

MEETING OF THE COMMISSION

Wednesday 16 September 2009

Session 3

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SCOTTISH COMMISSION FOR PUBLIC AUDIT 2nd Meeting 2009, 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:

Mr Robert Black (Auditor General for Scotland)

Russell Frith (Audit Scotland)

Richard Gibson (Haines Watts)

Diane McGiffen (Audit Scotland)

SECRETARY TO THE COMMISSION

Mark Brough

LOCATION

Committee Room 3

Scottish Parliament

Meeting of the Commission

Wednesday 16 September 2009

[THE CONVENER *opened the meeting at 10:33*]

Audit Scotland Annual Report and Accounts 2008-09 and Auditor's Report

The Convener (Angela Constance): Good morning, colleagues. I offer a warm welcome to members and to our witnesses. I remind colleagues to switch off their mobile phones. We have received no apologies this morning, although it should be noted that Hugh Henry is running a little late because of a constituency engagement.

Item 1 on the agenda is consideration of Audit Scotland's annual report and accounts for the year to 31 March 2009 and the auditor's report on the accounts. As we know, the Scottish Commission for Public Audit is responsible for securing the audit of Audit Scotland's accounts and has contracted Haines Watts to undertake that work. We have before us the 2008-09 annual report and accounts and the auditor's report. We now have a chance to take evidence on those.

We will hear first from representatives of Audit Scotland. We will then hear briefly from the auditors to confirm their opinion. I extend a warm welcome to Robert Black, the Auditor General for Scotland, who is the accountable officer for Audit Scotland; Russell Frith, the director of audit strategy for Audit Scotland; and Diane McGiffen, the director of corporate services for Audit Scotland. I invite Mr Black to make an opening statement.

Mr Robert Black (Auditor General for Scotland): Good morning. I confirm that the annual report and accounts were considered in detail and signed off by the Audit Scotland board. The commission will hear later from Mr Gibson of Haines Watts, which has issued a clean audit certificate and independent assurance for the internal control statement.

The year 2008-09 was one of significant achievement for Audit Scotland in which we made major progress towards the financial objectives that the SCPA has encouraged us to adopt. I turn first to the performance of Audit Scotland. In the year in question, we produced 30 public performance reports, examples of which include significant pieces of work on drugs and alcohol services in Scotland; day surgery; palliative care; the First ScotRail passenger rail franchise; a large

report on the management of major capital projects in Scotland; and reports on the management of spending on sport in Scotland, the management of prisoner numbers and its implications, and the use of consultants in central Government.

It is always important to emphasise that we do a lot of work that is not necessarily well sighted in the SCPA's view of the world. I refer to the 200 or so annual audits of public bodies in Scotland, some of which lead to reports. For example, reports on individual further education colleges, Western Isles NHS Board, Highlands and Islands Enterprise and VisitScotland have been considered in Parliament by the Public Audit Committee.

Lying behind the fairly large number of final audit reports, all of which are available on our website, are about 900 separate reports that have been produced for the 210 public bodies that we audit. The reports cover a wide range of areas such as financial systems, partnership working and information and communications technology. The Parliament's Public Audit Committee takes evidence on some of our reports, which adds greatly to the impact of Audit Scotland's work. Auditors can take issues only so far. In a sense, we then pass matters over to the PAC, so that it can hold people to account for what the audit reports say.

Another area of significant achievement in the past financial year was the completion of all 32 best-value reports on the 32 Scottish local authorities. Those have been considered and findings have been made by the Accounts Commission. There is no equivalent of that regime anywhere else in the United Kingdom. It is made possible only by the fact that devolved government in Scotland allows us to develop and run the system. Most councils now have improvement plans in place on the back of the best-value audits; others are working on them. In the annual report, we outline the principles that will be applied to the next round of local government best-value audits, such as greater emphasis on outcomes, partnership working, the experience of service users, and economy, efficiency and effectiveness. Finally on the best-value theme, we have made good progress in promoting a common best-value framework across the rest of the public sector in Scotland.

Audit Scotland also has a central role in supporting the Accounts Commission to help manage and reduce the overall scrutiny burden for public bodies in Scotland. That work is designed to improve the effectiveness of scrutiny, as well as to reduce the burden. The Accounts Commission has the formal co-ordinating role in relation to other scrutiny bodies. Along with the inspectors and

other scrutiny agencies, Audit Scotland is included in the development of a shared risk assessment approach. In the past year, we have also made significant progress in preparing for the impact of the new accounting standards—the international financial reporting standards, which members of the SCPA will know about.

For the interest of members, I will mention two other areas of work. First, we continue to run the national anti-fraud initiative, which has now identified around £40 million and led to at least 75 successful prosecutions. The initiative will be broadened out further in the current year. Secondly, I would like to touch on the work that we do with other countries. Audit Scotland is increasingly known and recognised for its work. That is reflected in the growing number of requests for assistance that we get from overseas organisations. The annual report contains a brief outline, but a separate report on our website gives more detail of the work that we have been doing, mainly with eastern European and developing countries.

Having described the broad spectrum of work that Audit Scotland has undertaken over the past year, I turn briefly to financial aspects. As I said, our accounts have been considered in detail by the Audit Scotland board, but I would like to highlight two points. The first is that our underlying financial performance is improving. Our outturn at the end of the year was much closer to budget than in previous years. Setting aside the impact of pensions and end-year flexibility, the outturn is only roughly £0.6 million, or £600,000, below budget, which is about 2 per cent of our overall budget. Frankly, for a relatively small organisation such as ours that has a fairly complex funding model, with income from different sources, that is as close as we would like to be. I do not think that we can get the figure down much more than that.

Through that and our EYF bid, which the commission will discuss later, we have followed up on our commitment to move to an end-year position that is closer to budget and to reduce our requests for EYF. We indicated previously that it would take about two years to move to that situation, and we are still on course for that. In fact, we are further ahead than we thought we might be.

Thank you for allowing me to make those opening comments, convener. My colleagues and I are happy to answer questions. They will be able to answer in greater levels of detail than I might.

The Convener: Thank you, Mr Black. We appreciate that overview. I have a general question before I open the floor to my colleagues. On page 1 of the annual report, Audit Scotland acknowledges that we are in

“the most challenging external economic environment since Audit Scotland began”.

Has the economic climate in which we are all operating had any implications or ramifications for Audit Scotland and its internal finances?

Mr Black: There are a couple of things to say on that. First, we must ensure that our work makes as big a contribution as possible to economy, efficiency and effectiveness in the public sector. We will continue to have dialogue on that with the Public Audit Committee. Secondly, there is the issue of how we carry out our work to minimise the burden on public bodies. The work that is being undertaken on improving our audit methodologies and linking into the scrutiny review are helping to reduce that burden. Having said that, in relation to the work that we do, one important point that I am sure commission members will appreciate is that, in the era of retrenchment and constrained resources that we all agree we are entering, it is even more important to have high-quality audit to ensure that budgets are well managed and that strong controls are in place throughout the public sector. I think that most, if not all, of the public sector will find it extremely difficult to manage us through the next few years properly.

In relation to our activities, there is no question but that the investment that we have made using EYF and other measures will make us a more efficient and effective organisation. I am grateful for the support that the SCPA has given in that regard in the past couple of years. We are coming out of that process in pretty good shape, with good information technology systems in place, which is enabling electronic working papers to be produced and so on. We are becoming more efficient. As our annual report notes, we have met our efficiency targets. When we present to the commission the budget for next year, which will probably be at the commission's next meeting, you will find that we are confident that we will be able to continue to meet that efficiency target.

It will become increasingly difficult for a body such as Audit Scotland to generate cash-releasing efficiencies, principally because our work centres on the work of professional people and support staff. Without revisiting fundamentally the nature and scope of audit work, it is difficult to see ways in which we can generate large cash savings in future years. However, we will produce a budget with a commitment to look seriously at our accommodation costs and to try to reduce them by a substantial amount, which will involve new ways of working and so on. However I would prefer to leave that issue until the commission's next meeting, when we will have fuller information available.

10:45

Robert Brown (Glasgow) (LD): I have a couple of overview questions. You have talked about the work that you do with other countries and so forth. Indeed, you made the point that best-value reviews of Scottish councils are ahead of what happened in the rest of the UK. From the experience that you gather from other countries, are you able to make any observation about the efficiency of councils and other public bodies in Scotland vis-à-vis those in other parts of the UK and abroad? Do we do better, worse or similarly? Can you give us a picture of all of that?

Mr Black: There is no simple answer to that question. When we undertake performance audit studies, we are sometimes able to include information that compares Scotland with other parts of the United Kingdom. For example, we can compare performance in parts of the health service in Scotland with performance elsewhere in the UK. Across the UK, for common activities such as the collection of council tax—although it is some time since we looked at that—we are able to compare the performance of Scottish local authorities with the performance of local authorities in the rest of the UK. In general, however, it is not possible for us to say whether performance is more efficient in Scotland than it is south of the border.

We continue to keep that issue under review, in partnership with bodies such as the National Audit Office and the Audit Commission. From time to time, it is possible for us to undertake joint pieces of work. However, the only one of significance that we have undertaken in recent years was a joint exercise, which we initiated, to develop performance indicators for corporate and central support services. That was an extremely useful exercise and it has been rolled out—to use that awful language—in the public sector through our audit process to encourage bodies as varied as higher education institutions, councils and FE colleges to adopt those performance indicators.

I am sorry that this is not a succinct answer. We are mindful of the issue and, whenever we plan a piece of work, we consider whether it is possible to compare Scotland with other parts of the UK. It is even more difficult to compare ourselves with Europe, as the services that are provided there are so different. We all know about the high-level comparators that are published by academic institutions and think tanks, which compare public services in the UK with those in other countries. However, those are always fraught with problems of data comparison and are always hedged with qualifications and restrictions. Given the fact that we proceed on the basis of robust audit evidence, it is usually quite difficult for us to do that.

Robert Brown: My other overview question relates to what you said about your auditing 210 public bodies. Has that number gone up or down in the past couple of years?

Mr Black: I ask Russell Frith to help us with that question.

Russell Frith (Audit Scotland): The figure of 210 is slightly higher than in the previous year, as a number of new public bodies that were created over the past two to three years came through. Those included the regional planning partnerships, the regional transport partnerships—although those might have been created the year before—and the community justice authorities.

The number will start to decline slightly due to some of the mergers and abolitions of bodies under the Government's reorganisation proposals. However, the number of bodies that we audit will not fall at the same speed as the number of public bodies, as many of those that are being merged or abolished do not produce separate reports and accounts of their own.

Robert Brown: Does that link into Audit Scotland's staffing levels, which have gone up over the past year for both full-time equivalent staff and seconded staff, or is there a broader explanation? There seems to have been a significant increase in the number of staff against the background of the climate that you are talking about.

Mr Black: Diane McGiffen will answer that question.

Diane McGiffen (Audit Scotland): Certainly. Good morning. The average number of staff that we had in post last year went up significantly. You can see the results of that in the outputs from the year—it was a very busy year for us. We have an establishment figure, which is the number of people that we need to do the jobs and the work that we have to deliver. That has stayed fairly constant over the past four or five years at 297. We have not achieved the average number of full-time employees each year because of staff turnover—people coming and going—and difficulties filling vacancies. We are much closer to that figure now as a result of a number of factors, such as the conscious efforts that we have made to fill vacancies permanently and the slowing down of turnover as the economic situation has changed. We are now much closer to our establishment figure. The number of employees that we need to do the job has not changed significantly over the past number of years, but the average number that we have had in post during the year has moved.

Robert Brown: I will come back on some minor points, but colleagues might want to come in first.

The Convener: I have a question about the 210 audits that were completed. The annual report helpfully includes a breakdown of those audits: 74 are central Government audits and 23 are national health service audits. It would also be useful to know—I do not necessarily expect you to have the information to hand—how many of the 74 central Government audits were completed by Audit Scotland and how many were completed by private firms. Similarly, how many of the 23 NHS audits were done by Audit Scotland and how many were done by private firms? I would also like that information for the audits that were carried out into further education colleges, councils, joint boards and so on.

Russell Frith: I do not have that information with me, but I am happy to provide it. I know that we have it readily available.

The Convener: I am sure that we have discussed this point before. I noticed that, numerically, there seems to be almost a 50:50 split between the work undertaken by Audit Scotland and that undertaken by private firms, but two thirds by public sector expenditure is covered by the Audit Scotland work. Is that a matter of chance or is there a reason for it?

Russell Frith: There is a reason for it. The number of bodies that the firms audit, as opposed to the value of the audits, is higher, because the firms do more of the smaller bodies; principally, they deal with all the further education colleges, which are, on average, small bodies.

Derek Brownlee (South of Scotland) (Con): In previous meetings we have discussed at some length the fee strategy and you have also talked about rebates. The breakdown in the accounts of the way that fee income has developed over 2008-09 indicates that the trend for local authorities and health bodies is a reduction in comparison with the previous year, whereas there is an increase for central Government and Scottish Water. Is that the result of a conscious decision, or is there another explanation for the emergence of the different trends?

Russell Frith: The main reason why the figures in note 5 in the notes to the accounts look as if they are falling in relation to local authorities and the health service is because the 2009 figures are net of the rebate of £1 million that was applied across most, but not all, bodies.

Derek Brownlee: You have perhaps answered this question in the past, but can you remind me why the rebate applies to those bodies but not to others?

Russell Frith: Sorry, it was also applied to some central Government bodies, but it was not applied to the further education bodies because

we did not feel that any of the underspend that gave rise to the rebate originated in that sector.

Derek Brownlee: If the rebate was applied to the central Government bodies, is there another reason why that income is still going up?

Russell Frith: There is a slightly increased number of bodies in the sector, but it is mainly a matter of timing around the work that is done pre and post 31 March. The income figure relates only to the central Government bodies that we charge for. We do not charge for a significant chunk, including the core Government account, so that work is therefore not reflected in the figure. The balance of the work that is done between the non-chargeable and the chargeable in any year also impacts on how those figures move between any given two years.

George Foulkes (Lothians) (Lab): As the questions that I want to ask may appear slightly critical, I begin by saying that I know from my membership of the Public Audit Committee—which is chaired so well by my colleague Hugh Henry, who is on my right—of the excellent work that is done by Audit Scotland, both at home and overseas. That work has been commended by the committee.

I want to ask about Audit Scotland's demographic profile, which is mentioned on page 14 of the annual report. The gender balance is excellent, in that you employ slightly more women than men. The age balance is almost a perfect—

Mr Black:—normal curve.

George Foulkes: Yes, but there are only five minority ethnic members of staff, despite your implementation of the Scottish Government's equality impact assessment tool, the provision of training and so on. Why do you think that that is the case?

Mr Black: I will start off, before inviting Diane McGiffen to give a much fuller answer. She will be able to give you an indication of how we operate our policies. I emphasise strongly that we take equality and diversity extremely seriously. That, of course, applies to our recruitment policy—we are extremely rigorous about trying to screen out any bias through the procedures that we use for recruitment. Broadly speaking, I think that it is fair to say that the make-up of the profile of our staff is pretty close to the make-up of the profile of the Scottish population. I am sure that Diane can help with that.

Diane McGiffen: That is correct. We analyse our staffing data against the Scottish population data and our staffing profile is highly consistent with the population of Scotland overall. However, as part of our commitment to diversity and equality, we have taken a close look at all our

practices, our recruitment tools and methodologies, our advertising and how we position ourselves in the labour market, to ensure that we are reaching the widest and most diverse group possible. We have worked closely with recruitment consultants who specialise in recruiting from minority ethnic groups, and they have given us advice on ways to position ourselves, recruitment markets and tools to use. We have not yet seen a positive outcome from that work in our recruitment figures, but it is something that we monitor closely. We are sure that the processes that we adopt are free of bias.

George Foulkes: Does the white group contain significant numbers of members of the immigrant communities that we have in Scotland, such as Poles, Germans, French people or Americans?

Diane McGiffen: I can tell you informally that there are such people among our staff, but the formal answer is that we do not collect the data in that way. We use the same categories that are used in the census, so people record their nationality in broader categories. However, I know from knowing my colleagues that they include many people with interesting and diverse backgrounds.

George Foulkes: I have one more question on the same subject. Is part of the problem the fact that not many accountants or people in related professions are from minority ethnic groups?

Mr Black: I do not have such information to hand. Russell Frith might know about that through his professional network.

Russell Frith: I do not know what the situation in Scotland is, but in the UK as a whole, a reasonable number of people in such professions come from Asian or oriental backgrounds, in particular.

11:00

George Foulkes: I would be grateful if you would keep an eye on the issue and do everything possible to ensure that people from different ethnic backgrounds have an equal opportunity.

My other, quite separate question refers to the information, also set out on page 14 of the annual report, that you managed to pay 92 per cent of invoices within your target time of 30 days. Do you know the percentage of invoices that were paid within the new standard time of 10 days? After all, you will know only too well that it is particularly important to small businesses that their bills be paid as quickly as possible.

Mr Black: I ask Diane McGiffen to help with the data in that area.

Diane McGiffen: I do not have that figure with me. However, we expect the new electronic purchase ordering system that we are about to introduce to allow us to speed up payments towards that 10-day target. I can come back to the commission with what information I can find, but I have to say that it might take some digging because that is not how we currently collect it.

George Foulkes: I would certainly find it helpful.

The Convener: The commission would appreciate that information.

Robert Brown: Last year, Mr Black told us at some length about a correspondence-handling pilot, which I believe cost £81,000 for 200-odd items of correspondence. That works out about £810 per item but, in your report, you say that you seek to acknowledge correspondence within 10 days and to respond within a month of that acknowledgement—in other words, six weeks or so in all. At first glance, that does not seem all that impressive. First, do you think that the cost of the correspondence-handling pilot was justified? Secondly, why can you not acknowledge correspondence within a day or so of receipt and provide a full reply slightly more quickly than the figures suggest?

Mr Black: I apologise for sounding rather defensive but, after conducting a review of correspondence in the past year, we came to the conclusion that the system at present is giving better performance and proving more effective at handling what are sometimes quite complex audit issues.

I ask Diane McGiffen to provide some more detail.

Diane McGiffen: The correspondence in question is not the routine business correspondence that Audit Scotland receives; it is, in fact, a very specific category of correspondence that relates to concerns about public bodies. We take up to 10 days to acknowledge such correspondence because we carry out a preliminary scan to ensure that we would consider the issue. In our first response, we also try to give people a clear steer as to whether we will be examining the issue; whether we are the right body to contact; or whether the matter should be referred elsewhere. Given that the people who write to us are often at the end of a long journey of trying to find a solution to or information about a problem that they have encountered with a public body, it can take time to untangle and unpick where in the system their concerns lie. Sometimes people write too early for us to be able to do anything; for example, the issue might not have been concluded by the public body involved. Sometimes they write to us after the issue has

been raised, considered and reviewed by other scrutiny bodies or public bodies.

As a result, this area of correspondence covers many issues, including whistle blowing by members of the public, other complex issues or, indeed, concerns about fraud. We have to take such matters very seriously and liaise with our local auditors, who do not always work for Audit Scotland—they might be with one of the firms. Many of these issues are just that bit more complex and sensitive.

I am not sure that the label that we have given to this work captures its complexity. The term “correspondence” is too generic for what are really issues of concern about public bodies.

Robert Brown: I realise that the matter is complex. However, it might be worth seeing whether the targets can be pushed a bit.

Hugh Henry (Paisley South) (Lab): Does the correspondence include items of correspondence that are dealt with by the Accounts Commission?

Mr Black: Yes.

Diane McGiffen: Yes.

Robert Brown: Page 16 of the annual report mentions your work to achieve green efficiencies, if I can put it that way, which seem to be quite impressive. Examples are the percentage reductions in power use for printers and the computer room that are shown at the bottom of the page. Have those issues been usefully drawn into your audit work with councils and other public bodies in order that they can achieve the same sort of effects? Do you consider that aspect when you carry out audits?

Mr Black: Diane McGiffen will talk about that in a moment. If we come out with recommended standards from undertaking a piece of audit work, we certainly apply them to ourselves and try to identify ways to improve. For example, we carried out our own best-value review of our use of consultants in parallel with the work that we did on consultancy last year.

We also increasingly try to ensure that we take best practice from Audit Scotland and build it into some of the toolkits that we make available to the auditors who work with audited bodies.

Diane McGiffen: We have recently had a major think about how we can make more impact on environmental issues through the work that we do, both in managing our own business and through the audit work that we conduct.

We have an internal mechanism in the form of our environmental group, which is a group of staff representatives who support and help us with our environmental work. We have incorporated environmental guidance in our procurement

guidance; a lot of the savings that you noted in the report come from the procurement of very efficient computing equipment. We were able to do that because of where we were in the cycle of replacing our computing equipment. We have made some significant and useful savings in energy use, although they have unfortunately not been reflected in cost reductions, because energy prices went up at the same time.

We network with other public bodies on computing and IT and so on. During the next few months, we will pull together a clear strategy for everyone to see that will explain how we join up our external audit work with our internal management of the business. It is very important for us to show people how we join those things together, to demonstrate best practice and to learn from things that we do. Our IT manager works with all our IT auditors who go out and audit public bodies, so there is a good flow of information about best practice from both perspectives.

Robert Brown: I have another, slightly esoteric question. You talked about data matching in relation to the powers in the Criminal Justice (Scotland) Bill, and you mentioned that your own desktop computers and laptops have encrypted hard disks. I am not a technical expert on all that, but it sounds like good stuff, as these things go. Have you lost any memory sticks or laptops?

Diane McGiffen: We have not lost any memory sticks or laptops. We lost one paper file, and we dealt with that. We had a break-in about two and a half or three years ago in which some laptops were stolen. We are continuously investigating new variants of encryption and further restrictions that we can put in place, and we are actively reviewing—as are all public bodies—all our arrangements for handling personal and sensitive data. We feel that we have good IT restrictions now—the bigger issue is what people do in the course of their daily work, which is something that we are working on.

Robert Brown: I am conscious that the nature of your work means that you take laptops around the country more often than other bodies might, so your answer is very encouraging.

I have a final question on efficiency savings. You indicate that you generated £92,000 of efficiency savings in 2008-09 in various ways, which I think is a bit below what was hoped for. You also indicate a target of £585,000 for 2009-10, which is of quite a different order from what you achieved this year. Can you give us some background to that? Can you explain why you think that you can do better on efficiency savings next year, and why this year was perhaps not as good as you had hoped?

Mr Black: If I may, I will take the concept of efficiency in a wider context. The first element is completing the audit for less than the budgeted cost, and we have talked about the rebate, which is a true cash-releasing saving to audited bodies. That did not happen by chance; it happened because of a progressive improvement in the way in which we plan and control the audit works. That sum was built up over two years and represented about 5 per cent of the audit fees up to March 2009. It is probably worth placing that on the record.

Robert Brown: Is that included in your previous figures or is it not calculated in the same way?

Mr Black: Do you mean the savings?

Robert Brown: Yes.

Mr Black: I am sorry; perhaps I do not quite understand the question. The £1 million that we gave back to the audited bodies has been documented.

Robert Brown: I am not asking so much about the documentation, but about the figures that you have given for cash-releasing savings and the like. Does that get included in that?

Mr Black: Does that get included in the £1 million?

Robert Brown: No, in the previous years' equivalent to the £92,000 saving made this year.

Diane McGiffen: We are talking about two different things. The £1 million is presented and discussed separately from the rest of the on-going efficiencies that we have made. Cumulatively, the annual recurring savings over three years total approximately £750,000, which is separate from the £1 million. In 2008-09, we generated £92,000 of savings from the things that we highlighted in the annual report, such as further reviewing our suppliers and contracts and so on.

In addition to those savings, we took on additional work at no extra cost in further supporting scrutiny work, working on streamlining risk assessments across the public sector for scrutiny bodies, and planning for the introduction of best-value audits of the police and fire services. So we have been involved in a mix of activity and the cash-releasing savings come from those sources. There is also the £1 million that was rebated to audited bodies and we are still seeing the benefit of some on-going cumulative savings from staffing reductions that we made in the organisation.

The Convener: I want to focus now on where expenditure has fluctuated or increased. With respect to fees paid to appointed auditors, you were over budget this year, but under budget last year. There was a more than 9 per cent increase

in your operating costs on previous years, but that figure has fluctuated quite significantly during the past two or three years. Other areas in which there has been an increase in costs are legal and professional costs, and property leases. Could you talk us through those areas, please?

Diane McGiffen: I will ask Russell Frith to start that off.

Russell Frith: First, fees and expenses paid to appointed firms have gone up. That is both an inflationary increase and reflects the variation in the final fees agreed with the audited bodies from those that we included in the budget. We set what we call an indicative fee for each of the audits, which is the sort of fee that we expect to be appropriate for that size of body on the assumption that it is reasonably well run and that no particular issues arise. The auditors have the flexibility to agree the final fee with the audited body—plus or minus 10 per cent of the indicative figure. We produce the budget on the basis that, on average, the indicative fees will be achieved and that that will be the amount that we will pay to the firms. However, if they have agreed greater or lesser fees, that will represent a variance from the budget. It will be matched by income on the other side, so there is no net impact on our bottom line net operating cost if a firm agrees either a higher or a lower final fee with the audited body; it will be matched out.

11:15

The Convener: If I have understood you correctly, fluctuation in expenditure on audit fees is something that we must expect.

Russell Frith: Yes. There will be a core increase—whatever the inflationary increase is—for payments to firms, which would have been 2.5 to 3 per cent for the audit year that came in half way through that financial year. The rest will be volume related, and that will be matched by a volume-related change in our income.

The Convener: Is it the norm for operating costs to fluctuate in the way that they have done?

Russell Frith: If you are talking about staff costs, the fluctuation largely reflects the change in numbers that you asked about. In relation to other costs, expenditure on legal and other professional fees has gone up substantially since 2008. However, if I remember the budget discussion correctly, we had been underspending in that area and expected to get closer to our budget in 2008-09 than we had done in previous years. That is exactly what happened.

The Convener: I was referring to the operating costs that are mentioned on page 23. Operating costs went up by 9.1 per cent last year, but in the

previous year they went down by 9.5 per cent and in the year before that they went up by 15 per cent. That is why I was asking about the fluctuating trend.

Russell Frith: Sorry, I was working from paragraph 4 in the notes to the accounts, which gives a more detailed breakdown. The operating costs in the table on page 23 represent expenditure other than the costs referred to in the three preceding lines. The biggest element of those costs is consultancy and legal and other professional fees, in relation to which we came much closer to our budget than we have done in recent years.

The Convener: Are you saying that although there was a significant increase in the use of consultants, it was in line with your budget projections?

Russell Frith: It was in line with the budget that we set in the first place.

Hugh Henry: Does

“legal and other professional fees”

refer to law and accountancy firms?

Russell Frith: Yes, and particularly to consultants who provide specialist input into studies.

Hugh Henry: Is there evidence that such consultants and other private companies who undertake work for you have curtailed their charges to reflect the changed economic circumstances? Are such companies continuing to charge whatever they previously charged?

Russell Frith: The firms that we appoint to do audit, which is the biggest single element of the expenditure, tell us that the rates that we pay are significantly below the rates that they would try to achieve in the private sector. We set the contracts before the economy was in recession. Because we give firms a reasonably substantial amount of work, with a minimum of five years before they must retender, we tend to get a good deal to start with. I would not expect a great deal of fluctuation as we move into less good times, because we have benefited substantially during better times. That said, we have included in our budget submission, which you will consider next month, proposals to make the work that is done by the firms bear the same level of efficiency savings as the work that is done by the rest of the organisation. In that way, we are effectively beginning to reduce the amount that they earn.

Hugh Henry: So, although we see a substantial increase in the fees to appointed auditors and the legal and other professional fees, given the five-year contract period to which you refer the actual charges will be relatively stable. Can we therefore

assume that the increase in expenditure is purely down to increased volume of work?

Russell Frith: Yes. The increase that you see, from 2007-08 to 2008-09, reflects an increase in the volume of work. Ignoring the appointed firms, the consultants element—the legal and professional fees—reflects an increase in volume.

Hugh Henry: Why is there such a substantial increase in volume?

Russell Frith: One of the reasons for that—but only one of them—is the fact that those figures include the fee that we pay to the Audit Commission for the work that it does for us on the national fraud initiative. There is £180,000-odd included in there that relates to the national fraud initiative, compared with zero in the previous year. That is one big element of the change. It is an exercise that is carried out every two years.

The Convener: On the theme of consultants, on page 14 of the annual report you say that you reviewed your use of consultants and that the review concluded that Audit Scotland “mostly” followed good practice. Can you say a bit about the areas that you identified for improvement?

Diane McGiffen: Among the areas for improvement was that of contracting people to do work for us for relatively low-value spends of, say, £10,000 to £15,000. Managers could plan that a bit better and draw on broader pools of potential consultants. Often, the need arises for specialist data analysis if something has gone wrong on a project and the project manager is looking to get someone with reliable skills quickly. That might lead to their returning to the same suppliers over and over again without realising it. We need to sharpen up some of the practice in that respect.

All the areas for improvement relate to relatively low-spend items and indicate where we could do a bit better.

The Convener: I have two brief, final questions. The figures show an increase of £137,000 in expenditure on property leases, year on year, from £586,000 to £723,000. That is an increase of 24 per cent. Can you say something about that, please?

Russell Frith: Yes, certainly. The 2007-08 figure was artificially reduced because, during that year, we wrote back our provision for rent reviews where the final settlement was less than we had expected. That is one element. Some other rent reviews also came through in 2008-09, which increased the rent.

The Convener: The management letter that the external auditors issued indicates that one recommendation was made on the control of internal purchase orders and that Audit Scotland responded that it is developing a new ordering

system, which should be operational by December. What progress is being made on that?

Diane McGiffen: We are on track with the implementation of that system. The improved electronic purchase ordering system will enable us to reconcile invoices with purchase orders much more quickly and, therefore, to pay more quickly. The action ties into the earlier question about the speed with which we can pay invoices.

The Convener: As there are no more questions, I thank our witnesses from Audit Scotland and ask them to retire briefly to the public gallery.

Mr Black: Convener, I crave your indulgence—as people used to say—on consultancy, as I have the impression that it is a concern to you. It is important to emphasise that the legal and professional fees include all the work and costs associated with the national fraud initiative, which generated £40 million of savings. They also include all the consultancy and support work for developing Audit Scotland's best-value regime—that is best value 2 and the roll-out of best value to the rest of the public sector, which we are required to do—and some of the consultancy work on developing our new performance management systems, about which we will say more when we present the budget.

I wanted to get that on record, convener. Thank you for that opportunity.

The Convener: Thank you. We are just asking questions at this stage.

I would be grateful if the Audit Scotland witnesses could retire to the public gallery briefly.

I welcome Richard Gibson, who is the lead contact on the external audit of Audit Scotland. Can he confirm that Haines Watts has received all the necessary information and explanations to inform its opinion on the accounts and provide an overview on any observations that arise from its work?

Richard Gibson (Haines Watts): Yes, I can.

The Convener: Would you like to give an overview of your work?

Richard Gibson: Yes, briefly. I remind the commission that Haines Watts was appointed external auditors for Audit Scotland four years ago, so this is the fourth audit that we have performed on the organisation. We had a three-year contract, which was extended last year at the Parliament's discretion.

The audit was undertaken between February and June this year and signed off on 16 June. Two documents have been tabled that are relevant to my evidence. The first is the annual report and accounts, which you have discussed. Page 52 of that report is my audit report. You will see that it is

what we call an unqualified audit report, which is what you would describe as a clean audit report. That is, we found no issues that suggest anything other than that the accounts are materially accurate.

The second document is a management report, which was submitted to the commission and Audit Scotland's audit committee. It summarises our audit process and findings. I confirm that the report contains no significant issues that should be brought to your attention that you have not already discussed with Audit Scotland. As far as Haines Watts is concerned, there are no other matters outwith those two documents that should be brought to your attention.

The Convener: Thank you very much, Mr Gibson. The commission takes some comfort from your comments.

Robert Brown: Audit Scotland responded to the note on purchase orders by saying that only 8 per cent of its total expenditure budget is on purchases that require purchase orders to be raised. Does that mean 8 per cent of the staff costs and everything?

Richard Gibson: Yes.

Robert Brown: That seems quite significant.

11:30

Richard Gibson: It is indeed a significant number, bearing in mind the organisation's fairly substantial budget. There is no suggestion at all that the organisation is spending inappropriately or is wantonly incurring costs. In a small proportion of the invoices, however, a process had not been adopted to approve them properly before they were paid. That was in a very small sample from the organisation—there had simply been a breakdown of the system on one or two specific occasions. That has been brought to your attention because, as external auditors, we review the internal auditors' reports, and we submit anything of relevance to you as part of our report to management.

Robert Brown: So it is not as if documentation is missing, in the sense that you cannot vouch for—

Richard Gibson: No, not at all. There is a system in place and, on one or two occasions, it was not followed. However, it is absolutely nothing to be concerned about.

The Convener: Thank you very much, Mr Gibson. Your time is appreciated.

Audit Scotland Autumn Budget Revision 2009-10

11:31

The Convener: Agenda item 2 is Audit Scotland's proposal for the 2009-10 autumn budget revision. I welcome back the Audit Scotland team, and I invite Mr Black to make a further opening statement.

Mr Black: I like to think that the document speaks for itself, so I will be brief. We have not made any new bids this year. All the money that we requested is for continuing with projects that have been approved in previous years. We have revisited those bids, and we have reduced them where possible. The proposal this year is for end-year flexibility of £500,000. Last year's bid was for £2.5 million, including the £1 million that was rebated back to clients. I like to think that we are performing against our commitment to get that sum down as quickly as possible. Inevitably, there are a few items for which we require EYF to continue into the next year; those are detailed on pages 2 and 3 of the document before you.

The Convener: I will start by exploring the information that you have given us regarding best-value development. You will understand that I look at these matters from a rather rudimentary perspective. I can well understand why you would want to use EYF for the work that needs to be done on the lifts, for example. That is the equivalent to work that might need to be done on the roof at home—we do not always anticipate such things, which tend to be one-off, larger capital costs. Could you say a bit more about the best-value development work? Why are there additional costs there, which might not be incorporated in your day-to-day work?

Mr Black: We have spoken about some of these issues in the past, when we were making the original EYF bids. It is not possible for Audit Scotland to carry balances over financial years. Therefore, we have an extremely restricted financial regime within which to operate. From time to time, developments need to take place that require funding. The only alternative would have been an adjustment to the level of fees that we charge on audited bodies. A short-term peak in development activity had to be funded somewhere. The easiest and most convenient way to do that by far was to use end-year flexibility. We have been most grateful to the commission for agreeing to that in the past, and we now have a commitment to continue with that.

In last year's autumn budget revision, we explained that we intended to appoint additional staff for a short period to help us do the work, and

that we thought that the total cost in 2009-10 and 2010-11 might be about £482,000. We are now able to reduce that sum by almost £100,000 to £385,000. During 2009-10, we have started the pathfinder audits in five councils, as we described earlier in relation to the annual report. The extra staffing resource is helping us with that. We have been developing shared risk assessments with other scrutiny bodies and all Scottish councils and supporting a joint scrutiny forum. By far and away the most efficient way to do that is to continue with EYF, albeit at a lower level than that which the commission agreed might be appropriate last year.

Hugh Henry: I want to follow up the point that was made about the lifts at 18 George Street. Do you have exclusive use of 18 George Street?

Mr Black: No.

Hugh Henry: Are other tenants paying a part of the costs?

Diane McGiffen: Yes.

Hugh Henry: Why is the landlord not meeting the cost of such a substantial capital investment?

Diane McGiffen: That is tied into the nature of the lease. We have a standard long-term lease, which means that we and the other tenants have to meet the repair costs.

Hugh Henry: Have you explored moving away from Edinburgh city centre, which clearly has premium rental rates?

Diane McGiffen: We have explored that many times.

Mr Black: Yes. When Audit Scotland was created, we looked at that possibility. However, we had to get up and working in a short period of time and we were tied into leases that we could not break terribly easily. The problem is that, being a public sector organisation, we could not afford—the public purse could not afford—to bear the penalty of breaking leases early. When we come back to the SCPA in the autumn with our budget requirements for the following year, we will be able to explain to you more fully what we have in mind to review and rationalise our accommodation costs over the next few years, as the leases run out.

Hugh Henry: When does your lease at 18 George Street expire?

Mr Black: In 2014.

Hugh Henry: Because of the nature of Audit Scotland, you are not part of the Scottish Government's investigations into relocation.

Mr Black: That is correct, formally.

The Convener: We have discussed the fees strategy in previous years. Will an updated fees strategy be produced alongside the 2010-11 budget proposal in due course?

Russell Frith: Yes.

Meeting closed at 11:38.

The Convener: Okay. Thank you very much. That was a rather brief return for the Audit Scotland team. I appreciate your time and co-operation, and your illuminating answers.

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