

Her Majesty's Inspectorate of Education

Report on the 2006/07 Audit



5 September 2007



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Executive Summary

Introduction

In 2006/07 we audited the financial statements of the Her Majesty's Inspectorate of Education (HMIE) and we looked at aspects of performance management and governance. This report sets out our key findings.

Financial Position

We have given an unqualified opinion on the financial statements of HMIE for 2006/07.

HMIE's income for the year from fees and charges was £1.212 million (2005/06: £1.110 million) whilst income from other sources in 2006/07 was £0.464 million (2005/06: £0.270 million). Most of the income received under fees and charges is from the Service Level Agreement which is set annually with the slight variation being due to real increases. Gross Administration costs for 2006/07 were £15.133 million (2005/06: £14.772 million), with the main element being staff costs of £10.758 million (2005/06: £10.730 million). Other administration costs for the year were £4.047 million (2005/06: £3.749 million); the most significant factor in the increase being this year's expenditure reflecting fuller costs of additional office premises.

In line with our normal practice, we will record our detailed audit findings, covering less significant matters, in a letter to management. The main theme identified in this element of the audit was the relationship between HMIE and the Scottish Executive and their respective roles in relation to aspects of financial arrangements. As the Agency evolves, there is a need to keep these arrangements under review and strike the correct balance between the economies of scale afforded by making use of Executive arrangements and the benefits of Agency taking on more direct responsibilities, a judgement that is not always as straightforward as it may seem as making use of Executive arrangements may involve extra procedures within HMIE to provide the required information and assurances.

Performance

HMIE carried out a Best Value self assessment exercise which was subject to audit review. Overall arrangements were assessed as well developed, with only 2 of the 9 individual characteristics being assessed as under development (sustainable development and equal opportunities). Our baseline review of similar assessments for central government bodies (January 2007) recorded that 70% of bodies considered their overall arrangements for securing Best Value were under development, indicating that HMIE are relatively well placed.

Governance

Corporate Governance is concerned with the structures and process for decision making, accountability, control and behaviour at the upper levels of an organisation. Overall the corporate governance and control arrangements for HMIE operated satisfactorily during the year, as reflected in the Statement on Internal Control. At the time of the audit committee's consideration of the financial statements we had an indication of the assurances that would be provided by the Scottish Executive auditors in relation to the Scottish Executive systems that HMIE rely upon. We can now report that we have obtained a formal statement confirming the anticipated satisfactory assurances.

During the year we facilitated a comparative self assessment of the business risks associated with information and communication technology; the survey comprised 2 sets of questionnaires: one for ICT users and one for ICT staff; the comparators were other UK public sector organisations. The findings identified areas of good practice/ good levels of staff knowledge and awareness, but also areas in which levels of awareness could be improved. At the time of the survey, the Head of IT indicated the intention to update the relevant aspects of guidance and action to increase awareness of issues.

Audit Scotland

Introduction

1. This report summarises the findings from our 2006/07 audit of Her Majesty's Inspectorate of Education (HMIE). The scope of the audit was set out in our Audit Plan, which described the work we planned to carry out on financial statements, performance and governance.
2. Appendix A of this report sets out the key findings highlighted in this report and the action planned by management to address them.
3. This is the first year of a five year audit appointment. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officers and members of HMIE during the course of our audit. This report will be submitted to the Auditor General for Scotland and will be published on our website, www.audit-scotland.gov.uk.

Financial Statements

4. In this section we summarise key outcomes from our audit of HMIE financial statements for 2006/07, and comment on the key financial management and accounting issues faced.

Our Responsibilities

5. We audit the financial statements and give an opinion on whether:
 - they give a true and fair view of the financial position of HMIE and its expenditure and income for the period in question.
 - they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements, and
 - in all material respects, the expenditure and receipts are regular (comply with statutes and guidance).
6. We also review the statement on internal control by:
 - considering the adequacy of the process put in place by the chief executive as accountable officer to obtain assurances on systems of internal control; and
 - assessing whether disclosures in the statement are consistent with our knowledge of HMIE.

Overall Conclusion

7. In relation to these responsibilities we have given an unqualified opinion on the financial statements of HMIE for 2006/07.

Financial Position

2006/07 outturn

8. HMIE had net operating costs for 2006/07 of £13.486 million (2005/06: £13.417 million). Payroll is the main expenditure item at £10.758 million (2005/06: £10.730 million) and the movements within it are consistent with staff movements. Other administration costs for the year were £4.047 million (2005/06: £3.749 million); the most significant factor in the increase being this year's expenditure reflecting fuller costs of additional office premises.
9. The Net Asset position increased slightly to £0.875 million (2005/06: £0.863 million). There have been no significant movements in fixed assets as expected.

10. Income from fees and charges during 2006/07 was £1.212 million (2005/06: £1.110 million), while income from other sources increased to £0.464 million (2005/06: £0.270 million).
11. Scottish Ministers set an initial resource budget for HMIE of £13.4 million for 2006/7 representing a 1% increase on the 2005/06 figure. Discussions with the Education Department resulted in a budget allocation of £15 million, an increase in anticipation of the development of the Inspectorate of Services for Children. However, £1.5 million of the budget allocation was released back to the Education Department in January 2007 for use in other projects. Development work will be completed in 2007/08 and expenditure will increase accordingly.

2007/08 budget

12. The Scottish Ministers have set the budget for 2007/08 at £15 million. No further increases are expected unless the Agency is requested to undertake further work on the behalf of Ministers.

Issues Arising from the Audit

13. As is our normal practice, we record our main audit findings in this final report on the audit, with less significant matters recorded in a letter to management. The main theme arising from the individual findings on this aspect of our work was the relationship between HMIE and the Executive (who does what, what is kept where, who reconciles what, etc). There is no standard model for this relationship because different Agencies take on different responsibilities from the Executive. As the Agency evolves, there is a need to keep arrangements under review and strike the correct balance between the economies of scale afforded by making use of Executive arrangements and the benefits of Agency taking on more direct responsibilities, a judgement that is not always as straightforward as it may seem as making use of Executive arrangements may involve extra procedures within HMIE to provide the required information and assurances.

Refer Action Plan No.1

Statement on Internal Control

14. The Statement on Internal Control provided by HMIE's Accountable Officer reflected the main findings from both external and internal audit work. This recorded management's responsibility for maintaining a sound system of internal control and set out HMIE's approach to this. No particular issues arose in relation to the disclosures contained in the Statement on Internal Control.

Performance

15. Public audit is more wide-ranging than in the private sector and can cover the examination of, and reporting on, performance and value for money issues. As part of Audit Scotland's approach we may plan to review aspects of the arrangements to manage performance, as they relate to economy, efficiency and effectiveness in the use of resources.
16. Accountable Officers have a duty to ensure the resources of their organisation are used economically, efficiently and effectively. These arrangements were extended in April 2002 to include a duty to ensure 'Best Value' in the use of resources.

Performance

17. There is a statutory duty of Best Value for local authorities but not in the wider public sector in Scotland (the Scottish Executive and its Executive Agencies, Executive NDPBs, and the NHS). Instead, the Scottish Executive issued high level guidance in May 2003, followed by more detailed draft secondary guidance in August 2003. This duty can be described as:
 - to make arrangements to secure continuous improvement in performance (while maintaining an appropriate balance between quality and cost);
 - to have regard to economy, efficiency and effectiveness, and the equal opportunity requirements; and
 - to contribute to the achievement of sustainable development.
18. In May 2005, Ministers decided that they would not bring forward legislation which extends Best Value in the wider public sector. However, Ministers do wish to encourage and embed the principles of Best Value across the wider public sector and revised guidance was issued in May 2006.
19. Starting in audit year 2005-06 Audit Scotland reviewed the arrangements in place to demonstrate Best Value across a sample of Central Government organisations, to identify how well-advanced they were and any areas of good practice that could be disseminated. This review was based on a diagnostic questionnaire to establish baseline information on the management arrangements in place on each of the nine characteristics that are considered to underpin the achievement of best value. These are:
 - Commitment and Leadership
 - Sound Governance at a Strategic and Operational Level
 - Accountability
 - Sound Management of Resources and Contractual Relationships

- Responsiveness and Consultation
- Use of Review and Options Appraisal
- A Contribution to Sustainable Development
- Equal Opportunities Arrangements
- Joint Working.

20. During the course of the current audit HMIE carried out a Best Value self assessment exercise which was subject to audit review. Overall arrangements were assessed as well developed, with only 2 of the 9 individual characteristics being assessed as under development (sustainable development and equal opportunities). This compared favourably with the results of our baseline review of similar assessments for central government bodies (January 2007), which recorded that 70% of bodies considered their overall arrangements for securing Best Value were under development.

21. In 2007/08 we will follow up progress on the further development of Best Value characteristics, including further embedding of arrangements as appropriate.

Refer Action Plan No.2

Governance

Overview of arrangements

22. This section sets out our main findings arising from our review of HMIE's governance arrangements. This year we reviewed:
- key systems of internal control;
 - internal audit; and
 - aspects of information and communications technology (ICT).
23. We also discharged our responsibilities as they relate to prevention and detection of fraud and irregularity; standards of conduct; and the organisation's financial position. Our overall conclusion is that arrangements within HMIE are sound and have operated throughout 2006/07.

Systems of internal control

24. Key controls within systems should operate effectively and efficiently to accurately record financial transactions and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In the annual report for 2006/07 the head of internal audit concluded that, based on the internal audit work undertaken during the year, there was reasonable assurance on the adequacy and effectiveness on the systems of internal control.
25. As part of our audit we reviewed the high level controls in a number of HMIE's systems that impact on the financial statements. Our overall conclusion was that key controls were operating effectively.

Internal audit

26. The establishment and operation of an effective internal audit function forms a key element of effective governance and stewardship. We therefore seek to rely on the work of internal audit wherever possible and as part of our risk assessment and planning process for the 2006/07 audit we assessed whether we could place reliance on HMIE's internal audit function. We concluded that the internal audit service operates in accordance with the Government Internal Audit Manual and therefore placed reliance on a number of internal audit reviews.

Information and communication technology

27. During the year we facilitated a comparative self assessment of the business risks associated with information and communication technology; the survey comprised two sets of questionnaires: one for ICT users and one for ICT staff; the comparators were other UK public sector organisations. The findings identified areas of good practice/ good levels of staff knowledge and awareness. However there were also areas in which levels of awareness could be improved. The details have been reported in a separate letter to management. By way of context, it is perhaps worth emphasising that that the findings of the survey should not be taken as indicating that the relevant controls are not in place, but rather that there are areas in which awareness levels could be improved. Studies have re-enforced the importance of staff knowledge and awareness in ensuring the effective operation of policies and procedures. At the time of the survey, the Head of IT indicated the intention to update the relevant aspects of guidance and action to increase awareness of issues. As part of the audit for 2007/08 we would seek to follow up HMIE responses to the survey.

Refer Action Plan No.3

Looking Forward

Faster closing

28. In 2006/07 HMIE brought forward the preparation of the draft financial statements to allow audited accounts to be included in the published annual report and accounts; this development was a significant achievement and means HMIE are well placed to meet any targets arising from the increased emphasis on “faster closing” for central government accounts. That said, HMIE need to build on this achievement, through reflecting on the outcomes and timings for 2006/07, to ensure that all the information required from others for preparation of the financial statements is obtained on time and is reviewed by management prior to its incorporation, including, as necessary, the review and analysis of information from Scottish Executive systems. This will also facilitate a complete set of working papers and supporting documentation being available at the start of the final audit.

Refer Action Plan No.4

Best value

29. As part of the 2007/08 audit we will follow up the progress that HMIE has made in strengthening their arrangements for securing Best Value. Over the next year we will also be developing and refining our approach to the audit of public bodies' arrangements to secure economy, efficiency and effectiveness in the use of resources, as this is one of our key objectives as auditors, set out within the new Code of Audit Practice approved by the Auditor General. This will inform our ongoing work to develop an approach to the audit of Best Value across the Scottish public sector. We intend to consult with both clients and stakeholders at key stages of these initiatives.

Refer Action Plan No.2

Appendix A: Action Plan

Key Issues and Planned Management Action

Action Point	Issue Identified	Planned Action	Responsible Officer	Target Date
1	<p>Respective roles of the Scottish Executive and HMIE As the Agency evolves, there is a need to keep systems and procedures under review and strike the correct balance between the economies of scale afforded by making use of Executive arrangements and the benefits of Agency taking on more direct responsibilities, a judgement that is not always as straightforward as it may seem as making use of Executive arrangements may involve extra procedures within HMIE to provide the required information and assurances.</p>	We will review respective roles annually in light of our ongoing experience and the findings from internal and external audit.	M Cochrane	May/June 2008
2	<p>Best Value HMIE self assessment confirms that Best Value characteristics/ arrangements are, overall, well developed. The Agency should continue to monitor progress on the further development of Best Value characteristics, including further embedding of arrangements as appropriate</p>	Best value will be embedded within HMIE's self-evaluation activities and be an integral part of the annual action planning that supports that strand of our work.	S Robinson	Ongoing
3	<p>ICT security awareness During the year HMIE participated in a facilitated, comparative self assessment of the business risks associated with information and communication technology. The findings identified areas of good practice/ good levels of staff knowledge and awareness. However, there were also areas in which levels of awareness could be improved. At the time of the survey, the Head of IT indicated the intention to update the relevant aspects of guidance and action to increase awareness of issues. As part of the audit for 2007/08 we would seek to follow up HMIE responses to the survey.</p>	We will update relevant guidance and promote greater awareness across the Inspectorate.	A Ryan/M Cochrane	December 2007

Action Point	Issue Identified	Planned Action	Responsible Officer	Target Date
4	<p>Faster closing</p> <p>HMIE and Audit Scotland need to build on the achievement of earlier completion of the accounts preparation and audit process in 2006/07, through reflecting on the outcomes and timings for 2006/07. For HMIE the focus is to ensure that all the information required from others for preparation of the financial statements is obtained on time and is reviewed by management prior to its incorporation, including, as necessary, the review and analysis of information from Scottish Executive systems. Such a review will also facilitate a complete set of working papers and supporting documentation being available at the start of the final audit process thereby improving the efficiency of the process overall.</p>	<p>We will reflect on the lessons learned from the 2006-07 audit and agree detailed actions as part of the audit planning meeting for 2007-08.</p>	M Cochrane	March 2008