

Midlothian Integration Joint Board

Year ended 31 March 2017

Annual Audit Report - draft

Audit and Risk Committee – 7 September 2017



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About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Midlothian Integration Joint Board (the IJB) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

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

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

Complaints

If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Russell Frith, Assistant Auditor General, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Purpose of this report

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as the external auditor of Midlothian Integration Joint Board (the IJB) for the five year period 2016/17 to 2020/21. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Auditing Practices Board; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Report is designed to summarise our key findings and conclusions from our audit work. It is addressed to both the members of the IJB and the Controller of Audit, and presented to both IJB management and those charged with governance, identified as being the IJB's Audit and Risk Committee. It will be published on Audit Scotland's website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the IJB. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

Scope and responsibilities

The Code sets out the responsibilities of both the IJB and the auditor. We provided details of these in our Annual Audit Plan, which was presented to the Audit and Risk Committee on 27 February 2017. We summarise the responsibilities of the IJB in Appendix A.

Our Annual Audit Plan also provided you with an overview of how we intended to carry out our responsibilities as your auditor. We carried out our audit in accordance with this plan.

We planned our procedures using a materiality of £1.8 million and a Tolerable Error of £0.9 million. We reassessed this using the actual year-end figures, to confirm that the materiality remained appropriate for the audit. No adjustment was made to materiality amounts communicated in our Annual Audit Plan. The threshold for reporting audit differences is £90,000.

Status of the audit and audit opinion

We have substantially completed our audit of the IJB's financial statements for the year ended 31 March 2017.

Subject to satisfactory completion of the following outstanding items we expect to issue an unqualified opinion on the IJB's financial statements. However until the following further work is complete, further amendments may arise:

- Ø review of the final version of the financial statements
- Ø completion of subsequent events review to the date of approval of the financial statements and receipt of signed management representation letter.

Key contacts

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Acknowledgement

We would like to thank all members of the IJB's management and staff who have been involved in our work for their co-operation and assistance during our audit work.

Accounting and audit matters – our reporting on the IJB's financial statements

Preparation of financial statements

- The unaudited financial statements were prepared to an acceptable standard. There are no adjusted or unadjusted audit differences arising from our audit.

Significant risks

- Our testing has not identified any material misstatements from revenue and expenditure recognition. Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the IJB's financial position based on manipulation of revenue or expenditure transactions.
- We have not identified any material weaknesses in the design and implementation of controls tested as part of our audit, or evidence of material management override through inappropriate judgements being applied.

Other matters and reporting requirements

- Our testing on opening balances was completed satisfactorily. We have no matters to bring to your attention in respect of our work on the qualitative aspects of the financial statements.
- We have concluded that the IJB has complied with the requirements of the Local Authority Accounts (Scotland) Regulations 2014.
- In respect of our 'Opinions on other prescribed matters', which includes the management commentary, the auditable part of the remuneration report, and the annual governance statement, we have concluded that our opinion is unqualified. We have not identified any other matters on which we are required to report by exception.

Wider scope audit dimensions – our judgements and conclusions on the IJB's arrangements

Financial sustainability – area of audit focus

- We have concluded that achieving financial sustainability continues to represent a significant challenge for the IJB. No similar risk sharing agreement is in place for 2017/18 and so the budget pressures being experienced need to be addressed to enable break-even to be achieved.
- Management have recognised the need to put in place longer term financial planning arrangements. The success of these is critical to supporting the achievement of the IJB's strategic objectives.

Governance and transparency – area of audit focus

- We have concluded that the IJB has established a sound basis to demonstrate good governance and transparency in its operational activity. A number of actions are highlighted in the Annual Governance Statement which have been delivered in year, but further areas for development have been recognised.
- In its role as the commissioning body, we believe the IJB needs to continue to consider what role it plays in governance in respect of when responsibility lies with the Board or where assurance should be obtained through the arrangements in place at its partners.

Financial management

- The IJB has established its core financial management arrangements, and we are satisfied that these are adequate for the current management of its financial activities.
- We have identified areas for action which reflect the need for the IJB to continue to develop its arrangements as activity matures.
- Those charged with governance, in conjunction with management, should ensure that the IJB has sufficient internal audit coverage to review the risks within the audit universe affecting the internal control environment on an appropriate timescale.

Value for Money

- In response to the need to measure performance and progress against the IJB's Strategic Plan, we have concluded that the IJB has identified local improvement goals to measure its performance which are appropriate to the stated national goals. In addition sources of data and information have been identified and reported to the Board.
- The IJB has prepared its Annual Performance Report for 2016/17. We will consider the findings of internal audit's review of performance reporting in 2017/18, including the robustness and accuracy of data gathering and reporting.

Appendices

We have confirmed our independence to act as auditors of the IJB. Auditor remuneration of £19,800 was agreed with management. Non non-audit services were provided.

We have made six recommendations for action by management, two of which are grade 1. All have been accepted by management.

1. Financial statements and accounting

1. Financial statements and accounting



The IJB's Annual Accounts enables the Board to demonstrate accountability for its resources and its performance in the use of those resources during the year. They are prepared in accordance with proper accounting practice, which is represented by the 2016/17 Code of Practice on Local Authority Accounting in the United Kingdom.

Audit opinion

In respect of the financial statements, we report on the truth and fairness in accordance with applicable law and the 2016/17 Code of Practice of the state of affairs of the IJB as at 31 March 2017 and of the surplus for the year then ended.

The detailed form and content of our audit report, plus the requirements underpinning the report, are contained in the Audit Scotland guidance at http://www.audit-scotland.gov.uk/uploads/docs/um/tgn_2017_5_local_authorities.pdf (Appendix 1).

We expect to issue an unqualified opinion based on the satisfactory completion of our work.

We have not identified any circumstances to notify the Controller of Audit that a statutory report may be required under the Local Government (Scotland) Act 1973.

Financial statements preparation

As part of your oversight of the Board's financial reporting process, we report on our consideration of the quality of working papers and supporting documentation prepared predominantly by the finance team to support the audit.

The nature of the IJB transactional activity during the year means that the production of the financial statements should not be a particularly onerous activity at this stage. Equally this was the first year in which the IJB was reporting on its activity and performance for the year.

We made no substantive comments on the core financial statements, although there were a number of matters where for example, prior year comparative information had not been correctly presented.

We made more substantive comments on the form and content of both the management commentary and the annual governance statement. Management have updated the narrative information to take account of our comments.

Materiality

We planned our procedures using a materiality of £1.8 million. We reassessed this using the actual year-end figures, to ensure that our level of materiality remained appropriate. We did not change our assessment of materiality as a result of this reassessment. Our Tolerable Error for the audit was £0.9 million and the threshold for reporting audit differences is £90,000.

We also identified areas where misstatement at a lower level than materiality might influence the reader and developed a specific audit strategy for them. They include:

- Remuneration disclosures including any severance payments, exit packages and termination benefits - we applied a materiality of £1,000 based on the potential sensitivity of these disclosures.
- Related party transactions - we considered the nature of these disclosures individually.

Audit differences

There are no unadjusted or adjusted audit differences arising from our audit.

Financial statements – our overall conclusions

- Our audit work is complete subject to final approval of the financial statements, receipt of management representation letter and update of subsequent events. We expect to issue an unqualified opinion on the IJB's financial statements.
- We undertook our audit in accordance with the materiality outlined to the Audit and Risk Committee in our Annual Audit Plan.
- The unaudited financial statements were prepared to an acceptable standard. There are no adjusted or unadjusted audit differences arising from our audit.

Our Audit Plan identified key areas of focus for our audit of the IJB's financial statements, including significant risks. This report sets out the results of our audit procedures plus any relevant observations, including our views on areas which might be conservative, and where there may be potential risk and/or exposure.

Significant risk – risk of fraud in revenue recognition

What is the risk?

Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

Given the nature of funding for the IJB, we rebutted the risk of improper recognition of revenue in respect of core funding from Midlothian Council and NHS Lothian. However, we considered the risk of improper recognition of the expenditure incurred by the IJB and how it accounted for this.

Results of audit procedures

We undertook the following procedures as part of our audit.

- ▶ Reviewed and tested revenue and expenditure recognition policies.
- ▶ Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias.
- ▶ Developed a testing strategy in respect of material revenue and expenditure streams.
- ▶ Reviewed and tested revenue cut-off around the year end.

The LASAAC-TAG Guidance concluded that IJBs would be acting as principal in their own right. This conclusion lead to the guidance that contributions to IJB funding should be treated as a distinct and separate transaction from the commissioning income received.

In line with the guidance, the IJB has identified partner funding contributions as un-hypothecated funding and hence presented them as 'Taxation and non-specific grant income and expenditure'. This included the 'set aside' element for large hospital services on the basis that the utilisation of the underlying resources is within the remit of the IJB's commissioning decision.

In accordance with the Integration Scheme, the IJB gave directions to both Midlothian Council and NHS Lothian. At a Board meeting in August 2016, the IJB agreed the final risk sharing model with its two partners which effectively ensured that any overspends within the directions provided would be covered by the partners on overall terms.

At the financial year end, confirmation was obtained from both Midlothian Council and NHS Lothian confirming the expenditure incurred during the year in respect of the directions provided to them by the IJB. We have agreed the figures from these confirmations to the financial statements. We have reviewed the minutes and papers of meetings held after the year end to ensure that financial information presented to the Board is in line with the unaudited financial statements provided for audit.

As the confirmations from the other organisations account for all of the spend in relation to the directions, management at the IJB do not prepare any accounting estimates in respect of income or expenditure at the year end.

Revenue recognition – what have we concluded?

- Our testing has not identified any material misstatements from revenue and expenditure recognition.
- Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the IJB's financial position based on manipulation of revenue or expenditure transactions.

2. Financial statements and accounting



Our Audit Plan identified other aspects of our work which arise either in accordance with International Standards on Auditing (UK & Ireland) or in accordance with the Code. These are set out below.

Significant risk – management override

What is the risk?

As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

Results of audit procedures

1. Test the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements

We obtained all journals posted by management to record the transactions of the IJB, which are hosted on the Midlothian Council financial ledger. All of the journals for the IJB's transactions were posted at the year end and we reviewed all of these in the course of our work.

Action plan point 1

2. Review accounting estimates for evidence of management bias, including management's retrospective consideration of prior year estimates

There are no material accounting estimates included in the financial statements. We confirmed the process for ensuring that there were no claims applicable to the IJB which required provision to be made as part of its participation in CNORIS (Clinical Negligence & Other Risks Indemnity Scheme).

3. Evaluate the business rationale for any significant unusual transactions

We did not identify any significant unusual transactions.

Other audit matters

Opening balances

International Standard on Auditing (UK and Ireland) 510: *Initial audit engagements – opening balances* requires auditors to obtain sufficient, appropriate audit evidence that opening balances do not contain misstatements that materially affect the financial statements. The standard also requires auditors to verify that appropriate accounting policies are reflected in the opening balances and that they have been consistently applied in the current period's financial statements.

Based on 2016/17 being the first year of operation of the IJB, the prior year financial statements did not contain any material balances to bring forward as opening balances.

Qualitative aspects of the financial statements

We have reviewed the significant accounting policies, which are disclosed in the annual accounts, and we consider these to be appropriate to the IJB.

There was no disagreement during the course of the audit over any accounting treatment or disclosure.

There were no significant difficulties encountered in the audit.

Management override / other audit matters – what have we concluded?

- We have not identified any material weaknesses in the design and implementation of controls tested as part of our audit, or evidence of material management override through inappropriate judgements being applied.
- Our testing on opening balances was completed satisfactorily. We have no matters to bring to your attention in respect of our work on the qualitative aspects of the financial statements.

2. Financial statements and accounting

The Local Authority Accounts (Scotland) Regulations 2014 set out the statements which should be included in the Annual Report and Accounts in addition to the financial statements. These items are covered by our independent auditor's report as *Other prescribed matters*, in accordance with the Audit Scotland requirements under the Code.

Other reporting requirements

The Local Authority Accounts (Scotland) Regulations 2014 (the Regulations)

Regulations 8 to 10 set out the statutory requirements in respect to the financial statements, their availability for public inspection and the consideration and signing by the IJB or a committee with an audit or governance remit.

As required, we received the unaudited Annual Accounts by the 30 June deadline. The full Integration Joint Board itself considered the unaudited Annual Accounts on 15 June 2017, in advance of the 31 August deadline. No statutory objections were received on the unaudited financial statements.

Management Commentary

The requirement for the IJB to include a management commentary is included in Regulation 8(2)(a). Audit Scotland requires us to read the information in the management commentary and express an opinion on whether the:

- ▶ information given in the management commentary is consistent with the financial statements and whether it has been prepared in accordance with the statutory guidance.

Guidance on the content of the management commentary was issued by the Scottish Government within Local Government Finance Circular 5/2015, while Part 2 of the Circular provides statutory guidance on the specific requirements. These have been interpreted for the circumstances for the IJB.

The management commentary was primarily focused on the financial performance of the IJB during the year. We suggested amendments to aid the clarity of presentation and to report on the link between financial and non-financial performance. Management took on board these comments and made changes to the audited financial statements.

Remuneration Report

Auditors are required by the Code to audit the disclosures of remuneration and pension benefit, pay bands, and exit packages and express a separate opinion within their independent auditor's report on whether they have been properly prepared in accordance with the Regulations.

The IJB disclosed the full voting membership of the IJB during the year. We considered this good practice. In line with the Additional Guidance on Accounting for Integration of Health and Social Care issued by LASAAC in March 2017, the Chair and Vice-Chair of the IJB were treated equivalently as senior councillors and included in the remuneration report.

Only the Chief Officer was included in the remuneration report disclosures presented for audit, with narrative explaining that the Chief Officer post is considered only 50% of the duties of the individual as they also have operational duties for Midlothian Council and NHS Lothian. Following discussion with management, information in respect of the Chief Finance Officer was included on the basis of transparency and good practice. We agree with this approach. No other amendments were required to the draft remuneration report to ensure its consistency with underlying records and presentation in accordance with the statutory requirements.

Annual Governance Statement (AGS)

Audit Scotland requires us to read the information in the annual governance statement and express an opinion on whether the information given in the annual governance statements is consistent with the financial statements and whether the statement has been prepared in accordance with *Delivering good governance in local government: framework 2016*.

We set out the work undertaken in respect of the IJB's annual governance statement as part of the Wider Scope – Governance and Transparency section of this Report. As a result, we required changes to the draft Annual Governance Statement to be made by management.

Other reporting requirements – what have we concluded?

- We have concluded that the IJB has complied with the requirements of the Local Authority Accounts (Scotland) Regulations 2014.
- In respect of our 'Opinions on other prescribed matters', which includes the management commentary, the auditable part of the remuneration report, and the annual governance statement, our opinion is unqualified.
- We have not identified any other matters on which we are required to report by exception.

2. Wider scope audit

3. Wider scope audit

In accordance with the Code, conclusions and judgements formed in respect of the four audit dimensions - financial management; financial sustainability; governance and transparency; value for money - which frame the wider scope of public sector audit contribute to the overall assessment and assurance on Best Value.

Wider scope audit risks

The Code requires us to undertake work in respect of each of the four dimensions on an annual basis. The Code also sets out an expectation that 'significant' risks identified through our planning process that relate to the wider scope dimensions will be communicated with you. In undertaking our risk assessment in respect of the wider scope audit areas, we distinguish between the definition of 'significant risks' which apply to the audit of the financial statements, by referring to 'Wider Scope Audit Focus Areas'.

In our Annual Audit Plan we identified two audit focus areas, one in respect of financial sustainability and one in respect of governance and transparency.

Financial management

The Public Bodies (Joint Working) (Scotland) Act 2014 includes an obligation on the Board to appoint a proper officer under section 95 of the Act (CFO). The section 95 officer is responsible for ensuring that appropriate financial services are available to the Board and Chief Officer. The CFO is employed by NHS Lothian and also holds the post of CFO at East Lothian Integration Joint Board. Financial regulations have been established for the IJB.

We are satisfied therefore that the Board has made arrangements for the proper administration of its financial affairs.

The IJB budget was under pressure at all points during the year. In August 2016, a risk sharing assurance model was provided to the Board whereby the budget pressures would be met by the funders. The table below summaries the outturn expenditure for the year. In total, additional funding of £5.42 million (4.2%) was required to meet the financial pressures faced in year.

Funding aspect	Original Budget £m	Additional in-year budget £m	Additional non-recurring support £m	Outturn expenditure £m
Midlothian Council	37.09	0.41	0.74	38.24
NHS Lothian (includes £3.59m social care fund)	82.28	4.41	0.86	87.55
Sub-total IJB	119.37	4.82	1.60	125.79
NHS Lothian - non-cash limited*	8.70	-	-	8.70
TOTAL - IJB	128.07	4.82	1.60	134.49

* non-cash limited budgets are met by the Scottish Government and do not strictly have a budget set by the IJB, but they do represent delegated functions

Financial reporting

The 2016/17 budget was not finalised until the first quarter of the financial year, as a final funding offer and acceptable financial assurance arrangement was not reached with NHS Lothian until Summer 2016. Regular reports were prepared and considered by the IJB during the year, from both the Chief Officer and the Chief Finance Officer, which outlined both operational and financial pressures facing the IJB. There was evidence of outturn forecasting being undertaken, and action to address the financial pressures so that the year-end outturn position was better than forecast by both Midlothian Council and NHS Lothian at quarter three.

We would note that on certain occasions during the year, the finance report was included as a 'To-follow' item on the agenda, but was not subsequently added to the public agenda papers.

Action point 2

3. Wider scope audit

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

Financial management (continued)

Monitoring of expenditure

In line with the Integration Scheme, the IJB issued directions to both Midlothian Council and NHS Lothian in respect of the services and activities it was commissioning from them. These directions had associated funding available with them, in an analogous way to setting a budget for the delegated functions of the IJB.

In discussion with management, it was recognised that the financial pressures facing the IJB and its partners resulted in the financial risk sharing model to account for the overspends which were anticipated in aggregate.

The Integration Scheme sets out the process to be followed for managing both over and underspends. This process was followed for overspends in 2016/17. In respect of underspends, the Integration Scheme allows that these are retained by the IJB as reserves where they relate to a direction given by the IJB.

As the IJB matures, and uses its directions to determine where services activity will be prioritised going forward, it is important that financial monitoring is developed such that there is clear incentive to obtain the performance outcomes required for each directed element within the funding identified and made available by the IJB. Further, should underspends arise, in line with good budget monitoring practice, the IJB should determine whether to carry these forward as reserves for future activity or to be reallocated to meet other in-year financial pressures.

Action point 3

Internal control and internal audit

The IJB draws on internal audit support through Midlothian Council and NHS Lothian, with the Council's Chief Internal Auditor acting in this role for the IJB. Internal audit work in the year was focussed on financial assurance, governance and follow-up of prior year recommendations. Additional audits within the 2016/17 plan are still to be reported in respect of Monitoring of Performance and Directions to the NHS and Midlothian Council and Performance Reporting.

On the basis of the work performed, internal audit's opinion for the year was that:

- ▶ the IJB has taken steps to develop a framework of governance, risk management and control in 2016/17 and that these will be further developed in 2017/18.
- ▶ overall, the IJB's framework of governance, risk management and control is adequate. Work however needs to be continued in 2017/18 to further develop the governance arrangements through the development of performance reports, workforce plans and improved financial planning.

In setting the internal audit plan for 2017/18, and considering a three year cycle for the audit universe, internal audit highlighted that they had sufficient resource to focus only on high risk areas. It is important that those charged with governance of the IJB, in conjunction with management, ensure that there is appropriate internal audit resource, linked to other sources of assurance, to provide an appropriate review of the effectiveness of internal control to be reported on annually, as required by regulations.

Action point 4

Financial management - what have we concluded?

- The IJB has established its core financial management arrangements, and we are satisfied that these are adequate for the current management of its financial activities. We have identified areas for action which reflect the need for the IJB to continue to develop its arrangements as activity matures.
- Those charged with governance, in conjunction with management, should ensure that the IJB has sufficient internal audit coverage to review the risks within the audit universe affecting the internal control environment on an appropriate timescale.

3. Wider scope audit

In accordance with the Code, conclusions and judgements formed in respect of the four audit dimensions - financial management; financial sustainability; governance and transparency; value for money - which frame the wider scope of public sector audit contribute to the overall assessment and assurance on Best Value.

Financial sustainability

Financial sustainability interprets auditors' requirements under ISA 570 *Going concern* and looks forward to the medium (two to five years) and longer term (longer than five years) to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

We identified in our Annual Audit Plan that achieving a balanced budget for the IJB in 2016/17 required a focus on actions to control expenditure as well as early approval that integration funding would be used as part of the mechanism to provide the IJB with the resources to meet expenditure.

It was also clear that moving into 2017/18 and beyond, delivering on the IJB's strategic priorities would, however, require an ability to transform and deliver significant recurring efficiency savings, while at the same time ensuring that core delivery is not affected.

We therefore identified financial sustainability as a wider scope audit focus area.

Wider scope audit focus area – financial sustainability audit procedures

What did we do?	What did we find?
<p>We considered whether:</p> <ul style="list-style-type: none"> ▶ financial balance has or will be achieved? ▶ have any short-term financial challenges been identified and addressed through a financial recovery plan? ▶ How appropriate are the arrangements put in place to address any identified funding gaps? 	<p>Financial balance was achieved in 2016/17 but only through adoption of the risk sharing model which saw additional budget provision made in year of £4.82 million and a further £1.6 million in total from both partners as non-recurring support to balance the year-end outturn.</p> <p>In 2017/18, the budget already recognised that the financial pressures faced in 2016/17 would continue to be challenging. A budget of £123.87 million has been proposed from the IJB's funding partners, representing an increase in funding from the original 2016/17 budget of £4.22 million. However with the actual outturn in 2016/17 at £125.79 million, excluding non-cash limited expenditure, and additional funding pressures identified for 2017/18, this is a substantial budget gap.</p> <p>It is acknowledged that a similar risk sharing model is not appropriate in 2017/18 and so an increased focus on monitoring the budgets and addressing pressures will be required at the IJB level as it requires to break-even.</p> <p>Financial pressures of £4.85 million were identified when the budget was approved and at that time, plans were available to address £2.80 million of these with a £2.05 million still to be met. Continued focus is required to manage these budget pressures in year.</p>
<ul style="list-style-type: none"> ▶ Has a reserves strategy been put in place and how does the current level of reserves match that strategy? 	<p>During 2016/17 the IJB approved a reserves strategy, in recognition of this being one element of best practice in establishing the longer term financial planning process for the IJB.</p> <p>The reserves strategy approved a level of 2% of net expenditure, equating to approximately £1 million.</p> <p>It is noted that currently no reserves are held and it is not anticipated that this will change at 31 March 2018.</p>

Action point 5

Financial sustainability (continued)

Wider scope audit focus area – financial sustainability audit procedures

What did we do?	What did we find?
<ul style="list-style-type: none"> Does the body understand the long-term pressures, including demand pressures, and have these been built into plans and strategies? 	<p>The IJB has identified the longer term changes in demographics which will impact on the delivery of its services. In discussion with management, it is clear that there is a full understanding of these challenges and how integration through transformation is essential to bring the greater focus on prevention than intervention in order to manage the long term pressures.</p> <p>At its meeting in April 2017, the Chief Finance Officer presented a report which quantified the identified financial pressures up until 2020/21, although it was acknowledged that further work was required to identify the longer term impact of population change on the activities of the IJB.</p>
<ul style="list-style-type: none"> How effective are the financial planning systems in identifying and addressing risks to financial sustainability across the shorter and longer terms? 	<p>Through 2016/17 the IJB set out a transitional approach to financial planning. The 2016/17 budget was essentially set by its partners separately and then presented to the IJB. In respect of 2017/18, with the IJB fully operational this process is considered by management to have become more tripartite.</p> <p>Key actions identified for 2017/18 include a review of the NHS Lothian 'fair-share' model for identification and allocation of resources that are delivered across the Lothian region. This was considered to be an appropriate initial model but more accurate information is now required on actual use of delegated resources and the amount included in the IJB's budget through the existing share model.</p> <p>The financial planning approach model identifies that for 2018/19, the IJB should become the lead in the budget setting process, consulting with its partners on its requirements. In this way, the financial planning will change from the IJB being involved primarily in identifying recovery actions to meet budget pressures to moving to setting the priorities for use of resources.</p> <p>Based on this a multi-year financial plan will be developed to support the IJB and its partners in prioritising resources and service provision over the medium term.</p> <p style="text-align: right;">Action plan point 5</p>

Financial sustainability – what have we concluded?

- We have concluded that achieving financial sustainability continues to represent a significant challenge for the IJB. No similar risk sharing agreement is in place for 2017/18 and so the budget pressures being experienced need to be addressed to enable break-even to be achieved.
- Management have recognised the need to put in place longer term financial planning arrangements. The success of these is critical to supporting the achievement of the IJB's strategic objectives.

3. Wider scope audit

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

Governance and transparency

The Board and officers of the IJB are responsible for establishing robust governance arrangements. This includes ensuring effective systems of internal control, including arrangements to safeguard public money, and compliance with applicable laws and regulations.

With this being the first year of full operation of the IJB, it is important that appropriate governance arrangements are established from the outset, to support delivery of strategic objectives and transparent scrutiny of the IJB's performance.

We therefore identified governance and transparency as a wider scope audit focus area.

Wider scope audit focus area – governance and transparency audit procedures

What did we do?	What did we find?
We considered whether:	The IJB has in place a number of the key requirements for good governance:
<ul style="list-style-type: none"> ▶ The IJB can demonstrate that the governance arrangements are appropriate and operating effectively. ▶ Is there effective scrutiny, challenge and transparency on decision making and financial and performance reports? ▶ Is the governance framework sound and are the governance arrangements effective? ▶ Is the Governance Assurance Statement complete and does it reflect key findings from audit, scrutiny and inspection? ▶ Is appropriate and effective leadership in place? 	<p>We have reviewed Board minutes and papers and found these to set out clearly the matters considered and discussed. Standing Orders regulate how the business of the IJB is conducted. The Audit and Risk Committee was established with clearly defined terms of reference.</p> <p>Pending finalisation of arrangements for a Code of Conduct for Members, the Board adopted an interim Code based on the existing Model Code for Members of Devolved Public Bodies in Scotland, and members have registered their interests according to that Code. The Scottish Government approved the IJB's code of conduct on 1 June 2016.</p> <p>Internal audit's opinion for the year was that the Board had taken steps to develop a framework of governance, risk management and control in 2016/17 and that these will be further developed in 2017/18. Overall, the IJB's framework of governance, risk management and control was considered adequate.</p> <p>We reviewed the Annual Governance Statement within the financial statements against the required guidance. We were satisfied that it met the requirements and was consistent with both the governance framework and key findings from relevant audit activity.</p> <p>We suggested a number of changes to the form and structure which management took on board and made appropriate revisions. In particular, in respect of certain matters noted as in development, we suggested that it was important for their to be clarity where responsibility was the role of the IJB, or one or other of its partners.</p> <p style="text-align: right;">Action plan point 6</p> <p>The Board appointed a Chief Officer and a Chief Finance Officer as required by the legislation. A Chief Internal Auditor has been appointed to carry out the Board's internal audit requirements and assist its Audit & Risk Committee.</p> <p>Subsequent to the year-end, the Chief Officer indicated her intention to retire and the Board has progressed to recruit her replacement, who will take up full duties at the start of October 2017.</p>

Governance and transparency – what have we concluded?

- We have concluded that the IJB has established a sound basis to demonstrate good governance and transparency in its operational activity. A number of actions are highlighted in the Annual Governance Statement which have been delivered in year, but further areas for development have been recognised.
- In its role as the commissioning body, we believe the IJB needs to continue to consider what role it plays in governance in respect of when responsibility lies with the Board or where assurance should be obtained through the arrangements in place at its partners.

3. Wider scope audit

Value for money is concerned with using resources effectively and continually improving services. This includes consideration of whether resources are being used effectively; services are improving and the IJB has appropriate arrangements to demonstrate Best Value.

Value for money

Monitoring of performance and achievement of better outcomes for the resources available is key to the demonstration of value for money. The Ministerial Strategic Group for Health and Community Care agreed that in 2017/18 progress by IJBs will be tracked across the following:

- (1) Unplanned admissions
- (2) Occupied bed days for unscheduled care
- (3) A&E performance
- (4) Delayed discharges
- (5) End of life care
- (6) The balance of spend across institutional and community services.

In response the IJB considered and agreed nine local improvement goals that would be appropriate to measure the IJB's performance in respect of these areas:

- ▶ Reduce unscheduled admissions by 5% by September 2018
- ▶ Reduce unscheduled hospital occupied bed days by 10% by April 2019
- ▶ Reduce the number of patients arriving by ambulance to A&E who are subsequently discharged home
- ▶ By April 2018 over 87% of patients who are subsequently admitted into hospital from A&E are within the 4 hour standard
- ▶ Maintain the current number of patients using A&E (ongoing)
- ▶ Reduce delayed discharge occupied bed days by 30% by April 2018
- ▶ No patients in the RIE or WGH with a delayed discharge over 72 hours by April 2018
- ▶ Reduce by 10% by April 2018 the number of Occupied Bed Days in the Royal Infirmary Edinburgh / Western General Hospital during the last six months of life
- ▶ Reduce the percentage of patients over 75 who are in a larger hospital from 1.9% to 1.6% and in a care home from 6.8% by a date, still to be agreed.

In setting these improvement goals, management have set out the available data and information available to enable monitoring of performance against these improvement goals and provided the IJB with performance reports during 2017/18 on how the IJB is performing against these measures.

Integration Joint Boards are required under the legislation to prepare an annual performance report by 31 July. The IJB has considered its draft report at its meeting on 24 August 2017, which sets out how the IJB performed during the year, in particular in making progress against its Strategic Plan 2016-2020. Internal audit are due to look at the performance reporting within the IJB as part of their work and we will review and consider the findings of this work as part of our audit work in 2017/18.

The Care Inspectorate undertook both scheduled and unscheduled inspections across a range of IJB services during 2016/17. The overall quality of care as assessed as good or better in 19 out of 27 services for the reporting period. Four community-based services were rated adequate or lower as were three Care Homes. Overall, 85% of care services graded 'good' (4) or better in Care Inspectorate inspections (Scottish rate 83%).

Value for Money – What have we concluded?

- In response to the need to measure performance and progress against the IJB's Strategic Plan, we have concluded that the IJB has identified local improvement goals to measure its performance which are appropriate to the stated national goals. In addition sources of data and information have been identified and reported to the Board.
- The IJB has prepared its Annual Performance Report for 2016/17. We will consider the findings of internal audit's review of performance reporting in 2017/18, including the robustness and accuracy of data gathering and reporting.

Appendices

- A. IJB Responsibilities**
- B. Required communications with the Audit and Risk Committee**
- C. Auditor independence**
- D. Management representations**
- E. Action plan**

A. The IJB's responsibilities



The Code of Audit Practice (the Code) summarises the responsibilities on all audited bodies falling within the public sector audit framework. We summarise these on this page.

Responsibilities of audited bodies

Corporate governance	Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including Audit and Risk Committees or equivalent) in monitoring these arrangements.
Financial statements and related reports	<p>Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:</p> <ul style="list-style-type: none"> • preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. • maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures. • ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority. • maintaining proper accounting records. • preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body. <p>Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.</p> <p>Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.</p>
Standards of conduct / prevention and detection of fraud and error	Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.
Financial position	<p>Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> • such financial monitoring and reporting arrangements as may be specified • compliance with any statutory financial requirements and achievement of financial targets • balances and reserves, including strategies about levels and their future use • how they plan to deal with uncertainty in the medium and longer term • the impact of planned future policies and foreseeable developments on their financial position.
Best Value	<p>Local authority bodies have a statutory duty, under the Local Government (Scotland) Act 1973 and associated statutory guidance, to make arrangements to secure best value through the continuous improvement in the performance of their functions.</p> <p>Specified audited bodies also have to prepare and publish performance information in accordance with directions issued by the Accounts Commission.</p>

B. Required communications



There are certain additional communications that we must provide to the Audit and Risk Committee, which are set out below.

Required communication - what is reported?	Our reporting to you
Terms of engagement Confirmation by the Audit and Risk Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice
Planning and audit approach Communication of the planned scope and timing of the audit, including any limitations.	Annual Audit Plan – 9 March 2017
Significant findings from the audit <ul style="list-style-type: none"> • Our view of the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures • Any significant difficulties encountered during the audit • Any significant matters arising from the audit that were discussed with management • Written representations we have requested • Expected modifications to the audit report • Any other matters significant to overseeing the financial reporting process • Findings and issues around the opening balance on initial audits 	This Annual Audit Report – 7 September 2017
Going concern Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: <ul style="list-style-type: none"> • Whether the events or conditions constitute a material uncertainty • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements • The adequacy of related disclosures in the financial statements 	No conditions or events were identified, either individually or together to raise any doubt about the IJB's ability to continue for the 12 months from the date of our report.
Misstatements <ul style="list-style-type: none"> • Uncorrected misstatements and their effect on our audit opinion • The effect of uncorrected misstatements related to prior periods • A request that any uncorrected misstatement be corrected • Significant corrected misstatements, in writing 	This Annual Audit Report – 7 September 2017
Fraud <ul style="list-style-type: none"> • Asking the Audit and Risk Committee whether they have knowledge of any actual, suspected or alleged fraud affecting the IJB • Unless all those charged with governance are involved in managing the entity, any fraud identified or information obtained indicating that a fraud may exist involving: <ul style="list-style-type: none"> (a) management; (b) employees with significant roles in internal control; or (c) others where the fraud results in a material misstatement in the financial statements. ▶ A discussion of any other matters related to fraud, relevant to Audit and Risk Committee responsibility. 	This Annual Audit Report – 7 September 2017

Required communication - What is reported?	Our reporting to you
<p>Significant deficiencies in internal controls identified during the audit</p> <ul style="list-style-type: none"> Significant deficiencies in internal controls identified during the audit. 	<p>This Annual Audit Report – 7 September 2017.</p> <p>No significant deficiencies were identified in the course of our audit which required immediate communication to the Audit and Risk Committee.</p>
<p>Related parties</p> <p>Significant matters arising during the audit in connection with the IJB's related parties including, where applicable:</p> <ul style="list-style-type: none"> Non-disclosure by management Inappropriate authorisation and approval of transactions Disagreement over disclosures Non-compliance with laws and/or regulations Difficulty in identifying the party that ultimately controls the entity 	<p>We have no matters to report.</p>
<p>Subsequent events</p> <ul style="list-style-type: none"> Where appropriate, asking the Audit and Risk Committee whether any subsequent events have occurred that might affect the financial statements. 	<p>We have asked management and those charged with governance. We have no matters to report.</p>
<p>Other information</p> <ul style="list-style-type: none"> Where material inconsistencies are identified in other information included in the document containing the financial statements, but management refuses to make the revision. 	<p>We have no matters to report.</p>
<p>External confirmations</p> <ul style="list-style-type: none"> Management's refusal for us to request confirmations We were unable to obtain relevant and reliable audit evidence from other procedures. 	<p>We have received all requested confirmations.</p>
<p>Consideration of laws and / or regulations</p> <ul style="list-style-type: none"> Audit findings of non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on "tipping off" Asking the Audit and Risk Committee about possible instances of non-compliance with laws and/or regulations that may have a material effect on the financial statements, and known to the Audit and Risk Committee. 	<p>We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations.</p>
<p>Independence</p> <ul style="list-style-type: none"> Communication of all significant facts and matters that have a bearing on EY's objectivity and independence. 	<p>This Annual Audit Report – 7 September 2017, Appendix C</p>

Professional ethical standards, and the Terms of our Appointment, require us to communicate all significant facts and matters that have a bearing on EY's objectivity and independence as auditor of the IJB.

What we are required to communicate?

Communicating key elements of the audit engagement partner's consideration of independence and objectivity such as:

- ▶ The principal threats
- ▶ Safeguards adopted and their effectiveness
- ▶ An overall assessment of threats and safeguards
- ▶ Information on the firm's general policies and processes for maintaining objectivity and independence
- ▶ Communications whenever significant judgments are made about threats to objectivity or independence and the appropriateness of safeguards.

Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan dated 9 March 2017.

We complied with the APB Ethical Standards and the requirements of Audit Scotland's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that you and your Audit and Risk Committee consider the facts known to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the Audit and Risk Committee on 7 September 2017.

Summary of fees

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31 March 2017.	Agreed fee per Annual Audit Plan	n/a
	Auditor remuneration	£19,800
We confirm that we have not undertaken non-audit work outside the Code requirements.	Fixed costs *	£5,540
	Non-audit fees	-
Our audit fee was not agreed with management at the time of our Audit Plan. Fees now agreed are shown in the table opposite.	Total audit fees	£25,340

* Fixed costs, which are determined by Audit Scotland, comprise £1,040 pooled costs, £3,790 contribution to Audit Scotland's Performance Audit and Best Value and £710 contribution to Audit Scotland costs

ISA (UK and Ireland) 580.10 requires the auditor to obtain written representation that management, including those charged with governance, has fulfilled its responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant, their fair presentation.

Ernst & Young LLP
Ten George Street
Edinburgh EH2 2DZ
[Date]

This letter of representations is provided in connection with your audit of the financial statements of Midlothian Integration Joint Board ("the IJB") for the year ended 31 March 2017. We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the financial statements give a true and fair view of the IJB financial position of Midlothian Integration Joint Board as of 31 March 2017 and of its income and expenditure for the year then ended in accordance with CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.

We understand that the purpose of your audit of our financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK and Ireland), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose - all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

A. Financial Statements and Financial Records

1. We have fulfilled our responsibilities, under the relevant statutory authorities, for the preparation of the financial statements in accordance with the Local Authority Accounts (Scotland) Regulations 2014, Section 12 of the Local Government in Scotland Act 2003 and CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.
2. We acknowledge, as members of management of the IJB, our responsibility for the fair presentation of the financial statements. We believe the financial statements referred to above give a true and fair view of the financial position, financial performance (or results of operations) and cash flows of the IJB in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17. We have approved the financial statements.
3. The significant accounting policies adopted in the preparation of the financial statements are appropriately described in the financial statements.
4. As members of management of the IJB, we believe that the IJB has a system of internal controls adequate to enable the preparation of accurate financial statements

in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17, that are free from material misstatement, whether due to fraud or error.

5. There are no unadjusted audit differences identified during the current audit and pertaining to the latest period presented.

B. Fraud

1. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.
2. We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
3. We have no knowledge of any fraud or suspected fraud involving management or other employees who have a significant role in the IJB's internal controls over financial reporting. In addition, we have no knowledge of any fraud or suspected fraud involving other employees in which the fraud could have a material effect on the financial statements. We have no knowledge of any allegations of financial improprieties, including fraud or suspected fraud, (regardless of the source or form and including without limitation, any allegations by "whistleblowers") which could result in a misstatement of the financial statements or otherwise affect the financial reporting of the IJB.

C. Compliance with Laws and Regulations

1. We have disclosed to you all identified or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.

D. Information Provided and Completeness of Information and Transactions

1. We have provided you with:
 - Access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - Additional information that you have requested from us for the purpose of the audit; and
 - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

D. Information Provided and Completeness of Information and Transactions (continued)

2. All material transactions have been recorded in the accounting records and are reflected in the financial statements.
3. We have made available to you all minutes of the meetings of the IJB and audit and risk committee (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the year to the most recent meeting on the following dates: 14 September 2017 for the IJB and 7 September 2017 for the audit and risk committee.
4. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the IJB's related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the period ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the financial statements.
5. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.
6. We have disclosed to you, and the IJB has complied with, all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

E. Liabilities and Contingencies

1. All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the financial statements.
2. We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.
3. We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed in the financial statements all guarantees that we have given to third parties.
4. No other claims in connection with litigation have been or are expected to be received.

F. Subsequent Events

1. As disclosed in the financial statements, there have been no events subsequent to period end which require

adjustment of or disclosure in the financial statements or notes thereto.

G. Other information

1. We acknowledge our responsibility for the preparation of the other information. The other information comprises the Management Commentary, the Remuneration Report, the Annual Governance Statement and the Statement of Responsibilities.
2. The disclosures within the Management Commentary reflects our understanding of the financial and non-financial performance of the IJB over the reporting year, is consistent with the financial statements and has been prepared in accordance with relevant guidance.
3. The information given in the Annual Governance Statement for the financial year for which the financial statements are prepared reflects the IJB's governance framework, is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016).
4. The information contained in the auditable part of the Remuneration Report has been prepared in accordance with The Local Authority Accounts (Scotland) Regulations 2014.
5. We confirm that the content contained within the other information is consistent with the financial statements.

Yours faithfully,

Chief Finance Officer

Chief Officer

Chair of the IJB

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Board or management to action.

Classification of recommendations

Grade 1: Important weaknesses and/or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.

Grade 2: Weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.

Grade 3: Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.

No.	Findings and risk	Our recommendation and grading	Management's response
1	<p>Journal processing</p> <p>All journal processing for the IJB was undertaken at the year end.</p> <p>There is a risk that the financial records of the IJB during the year exist only in a range of reports arising from end user analysis and production.</p>	<p>It would be good practice to reflect the initial budget allocation of income as an initial journal and then additional budget and expenditure information within the financial ledger as this becomes reported. This will ensure that the transactions of the IJB are being recorded at appropriate intervals during the financial year.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Agreed. The IJB's books of account are maintained by Midlothian Council. There was considerable discussion as to what would be reflected in these accounts in 16/17 hence the delay in actioning. However, we will liaise with Midlothian Council to reflect transactions more timeously in 2017/18</p>
2	<p>Financial reporting</p> <p>We would note that on certain occasions during the year, the finance report was included as a 'To-follow' item on the agenda, but was not subsequently added to the public agenda papers. There is a risk that business of the IJB is perceived to be undertaken without full transparency on financial reporting.</p>	<p>Management should ensure that all agenda items, except where they are permitted to be considered in private, are made publically available, even when listed initially as items 'to follow'.</p> <p style="text-align: right;"><i>Grade 3</i></p>	<p>Agreed</p>
3	<p>Use of directions / budget monitoring</p> <p>It is recognised that the financial risk sharing arrangements which applied in 2016/17 were a reflection of the approach to budget setting in the year and the support of the partners to ensure the first year operations of the IJB were provided with appropriate financial support.</p> <p>By allocating resources to the individual directions made by the IJB, there is a risk that these are not used in future to drive the prioritisation of resources which the IJB has determined through its planning processes.</p>	<p>As the IJB matures, financial monitoring should be developed such that there is clear incentive to deliver on the directions made by the IJB within the funding allocated as part of the direction.</p> <p>Where underspends arise, in line with the integration scheme, the IJB should determine whether to carry these forward as reserves or to reallocate in year to meet other financial pressures.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>Agreed. The IJB is continuing to develop its directions mechanism which will allow directions to become the key part of the governance and delivery mechanism for the Strategic Plan. Performance against individual directions will be monitored in terms of actions, required, financial resources used and outcome delivered.</p>

E. Action Plan (continued)



This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Board or management to action.

No.	Findings and risk	Our recommendation and grading	Management's response
4.	Internal audit In setting the medium term internal audit plan, internal audit highlighted that they had sufficient resource to focus only on high risk areas over a three year cycle. There is a risk that there is insufficient internal audit resource to review the control arrangements established by management in respect of the key risks facing the IJB.	It is important that those charged with governance of the IJB, in conjunction with management, ensure that there is appropriate internal audit resource, linked to other sources of assurance, to provide an appropriate coverage and audit of the IJB's internal control arrangements. <i>Grade 2</i>	Agreed in principle however the IJB recognises the resource constraints of its partners who provide this function. If internal audit resources are constrained then the IJB will have to recognise that in its risk register and risk management processes.
5	Financial planning and sustainability The IJB is already facing significant financial pressures in 2017/18 with a need to plans to manage these in year to ensure break-even by 31 March 2018. Forward financial planning has commenced to identify the financial pressures over the next three years and the steps which the IJB will need to take to manage these.	It is clear that there is full recognition of the need to develop longer term financial plans but given the significance of financial sustainability to the IJB, the Board should ensure that this remains an urgent priority. <i>Grade 1</i>	Agreed. The IJB is fully aware of this issue and the IJB is proposing to produce a multi year financial plan for the end of this calendar year.
6	Governance responsibilities In reviewing the Annual Governance Statement we identified a number of areas where the content could be clarified to make it clear what arrangements were in place and whether assurance was the responsibility of the IJB or one or both of its partners.	As the IJB continues to mature, focus is required on mapping the sources of governance assurance to ensure that Board members are clear on how their responsibilities are discharged. <i>Grade 2</i>	Agreed.

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