

National Libraries of Scotland

Report on the 2006/07 Audit



November 2007





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Executive summary

Introduction

In 2006/07 we audited the financial statements of the National Libraries of Scotland (NLS) 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 NLS for 2006/07.

The new FReM requirement to account for grant-in-aid as a credit to reserves has resulted in an excess of expenditure over income of £11.948 million for 2006/07 (2005/06 restated: £11.506 million). The grant-in-aid for running costs credited to reserves for 2006/07 was £12.382 million (2005/06: £11.354 million).

NLS operated within the budget limits set by the Scottish Executive for capital spending and operating expenditure.

Performance

The work of the NLS is guided by the strategic goals described in *Breaking through the Walls*, the strategy adopted by NLS in 2004. Significant achievements during the year included acquisition of the John Murray Archive in March 2006, which is now on display.

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 NLS operated satisfactorily during the year, as reflected in the Statement on Internal Control.

Looking forward

On 1 April 2007 the National Library of Scotland merged with the Scottish Screen Archive (SSA) taking over responsibility for the custodianship of the film media heritage of Scotland. This is a major change and there is a wide range of issues for NLS to resolve. The 2007/08 accounts will incorporate the balances and related transactions of the SSA. We will review the merger process as part of our interim audit.

Capital charges comprising depreciation and cost of capital make up about 22% of NLS's initial financial allocation in 2007/08, and are likely to remain a significant item in NLS accounts for the foreseeable future. They are a non-cash revenue budget allocation at present but this is under review by the Scottish



Government. The basis and quantification of the charge is largely uncontrollable, and NLS will need to monitor the position closely to ensure that it does not reduce budget provision in other activity areas.

As part of the 2007/08 audit we will be reviewing the progress that NLS has made in strengthening their arrangements for securing Best Value since the baseline review work in 2005/06. We will monitor the implementation of the management structures and finance function reviews.

Audit Scotland
November 2007



Introduction

1. This report summarises the findings from our 2006/07 audit of NLS. The scope of the audit was set out in our Audit Plan, which was presented to the Audit Committee on 2 May 2007. This plan described the work we planned to carry out on financial statements, performance and governance.
2. 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 NLS 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

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

Our responsibilities

4. We audit the financial statements and give an opinion on:
 - whether they give a true and fair view of the financial position of NLS and its expenditure and income for the period in question
 - whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements
 - the regularity of the expenditure and receipts.
5. 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
 - assessing whether disclosures in the statement are consistent with our knowledge of NLS.

Overall conclusion

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

Financial position

2006/07 Outturn

7. The new FReM requirement to account for grant-in-aid as a credit to reserves has resulted in an excess of expenditure over income of £11.948 million for 2006/07 (2005/06 restated: £11.506 million). The grant-in-aid for running costs credited to reserves for 2006/07 was £12.382 million (2005/06 restated: £11.354 million). In addition NLS received a grant in aid of £1.165 million for capital expenditure (2005-06: £1.120 million). During the year, NLS acquired fixed assets to the value of £1.661 million.
8. A purchase grant of £1.3 million was allocated to NLS for 2006/07 (2005/06: £1.058 million) to add to the collections. During the year purchases with a value of £1.224 million were charged to the Collection Purchase Fund.



9. NLS's net asset position increased to £104.995 million (2005/06: £101.433 million).
10. NLS operated within the budget limits set by the Scottish Executive for capital and operating expenditure.

2007/08 Budget

11. Scottish Ministers have set an initial financial allocation for NLS of £20.142 million for 2007/08. This comprises:
 - £13.984 million grant-in-aid which is an increase of £1.602 million compared to 2006/07
 - a capital grant of £0.450 million
 - a purchase grant of £1.3 million which is the same as 2006/07
 - £4.408 million to cover non-cash costs.
12. NLS has established a detailed budget for 2007/08 based upon operating within the above limits, and providing also for the project of modernisation of the main Library building and the continuing development of the Trusted Digital Repository. NLS recognises the need to keep budget pressures under close review, particularly those arising from taking over the Scottish Screen Archive, where a number of uncertainties have been identified.

Issues arising from the audit

13. We reported the following issues to the Audit Committee.
14. **Internal control assurances** – Although the Scottish Public Finance Manual requires all public bodies to operate a cascaded Certificate of Assurance approach to support assertions made in Statements on Internal Control, NLS does not. NLS does conduct a review to support the Statement on Internal Control, but this is not formalised and documented per the requirements of the Manual. Certificates of assurance are now a standard part of corporate governance regimes in the public sector, and are normally completed by the Senior Management Team or equivalent in order to improve accountability and provide assurance to the Accountable Officer on specific aspects within their area of responsibility, including the management of risk, the maintenance of effective systems of internal control and compliance with relevant policies and legal provisions. NLS has agreed to consider this and to implement appropriate changes, taking into consideration the structure and nature of the Senior Management Team.
15. **Financial statements disclosures** – During the course of the audit we made a number of suggestions to update or improve the financial statement disclosures, in line with FReM requirements, which NLS has accepted and implemented. With changes in FReM planned to reflect international



financial reporting standards we have agreed to work with NLS to support enhanced disclosures and presentation in the 2007/08 financial statements.

16. **Fixed assets** – At the year-end, NLS undertakes an exercise to identify all new assets purchased during the year, rather than coding such purchases to capital asset codes. A similar exercise was carried out to identify disposals and this identified a large number of assets that were either disposed of or scrapped in earlier years. In addition, we note that, in previous years, Internal Audit has expressed their concerns about the accuracy of the fixed asset register and our audit findings supported those recommendations. NLS are currently bringing the financial fixed assets records up to date by identifying assets no longer held by NLS and are planning to implement a common asset register jointly with the Estates Department. The process for identifying capital purchases has also been changed and all purchase invoices over £5,000 are reviewed at the time of posting to the ledger.
17. **Bank reconciliations** – During our audit we identified that bank reconciliations are not being carried out for all NLS bank accounts and some are not prepared on a regular basis. In addition we noted that there was no standard method of completing bank reconciliations and none are prepared using a generally accepted method. NLS have commissioned the Sun Accounts Reconciliation Manager facility and steps are being taken to implement proper procedures for all bank accounts.(see paragraph 27)
18. **Account submission** – Draft accounts were submitted for audit on the 16 July in line with the agreed timetable however there were substantial elements of the accounts missing. A further draft was provided but there were still missing notes and information. A substantially complete set of accounts was not received until the end of September and a full set was not submitted until 19 October. NLS are currently identifying and designing accounting improvements that should result in a more efficient accounts preparation and audit process.
19. **Unadjusted errors** - Several errors were identified during the audit, where if adjustments were made these would have a net effect of increasing by £17,527 the excess of expenditure over income for the year shown in the income and expenditure account. The net impact on the balance sheet would be that net assets would decrease by £17,527. As these errors are immaterial to the accounts as a whole, officers in finance did not adjust the accounts for these errors and we agreed with this.

Statement on internal control

20. The Statement on Internal Control (SIC) provided by NLS'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 it set out NLS's approach to this.



Regularity assertion

21. The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors that requires us to certify that, in all material respects, the expenditure and receipts shown in the accounts were incurred or applied in accordance with applicable enactments and guidance issued by the Scottish Ministers. We have been able to address the requirements of the regularity assertion through a range of procedures, including written assurances from the Accountable Officer as to his view on adherence to enactments and guidance. No significant issues were identified for disclosure.



Performance

22. Public audit is more wide-ranging than in the private sector and covers the examination of, and reporting on, performance and value for money issues. As part of our audit we are required to plan reviews of aspects of the arrangements to manage performance, as they relate to economy, efficiency and effectiveness in the use of resources.
23. Accountable officers also 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

24. The work of the NLS is guided by the strategic goals described in *Breaking through the Walls*, the strategy adopted by NLS in 2004. These goals fall into six broad categories: Developing the Collections, Widening Access, Consultation and Communication, Collaboration and Partnerships, Organisational Development and Infrastructure. Significant achievements during the year included displaying the John Murray Archive, refurbishment work in the George IV Bridge Building, winning awards from the Web Marketing Association for Best Government Website and from Communicators in Business Scotland, and securing funding for the Trusted Digital Repository project which will enable capture and storage of digital cultural history.



Governance

Overview of arrangements

25. This section sets out our main findings arising from our review of NLS governance arrangements.

This year we reviewed:

- key systems of internal control
- internal audit.

26. 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 (see paragraphs 7-10). Our overall conclusion is that arrangements within NLS are sound and have operated throughout 2006/07.

Systems of internal control

27. 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. As part of our audit we reviewed the high level controls in a number of NLS systems that impact on the financial statements. Our overall conclusion was that key controls were operating effectively however we did identify some weaknesses in procedures covering the preparation of bank reconciliations and this is highlighted in the SIC which refers to initiatives taken in the area of financial management and control to review the effectiveness of processes and the appropriateness of resources employed.

28. In their annual report for 2006/07 Scott-Moncrieff, the internal auditors, provided their opinion that NLS had a framework of control capable of providing reasonable assurance regarding the effective and efficient achievement of NLS's objectives. However they had continued to identify an increasing number of individual systems of control which needed to be enhanced and had previously been concerned that NLS was encountering difficulties in addressing these. We will monitor progress on this issue during 2007/08.

Internal audit

29. 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 the internal audit service provided by Scott-Moncrieff. 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.

Looking forward

30. NLS faces a number of challenges in 2007/08, which include:

- **Merger** – on 1 April 2007 the National Library of Scotland merged with the Scottish Screen Archive (SSA) taking over responsibility for the custodianship of the film media heritage of Scotland. This is a major change and there is a wide range of issues for NLS to resolve. The 2007/08 accounts will incorporate the balances and related transactions of the SSA. We will review the merger process as part of our interim audit.
- **Capital charges** - depreciation and the cost of capital make up about 22% of NLS's initial financial allocation in 2007/08, and are likely to remain a significant item in NLS accounts for the foreseeable future. They are a non-cash revenue budget allocation at present but this is under review by the Scottish Government. The basis and quantification of the charge is largely uncontrollable, and NLS will need to monitor the position closely to ensure that it does not reduce budget provision in other activity areas.
- **Best Value** – as part of the 2007/08 audit we will be reviewing the progress that NLS has made in strengthening their arrangements for securing Best Value since the baseline review work in 2005/06. 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.
- **Efficient government** – the achievement of future Efficient Government targets represents a challenge for NLS.
- **Whole of Government Accounts (WGA) and faster closing agenda** – the timetable for the completion of audited accounts for all public sector bodies is being brought forward in stages to facilitate the completion of a WGA for the UK public sector. The overall project is managed by HM Treasury, with the Scottish Executive co-ordinating the process in Scotland. NLS will need to maintain close liaison with staff in the Scottish Executive on timetabling and related resourcing issues arising from this project.
- **Impending changes in the valuation of heritage assets** – in December 2006 the Accounting Standards Board issued an exposure draft (ED 40 – Accounting for heritage assets) proposing changes in the valuation and recognition arrangements for heritage assets. There has been a mixed response to the ED, and it is not clear that any resulting Financial Reporting Standard (FRS) will reflect in full the ED proposals. Nevertheless, any changes in the accounting and disclosure requirements are likely to be adopted by the FReM and will therefore be applicable

to NLS. Given the extent of heritage assets owned by NLS, it is important that developments in this area are monitored closely by NLS Finance Department.

- **International Financial Reporting Standards** - the introduction of IFRS's from 2008/09 is likely to significantly change some accounting policies. NLS will need to review their accounting policies to ensure that appropriate disclosures are made in the financial statements.
- **Change in internal audit provider** - the internal audit function is now provided by Baker Tilly (previously Scott-Moncrieff). We will continue to liaise with the internal auditor in order to maximise the extent to which we can place reliance on their work and thereby reduce the overall audit burden on NLS.