. The Committee would like to thank all those who provided evidence, a list of whom is contained in Annexe A to this report.

Photograph of Garry Coutts, Chair; Elaine Mead, Chief Executive and Nick Kenton, Director of Finance, from NHS Highland giving evidence to the Public Audit Committee at the Scottish Parliament on 13 May 2015.
Financial management at NHS Highland in 2013/14

5. In 2013/14 the Scottish Government allocated £634.3 million to NHS Highland: £617.9 million for revenue and £16.4 million for capital. NHS Boards are required to break even against their revenue and capital budgets. In 2013/14 NHS Highland met its capital budget but it needed £2.5 million in brokerage from the Scottish Government in order to break even against its revenue budget (in fact NHS Highland delivered a small surplus of £0.1 million against its revenue budget).

6. The Scottish Government explained that brokerage is a mechanism whereby it can work with Boards to support their medium to long term financial planning by providing additional in-year funding that is recovered in future years.

7. NHS Highland explained that for the 11 years prior to 2013/14, it had not required brokerage. The Chair of NHS Highland expressed his disappointment that brokerage was required in order to break even and that the Board was “working hard to ensure that we learn from the areas of weakness that were identified.”

8. NHS Boards receive their allocation of funding from the Scottish Government based on a formula developed by the National Resource Allocation Committee (NRAC). This formula has been in operation since 2009/10 and the Scottish Government is aiming for all NHS Boards to be within 1% of their target allocations by 2016/17. The AGS reported that in 2013/14 NHS Highland was 2.2% (£11.3 million) below the funding level calculated by the NRAC formula.

9. The Committee agrees with the AGS that brokerage can be used by NHS Boards and the Scottish Government as part of a clear financial strategy, such as to provide flexibility to deliver large capital projects or to manage significant service redesign.

10. As such the provision of brokerage to a NHS Board does not, in itself, give rise to a Section 22 report by the AGS. In the case of NHS Highland however, whilst funding below the NRAC target may have contributed to NHS Highland’s financial difficulties, the AGS reported that brokerage was required at the end of financial year 2013/14 as a result of weaknesses in financial management and reporting to the Board.

11. These weaknesses in financial management and reporting also meant that, as is highlighted throughout this report, it was difficult for the Committee to obtain clear, unequivocal evidence about the specific dates, nature of
discussions and decisions taken at NHS Highland in relation to the brokerage required in 2013/14.

12. Continuing to deliver high quality services during times of financial constraint demands good corporate governance arrangements; informed and transparent decision taking, with the Board and Chief Executive acting as a check and balance on each other. In this instance, given our comments throughout this report (see paragraphs 57-60, 73-75 and 79), we are not convinced that NHS Highland has demonstrated these attributes.

Overspending at Raigmore Hospital, Inverness

13. The Committee heard from NHS Highland about the sequence of events that led to the need for £2.5 million in brokerage from the Scottish Government in order to break even in 2013/14. The most significant of these was overspending at Raigmore Hospital.

14. There has been a history of overspending against budget at the Hospital in recent years. The internal auditor, Scott Moncrieff,\(^\text{12}\) explained that the Director of Finance at NHS Highland had expressed concerns about the financial position in 2012/13 as—

> it had been known that for a year or two that hospital was overspending. There was a recognition by management that that was unsustainable and they wanted to understand why it was happening.\(^\text{13}\)

15. Table 1 sets out the overspending for each year between 2010/11 and 2014/15. The Committee heard that in order to address the initial increase in overspending to 2011/12, NHS Highland had taken all the local measures it could to oversee, support and train individuals within the organisation but had not seen any reduction in overspend as it had expected so—

> at that point we were persuaded that there were increased pressures on the hospital.\(^\text{14}\)

16. Therefore at the beginning of 2012/13 NHS Highland decided to take the unusual step and rebase the budget at Raigmore Hospital—

> in fact, we wiped off its budget deficit with an additional £5 million as we went into the year beginning 2012/13.\(^\text{15}\)
Table 1: Overspending at Raigmore Hospital

<table>
<thead>
<tr>
<th>Financial Year</th>
<th>Budget (£m)</th>
<th>Actual (£m)</th>
<th>Overspend (£m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010/11</td>
<td>130</td>
<td>130.6</td>
<td>0.6</td>
</tr>
<tr>
<td>2011/12</td>
<td>130</td>
<td>134.8</td>
<td>4.8</td>
</tr>
<tr>
<td>2012/13</td>
<td>135.8 (includes 5.0 additional budget)</td>
<td>137.7</td>
<td>1.9</td>
</tr>
<tr>
<td>2013/14</td>
<td>136.2</td>
<td>145.9</td>
<td>9.6</td>
</tr>
<tr>
<td>2014/15</td>
<td>138.9</td>
<td>145.8</td>
<td>6.9</td>
</tr>
</tbody>
</table>

17. NHS Highland explained it was disappointing that, even though the budget had been rebased in 2012/13 with a resulting £1.9 million overspend, the situation deteriorated during 2013/14. This, NHS Highland stated, was as a result of poor financial management as well as a lack of budgetary control throughout 2012/13 and into 2013/14.¹⁷

18. As a result of this deterioration, and management recognition that it was unsustainable, the internal auditor was asked to undertake a review. In April 2013 the internal auditor reported with recommendations for improving governance and accountability at the hospital. The internal auditor explained that the main issue identified—was the culture in the hospital. There was not a strong culture of tight financial management. That partly because, until recently the hospital had had enough money...in 2010, the hospital was in recurring balance. Therefore, until fairly recently, there had not been a need for very tight financial management¹⁸

19. NHS Highland explained that the view expressed that Raigmore Hospital “had had enough money” arose because its budget had been rebased in 2012/13.¹⁹ The Committee heard from the internal auditor that “the overspends at the hospital had been managed by making compensations elsewhere in the health board.”²⁰

20. NHS Highland identified some of the areas where these compensatory savings were made, such as reducing overall costs for supplementary staffing across the organisations, exceeding the target for savings in the central core every year, smarter procurement and buying things cheaper.²¹

21. The follow-up review of the 2013 internal audit report by the internal auditor reported in May 2014 and highlighted a lack of progress with implementing the recommendations in the 2013 report.²² The AGS reported that the May 2014
internal audit report identified that one of the underlying causes of the hospital's overspend for the year 2013/14 was inadequate budget management by budget holders and overspends not being monitored or addressed.  

22. The AGS reported that by 2013/14 the overspend at the hospital was £9.6 million which, as acknowledged by the Director of Finance, was the key problem that contributed to the requirement for brokerage in order for NHS Highland to break even in 2013/14. 

23. The Chair of NHS Highland explained that following the 2013 internal audit report, training with budget holders at Raigmore Hospital on budget management was put in place. The Board, the improvement committee and audit all examined the outcomes of the internal audit report and the financial recovery plan that was put in place. Early in 2013/14 the then Director of Operations and the Head of Finance reported that there had been positive progress. However—

Some of the actions that we understood had been taken did not, in fact, materialise and we found further deterioration in the position... the scale became apparent to us in month 10 in 2013/14. By that time, we had a new management team looking at the financial position.

24. We are concerned at the increase in overspending at Raigmore Hospital over a number of years from £600,000 in 2010/11 to a £9.6 million overspend in 2013/14, despite its budget being increased by £5 million in 2012/13.

25. The comments that "until fairly recently there had not been a need for a tight financial management" at Raigmore Hospital, combined with the observation that "another contributing factor is that there is a perception that Raigmore Hospital was underfunded" describes to us a situation where complacency about the importance of rigorous budget management had arisen.

26. We acknowledge that NHS Highland took action to understand the reasons for the overspending at Raigmore Hospital by requesting an internal audit review (in 2013 and again in 2014). However we are concerned to note that the progress made by the Board in addressing the issues raised in the 2013 internal audit report was described by the AGS as "slow" and by the Chair of NHS Highland as "not sufficient".

27. The slow progress made in addressing the causes of overspending at Raigmore Hospital may have been aided by the accepted practice of the Board compensating for overspends at the Hospital through underspends generated elsewhere in NHS Highland.

28. We also note that progress in fully implementing some of the agreed actions identified in the 2013 and 2014 internal audit reports remains on-going despite the original target dates of mid-2014.
29. It does not appear that NHS Highland had understood the causes of overspending at Raigmore Hospital prior to its decision to rebase the budget at Raigmore Hospital in 2012/13. The increase in its overspending to £9.6 million in 2013/14 suggests to us that the additional funding of £5 million did not address the root causes of the overspending but merely offset it for that year.

30. NHS Highland noted that although the costs at Raigmore Hospital are comparable with other acute hospitals, Raigmore Hospital should not be overspending year-on-year. As a result, following the 2014 internal audit report, a three year recovery plan was agreed with a target of financial break even at Raigmore Hospital within the 3 year period. This plan had targeted a £6 million overspend for the financial year 2014/15. Audit Scotland’s review of NHS Highland financial management in May 2015 (hereafter referred to the 'May 2015 review’) reported that the overspend was actually £6.9 million.

31. In evidence the Chief Executive of NHS Highland explained that the reduction in overspend to £6 million had been achieved at Raigmore Hospital in 2014/15 by making—

> great inroads into reconfiguring services and taking waste out of the system. It reduced demand and transformed how it delivers services. Its reliance on supplementary staff had reduced and it was making a significant impact on some other pressures it had experienced in-year.

32. The May 2015 review reported that the new senior management team at Raigmore Hospital is developing a culture based on a greater focus on financial management and budgetary control.29

33. The Committee acknowledges that Raigmore Hospital has reduced its overspending by £2.8 million in 2014/15. However we note that the Hospital received a £2.7 million budget increase from 2013/14 to 2014/15. Given this and NHS Highland’s previous experience in 2012/13 of rebasing the budget of Raigmore Hospital (which delivered a reduction in overspend for only 1 year) it does not appear that the underlying causes of overspending at Raigmore Hospital have yet been understood or addressed.

34. In 2012/13, there was initial optimism about the positive progress made by the Hospital in addressing the causes of the overspending which later proved not to be the case. So whilst we welcome the improvements outlined by the Chief Executive of NHS Highland (at paragraph 31) we seek further reassurance from the AGS (as part of an update at the end of the year) on the extent to which NHS Highland:
uses management reports and performance indicators to reassure itself that Raigmore Hospital has improved the efficiency and effectiveness of its services;

determines whether the causes of previous overspending are now being addressed and that robust financial management and scrutiny is now being delivered.

35. We would also welcome confirmation from the AGS of the planned annual budget for Raigmore Hospital and the targeted overspend for each of the remaining years of the 3 year recovery plan.

36. Finally given Raigmore Hospital missed by £900,000 its target to reduce its overspend to £6 million in 2014/15 we would welcome an update from the AGS on the actions NHS Highland has taken to review the 3 year recovery plan for Raigmore Hospital to ensure it remains realistic.

Weaknesses in financial management and reporting

37. NHS Highland explained that at the start of 2013/14 its Board had identified a £20 million deficit which it had to address by the end of the financial year in order to break even. In evidence to the Committee it was confirmed that at Board meetings, members received monthly financial reports along with forecast overspend at year end and management actions being taken at Raigmore Hospital or in other areas to reduce that deficit.

38. Throughout the year until February 2014, NHS Highland was forecasting that it would break even at the end of the financial year (March 2014). Despite showing significant overspends against the budget each month, monthly information provided to the Board and Scottish Government reported that the deficit would be addressed from 'management planned actions'. The AGS reported that there were no sufficiently detailed plans to bridge the gap between its in-year deficit position and its forecast break-even position.

39. The Scottish Government confirmed that its officials meet regularly with NHS Directors of Finance to discuss financial planning and emerging financial issues. In addition NHS Highland carried out a review of its financial plan and in-year performance, with the agreement of and facilitated by the Scottish Government. The overall conclusion of that review was that—

NHS Highland should be capable of following through to complete those actions identified during the course of the review and manage within its RRL [Revenue Resource Limit] for 2013/14.

40. The Chair of NHS Highland's Board was clear that, throughout 2013/14, Board members were aware of the financial expenditure to date, the deficit which required to be addressed in order to break even and the actions being taken to address that deficit. In that regard the Chair reiterated that from August 2013
onwards the Board reported to the public its belief that NHS Highland would break
even and, with sufficient management actions, close the deficit gap. At the Board
meeting on 3 December 2013, the potential forecast overspend was £8.5 million
(that is the deficit that had to be bridged to break even at year end).

41. On 13 December 2013, the Scottish Government summary letter of the half-year
review confirmed anticipated breakeven but noted some risks. At that point the
potential deficit was £6.5 million.

42. In December 2013, Mr Douglas Griffin (a former Director of Finance from NHS
Greater Glasgow and Clyde) was invited to review NHS Highland’s position—
he looked at our plans, interrogated us, discussed our position with us,
spoke to colleagues who are now the new management team at Raigmore
hospital and was to give us the confidence in the way forward. He felt that,
if the way forward went to plan, we would break even.

43. At the NHS Highland Board meeting on 4 February 2014, the December 2013
figures were considered with a potential over spend of £5.6 million forecast but
with break even at year end still formally reported. NHS Highland expected that
in the last quarter of 2013/14 this overspend would be address by:

- an improvement at Raigmore Hospital of £1 million
- additional funding from Highland Council of £1 million
- asset life plans delivering benefits of £2 million
- management action including vacancies and additional procurement benefits to
deliver £1.6 million in savings.

44. On 18 February 2014 the figures up to January 2014 (month 10) were published
which showed a deterioration in the forecast for Raigmore Hospital of £400,000
rather than the improvement of £1 million predicted. The internal auditor
explained that additional activity had been commissioned internally at Raigmore
Hospital at the end of the year “without a recognition of the financial implication of
the decision. The financial implication came through the following month, by which
time it was too late to make any amendments to the budget.”

45. In addition in February 2014, there was an accounting error in relation to children’s
services arising from differences in adjustments made before reconciliations were
carried out. As a result there was a reduction of £400,000 in the amount that NHS
Highland expected to receive from the Asset Lives valuation.

46. In light of the deterioration in the figures revealed on 18 February 2014, in early
March 2014, the Chief Executive of NHS Highland asked the Director of Finance
to begin discussions about brokerage with the Scottish Government.
47. The Committee heard that as Accountable Officer the Chief Executive has ultimate responsibility to the Scottish Parliament for the decisions that are taken about finance and that the standing financial instructions were silent on whether the Accountable Officer or the Board have responsibility for taking the decision on whether to seek brokerage.  

48. Brokerage of £2.5 million was agreed in principle with the Scottish Government on 6 March 2014.  

49. This was then confirmed on 12 March 2014 and the Chief Executive then informed the Chair. The brokerage of £2.5 million represented 0.3% of NHS Highland's total revenue budget.  

50. On 25 March 2014 Board papers were issued to members confirming the brokerage requirement, which was then discussed at the Board meeting on 1 April 2014. The Chief Executive confirmed that there had been no papers provided to Board members to inform the discussion of the risks, benefits and consequences of seeking brokerage or alternatively achieving savings by reducing services over the remaining time before year end.  

51. We heard that there was an Improvement Committee meeting on 3 March 2014 at which it is noted that “the board is in dialogue with the SG regarding options for managing the position.” However the paper supporting this discussion at the Improvement Committee does not explicitly refer to brokerage.  

52. In relation to when the Board members first discussed that brokerage might be required, the Chair explained that, at an informal Board development session on 4 March,—  

   one of our board members...asked whether at that stage it would not be sensible to look at brokerage instead of continuing to try and find savings... in that financial year.  

53. In written evidence, NHS Highland confirmed that at the informal Board development session on 4 March 2014, the implications of action necessary to break even, including the impact on services and the possibility of brokerage were discussed and—  

   we were directed to take all necessary action to secure [a] break even position.  

54. It was on this mandate that the Chief Executive explained that she made the decision to request and secure brokerage from the Scottish Government. The Committee was told that this was not a "blank cheque" but that the board was clear about the scale and actions that were being taken and the alternative actions that would be necessary should it not secure brokerage. The Chair apologised for the fact that “the decision was not made formally at a board meeting".
55. However, at the Public Audit Committee meeting on 2 February 2015, the Chair explained that the Chief Executive and Director of Finance were told by the Board at a January meeting\(^{62}\) that "They had to take whatever action was required in finding savings to ensure we broke even."\(^{63}\)

56. The January 2015 internal audit review reports that "Discussions with the Scottish Government about the possibility of brokerage" took place on 18 February 2014 with the Board members being informed of discussions with the Scottish Government on 4 March 2014.\(^{64}\) However the NHS Highland written submission dated 13 January 2015 does not include the 4 March Board development session in its “Timeline of Key Events Relevant to the Section 22 Report.”

57. Despite two oral evidence sessions with NHS Highland witnesses and a number of written submissions and reports, we have been unable to reconcile the evidence we received about when brokerage was first discussed with the NHS Highland Board and how the Board was kept informed, as is highlighted by the contradictory evidence in the four preceding paragraphs.

58. It is unclear why a board member was suggesting seeking brokerage at the Board development session on 4 March 2014, given at that stage other evidence suggests it was already being sought. Given this and the contradictory evidence provided we question how well informed Board members really were.

59. The Chair of NHS Highland stressed to the Committee that for the 11 years prior to 2013/14, NHS Highland had not required brokerage. In those circumstances, the Committee would have expected that a decision to seek brokerage (and late in the financial year) would be a significant one with all the more need for transparent robust decision taking by the Board which was well documented. This was not the case.

60. The fact that the discussions at Board development sessions were undocumented added to the Committee’s difficulty in establishing a clear picture of the Board’s decision making process. We are also concerned that this approach meant that there was little or no opportunity for the NHS staff and the public to be informed of the circumstances under which brokerage was being sought. As the Committee heard, there could have been serious repercussions for patients had brokerage not been agreed by the Scottish Government with the possibility of a reduction in the services available in NHS Highland.

61. We welcome the decision by NHS Highland officers to now note and minute the informal discussions it has with the Board to provide an audit trail. We also acknowledge the Chair’s commitment to ensure that, in future, decisions such as the requirement for brokerage would be taken formally at Board meetings.
62. We recommend that NHS Highland, within this financial year, clarify its standing financial instructions to be clear about whether the Accountable Officer or the NHS Highland Board are the decision taking authority regarding seeking brokerage or additional financial support from the Scottish Government.

The role of the NHS Highland Board

63. In its report entitled The role of Boards, the Auditor General for Scotland identified that—

Boards must hold the management of the organisation to account by challenging and scrutinising their work to ensure that it meets organisational objectives.65

64. NHS Highland explained that issues of financial significance were regularly discussed with the Board as well as each Board member receiving a report pack detailing the financial position each month. Throughout the year the board delegates to officers the authority to make decisions. In that regard board members do not routinely make financial decisions but monitor the overall position, which is delegated to officers.66

65. The Chair explained that—

the routine way of making decisions is that every decision is made in public. Informal meetings are for information, briefings and developing our understanding of the complex system that we are managing; they are not about decision making.67

66. The Chair acknowledged that whilst the Board was informed of the decision to seek brokerage the decision was not made formally at a Board meeting. He confirmed that this would not happen should brokerage ever be required again in future.68 The Chief Executive recognised that she was remiss in asking members to note the brokerage decision and the terms of its payback rather than seek their clear understanding and agreement to it.69

67. The Committee heard that no Board member questioned the need for or subsequent agreement to brokerage at any stage of the process.

68. The Chief Executive explained that in requesting that she do everything necessary to break even, the Board members were executing their governance responsibility by keeping very clear to the position and discussing the action the Chief Executive should take.70

69. The Committee heard that every non-executive Board member who joins the Board undertakes a training programme. In addition each non-executive is
evaluated each year with a formal evaluation conducted by the Chair with all the Board members.  

70. Responding to questions regarding whether he should have called a special board meeting to discuss the requirement for brokerage, the Chair explained that—

we have to give board members two clear weeks' notice of a special board meeting. There would have to be a substantial period of time until our next scheduled meeting in order to make having special meeting worthwhile. As it was the period between the agreement of the brokerage and the meeting at which it was reported was only a little more than the fortnight anyway, so I would not have deemed it appropriate or as adding value to call a special meeting.  

71. The Chair explained that he could have phoned around members, however some live in Argyll, the islands and others work part-time which limited the time that members are available. The Chair acknowledge however that—

In light of the discussion that we are having here and the importance that is being attached to the issue, I should have maybe taken a different view.  

72. We acknowledge the steps taken in 2014/15 to improve the financial reporting to the NHS Highland Board such as close monitoring of savings trajectories, the inclusion of savings table in financial reports, and the establishment of a Programme Board to monitor delivery of key efficiency projects on a weekly basis.  

73. However, in considering the role of the Board during the decision making process regarding brokerage we are concerned at witness comments that the Board's role was to 'monitor' the management of NHS Highland's finances (rather than to 'scrutinise and challenge' as recommended by the AGS). This does not suggest to us a climate of constructive challenge and scrutiny within the Board. We therefore request clarification from NHS Highland as to how it is encouraging this culture in its Board members.  

74. We are also uneasy at the Board's decision to mandate the Chief Executive to do 'whatever necessary to break even' at a time when NHS Highland was still publically reporting it would break even. Such a mandate appears to us to amount to 'moral hazard' whereby the risk of brokerage being required (for the first time in 11 years) was not viewed as significant because that risk fell on the Scottish Government.  

75. We also question the Chair's decision not to call a special Board meeting given this was the first time in 11 years that the Board had required brokerage to break even. Whilst the Chair acknowledges he might have acted differently in view of "the importance that is being attached to the issue" we consider that there was time for a special board meeting to be
called with the appropriate 2 week notice period. On 18 February it became clear that NHS Highland would require brokerage to break even. At that time the next scheduled Board meeting was 6 weeks away on 1 April.

76. A special meeting would have enabled the Board to discuss and endorse the decision to seek brokerage before financial year end and consider the longer term implications for NHS services of repaying the brokerage. Instead the Board was asked to note the decision on 1 April after year end.

77. We remain concerned that the Chair of NHS Highland considers a special board meeting can only be held if Board members receive two or more weeks' notice.

78. We recommend that NHS Highland reviews the circumstances under which a special board meeting is called and considers different ways of working such as videoconferencing and Skype in order to improve the speed of its responsiveness to significant issues. In noting the Chair's comments regarding 'ringing' Board members to discuss issues, we also recommend that the Board explore other ways of working such as electronically which in turn would also provide a better audit trail of what information has been provided to members (and when).

79. In considering the role of the Board and the process by which a decision to seek brokerage was arrived at, we consider that the culture of poor budgetary oversight at Raigmore Hospital was to some extent also exhibited by the NHS Highland Board. Given our concerns set out above we consider that the leadership demonstrated at NHS Highland was poor both at Board level and in terms of the governance arrangements.

80. The AGS report entitled The role of Boards reported that the UK Corporate Governance Code (which sets out best practice for private sector companies) recommends that any review of the board's performance should involve someone from outside the board who could bring an independent perspective. This approach can also assist in sharing and promoting best practice.  

81. Given our concerns at paragraph 73 we recommend NHS Highland consider seeking external peer review in evaluating its Board's performance.

82. We also seek the views of the Scottish Government on whether it would propose to update its guidance to NHS Boards to recommend external peer reviews of NHS Boards' performances.

The role of the Scottish Government

83. As noted above the Scottish Government agreed to and facilitated an in-year review of NHS Highland's financial plan and performance during 2013/14. This
concluded that NHS Highland should be capable of following through to complete those actions identified during the course of the review and managing with its Revenue Resource Limit for 2013/14. The Scottish Government took reassurance from reviewing this report that the actions which had been identified would deliver financial balance in the current year and that strategic forward planning was in place to produce a financial plan (2014/15) which was both sustainable and achievable. 76

84. This review was in addition to regular meetings between the Scottish Government and the Director of Finance and other senior NHS Highland officers at which a range of issues including financial performance and future financial planning were discussed. In addition the Scottish Government confirmed that it has met with Audit Scotland to understand the extent to which the issues identified at NHS Highland could apply elsewhere. 77

85. The Committee agrees with the Scottish Government that brokerage can be a helpful mechanism which can assist NHS Boards with their long term financial planning. However, we do not consider that the current process by which brokerage is agreed is transparent. We also have concerns over the current process by which brokerage is agreed and consider that it may be viewed by Boards as a short term solution rather than to support long term financial planning.

86. In addition, whilst we acknowledge the steps taken by the Scottish Government to monitor and review NHS Highland's financial performance, we are concerned that, in this case, brokerage appears to have been sought by NHS Highland officers and agreed to by the Scottish Government without the formal consideration of the Board to this specific course of action.

87. The Committee therefore recommends that the Scottish Government reviews the process and basis upon which brokerage is considered and agreed to and the transparency of the decision making process. In particular we would recommend the Scottish Government reviews whether its agreement to brokerage should be predicated upon the relevant NHS Board having been informed of that course of action on the basis of robust financial and risk information.

88. Finally, NHS Highland achieved a break even position for a number of years prior to 2013/14 by, in part, generating additional savings across other services to compensate for overspends at Raigmore Hospital. In light of this, we seek further information from the Scottish Government on the extent to which its in-year reviews and monitoring of NHS Boards’ finances includes scrutiny of how, within each NHS Board, key parts of the service are performing financially.
Financial management in 2014/15 and beyond

89. The Committee heard about the actions taken in 2014/15 to ensure that NHS Highland will break even at financial year end. These actions include changes in the content and timing of financial reports, including more detail regarding risks and trajectories of expenditure and savings. A Delivering Financial Balance Programme Board has also been established to focus on achieving savings targets by monitoring and scrutiny of project charters and plans. In addition, topics discussed informally at Board meetings will be noted in formal minutes of the Board and NHS Highland is looking at the timing of the publication of its in-month figures to try and report to the Board in a more timely way.

90. NHS Highland reported that, subject to external audit, it had delivered break even for 2014/15, despite challenging savings target of £22.4 million (which includes £0.5 million repayment for brokerage).

91. In its May 2015 review, Audit Scotland reported that the Board has established a more strategic approach to savings via seven savings charters and progress against these is regularly reported to the Board. There has also been a stronger focus on converting non-recurring savings to recurring to reduce financial pressures in the future. That review reports that there is a three year phased return to recurring balance over three years which includes:

- an overall savings requirement of £21.9 million in 2014/15, £3.7 million of which would be non-recurring; (the Board anticipated an underlying deficit of £6 million at the end of 2014/15 as a result of carrying forward £8 million non-recurring savings from 2013/14)
- an indicative savings requirement of £18 million in 2015/16; £4 million of which will be non-recurring savings;
- an indicative savings requirement of £26 million in 2016/17; £2 million of which will be non-recurring savings.

Non-recurring savings

92. The Chair of NHS Highland stated that NHS Highland had brought down its levels of non-recurring savings to zero by 2009/10. However, as a result of service changes planned by NHS Highland the percentage of savings delivered as non-recurring increased to 62% (£11.4 million) in 2013/14. The board's total savings in 2013/14 were £18.4 million.

93. In evidence, the Chair of NHS Highland explained that sustainable service redesign is needed to get the balance of NHS Highland activity correct so that the level of non-recurring savings can be addressed. The Board has had a number of
longer term plans for parts of its services such as adult care and a refreshed ten year plan was to be considered by the Board in early February 2015. The Chair however also recognised that—

94. In written evidence NHS Highland confirmed that it had exceeded its target reduction on the underlying deficit carried forward into 2015-16 by reducing the non-recurring savings it relied upon to break even to £5.6 million (60% of the total savings).

Vacancy management

95. Responding to questions about where the £5.6 million in non-recurring savings came from, the Committee heard that the vast majority of the savings are achieved through holding posts vacant. NHS Highland stated that it was routine management to hold posts vacant if that is feasible and that there could be a range of reasons why posts were not filled. Such reasons include that some posts are hard to fill whilst other posts could be removed through service redesign. In that regard part of NHS Highland's savings programme, which the Board approved, would have assumed some level of vacancy management.

96. As an example NHS Highland explained that its working practice in corporate services is for vacancies to be held for six months, which would generate some non-recurring savings.

97. NHS Highland explained that—

98. NHS Highland confirmed that its staff governance Committee monitored staff vacancies with that Committee reporting to the Board. A staff partnership is also part of the staff governance arrangements.

99. Subsequently we learned that the staff governance Committee discussed workforce planning at its meeting on 11 November 2014, including "managing and reducing the workforce cost base through workforce productivity and efficiency approaches, underpinned by quality improvement and service redesign."

100. In the May 2015 review, Audit Scotland reported that the board's sickness/absence rate at the end of 2014/15 had increased slightly to 4.9% (against a national target of 4%).
101. NHS Highland confirmed that it continually assesses and reports back to local management on the staff vacancy and sickness rates and they take action locally to manage that as required. Whilst there had been increasing pressure on staff in corporate services, NHS Highland did not consider there to be a link between its sickness/absence rate and its policy of leaving posts unfilled for several months.\(^9\)

102. The Committee is concerned at the significant increase in non-recurring savings which has arisen at NHS Highland over the last four years, noting it is almost double that which the Chair considered acceptable.

103. And whilst we acknowledge the reduction in reliance on non-recurring savings in 2014/15 this has been achieved in large part through staff vacancies. We are concerned at comments that it is routine to hold posts vacant such as the practice of holding corporate vacancies for 6 months. The evidence we received does not suggest to us that this is a sustainable, strategic approach underpinned by quality improvement and service redesign. We consider that, based on the evidence provided to us by NHS Highland, the substantive purpose of the vacancy management system is to generate savings.

104. Whilst we note the focus of the savings charters on reducing medical locums, we request a summary from NHS Highland of its workforce plan including its strategic approach to managing vacancies.

105. More generally we seek clarification from the Scottish Government on the extent to which it challenges NHS Boards on their balance of non-recurring to recurring savings during in-year meetings and reviews of NHS Boards’ finances.

**NHS Scotland National Resource Allocation Committee (NRAC) funding**

106. In January 2015, the Scottish Government announced that over and above the additional £2.5 million of NRAC funding planned for 2014/15 and £5 million planned for 2015/16 it was also going to provide an additional £6.5 million for 2015/16 to bring NHS Highland within 1% of its NRAC target for funding.

107. As set out in the table below, in order to better balance or ‘smooth’ the amounts of the additional funding between 2014/15 and 2015/16 the Scottish Government agreed to bring forward to 2014/15 £3 million of the £11.5 million due for payment in 2015/16 (with a corresponding reduction in that year).\(^9\)
Table 2: Additional NRAC funding for NHS Highland

<table>
<thead>
<tr>
<th></th>
<th>Actual for 2014/15 £000s</th>
<th>Planned for 2015/16 £000s</th>
</tr>
</thead>
<tbody>
<tr>
<td>NRAC uplift planned at the start of 2014/15</td>
<td>2,500</td>
<td>5,000</td>
</tr>
<tr>
<td>Additional NRAC funding agreed in January 2015</td>
<td>0</td>
<td>6,500</td>
</tr>
<tr>
<td><strong>Total NHS Highland NRAC uplift</strong></td>
<td><strong>2,500</strong></td>
<td><strong>11,500</strong></td>
</tr>
<tr>
<td>Adjustment due to smoothing</td>
<td>3,000</td>
<td>-3,000</td>
</tr>
<tr>
<td><strong>Total uplift following smoothing</strong></td>
<td><strong>5,500</strong></td>
<td><strong>8,500</strong></td>
</tr>
</tbody>
</table>

108. As a consequence NHS Highland will receive an additional £5.5 million in 2014/15 and £8.5 million in 2015/16 which will offset the level of savings required to be made in each of those years.

109. The Chair of NHS Highland explained that the additional NRAC funding in 2014/15 had enable the Board to—

> Manage the year-end position a lot more comfortably without making some decisions that might have inconvenienced some of our patients.  

110. The Chief Executive stated that whilst NHS Highland was on track to break even in 2014/15 the additional NRA funding alleviated the pressure and ensured that it did not have to take resources from front line services. It had also enabled the creation of three additional permanent posts of Deputy Directors of Operations in Highlands. NHS Highland explained that following a reduction on senior management staff, it was agreed with Union colleagues, senior managers and clinical staff that these new posts were required to unlock the savings and enable the transformation of services across the rest of Highland.

111. NHS Highland confirmed that should there be any changes to the current organisation structure then these additional posts would be transitional.

112. The Committee welcomes the increased funding from the Scottish Government as moving NHS Highland towards NRAC funding parity. This has enabled NHS Highland to report that, subject to external audit, it will break even in 2014/15.

113. Whilst we acknowledge that the additional £3 million of NRAC funding brought forward to 2014/15 has meant that some front line services were not reduced, we remain concerned that this additional funding in 2014/15 and 2015/16 may reduce the Board's focus on addressing the underlying poor financial management issues which arose in 2013/14.

114. In that regard we seek further information from the AGS as to the extent to which NHS Highland has used the NRAC funding for 2014/15 to support
long term sustainable service redesign. We also seek clarification from NHS Highland as to how agreed workforce plan for 2014/15 supports the decision to recruit three additional Deputy Director posts.

Concluding remarks

Whilst we note that NHS Highland has taken steps to improve its financial management and reporting to the NHS Highland Board, it is essential for the future financial health of NHS Highland that all the actions and recommendations identified in the internal and external audit reports it has received to date are acted upon. We therefore invite the AGS to update the Committee by the end of 2015 on the progress made by NHS Highland in addressing the issues identified within the 2013/14 audit of NHS Highland.

We also invite the Scottish Government to review the corporate governance arrangements for NHS Boards, as set out in the Scottish Public Finance Manual, in light of the issues identified in this report, to determine that they are robust, transparent and appropriate.
Section 22 reports highlight issues within the audit of accounts of individual public bodies.


Scottish Government written evidence, 8 December 2014.

Scottish Government written evidence, 8 December 2014.

The revenue budget is known as the Revenue Resource Limit (RRL) and the capital budget is known as the Capital Resource Limit (CRL).


Hereafter referred to as “the internal auditor”.

Scottish Parliament Public Audit Committee, Official Report, 2 February 2015, Col 34.


Table 2, NHS Highland Financial Management Review, May 2015; and NHS Highland website, Board meeting papers


Scottish Parliament Public Audit Committee, Official Report, 2 February 2015, Col 34.


That is NHS Highland’s committed expenditure at the start of the financial year was £20 million higher than the budget it had received.


NHS Highland written evidence, 13 January 2015.

The 2013/14 audit of NHS Highland: Financial Management, paragraph 6


NHS Highland written evidence, 13 January 2015.
The NHS Highland website confirms that the first Board meeting in 2014 was on 4 February 2014 with a Board development session on 3 February 2014.

Annexe A

EXTRACT FROM THE MINUTES OF THE PUBLIC AUDIT COMMITTEE

17th Meeting, 2014 (Session 4) Wednesday 5 November 2014


Caroline Gardner, Auditor General for Scotland;
Stephen Boyle, Assistant Director, and Tricia Meldrum, Senior Manager, Audit Scotland.


Angela Canning, Assistant Director, Audit Scotland.

The Committee agreed to seek written evidence from the Scottish Government and NHS Orkney on issues raised in discussion. The Committee also agreed to seek oral evidence from NHS Highland at a future meeting.

20th Meeting, 2014 (Session 4) Wednesday 17 December 2014


The Committee agreed to defer consideration of whether to take evidence on these reports from the Scottish Government.

3rd Meeting, 2015 (Session 4) Monday 2 February 2015


Garry Coutts, Chair, Elaine Mead, Chief Executive, Nick Kenton, Director of Finance, and Chris Brown, Chief Internal Auditor, NHS Highland.
Section 22 - The 2013/14 audit of NHS Highland: Financial management (in private): The Committee considered the evidence received at agenda item 2 and took evidence from—

Fraser McKinlay, Director and Controller of Audit, Angela Canning, Assistant Director, and Stephen Boyle, Assistant Director, Audit Scotland.

The Committee agreed to consider a draft report at a future meeting.

5th Meeting, 2015 (Session 4) Wednesday 11 March 2015


The Committee agreed to seek oral evidence from NHS Highland at a future meeting and to consider an approach paper, in private, at a future meeting.

9th Meeting, 2015 (Session 4) Wednesday 13 May 2015


Elaine Mead, Chief Executive, Garry Coutts, Chair, and Nick Kenton, Director of Finance, NHS Highland.

Section 22 report - The 2013/14 audit of NHS Highland: Financial management: The Committee considered the evidence received at agenda item 2 and took evidence from—

Fraser McKinlay, Director of Performance Audit and Best Value, and Stephen Boyle, Assistant Director, Audit Scotland.

The Committee agreed to consider a draft report in private at a future meeting.

11th Meeting, 2015 (Session 4) Wednesday 10 June 2015


The Committee then agreed its report subject to some further changes to be agreed by correspondence. The Committee agreed the arrangements for its publication.
Annexe B

ORAL EVIDENCE AND ASSOCIATED WRITTEN EVIDENCE

Please note that all oral evidence and associated written evidence is published electronically only, and can be accessed via the Public Audit Committee’s webpages, at: http://www.scottish.parliament.uk/parliamentarybusiness/CurrentCommittees/29860.asp

17th Meeting, 2014 (Session 4) Wednesday 5 November 2014

ORAL EVIDENCE
Caroline Gardner, Auditor General for Scotland; Stephen Boyle, Assistant Director, and Tricia Meldrum, Senior Manager, Audit Scotland.

3rd Meeting, 2015 (Session 4) Wednesday 2 February 2015

ORAL EVIDENCE
Garry Coutts, Chair, Elaine Mead, Chief Executive, Nick Kenton, Director of Finance, and Chris Brown, Chief Internal Auditor, NHS Highland.

Fraser McKinlay, Director and Controller of Audit, Angela Canning, Assistant Director, and Stephen Boyle, Assistant Director, Audit Scotland.

9th Meeting, 2015 (Session 4) Wednesday 13 May 2015

ORAL EVIDENCE
Elaine Mead, Chief Executive, Garry Coutts, Chair, and Nick Kenton, Director of Finance, NHS Highland.

Fraser McKinlay, Director of Performance Audit and Best Value, and Stephen Boyle, Assistant Director, Audit Scotland.

WRITTEN EVIDENCE

• NHS Highland Financial Management review, published May 2015 (515KB pdf)
• Audit Scotland to the Public Audit Committee, dated 14 May 2015 (25KB pdf)
• NHS Highland to the Public Audit Committee, dated 20 April 2015 (157KB pdf)
• Public Audit Committee to NHS Highland, dated 26 March 2015 (137KB pdf)
• NHS Highland to the Public Audit Committee, dated 3 March 2015 (264KB pdf)
• Public Audit Committee to NHS Highland, dated 6 February 2015 (121KB pdf)
• Scottish Government to the Public Audit Committee, dated 4 February 2015 (82KB pdf)

• NHS Highland to the Public Audit Committee, dated 13 January 2015 (286KB pdf)