

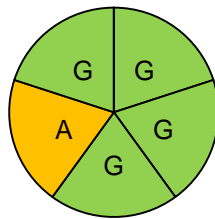
Internal Audit



Financial Planning

March 2016

Report Assessment



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Introduction

Financial planning is concerned with ensuring that NHS Lothian has adequate financial resources to meet its commitments and deliverables as a healthcare provider. NHS Lothian must also ensure that budget allocations across departments accurately reflect the level of expenditure required.

In line with the financial constraints felt across the public sector, NHS Lothian, like all health boards in Scotland, must deliver cash releasing savings each year in order to achieve financial balance. This requires the Board to identify innovative ways of making savings to ensure that the same or a better level of service can be delivered for less expenditure.

In its Financial Plan 2015/16 to 2019/20, NHS Lothian has set out how its annual budget of £1.5 billion would be split across each business unit. The Financial Plan also sets out how NHS Lothian plans to deliver £32 million of savings during 2015/16. NHS Lothian assessed 82% of the £32 million savings as either high or medium risk. It is essential that savings schemes are closely monitored and scrutinised to ensure the inherent risks are mitigated and the savings are delivered in a timely fashion.

Scope

The audit evaluated the process for financial planning across NHS Lothian. In particular, the audit focused on how financial planning is linked to strategic and operational plans, and how NHS Lothian agrees detailed savings plans for current and future financial years.

Acknowledgements

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

Executive Summary

Conclusion

NHS Lothian's overall financial position is extremely challenging for a number of reasons including: the level of funding available from the Scottish Government; population growth and demographic change leading to increasing and more complex patient demand; a focus on waiting times; and continued efficiency targets. All of these factors mean a great deal of work is required each year in order to arrive at a balanced financial plan and, at the time of our audit, that work was not complete for 2016/17. As a result the plans we reviewed still contained significant funding gaps.

However, our audit was concerned with the process employed by NHS Lothian in order to develop achievable, balanced financial plans. While the financial planning process for 2016/17 was still in progress during our audit, we found that the controls surrounding the financial planning process to date are for the most part operating effectively. Our audit highlighted that there are a number of high risk recovery plans being proposed in order for NHS Lothian to break even, some of which may not be viable. NHS Lothian's draft financial plan was submitted to the Scottish Government on the 21 March 2016. Following that consultation process, further work may be required around the viability of recovery plans identified to break even and the plan will have to be presented to NHS Lothian's Board for approval prior to the final submission to the Scottish Government on 31 May 2016.

Summary of Findings

The table below summarises our assessment of the adequacy and effectiveness of the controls in place to meet each of the objectives agreed for this audit. Definitions of the ratings applied to each action are set out in Appendix 1.

No.	Control Objective	Control objective assessment	Number of actions by action rating			
			Critical	Significant	Important	Minor
1	NHS Lothian has developed and implemented an effective financial planning process.	Green				
2	Detailed financial plans are developed for all areas of the organisation with input from relevant department heads and budget holders as required.	Green			1	
3	Financial planning is consistent with the strategic plan, ensuring that adequate resources are in place to support the achievement of NHS Lothian's short, medium and long-term objectives.	Green				

No.	Control Objective	Control objective assessment	Number of actions by action rating			
			Critical	Significant	Important	Minor
4	The financial planning process is linked to the development of savings plans and efficiency targets.	Amber		1	1	
5	Financial planning is completed and communicated on a timely basis.	Green				1

Control Objective Ratings

Action Ratings	Definition
Red	Fundamental absence or failure of controls requiring immediate attention (60 points and above)
Amber	Control objective not achieved - controls in place are inadequate or ineffective (21 – 59 points)
Green	Control objective achieved – no major weaknesses in controls but may be scope for improvement (20 points or less)

Main findings

We identified a number of areas of good practice during the review.

The Board recognised that the existing process for financial planning was not effective in achieving service engagement in delivering the plan and that the achievement of the Local Reinvestment Plan (LRP) was becoming more challenging with an increasing year on year recurrent gap. The Board agreed to implement a revised process for 2016/17 with a bottom up approach being applied. This meant that rather than a corporate plan being prepared, individual business units were to prepare their own local plans with actions required to breakeven at the end of the year. These plans were then consolidated to create the overall NHS Lothian Financial Plan.

Key budget holders were notified of the revised financial planning process in sufficient time for the start of the planning cycle. Budget holders at all levels within the services have been involved in the identification of cost pressures and in identifying potential service developments for the 2016/17 financial year. These service developments were analysed into local/organisational priorities and categorised as either 'must do' or optional developments. In addition, budget holders have been involved in identifying areas where savings could be made and/or efficiencies created.

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Monitoring controls are in place to ensure that financial plans are regularly reviewed and updated as the planning process evolves and it was evident that information is amalgamated into the organisation's financial plan for reporting to Board committees. Access to the master plan for the organisational financial plan is password protected ensuring only authorised personnel can update and adjust the contents.

We identified one significant and two important areas for improvement during the review. These are listed below:

- Financial recovery plans have been developed by each Business Unit and Corporate function which detail proposed actions to deliver savings or efficiencies. These proposals in turn will aid in NHS Lothian achieving financial balance at the end of the 2016/17 financial year. The draft financial plan as at the 25 February 2016 highlighted that recovery plans totalling £62.5m had been proposed. However, almost 65% (£40.4m) have been rated as high risk proposals;
- Key budget holders did not sign off their budget allocation at the end of the 2015/16 financial planning cycle which could have reduced the ownership and accountability of managing the budget;
- The current draft financial recovery plans have a nominated lead; however metrics for measuring and monitoring the progress and achievement of these financial recovery actions have not yet been identified for all proposals, although this would be expected by the time the financial plan concludes.

Further details of these matters, and other less significant matters, are set out in the Management Action Plan.

Management Action Plan

Control objective 1: NHS Lothian has developed and implemented an effective financial planning process

In September 2015 the Finance and Resources Committee endorsed a revised financial planning process to be used in the development of the 2016/17 financial plan. The revised process requires individual business units and corporate areas to prepare financial plans which set out the actions required to breakeven at year end. The requirement for the annual delivery of Local Reinvestment Plans (LRPs) has been replaced with the requirement to develop financial recovery plans which will detail how the breakeven position will be achieved.

Guidance on the revised financial planning process was issued to key budget holders and finance staff in September 2015. A timetable was also created and communicated to all involved in the planning process which detailed deadlines for initial drafts, review and updates and incorporated the Scottish Government deadlines for submission.

The Business Partners and Management Accountants have been working with their allocated service areas to identify information for inclusion in their financial plans. This has ensured that there has been sufficient service engagement in the creation of the plans.

The Corporate Finance team have been monitoring the return of the individual business unit plans as they have been evolving and have been consolidating the information from these to create NHS Lothian's overall organisational financial plan. Regular updates have been provided to the Board Committees.

Control objective 2: Detailed financial plans are developed for all areas of the organisation with input from relevant department heads and budget holders as required	
2.1: 2015/16 budget allocations were not signed off by divisional managers and service managers	Important
<p>Observation and Risk:</p> <p>Key budget holders are required to sign off their budget allocation at the start of each financial year. In signing off the budget they are reinforcing their commitment to meet the budgetary management expectations that are detailed in the Standing Financial Instructions (SFIs).</p> <p>Finance monitors the return of budget agreements and spreadsheets are maintained by the team which show that the process was completed in 2013/14 and 2014/15. However, this process was not followed in 2015/16 as many budget holders did not feel that their budgets were achievable. As such, the Directors of Scheduled and Unscheduled Care signed off on the 2015/16 budgets instead.</p> <p>If key budget holders do not agree and sign off on their budget there is a risk that they may not take ownership of the allocation or management of the budget in line with the SFIs.</p>	
<p>Recommendation:</p> <p>The Director of Finance should ensure that key budget holders have been identified and that they are required to provide a signed acceptance of their budget allocation each financial year.</p> <p>Completion of the exercise should be reported to the relevant Board Committee with any exceptions noted and explained.</p>	
<p>Management Response:</p> <p>At the start of 2015/16 the Acute Division was undergoing a major reorganisation, with many key budget holders still to be appointed and were not in a position to fully understand and sign off their budgets. A compromise position was therefore agreed with responsibility for sign off being assumed by the Directors of Scheduled and Unscheduled Care.</p> <p>Management Action:</p> <p>Key Budget holders will be asked to sign off their Business Unit Financial Plans, including agreed Financial Recovery Actions to achieved financial balance, in line with the financial planning cycle. Progress in achieving full sign off and any material issues will be reported to the Finance and Resources Committee.</p>	
<p>Responsibility: Head of Management Accounting</p>	<p>Target date: 31st May 2016</p>

Control objective 3: Financial planning is consistent with the strategic plan, ensuring that adequate resources are in place to support the achievement of NHS Lothian's short, medium and long-term objectives

While the individual business unit financial plans do not specifically reference the NHS Lothian Strategic Plan or Corporate Objectives, the plans identify proposed service developments which have been assessed as either local or organisational priorities.

As the individual financial plans are required to demonstrate how financial balance is to be achieved across the year this has meant that the service development priorities have been reviewed and reprioritised as part of the planning process.

Inspection of the financial plans highlighted that the organisational priorities generally related to a business case which was linked to a strategic plan work stream. The developments have been prioritised as either essential or optional and cost pressures associated with the developments have been recorded.

We are currently undertaking an audit of Strategic Planning. This includes consideration of the mechanisms for monitoring achievement of the Strategic Objectives. To avoid duplication, we will report all findings concerning the links between the Strategic Plan and supporting documentation such as financial plans in that report.

Control objective 4: The financial planning process is linked to the development of savings plans and efficiency targets	
4.1: Financial recovery plans in the draft financial plan may not be viable	Significant
<p>Observation and Risk:</p> <p>Business units and corporate departments are currently developing financial recovery plans to eliminate the gap between income and projected expenditure in 2016/17. The recovery plans are risk assessed to indicate the likelihood of the plans being achieved, based on available information. The draft financial plan as at 25 February 2016 highlighted that recovery plans totalling £62.5m had been proposed. However, almost 65% (£40.4m) have been rated as high risk proposals as many are either potentially politically sensitive, or are reliant on the actions of third parties. Only 13% (£8.1m) of the proposed plans have a low risk rating and 22% (£13.9m) have been rated as medium risk.</p> <p>A Board presentation took place in March 2016 to ensure the Board were aware of the challenges NHS Lothian faces in producing a balanced financial plan for 2016/17. The Director of Finance is in discussion with the Scottish Government to seek agreement to take forward some of the high risk proposals. In addition, the Director of Finance is seeking additional funding from the Scottish Government to address the shortfall in the NRAC funding provision allocated to NHS Lothian.</p> <p>Where high risk recovery plans are included in the financial plan for 2016/17, which may not be viable, there is a risk that NHS Lothian will not be able to achieve financial balance at the end of the financial year. In the instance where the Scottish Government does not agree to the proposed high risk plans presented by NHS Lothian and further work is required to address the gap there is a risk that there may be a delay in producing the final financial plan to be approved by the Board and submitted to the Scottish Government by the end of May 2016.</p>	
<p>Recommendation:</p> <p>The final financial plan should only include achievable high risk recovery plans that have been agreed by the Scottish Government. Where the Scottish Government disputes the high risk plans being presented by NHS Lothian in their draft plan, NHS Lothian should re-assess the recovery plans across the organisation to try and identify further plans which are viable to help achieve financial balance for 2016/17.</p>	
<p>Management Response: The Financial Plan presented to the Board on the 6th April included £35.7m of Business Unit recovery plans. However recognising the challenges of delivery in previous years and a high level assessment of timing of delivery the Financial Plan now assumes a reduced value of £24.7m for 16/17. No high risk recovery actions are included in the Financial Plan at this stage.</p> <p>Management Action: A robust assessment of the recovery actions currently presented by each Business Unit will be undertaken to ensure they are deliverable within the timeframe required. In addition further recovery actions will be developed and implementation plans actioned as quickly as possible to close the gap in each Business Unit.</p>	
Responsibility: Business Partners & BU key budget holders	Target date: 30th April 2016

Control objective 4: The financial planning process is linked to the development of savings plans and efficiency targets	
4.2: Monitoring arrangements for delivery of recovery plans have not been identified for all plans.	Important
<p>Observation and Risk:</p> <p>The delivery of savings identified in the financial recovery plans should be measured and reported throughout the 2016/17 financial year. Many of the proposals do not currently detail how the success of a plan will be measured locally or how progress will be monitored and reported.</p> <p>The Board has to demonstrate a 3% efficiency gain during the year, however not all proposed efficiency plans will result in gains that are easily identified or measured. Finance is working closely with the relevant service managers for each of the financial recovery plans to establish measures that will result in meaningful information and evidence valid efficiency gains.</p> <p>Where the proposed recovery actions do not have success criteria defined it will be difficult to assess the viability of the proposal. In addition, without adequate monitoring and reporting arrangements there is a risk that service areas may not be able to provide assurance that they are on course to deliver financial balance. This may lead to under achieving plans not being identified on a timely basis to allow corrective action to be taken.</p>	
<p>Recommendation:</p> <p>Methods for measuring savings should be identified and documented with monitoring arrangements agreed for each financial recovery plan taken forward for the 2016/17 financial year.</p>	
<p>Management Response:</p> <p>Work is ongoing in the development of the revised financial planning and budget setting process and the next stage will include the monitoring of the recovery plans.</p> <p>Management Action:</p> <p>As part of the review mentioned in 4.1 above clear measurement and monitoring arrangements will be agreed for the large value plans. The monitoring process will be documented as part of the financial planning and budget setting procedure.</p>	
<p>Responsibility: Head of Management Accounting and Business Partners</p>	<p>Target date: 31st May 2016</p>

Control objective 5: Financial planning is completed and communicated on a timely basis	
5.1: Financial Operating Procedures are yet to be documented	Minor
<p>Observation and Risk:</p> <p>Guidance on the financial planning process for the development of the 2016/17 financial plans was communicated to key budget holders prior to the start of the financial planning process. The initial instructions and timelines were issued via email and further guidance was provided through discussions with the designated Business Partner and Finance.</p> <p>The instructions and guidance provided to staff have not yet been formalised into a Financial Operating Procedure which would ensure that those involved in the financial planning process were aware of their roles and responsibilities and also reduce the risk of any inconsistencies in developing the financial plans for the service areas.</p> <p>Inconsistencies were identified in the Data Diagnostic Review recently undertaken by Deloitte which involved a review of documentation relating to the existing Local Reinvestment Plans for 2015/16. Deloitte's findings included, amongst others, that plans were inconsistent in their level of detail, lacked adequate implementation plans, and did not always represent a good return on investment.</p> <p>Where Financial Operating Procedures have not been documented there is a risk that plans may be created inconsistently and that staff members do not have documented procedures to refer to.</p>	
<p>Recommendation:</p> <p>At the conclusion of the 2016/17 financial planning process a review of the process and timetable should be undertaken to assess the effectiveness of the revised process in developing and finalising the financial plans. Thereafter, a Financial Operating Procedure should be developed which includes detailed guidance on the minimum quality and nature of information to be included in financial recovery plans. The Financial Operating Procedure should be subject to the appropriate review and approval procedures.</p>	
<p>Management Response:</p> <p>It was recognised early on that the 2016/17 financial planning process would be an evolving one, and there would be a requirement to evaluate and document for future years. The changes were considered necessary to strengthen the link between business unit plans and delivery of financial balance.</p> <p>Management Action:</p> <p>The 2016/17 financial planning process will be reviewed and documented, recognising areas of required improvement for 2017/18.</p>	
<p>Responsibility: Head of Management Accounting</p>	<p>Target date: 30th June 2016</p>

Appendix 1 - Definition of Ratings

Management Action Ratings

Action Ratings	Definition
Critical	The issue has a material effect upon the wider organisation – 60 points
Significant	The issue is material for the subject under review – 20 points
Important	The issue is relevant for the subject under review – 10 points
Minor	This issue is a housekeeping point for the subject under review – 5 points

Control Objective Ratings

Action Ratings	Definition
Red	Fundamental absence or failure of controls requiring immediate attention (60 points and above)
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