

# NHS Lothian

## Internal Audit Report 2022/23

### Core Financial Controls - Budgeting

Assurance Rating: **Significant Assurance**

Date: 3 October 2022

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The contacts in connection with this report are:

**Joanne Brown**  
Partner  
T: 0141 223 0848  
E: [joanne.e.brown@uk.gt.com](mailto:joanne.e.brown@uk.gt.com)

**Peter Clark**  
Director  
T: 0141 223 0785  
E: [peter.c.clark@uk.gt.com](mailto:peter.c.clark@uk.gt.com)

**Jamie Fraser**  
Internal Audit Assistant Manager  
T: 0141 223 0886  
E: [jamie.a.fraser@uk.gt.com](mailto:jamie.a.fraser@uk.gt.com)

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## Timetable

- Date closing meeting held: 14 September 2022
- Date draft report issued: 15 September 2022
- Date management comments received: 30 September 2022
- Date Final report issued: 3 October 2022
- Date presented to Audit and Risk Committee: 21 November 2022

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# Executive Summary

## Introduction

On an annual basis NHS Lothian needs to set a budget which demonstrates a breakeven financial position. The Director of Finance, with the management team, developed the NHS Lothian Financial Plan for 2022/23 which was presented to the Board in April 2022 for approval. This is consistent with the Board's Standing Orders which state the requirement: "The Board shall approve its Financial Plan for the forthcoming financial year, and the opening revenue and capital budgets."

The Finance and Resources (F&R) Committee, in its consideration of the Financial Plan for 22/23 and longer-term financial strategy endorsed the plan, in order for initial budgets to be set. However, the F&R Committee highlighted, and asked the Board to take into account, that the on-going financial challenges resulting from the pandemic means that they could not offer assurance that NHS Lothian would be able to deliver a balanced financial position for 2022/23.

The overall budget gap for 2022/23 totals £107m and is split into two elements. There is a £28m gap relating to the Core financial position and a further £79m relating to projected NHS costs associated with Covid.

The Core Financial Position gap, the potential volatility of Covid costs, uncertainty about funding, and the challenge of recovery and remobilisation, are all areas of concern to management and will require close management and control.

## Scope

The objective of the audit was to evaluate the adequacy of internal controls in place around Budgeting and review the design and operating effectiveness of the controls in place to mitigate against the following potential risk areas:

- There is a lack of knowledge and expectations over the budgeting process and as a result, budgets are not effectively managed.
- The budgets set lack flexibility and are not sufficiently reviewed by budget holders and management accountants, resulting in the budgets not taking account of areas of uncertainty and variances that could arise during the financial year.
- There is limited or no reporting and monitoring of budgets oversight to ensure scrutiny and challenge over budgets and actuals, resulting in remedial actions not being identified and/or implemented in a timely manner.
- Key steps identified to assist with management and control of the budget process for 2022/23 have not been implemented and as a result, the organisation may be unable to close the Core Financial Position gap identified.

## Approach

Our audit approach was as follows:

- Obtain understanding of the key areas outlined in scope above, through discussions with key personnel, review of management information and walkthrough test, where appropriate.
- Identify the key risks relevant within the Budgeting process.
- Evaluate the design of the controls in place to address the key risks.
- Test the operating effectiveness of the controls in place.

It is Management's responsibility to develop and maintain sound systems of risk management, internal control and governance and for the prevention and detection of irregularities and fraud. Internal audit should not be seen as a substitute for Management's responsibilities for the design and operation of these systems.

A complete list of staff involved in the audit and documents reviewed can be seen at Appendix 1.

## Acknowledgments

We would like to thank all staff consulted during this review for their assistance and cooperation.

## Limitations in Scope

Please note that our conclusion is limited by scope. It is limited to the risks outlined above. Other risks that exist in this process are out with the scope of this review and therefore our conclusion has not considered these risks. Where sample testing has been undertaken, our findings and conclusions are limited to the items selected for testing.

This report does not constitute an assurance engagement as set out under ISAE 3000.

## Summary of Findings

We have concluded that the controls in place in respect of NHS Lothian's budgeting processes provides a **SIGNIFICANT** level of assurance. The table below provides a summary of the findings. The ratings assigned are based on the agreed internal audit rating scale (**Appendix 2**).

Detailed findings, recommendations and agreed management actions are found in Section 2 of this report.

Significant Assurance			
HIGH	MEDIUM	LOW	ADVISORY
-	-	2	-

Ref	Issue	H	M	L	A
2.1	<p><b>Risk area as per scope: There is a lack of knowledge and expectations over the budgeting process and as a result, budgets are not effectively managed.</b></p> <p>Budget holders are not signing-off their budget in line with procedures and the Board's Standing Financial Instructions.</p>	-	-	1	-
2.2	<p><b>Risk area as per scope: There is a lack of knowledge and expectations over the budgeting process and as a result, budgets are not effectively managed.</b></p> <p>Updated Financial Operating Procedures for Budgetary Control not shared with staff in a timely manner</p>	-	-	1	-
<b>TOTAL</b>		-	-	2	-

## Areas of Good Practice

Budget holders are provided with ongoing support and assistance by the Finance team. This is made up of daily communications to discuss queries as well as formal monthly meetings with Management Accountants and Assistant Finance Managers to talk through the financial information provided via the Financial Performance dashboard (Tableau). Whilst formal training has been paused during the pandemic, the Finance team have created a Budget Holder Training Project, led by the Finance Manager (Acute Services) and Finance Business Partner. The aim to ensure budget holders are part of continuous finance learning and to reduce the finance skill gap of budget holders. A Programme of Work has been developed under 4 streams:

1. Presentations (Road Shows)
2. LearnPro Modules
3. One2One Training
4. Budget Holder Checklist

The project will delivered over the course of 2022/23 and feedback will be sought from budget holders in order to make improvements going forward.

## Areas of Good Practice cont.

The Finance Team conduct a Quarterly Review process which focuses on the core underlying position. Budget holders are provided with financial information ahead of the meetings with discussions focussed on comparing budget per Financial Plan versus actuals at Q1. Where there are variances, budget holders are expected to implement actions to ensure their budget returns to the target level. At the time of the audit, the Q1 review was just commencing and budget holders had been contacted to schedule meetings.

Monthly financial position reporting is produced by the Finance Team. This is made available to budget holders via Tableau. The reporting is presented to Clinical Management Teams, the Senior Finance Team, the Corporate Management Team, the Finance and Resources Committee and the Board at their regular scheduled meetings throughout the financial year. Each IJB is also provided with financial position reporting on a monthly basis and the Chief Financial Officers/Finance Business Partners attend the Senior Finance team meetings.

Additionally, as part of the 2022/23 Financial Plan, the organisation has identified a target for achieving efficiency savings and progress in delivering these savings is reported to the Finance and Resources and the Board. In 2021/22, the Corporate Management Team endorsed a multi-faceted programme for the delivery of Financial Sustainability and Value for NHS Lothian, which has more recently been constructed into a three horizon approach. Progress on delivery is being monitored by the Corporate Management Team via the Financial Oversight Board on a monthly basis. Regular updates are also provided to the Finance and Resources Committee. As part of this programme, thematic programmes of efficiency are being constructed around traditional themes of expenditure and a deadline of December 2022 has been set to develop fully quantified plans.

Due to the uncertainty in the financial position of the organisation and ongoing funding provided by the Scottish Government, the Finance team continue to assess the ongoing costs of Covid-19 and regular review areas of uncertainty, assumptions and growth estimates to ensure a clear outlook on the financial position of the organisation is presented through the governance framework.

A Finance risk (3600) is documented within the Corporate Risk Register and this is reviewed by the Finance and Resources Committee and the Board at each meeting. Mitigations and actions are in place to aid the organisation in reducing the risk score.

## Main Findings

As part of the annual budgeting process outlined in the Standing Financial Instructions and Financial Operating Procedure – Budgetary Control, budget holders are required to sign-off their part of the budget following formal approval of the Financial Plan by the Board. For 2022/23, a deadline of 1 July 2022 was set for sign-off to be provided for 27 budget statements. As at 26 August 2022, sign-off had been provided for 22 budget statements; 20 of which were by the deadline and two were 12 days after the deadline. However, for the remaining five, sign-off was not yet obtained by the budget holders at the time of the audit.

The Financial Operating Procedure – Budgetary Control was last updated in March 2022 and while this document has been made available to the Finance Team via a shared drive, it has not yet been communicated to staff across the organisation via the staff intranet.

## Follow Up

Approximately two weeks following issue of the final Internal Audit report, a member of the Audit Team will issue an evidence requirements' document for those reports where management actions have been agreed.

This document forms part of the follow up process and records what information should be provided to close off the management action. The follow-up process is aligned with the meetings of the Board's Audit & Risk Committee. Audit Sponsors will be contacted on a quarterly basis with a request to provide the necessary evidence for those management actions that are likely to fall due before the next meeting of the Audit and Risk Committee.

# Management Action Plan

**Risk area as per scope:** There is a lack of knowledge and expectations over the budgeting process and as a result, budgets are not effectively managed.

**Finding 2.1 – Budget holders are not signing-off their budget in line with procedures and the Board’s Standing Financial Instructions.**

Low

## Control

The Financial Operating Procedure - Budgetary Control clearly states that budget holders are required to sign-off their annual budget following Board agreement of the Financial Plan.

## Observation

The 2022/23 Financial Plan for NHS Lothian was approved by the Board on the 6th of April 2022. Each budget holder was provided with their budget statement alongside a letter from the Director of Finance on 2nd June 2022. This was almost two months after approval was provided by the Board. Whilst we understand that the delay in the Board approving the financial plan is a result of the ongoing Covid-19 pandemic and delays in receiving 2022/23 funding confirmation from Scottish Government, budget holders were not provided with their budget statements for the financial year for sign-off in a timely manner.

In the letter provided to budget holders, it was requested that they provide sign-off on the delegated budget for their Business Unit/Directorate by Friday 1st July 2022. This is for the budget holder to agree that they can deliver a balanced position for the financial year. A budget sign-off tracker is held by the Finance team that records when sign-off is received by budget holders and evidence of approval is retained. Review of the budget sign-off tracker noted the following:

- Of the 27 budget statements issued to budget holders for sign-off, five budgets had not yet been signed-off as at 26 August 2022.
- 20 budget statements received sign-off by the 1 July deadline.
- Two responses were received 12 days after the 1 July deadline.

Therefore, budget holders are not signing-off their budget in line with procedures and the Board’s Standing Financial Instructions.

## Risk

Without timely issue of the budgets and prompt receipt of sign-off, management cannot demonstrate that the Financial Operating Procedures and Standing Financial Instructions are being followed.

## **Recommendation**

Where possible, Management Accounting should endeavour to issue budgets for agreement each year as soon as possible following approval of the Board’s Financial Plan. To ensure prompt response from key budget holders, controls should be set up to chase agreement after a number of days and, where necessary, escalate instances where significant delays have occurred.

## **Management Response**

The last 2 years have been affected by Covid issues, impacting on year end arrangements and creating an element in delay in setting budgets in the ledger for the new financial year. Consequentially this has delayed the production and distribution of Budget Sign off letters.

## **Management Action**

For 23/24 Budget Sign off, the timetable for issue and return of signed agreements will be reviewed to ensure this is progressed on a timely basis following agreement of the budget at the Board, with appropriate follow up to ensure timely receipt of signed off budget letters.

## **Responsibility:**

**Deputy Director of Finance**

## **Target Date:**

**30 June 2023**

**Risk area as per scope:** There is a lack of knowledge and expectations over the budgeting process and as a result, budgets are not effectively managed.

**Finding 2.2 – Updated Financial Operating Procedures for Budgetary Control not shared with staff in a timely manner**

Low

Control

The NHS Lothian Standing Financial Instructions (April 2021) and Financial Operating Procedure - Budgetary Control (March 2022) documents clearly communicate the organisation's arrangements for budgetary control and the roles and responsibilities of budget holders.

Observation

The Standing Financial Instructions are available on the NHS Lothian website and are therefore accessible to required staff members.

We ascertained from the Senior Finance Manager that the Financial Operating Procedure - Budgetary Control is saved in a shared folder for management accounting staff to access. However, budget holders do not have access to the most recent version as it has not been updated on the staff intranet as the management accounting on-line offering is all being reviewed currently. The version available online is out of date; however, we confirmed that only minor changes were made to the document which had no impact on the roles and responsibilities of budget holders.

Risk

Without up-to-date procedures, there may be a risk that staff may be unclear about the process for setting and approving budgets.

**Recommendation**

Management Accounting should ensure that when the Financial Operating Procedure – Budgetary Control is revised, it is shared with staff across the organisation in a timely manner via the staff intranet.

**Management Response**

Whilst the Financial Operating Procedure – Budgetary Control has been reviewed and updated for the current year, this has not been published, and therefore not accessible to budget holders. That said, the previous version is currently still available and there has been no change to budget holder responsibilities within the policy.

**Management Action**

Ensure publication of the Financial Operating Procedure - Budgetary Control is published on the intranet and is accessible to staff.

**Responsibility:**

**Deputy Director of Finance**

**Target Date:**

**31 October 2022**

# Appendices



# Appendix 1 – Staff Involved and Documents Reviewed

## Staff Involved

- Deputy Director of Finance
- Senior Finance Manager
- Assistant Finance Manager for Diagnostics, Anaesthetics, Theatres and Critical Care (DATCC)
- Finance Manager (Acute Services)
- Assistant Finance Manager – Corporate Team
- Management Accountant – Corporate Team
- Dental Care Professional Manager
- Specialist Education Lead: Workforce Development
- Clinical Nurse Manager for Cardiology, Cardiothoracic Surgery & Respiratory Medicine – Royal Infirmary Edinburgh
- Clinical Nurse Manager – Paediatric – Medical Nursing

## Documents Reviewed

- 2022/23 Financial Plan approved in April 2022 by NHS Lothian Board
- NHS Lothian Board Papers and Minutes April – August 2022
- Finance and Resources Committee Papers and Minutes April – August 2022
- NHS Lothian Standing Financial Instructions April 2021
- NHS Lothian Scheme of Delegation April 2021
- Financial Operating Procedure – Budgetary Control March 2022
- Quarter 1 Scottish Government NHS Board Financial Performance Return
- Financial Position reports provided to Corporate Management Team, Clinical Management Teams, Finance and Resources Committee and the Board April – August 2022
- Financial Sustainability Programme Update reports to Corporate Management Team July and August 2022
- Thematic Efficiency Programme Documentation – Letter to SROs and Exec Leads and Primary Care Prescribing and Nursing Workforce programme briefs
- NHS Lothian Quarter 1 Finance Performance review – email to budget holders August 2022
- Budget Holder Training Project
- Source and Application File 2022/23
- Budget Holder Sign Off Tracker 2022/23

# Appendix 2 – Our IA Report assurance levels

The table below shows the levels of assurance we provide and guidelines for how these are arrived at. We always exercise professional judgement in determining assignment assurance levels, reflective of the circumstances of each individual assignment.

Rating	Definition	When Internal Audit will award this level
<b>Significant assurance</b>	<p>The Board can take reasonable assurance that the system(s) of control achieves or will achieve the control objective.</p> <p>There may be an insignificant amount of residual risk or none at all.</p>	<p>There is little evidence of system failure and the system appears to be robust and sustainable. The controls adequately mitigate the risk, or weaknesses are only minor (for instance a low number of findings which are all rated as 'low' or no findings)</p>
<b>Moderate Assurance</b>	<p>The Board can take reasonable assurance that controls upon which the organisation relies to achieve the control objective are in the main suitably designed and effectively applied.</p> <p>There remains a moderate amount of residual risk.</p>	<p>In most respects the "purpose" is being achieved. There are some areas where further action is required, and the residual risk is greater than "insignificant".</p> <p>The controls are largely effective and in most respects achieve their purpose with a limited number of findings which require management action (for instance a mix of 'medium' findings and 'low' findings)</p>
<b>Limited Assurance</b>	<p>The Board can take some assurance from the systems of control in place to achieve the control objective, but there remains a significant amount of residual risk which requires action to be taken.</p>	<p>This may be used when:</p> <ul style="list-style-type: none"> <li>There are known material weaknesses in key control areas.</li> <li>It is known that there will have to be changes that are relevant to the control objective (e.g. due to a change in the law) and the impact has not been assessed and planned for.</li> </ul> <p>The controls are deficient in some aspects and require management action (for instance one 'high' finding and a number of other lower rated findings)</p>
<b>No assurance</b>	<p>The Board cannot take any assurance from the audit findings. There remains a significant amount of residual risk.</p>	<p>The controls are not adequately designed and / or operating effectively and immediate management action is required as there remains a significant amount of residual risk (for instance one Critical finding or a number of High findings)</p>

# Appendix 3 - Continued

The table below describes how we grade our audit recommendations based on risks

Rating	Description	Possible features
<b>High</b>	Findings that are fundamental to the management of risk in the business area, representing a weakness in the design or application of activities or control that requires the immediate attention of management	<ul style="list-style-type: none"> <li>▪ Key activity or control not designed or operating effectively</li> <li>▪ Potential for fraud identified</li> <li>▪ Non-compliance with key procedures / standards</li> <li>▪ Non-compliance with regulation</li> </ul>
<b>Medium</b>	Findings that are important to the management of risk in the business area, representing a moderate weakness in the design or application of activities or control that requires the immediate attention of management	<ul style="list-style-type: none"> <li>▪ Important activity or control not designed or operating effectively</li> <li>▪ Impact is contained within the department and compensating controls would detect errors</li> <li>▪ Possibility for fraud exists</li> <li>▪ Control failures identified but not in key controls</li> <li>▪ Non-compliance with procedures / standards (but not resulting in key control failure)</li> </ul>
<b>Low</b>	Findings that identify non-compliance with established procedures, or which identify changes that could improve the efficiency and/or effectiveness of the activity or control but which are not vital to the management of risk in the business area.	<ul style="list-style-type: none"> <li>▪ Minor control design or operational weakness</li> <li>▪ Minor non-compliance with procedures / standards</li> </ul>
<b>Advisory</b>	Items requiring no action but which may be of interest to management or which represent best practice advice	<ul style="list-style-type: none"> <li>▪ Information for management</li> <li>▪ Control operating but not necessarily in accordance with best practice</li> </ul>



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