

MEETING OF THE COMMISSION

Wednesday 23 April 2008

Session 3

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SCOTTISH COMMISSION FOR PUBLIC AUDIT **1st Meeting 2008, Session 3**

CONVENER

*Angela Constance (Livingston) (SNP)

COMMISSION MEMBERS

*Robert Brown (Glasgow) (LD)

*Derek Brownlee (South of Scotland) (Con)

George Foulkes (Lothians) (Lab)

*Hugh Henry (Paisley South) (Lab)

*attended

THE FOLLOWING GAVE EVIDENCE:

Jay Hussain (HW Chartered Accountants)

SECRETARY TO THE COMMISSION

Mark Brough

LOCATION

Committee Room 4

Scottish Parliament

Meeting of the Commission

Wednesday 23 April 2008

[THE CONVENER *opened the meeting at 10:32*]

Economy, Efficiency and Effectiveness Examination of Audit Scotland

The Convener (Angela Constance): Good morning, colleagues. I apologise for being slightly late; the traffic on the M8 was hectic this morning, although I am sure that other people have had to travel from further afield. I remind colleagues to turn off mobile phones. We have received apologies from George Foulkes, who has a long-standing pre-existing engagement and unfortunately cannot be with us.

There are a couple of items on our formal agenda. I think that it would be useful for us to have, with members' indulgence, an informal discussion in preparation for our next meeting. I intend that the formal and informal parts of today's meeting will be concluded before 12 o'clock, if members consider that to be appropriate.

Under agenda item 1, we will take a further look at a follow-up to the previous three Es—economy, efficiency and effectiveness—study in terms of scope, efficiency and purpose. I welcome Jay Hussain, who represents the auditors Haines Watts Chartered Accountants and thank him for coming. We have a paper in front of us that has been circulated to members; perhaps you can say a few words to introduce your paper, and no doubt members will have a few questions afterwards.

Jay Hussain (HW Chartered Accountants): As ever, it is a pleasure to be here, so thank you for inviting us. As members know, the Scottish Commission for Public Audit commissioned a value-for-money review in our first year as the commission's external auditors. The review, which was undertaken in 2006 and presented to the SCPA in November of that year, examined the fees and charges mechanism that is used by Audit Scotland in local authorities and public sector bodies. It considered how those fees are derived and calculated, and how much it costs to deliver the audit by Audit Scotland.

The issue is not how cheap that audit product is, but how effectively it is delivered. As a result, the report was ultimately quite expansive. It covered a lot of areas and we tried to look at many streams in some depth; there is a lot to take on board. Yesterday, I cantered quickly through the report

but the time is about right to take stock of where Audit Scotland stands against some of the issues that emerged in the report.

As I said, there was a lot in the report—it was 48 pages long—although we distilled the key issues into the executive summary and converted them into recommendations that Audit Scotland agreed to have regard to and implement. Those recommendations are contained in the attachment to the paper that I submitted. The purpose of a follow-up would be to take stock of where Audit Scotland is on those issues. Some of the issues are fundamental, while most are strategic and far-reaching, and they are consistent with Audit Scotland's corporate plan; that is the bit in which the SCPA will become interested.

The key objectives in Audit Scotland's corporate plan are about the efficient management of financial resources, maximising the value of the audit product that is delivered to local authorities and health sector bodies, and building an effective and efficient organisation. I like to think that our report touched on those areas, either in summary or in detail. Audit Scotland was, at that time, evolving, moving and looking at its fee structure, but that process was about looking to the future. Now that it has been 12 or 18 months since the review, we advise that some form of follow-up should be done, by us or by your internal auditor.

The commission has in front of it our suggestion for a limited scope follow-up. Follow-ups, by their nature, can be anything from a self-assessment exercise that takes a day or two, to something quite detailed, which was the foundation of our original terms of reference, or something in between, which is what we suggest. However, because of the expansive nature of the review that was undertaken a couple of years ago, some effort will need to be put into a follow-up to get some meaning from it. There is always a risk that, during a follow-up, the issues are looked at in broad-brush terms, and it is arguable that that will not add much value or tell you anything that you do not already know from your discussions with Audit Scotland.

That is the background to the paper that members have in front of them. I am happy to have the discussion and take questions.

The Convener: Thank you. Questions, please.

Hugh Henry (Paisley South) (Lab): What would the implications be if we did not have a follow-up? Have we done sufficient work in the audit process so far to assure ourselves that Audit Scotland is using resources carefully, prudently and expeditiously? What added value will we get if we carry out this extra bit of work?

Jay Hussain: I would not look at it as an extra piece of work; it would just be a completion of

what was started two years ago. That said, if you feel that you have sufficient evidence, and you are comfortable that each of the areas mentioned in our report has been adequately addressed by Audit Scotland, you might decide that you do not want to commission a follow-up. That decision would be based entirely on the evidence that you have to date that the recommendations have been actioned.

Hugh Henry: My question is what benefit we would get from doing this extra piece of work that we would not get if we did not do it.

Jay Hussain: There is a governance issue. When you pay for an audit or inspection report, there is always a risk that it will come up with recommendations. You need to be sure that those recommendations have been taken seriously and that something has been done about them, otherwise the value of the original piece of work could be questioned. From an audit perspective there is, among other things, an issue of completeness.

There are issues with regard to added value. The report picks up on the fact that, at the time of the audit, we challenged the input-orientated nature of Audit Scotland's operations. There was not much emphasis on how much a piece of work would cost; the emphasis was very much on quality, whatever the cost. It is acknowledged that that needs to change slightly if Audit Scotland is to build an effective and efficient organisation.

The director of strategy had just set up a working group to look at the time recording system; although there was a system in place, it was not being fully utilised, so that gave rise to a value-for-money issue. We would ask Audit Scotland how that work had progressed and whether it had started to cost properly assignments that are undertaken by the public reporting group in producing national reports. At the moment, we do not know the answer to such questions. I did not know at the time of the audit; that is what we commented on. You may feel that you have sufficient evidence—that is up to you.

Robert Brown (Glasgow) (LD): Previously, we discussed end-year flexibility and the difficulty that arises with transparency in relation to inputs and so forth, because of the carryover and the audit issues that arise from the year end. There are issues about all of that.

Another issue was that the Auditor General and Audit Scotland should institute best practice as an exemplar to the profession. Could the follow-up work take on board, as part of its consideration of transparency, the issues that we were concerned about previously?

Jay Hussain: The short answer is yes. We were being guarded, but the clear subtext that ran

through the review that we undertook two years ago was transparency. The fee-setting mechanism is complex. That is not deliberate; it is just the way in which the structure has evolved. The old system was based on how many days it would take to do an audit. The new fee-for-audit element was introduced in 2000, following the commissioning of work on the fee structure by Robson Rhodes. The system includes bits of both those elements.

On top of that, there are fees that are directly attributable to an audited body and there are costs of national reviews that are apportioned to audited bodies. The question that arises is whether the audited bodies should be able to challenge the value they get for that apportioned cost of national studies, which might not be relevant to them. Many different things are going on in respect of fee-setting and the issue around deliverables or audit products. That was a bit of a roundabout explanation, but the answer to your question is yes—it is about transparency.

One recommendation in our report is that when Audit Scotland sets the audit fee, it should be clear what part of the fee is directly attributable to the audited body and what is not. Part of the fee is not directly attributable to the audited body, but the body is charged the fee anyway because Audit Scotland's public reporting group is producing a national report from which it will have some indirect benefit. That is fair enough, but let us be clear about it and about the potential benefit that the audited body can get from the review. That goes straight to transparency.

Derek Brownlee (South of Scotland) (Con): In the review's recommendations, it was suggested that the time and cost recording systems were perhaps not as developed as you would want them to be. I presume that the follow-up study would analyse progress in that regard. If the follow-up study was commissioned and the work was undertaken, would that allow us to assess, from our other perspective of examining Audit Scotland's budget, the extent to which there is slack or pressure—if any—within Audit Scotland in respect of its audit capabilities, compared with what it is structured and resourced to do?

10:45

Jay Hussain: Theoretically and practically, yes. That is the whole point. To know how much it costs to do something, it is necessary to know how much time has been spent doing it.

There are two aspects to that. First, there is the general issue that Audit Scotland has in place a time recording system that has been paid for but is not being used. Straight away, that is a cost from which no benefit is being gained. If that system is to be used, there will need to be a bit of a culture

change in Audit Scotland. This is not a fault but, like the Audit Commission in England and Wales, historically, Audit Scotland has been very much an input-orientated organisation, unlike the firms. That is why the market was opened up to bring in the firms, which injected an element of competition.

When we produced our report, I believe that Russell Frith was looking into the development of the time recording system with a view to ensuring that people on the ground recorded their time. Even before that happens, a cost budget needs to be set for a particular assignment. At the moment, I do not think that that happens. A time budget is set, but not necessarily a cost budget. If a cost budget were set, the time recording system would need to be used to calculate the costs against that cost budget. The answer to your question is yes. The review would assess how far Russell Frith has gone in developing the system and to what extent it has been rolled out.

The Convener: In the first recommendation, you say that the fixed part of the fee should be related to outputs. As a layperson, I wondered why only the fixed part of the fee, rather than the whole fee, should be related to outputs.

Jay Hussain: I will work backwards. The audit fee has two components—it is made up of the fixed charge and the agreed fee. The agreed fee is agreed with the audited body anyway, so the audited body knows what it will get for that fee. The fact that that part of the audit fee is agreed directly with the audited body means that it is transparent.

The fixed charge is the cost that is incurred by Audit Scotland in delivering national reports and health sector audits, and it absorbs the overheads that are involved in running Audit Scotland. That sum is apportioned among the audited bodies. It is evident that that part of the audit fee is less transparent. I would not like to say that the fixed charge is an overhead; in essence, it is a more indirect element of the audit fee.

If Audit Scotland's public reporting group undertakes a national review of social care and children's services, the cost of undertaking that study has to be apportioned among health bodies. A health body could object to being apportioned a charge of £X on the ground that it was not sure how that national study would benefit its work in a particular year. The recommendation to which you refer is about Audit Scotland giving—right at the beginning of the process, when the fixed charge is set—a much clearer explanation to the audited bodies of why they will be asked to pay that chunk of fee and how the national study in question could benefit them.

I do not know whether I have made the position clearer or muddier. We refer only to the fixed-charge element, because that is the more indirect element of the total audit fee. The agreed fee is the direct cost of delivering the audited body's statutory audit—that bit is okay.

The Convener: As members have no more questions, I am interested to hear views on how we should proceed. Having listened to colleagues' questions, I get the feeling that although we could all do with some assistance from professionals to ensure that the recommendations of what was a rather expansive study have been met, and that they help us in our continuing role, we should guard against audit for audit's sake. Are the proposals in front of us acceptable or do members want to discuss them further?

Robert Brown: I think that the proposals are acceptable. I accept Hugh Henry's point about not doing unnecessary work, but there is a follow-up job to be done. Significant issues emerged from the general discussions that we have had about the extent to which Audit Scotland was being transparent and the mechanisms that caused us—never mind members of the public—difficulties in understanding the position. There is a reason to go ahead with a further report. The cost is £5,000-odd. That is the downside. On the other hand, we should be able to get some benefit from it. If it is seen as a one-off, it is probably okay.

The Convener: Do other colleagues think that the proposal is proportionate?

Derek Brownlee: In cost terms, the proposal seems proportionate, given the proposed fee in relation to the Audit Scotland project. If we consider the proposal in the context of not just follow-up work but how it might assist us in our other roles in relation to scrutiny of Audit Scotland, it seems reasonable.

Hugh Henry: I am content to go along with those views.

The Convener: Mr Hussain, I think that we have unanimous agreement that we are happy to proceed with the follow-up work in the terms that you have laid out. Thank you for your journey time and your time with us this morning.

Jay Hussain: Not at all. It is a pleasure.

Budget Process (Finance Committee Review)

10:51

The Convener: Agenda item 2 is consideration of correspondence from Andrew Welsh, the convener of the Finance Committee. He alerts the commission formally to the review of the budget process. If, as a result of the review, any changes are proposed to our relationship or written protocol with the Finance Committee, we will be duly informed and consulted. Any changes will be agreed mutually. I do not see this as particularly controversial, unless somebody knows something that I do not, which is possible.

Derek Brownlee: I sit on the Finance Committee. The review is much more focused on the Government budget than the SCPA. I stand to be corrected, but I would be surprised if the Finance Committee were to receive any representations on the SCPA's part of the budget process, unless we choose to make any. Having said that, if there are any deficiencies in the current process, this would seem the natural time to try to address them as part of a broader review. I imagine that there will be a fair opportunity for the SCPA to influence the way that the process works in relation to our role.

Robert Brown: I think that that is right. We all have our strong views about the budget process and its advantages or deficiencies. However, I do not think that it is the role of the SCPA to comment on broader issues. I do not know whether there is much in the review that relates to our interests.

The Convener: We shall just note Mr Welsh's letter. Members will be duly informed if there is any need for our further involvement.

Meeting closed at 10:53.

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