Accounts Commission for Scotland

A matter of trust

GUIDANCE ON TRUST REORGANISATION

MARCH
1999

The Accounts Commission for Scotland is a statutory, independent body which, through the audit process, assists local authorities and the health service in Scotland to achieve the highest standards of financial stewardship and the economic, efficient and effective use of their resources. The Commission has five main responsibilities:

- securing the external audit
- following up issues of concern identified through the audit, to ensure satisfactory resolutions
- reviewing the management arrangements which audited bodies have in place to achieve value for money
- carrying out national value for money studies to improve economy, efficiency and effectiveness in local government and the NHS
- issuing an annual direction to local authorities which sets out the range of performance information which they are required to publish.

The Commission secures the audit of 32 councils, 34 joint boards (including police and fire services), 15 health boards, 46 NHS trusts and six other NHS bodies. In total, these organisations spend public funds worth around £12 billion a year.

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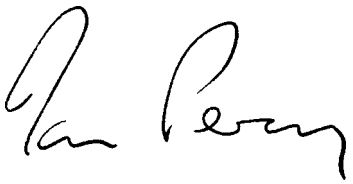
Chairman's foreword

At a period of significant change for the NHS in Scotland, I am pleased that the Accounts Commission has the opportunity of producing this guidance for the new trusts. We are in a unique position to draw on our experience of auditing governance arrangements in the NHS, and reorganisation in local government, to highlight practical issues which need to be addressed as the new NHS comes into being. Proper management arrangements will help to ensure that the NHS provides the best possible care to the people of Scotland.

Corporate governance is often defined as the system by which organisations are directed and controlled. However, too much emphasis on control can stifle the innovation that is needed for an organisation to offer the best care to the community it serves. Governance is defined in the *Oxford English Dictionary* as 'the action or manner of governing'; ' a mode of living, behaviour and demeanour'. The purpose of good governance is not only the direction and management of the affairs of an organisation, but also the alignment of corporate behaviour with the expectations of society, and accountability to stakeholders in the public interest. The process of governance involves the clear identification of responsibilities and accountabilities, and ensuring that there are checks and balances to ensure proper behaviour through a system of supervision, control and communication.

The governing bodies of the new trusts will be made up of trustees. I believe that the role of a trustee is to ensure proper corporate behaviour: the maintenance of probity in the public interest, the achievement of value for money from scarce resources, and the attainment of the primary objective of providing high quality patient care. The lead set by trustees will be crucial in ensuring good corporate governance; I hope that this paper will help to identify the necessary principles and procedures to turn that lead into action.



PROFESSOR IAN PERCY
CHAIRMAN

Introduction

The White Paper '*Designed to care*' was the catalyst for reorganisation of the NHS in Scotland. On 1 April 1999 the existing 46 NHS trusts on the mainland of Scotland will be replaced by 28 new trusts and a Special Health Board. The boards of the new trusts were established in February 1999, and they are now operating as shadow trusts alongside the existing trusts until 31 March 1999. The White Paper also signalled an end to the internal market, an increased focus on primary care, and a new statutory duty for the quality of care. All of these changes will affect corporate governance in the NHS.

Reorganisation presents opportunities, but risks are also involved. In the short term, there are risks associated with the disruption of current management arrangements, and the transfer of services and functions. In the medium term, there are the risks which arise from new management arrangements and controls which have not been tested over time. One of the objectives of reorganisation is to make savings by cutting out unnecessary bureaucracy, but it is important that a sound control environment is established and maintained.

The Accounts Commission is able to draw upon the experiences and lessons learnt from the reorganisation of local government in 1996, and from previous work on corporate governance in the NHS in Scotland. The Commission's report '*All above board?*' was published in December 1996, summarising the state of development of corporate governance in trusts and boards, and highlighting areas for improvement. The aim of this paper is to highlight the key aspects of corporate governance which the members of the new trust boards need to address.

New trusts need to give a high priority to creating a sound framework of governance. If trusts get the governance arrangements right in the early stages, then the likelihood of major problems in future years is significantly reduced. The purpose of this paper is to provide high level guidance to trust board members, audit committees and auditors on the risks of reorganisation. Its objectives are:

- to assist new trusts in realising the opportunities presented by reorganisation
- to contribute to minimising the risks associated with major organisational change
- to promote the principles of good governance in the new trusts.

New trusts will develop a variety of management arrangements which reflect local circumstances and preferences. There is, however, a practical agenda of issues relating to governance and stewardship which apply to all trusts. The first part of this paper looks at the different dimensions of governance, including financial management, information technology and value for money. The second part goes on to examine the risks involved in reorganisation, with the accent on probity.

Summary of recommendations

For new trusts:

1 **Corporate governance** should be high on the agenda of all new trusts.
2 A sound **control environment** is one of the core values upon which new trusts should be based. **Standing Orders including schedules of decisions reserved for the board, schemes of delegation, and standing financial instructions** will need to be considered carefully.
3 The **board** has overall responsibility for the proper management of the trust.
4 New **financial systems** should contain key aspects of control from the outset.
5 Each trust must commission an adequate and effective **internal audit** service which meets the NHS Internal Audit Standards.
6 **Effective audit and remuneration committees** should be established in line with the Audit Committee Handbook and other relevant guidance. Audit committees in particular need to form robust relationships with their external auditors. New board members may require training and support in carrying out their roles.
7 Good governance principles of clear lines of communication and accountability must be applied to **joint arrangements**.
8 The control environment governing **IT provision** is important.
9 Trusts should nominate an executive director to take corporate responsibility for **year 2000** issues.
10 Trust boards should consider how they aim to achieve their new statutory duty for quality of care and implement **clinical governance** principles.

For outgoing trusts:

11 The reorganisation process will present **increased risks** which must be recognised and addressed.
12 A **prudential approach** to financial management must be maintained.
13 A **sound control environment** must be maintained right up to the changeover date.
14 **Internal audit** has a prominent role to play during the reorganisation process and must be adequately resourced.
15 '**Appointed Officer' posts** must be maintained right up to the changeover date.
16 Existing trusts must ensure that appropriate staff responsibilities are maintained in particular areas where **separation of duties** is essential for internal financial controls.
17 Comprehensive registers of all **assets** should be maintained.
18 Existing trusts will need to compile comprehensive registers of all **contracts** and underlying documentation.
19 **Accounting records** will need to be maintained right up to the last day.

Bringing in the new

Background

Trust reorganisation provides an opportunity to take a fresh look at such fundamental issues as the kind of services desired, how decisions will be taken, and how services will be commissioned or delivered. Part of the challenge will be to use the opportunity presented by reorganisation to explore these issues and to seek innovative ways of meeting the needs of patients

New trusts will be focused initially on the need for continuity of patient care. For most trusts, the range of services to be provided will change on 1 April 1999. For primary care trusts, in particular, this will mean new responsibility for the delivery of primary care services and accountability for Local Health Care Co-operatives (LHCCs). The White Paper '*Designed to care*' also proposed a new statutory duty of quality of care for trusts. Corporate governance has been extended to encompass both financial and quality issues, building on the existing arrangements for corporate accountability.

Trusts need to ensure that sound financial arrangements are in place from the first day of the new trusts. Income must be collected, debts pursued, and staff and creditors paid from the outset. In many cases, it will be convenient and appropriate to build on the arrangements of the outgoing trusts. But reorganisation provides a unique opportunity for each shadow trust to look afresh, not just at the existing financial management arrangements, but at the wider corporate governance framework needed by a trust preparing for the challenges of the new NHS.

Corporate governance

The Cadbury Report defines corporate governance as 'the system by which organisations are directed and controlled'. There are three fundamental principles:

- openness
- integrity
- accountability.

The NHS Management Executive published Codes of Conduct and Accountability for NHS Boards in April 1994. These codes adopt the same three principles as the crucial public service values which must underpin the work of the health service. Supplementary guidance covers audit and remuneration committees, annual reports, and standards of business conduct for staff. The guidance was complemented by the Code of Practice on Openness in the NHS in Scotland, in May 1995, and the concept of openness has been reinforced with the requirement for trusts to hold board meetings in public from February 1998.

The Accounts Commission fully supports these principles. Openness is particularly important where the stewardship of public funds is involved. It is right that trusts are obliged to take most of their decisions in public; trust board members also require full and accurate information, together with sound professional advice, before decisions are made.

> Each public sector body is accountable for the way in which it has discharged its stewardship of public funds. Stewardship is a function of both executive and non-executive management and, therefore, responsibility for effective stewardship rests upon both the members and officers of a public sector body.
>
> That responsibility is discharged by the establishment of sound arrangements and systems for the planning, appraisal, authorisation and control over the use of resources, and by the preparation, maintenance and reporting of accurate and informative accounts.
>
> Source: *Accounts Commission Code of Audit Practice*

Reorganisation will not change the traditional public sector values of impartiality, openness and transparency, and the highest standards of probity and propriety appropriate to the handling of public money. It does, however, present an opportunity to re-emphasise these key aspects of governance.

The organisationof primary care will be affected by the creation of primary care trusts (PCTs). These trusts will be responsible for all primary care, including networks of GPs in Local Health Care Co-operatives (LHCCs), which will replace GP fundholding.

At the same time, primary care administration (which includes patient registration and payments to practitioners) is being moved away from health boards to the Common Services Agency (CSA). PCTs will be accountable for the development of primary care and for payments to primary care practitioners, with the CSA acting as their paying agent.

PCTs will also be accountable for LHCCs, voluntary organisations of GPs which form part of the PCT. The accountability of LHCCs is another governance matter that will need to be considered by PCT boards at an early stage.

In addition to these structural changes, all trust boards will be affected by the new statutory duty for clinical care. There are no simple answers on how best to implement clinical governance as part of the overall governance framework, but boards will need to address a range of issues:

- structure: How is responsibility for the quality of care to be delegated and carried through in practice?
- process: What clinical audit is planned or underway? Are clinical guidelines actively used and monitored? Has accreditation been sought?
- outputs: What information is available? How is it used?
- outcomes: How is the culture of clinical governance being developed? Is there evidence that it is changing?

Boards need to consider these high level aspects of corporate governance as a priority. However, there are a range of practical aspects which also need early attention, particularly in the light of the new requirements for executive and non-executive board directors to sign statements on internal financial controls.

A sound control environment

A sound control environment is essential to the efficient management of any trust, and is an important element of the culture of the organisation. It does not imply rigidity or centralisation in management arrangements; each trust must ensure that the system of internal controls is appropriate for its own organisation.

The Accounts Commission's Code of Audit Practice draws on the Auditing Practices Board's definition of an internal control system:

> It includes all the policies and procedures (internal controls) adopted by the directors and management of an entity to assist in achieving their objective of ensuring, as far as possible, the orderly and efficient conduct of its business, including adherence to internal policies, the safeguarding of assets, the prevention and detection of fraud and error, he accuracy and completeness of accounting records and the timely preparation of reliable financial information. Internal controls may be incorporated within computerised accounting systems. However, the internal controls system extends beyond those matters which relate directly to the accounting systems.
>
> Source: *Accounts Commission Code of Audit Practice*

This definition covers not only financial controls, but all the internal controls of the organisation. Responsibility for the establishment, operation and effectiveness of internal controls rests firmly with the trust board on a corporate basis in line with the Code of Accountability.

Statements on the adequacy of internal financial controls are required for the first time in 1998/99; the chief executive signs a statement on behalf of the board to confirm that they have reviewed the effectiveness of the organisation's internal financial controls. It is anticipated that these statements will be extended to include all internal controls in future.

Primary care trust boards have particular issues for attention in this area. The extension of the traditional trust services to include primary care services will have a significant impact. PCTs will be accountable for the provision and quality of primary care services, and for payments to primary care practitioners. This new role requires PCTs to work closely with their LHCCs and with the CSA.

LHCCs will be managed at a local level, even though they are legally part of the PCT. The PCT will remain accountable for the provision of care by LHCCs, and for monitoring their finances. PCTs therefore need to allow LHCCs to operate with flexibility and freedom, while ensuring that they function within a coherent and acceptable governance framework. Boards of PCTs need to give early priority to setting the governance frameworks within which LHCCs must operate.

Under the new regime, PCTs will also be accountable for primary care expenditure. However, the system for making payments to primary care practitioners will be operated by the Common Services Agency (CSA) as the agent of primary care trusts. This means that PCTs will be accountable for expenditure which they do not manage directly. PCTs will need to ensure that they have adequate systems in place to allow them to monitor primary care expenditure, both at the level of individual GPs and LHCCs (to ensure expenditure remains within budget), and at the overall trust level.

PCT boards will have to consider how they will obtain the assurances that they require on the accuracy and validity of these payments. PCTs may wish to seek assurances from the CSA on the adequacy of systems for calculating and making payments, and use the services of their internal auditors to review the systems in place for monitoring expenditure.

The Commission expects the **boards** of shadow trusts to recognise their stewardship responsibilities in all of their deliberations, and encourages each of them to ensure that a sound control environment is one of the core values upon which the new trust will be organised and managed. From the outset, the board needs a clear commitment to the trust's control environment. The importance of clear lines of responsibility and accountability cannot be over-emphasised.

The role of the **chief executive** is important. The Code of Accountability states that the Chief Executive is directly accountable to the chairman and the board for the operation of the organisation, and for implementing the board's decisions. Trust **chairmen** are asked to nominate their Chief Executives as 'Appointed Officers' and this role brings with it clear responsibilities. In particular, the Appointed Officer is required 'to ensure that the trust carries out its functions in a way which ensures proper stewardship of public money and assets. Specifically, there is a requirement to assist the Chairman to implement the requirements of corporate governance as set out in the Codes of Conduct and Accountability.'

The board is ultimately responsible for internal control, but the chief executive has primary responsibility for ensuring that internal controls are implemented and continue to operate effectively. In practice the Chief Executive will do this by delegating authority to a number of other executive directors and senior managers. Under the NHS (Scotland) Act 1978, a **director of finance** is required to:

- provide financial advice to the board and its officers
- supervise the implementation of the board's financial policies
- design, implement and supervise systems of financial control
- prepare and maintain such accounts, certificates, records and reports as the board may require.

The trust board has overall responsibility for the proper management of the trust and for the appropriateness of the arrangements established. The board must therefore ensure that the officers of the trust recognise the importance of the principles of good governance in public affairs. It is also the duty of the chief executive, in his or her role as Appointed Officer, to ensure that these principles are reflected in sound management arrangements.

The early deliberations of the chief executives and boards of the new trusts should fully reflect the need for a sound control environment - in policies, structures and processes. The required framework of controls extends beyond those relating to financial issues, including those designed to ensure that:

- the organisation's policies are put into practice
- the organisation's values are met
- laws and regulations are complied with
- required procedures are adhered to
- financial statements and other published information are accurate and reliable
- human, financial and other resources are managed efficiently and effectively
- social concerns are met, including environmental and community concerns (eg fairness to all the various stakeholders, including resource providers, patients and staff.)

An essential part of those arrangements will include the consideration and formal adoption of Standing Orders, including Schedules of Decisions Reserved for the Board, Schemes of Delegation, and Standing Financial Instructions. Shadow trust boards should take the opportunity to consider these vital documents carefully, to ensure that they are founded on sound principles of good governance and comply with the appropriate guidance. Trust board members should also be made aware of their roles, as defined in the Codes of Conduct and Accountability.

"An effective internal control system is an essential part of the efficient management of any organisation."
Accounts Commission
Code of Audit Practice

There are also a number of key financial aspects of the control environment which need to be addressed:

- the security of key financial systems
- adequate and effective internal audit
- reliable accounts production processes
- a strong audit committee.

Security of key financial systems

The key financial systems for NHS bodies include payroll, budgetary control, and income. Reorganisation offers an opportunity to ensure that sound financial management arrangements are established at the outset, and that key financial systems are founded upon robust processes to ensure probity and good governance. Most new trusts will be using systems inherited from their predecessors to varying degrees, but board members will still require assurance on the controls which are in place. This should form part of an effective risk management policy, overseen by the trust board.

"Internal audit should be a key element of the internal control system which is set up by management. A strong internal audit function is considered to be an important feature for the effectiveness of the internal control systems established."
Accounts Commission
Code of Audit Practice

Internal audit

An adequate and effective internal audit function has been a key feature of the internal control mechanism within the NHS for a number of years. An NHS Internal Audit Manual was first published in 1987, establishing a benchmark for measuring internal audit performance by setting out the minimum standards for NHS internal audit. This manual was updated in 1990 and again in 1995.

The significance of the NHS Internal Audit Manual was confirmed by the ME with the publication of the NHS Internal Audit Standards in March 1996. This sets out the nine standards with which NHS internal audit services must comply.

The liaison between internal and external in the audit is generally good, contributing to an efficient use of the overall audit resource. Some auditors appointed by the Accounts Commission have, however, continued to make

reference to their inability to rely fully on internal audit, mainly due to the fact that the planned internal audit work was not completed.

An effective internal audit function is a key resource for the audit committee. Each internal audit service should produce an annual statement to the audit committee on the adequacy and effectiveness of internal control within the organisation. However, the Accounts Commission noted in 1996 that this happened in very few health bodies in Scotland.

"The overall performance of audited bodies and auditors ... was commendable"
The 1997/98 audit of National Health Service bodies in Scotland SR98/3

Reliable accounts production processes

Annual accounts form an essential element of good governance, through their role in demonstrating the trust's financial accountability for the stewardship of public funds. That process requires that the annual accounts of trusts are prepared and audited by 30 June each year (or 31 July at the latest), that they show a true and fair view of the trust's state of affairs, and that an annual report is presented in public at an annual general meeting by 30 September each year.

In the past the target date for audited accounts has been achieved by most trusts, with all but a few exceptions being completed by the deadline of 31 July. The target date for the preparation of accounts and the completion of the audit is extremely tight, and the Commission recognises the achievement of trusts and auditors in meeting it.

Strong audit committee

Audit committees are advocated by the Cadbury Report. The Code of Accountability, issued in April 1994, required each trust to establish an audit committee for the first time. The Audit Committee Handbook, issued in 1996, provides detailed guidance on:

- objectives and benefits
- composition, establishment and duties
- measures to improve the effectiveness of audit committees.

The Commission reported in 1996 that every health body in Scotland had established an audit committee, but that very few of them reviewed their effectiveness or looked for ways of improving their performance. The Commission expects audit committees to perform, as a minimum, the duties set out in the Audit Committee Handbook, including:

- reviewing the trust's system of internal control and providing assurance to the board that internal control systems are operating effectively
- establishing professional relationships with both internal and external audit
- reviewing action taken by the chief executive on audit recommendations
- reviewing changes to the Standing Orders and Standing Financial Instructions, and examining the circumstances whenever the Standing Orders are waived.

The establishment of an effective audit committee is an integral part of good governance. Boards of trusts will soon be determining their committee structures, and the Accounts Commission urges each new trust to establish its audit committee, as soon as possible, in line with the Audit Committee Handbook.

Exhibit: Accounts Commission expectations of the appointed auditor in supporting the audit committee

- **Audit plans:** the auditor should involve the audit committee in developing and agreeing the audit plan, based on sound risk assessment and a knowledge of local priorities. Progress against the plan should be monitored throughout the year.
- **Reports:** audit committees are the main audience for external audit reports**,** whether management letters, value for money reports or final reports. Auditors should communicate their findings to audit committees in a clear and timeous way, concentrating on the most significant issues.
- **Focus on agreeing action plans:** all types of audit reports should act primarily as a catalyst for action. Auditors should work with audit committees to develop plans for agreed, measurable actions, which can be used as the basis for monitoring change.

Clinical governance

In addition to the existing responsibility for good financial management and probity, the new trusts will also have a new and equally important responsibility for clinical governance. The White Paper '*Designed to care*' made several commitments in relation to clinical governance:

- the Government will amend trusts' statutory duties to make explicit their responsibility for quality of care
- trust chief executives will be accountable for the quality of care provided by their trust, in the same way as they are accountable for proper use of resources
- trust chief executives will be expected to ensure that there are suitable local arrangements to give them, and the trust board, the assurance they need that this duty is being met.

Guidance on clinical governance for the executive teams of new trusts was issued in November 1998. It builds on existing patterns of professional self-regulation and corporate governance principles, but offers a framework for extending this more systematically into the local clinical community. The guidance identifies activities to support the delivery of clinical governance, such as clinical audit, clinical guidelines, and quality assurance and accreditation, and states that trust boards should establish committees to review clinical governance.

There will be no single 'right' way of fulfilling this new duty, but the boards of new trusts must consider how they are going to be assured of the quality of care, embracing the principles in the national guidance.

Different ways of working

Prior to the publication of '*Designed to care*' in December 1997, the Government had already signalled its intention to end the internal market in the NHS, replacing it with joint arrangements aimed at providing an integrated system of health care. The annual priorities and planning guidance was refocused, to encourage collaboration and co-operation rather than competition, and guidance was issued on reducing bureaucracy and on partnership schemes.

The new arrangements are based on Health Improvement Programmes (HIPs), which are the main responsibility of boards, and matching Trust Implementation Plans (TIPs), which set out how the HIP will be put into practice. This means that trusts must work in collaboration with health boards, other local trusts, GPs and others.

In September 1997, the Scottish Office invited applications for Local Care Partnership Schemes. These schemes require trusts to work in partnership with health boards, GPs, local authorities and other agencies to remove administrative or other barriers to effective and efficient local integration of health, housing and social care services in the community.

This has recently been followed by '*Modernising community care: An action plan*'. This action plan focuses on how the statutory organisations responsible for the delivery of community care - trusts, health boards, local authorities, and Scottish Homes - can better manage and deliver community care.

Trusts were first invited in July 1997 to review the way in which they deliver services, with a view to a more collaborate and co-operative approach. In particular, it was suggested that there could be benefits in sharing support services such as laundry, energy, sterile services, patient transport, catering, human resources and finance. The responsibility for the quality of support services lies firmly with trust boards, and shadow trusts have been asked to prepare plans on how they intend to achieve best value over the next five years.

There can be clear benefits in both costs and effectiveness through shared arrangements, but the good governance of clear lines of communication and accountability must be applied to any joint arrangements. The Commission has published guidance on working with arms-length organisations, and many of the same principles will apply to consortia within the NHS.

Exhibit: Key principles from *'Following the public pound'*

- An NHS body must be clear about its reasons for agreeing to transfer funds to an external organisation.
- The NHS body should spell out clearly the nature of the financial relationship and the extent of its financial commitment to the external organisation .
- The NHS body should set out how it intends to monitor its relationship with the external organisation, and what information it requires on financial performance, the achievement of targets, and future plans.

IT issues

The provision of information technology will be of particular concern to new trusts. There are two challenges associated with reconfiguration:

- to ensure that information systems continue to run from the changeover day on 1 April 1999
- to deal effectively with the aggregation or disaggregation of existing systems.

However, in addition to reconfiguration, there are other major IT concerns currently facing the NHS in Scotland:

- the change of supplier for centrally provided IT systems, with effect from 1 April 1999
- the year 2000 issue.

The immediate priority will be to ensure that adequate systems exist for all the main applications (patient administration, payroll, creditors etc) from the first day. For a smooth transition, outgoing and shadow trusts should be liaising and planning together for the future. It is likely that the new trusts will initially be using information systems from a variety of sources, but sound planning will enable them gradually to rationalise provision and develop sound strategies.

Information technology working groups should already have been established to plan for a smooth transition, and should be addressing the following key areas:

- project planning - ensuring that arrangements are in place for a smooth handover of all relevant IT systems
- IT information and records - preparing detailed inventories covering equipment, software, facilities, service levels and staff skills
- IT information systems - identifying and evaluating systems, and assessing their transportability
- commitments and contracts - identifying and evaluating existing contractual commitments
- security and data protection - ensuring that data security is not compromised during the transition period.

The new trusts will need to begin to develop longer term strategies for information, but the position may be complicated by the transfer of the central NHS information service contract from CSC to SEMA with effect from 1 April 1999. Action is needed at a national level to ensure that the transition is as smooth as possible. At a local level, trust boards should be seeking assurances that there will be no disruption to the services provided.

It is the responsibility of management to address the problems and potential risks associated with the year 2000 issue. Most trusts are continuing to take action to address the risks to computerised financial and patient management systems, The Management Executive has issued guidance through a series of MELs, and a target date of 31 December 1998 was set for all critical systems to be ready and fully tested, or for contingency plans to be in place for those systems that will not be ready in time.

New trusts will need to take over responsibility for this work. The boards of new trusts should nominate an executive director to take corporate responsibility for year 2000 issues, and to liaise with nominated directors in the outgoing trusts.

Value for money

The auditors appointed by the Accounts Commission have a duty to satisfy themselves that health bodies have arrangements in place for securing economy, efficiency and effectiveness in their use of resources. The Commission will continue to develop, in partnership with trusts, guidance on management arrangements which auditors can use in carrying out this duty. The first module, '*Managing people*', will be available in the first operational year of the new trusts.

The Commission will also continue to produce guidance for auditors on specific value for money issues, taking account of NHS priorities, the scope for better value for money, and the views of stakeholders throughout the service.

Audit Committees should be fully involved in planning value for money work carried out by their auditors, and in receiving the reports and action plans which result from that work. Robust mechanisms for ensuring that recommendations are implemented are particularly important.

Exhibit: Approaches to VFM

The Commission takes a collaborative approach to its VFM responsibilities, working with audited bodies and other stakeholders both to select worthwhile topics for study and to identify and achieve potential improvements in value for money. Each study is researched by a small team within the Accounts Commission, supported by experts from the NHS in Scotland, to identify good practice and comparative information which can be used in assessing performance locally. There are three broad approaches to local follow-up:

- follow-up by local auditors
- self-assessment
- follow-up by central specialist teams.

Under the first approach, the Commission's auditors are provided with a methodology for local review, training and ongoing support, and are asked to apply it in each relevant health service body across the country. They work with local managers and clinicians to review local performance, and to agree an action plan to tackle any problems. Each of these studies is tailored to local needs using short 'overviews', which helps the auditor and local managers to decide whether the study is worth doing at an individual trust and, if so, which are the priority areas. This information can be used to plan how best to use the limited audit time available. Auditors will return two or three years later (depending on the study) to ensure that the action plan has been implemented.

Other studies are designed for self-assessment. In the most important example of this type of study so far, the Accounts Commission team developed a methodology for comparing residential and nursing homes across the council, voluntary and private sectors, with indicators of cost, quality and the dependency of residents. This methodology, together with robust comparative information, enables councils to carry out their own service reviews and identify areas where value for money can be improved.

The third type of study is carried out entirely by a specialist team within the Accounts Commission, supported by experts from the area under review. This team develops the methodology, and also visits each relevant health body in Scotland to review local performance and agree action plans.

Winding down the old

Background

The timescale for reorganisation is tight, with only 15 months between the publication of the White Paper '*Designed to care*' and the establishment of the new trusts. This has placed significant pressures on the staff of existing trusts, charged with ensuring a successful transfer of services, staff, assets and information.

The temptation to concentrate on the establishment of the new trusts is clear, but existing trusts need to ensure that service delivery is maintained until the final day, and they should be managed as going concerns until that point.

Existing trusts need to co-operate with one another and with shadow trusts to avoid conflict, particularly in the exchange of information and the deployment of key staff. The Accounts Commission's recent experience of local government reorganisation has confirmed the difficulty of preventing deteriorating of controls in the last few months of an outgoing body, not least as key staff obtain jobs in the new trusts or leave the service altogether.

Motivation and retention of key staff will be critical in the final period. It is likely that, in order to minimise disruption to services and ensure a smooth handover, some staff will need to carry out dual roles for the next few months, retaining responsibility for their previous posts and making preparations for the new.

The reorganisation process itself will introduce a number of risks:

- outgoing trusts may lose the experience and expertise of current board members and staff
- the trustees and senior managers of the new trusts may not have experience of managing the type and scale of the new service (particularly in the case of primary care trusts)
- the motivation of some existing board members and staff may suffer
- the transfer of services, staff, assets and information contains inherent risks, particularly of loss, or of incomplete or inaccurate transfer
- all of these risks may contribute to weakened financial controls in existing trusts.

This section sets out some of the key areas of risk, together with guidance on the Commission's expectations of the outgoing trusts. A sound control environment must be maintained by outgoing trusts right up to the point when the accounts have been prepared and audited. This is likely to be after the official cessation date of 31 March 1999, so robust plans will be required for the transitional period.

Accent on probity

Prudential guidelines

Trusts are expected to adopt a prudent and responsible approach to financial management at all times, but this expectation assumes even greater importance in a period of major change.

CIPFA produced a Code of Practice on the prudential approach to financial management prior to local government reorganisation. This contained guidance in a number of areas which are equally applicable to the reorganisation of the NHS, including:

- consultation with successor trusts
- use of assets
- new contractual commitments
- collection of debtor balances
- borrowing and investment
- information technology.

The outgoing trusts need to adopt formal guidelines on the management of their affairs in the last months.

The Management Executive is due to set out which of the successor trusts will be required to take responsibility for the accounts of their predecessors. Practical responsibility for preparing the final accounts of the outgoing trusts will lie with the chief executive and director of finance of the successor trusts, and these individuals, together with the chairman of the new trust, will also have responsibility for signing the statements of account. They will have to take assurance from the Internal Financial Control Statements signed by members of the boards of the outgoing trusts. It is important that any potential problems are identified as soon as possible, and contingency plans made to deal with them.

The timescale for the submission of audited accounts has always been tight. Extra vigilance will be needed in the final year to ensure that there is no slippage in the timetable. Any slippage may have a significant effect upon the new trusts, auditors and the Management Executive. Some of the problems experienced in local government organisation, particularly the large liabilities or deficits inherited by some of the new unitary councils, were directly related to delays in closing down the accounts and preparing the final sets of financial statements for the old councils.

Internal controls

The wind down period is fraught with risks, and financial systems themselves are vulnerable to a lack of financial controls. It is crucial that the outgoing trusts maintain proper financial control and operate sound and reliable systems right up to the changeover date.

The internal audit function should play a prominent role during reorganisation, and increased vigilance will be required where internal systems are at risk of breakdown. The management of the outgoing trusts should ensure that the internal audit role is given the attention it requires during reorganisation, and that resources are provided to ensure that potential risk areas are adequately monitored and reported. In particular, management should avoid diverting internal audit resources to undertake the tasks of depleted finance functions.

Internal audit activity in the period up to reconfiguration should be particularly focused to reflect the potential risks of:

- asset loss
- declining computer security
- deteriorating financial controls
- the possibility of increased scope for fraud.

IT systems affect every aspect of a trust's activities, and it is vital to ensure that control over access to these systems is maintained during the transition period. The responsibility of the existing trusts for the security of IT systems, data and assets does not cease until those systems have been transferred to the successor trusts.

Access controls must continue to be rigorously applied. It is likely that there will be an increased need for staff to access data and software to aid the transition period, but, trusts must ensure that access is necessary, authorised and secure. As staff leave the outgoing trusts, arrangements for secure access must keep pace with change. Sound arrangements are needed to ensure that:

- separation of duties is maintained and access controls are used to reinforce this separation
- officers responsible for managing access controls are notified promptly of staff movements and changes of responsibility
- the access rights of departing staff are terminated as soon as possible.

Tight control is needed over financial and budgetary control in the final months of the outgoing trusts. Budgetary control continues to be crucial as trusts near their end, and all trusts continue to face statutory financial targets for their final year of existence.

The Minister for Health has said that every effort will be made to avoid compulsory redundancies as a result of trust reconfiguration. However, it is likely that a number of staff will leave during the transitional period, and all trusts need to comply with the guidance on termination settlements for staff. In particular, they need to follow the recent MELs on pay and conditions of service for general and senior managers. The importance of these issues has been highlighted in the recent statutory reports on Tayside Health Board, and on the 1997/98 audit of NHS bodies.

Trust boards should not be concerned only with following guidance from the Management Executive; they must also ensure that they maintain an overall governance role in matters such as setting general and managers' salaries, terms and conditions of service, termination settlements, and staff relocation costs. The board will need to take advice from the remuneration committee on these matters, and it is essential that the committee plays its role effectively. Where it has been identified that certain posts will become redundant, trusts should give notice to employees as early as possible to avoid payments in lieu of notice.

Overall, extra vigilance is needed to ensure that existing controls are fully maintained during the transitional period.

Appointed officers

Many senior staff will be transferring to new trusts or leaving the service, but the roles of the chief executive and the director of finance will be particular significant in the period up to changeover.

The transfer process

Staff

During reorganisation, outgoing trusts will depend heavily on the skills, experience and motivation of their staff, both for the continued delivery of high quality services and for the proper administration of the trust's affairs. The process of staff movements will increase the risk of uncertainty and of a lack of commitment or motivation for the staff of outgoing trusts, and this risk needs to be recognised and addressed. Trusts must identify those key staff who are essential for continued service delivery, and ensure regular, ongoing consultation and communication with existing staff.

Trusts must be clear about those posts and staff which are essential to the sound management and control of the organisation, and ensure that appropriate measures are taken swiftly to cover for any vacancies arising in key posts. Vigilance over vacancies is especially important in relation to the finance and audit functions.

"Deficiencies in trusts' asset registers have been a recurring theme in auditors' reports... In view of the substantial sums represented by assets it is essential that there are sound systems to safeguard them from loss and reliable records to ensure that they are properly charged through the accounts."
The 1996/97 audit of National Health Service bodies in Scotland SR 97/4

Assets

Trusts are required to maintain comprehensive registers of all the capital assets they own for the purposes of capital accounting, although it is clear from auditors' reports that comprehensive registers are not in place in all trusts. It should be a matter of priority to ensure that these registers are fully up to date before changeover.

Arrangements will also be needed to govern the transfer of assets between the outgoing and the new trusts. A revaluation of the NHS estate is due to take effect on 1 April 1999, for which valuers are currently undertaking inspections and preparing reports. The Management Executive is due to issue further guidance on the transfer and revaluation of assets.

Finance

Reorganisation will increase the risk of accounting shortcomings arising from incomplete reconciliations, uncleared suspense accounts, and the general risk of 'quick fix' accounting solutions being applied. These types of accounting shortcomings caused problems when trusts were originally established, and during local government reorganisation.

The increased risks of fraud or misappropriation are obvious, reinforcing the importance of maintaining proper accounting records right up to the last day. The maintenance of a sound control environment in outgoing trusts is a board responsibility, and requires a high priority during the remaining period before reorganisation. The roles of internal audit and of the chief executive and director of finance as appointed officers will be crucial.

Contracts

The new trusts will inherit the contractual rights and responsibilities of their predecessors. In order to transfer properly the rights and liabilities which fall to the new trusts, comprehensive registers of all contracts and the underlying documentation will be needed. The difficulties here are likely to be greater where outgoing trusts are disaggregating.

Bibliography of relevant publications

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Code of Audit Practice

Local government reorganisation and the stewardship of public funds

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Effective internal control: A framework for public service bodies

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Corporate governance: A framework for public service bodies

Financial reporting: An Institute statement

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Code of conduct for NHS boards

Code of accountability for NHS boards

Code of practice on openness in the NHS in Scotland

Audit committee handbook

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Role of the director of finance

MEL (1994) 80 Corporate governance: Supplementary guidance

18 George Street Edinburgh EH2 2QU

Telephone 0131 477 1234

http://www.accounts-commission.gov.uk

publications@scot-ac.gov.uk

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