The Committee will meet at 10.00 am in Committee Room 1 to consider the following agenda items:

1. **Choice of Convener:** The Committee will choose a new Convener.

2. **Budget Process 2007-08:** The Committee will take evidence from—
   
   Margaret Jamieson MSP, Convener, Scottish Commission for Public Audit.

3. **Decisions on taking business in private:** The Committee will decide whether to consider its draft report on the Budget Process 2007-08 in private at its next meeting and any subsequent meetings where the report is considered.

4. **Education (School Meals) (Scotland) Bill and Schools (Health Promotion and Nutrition) (Scotland) Bill (in private):** The Committee will consider its draft report on the Financial Memoranda of the Education (School Meals) (Scotland) Bill and Schools (Health Promotion and Nutrition) (Scotland) Bills.

5. **Protection of Vulnerable Groups (Scotland) Bill (in private):** The Committee will consider its draft report on the Financial Memorandum of the Protection of Vulnerable Groups (Scotland) Bill.

Susan Duffy
Clerk to the Committee
Room T3.60
Extn 85215
The papers for this meeting are:

**Agenda Item 2**

Paper from the Clerk

Report from the Scottish Commission for Public Audit

Audit Scotland’s 2007-08 budget proposal

**Agenda Item 4**

PRIVATE PAPER

**Agenda Item 5**

PRIVATE PAPER

Supplementary submissions from:

- SCVO; and
- Scottish Executive.
Finance Committee

29th Meeting 2006 – Tuesday 21 November 2006

Budget Process 2007-08 - SCPA Report on Audit Scotland’s Spending Proposals

Introduction

1. At its meeting on 14 November the Committee agreed to invite the Convener of the Scottish Commission for Public Audit to attend the meeting on 21 November to provide information on the SCPA’s scrutiny of Audit Scotland’s budget proposal for 2007-08.

Background

2. The Finance Committee has overall responsibility for scrutinising all expenditure paid out of the Scottish Consolidated Fund. However the Scottish Commission for Public Audit has direct responsibility for scrutinising Audit Scotland’s budget proposals.

3. The SCPA forwards a copy of its report on Audit Scotland’s budget proposal to the Finance Committee in accordance with the Written Agreement between the Committee and the Commission. In this way, the Committee is not directly scrutinising Audit Scotland’s Spending Plans but is able to consider the SCPA’s scrutiny and take account of it in its report.

4. Under the Written Agreement, the SCPA agrees that in order to assist the Committee’s understanding of Audit Scotland’s expenditure plans, it will seek to answer any questions from the Committee and make information available to the Committee.

5. On this basis, Margaret Jamieson MSP, Commission Convener, has accepted the Committee’s invitation to attend the Committee meeting on 21 November. Margaret Jamieson will provide a verbal report back to the Committee detailing the work undertaken by the Commission in scrutinising Audit Scotland’s budget proposal and the information which formed the basis for the recommendations reached in its report.

6. The paper circulated for the meeting on 14 November which summarises the contents of the SCPA’s report and annexes the written agreement between the SCPA and the Committee is attached. In addition, Members have been issued with the SCPA’s full report (FI/S2/06/29/2) and Audit Scotland’s budget proposal (FI/S2/06/29/3).

Conclusion

7. The Committee is invited to consider the SCPA’s scrutiny of Audit Scotland’s 2007-08 budget proposal.
Introduction

8. This paper outlines the respective roles of the Finance Committee and the SCPA within the annual budget process and highlights the main issues raised within the SCPA’s report on Audit Scotland’s 2007-08 budget proposal.

Background

9. The Finance Committee has overall responsibility for scrutinising all expenditure paid out of the Scottish Consolidated Fund. In addition to scrutinising the Executive’s Draft Budget, the Committee also scrutinises the budget of the Scottish Parliamentary Corporate Body (SPCB) which is top-sliced from the Scottish Consolidated Fund (ie, the money for this is allocated before the Executive makes its allocations).

10. The other body whose budget is top-sliced is Audit Scotland. However, their spending plans are not directly scrutinised by the Finance Committee. The Public Finance and Accountability (Scotland) Act 2000 (the “PFA Act”) set up the Scottish Commission for Public Audit (SCPA) to scrutinise the spending plans of Audit Scotland. Under the terms of Section 11(9) of the PFA act, Audit Scotland must:

“for each financial year, prepare proposals for its use of resources and expenditure and send the proposals to the Scottish Commission for Public Audit...which is to examine the proposals and report to the Parliament on them”.

11. The SCPA’s membership is cross-party and is approved by Parliament. Each year, the SCPA receives Audit Scotland’s spending plans, takes evidence from the Auditor General and Audit Scotland on them and produces a report on the plans. In effect, the SCPA is giving its views on whether Audit Scotland’s spending plans should be approved or not. This report must be laid before Parliament.

12. As well as laying the report, the SCPA forwards a copy of its report to the Finance Committee and the Finance Committee includes a copy of this report in an annexe to its stage 2 budget report. In this way, the Committee is not directly scrutinising Audit Scotland’s Spending Plans but is considering the SCPA’s scrutiny and taking account of it in its report.
13. The Finance Committee debates its report in Parliament and this is followed by a vote. As the SCPA’s report is annexed to the Finance Committee’s report, then in effect, Parliament is approving Audit Scotland’s proposals through this route. It should be noted that Audit Scotland’s budget does appear in the subsequent Budget Bill which is voted on in its entirety by the Parliament.

14. The Written Agreement which exists between the Finance Committee and the SCPA (agreed by Parliament) formalises this practice. This Agreement details the procedures to be followed with regard to the examination by the SCPA of Audit Scotland’s spending proposals and details the procedure to be followed in the event that there is disagreement between the SCPA and the Finance Committee. A copy of the finalised Agreement is attached for the Committee’s information.

SCPA conclusions and recommendations on Audit Scotland’s 2007-08 budget proposal

- The SCPA’s report recognises improved presentation of direct and indirect costs by Audit Scotland, as requested by the Commission which has aided its scrutiny.

- The report recommends that, in future, Audit Scotland provides a breakdown of targets for planned efficiency savings (analysed between cash releasing and time releasing).

- In relation to governance issues, the report recommends that Audit Scotland writes to the Commission each time it proposes an increase in its overall staffing complement, or any form of restructuring, to provide a justification for this change and details of the financial impact of any such change.

- Whilst the SCPA recommends in its report that Audit Scotland’s budget bid be approved, the recommendation is on the basis that the SCPA intends to separately pursue the issue of a lack of budgeting for an unintended £300,000 pension liability for Audit Scotland caused by a loophole in the Scottish Public Services Ombudsman Act 2002. The report states that ‘the Commission considers that reflecting this liability within the 2007-08 proposal would have constituted prudent financial management.’

Conclusion

15. The Committee is invited to consider the SCPA’s report.

Susan Duffy
Clerk to the Committee
THE BUDGETING PROCESS
AGREEMENT BETWEEN
THE SCOTTISH COMMISSION FOR PUBLIC AUDIT
AND THE FINANCE COMMITTEE

Foreword

1. This document sets out a revised understanding between the Scottish Commission for Public Audit (SCPA) and the Finance Committee of the Scottish Parliament, in relation to arrangements to be observed in connection with the annual budgeting process. It is not intended to create any legal rights or obligations on either the SCPA or the Finance Committee of the Scottish Parliament.

2. Under the terms of a revised agreement concluded with the Scottish Ministers the Finance Committee has agreed to participate in a biennial budget cycle with a full three-stage process in Spending Review years and a more limited process in non-Spending Review and election years. A separate administrative arrangement also exists between the SCPA and Audit Scotland.

Background

3. Scottish Ministers have undertaken to submit each year in which a Spending Review occurs to the Parliament (by 31 March or the first day thereafter on which the Parliament sits), a provisional expenditure plan. This document will set out the Executive’s view on priorities for the coming Spending Review period; an initial assessment of progress against the key performance targets for each portfolio set in the previous Spending Review; and general expenditure proposals for those forward years for which aggregate figures at programme level are available. The Finance Committee can then seek views from a variety of sources including members of the public and other Committees of the Parliament.

4. Normally, the Scottish Ministers will present detailed expenditure proposals for the next financial year) by 20 September or the first day thereafter on which the Parliament sits. The Finance Committee will then produce a report in consultation with other committees of the Parliament. This will comment on the Scottish Ministers’ proposals and may include an alternative set of proposals. If it does, the total spend proposed by the Finance Committee will not exceed the total proposed by the Scottish Ministers. A plenary debate on the report will follow in which Committees and individual members will debate the Finance Committee’s report and may seek to propose amendments to the Executive’s expenditure proposals through the
mechanism of tabling amendments to the Finance Committee motion. It should be noted that even if such amendments are agreed to, this does not automatically guarantee that expenditure proposals will be amended in the subsequent Budget Bill, within the total proposed.

The Scottish Ministers will produce a Budget Bill by 20 January each year or the first day thereafter on which the Parliament sits.

**Audit Scotland’s Budget**

5. The expenditure plans of any body which has a prior call on the Scottish Consolidated Fund will reduce the total amount available to the Scottish Ministers for inclusion in their plans. Audit Scotland’s budget falls into that category, albeit that this budget forms a very small proportion of the total available resources. It is therefore important that, wherever possible, accurate information about the spending plans of Audit Scotland is provided to the Finance Committee and the Scottish Ministers at an early stage.

6. To this end, the SCPA, as the body which has responsibility for examining and reporting on Audit Scotland’s expenditure proposals has agreed that it will provide to the Finance Committee and to the Scottish Ministers, by mid-March each year, Audit Scotland’s provisional expenditure plan. The SCPA will also provide to the Committee and to the Scottish Ministers, no later than the end of the second week in November, a further expenditure plan for Audit Scotland reflecting any changes which have occurred since March.

7. The SCPA also undertakes to keep both the Committee and the Scottish Ministers informed throughout the period between March and January of any substantive changes to Audit Scotland’s budget in recognition of the fact that these would affect the Scottish Ministers’ expenditure plans and the Parliament’s consideration of them.

8. By convention, the Finance Committee’s consideration of the Executive’s draft budget (i.e. stage 2 of the budget process) has included a discussion of the SCPA’s report on Audit Scotland’s expenditure proposals. The SCPA’s report has then been included as an annexe to the Finance Committee’s report. The Committee and the SCPA wish to formalise this link, in recognition of the fact that whilst the SCPA has primary responsibility for scrutinising Audit Scotland’s expenditure proposals, the Finance Committee is responsible for scrutinising Scottish Ministers’ expenditure proposals as a whole.

9. This process creates the possibility of disagreement between the two bodies if they were to take a different opinion on Audit Scotland’s proposals. This could result in the Finance Committee’s report containing a different recommendation on Audit Scotland’s proposals from that reported by the SCPA.
10. To attempt to avoid such a scenario, the Finance Committee and the SCPA can discuss the SCPA’s report before the Finance Committee produces its report. The SCPA agrees that in order to assist the Committee’s understanding of Audit Scotland’s expenditure plans, it will seek to answer any questions from the Committee and make information available to the Committee.

11. If there is still disagreement between the Finance Committee and the SCPA, the Committee can express its comments on Audit Scotland’s proposals in its report or in the motion to discuss its report. The SCPA is free to lodge an amendment to the Finance Committee’s motion. The Parliament will then vote on the Finance Committee’s motion.

12. In situations where the SCPA’s report expresses discontent with Audit Scotland’s expenditure proposals and the Finance Committee either has no comment to make or is in agreement, the SCPA can lodge a motion on its report and seek to secure parliamentary time to debate this. Alternatively, the Finance Committee could, with the SCPA’s agreement, express any discontent in its report which could then be debated in the Parliament.

13. In either case, the final expenditure proposals for Audit Scotland will appear in the annual Budget Bill, which will be voted upon by the Parliament.
Scottish Commission for Public Audit

1st Report 2006

Audit Scotland’s Expenditure Proposals 2007-2008

Presented to the Scottish Parliament and published pursuant to section 11(9) of the Public Finance and Accountability (Scotland) Act 2000

9 November 2006
For information in languages other than English or in alternative formats (for example Braille, large print, audio tape or various computer formats), please send your enquiry to Public Information Service, The Scottish Parliament, Edinburgh, EH99 1SP.
You can also contact us by fax (on 0131 348 5601) or by email (at sp.info@scottish.parliament.uk).
We welcome written correspondence in any language.
Scottish Commission for Public Audit

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9 November 2006
Scottish Commission for Public Audit

membership

Membership:
Margaret Jamieson (Convener)
Brian Monteith
Cathy Peattie
Margaret Smith
Andrew Welsh

Secretary to the Commission
Rosalind Wheeler

Assistant Secretary to the Commission:
Clare O'Neill

Audit Adviser:
Andy Munro
The Scottish Commission for Public Audit

1st Report, 2006 (Session 2)


The Commission reports to the Parliament as follows—

Introduction

1. The Commission took evidence on 27 September 2006 on Audit Scotland’s Annual Accounts and Report for the year to 31 March 2006, Audit Scotland’s budget proposals for the year 1 April 2007 to 31 March 2008 and the Autumn Budget Revision. The Commission took evidence from Robert Black, Auditor General for Scotland; Caroline Gardner, Deputy Auditor General for Scotland; Russell Frith, Director of Audit Strategy, Audit Scotland; and Diane McGiffen, Director of Corporate Services, Audit Scotland.

2. Further evidence was provided by Richard Gibson of Haines Watts CA, the external auditors of Audit Scotland. The Commission requested additional written information from Audit Scotland, which was provided by the Auditor General on 20 October 2006. The Commission thanks Audit Scotland and Haines Watts CA for their cooperation in providing evidence.

3. A report of the evidence session on 27 September 2006 can be found at Annexe A. Annexe A also contains a report of the meeting of the SCPA on 26 April 2006 where, amongst other things, the Commission took evidence on Audit Scotland’s Corporate Plan. Annexe B contains the submission received from Audit Scotland in advance of the evidence session on 27 September and their supplementary submission. Annexe C contains the minutes of both of these meetings.


4. In terms of section 11(9) of the Public Finance and Accountability (Scotland) Act 2000, the Scottish Commission for Public Audit (“the Commission”) must examine Audit Scotland’s proposals for its use of resources and expenditure for each financial year, and report on them to the Parliament.
5. Audit Scotland’s Total Net Expenditure for 2006-07 is £25,879,000. Its estimated income from charges to audited bodies is £19,294,000. The total resource requirements (expenditure which is payable out of the Scottish Consolidated Fund) for 2007-08 is £7,108,000: a net operating cost of £6,585,000 and capital of £523,000. (Table 1 in appendix 1 provides more detail on Audit Scotland’s resource requirements.)

6. Total resource requirements for 2007-08 represent a 3.0% increase on last year’s proposal and are based on a general price inflation assumption of 2.5%. The Auditor General informed the Commission that the difference can largely be attributed to increases in depreciation costs offset by decreases in employer’s pension contributions and reductions in a number of other corporate budgets.

Direct and in-direct costs

7. In response to a previous recommendation by the Commission, Audit Scotland has restated its allocation of direct and indirect costs (See Table 3). The statement is supplemented by explanatory notes outlining the basis of allocating each line of budgeted expenditure. The Commission acknowledges the efforts made by Audit Scotland in this regard and considers the level of detail provided in this clear format has aided the Commission’s scrutiny of the 2007-08 budget. The Commission recommends that this statement on direct and in-direct costs is prepared on an annual basis going forward to enable the Commission to better scrutinise Audit Scotland’s corporate costs and overheads.

Efficiency savings

8. The Auditor General advised that Audit Scotland has identified a number of efficiency savings and these have been included in the 2007/08 budget proposal. Efficiencies included in the budget proposal include a reduction of £160,000 in management costs arising from the departure of a member of the management team and the decision not to refill this post. An additional £75,000 in staff costs is proposed arising from the dissolution, and no requirement to separately audit, NHS Argyll and Clyde. Whilst the Commission acknowledges that the above are cash savings, it notes that these do not constitute ‘planned efficiency savings’, having arisen from unforeseen events out-with Audit Scotland’s direct control.

9. Reference was made to a number of planned cash releasing savings including: a decrease in recruitment costs arising from changes in the way Audit Scotland advertises for staff; and in training costs, due to the downsizing of a management development programme. The Auditor General made further reference to a number of other initiatives including efficiencies in the proportion of support staff to operational staff. The Deputy Auditor General has advised the Scottish Executive that efficiency savings should be defined in terms of measurement, methodology and eligibility. The Commission would recommend a similarly structured approach to Audit Scotland’s planned savings. The Commission recommends that, going forward, Audit Scotland provides a break down of targets for planned efficiency savings (analysed between cash releasing and time releasing).
Pension liabilities

10. In supplementary written evidence received on 21 September 2006, the Auditor General advised the Commission of a potential pension liability of £300,000 arising from former Scottish Commissioners (the Commissioner for Local Administration in Scotland, the Health Service Commissioner and the Scottish Parliamentary Commissioner for Administration). Prior to the establishment of the Public Services Ombudsman by statute in 2002, Audit Scotland provided administrative and back office services for the Ombudsman’s predecessors. Audit Scotland had assumed that the liability for pensions for former commissioners and a pension enhancement for one of their former staff members had transferred to the Scottish Public Services Ombudsman’s office post 2002 via the legislation establishing the new SPSO. However it has emerged that responsibility for former staff, (i.e. those who did not transfer to the Scottish Public Services Ombudsman following the legislative change in 2002) has remained as a liability to be met by Audit Scotland as the Scottish Public Services Ombudsman Act 2002 did not achieve the intended outcome of transferring liability to the SPSO.

11. Having identified this issue, the SPSO and Audit Scotland have jointly sought the opinion of Senior Counsel. The opinion expressed in the response, that liability falls with Audit Scotland, appears unequivocal. Audit Scotland have since written to the Scottish Executive asking it to consider the options for resolving the difficulty. The Auditor General outlined what he considered to be the options for action to resolve this matter stating:

“The options that seem to us to be open are: first, that the Scottish Executive agrees that we make an additional request for funding through the Scottish Commission for Public Audit; secondly, that the Scottish Executive assumes direct responsibility for the costs; or thirdly, that the Executive amends the legislation to transfer the legal liability to the ombudsman. Until we receive a response from the Scottish Executive on those three options—or on other options that we have not identified—it is difficult for me to advise further.”

12. The Commission considers that action from the Executive to resolve this issue is unlikely to be immediate and Audit Scotland do not appear to have any indication as to which of the options outlined above the Executive will take. Given the uncertainty as to when this situation will be resolved and what the outcome will be, the Commission is concerned that Audit Scotland has not accounted for this liability within its 2007-08 budget proposal. The Commission intends to take additional evidence from Audit Scotland in an attempt to resolve this issue, however, the Commission considers that reflecting this liability within the 2007-08 proposal would have constituted prudent financial management.

13. The Commission understands that the issue of this liability arose after the finalisation of the audit of Audit Scotland’s 2005/06 accounts by the external auditor. Indeed, Haines Watts were unaware of this issue until it was raised in evidence with Audit Scotland on 27 September when Haines Watts’ representative Richard Gibson was present. It does not constitute good practice for Haines Watts to learn of a £300,000 liability during a public evidence session as a result of a

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1 Letter from the Auditor General for Scotland to the Secretary, 21 September 2006
2 Report from the 2nd meeting of the SCPA, 27 September 2006
The Commission considers that it would have been appropriate for the Auditor General to have formally notified the external auditor as soon as he was aware that, according to independent legal advice, the £300,000 liability rested with Audit Scotland.

Annual Accounts and Report on Accounts for the year to 31 March 2006

14. In accordance with section 25(3) of the Public Finance and Accountability (Scotland) Act 2000, the Scottish Commission for Public Audit (“the Commission”) must receive a report on Audit Scotland’s accounts, together with a qualified auditors report.

15. During the evidence with Richard Gibson (Partner, Haines Watts CA) on 27 September, the Commission received assurances that he and his team had received all the information and explanations required by them to form their unqualified opinion on Audit Scotland’s annual accounts.

16. The Commission sought explanations from the Auditor General on a number of specific matters arising from the annual report and accounts on 27 September and these are outlined below.

Income from local authorities

17. The Commission sought further information on an apparent increase of 38%, year on year, in income from local authorities (from £9,619,000 in 2004/05 to £13,229,000 in 2005/06). The Auditor General has advised that this is entirely due to the timing of Audit Scotland’s business year versus its accounting year. The actual year on year increase in charges to local authorities in the 2005/06 business year was 3.5% which reflected inflation increases in Audit Scotland’s costs.

Salary increases

18. Audit Scotland reports that its five most senior staff members are in salaries bands of £5,000 (e.g. Salary between £70,000 and £75,000). The Commission noted that salaries for certain senior staff had increased by more than one salary band in the year from 2004/05 to 2005/06. The Auditor General reported that the average salary increase for the five senior staff reported in the period from 2004/05 to 2005/06 was 8.12%. The highest percentage increase year on year was 15.81% and the lowest 3.13%. The Auditor General advised that the increases recorded were largely due to an independent market salary benchmarking exercise undertaken during 2005.

Staffing levels

19. The Commission has previously noted a trend of year on year increases in Audit Scotland’s staff. The average number of staff directly employed by Audit Scotland during 2005/06 was 279, an increase of 5 posts from the previous year. During the evidence session on 27 September, the Deputy Auditor General advised that the staffing establishment of Audit Scotland was currently slightly higher than 279. The Auditor General added that the increased staff establishment was due to more efficient working arising from less use of consultancy and agency staff and more use of in-house staff.
20. In contrast to Audit Scotland’s establishing legislation, the Public Finance and Accountability (Scotland) Act 2000, which allows the Auditor General to appoint any necessary staff, certain commissioners and ombudsman are required to actively seek approval from the SPCB for additional staff. Whilst the Commission acknowledges the distinction between the roles of commissioners / ombudsman and Audit Scotland the Commission would appreciate being provided information which allows it to keep more of a watching brief on changes in Audit Scotland staffing levels.

21. The Commission recommends that, in the interest of good governance, the Auditor General should write to the Commission with notification of any proposed increase in Audit Scotland’s overall staffing complement and include details of the cost and justification of such an increase. The Commission would also appreciate similar information for any proposed staffing restructuring.

Conclusions

22. The Commission draws the Parliament’s attention to the observations made and recommends, on the basis that the Commission will pursue the pensions liability issue with Audit Scotland, that the bid for a budget of £7,108,000 for the year 2007/08 should be approved by the Parliament.
## Table 1: Summary of Audit Scotland’s resource requirements

<table>
<thead>
<tr>
<th>Summary of resource requirements</th>
<th>2007 ~ 08 £(000)</th>
<th>2006 ~ 07 £(000)</th>
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<tr>
<td>Accounts and governance</td>
<td>18,241</td>
<td>17,359</td>
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<tr>
<td>Performance audit</td>
<td>7,416</td>
<td>7,610</td>
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<tr>
<td>Other</td>
<td>222</td>
<td>222</td>
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<tr>
<td><strong>Total Net Expenditure</strong></td>
<td><strong>25,879</strong></td>
<td><strong>25,191</strong></td>
</tr>
<tr>
<td>Income from charges to audited bodies</td>
<td>19,294</td>
<td>18,798</td>
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<tr>
<td><strong>Net Operating Cost</strong></td>
<td><strong>6,585</strong></td>
<td><strong>6,393</strong></td>
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<tr>
<td>Capital</td>
<td>523</td>
<td>508</td>
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<td><strong>TOTAL RESOURCE REQUIREMENTS</strong></td>
<td><strong>7,108</strong></td>
<td><strong>6,901</strong></td>
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Appendix 1

Table 2: Subjective breakdown of Audit Scotland’s running costs

<table>
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<tr>
<th>2007-08 Budget</th>
<th>TOTAL (£000)</th>
<th>Local Government (£000)</th>
<th>NHS (£000)</th>
<th>Further Education (£000)</th>
<th>Scottish Executive (£000)</th>
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<tr>
<td>Accounts and governance</td>
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<td>8,669</td>
<td>3,768</td>
<td>525</td>
<td>5,279</td>
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<td>Performance audit</td>
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<td>1,456</td>
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<tr>
<td>Other</td>
<td>222</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Net Expenditure</strong></td>
<td>25,879</td>
<td>12,631</td>
<td>5,666</td>
<td>625</td>
<td>6,735</td>
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<tr>
<td>Income from charges to audited bodies</td>
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<td>(12,631)</td>
<td>(4,368)</td>
<td>(525)</td>
<td>(1,770)</td>
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<tr>
<td>Net operating cost</td>
<td>6,585</td>
<td>0</td>
<td>1,298</td>
<td>100</td>
<td>4,965</td>
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<th>2006-07 Budget</th>
<th>Total Net Expenditure (£000)</th>
<th>Local Government (£000)</th>
<th>NHS (£000)</th>
<th>Further Education (£000)</th>
<th>Scottish Executive (£000)</th>
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<tr>
<td>Income from charges to audited bodies</td>
<td>(18,798)</td>
<td>(12,311)</td>
<td>(4,351)</td>
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<td>Net operating cost</td>
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<td>1,050</td>
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### Table 3: Subjective breakdown of Audit Scotland’s running costs by cost classification (Direct / Indirect)

<table>
<thead>
<tr>
<th>Cost Category</th>
<th>2007 ~ 08 Direct £(000)</th>
<th>2006 ~ 07 Direct £(000)</th>
<th>2007 ~ 08 Indirect £(000)</th>
<th>2006 ~ 07 Indirect £(000)</th>
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<td><strong>Employees:</strong></td>
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<tr>
<td>Salaries and temporary staff</td>
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<td>10,815</td>
<td>9,527</td>
<td>9,352</td>
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<td>Employer's oncosts</td>
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<td>3,059</td>
<td>2,393</td>
<td>2,645</td>
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<td><strong>Total employee costs</strong></td>
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<td>13,874</td>
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<td>Performance audit and other consultancy</td>
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<td>Training and development</td>
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<td>561</td>
<td>444</td>
<td>485</td>
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<td>Travel and subsistence</td>
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<td>846</td>
<td>833</td>
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<tr>
<td>Recruitment &amp; Other Staff Costs</td>
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<td>265</td>
<td>268</td>
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<td>Professional Subscriptions</td>
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<tr>
<td>Depreciation</td>
<td>610</td>
<td>319</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Cost of capital</td>
<td>50</td>
<td>20</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Audit Scotland expenditure</strong></td>
<td>25,913</td>
<td>25,285</td>
<td>20,272</td>
<td>19,800</td>
</tr>
<tr>
<td>Accounts Commission costs</td>
<td>157</td>
<td>159</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Sundry income</td>
<td>(215)</td>
<td>(253)</td>
<td>-100</td>
<td>-138</td>
</tr>
<tr>
<td><strong>Total Net Expenditure</strong></td>
<td>25,855</td>
<td>25,191</td>
<td>20,172</td>
<td>19,662</td>
</tr>
</tbody>
</table>
Appendix 1

Notes to Table 3

Basis of allocating direct and indirect costs

Direct and Indirect costs can be apportioned in many different ways depending on the nature of the business and the purpose for which the analysis is required. The essential requirement is to enable comparison between years.

The analysis in the table is based on apportioning costs based on the nature of the cost or on the type of work being undertaken.

Staff costs, training and development and professional subscriptions are apportioned on the basis of headcount. Those staff working in the Audit Services Group (planning, delivering and reporting annual audits of audited bodies), Performance Audit Group (planning, delivering and reporting national performance audit studies and best value audits) and Audit Strategy Group (supporting auditors with professional guidance) are regarded as direct costs. Those staff working in the Corporate Services Group (HR, Finance, Information Systems, Communications and Office Services) are treated as indirect costs.

Other categories of costs are allocated as direct or indirect based on their type or, in the case of performance and other consultancy, allocated according to the purpose of the expense eg consultancy to support national studies is treated as a direct cost whereas corporate legal fees are treated as indirect.

In previous years the analysis was presented between the different parts of Audit Scotland and analysed certain costs such as premises, IT and depreciation according to the type of activity being supported. The 2006/07 figures have been restated on the new basis of allocation.
Item in Private

The Convener (Margaret Jamieson): Good morning. I welcome everyone to this meeting of the Scottish Commission for Public Audit. I realise that I am opening the meeting five minutes early, but I can do that because the SCPA is not seen as an official committee of the Parliament. I ask everyone to switch off mobile phones, pagers and so on, and I welcome to the meeting Richard Gibson from Haines Watt. We have received apologies from Cathy Peattie and from Margaret Smith, who is unwell.

Under agenda item 1, I seek members’ agreement to take in private agenda item 6 in order to consider the evidence that we will take at this morning’s meeting. Are members agreed?

Members indicated agreement.

Mr Andrew Welsh (Angus) (SNP): The report quotes the NAO’s 2006 corporate plan, which says:

“the National Audit Office is committed to reducing annual costs by over £1.3 million over the four years to 2008-9”.

How difficult is such a target to meet? What would be the equivalent in Scotland?

The Convener: As we did not look into that matter, we cannot really give you that information.

Mr Welsh: The report points out that the NAO has achieved a saving of £8 for every pound of net expenditure. Was there a reason for adopting that particular ratio?

The Convener: I do not think that it is a question of adopting such a position. The NAO has found itself in that position as a result of the various peer reviews and the external review that have been undertaken. Indeed, I believe that the figure is being changed.

Mr Welsh: I see that in 2007 it will go up to £9 for every pound spent.

The Convener: Indeed. You should also understand that the departments and budgets that the NAO examines are much larger than those under examination in Scotland.

Do members agree to note the conclusions in paragraphs 14 and 15 of the paper?

Members indicated agreement.
Accounts 2005-06

10:15

The Convener: Agenda item 3 is the first of our two evidence-taking sessions this morning. I welcome the Auditor General for Scotland, Robert Black; Russell Frith, director of audit strategy in Audit Scotland; and Diane McGiffen, director of corporate services in Audit Scotland. They will give evidence on Audit Scotland’s annual accounts and report on accounts for the year to 31 March 2006.

I invite Mr Black to make a short opening statement.

Mr Robert Black (Auditor General for Scotland): Thank you, convener. I should point out that Caroline Gardner has kindly agreed to come along and help me.

It is a pleasure to bring to the commission Audit Scotland’s annual report, which outlines our progress under our three corporate priorities. I believe that those priorities, having been set out in our corporate plan, are well known to the commission and to the Parliament’s Audit Committee. They are, first, to support effective democratic scrutiny, which is, in effect, the work of the Parliament; secondly, to maximise the value of audit—because, after all, we account for a significant amount of public spending; and, thirdly, to build an efficient and effective organisation.

Over the past year, we have made significant progress in delivering an audit regime that is valued by the audited bodies and useful to the Parliament. As we are still a comparatively young organisation, we continue to develop. Our twin aims continue to be to hold public bodies independently to account, which is our core aim, and to use Audit Scotland’s expertise and knowledge to continue to improve the services that those bodies deliver. We have made real progress in achieving those goals. For example, as the commission knows, the largest amount of our resource is spent on auditing all the public bodies in Scotland. Indeed, Audit Scotland interacts with roughly 200 public bodies.

In 2005-06, we rolled out our modernised audit approach completely across the health service and piloted it in both local government and central Government. We continue to look for ways of improving the new audit model, which I venture to suggest is a pioneering approach not only in the United Kingdom but in a much wider context. So far, the audited bodies, particularly those in the health service where the model has been rolled out most fully, have responded positively to the model, and our annual report contains information on how we are maximising the value of audit through the process.

This year, we have responded to suggestions that were made by the Audit Committee—and, indeed, by the commission in earlier days—that we should provide some examples of good work that we have found in public services. We have attempted to summarise and include some examples of that in the annual report. I have absolutely no doubt that with our unique and independent insight into all public bodies we are well placed to identify what works best and to encourage the roll-out of such practice to the rest of the public sector. Public bodies have been responsive in that respect. Because the reports that I present to Parliament must be strategic, we do not always have the opportunity to reflect on our positive engagement with the audited bodies, but that is a great strength of the current audit regime in Scotland.

The SCPA is concerned, quite rightly, with the costs of our work. We strive to keep the costs of audit down. Indeed, since Audit Scotland’s inception, I have avoided coming to the commission to ask for a significant increase in resources other than those that are needed to support new burdens such as the introduction of best value, the establishment of Transport Scotland and taking over responsibility for auditing further education colleges and Scottish Water. I should also point out that, although it is right for the commission to scrutinise it, our annual expenditure remains at significantly less than 0.1 per cent of the public expenditure that we audit.

We must keep challenging ourselves to deliver public audit more efficiently and effectively and, as we have attempted to itemise in the report, we have responded to the challenge of best value in our organisation. We are certainly making progress in that area and we are happy to answer the commission’s questions in that regard. We will continue in that direction, which was, after all, set out clearly in the corporate plan that we produced earlier this year and which we had the pleasure of discussing at the previous SCPA meeting.

I want to capture some highlights of our work over the past year to show what the public and the Parliament are getting for their investment in Audit Scotland. The local government best-value regime has now been fully rolled out and, in 2005-06, there were eight best-value audit reports on eight Scottish councils. Moreover, 38 performance audit reports and 196 annual audit reports on Scottish public bodies were produced. The Parliament tends not to have direct sight of those reports but, through the offices of Audit Scotland, I draw on them to compile my reports to Parliament. I am satisfied that the quality of the work in the reports is improving steadily and that the work is valued more and more by the audited bodies.

Last year, we concluded the national fraud
initiative, which was conducted for all local authorities and through which we identified £15 million of overpayments and savings. As I pointed out recently to the Finance Committee, that alone is well over twice the resources that we call for from the Parliament—it is a significant sum.

Last year, we published integrated overview reports on the national health service and local government. The Audit Committee appreciated receiving the NHS overview report, which was taken to a new level last year, because we reported in an integrated way on the overall performance of the health service in Scotland as well as on its use of resources. Generally, the report was seen as a significant contribution to holding the health service to account. Such a report could not be produced without the detailed audit work that is done on the health bodies in Scotland, which allows us to build up a consistent national picture.

This year, we will extend the overview reporting. Later this week, we will lay before the Parliament an overview of the transport budget that will cover all transport spending in Scotland and give a description of the performance for all transport activity.

A significant achievement last year was the successful procurement process to appoint five firms to work with us for the next five years in undertaking the audit of public bodies.

That is a brief overview, but my colleagues and I are happy to answer any questions that the commission may have.

**The Convener:** I thank Robert Black for that introduction. I apologise to Caroline Gardner—I understood that she was here only for agenda item 4. She is welcome to chip in.

The income that you have received from local authorities has increased significantly. Is that all as a result of additional work that you have undertaken, for instance on best value?

**Mr Black:** Russell Frith will help you with that.

**Russell Frith (Audit Scotland):** The increase is a result of a combination of factors. The main factor during 2005-06 was that, following the reorganisation of the in-house audit teams during 2004-05, the teams made more progress in completing the audits during 2005-06, which means that they earned more income. The amount of income that is earned depends primarily on the stage of completion of audits at 31 March, which is our financial year-end. In 2006, the local government teams were considerably further advanced in their audits than they were at the same date the previous year. The teams did about 109 per cent of a year’s work in that year—they caught up.

**The Convener:** Obviously, that adds to the local authorities’ burden.

**Russell Frith:** No, it does not. We charge local authorities an agreed fee for the audits, irrespective of the period over which the audits take place. We agree the fee for the audits of the financial statements for a given year. Some of the work is done before the end of March and some is done after that; if the proportion changes from year to year, that does not affect the amount that we charge local authorities, but it affects the way in which our income is set out in our accounts, under the resource accounting rules.

**Mr Black:** I will build on Russell Frith’s comments. I remind the commission of our business cycle versus the financial cycle. This summer, we had to estimate the cost of the audits that start in early November and run through to the following October. That is broadly the timescale for the audits for the financial year 2006-07. In putting together the budget, we must try to anticipate how much work will be concluded this year and how much will go over into next year. We also need to think beyond November to the spring of 2008, because the auditors will then start the work for the audits of the next financial year, which will start in the autumn.

There is always volatility in the area. Russell Frith referred to a significant improvement in audit performance and a significant improvement on the part of local government in presenting good accounts in a timely way for the auditors to examine. We are succeeding in bringing forward the timetable for undertaking the audits of local authorities. That is a benefit of the modernised audit approach that I mentioned in my introductory remarks. I see it as a productivity and efficiency gain that we are doing the work more quickly, but it means that for our budget we have the somewhat artificial cut-off date of 31 March, when we are just part way through the work.

**The Convener:** Russell Frith indicated that there had been a 9 per cent increase in productivity. That does not equate to the 38 per cent increase in fees that has been charged.

**Russell Frith:** Not entirely, but the 2005 figure was lower than it might have been. I said that 109 per cent of a year’s worth of work was done in 2005-06, but 100 per cent of a year’s worth of work was not done in 2004-05. Largely because of the reorganisation of teams, the auditors slipped back. In 2004-05, only 94 or 95 per cent of a year’s worth of work was done.

**Mr Black:** The auditors underdelivered last year and overdelivered this year.

**The Convener:** The increase still does not add up to 38 per cent.
Mr Black: Russell Frith will have to help you with the detailed figures.

The Convener: He may not have that information to hand. I would be happy for him to provide it to us in writing at a later date—although not too late, because we are trying to keep to a tight timetable.

Mr Brian Monteith (Mid Scotland and Fife) (Ind): Page 23 of the remuneration report shows the salary bands of senior management. Although the range of bands is not listed, it appears from the information given that some senior staff are going through two salary bands as a result of the change in remuneration. Is that the case? How do the salary increases of Audit Scotland’s senior staff compare with those of other Audit Scotland staff?

Mr Black: You asked two questions, the first of which was about banding. In 2004-05, there were five people in the senior management category. In 2005-06, there are nine, and in 2006-07, there will be seven. The change is due largely to the fact that the fixed-point salaries of staff straddle the salary bands. If someone is at the top of one band, they tend to move to the bottom of the next band.

The second question was about how salaries are determined. As I may have advised the committee in the past, the terms and conditions of the bulk of our staff mirror those of staff in local government. The local government settlement tends to drive the salaries of the great majority of our staff. The most senior staff are on fixed-point salaries. There is an element of job sizing and performance rewarding. We set an overall ceiling on the amount of money that is available to remunerate our senior staff. With the approval of the Audit Scotland board, I determine what the salary point for those individuals should be. We cap the total amount very tightly, broadly having regard to the uplift for main-grade staff.

Mr Monteith: Would it be possible for you to provide written evidence on the year-on-year percentage pay awards?

Mr Black: We certainly have that information. Individual members of the senior staff are moved through the pay bands at different rates. The system that I operate at Audit Scotland is that I do not believe it is necessary for each colleague to know exactly what other colleagues are being paid, so, although I am absolutely committed to transparency, I am not sure that it would be helpful to give you full details of the remuneration of each individual person.

10:30

Mr Monteith: We understand that.

Mr Black: However, if you would like some aggregated information, we can certainly provide that.

Mr Monteith: Thank you.

Mr Welsh: Do the advertised jobs in your performance audit group represent an increase in your overall staff complement beyond 279?

Mr Black: No. The number of staff in the establishment remains at 279 and the posts that are advertised are within that.

Last time we discussed the matter, I assured you that the number of staff was around the 270 mark—I think that that is what I said. In fact, it was 274. The number has gone up slightly because of more efficient working. We are using consultancy and agency staff less and using our own staff more. By and large, the establishment is now stable at 279 posts.

Caroline Gardner will expand on that general comment.

Caroline Gardner (Audit Scotland): We are advertising the posts to replace members of staff who have left to take up other career opportunities. At Audit Scotland, we are proud of the number of staff who move on to more significant, wider roles elsewhere. We think that that is a good sign of how we are doing. Having said that, the number of staff in the establishment is currently slightly higher than 279. The increase is at the margins, but the number is slightly up. As Bob Black said, we made a couple of adjustments to our staffing arrangements that make us more efficient but have the effect of slightly increasing our head count.

An example is that a significant proportion of our performance audit work used to be done via the firms and the audit services teams that carry out the audit appointments of the 200 bodies that Bob Black mentioned. We brought some of that resource in house because we found that we can do the work more consistently and to a higher standard. That involved converting some of the money into posts. We made a saving by doing that, but it converts into a small increase in head count, which will be seen when we consider this year’s annual report at the end of 2007.

Mr Welsh: Audit Scotland deals with a vast range of work and there seems to be an ever-increasing demand for your services. That is a measure of your success so far. However, is there a danger of overstretch? What do you consider as being your establishment of staff?

Mr Black: There is a risk of overstretch, in the sense that we have been through a significant change management exercise during the past few years. As I mentioned, the larger part of our resource is devoted to delivering the audit of public bodies. In the past, I have described to the
From the beginning, we review its financial audit practice on an annual basis? Audit Scotland employ an external body to peer underlie everything that Audit Scotland does. Does quality must maintain the quality of what you do. Quality must skilful level in their engagement with the auditor bodies.

I compare the modernised audit approach with the situation many years ago, when the core work comprised providing certificates on accounts and a limited level of assurance. We now ask the staff to do a lot more, but that is reasonable because they are highly expert and fully qualified and I find that they are rising to the challenge. The judgment to be made in management is how much change one can drive through an organisation at one time. I am confident that, through the good leadership of my colleagues, we are managing to keep that balance pretty well in relation to the modernised audit.

The second area of risk is in the bedding in of the best-value regime in local government. We are asking Audit Scotland staff to look in the round at the performance of all local authority activities. Across the piece, that has been a highly successful innovation. Caroline Gardner and I, and Alastair MacNish, who is the chair of the Accounts Commission, met representatives of the Society of Local Authority Chief Executives and Senior Managers earlier in the summer. The local authority chief executives acknowledged that the regime was appropriate and fit for purpose; generally, they gave it their full support. That is a development of traditional audit and a new type of activity for auditors to undertake.

Thirdly, producing documents such as the overview in the NHS, which considers all aspects of performance and financial control, is much more challenging for professional staff than what was done in years gone by. There are risks, but we think that we are managing them reasonably effectively.

Mr Welsh: Adequate staffing is important to maintain the quality of what you do. Quality must underlie everything that Audit Scotland does. Does Audit Scotland employ an external body to peer review its financial audit practice on an annual basis?

Mr Black: The short answer is no, but it might be helpful if we were to give a description of how we quality assure the work. I am conscious of the fact that the commission has been informed by the visit that the convener and members paid to London to interact with the National Audit Office. However, some features of the work that we do in Scotland are distinctive.

First, we are a new organisation. It has been a pleasure and a privilege to be able to think from first principles about how we do our work. Audit Scotland’s structure is different from that of the NAO. In Audit Scotland, we have got—I will use shorthand language—the provider activity, which Caroline Gardner leads as the deputy auditor general for Scotland and which does all the work. Russell Frith, as director of audit strategy, is independent of that. He sits at my right hand to oversee all the quality work that we do in the organisation. That is different from what happens in the NAO—it would be rather like Sir John Bourn having an independent unit sitting alongside him that was somewhat at arm’s length from the delivery wing of the NAO. It is important that I maintain that distinction and that Russell Frith’s accountability is directly to me and to the Accounts Commission. Russell Frith prepares reports on the quality and performance of all our auditors, in house and external, directly to the Accounts Commission and to me. The Accounts Commission and I sit together in a committee—the financial audit and assurance committee—to oversee that work.

Secondly, the audit that we do is wider in scope than the audit that is undertaken in the private sector. If we were simply to apply the quality assurance systems that the accountancy profession applies to private sector audits, we would be selling short. We have got a more comprehensive quality assurance system than is the case in the accountancy profession.

The third element that is different is the amount of work that we put out to the firms. About 37 per cent of the work is done by the five firms that I mentioned earlier. That provides an independent check and balance, which Russell Frith can use to assess the quality of Audit Scotland’s work against the firms’ work and the firms’ work against Audit Scotland’s work. We find that that provides a healthy constructive tension, shall we say, to control the quality of what is achieved.

Fourthly, when we undertake the design and implementation of quality review systems, we involve people from the private sector. Senior people from the private sector frequently work with Russell Frith on the design, updating and implementation of the quality assurance process.

That gives you a general picture of where we are with quality assurance. As the performance audit work has developed, we have sought to apply the same rigour to quality assurance as is applied to the performance audit work. Russell Frith is engaging with Caroline Gardner on that.

It might be helpful if Caroline Gardner were to give you a brief picture of how things operate in relation to performance audit to ensure that the quality of studies is assured.

Caroline Gardner: From the beginning, we
have tried to build in a degree of external challenge in both the agreement of the overall programme that we undertake and the individual studies as they are performed. Members will be aware from the Audit Committee’s recent work on the matter that we consult on the overall programme for both the Auditor General for Scotland and the Accounts Commission on roughly a two-year basis. The consultation ranges widely. The aim is to test our thinking about the key issues that we might wish to consider and to ask people to identify issues that we might have missed, which could be high priorities for us to work on. That informs the agreement of a shared programme by the Accounts Commission and the Auditor General, which takes us over an 18-month period.

Once that programme has been agreed, the teams go through the application of a well-established project management framework for each of the topics that we intend to take forward. That is based on the work of what we call an external study advisory group, which brings together eight to 10 people, typically, from across the range of interests that is affected by a particular study. For the study that is under way on the social work and health care that are provided to people with long-term conditions, we take into consideration the professionals involved, the health service managers, the social work departments, the voluntary organisations that provide services, the carers and the people who suffer from the conditions in order to ensure that the right issues are identified for the study and that our proposed methodology is the right one for getting under the skin of the issues. Finally, we test the findings and recommendations that we make at the end.

We think that bedding in the external challenge all the way through the study process is a strong way to ensure that we think widely about the right issues and that we are not captured by any particular professional orientation, including our own as finance people and researchers, and to ensure that whatever emerges at the other end is practical and grounded in real-world improvements.

Mr Welsh: Thank you for that detailed answer.

As regards assessing the impact of audit, I believe that you have been working with other audit agencies through the public audit forum. What review practices is Audit Scotland considering adopting as a result of its work with that forum?

Mr Black: Diane McGiffen is leading that work on behalf of Audit Scotland, so she is best placed to give you a full answer.

Ms Diane McGiffen (Audit Scotland): Over the summer, we worked with members of the public audit forum representing all the United Kingdom audit agencies. That has resulted in a paper to the forum, setting out high-level principles of a framework that all the audit agencies might consider adopting and below which they can build their own suites of measures for assessing the impact of audit.

As well as that work at national level, we have been piloting some new methods for ourselves over the summer for following up on the impact of our study programme. We considered three reports that had been completed between one and two years ago, and we tried different methods of following up the studies, using existing information rather than conducting a full follow-up study, which would obviously have resource implications. From those three exercises, we found a number of actions and activities that we can undertake and build into our routine work to ensure that we systematically follow up the output from our reports and the recommendations that have been implemented. We have built that into our project management framework so that, as a study ends, the way in which we assess its impact on an ongoing basis will be fleshed out. We will not use the same method for every study, because the method will need to be appropriate to the sort of issue that we are looking at.

However, even in the work that we undertook over the summer, we found some efficient ways of being able to demonstrate follow-up. One of the issues to emerge from that work was the length of time that we need to allow between the publication of a study and a full assessment of impact being made. That will vary by study but, in some cases, a minimum of two years seems to be required to gauge the total range of activity. Beyond two years, there are risks for us in assessing impact, because many other factors will have changed in the environment that public sector organisations are working in.

We have done some quite detailed work that has resulted in revisions to our project management framework for performance audit studies. We will be able to report in detail across the range of historical studies that we have done and summarise that information at a point that is appropriate for the sort of recommendations that a particular study was looking at.

10:45

Mr Welsh: Thank you. You have again illustrated the complexity in the timescales and the range of Audit Scotland’s activities.

Does Audit Scotland employ an external body to peer review its value-for-money work in a similar fashion to, for example, the NAO?
Caroline Gardner: We do not use the same method as the NAO. I have described the way in which our project management framework includes external challenge all the way through. At the moment, the approach that we have taken to looking at impacts afterwards is as Diane McGiffen described, with a formal stage in the project management framework at which people are asked to identify the measures of change that we expect to see and to specify how they will follow them up in the future. We do not use the sort of external review that the NAO has in place.

The Convener: Thank you for your evidence.

I ask Richard Gibson to confirm that Haines Watts has received all the necessary information and explanations to inform its opinion on the accounts and to provide an overview of any observations arising from its work.

Richard Gibson (Haines Watts): Yes; I confirm that we received all the information and explanations that we required to undertake our audit. Haines Watts was appointed by competitive tender this year, and this is the first time that we have reported to the commission.

There are two main requirements of Haines Watts. The first is to provide an audit opinion, which you will see on pages 47 and 48 of your accounts. I am pleased to say that that is an unqualified audit report, as you would expect. The second requirement is to provide you with a report to management—a management letter, as we tend to call it in the industry—which is an overview of our findings and recommendations for improvements in the systems. That document has not yet been finalised but will be with you for your meeting in November. There is absolutely nothing in that document that should concern the commission. I suggest that, when you get the report in November, it will be simply a case of noting its contents and approving it.

It is fair to say that, for our first year, the conduct of the audit went very smoothly. Despite the fact that we were new to the job and the fact that new financial reporting guidelines were introduced, the job went very well—thanks, in significant part, to the efforts of the staff of Audit Scotland. I am very grateful to them for their help. We are happy with the way that the audit went.

The Convener: Why do we have to wait until November for the management letter?

Richard Gibson: That is the next time that the commission will meet. The management letter has been discussed with staff at Audit Scotland, and it is now simply a case of signing off the letter and submitting it to you. That has not been done yet. I apologise for that. It should probably be with you just now.
Budget Proposals 2007-08 and Autumn Budget Revision

10:50

The Convener: Item 4 is Audit Scotland’s budget proposal for 2007-08 and the autumn budget revision. Caroline Gardner has been identified as giving evidence. I ask Andrew Welsh to kick off questions.

Mr Welsh: Which aspects of the budget bid hold the greatest uncertainty in estimating required funds?

Mr Black: Probably the estimation of how far through the work the auditors will be by the end of the financial year. However, it is a good question on which I will ask Russell Frith, who is closely involved in the budget preparation, to speak.

Russell Frith: The Auditor General got it absolutely right: the biggest volatility in our budget versus outturn in any year is the level of audit activity in that year. Where firms are involved in carrying out the work, the bottom line of the audit is neutral, because the income matches the expenditure that we incur. However, we incur staff costs with our in-house teams, so there is vulnerability to changes in audit activity.

Mr Welsh: How tight are the budgets? I note that some budgets have been reduced. What effect will that have on staff in programmes? What allowance do you make for unforeseen circumstances?

Mr Black: As we have discussed previously with the commission, Mr Welsh, I am reluctant to impose a top-down target for an efficiency saving. As we have attempted to describe in the various papers that we have given you, we take a best-value approach that considers the actual spend in different parts of our activity and the burden going forward, and scrutinises the budget for efficiency savings that we can deliver. You will find in the various papers examples of how we do that.

As we get to know our business better and bed in our new financial management system, we are becoming more efficient at managing our resources. We have a good fit between our request for resources and our knowledge of the spend that we are likely to incur. However, as Russell Frith and I have indicated, we are similar to a business in the sense that our income and spending over a short period can fluctuate, depending on the volume of activity, so we must watch our cash flow. Every year at the year end, it is fair to say that I am obsessed with ensuring that we do not overspend on the budget, not because of loss of control, but simply because of the work going at a faster rate than we have resources to cover. That is the big risk area, but we understand the costs pretty well now in Audit Scotland.

Mr Monteith: I will pick up on efficiency savings, which the Auditor General touched on. Your supplementary written evidence shows that for the 2007-08 budget the corporate services group will receive a budget reduction of £115,000 and other budgets will be reduced by £250,000. You will also make a reduction of £160,000 in senior management costs. Those reductions equate to 2 per cent of total Audit Scotland expenditure. Do the cuts to budgets outlined in the 2007-08 budget reflect efficiency savings that were made in 2005-06 and that are anticipated for 2006-07? If so, how have such efficiency savings been achieved?

Mr Black: The answer takes us down into quite a level of detail. Although sums such as £115,000 are significant, if we break them down we end up talking about quite small sums of money. I will need to call upon Diane McGiffen and Russell Frith to help us with our understanding of that. However, in answer to your general question, yes, these are efficiency savings that are being driven out this year and next year.

It is important that we bear in mind the fact that efficiency is about not only cost reduction but productivity and output. For example, in corporate services, between 2002-03 and 2005-06 the ratio of our personnel staff—I think that they are called human resources staff in modern language—to other staff has moved from 1:56 to 1:70. Similarly, the ratio of information technology team members to other staff has moved from 1:45 to 1:56. We are accommodating growth in the volume of activity in Audit Scotland, which has been significant over that period. Staff increases would have been necessary to deliver things such as best value, but we are delivering it with the same core staff in corporate services by training and skilling them to operate more effectively and by introducing better IT such as the new financial management system that I mentioned earlier.

You asked about what comprises the various elements of the budget reductions. I ask Russell Frith to talk about that and invite Diane McGiffen to provide further amplification.

Russell Frith: The £160,000 saving in management costs is a result of a deliberate decision not to replace the managing director of the audit services group after the post was vacated. We are cutting the amount of senior management in the organisation. That is a direct efficiency measure.

In our budget proposal we mention that we will be reducing the cost of NHS audit by £75,000 as a result of the abolition of NHS Argyll and Clyde and its merger with NHS Highland and NHS Greater Glasgow. That efficiency saving is reflected in a reduction in staff numbers in the audit services
In corporate services, we have reduced the budget for training and recruitment. The training budget has been reduced because, during the current year, we have a significant push on our management development programme. Although that programme will carry on into 2007-08, we anticipate that it will not be at the same level of cost.

**Ms McGiffen:** Within corporate services, the other area of reduction is recruitment. That is a result of reviewing our recruitment activity last year, appointing new partners to work with us on recruitment, examining the opportunities to generate savings when we advertise by making greater use of the internet and developing more sophisticated advertising that uses less print space and provides more information online. The big cost in recruitment advertising is placing adverts in newspapers. We are examining more effective ways of doing that.

We need to use our money effectively with regard to recruitment. Obviously, it is important that we attract a high calibre of staff. We are in a competitive market, given the existence of the financial services sector in Edinburgh. However, through our new partnership arrangements, we can deliver a quality recruitment strategy more efficiently. We are also taking into account the fact that the growth in the organisation will stabilise so, with the exception of vacancies arising from turnover, we do not expect to be recruiting as heavily as when the organisation started up.

We will always advertise annually for graduate trainees to join our graduate training scheme—I think that we discussed that at our meeting in April—which means that we will always have to invest in recruitment and training. The savings in recruitment are a combination of a new working arrangement following a review, new partners and new methods of recruitment, as well as our having planned for expected lower levels of activity relating to where we are in our organisational cycle.

11:00

**Mr Monteith:** You touched on the issue of productivity. If possible, could you put a figure on the proportion of savings that are cash-releasing and the proportion that are time-releasing? That would be helpful to us, although you do not have to provide that information today.

**Mr Black:** We will do our best to answer that.

**Mr Monteith:** I want to pick up on the item in your letter of 21 September about potential liability for former ombudsman pensions. Will you expand on that for us? It is fair to say that we are intrigued that “the Act attempted to transfer all assets and liabilities”.

Why did the ombudsman seek legal advice? It would be interesting to know if that is an opinion or advice that has not been qualified. What stage is the situation at? You have told us that Audit Scotland has not made allowance for the £300,000 liability. Why is that and might it change? If liability was meant to have been transferred to the Scottish public services ombudsman, one would expect that office to have a liability that might go unused. Will arrangements be made for the transfer of that sum from one organisation to the other, if that is not ultra vires?

**Mr Black:** It might help the commission’s understanding if I paint a bit of the background. The former local government ombudsman for Scotland was established in 1975. The legislation provided that the support services should be supplied by a designated body to avoid unnecessary duplication in establishing separate support services for the local government ombudsman service, so the issue of the efficiency of such bodies has been around for some time. At that time, it was decided that the designated body would be the Accounts Commission for Scotland. Thereafter, the commission met the expenses of the local government ombudsman service and recovered the costs from local authorities. Clearly, the old Accounts Commission used to recover its fees in that way, so it made for a streamlined recovery process. That all seemed to be in the interests of efficient government.

We then roll forward to 2000, when Audit Scotland was created and the statutory arrangement for and the powers of the Accounts Commission were significantly altered. The support services for which the Accounts Commission was responsible were transferred to Audit Scotland as the provider body. Audit Scotland therefore inherited all the duties and obligations of the former Accounts Commission and became the designated body for a period of time. We then roll forward again to the creation of the unified ombudsman service under the Scottish Public Services Ombudsman Act 2002, when Audit Scotland ceased to provide the support services. Audit Scotland has always taken the view that the Scottish Public Services Ombudsman Act 2002 intended that the previous liabilities for the constituent ombudsman services would be transferred to the new ombudsman.

As Mr Monteith’s remark indicated, it appears that the legislation did not have that effect in relation to one of the liabilities of the former local government ombudsman. The legal opinion offered to Audit Scotland was that the intention of the legislation was to transfer that liability, so we did not readily accede to the opinion that came late in the day from the SPSO’s office that there
was no legal provision for the transfer of that liability. To resolve the situation, we jointly sought the opinion of Queen’s counsel, who gave a clear view that what we understood was the intent of the legislation was not actually present in statute, therefore we are left with the liability.

I should say that although the pension liability rests with us, the financial benefit of the post no longer being of the establishment rests with the Scottish public services ombudsman. In effect, there is a lack of equity in how the issue has been treated.

The secretary to the Audit Scotland board has now written to the Scottish Executive asking it to consider the options for resolving the difficulty. Until we have a response, I do not think that it is appropriate to include a provision in our budget request, but it is right for the commission to be aware that it is an outstanding issue.

Mr Monteith: Was any provision made for the liability in other budgets?

Mr Black: To the best of our knowledge, no.

The Convener: Could I pick up on that? You said that you jointly sought QC opinion. When was that?

Mr Black: It was very recently—over the summer.

Russell Frith: The QC’s opinion was received only in August this year.

The Convener: Did you raise the liability with Haines Watts in preparing the accounts or prior to today’s meeting? Is the issue new to it as well?

Russell Frith: No, we did not raise it with Haines Watts. At the time, we were acting on our own legal opinion, which was that there was no liability.

The Convener: Would it not have been prudent to indicate that there was a possible conflict?

Mr Black: No, that would have been inappropriate, because we did not recognise that there was an obligation on Audit Scotland.

The Convener: You said that you have written to the Scottish Executive. To which department have you written and is it possible for us to have a copy of your correspondence?

Mr Black: We have written to the public services group in the Finance and Central Services Department of the Scottish Executive, and you are welcome to a copy of the letter, which is dated 7 September.

The Convener: My other question is, has the issue been flagged up to the Scottish Parliamentary Corporate Body, which provides funds to Audit Scotland and the Scottish public services ombudsman?

Mr Black: We see it as a matter for the Scottish Executive to resolve, as we have no formal jurisdiction over the ombudsman. We have therefore suggested in our letter that the Executive might want to pursue the matter. We will have to await a response to see how it is resolved.

The Convener: There is a £300,000 liability. Whether that is deemed to be for Audit Scotland or the ombudsman, the money has to come out of the top-slicing of the consolidated fund.

Mr Black: Yes. I would not wish to leave you with the impression that the liability would necessarily fall to be a burden met by the Scottish Parliamentary Corporate Body. The legal opinion from Queen’s counsel is that the liability falls to be met by Audit Scotland. There is currently no legal duty on the corporate body to make allowance for that.

The options that seem to us to be open are: first, that the Scottish Executive agrees that we make an additional request for funding through the Scottish Commission for Public Audit; secondly, that the Scottish Executive assumes direct responsibility for the costs; or thirdly, that the Executive amends the legislation to transfer the legal liability to the ombudsman. Until we receive a response from the Scottish Executive on those three options—or on other options that we have not identified—it is difficult for me to advise further.

Russell Frith: I would like to add one point on why we did not feel that there was any liability on Audit Scotland. When it was formed, the Scottish public services ombudsman made payments relating to liability annually. The issue only came up once the ombudsman had to produce full accruals accounts as opposed to the cash accounts it produced in the early years.

The Convener: That is interesting. Thank you.

I turn now to the autumn budget revision. We note that you plan to apply the 2005-06 underspend to reduce audit charges and to support a number of other issues, including £130,000 for the 2006 national fraud initiative and £130,000 for the development of best value outwith local government. What targets have been set for that additional spending?

Mr Black: I think that the targets are the amounts that we have recorded in our paper. For the national fraud initiative, the £130,000 relates to the costs that have been incurred in our past experience. Similarly, for best value, we feel a need to apply a resource to develop the best-value regime in the rest of the public sector. Those comparatively small sums will allow us to do what we want to do. I invite Russell Frith to comment further on the national fraud initiative and Caroline
Gardner to comment on best value.

Russell Frith: The £130,000 for the national fraud initiative represents the cost that we will pay to the Audit Commission for the handling and processing of all the data. This time, it will cover not only local government bodies but NHS boards, so it represents an expansion on the previous exercise.

As I said in evidence to the Audit Committee on the 2004 national fraud initiative exercise, whether the next exercise shows higher or lower savings is not a determinant of whether the exercise is more successful or less successful. There should be a deterrent effect, so I would not necessarily expect to see a significant increase in the amount of savings identified. Indeed, in one way I hope to see a reduction.

Caroline Gardner: The work on best value in local government is having a significant impact. We see improvements in the way in which councils are run and in the services that they provide for local people. That is partly as a result of audit work, which gives a rounded picture of performance on a cyclical basis.

Members of the Scottish Commission for Public Audit will be aware that best value is also a duty on accountable officers across the rest of the public sector, although it is played out in rather different ways. We have been considering how audit can contribute to the same sorts of improvements in other parts of the public sector. I stress that we do not expect a significant increase in demand for audit in best-value areas, but we think that investing this sum of money over the next 12 months or so will let us re-engineer our audit approach at the margins to ensure that annual audit work and periodic performance audit work give assurance on best value for the other half of the public sector. We hope that that will generate improvements for the people who use and pay for services, and that it will allow us to make better use of all scrutiny work in line with the scrutiny review that the Executive is currently sponsoring. We are doing development work that we expect to lead to better use of the rest of our resources.

The Convener: Will the additional expenditure on those initiatives recur or is it a one-off for this year alone?

Mr Black: Do we propose to carry out the national fraud initiative annually?

Russell Frith: No, it happens every two years.

Mr Black: Yes, that was my recollection—it is undertaken every second year.

Caroline Gardner: As I have said, we expect the best-value development work to lead to better use of our mainstream resources rather than to a bid for additional resources.

Mr Black: I would not want to mislead the commission on this: as we roll out the pilots, we might feel that there is a need for a continuing commitment of resources. It is just too early to say. However, we are not talking about large sums of money—I give you that assurance.

The Convener: Thank you for your evidence. At our next meeting, which will be in November, we will again address the examination of the three Es—economy, efficiency and effectiveness—with which we have charged Haines Watts. I hope that we will get that information in advance of the meeting so that members can have a look at it. I encourage Audit Scotland and Haines Watts to place that high on their agenda.
Working Practices

11:16

The Convener: Our final item is the commission’s working practices. Evidence was requested by the Finance Committee, the Auditor General and ombudsmen on some of the issues that the commission has come up against. Initially, we had difficulty in ensuring that all our meetings were held in public session, that we had the use of microphones and that we had an Official Report. We still do not appear in the Parliament’s Business Bulletin and we are not entitled to have an Official Report of our meetings. We took the opportunity to air those concerns, and we received some support from the Finance Committee in its recent report on its inquiry into accountability and governance.

Do members have any comments on the paper that has been circulated or on any of the issues that I have raised?

Mr Monteith: I support the recommendations in paragraph 10, which are eminently sensible. The Finance Committee’s report discussed some other aspects of the Scottish Commission for Public Audit. Is it your intention to place on the agenda for a future meeting a discussion of our reaction to that report, so that we might consider other aspects of it?

The Convener: As we get nearer to dissolution, there will be an opportunity for us to have that discussion and to produce a legacy paper.

Mr Monteith: I would be happy with that.

Mr Welsh: We are, in a sense, the auditor’s auditor. We must always be aware of the need to respect the independence of Audit Scotland. In many ways, we have been an exception to the normal parliamentary committee rules. I would relish the opportunity to make the work of the commission—that is, the work of Audit Scotland— as widely known as possible, therefore I agree with your proposal, convener.

The Convener: Thanks very much. That brings us to the end of the public session. We will take a short break before we go into private session.

11:19

Meeting suspended until 11:30 and thereafter continued in private until 11:44.
Scottish Commission for Public Audit

Wednesday 26 April 2006

[THE CONVENER opened the meeting at 11:34]

Provisional Expenditure Plan 2007-08 and Corporate Plan 2006-09

The Convener (Margaret Jamieson): Good morning and welcome to the first meeting in 2006 of the Scottish Commission for Public Audit. I ask members to ensure that they switch off mobile phones, pagers and all other electronic equipment that might interfere with the sound recording.

I have received apologies from Brian Monteith. We have with us representatives of Haines Watt, which has just been appointed as auditor to Audit Scotland. They will be present for the meeting, although they will not speak.

Agenda item 1 is discussion of Audit Scotland’s provisional expenditure plan for 2007-08 and its corporate plan for 2006 to 2009. We have the provisional expenditure figures in accordance with the established three-stage annual budget process. I welcome Bob Black, who is the Auditor General for Scotland; Diane McGiffen, who is the director of corporate services at Audit Scotland; and Barbara Hurst, who is the director of performance audit in health and community care at Audit Scotland.

I invite Bob Black to make an opening statement.

Mr Robert Black (Auditor General for Scotland): Thank you very much, convener. As in previous years, we will provide the commission with our detailed expenditure proposals for the next financial year in the autumn. At this stage, as is customary, I have simply provided a provisional estimate. As you will be aware from my letter, that estimate is for expenditure of £7.14 million, comprising £6.617 million to cover the revenue expenditure and £523,000 to cover capital expenditure. In that, we assume a general inflationary increase of 3 per cent and I have increased our provision for depreciation to take account of a higher asset base, notably the work on one of our properties in 18 George Street and some other infrastructure projects. In the autumn, I will come back with a full budget statement.

There is one other point that is perhaps worth bearing in mind in that regard: the audit work for the past financial year is now in full flow and, until that is concluded, it will not be possible to give a definitive set of estimates for the following year because the next year’s work will not start until November, which is the point of handover from the previous year to the next year.

I have nothing further to say on the provisional estimate.

Mr Andrew Welsh (Angus) (SNP): I ask you to consider savings and savings targets. Audit Scotland is assessing the arrangements that public bodies have put in place to implement the efficient government initiative, and your corporate plan states:

“all business units in Audit Scotland are committed to savings targets each year.”

Will you give me examples of the types of savings that are being made in Audit Scotland and state whether they are time releasing or cash releasing?

Mr Black: I am happy to answer that question, but I ask for clarification of whether you are talking about our budget estimate, the corporate plan or the past financial year.

Mr Welsh: I am talking about the estimates and the plan.

Mr Black: In the summer, I will produce an annual report, which will give an account of our outturn expenditure, which will relate to the budget about which we talked last year. Therefore, I am not well placed to talk about our performance in the past financial year.

Mr Welsh: Will you give examples of the types of savings that you are seeking to make within Audit Scotland? What is their general direction?

Mr Black: The biggest element in our budget is the cost of the audits that are undertaken on public bodies. The procurement exercise that we go through is designed to get as much efficiency out of the budget as possible, and we have recently concluded an extensive procurement exercise that will put in place the audit arrangements for the next five years.

In association with and as part of that procurement exercise, extensive analysis was undertaken to compare the costs of audit as reflected in Audit Scotland’s audit charges, which are provided in an indicative form to the appointed auditors, with those of our sister bodies—the National Audit Office and the Audit Commission. We also consider the costs of contract work that audit firms undertake for other parties in Scotland. I am well satisfied that our cost profile is less than the costs that we see elsewhere. Such benchmarking is extremely important.

We undertake a programme of best-value reviews—for which provision will also be made in the corporate plan—of our support services in Audit Scotland.
As members will recall, over the past two years I have taken 5 per cent in each year out of the costs of the audits to the national health service, so we have delivered significant savings over that period.

We plan to limit ourselves to a budget uplift of an overall 3 per cent, which includes our finding savings within the year to accommodate things such as the movement in our staff’s increments. We are still a young organisation and staff are entitled to incremental increases that amount to about 1.2 per cent of our salary bill.

On our major elements, which are the costs of the audits, we have been through a procurement exercise. On our major cost on staff, I am limiting the budget increase to 3 per cent, which includes increments. On best value on corporate services, we are running a series of programmes. The final element to mention, of course, is that we run a programme of internal audit reviews, which report to the Audit Scotland board regularly.

The sums of money that we generate from savings in some of the smaller activities are small relative to the size of our budget. The spend profile that matters is the spend on audit charges to audited bodies.

Mr Welsh: And the savings apply throughout the organisation to all business units that are committed to the savings plans.

Mr Black: As I said, there is a big difference between the charges that we make for audits to public bodies in Scotland. I have talked about how we procure those audits and set the charges, and the costs of, let us say, staffing associated with corporate services. We do not make an across-the-board saving; we undertake audit and best-value reviews of our individual business activities to ensure that we get best value out of them.

Mr Welsh: I asked a complex question, so if you wish to add anything in writing to what you have said, that would certainly assist the committee.

Mr Black: When we come forward in the autumn with the full budget proposal and the annual report, which will also be available to you then, there will be full analysis of what we have undertaken in efficiency reviews, savings exercises and best-value reviews over the past year.

Mr Welsh: You said that your overall savings target was 3 per cent.

Mr Black: No, I am sorry if I misled you on that. The budget submission that I provided for you is a 3 per cent uplift for the next financial year, which starts next April, so it is a long way ahead. I am saying that we will absorb all our cost increases within that 3 per cent, including the cost of increments to staff, which in general puts about 1.2 per cent on to our pay bill.

Mr Welsh: What percentage of savings against its overall budget does Audit Scotland aim to achieve? How would that compare with the 3.4 per cent of efficiency savings that the efficient government initiative requires from local government?

Mr Black: I am sorry, but we do not have a figure that is calculated like that. As I said, the bulk of our costs—about 75 per cent—are the fees that are charged to audit bodies. We have gone through an exercise to benchmark those costs against similar organisations and limited the indicative fee increase to quite a tight level. That covers 75 per cent of our budget. Within the remaining 25 per cent, rather than agree an overall target for efficiency savings, we do specific pieces of work in each area of activity to get maximum added value out of our exercise. The sum total of that is that I am giving an undertaking that the general inflationary increase for the next financial year, starting in April of next year, will be 3 per cent. However, that will be less than the total cost uplift of our business, which is also influenced by factors such as the need to pay our staff increments, which puts on another 1.2 per cent. Therefore, we are absorbing efficiency gains by running a tight cash limit in all our budgets.

11:45

Mr Welsh: Which organisations do you benchmark against?

Mr Black: We receive confidential information from the National Audit Office and the Audit Commission.

The Convener: The National Audit Office said recently that it believes that £8 of efficiency savings are achieved within the organisation for every £1 that it spends. Is Audit Scotland prepared to provide similar information to the commission in the future?

Mr Black: I have discussed such matters with the Audit Committee when I have presented corporate plans in the past—I am going right back to when Audit Scotland started—and have said that it would be possible for us to put together a programme of value-for-money studies that identified notional savings that could be obtained from public spending in Scotland. However, realising such savings would require ministers, members of the Scottish Parliament and audited bodies to make hard policy choices. It is important that we do not use Audit Scotland’s resources on studies whose savings, for perfectly understandable policy reasons, it would not be possible to generate in the short term.

That is not to say that we have not done such pieces of work in the past. I remind members of the major study that we undertook on rationalising
That programme will include studies that are of matters such as the prevention and detection of fraud, on which we will produce a report next month.

Our position is rather different from that of the National Audit Office, which audits large departments of state such as HM Revenue and Customs and the Department for Work and Pensions, whose budgets are enormous. It is the big departments of state that will tend to generate efficiency savings and studies on specific staff costs, and it is difficult to generate savings on hospital building commitments and drugs. It is therefore highly unlikely that imposing a top-down target of saving X pounds for Y pounds in the NHS would be the best use of our resources. Doing so would distort our activity, and I am not sure that the best output would be achieved. As I have said, we have made a significant contribution towards improving the performance of the NHS in Scotland over a number of years.

Much of the work that we undertake in relation to audited bodies consists of reports to audited bodies locally. Such reports are to do with improving the standard and quality of management in those public bodies. The best-value council reviews that we undertake, in which we challenge local authorities to consider generating efficiencies through various means, provide the most fully developed example of those reports. Such reviews will help to generate efficiency savings.

The Convener: I would not expect to see such things in every Audit Scotland report, but I recall the issues that were raised about prescribing, for example. Identifying the savings that could be achieved as a result of minor changes in how medicines are prescribed was right and proper.

In certain areas it is right to identify financial savings, but changes to how people work and cooperate can also generate savings, so I accept that it is not always appropriate to focus on the pound sign. However, if Audit Scotland indicated the savings in the Scottish budget that its work could achieve, we would have a helpful overall picture. Such an approach might assist, given that disquiet is sometimes expressed by the individuals who pay Audit Scotland’s fees.

Mr Black: I agree. That is why we will describe our study that challenged councils’ council tax collection levels. My approach is to present a balanced programme of studies for consultation with the Parliament. That programme will include studies that are directed at improving performance and enhancing the quality of services, studies that are designed to generate efficiency savings and studies on specific matters such as the prevention and detection of fraud, on which we will produce a report next month.

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Mr Black: I agree. That is why we will describe in our annual report what was delivered during the past year, as I said. We will attempt to address more fully the impact of our work, which will include the identification of areas in which we highlighted the possibility of making savings or cash-releasing initiatives.

Margaret Smith (Edinburgh West) (LD): Audit Scotland’s work programme, which is considered by the Audit Committee, is outlined in one of the appendices to the corporate plan. A significant number of studies are planned, but the corporate plan gives no details about the basis on which the projects were selected. I assume that you have to assess whether a proposed study would generate beneficial results for management, is topical, or might realise notional savings, for example. How do you assess such matters and decide which studies to conduct?

Mr Black: The current programme of committed studies, which will run to 2007, is highlighted in the corporate plan. We do not present a full analysis in the plan of how those studies, which were agreed to after consultation, were selected. We will go to consultation during the summer and we will bring to the Audit Committee and the Parliament in the autumn a major piece of work, which will lay out for consideration my views on the study programme from 2007 onwards. In that context we will explain why each topic has been suggested.

I might have said to the commission that we face a problem not in deciding what to do, but in deciding what not to do, because there are many issues that we could consider. In the autumn we will present a full analysis of the range of topics that might be appropriate and invite comments and views from all our stakeholders on which topics should be given priority. We will also invite suggestions for topics that we might not have considered. We will pull all that work into a formal programme of studies, which I will approve before the end of the calendar year. That is the process.

You asked how we select topics from the almost infinite list of topics that we could consider. We do a number of things in that regard. We try to balance studies that will impact on major areas of public spending. For example, we always carry out a number of studies in the health service, which accounts for at least half the Scottish block, if we disregard the funding of local government. Materiality—to use the accountants’ term—is important. We consider big areas of spend. We also attempt to consider coverage—we would like to have a balanced programme of studies that covers local government and central Government as well as the NHS. We tend to consider studies when there is evidence of variation in performance and scope for improvement; we do scoping studies on that.

Increasingly, we will have a balanced programme that contains overviews of major areas
of public spending, such as the whole transport system, together with more specific pieces of work on themes such as the management of assets in the Scottish block and studies of particular services that are provided in the health service, for example. We evaluate all that within a framework and we undertake a full consultation.

**Margaret Smith:** That was a full answer. Is any of those matters weighted as much more significant than others? For example, is materiality your number 1 priority, or would it be simplistic to say that?

**Mr Black:** The arrangement is more complex than that. I am concerned to ensure that, over several years, Audit Scotland’s limited resource should cover most of the major areas of public spending. The main method for doing that is the developing programme of overview studies, which is heavily weighted.

On the other hand, it is important that we examine smaller budgets; we do not ignore organisations with such budgets. For example, Scotland has a large number of non-departmental public bodies. Some of them spend less than £50 million, but they are important for the services that they provide to the people of Scotland, so we must include them in our coverage.

Some services do not involve high levels of spending relative to the Scottish block but are important for ordinary people. We want to ensure that we cover them in the programme. For example, although I would not say that it involved low spend, we have it in mind to consider how public services as a whole, led by the NHS, treat some chronic conditions, by using them as a tracer through the system. That study will not be primarily budget focused; it is more to do with the impact of services on vulnerable people.

**Margaret Smith:** I wish you well on that. The convener was the deputy convener of the Health and Community Care Committee when I was that committee’s convener and at that time it was a major problem for health boards to say even how much money was spent, on what it was spent and what effect it had.

On effectiveness, how do you evaluate the impact and benefit of studies that you have undertaken?

**Mr Black:** I ask Barbara Hurst to speak; I have done a lot of talking.

12:00

**Barbara Hurst (Audit Scotland):** I could have answered the previous question more easily.

The question how much can be attributed to one of our reports and how much was happening anyway makes it difficult to measure the impact of our work. When we start to do a study—particularly one that is of national significance—much activity suddenly starts to happen, although we cannot put a figure on that. In a sense, that is a result for us, but we cannot formally produce it and say, “This is a result of our work.” However, that result is as important as what happens after we have produced our report and started to measure its effect. That means that we must be very careful that our study selection does not distort services’ priorities—we are keen not to do that.

We make recommendations as a result of specific studies and follow them up by going back in and looking at what is happening on the back of those recommendations. We would be keen to involve service users in that work. In our follow-up, we would always want to consider—where relevant, of course—the impact in terms of improving services for people in Scotland. Diane McGiffen has done detailed work with sister organisations on how we measure impact, so she can pick up on that.

**Ms Diane McGiffen (Audit Scotland):** The discussion has focused on our performance audit study programme; the question of how we measure the impact of our work applies to all our work, including our regulation and governance work. We are working on a project within Audit Scotland on how we can better assess the impact of all our work. The issues around attribution that Barbara Hurst and Bob Black outlined are ones that we have in common with the other audit agencies. We do a study and follow it up a couple of years later, but the environment in which an organisation works is dynamic and change happens anyway. It can be difficult to ensure that the change that we report is the result of our work, as opposed to change that has taken place for other reasons. There is a question for all the audit agencies about the proportionality of follow-up work. Given that the public sector is dynamic, how much time and effort do we and the audited bodies want to spend in tracking old studies when the world has moved on?

I say this to give you a flavour of the context within which we are trying to get better impact measures, not to give reasons for not trying to get better impact measures. These factors are just part of the landscape of working through something that will be meaningful and add value to you and to our other stakeholders. We need to pull together various things for a rounded report of our impact. We must ensure that we capture aspects such as the value that is added to the public by the fact that independent audit provides public assurance that public money is being well spent. That is a tricky thing to do; most members of the public will not be fully aware of the audit arrangements that apply in their local areas to their local audit bodies and so on. However, we are sure that independent auditing of how public
funds are spent and, what is important, the public reporting of the results of that audit, add something that is of public value.

We are also considering how we can capture better information on the impact of our work to support elected representatives and board members to do their work in holding public bodies to account and so on; that is also part of assessing the impact of our work. As well as the study programme, we bring issues to the attention of Parliament through mechanisms such as section 22 reports, which raise issues of interest and concern that Parliament can then pick up. We have a range of work areas and we are considering how we can build a mosaic that will provide a richer picture of the impact that we make, taking into account our concerns about the proportionality of tracking the long-term impact of our work.

**Mr Black:** If I may, I will add one further point to Diane’s point about helping elected representatives, board members and so on to do their work. I am sure that the commission will recall that one of the key elements in the corporate strategy that flows from a strategic statement that I produced last year is supporting democratic scrutiny. The work of supporting the Parliament is important. The Audit Committee is in a powerful position to assist the follow-through process, because once it has taken evidence and produced a report with recommendations, it can require the Executive to report back—after an appropriate time—on what promises and undertakings have been implemented. That is a comparatively straightforward, but extremely influential and effective way of ensuring that change happens.

**Margaret Smith:** I agree. Barbara Hurst made the point that there is a great deal of activity when a report is published, but we must ensure that that does not fall away. It is important that we use all the different mechanisms that we have at our disposal. Are there occasions on which your organisation feels that an initial report has not had the impact that you hoped that it might have and that, rather than use the Audit Committee or another body, you would rather do follow-up work in house, or are you so swamped by the range of available options that producing a second piece of work slips down the list of priorities?

**Barbara Hurst:** As you were talking, I remembered that several years ago we did some work on bank and agency nursing. What needed to be done was straightforward. Since then, although there has definitely been a reduction in the use of agency nursing, the use of bank nursing has increased. Some issues remain to be resolved, so along with the high-level work that we are doing to follow up a previous report on ward nursing, we want to conduct a detailed review of the use of bank and agency nursing because we think that not enough has happened on that front. We are slipping that work in through a different reporting route.

**Margaret Smith:** I am glad that you gave that answer, because I was going to suggest that you do that.

During the evidence that you gave to the commission in May last year, you stated that Audit Scotland was pioneering a new, modernised approach to audit that aimed to address the major risks and performance issues in public bodies. Will you give us an update on that?

**Mr Black:** Yes. There has been a huge amount of activity in that area. As you know, Audit Scotland has a relationship with more than 200 public bodies in Scotland. A large part of the work that we undertake is done through the interaction between the appointed auditor, who I appoint, and the organisation. You will recall from our previous discussions that I was concerned that the resource that was being devoted to the audit of public bodies was not adding as much value as it might.

We have been steadily developing a significantly different approach to how audits are undertaken. That new approach had its second year of operation in the health service over the past year and is now in its first year of running throughout local and central Government. The general approach is to start off by conducting a clear and careful planning process, during which we draw up a priorities and risks framework—which I will call a PRF for short, if you will pardon the jargon—for the sector concerned. The PRF is designed to capture from an audit point of view the sector’s major priorities for delivery in the year ahead, the major risks that it might face and any areas of performance weakness that might need to be addressed. That document is used as a basis for corporate discussion within Audit Scotland and with the firms about how we might prioritise and target the audit activity in individual bodies.

That exercise brings two highly significant benefits, the first of which is of direct interest to Parliament. It means that when I prepare an overview of the NHS, I can have reasonable confidence that the issues that are dealt with in the overview that Barbara Hurst’s team has prepared reflect the reality on the ground because the information has been gathered consistently. We get comprehensive coverage of a particular topic in 15 health boards. That provides an assurance to me before I report to Parliament.

The second significant benefit is to audited bodies. If the auditor says, “We think that you have a risk that you’re not addressing in this area or a performance weakness in that area,” it is an opportunity for management to engage with the
auditor to develop a plan of action to address the areas of weakness in real time. That adds more value to the management of public bodies in Scotland. We are already seeing indications that the public bodies value the work highly and I will be able to report more fully on that in the annual report in the summer. In that annual report, I will indicate how the audit has been received—particularly in the health service—in its new form over the past year.

Cathy Peattie (Falkirk East) (Lab): The corporate plan talks about the need to maximise the value of audit and about rolling out a newly defined corporate quality management framework. Will you give me some examples of how that corporate framework is intended to improve the overall service to audited bodies?

Mr Black: I invite Diane McGiffen to answer that question.

Ms McGiffen: Gladly. The corporate quality framework, of which there is a copy on our website, sets out our expectations for internal challenge processes for how we do our work and review processes. Each business group in Audit Scotland has its own quality process appropriate to its work.

Those business group processes adhere to a set of high-level principles about introducing after-action reviews; bringing in someone from outwith the project team and, preferably, outwith the business area, to be a critical friend as part of the review process; looking at how we share information on the outcome of that activity across the business so that everyone can learn from messages about improvement and so on; and looking at how we incorporate the views of clients, partners and others with whom we work on how we have done our work, the effect of that work and how we might do it better.

Those principles include the provision for an annual report to the management team about what activity has been undertaken, what the findings were, what actions have been taken and any messages for us from that process. That sits alongside the formal quality assurance process that my colleague Russell Frith runs through the audit strategy group, which does a detailed, in-depth review of the quality of the audits that we deliver on a cyclical basis during the course of audit appointments.

Cathy Peattie: Interesting. Can you give some examples of the actions that have been taken and any emerging themes from the feedback?

Ms McGiffen: We looked at a review of a recent performance audit study. Although it is too early to look at the impact of the study, we had a review meeting to look at the process of producing the publication—how we carried out the research, how we met timescales and delivered the product and what that tells us. That is still a work in progress so there is no final conclusion and it is too early to say whether lessons from that are applicable to other work that we do.

The first annual report on the quality process will come much later in the year.

Cathy Peattie: Have there been any themes whose similarity has surprised you?

Ms McGiffen: If we take performance audit studies, one of the things that surprises us is the impact that the topic that we look at has on the study, which might seem from the outside to be a similar process whatever the context. There are differences between how we might look at a study in the NHS as opposed to central Government because of the different environments in which we are working. However, those are emerging thoughts; we are not drawing any profound conclusions from them. When we have the first annual report, we will be in a much better position to consider what themes are emerging.

12:15

The Convener: Thanks very much. I will ask some questions on your recent job advert for graduates. There has been an increase in your staffing: your average number of staff was 242 in 2003-04 but rose to 274 in 2004-05. Are your recent vacancies for posts additional to the 274?

Mr Black: The establishment is not increasing beyond the rough 270 mark. In effect, we are recruiting up to that complement. As I am sure you recall from discussions on previous corporate plans and annual reports, we have talked about how the staffing level has changed with pressures on the business such as the taking on of the best-value agenda, the creation of Transport Scotland, and our work on whole of government accounts.

Our staffing is stable at round about the 270 mark. I have it in mind that we would take on, roughly speaking, half a dozen graduates a year. Staff move through the organisation and some of them leave it. There is no set number of graduate trainees, but it is part of the natural staff turnover in an organisation the size of ours that we take in about six trainees a year.

Ms McGiffen: We are looking for about four graduate trainees this year; last year, we took on 12. We have discussed our graduate training programme in some detail and, as you therefore know, we are strongly committed to ensuring that the scheme provides good-quality graduate trainees for Audit Scotland, but may also contribute to developing skilled financial professionals in the public sector generally.

The Convener: The vacancies that you have
Mr Black: Yes.

The Convener: They are not posts additional to those that you already have.

Ms McGiffen: The graduate training scheme runs almost alongside our establishment. To keep the scheme viable, we have to recruit to it every year otherwise there will be no follow-on of graduates coming out the other end and progression for the graduate trainees in their work would be made more difficult, given the coursework and other work-based exercises that they have to complete. We have to keep a throughput of graduates in the graduate training scheme.

Mr Welsh: I will ask about information technology systems. The corporate plan states that Audit Scotland is seeking to build an effective and efficient organisation by, among other things, implementing a new finance system and a new electronic document and records management system. How are those projects progressing and what are the target dates for their completion?

Ms McGiffen: Our new finance system is currently double-running with our old finance system and its go-live date is July—I am conscious of my auditor colleagues sitting here. The new system has been progressing well. We have transferred data from the old system to the new one and are checking it all. That has gone well and we have quality processes in place for the management of that project, which is at an advanced stage.

I always struggle with the order of the words “electronic records and document management system”, so I am told that I should call it an e-docs system to avoid any confusion. We are about to go out to tender to procure that system, so it is not as advanced as the finance system. We hope to have the e-docs system in place by January 2007 at the moment.

Mr Welsh: I wish you success with those projects.

Ms McGiffen: Thank you very much.

The Convener: There are no further questions, so I thank the representatives from Audit Scotland for their assistance. We look forward to receiving their detailed expenditure figures when we next meet in November.
ANNEXE B

LETTER FROM THE AUDITOR GENERAL FOR SCOTLAND TO THE SECRETARY – 21 SEPTEMBER 2006

Dear Secretary

In your letter to me on 15 May 2006, you wrote that the Commission would appreciate further information on the specific savings targets which all business units in Audit Scotland are committed to each year. I write to provide further information to the Commission on this issue, provide an update of our work on impact and quality, and to inform the Commission of a potential liability facing Audit Scotland.

Efficiencies

A key driver for our business is the level of increases in charges to audited bodies, which account for around 75% of our income, and the level of increase in funding from Parliament. Increases in charges to local authorities are subject to scrutiny by the Accounts Commission and those for all sectors are subject to comment from the audited bodies themselves. Over recent audit years the basic average increases in charges have been:

<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003/04</td>
<td>5%</td>
</tr>
<tr>
<td>2004/05</td>
<td>2%</td>
</tr>
<tr>
<td>2005/06</td>
<td>3.8%</td>
</tr>
<tr>
<td>2006/07</td>
<td>3.0%</td>
</tr>
</tbody>
</table>

When proposing increases in charges Audit Scotland also provides an indication of the likely increase for the following audit year in order to allow audited bodies, particularly those working to three year budgets, to plan their future costs. For each of the audit years 2005/06 and 2006/07 Audit Scotland has been able to reduce the actual average increase from those previously notified (from 5% to 3.8% for 2005/06, and from 3.8% to no more than 3% for 2006/07).

As detailed in our budget proposal, in NHS audits the final elements of the reductions in cost arising from the abolition of trusts will be in place for the 2006-07 audits, meaning that the total recurring annual savings are in audit fees are £264,000 and the cumulative total up to the 2006-07 audits some £675,000.

We have consistently managed our business to improve our performance and contain fee increases to a minimum consistent with ensuring that we can respond to essential increases in our underlying costs and securing the quality of our audit work and compliance with international accounting standards.

Efficiencies are reviewed and targeted during our budget process. After reviewing the potential for efficiencies, and based on previous performance, we set a challenging £s target for expenditure for each business group, rather than a percentage efficiency target. Groups must deliver the same or increased levels of outputs for that target. For the 2007-08 budget which the Commission will be considering, for example, the Corporate Services group received a budget reduction of £115,000, and other budgets were reduced by nearly £250,000. In addition, we have made a reduction of £160,000 in senior management costs. These reductions equate to 2% of total Audit Scotland expenditure.

As the Commission knows, we have been going through a process of reviewing and modernising our core business processes to deliver the audit, and that process has not yet been fully implemented across all our sectors. Once the implementation is complete, we will be able to review the costs and benefits of the new process across all sectors and make informed decisions about potential percentage efficiency targets. The modernisation process is already delivering efficiencies, however, as it has incorporated revisions to auditing standards in our core work without additional cost.

We have been driving efficiencies in our internal management through more effective use of staff. In our corporate services, for example, between 2002-03 and 2005-06, the ratio of HR team members to staff has moved from 1:56 to 1:70. Similarly, in the same period, the ratio of IT support and infrastructure team members to staff has moved from 1:45 to 1:56.
This demonstrates efficiency gains in our internal support services.

**Best value reviews**

To improve on the targets set during our budget process, we also have a programme of internal best value reviews to 2009-10. In 2006-07, we are reviewing the following areas:

- Corporate printing provision
- Correspondence and complaints handling
- Best value audit in local government
- Programme and project management in corporate services

In 2005-06, we completed a best value review of our facilities management and corporate administrative support services which resulted in a restructuring of internal resources designed to deliver improved quality of provision. We have a corporate approach to best value reviews which ensures a rigorous process.

We are taking part in a support services benchmarking exercise, and although the project is not yet complete, early results on IT show that support costs are lower than comparable organisations.

**Impact of audit**

In your letter, you report that the Commission would be interested in receiving a copy of the findings of our work to improve the assessment of the impact of all of Audit Scotland’s work. Although this work has not yet concluded, I thought the Commission might welcome a progress report on this.

Our work has two dimensions: actions internally to improve our ongoing assessments of the impact of our work; and working with the other national audit agencies to progress improved ways of consistently assessing impact.

We have been piloting ways of assessing impact without conducting a specific follow up study. Over the summer we ran three pilots to test how impact could be assessed using existing information. The pilots were testing:

- The availability of information
- The staff time required to collect and analyse information
- How regularly data sources should be reviewed
- Whether there is sufficient robust information to answer questions about the impact of a study
- The degree of commonality across studies in terms of the sources that need to be reviewed.

Following the pilots, we have now revised our project management framework to include specific comments about impact when we consider the study selection criteria, and how potential and actual impacts are assessed during the planning and post implementation periods of studies.

We have also been contributing to work by the Public Audit Forum (PAF) over the summer involving all audit agencies in reviewing methods for assessing the impact of audit. The next meeting of the PAF is considering an interim report on this work, and, with the Commission’s permission, I will report how that will be taken forward on a national basis at our next meeting.

I will be pleased to provide further information on the progress of this work as it develops.

**Quality process**

Our first annual report on our quality processes will be finalised in October, and I shall ensure that the Commission receives a copy of this when it is available.

I will be happy to discuss any of the issues contained in this letter at our meeting on 27 September.

**Potential Liability for former Ombudsman Pensions**
Finally, I wish to draw the Commission’s attention to a potential liability. When Audit Scotland was established it took over the statutory responsibilities of the Accounts Commission as the “designated body” for the local government ombudsman. This was a statutory arrangement under which the Accounts Commission/Audit Scotland provided all the back office services for the Ombudsman and incorporated the financial transactions within its accounts. This activity ceased when the Public Services Ombudsman was established under the 2002 Act and the Act attempted to transfer all assets and liabilities of the various former ombudsmen to the new Public Services Ombudsman.

However recent legal advice obtained at the request of the Ombudsman is firmly of the view that the Act was ineffective as far as pension liabilities relating to former local government ombudsmen are concerned. This means that Audit Scotland may be left with a liability of up to £300,000 which was not intended under the legislation and for which no provision has been made. Audit Scotland is in contact with the Scottish Executive to seek their assistance in resolving this matter and implementing the intention of the legislation. At this stage no amounts relating to this potential liability have been incorporated into the Autumn Budget Revision or the Budget proposal for 2007/08 but I felt the Commission should be aware of the issue now, as it may be included in future papers.

I will be happy to discuss any of the issues contained in this letter at our meeting on 27 September.

Yours sincerely

Robert W Black
Auditor General for Scotland
LETTER FROM THE CONVENER TO THE AUDITOR GENERAL FOR SCOTLAND – 5 OCTOBER 2006

Dear Auditor General

I am writing to thank you and your colleagues, Diane McGiffen, Russell Frith and Caroline Gardner for the evidence you gave to the Scottish Commission for Public Audit on 27 September 2006. I attach the report from the meeting for your information.

As noted during the evidence session, the Commission would appreciate further information on the following:

- Staff turnover year on year since Audit Scotland’s establishment;
- Salary increases for senior staff year on year for the same period and how this compares with senior staff in other parts of the public sector;
- The specific basis for the 38% increase in income from local authorities;
- Details of how the efficiency savings achieved by Audit Scotland are divided between cash releasing savings and time releasing savings, and the definition of an efficiency saving adopted by Audit Scotland;
- A copy of the legal advice from the Queen’s Council on the local government ombudsman pensions liability issue;
- A copy of the letter from Audit Scotland to the Scottish Executive seeking action on the pensions liability issue;
- Any correspondence with the SPCB or the ombudsman in relation to this issue; and
- Clarification as to whether any provision has been made within the SPSO’s budget for the liability.

In order to submit the SCPA’s report on Audit Scotland’s budget proposal to the Finance Committee in time to inform its Stage 2 report on the 2007-08 budget, the finalised report will need to be agreed by members and published by 8 November at the latest. Given the short timescale for the drafting of this report I would very much appreciate a response by 21 October.

In addition, as noted at the meeting, I would be grateful if you could ensure that the 2006—07 management report, which I understand is currently with you for clearance, could be provided to the SCPA in advance of its next meeting on 22 November.

Yours sincerely

Margaret Jamieson

Scottish Commission for Public Audit
LETTER FROM THE AUDITOR GENERAL FOR SCOTLAND TO THE CONVENER – 20 OCTOBER 2006

Dear Convener

Thank you for your letter of 5 October 2006 following the Commission’s meeting on 27 September requesting further information on several matters. Responses to the request are set out below.

Staff turnover

Audit Scotland’s staff turnover for the last 4 years is set out in the table below:

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Staff leaving</th>
<th>Percentage of staff</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002/03</td>
<td>18</td>
<td>8.4%</td>
</tr>
<tr>
<td>2003/04</td>
<td>18</td>
<td>7.0%</td>
</tr>
<tr>
<td>2004/05</td>
<td>13</td>
<td>5.5%</td>
</tr>
<tr>
<td>2005/06</td>
<td>20</td>
<td>7.0%</td>
</tr>
</tbody>
</table>

Staff turnover is reported quarterly to the Management Team and Audit Scotland Board.

Salary increases for senior staff

Audit Scotland’s senior management gradings were not comprehensively reviewed when the organisation was created. The TUPE requirements were applied. Audit Scotland has experienced some difficulty in attracting suitable candidates to its most senior posts, and in one case (during 2004), the salary was increased to ensure the candidate did not experience a financial disadvantage compared with their former post. In 2005, once the business needs of the organisation were clear, a market salary benchmarking exercise was undertaken by external independent remuneration advisers Adams Associates. Some salary adjustments were made in the light of the consultant’s analysis. The table below provides details of awards for the Audit Scotland Management Team (including the Auditor General, although he is not an employee of Audit Scotland and his salary is not set by Audit Scotland.)

The table below provides details of awards for Audit Scotland Management Team:

<table>
<thead>
<tr>
<th>Year</th>
<th>Number</th>
<th>Highest</th>
<th>Lowest</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>April 2002</td>
<td>4</td>
<td>3.01%</td>
<td>2.84%</td>
<td>2.97%</td>
</tr>
<tr>
<td>April 2003</td>
<td>4</td>
<td>3.01%</td>
<td>2.34%</td>
<td>2.84%</td>
</tr>
<tr>
<td>April 2004</td>
<td>5</td>
<td>17.19%</td>
<td>2.14%</td>
<td>8.68%</td>
</tr>
<tr>
<td>April 2005</td>
<td>5</td>
<td>15.81%</td>
<td>3.13%</td>
<td>8.12%</td>
</tr>
<tr>
<td>April 2006</td>
<td>5</td>
<td>3.39%</td>
<td>2.95%</td>
<td>3.04%</td>
</tr>
</tbody>
</table>
Public sector awards

The table below provides details of the median public sector pay settlements:

<table>
<thead>
<tr>
<th>Year</th>
<th>Median Settlement</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>3.6%</td>
</tr>
<tr>
<td>2003</td>
<td>3.5%</td>
</tr>
<tr>
<td>2004</td>
<td>3.0%</td>
</tr>
<tr>
<td>2005</td>
<td>3.0%</td>
</tr>
<tr>
<td>2006</td>
<td>2.95%</td>
</tr>
</tbody>
</table>

*Source: Incomes Data Services*

The table below provides details of the Senior Salaries Review Body settlements:

<table>
<thead>
<tr>
<th>Year</th>
<th>Settlement</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>3% for 60% of senior civil servants, range of 0 to 10%</td>
</tr>
<tr>
<td>2003</td>
<td>Average award 4.5%. Pay bands increased by 2.25%. Range of 0 to 9% merit increases</td>
</tr>
<tr>
<td>2004</td>
<td>3.7% average earnings growth</td>
</tr>
<tr>
<td>2005</td>
<td>4.2% average base pay award. Pay bands increased by 2.5%</td>
</tr>
<tr>
<td>2006</td>
<td>Average individual award 3.25%. 1% with remainder of award worth 1.75% on paybill.</td>
</tr>
</tbody>
</table>

*Source: Incomes Data Services*

Increase in income from local authorities

Audit Scotland’s business cycle means that work from two audit years will be included in each financial year. The table below shows how the income for each of the last two financial years is made up of income from more than one audit year.

<table>
<thead>
<tr>
<th>Audit year</th>
<th>Included in Accounts for Financial Year</th>
<th>03/04 £000</th>
<th>04/05 £000</th>
<th>05/06 £000</th>
<th>Additional work £000</th>
<th>Total for financial year £000</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003/04</td>
<td>3,372</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004/05</td>
<td>6,502</td>
<td>2,956</td>
<td></td>
<td></td>
<td>161</td>
<td>9,619</td>
</tr>
<tr>
<td>2005/06</td>
<td></td>
<td>8,657</td>
<td>4,304</td>
<td></td>
<td>268</td>
<td>13,229</td>
</tr>
<tr>
<td>2006/07</td>
<td></td>
<td></td>
<td></td>
<td>7,691</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total for Audit Year</td>
<td>9,874</td>
<td>11,593</td>
<td>11,995</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The increase in charges between audit years 2003/04 and 2004/05 were 17.5% comprising a 2% basic increase for inflation, 8% to reflect the change in Audit Scotland’s VAT status and 7.5% for the new statutory best value audits for which authorities had been specifically funded by the Scottish Executive. The increases for other sectors were all 10% reflecting the inflation and the VAT change.

The increase in charges between audit years 2004/05 and 2005/06 of 3.5% reflected inflation increases in Audit Scotland’s costs and was the same for all sectors.

The increase in income between the 2004/05 and 2005/06 financial years is therefore a combination of the timing effects of more work being carried out as explained at the Commission meeting, a small impact from additional work (mainly additional fees for work such as opinions on proposed PFI/PPP projects) and the residual impact of the higher charges from 2004/05 audits onwards for the change in VAT status and best value audits.

Cash savings and time releasing savings

All of the savings referred to in the 2007/08 Budget paper and at the Commission meeting are cash savings.

Audit Scotland will include a saving as an efficiency saving if it arises from a reduction in expenditure or staff time which is not anticipated to have an impact on the quantity, quality or timing of audit work or if it arises from deciding to stop doing something which is no longer regarded as necessary. An example of the former type is the reduction in senior management costs and an example of the latter is the decision last year to no longer publish separate paper versions of local authority performance indicators and to make them available on the web only.

Potential Liability for former Ombudsman Pensions

Copies of the Counsel’s Opinion, the Memorial instructing Counsel [not reproduced in this report, copies available on request from the Secretary] and the subsequent letter to the Scottish Executive are attached. There has been no correspondence between Audit Scotland and the SPCB. Much of the earlier discussion with the Ombudsman was by telephone and e-mail and the position of each party is set out in the memorial.

We understand that no provision has been made in the SPSO’s budget for the liability as they are acting on the Counsel’s opinion that the liability has not been effectively transferred to them.

I trust that this response will assist the Commission in making its report and I confirm that we will work with Haines Watt to ensure that the Management Report is available before the next meeting of the Commission.

Yours sincerely

Robert W Black

Auditor General for Scotland
Dear Ms Parsons

I am writing to ask for your help with an issue concerning the Ombudsman service. There is quite a bit of history attached to this, and I apologise in advance for the lengthy explanation which follows.

When the Local Government Ombudsman service was established in 1975 the legislation provided that support services for the Ombudsman would be carried out by a designated body. We believe that the intention of this provision was to avoid unnecessary duplication in the establishment of a small office. Ministers decided that the Accounts Commission for Scotland would be the designated body, and thereafter the Commission’s organisation met the expenses of the Ombudsman and recovered the cost from local authorities as a separate item in its invoicing process. The relevant statutory provisions governing this are in the Local Government (Scotland) Act 1975.

In 2000, with the establishment of the new public audit arrangements under the Scottish Parliament, support services for the Accounts Commission transferred into Audit Scotland. As the Commission no longer had the power to incur expenditure, arrangements were made for Audit Scotland to become the designated body for the Local Government Ombudsman.

When the unified Ombudsman service was created by the Scottish Public Services Ombudsman Act 2002 Audit Scotland ceased to perform the function of designated body. Since then there have been issues about the inherited liabilities from the former Local Government Ombudsman’s service. The first of these related to the occupation of premises in Walker Street, where the lease had been taken in the name of the Accounts Commission. Following extensive discussions, the Scottish Executive assumed responsibility for that building when the new Public Services Ombudsman moved to her premises in Melville Street. The second issue relates to liability for pension costs.

The Ombudsman has argued that the cost of pensions for Local Government Ombudsman staff who retired before her service was created should be met by Audit Scotland. Audit Scotland, on the other hand, has argued that the liability for those costs transferred to the Ombudsman service. The legal arguments for this are rehearsed in the attached papers which culminate in an Opinion of Senior Counsel to the effect that these are liabilities of Audit Scotland.

There would seem to be little point in pursuing the legal issues any further, incurring expenditure on an argument between two public bodies. We in Audit Scotland believe that the intention of the legislation setting up the Ombudsman service in 2002 was that the previous liabilities of the constituent Ombudsman services would transfer to the new service. It appears that the legislation did not have that effect in relation to liabilities of the former Local Government Ombudsman service. This is an unfortunate result, as Audit Scotland must now accept responsibility for expenditure which does not relate to the audit of public bodies.

We are particularly concerned about the costs of the early retirement of the former Secretary of the Local Government Ombudsman. The decision to give the holder of that post early retirement was made following a recommendation by the then Ombudsman and resulted in substantial savings to the Ombudsman’s budget. Those savings are now enjoyed by the Ombudsman service, but the costs are to be met by Audit Scotland and we do not feel that this is an equitable outcome.

We would therefore like you to consider options for resolving this difficulty. It seems to us that some of the options are:

1. Audit Scotland requests additional funding from the Scottish Commission for Public Audit in order to meet these costs.
2. The Scottish Executive assumes direct responsibility for meeting these costs.
3. The Scottish Executive promotes an amendment to the legislation in order to transfer the legal liability to the Ombudsman service.

We will, of course, be happy to discuss these issues further. As Audit Scotland must submit its budget proposals for 2007/8 to the Scottish Commission for Public Audit by the end of September we would welcome an early indication of your response.

I am copying this letter to the Ombudsman and to the Scottish Parliamentary Corporate Body who have been involved in discussions to date.

Yours sincerely

W F Magee
Secretary
ANNEXE C

SCOTTISH COMMISSION FOR PUBLIC AUDIT

EXTRACT FROM THE MINUTES

1st Meeting, (Session 2) 2006

Wednesday 26 April 2006

Present:
Margaret Jamieson (Convener) Cathy Peattie
Margaret Smith Mr Andrew Welsh.

Also present: Andy Munro, Audit Adviser, Steve Connors and Gibson, Haines Watts

Audit Scotland’s Provisional Expenditure Plan 2007-08 and Corporate Plan 2006-09:
The Commission considered Audit Scotland’s Provisional Expenditure Plan for the financial year 2007/08 and Audit Scotland’s Corporate Plan 2006-09. The Commission took evidence from—

Mr Robert Black, Auditor General for Scotland;

Ms Diane McGiffen, Director of Corporate Services; and

Barbara Hurst, Director of Health and Community Care.

Members requested additional information in relation to savings targets.

SCPA Away day: The Commission considered the outcomes from its away day. The Commission agreed the following:

• to invite Haines Watts, external auditors to Audit Scotland to conduct a 3 Es examination of Audit Scotland and to report to the Commission in advance of its meeting in November 2006;

• to undertake a visit to the Public Accounts Commission, members availability allowing, and to bid to the Conveners Group for funding for any such visit;

• to make a submission to the Finance Committee’s Inquiry into Accountability and Governance.
Present:
Margaret Jamieson (Convener)    Brian Monteith
Mr Andrew Welsh

Also present: Andy Munro, Audit Adviser, and Richard Gibson, Haines Watts

Apologies were received from Cathy Peattie and Margaret Smith

**Items in private:** The Commission agreed to take agenda item 6 in private.

**SCPA Visit to the Public Accounts Commission:** The Commission received a report from the Convener on the SCPA visit to the Public Accounts Commission. The Committee noted the paper on the visit and agreed that issues of best practice would be incorporated into the Commission’s legacy paper which will be considered at a future meeting.

**Annual Accounts and Report on Accounts for the year to 31 March 2006:** The Commission took evidence from—

- Mr Robert Black, Auditor General for Scotland;
- Caroline Gardner, Deputy Auditor General;
- Russell Frith, Director of Audit Strategy; and
- Ms Diane McGiffen, Director of Corporate Services.

and then from—

- Richard Gibson, Haines Watts, External Auditors to Audit Scotland.

**Audit Scotland's Budget Proposal for 2007-08 and Autumn Budget Revision:** The Commission will took evidence from—

- Mr Robert Black, Auditor General for Scotland;
- Caroline Gardner, Deputy Auditor General; and
- Ms Diane McGiffen, Director of Corporate Services.

During the course of the evidence sessions Audit Scotland agreed to provide a number of pieces of supplementary evidence to the Commission.

**Working Practices of the Commission:** The Commission considered a paper from the Convener on proposed changes to procedures of the Commission. The Commission
agreed to write to the Procedures Committee requesting it to consider changing procedures as outlined in the paper. The Commission also agreed to instruct the Secretary to arrange a specific cost centre for the Commission.

**Audit Scotland evidence (in private):** The Commission considered the evidence taken at agenda items 3 and 4 including the possible contents of its report on Audit Scotland’s Budget proposal for 2007-08. The Committee agreed to write to the Auditor General for Scotland on issues raised during discussions and agreed to consider a draft report on Audit Scotland’s Budget Proposal for 2007-08 by correspondence.
Audit Scotland
Budget Proposal 2007-08

Introduction

Audit Scotland provides services to the Auditor General for Scotland and the Accounts Commission. The principal activities of Audit Scotland are to carry out the annual external audit of around 200 public bodies and to carry out a programme of performance audit studies across all parts of the public sector in Scotland.

Audit Scotland’s funding comes partly from charges to audited bodies and partly from the Scottish Consolidated Fund. Audit Scotland is required to submit its budget proposals to the Scottish Commission for Public Audit (SCPA) for their consideration. The SCPA then make a report to the Scottish Parliament as part of the annual Budget Act approval process.

This paper represents Audit Scotland’s budget proposals for the 2007/08 financial year. A separate paper provides information on Audit Scotland’s proposal for the Autumn Budget Revision for 2006/07.

Business

The business operations and developments are set out in the Corporate Plan 2006-09 as previously outlined to the Commission. Briefly the core business is:

- To deliver the annual audit of around 200 public bodies including the Scottish Executive, Executive Agencies, Non Departmental Public Bodies, NHS Boards and Trusts, Local Authorities and Further Education Colleges
- To deliver a programme of performance audit studies, Best Value audits and overview reports for the Auditor General and the Accounts Commission
- To prepare reports on issues of public concern arising during the year at the request of the Auditor General or the Accounts Commission
- To contribute to the development of public sector policies and practices and to accounting and auditing standards

The environment in which Audit Scotland operates continues to change. Some of the principal factors affecting Audit Scotland’s work are:

- The continuing need for public services to provide improved public services more efficiently
- The growth in devolved public spending and the creation of new spending bodies
- The impact of best value legislation in local government and the application of best value principles across all public services
- The extent and respective roles of audit, regulation and inspection
- The introduction of proportional representation in local government and the likely number of new elected members
Priorities for development of the business include:

- Consolidating and refining the revised risk based audit approach to all sectors including enhancing the links with other work such as Best Value audits
- Completing the first round of Best Value audits in local government, development of Best Value work in other sectors and consideration of the scope of the second round of Best Value audits in local government
- Completing the delivery of the Management Development programme to equip all managers for their roles
- Implementing an electronic documents and records management system
- Contributing to the Scottish Executive’s scrutiny review and the efficient government programme

Efficient Government

The Efficient Government agenda affects all of the organisations that we audit. Audit Scotland is committed to assisting the public sector to achieve efficiencies and is also fully committed to generating its own efficiencies which can be redirected towards better services or returned to audited bodies.

In preparing this budget proposal Audit Scotland has considered ways in which efficiencies may be achieved. Efficiencies included in the budget proposal include a reduction of £160,000 in management costs by not replacing a member of the management team (which represents over 10% of total management salary costs). In addition we have during 2006/07 deleted a further director post in central government work and merged his responsibilities with those of the respective health directors. Assistant Director support to these merged posts has been strengthened. We are also planning a reduction of £75,000 in the cost of NHS audit arising from the dissolution of NHS Argyll & Clyde.

Efficiencies put into place in earlier years will also continue – for example we will continue to only produce local government performance indicators in electronic format, replacement computers will continue to have their useful lives assessed at four years rather than three, and environmental initiatives to continuously reduce consumption of paper and energy. In NHS audits the final element of the reductions in costs arising from the abolition of trusts will be in place for the 2006/07 audits meaning that the total recurring annual savings are £264,000 and the cumulative total up to the 2006/07 audits some £675,000.

Our modernising the audit agenda is directly concerned with improvements to service quality and adding value. NHS audits completed during 2005/06 were the first to be undertaken using the new methodology and early feedback from audited bodies suggests that they consider the audit to be more useful than before. In local government and central government the first year of modernised audits will be completed during the Autumn and we will continue to refine the approach to add greater value and better integration with other audit work such as best value audit. In addition the Accounts Commission are commissioning
Audit Scotland  
Budget Proposal 2007-08

A review of the Best Value audits in local government now that half of the first cycle of audits have been undertaken to see whether improvements can be made and to inform the approach to the second cycle of audits.

Internal reviews of the business along best value principles have commenced and will continue during 2007/08.

Summary of Resource Requirements

<table>
<thead>
<tr>
<th>Summary of resource requirements</th>
<th>2007 ~ 08</th>
<th>2006 ~ 07</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£(000)</td>
<td>£(000)</td>
</tr>
<tr>
<td>Accounts and governance</td>
<td>18,241</td>
<td>17,359</td>
</tr>
<tr>
<td>Performance audit</td>
<td>7,416</td>
<td>7,610</td>
</tr>
<tr>
<td>Other</td>
<td>222</td>
<td>222</td>
</tr>
<tr>
<td><strong>Total Net Expenditure</strong></td>
<td>25,879</td>
<td>25,191</td>
</tr>
<tr>
<td>Income from charges to audited bodies</td>
<td>19,294</td>
<td>18,798</td>
</tr>
<tr>
<td><strong>Net Operating Cost</strong></td>
<td><strong>6,585</strong></td>
<td><strong>6,393</strong></td>
</tr>
<tr>
<td>Capital</td>
<td>523</td>
<td>508</td>
</tr>
<tr>
<td><strong>TOTAL RESOURCE REQUIREMENTS</strong></td>
<td><strong>7,108</strong></td>
<td><strong>6,901</strong></td>
</tr>
</tbody>
</table>

The Total Resource Requirement represents an increase of 3.0% over last year representing increases in costs and is equivalent to the average gross increases in charges to audited bodies. The increase reflects significant increases in depreciation offset by a reduction in employer’s pension contributions and reductions in a number of other corporate budgets. Annex 1 provides a breakdown of costs by sector and Annex 2 provides an analysis by type of expense and analyses this between direct and indirect costs. Notes to the Annex explain the basis of the allocations.
The Capital Expenditure proposal represents an increase of 3% and is principally for Audit Scotland’s rolling Information Technology replacement and upgrading programme.

**Principal Assumptions**

The principal assumptions underlying the budget proposal are:

- General price inflation is included at 2.5%

- Provision has been made for pay increases including increments. Audit Scotland’s pay increases are based on local government arrangements where the basic increase on 1 April 2007 has now been agreed at 2.5%

- Employer’s pension contributions remain at 13% plus £200,000 for 2006-2009 as recommended by the actuarial valuation completed in early 2006

- Increases to approved auditors will be 4% in November 2006 and a further 2.5% in November 2007. The higher increase in 2006 reflects the impact of adopting International Standards on Auditing. These standards have been adopted by all the UK National Audit Agencies. Costs of audit by in house teams are not assumed to rise in the same way as the International Standards have already been incorporated into the revised methodology now in use

- Depreciation will increase from £319,000 to £610,000 as a result of the completion of the refurbishment of the offices at 18 George Street, Edinburgh and the implementation of several technology projects including a new phone system and replacement printers and computers
## Appendix 1

### Cost breakdown in gross terms

The table below analyses the expenditure estimated to be incurred by Audit Scotland:

<table>
<thead>
<tr>
<th>2007-08 Budget</th>
<th>TOTAL</th>
<th>Local Gov't</th>
<th>NHS</th>
<th>Further Educ'n</th>
<th>Scottish Executive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts and governance</td>
<td>18,241</td>
<td>8,669</td>
<td>3,768</td>
<td>525</td>
<td>5,279</td>
</tr>
<tr>
<td>Performance audit</td>
<td>7,416</td>
<td>3,962</td>
<td>1,898</td>
<td>100</td>
<td>1,456</td>
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<tr>
<td>Other</td>
<td>222</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Net Expenditure</strong></td>
<td><strong>25,879</strong></td>
<td><strong>12,631</strong></td>
<td><strong>5,666</strong></td>
<td><strong>625</strong></td>
<td><strong>6,735</strong></td>
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<tr>
<td>Income from charges to audited bodies</td>
<td>19,294</td>
<td>(12,631)</td>
<td>(4,368)</td>
<td>(525)</td>
<td>(1,770)</td>
</tr>
<tr>
<td><strong>Net operating cost</strong></td>
<td><strong>6,585</strong></td>
<td>0</td>
<td>1,298</td>
<td>100</td>
<td>4,965</td>
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</table>

### 2006-07 Budget

<table>
<thead>
<tr>
<th>2006-07 Budget</th>
<th>TOTAL</th>
<th>Local Gov't</th>
<th>NHS</th>
<th>Further Educ'n</th>
<th>Scottish Executive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Net Expenditure</td>
<td>25,191</td>
<td>12,311</td>
<td>5,401</td>
<td>644</td>
<td>6,613</td>
</tr>
<tr>
<td>Income from charges to audited bodies</td>
<td>(18,798)</td>
<td>(12,311)</td>
<td>(4,351)</td>
<td>(544)</td>
<td>(1,592)</td>
</tr>
<tr>
<td><strong>Net operating cost</strong></td>
<td><strong>6,393</strong></td>
<td>0</td>
<td>1,050</td>
<td>100</td>
<td>5,021</td>
</tr>
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</table>
# Subjective breakdown of running costs:

<table>
<thead>
<tr>
<th></th>
<th>2007 ~ 08 (£000)</th>
<th>2006 ~ 07 (£000)</th>
<th>Direct 2007 ~ 08 (£000)</th>
<th>Direct 2006 ~ 07 (£000)</th>
<th>Indirect 2007 ~ 08 (£000)</th>
<th>Indirect 2006 ~ 07 (£000)</th>
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<tr>
<td><strong>Employees:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries and temporary staff</td>
<td>10,950</td>
<td>10,815</td>
<td>9,527</td>
<td>9,352</td>
<td>1,423</td>
<td>1,463</td>
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<tr>
<td>Employer's oncosts</td>
<td>2,750</td>
<td>3,059</td>
<td>2,393</td>
<td>2,645</td>
<td>357</td>
<td>414</td>
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<tr>
<td><strong>Total employee costs</strong></td>
<td><strong>13,700</strong></td>
<td><strong>13,874</strong></td>
<td><strong>11,919</strong></td>
<td><strong>11,997</strong></td>
<td><strong>1,781</strong></td>
<td><strong>1,877</strong></td>
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<tr>
<td>Approved auditors</td>
<td>6,089</td>
<td>5,502</td>
<td>6,089</td>
<td>5,502</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Performance audit and other consultancy</td>
<td>1,162</td>
<td>1159</td>
<td>952</td>
<td>932</td>
<td>210</td>
<td>227</td>
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<tr>
<td>Training and development</td>
<td>510</td>
<td>561</td>
<td>444</td>
<td>485</td>
<td>66</td>
<td>76</td>
</tr>
<tr>
<td>Travel and subsistence</td>
<td>833</td>
<td>846</td>
<td>833</td>
<td>846</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Recruitment &amp; Other Staff Costs</td>
<td>265</td>
<td>268</td>
<td>0</td>
<td>0</td>
<td>265</td>
<td>268</td>
</tr>
<tr>
<td>Professional Subscriptions</td>
<td>40</td>
<td>44</td>
<td>35</td>
<td>38</td>
<td>5</td>
<td>6</td>
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<td>Premises</td>
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<td>0</td>
<td>0</td>
<td>1,419</td>
<td>1,429</td>
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<tr>
<td>Office expenses</td>
<td>511</td>
<td>588</td>
<td>0</td>
<td>0</td>
<td>511</td>
<td>588</td>
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<tr>
<td>IT</td>
<td>451</td>
<td>392</td>
<td>0</td>
<td>0</td>
<td>451</td>
<td>392</td>
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<tr>
<td>Publications and media</td>
<td>273</td>
<td>283</td>
<td>0</td>
<td>0</td>
<td>273</td>
<td>283</td>
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<tr>
<td>Depreciation</td>
<td>610</td>
<td>319</td>
<td>0</td>
<td>0</td>
<td>610</td>
<td>319</td>
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<tr>
<td>Cost of capital</td>
<td>50</td>
<td>20</td>
<td>0</td>
<td>0</td>
<td>50</td>
<td>20</td>
</tr>
<tr>
<td><strong>Total Audit Scotland expenditure</strong></td>
<td><strong>25,913</strong></td>
<td><strong>25,285</strong></td>
<td><strong>20,272</strong></td>
<td><strong>19,800</strong></td>
<td><strong>5,641</strong></td>
<td><strong>5,485</strong></td>
</tr>
<tr>
<td>Accounts Commission costs</td>
<td>157</td>
<td>159</td>
<td>0</td>
<td>0</td>
<td>157</td>
<td>159</td>
</tr>
<tr>
<td>Sundry income</td>
<td>(215)</td>
<td>(253)</td>
<td>-100</td>
<td>-138</td>
<td>-115</td>
<td>-115</td>
</tr>
<tr>
<td><strong>Total Net Expenditure</strong></td>
<td><strong>25,855</strong></td>
<td><strong>25,191</strong></td>
<td><strong>20,172</strong></td>
<td><strong>19,662</strong></td>
<td><strong>5,683</strong></td>
<td><strong>5,529</strong></td>
</tr>
</tbody>
</table>
Notes to Appendix 2

Basis of allocating direct and indirect costs

As a result of discussion with the Commission in previous years about the presentation of information on direct and indirect costs we have reviewed the presentation of this information and concluded that it would be more useful if the analysis of direct and indirect costs was shown on the basis of the subjective breakdown of costs.

Direct and indirect costs can be apportioned in many different ways depending on the nature of the business and the purpose for which the analysis is required. The essential requirement is to enable comparison between years.

The analysis in the table is based on apportioning costs based on the nature of the cost or on the type of work being undertaken.

Staff costs, training and development and professional subscriptions are apportioned on the basis of headcount. Those staff working in the Audit Services Group (planning, delivering and reporting annual audits of audited bodies), Performance Audit Group (planning, delivering and reporting national performance audit studies and best value audits) and Audit Strategy Group (supporting auditors with professional guidance) are regarded as direct costs. Those staff working in the Corporate Services Group (HR, Finance, Information Systems, Communications and Office Services) are treated as indirect costs.

Other categories of costs are allocated as direct or indirect based on their type or, in the case of performance and other consultancy, allocated according to the purpose of the expense eg consultancy to support national studies is treated as a direct cost whereas corporate legal fees are treated as indirect.

In previous years the analysis was presented between the different parts of Audit Scotland and analysed certain costs such as premises, IT and depreciation according to the type of activity being supported. The 2006/07 figures have been restated on the new basis of allocation.
SUPPLEMENTARY EVIDENCE – SCOTTISH COUNCIL FOR VOLUNTARY ORGANISATIONS

Following our evidence session to the Finance Committee on the Protection of Vulnerable Groups (Scotland) Bill, SCVO would like to submit further information on the calculation used for our estimates of £20 million administration costs. We have also provided further information on disclosure checks as a barrier to volunteering together with an idea of the potential costs to Scotland through lost volunteering.

Admin costs calculations

SCVO estimates that from application to receipt of disclosure check the administration costs faced by voluntary organisations are £21.50 per check. This includes time spent by the employee, by administration staff, and by management staff in filling out the application, ID checking, countersigning applications etc as well as postage, stationery, phone and office overheads.

At £21.50 per disclosure check, this amounts to over £20 million (£20,554,000) for the up to 956,000 paid and unpaid staff in the voluntary sector within the scope of the proposed legislation.

Our estimate does not include travel costs/time. However it should be noted that some organisations are spread over a large geographical area. For these organisations this will be a significant further cost over and above our estimates here.

These estimates correspond with a number of our members’ own estimates including the example quoted in verbal evidence of WRVS £250,000 for 12,000 volunteers (around £20.80 a check).

Volunteering statistics

We have received a great deal of anecdotal evidence that disclosure is a major barrier to volunteering, particularly volunteering to work on management committees. This is confirmed by research conducted by Youth Scotland and VDS.

- Disclosures, red tape and compliance consistently cited as barriers to youth volunteering in recent Youth Scotland research
- Those unwilling to work with vulnerable groups increased from 6% in 2004 to 9% in 2005 (VDS)

Youth Scotland

As part of the National Youth Work Strategy consultation: “Youth work – Opportunities for All” the Scottish Executive invited Youth Scotland to consult volunteers in the youth work sector and to gather their views.

Disclosures were consistently cited by respondees as a barrier to volunteering and as an area where support is required. Paper-work, red tape and compliance issues were separate but related issues also highlighted as barriers throughout the research document.
One respondent stated: “Paperwork takes up too much time. Legislation is difficult to navigate. Difficult to get volunteers as it is. Disclosure and fear of litigation is enough to deter people who need some persuading in the first place”.

VDS

The Annual Digest of Statistics on Volunteering in Scotland 2006 brought together by VDS is the most recent research into volunteering. The Digest shows that the number of adults unwilling to undertake a disclosure check to volunteer with children, young people or vulnerable adults has increased from 6% in 2004 to 9% in 2005. Based on 2001 Census figures this represents a further 122699 potential volunteers now stating that they are unwilling to work with these client groups, and a total of 368095.

Financial worth of lost volunteering

A financial equivalent to the additional 122699 people now unwilling to volunteer with vulnerable groups is very difficult to accurately and realistically calculate.

VDS estimate the notional worth of volunteering to be £2.52 billion which would equate the financial ‘value’ of these 122699 people as volunteers to just under £200 million (£198,947,839) for all sectors and just over £150 million (£151,200,047) for those volunteering in the voluntary sector. If 38% (current rate of volunteering) of these people volunteered it would equate to a financial ‘value’ of volunteering in Scotland of around £75 million (£75,600,178) and just over £57 million (£57,456,017) for volunteering in the voluntary sector.

<table>
<thead>
<tr>
<th>Cost of lost volunteers – 100% volunteer</th>
<th>Volunteering across all sectors</th>
<th>£200 million</th>
<th>£150 million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of lost volunteers – 38% volunteer</td>
<td>Volunteering in voluntary sector</td>
<td>£75 million</td>
<td>£57 million</td>
</tr>
</tbody>
</table>

It is impossible to say how many of the 122699 people would actually volunteer but for the barrier of the disclosure system, however these calculations show the potential scale of the damage being caused by the current system and the further damage that could be caused by the proposed Scheme.

I trust you will find this further information useful.

For further enquiries:

Russell Gunson
Policy & Communications Officer
SCVO
Dear Susan

PROTECTION OF VULNERABLE GROUPS (SCOTLAND) BILL: FOLLOW-UP POINTS FROM FINANCE COMMITTEE EVIDENCE SESSION ON 7 NOVEMBER 2006

Thank you for your e-mail of 8 November seeking clarification of a number of points following the oral evidence session on 7 November 2006.

I attach a response to the points you raised in your e-mail. I hope this is helpful to the Committee. Please do not hesitate to be in touch if there is any further clarification which we can provide to you or if the Committee requires any further briefing.

Yours sincerely,

Andrew Mott
Bill manager, Protection of Vulnerable Groups (Scotland) Bill
PROTECTION OF VULNERABLE GROUPS (SCOTLAND) BILL: ADDITIONAL INFORMATION ON COSTS

Clarification of the costs for training the workforce

1. In recognising the concerns surrounding the burden that the Protection of Children (Scotland) Act 2003 would place on certain voluntary organisations, the Executive awarded a grant of £360,000 to a voluntary sector consortium for the development of a support package to assist the sector in implementing the legislation. This grant was to be used to support the achievement of a number of objectives:

   • development of a training and guidance pack;
   • support mechanisms for the raising of awareness in relation to the legislation and its implications; and
   • the delivery of a number of training seminars.

2. It is clear that training was merely one component of the intended support package. When considering the new scheme, the Executive recognised the need for similar support mechanisms to those identified above and reflected this in the Financial Memorandum. On the basis of a like-for-like comparison, we would suggest that the equivalent figure for this Bill would be £800,000, being the sum of the first two rows of the table at paragraph 215 of the Financial Memorandum.

3. Broadly speaking, both children's and adults' workforces are already familiar with the enhanced disclosure regime and the children's workforce is familiar with the requirements of the Protection of Children (Scotland) Act 2003. The new scheme builds on these structures whilst reducing some of the bureaucracy with the result that it should be easier for users. Therefore, it is not anticipated that scheme members would require formal training and the resources have been allocated on a pro rata basis on the assumption that only managers and practitioners would be required to understand all the scheme details.

4. It was acknowledged in the Committee session that awareness-raising for non-practitioners had not been separately identified in the Financial Memorandum. Parents and non-practitioner members of the scheme would benefit from the development of the training and guidance pack principally through awareness raising mechanisms rather than formal training.

When consulting on the options for the Central Barring Unit, were the costs of each option provided so that consultees could consider value for money as well as the principle of each option?

5. The consultation specifically sought views around appropriate governance arrangements for the Central Barring Unit. In particular, it sought to explore the extent to which those arrangements should separate Ministers from the decision making process around individuals. No information was provided on the costs of each option but value for money for the scheme as a whole was explored through seeking consultees' views on an acceptable level of fee. Consultees welcomed the proposals for streamlined vetting and barring but only if the additional cost was modest: the Bill should not increase the overall cost to all users at all.
6. The paper highlighted three possible options for the Central Barring Unit – an executive agency; a core civil service; or a Non Departmental Public Body. It also identified a possible single organisation encompassing Disclosure Scotland and the Central Barring Unit. George Street Research's Analysis of the Consultation identifies a single organisation as the most popular choice (page 46). This model has the benefit of ensuring that Ministers are distanced from decision making, while the organisation is held directly accountable for the delivery of services to a specified standard. It meets the three tests set out in the consultation: it ensures effective flow of information with an end to end process managed by a single organisation; it has a clear and appropriate line accountability; and it is transparently more cost effective than having two separate organisations and associated overheads. This was the option ultimately favoured by Ministers and reflected in the Financial Memorandum.

7. The likely costs of the three options were not set out in the consultation paper. Indeed, it would have been difficult to do so meaningfully. The costs for an executive agency and for core civil service would be essentially the same since staff would be on the same terms and conditions and make use of the same core SE functions. The costs for an NDPB would be very difficult to quantify as they would be dependent on terms and conditions of employment, which would need to be established by the NDPB itself.

If the decision-making structure is likely to be similar to that which is in place now, why has it been determined that the Central Barring Unit will require 30 staff?

8. The financial memorandum identified that the costs of operating the current DWCL are £240,000 per annum to process around 75-80 organisational referrals per annum (paragraph 209). Under current arrangements, it is the organisational referrals which require the effort: court referrals are automatically included on the list. We estimate that the total manpower dedicated to this task is around 4.5 members of staff (including IT support and admin services). We estimated some 2200 to 2500 cases will be referred each year to the Central Barring Unit (paragraph 210), the increase being due to the creation of the adults' list and the continuous vetting of the workforce. Allowing for some modest economies of scale in scaling up operations, 30 staff was the best estimate for the number of staff required.

What is the breakdown of the £1.5 million required for total running costs?

9. The £1.5 million (paragraph 212 of the Financial Memorandum) is the anticipated additional running costs for the barring functions to be added onto the existing functions of Disclosure Scotland. The £240,000 per annum costs of the current DWCL cover approximately 4.5 members of staff (including IT support and admin services). Scaling this up to around 30 staff takes the cost up to around £1.5 million.

10. The figure is equivalent to a cost of £50,000 per head per annum for each of the 30 posts. The £50,000 figure is consistent with experience of previous organisations and includes all overheads such as accommodation, equipment, stationery etc as well as salary and employment costs. Recognising that there will be a range of grades covered, from the chief executive to junior administrative grades, we are satisfied that it represents a reasonable working estimate.

11. The total running costs for the Central Barring Unit, were it being established as a separate entity, would be likely to be significantly higher.
The start-up costs are estimated to be £3.35 million including £400,000 for recruitment and relocation and £600,000 for premises. Where will the agency will be located and how have these figures being arrived at?

12. As a new agency, location will need to be reviewed as part of the Executive’s relocation policy. Any such review will need to take account of:
   - business continuity and the need not to disrupt unduly Disclosure Scotland’s ongoing business;
   - the terms of the Public Private Partnership with BT plc;
   - the overcrowding of current accommodation for Disclosure Scotland;
   - the need for additional staff during the transition onto the new scheme and a reduced requirement thereafter; and
   - the establishment of the Scottish Police Services Authority (into which the rest of the Scottish Criminal Record Office will go) and their own review of their accommodation requirements.

13. The figure of £400,000 for recruitment and relocation was intended to cover the costs associated with recruitment of new staff, relocation of civil servants moving to the agency and the cost of employing staff in the months prior to the scheme going live, in order to provide training for their new roles. The estimate was based on the 30 staff required for the Central Barring Unit, not currently part of Disclosure Scotland, some of whom would need to be recruited externally with the remainder being recruited from the civil service.

14. The figure of £600,000 is based on estimates of £400,000 +VAT to fit out any new accommodation and £125,000 to furnish it. These are based on the total staff of the new agency to furnish and equip any new premises that the agency ultimately occupy. In the short term, it is proposed to use the existing Disclosure Scotland office space as well as temporary additional accommodation. This would allow space to undertake the increased activity required for the first three years of operation.

Staff currently working for Disclosure Scotland will be transferred into the main civil service. What will this cost (assuming employees will be transferred onto civil service terms and conditions) and has this been factored into the overall costs of setting up the new agency?

15. The cost of staff transfer onto civil service terms and conditions have not been included in the Financial Memorandum because a transfer of some sort would have happened regardless of the advent of this Bill. Disclosure Scotland staff are part of the Scottish Criminal Record Office and, as such, would have been due to transfer to the Scottish Police Services Authority in April 2007.

16. There will be one-off costs associated with pension transfers. This includes Government Actuary costs to effect the transfer, estimated to be in the region of £50,000 to £100,000. There is also the cost of making up any pension shortfall at the point of transfer, which depends on the financial health of the Strathclyde Pension Scheme on the day of transfer. The Executive will be required to make good any shortfall. Preliminary estimates suggest that this will not be significant, as the Strathclyde scheme is very buoyant and Disclosure Scotland staff have relatively few years of contributions to the scheme.
Numbers of individuals in the scheme

17. There was some confusion at the Committee hearing as to the number of individuals who would require to be scheme members. The Financial Memorandum is predicated upon the following numbers and assumptions:

- 800,000 individuals undertake voluntary work in sectors affected by the scheme\(^1\). This does not necessarily mean they need to be scheme members;
- 580,000 individuals undertake paid (i.e. not voluntary) work which will be regulated work and, therefore, they will be required to be scheme members\(^2\);
- there is significant overlap between these two categories of people, we assumed 60% of the 580,000 individuals (= 350,000) undertaking paid work would also volunteer\(^3\);
- therefore, 450,000 volunteers would not be scheme members through any paid work they may do; and
- the financial memorandum further assumes that only 50% of these 450,000 volunteers (= 225,000) actually need to be scheme members\(^4\) (for example, a volunteer fundraiser for Barnardos is in the sector but not doing regulated work).

<table>
<thead>
<tr>
<th>Involvement with scheme</th>
<th>Number of individuals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individuals paid to do regulated work who don't volunteer</td>
<td>230,000</td>
</tr>
<tr>
<td>Individuals paid to do regulated work who also volunteer</td>
<td>350,000</td>
</tr>
<tr>
<td>Volunteers who don't do paid regulated work who need to be scheme members on basis of 50% assumption</td>
<td>225,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>805,000</strong></td>
</tr>
</tbody>
</table>

Table showing summary of workforce coverage.

18. The figure of up to one million individuals (paragraph 200) is attained if 100% of volunteers in the sector need to be covered (the total in the table above rises to 1,030,000 individuals). The Financial Memorandum illustrates the effect of this on costs and fees in the final two rows of table 3.

19. The modelling to calculate the number of full and nominal checks required by sector is complicated but the table above shows that we believe the number of volunteers needing to join the scheme *only because of their volunteering activity* is very much less than the 800,000 total volunteers in the sector. When natural volunteer turnover is factored into an

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\(^1\) According to the Scottish Household Survey, there are 1 million volunteers in Scotland. From the Scottish Council of Voluntary Organisations, we know that 80% of all volunteers volunteer in sectors which would be covered by the Bill. Combining these two sources suggests 800,000 volunteers will be working in sectors affected by this scheme.  
\(^2\) Assembled from official Government employment statistics in relevant sectors.  
\(^3\) The Scottish Household Survey indicates that around 30% of adults in any employment also volunteer. We have assumed a much greater propensity to volunteer amongst individuals undertaking paid regulated work. We have assumed that 60% of this workforce will volunteer.  
\(^4\) This 50% assumption was explained by officials at Col 4126 of the official report. For the sake of clarity, the argument is repeated here. Data from Volunteer Development Scotland, while not directly supporting this assumption of 50% of volunteers requiring checking, provides crude upper and lower bounds for the proportion of 75% and 32% respectively. The bounds come from the (overlapping) breakdown of volunteering in Scotland by activity. Some 68% of volunteers spend at least part of their time raising money, which implies that the 32% who do not are likely to require to be checked as their volunteering is likely to involve contact with vulnerable groups. Adding up the 31%, 19% and 24% (= 74%) who are listed specifically as taking part in volunteering activities of one sort or another that involve contact with vulnerable groups gives the upper bound figure. Taking the mid-point of this range gives 53%, which is comfortably close enough to the assumed value to give a degree of confidence to the assertion.
extended transition period, the number of "retrospective checks\textsuperscript{5}" required rapidly diminishes.

Other points

47\% rise in disclosure fees

20. On more than one occasion, it was suggested in the Committee session, and recorded in the official report, that the recent 47\% increase in disclosure fees was a consequence of the Protection of Children (Scotland) Act 2003. For the record, the fee increase in April 2006 was a reflection of fewer than expected disclosure applications in the first four years of operation of the system, therefore yielding a much lower revenue than anticipated. We now have a much better understanding of the volume of requests for disclosure checks which has informed the development of this Financial Memorandum. The fee increase was not connected to the commencement of the 2003 Act on 10 January 2005.

£100m additional costs

21. In Column 4138 of the official report, Wendy Alexander MSP asks whether there was a cheaper way of obtaining the same policy effect rather than spend £100 million over ten years. Paragraph 193 of the financial memorandum is clear that the current disclosure system costs £100m over ten years and this scheme is estimated to be less expensive through increased efficiency. It is therefore important to note that there is no £100 million additional expenditure but rather a slight reduction on planned expenditure of £100 million over 10 years. The overall effect of the scheme should be to reduce the total amount of disclosure fee revenue collected.

Protection of Vulnerable Groups (Scotland) Bill Team
16 November 2006

\textsuperscript{5} I.e. checks required to get individuals onto the scheme during the transition period other than through taking up a new post