

# Water Industry Commissioner for Scotland and Water Industry Commission for Scotland

Report on the 2005-06 Audit

December 2006



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# Executive Summary

## Introduction

Under the terms of the Water Services etc (Scotland) Act 2005 the Water Industry Commissioner for Scotland was replaced by the Water Industry Commission for Scotland, as from 1 July 2005, with all assets and liabilities transferred to the new body.

In 2005-06 we audited the financial statements of the Water Industry Commissioner for Scotland, for the three month period 1 April to 30 June 2005 and the financial statements of the Water Industry Commission for Scotland (WIC), for the nine month period 1 July 2005 to 31 March 2006, and looked at aspects of governance. This report sets out our key findings for both the Commissioner and WIC.

## Financial Statements

We have given an unqualified opinion on the financial statements of the Water Industry Commissioner for Scotland and the Water Industry Commission for Scotland.

## Governance

Corporate governance and control arrangements operated satisfactorily in the period under review as reflected in the Statement on Internal Control. We have also found the work of the internal audit service to be satisfactory and continue to place formal reliance on its work.

I would like to record my thanks to management and staff for their co-operation and assistance.

Linda Porter CPFA, Senior Audit Manager



# Introduction

## Scope of the Audit

1. This report summarises the findings from our 2005-06 audit of both the Water Industry Commissioner and the WIC. The scope of the audit was set out in our Audit Plan, which was agreed with the WIC in April 2006. This plan described the work we planned to carry out on financial statements, governance and performance.
2. This report to management sets out our findings from the review carried out. The weaknesses outlined are only those which have come to our attention during the course of our normal audit work and are not necessarily, therefore, all the weaknesses which may exist. Although we include a specific recommendation in this report to strengthen internal control, it is the responsibility of management to determine the extent of the internal control system appropriate to the WIC. We would stress, however, that an effective internal control system is an essential part of the efficient management of any organisation. The contents of this report have been agreed with relevant officers to confirm factual accuracy.
3. This is the final year of a five year audit appointment. We note that Audit Scotland has been appointed as external auditors of the WIC for the period 2006-07 to 2010-11. In compliance with International Standards on Auditing and general good practice we will rotate some staff who have worked on this audit for a number of years.
4. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officers and members of the WIC during the course of our appointment. This report will be submitted to the Auditor General for Scotland and will be published on our website at [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

## Prior Period Follow Up

5. Two main issues were identified in our Report on the 2004-05 Audit. We are satisfied that the WIC has followed up the recommendations in 2005-06. We are aware that the T&S guidelines are at draft stage and are to be formalised by the board in the near future. We noted during our audit that all fixed assets now have asset recognition tags.



## **Management Action**

6. Audit recommendations, together with management comments, on those areas where further improvements could be achieved are included in the action plan at Appendix A of this report.



# Financial Statements

## Our Responsibilities

7. We audit the financial statements and give an opinion on whether:

- they give a true and fair view, in accordance with the Local Government etc (Scotland) Act 1994, as amended by the Water Industry Act 1999 and the Water Industry (Scotland) 2002 and directions made thereunder by the Scottish Ministers, of the state of affairs of the Water Industry Commissioner for Scotland as at 30 June 2005 and of its deficit, total recognised gains and losses and cash flows for the year then ended
- they give a true and fair view, in accordance with the Local Government etc (Scotland) Act 1994, as amended by the Water Industry Act 1999 and the Water Industry (Scotland) 2002 and directions made thereunder by the Scottish Ministers, of the state of affairs of the Water Industry Commission for Scotland as at 31 March 2006 and of its surplus, total recognised gains and losses and cash flows for the year then ended
- they and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Local Government etc (Scotland) Act 1994, as amended by the Water Industry Act 1999 and the Water Industry (Scotland) 2002 and directions made thereunder by the Scottish Ministers
- in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

8. We also review the Statement on Internal Control by:

- considering compliance with Scottish Executive guidance
- considering the adequacy of the process put in place by the Accountable Officer to obtain assurances on systems of internal control
- assessing whether disclosures in the Statement are consistent with the information emerging from our normal audit work.



## Overall Conclusion

9. We have given an unqualified opinion on the financial statements of the Water Industry Commissioner and the WIC for 2005-06. We are able to conclude that the financial statements give a true and fair view of the financial position for the periods from 1 March 2005 to 30 June 2005 and 1 July 2005 to 31 March 2006 and that, in all material respects, the expenditure and receipts shown in the accounts were incurred or applied in accordance with applicable enactments and relevant guidance.
10. Audit work was scheduled to achieve a certification date that would permit the laying of the accounts before the Scottish Parliament by the end of December 2006. The draft accounts were duly submitted on the agreed date and the completion timetable achieved.

## Financial Performance

11. The Water Industry Commissioner's income and expenditure account for the period 1 March 2005 to 30 June 2005 records income (including grant in aid) of £0.606m and expenditure on operating activities of £1.294m, resulting in an operating deficit of £0.688m
12. The WIC's income and expenditure account for the period 1 July 2005 to 31 March 2006 records income (including grant-in-aid) of £3.080 million and expenditure on operating activities of £2.526 million, resulting in an operating surplus of £0.554 million.

## Statement on Internal Control

13. The Statements on Internal Control were signed by the Accountable Officer on the 14 November 2006. These set out the arrangements operated for risk identification and review, management of identified risks and assurance of effectiveness.
14. We are satisfied that the Statements on Internal Control comply with Scottish Executive guidance, the process put in place by the Accountable Officer to obtain assurances on systems of internal control is adequate and the contents of the Statements were not inconsistent with the information emerging from our normal audit work. We note that the WIC plans to further strengthen the system of internal controls with the introduction of comprehensive financial procedures manuals, production of a business entertainment policy, monthly financial reporting and improvements in procedures for authorisation of travel and subsistence claims. We will follow up progress with these developments in 2006-07.





## ISA 260: Communication of Audit Matters to Those Charged with Governance

15. My responsibilities in relation to the communication of audit matters to those charged with governance are covered in International Standard on Auditing 260 and outcomes against the requirements of the Standard were reported in a letter to the Accountable Officer on 10 November 2006.
16. There were a small number of immaterial adjustments and presentational issues. All adjustments were reflected in the audited version of the financial statements.

### Issues Arising

17. We would like to draw attention to the following issue arising from our audit of the financial statements:
  - As reported in 2004-05 we noted instances of payments for alcoholic beverages being included in T&S claims. Provision of alcohol is in breach of normal public service T&S terms and conditions. The revised T&S policy and hospitality guidelines should be agreed with the Scottish Executive and implemented as soon as possible.

**Action point 1**



# Governance

## Introduction

18. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of an organisation. This section sets out the main findings arising from our review of the WIC's corporate governance as it relates to:

- fraud prevention and detection arrangements
- systems of internal control
- review of internal audit.

## Overall Conclusion

19. During our audit we reviewed Internal Audit's follow up report of the financial controls operating at the WIC. The report recognised that significant work has been undertaken to develop and integrate a robust internal financial control environment, however, the report also identified a number of areas where there is scope for some further enhancement of the internal financial control procedures.

## Fraud Prevention and Detection Arrangements

20. The WIC's arrangements for preventing and detecting fraud and corruption were assessed during the audit and found to be satisfactory. No frauds were identified by the WIC in 2005-06.

## Systems of Internal Control

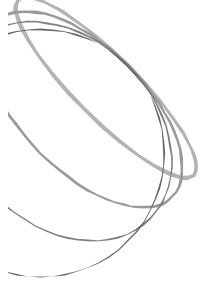
21. During our audit visit we carried out some assessment of systems and controls in relation to grants, payroll and non-payroll expenditure. There are no significant points to highlight in this report.

## Review of Internal Audit

22. The WIC recognises that internal audit is a key element of the internal control system set up by management. A strong internal audit function is necessary to ensure the continuing effectiveness of the internal control system established. To maximise the reliance that external audit can place on internal audit and to avoid duplication of effort, the adequacy of internal audit is assessed each year.

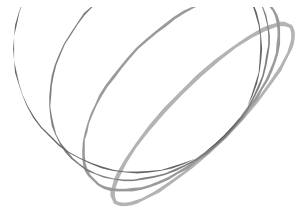


23. Internal audit is provided by Scott Moncrieff, Chartered Accountants. From our review of the internal audit arrangements we are pleased to confirm that we placed reliance on their work in a number of areas during 2005-06, as was anticipated in our audit plan.



# Appendix A: Action Plan: Recommendations for Further Improvements

Action Point	Para. No	Issue and Audit Recommendation	Management Response	Responsible Officer	Target Date
1	17	<p><b>Travel and Subsistence/Business Hospitality</b></p> <p>As reported in 2004-05 we noted instances of payments for alcoholic beverages being included in T&amp;S claims. Provision of alcohol is in breach of normal public service T&amp;S terms and conditions.</p> <p>This item remains outstanding from the previous year's action plan. We understand that WIC are at present reviewing their guidelines.</p> <p><i>We recommend that both T&amp;S and hospitality guidelines are agreed with the Scottish Executive and implemented as a matter of priority.</i></p>	<p>The recommendation is noted. At the current time, there is an on-going debate about the governance of Waterwatch Scotland. This directly impacts on all the policies of the Water Industry Commission. Once this issue has been resolved completely, we will be in a position to begin the process of agreeing all the Commission's policies with the Scottish Executive.</p>	Katherine Russell	As soon as Waterwatch issue is resolved.



# Appendix B: Auditor General for Scotland published reports

Auditor General for Scotland

*Relocation of Scottish Executive departments, agencies and NDPBs (published 21 September 2006)*

1,653 posts have been transferred from Edinburgh and a further 1,164 posts have been created outside the city. Audit Scotland found that most of the reviews arose from the creation or restructuring of organisations, or from breaks in property leases. Only two of 38 reviews were the result of potential efficiency improvements identified by the organisations in their business plans. In most cases, it was not clear whether relocation would deliver wider policy objectives.

Accounts Commission and Auditor General for Scotland

*Community planning: an initial review (published 16/06/2006)*

Community planning partnerships have made progress but need to do more to show how their work is improving public services. The report also says that their complex remit makes it difficult for them to achieve their aims and calls on the Executive to support community planning more effectively.

Accounts Commission and Auditor General for Scotland

*No hiding place: the National Fraud Initiative in Scotland (published 17 May 2006)*

Scotland's councils have worked with other public bodies to identify £15m worth of fraud and errors in a national detection exercise.

Auditor General for Scotland

*Scottish Further Education Funding Council: A progress report (published 26 January 2006)*

The Scottish Further and Higher Education Funding Council (Funding Council) is making progress on a number of fronts, according to a report published today by the Auditor General for Scotland.

Auditor General for Scotland

*Leadership development. How Government Works (published 17 November 2005)*

Scotland's public sector has good examples of investment in leadership but many individual organisations do not have clear policies and most are unable to link the spending to improvements in their performance. Public bodies need to do more to track the £5m they invest each year in leadership development and make sure it results in better managed organisations and better public services, says Audit Scotland.

Auditor General for Scotland

*Scottish Executive: supporting new initiatives. How Government Works (published 10 November 2005)*

Last year the Scottish Executive launched new initiatives amounting to £1.4 billion. The management of these projects is generally sound, but making changes could help to improve control of the funding and allow better assessment of whether the money is helping to achieve policy aims.



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