

Scottish Executive

Report on the 2006/07 audit



October 2007

Note:

Prior to September 2007 the Scottish Administration was generally referred to as the Scottish Executive. It is now called the Scottish Government. When dealing with the earlier period this report refers to the Scottish Executive. Recommendations for the future refer to the Scottish Government.

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. It provides services to the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Government and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

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Key Messages

This report provides the Scottish Government, the Auditor General and the Scottish Government Audit Committee with a summary of the key messages arising from our audit of the Scottish Executive in 2006/07. In particular, the Scottish Government Audit Committee should consider the outcomes from our audit in supporting a recommendation to the Permanent Secretary on the certification of the Consolidated Accounts.

We have reviewed the Scottish Executive's (the Executive) governance, performance and financial position for the year to 31 March 2007. As part of our audit approach we have also assessed how the Executive has managed some of the main strategic priorities and risks that it faces.

Financial Stewardship

Audit Report on Accounts

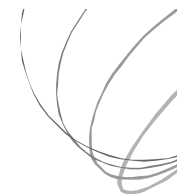
We have concluded that the financial statements of the Scottish Executive give a true and fair view of the state of affairs of the Scottish Executive and the consolidation of the entities within the departmental accounting boundary at 31 March 2007 and of the consolidated net resource outturn during the year.

We have also concluded 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, including the limits authorised by the Budget (Scotland) Act 2006.

We have reviewed the other issues we are required to consider as part of our audit opinion, such as the Annual Report, the Remuneration Report and the Statement on Internal Control. We can confirm that there are no further matters that we need to bring to the Scottish Government's attention.

Section 22(3) Reports

The Auditor General considers whether there are issues relevant to the audit of the Scottish Executive that should be reported to Parliament under Section 22(3) of the Public Finance and Accountability Act 2000. The Auditor General has concluded that there are no such matters arising from the 2006/07 audit.



Financial Position

The final outturn for the 2006/07 financial year was £25,664 million, against a net resource budget of £25,920 million, representing an underspend of £256 million (just under 1% of the Executive's overall budget). This compares with a final outturn for last year of £23,901 million, and an underspend of £296 million. All Departments remained within their Budget Act limit.

In June 2007 the Cabinet Secretary for Finance and Sustainable Growth announced that the Executive had unspent balances of £1.5 billion which were held by the Treasury on Scotland's behalf. This balance includes £1,180 million of earmarked funding for individual portfolios which is held within the Central Unallocated Provision (CUP). Over the last three years this balance has significantly increased. The diminution of the purchasing power of these reserves over time, combined with the opportunity cost from not using the funds, results in a consequential risk that better value could have been achieved through earlier use.

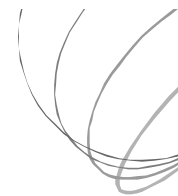
Governance

Corporate Governance

In 2005/06 we reviewed corporate governance arrangements within the Executive. The Executive indicated that the issues raised would be considered as part of the Taking Stock review, and we planned to follow-up the report findings and recommendations as part of the 2006/07 audit. The significant changes in accountability and governance arrangements since the election means that this work is best deferred until the new arrangements are embedded. We will therefore follow-up our report as part of a review of the newly established arrangements in 2007/08.

Financial Management and Budgetary Control

In 2005/06 we also reviewed Financial Management and Budgetary Control (FMBC). Since then, a number of our recommendations aimed at operational improvements have been taken forward by the Finance Directorate. In the meantime, the key strategic findings have been subsequently endorsed and re-enforced by high-level, external exercises commissioned by the Executive, notably the Taking Stock Review. We have followed-up progress on the key strategic issues highlighted and a draft report is with the Permanent Secretary for comment. It highlights our continuing concerns about the role and status of the finance function and the organisational barriers that impact on its ability to operate more strategically and efficiently across the organisation. This presents particular risks in the period of transition following the May election, with new governance and accountability arrangements being introduced, and going forward during a time of tightening financial constraints. Further work is planned as part of the 2007/08 audit to follow up all the report findings as new governance arrangements bed down.



Internal Control Framework

The establishment and operation of an efficient and effective internal audit function forms a key element of effective governance and stewardship. We have reviewed the Scottish Executive Internal Audit Division and concluded that they continue to comply with Government Internal Audit Standards and that we are able to place reliance on their work for the purposes of our audit.

With the specific exception of the payroll system, we have concluded that the Executive's financial systems and procedures operate adequately to enable us to place reliance on them and to limit the risks of material misstatement of the accounts, error or fraud. With respect to the Executive's payroll system, we concluded that only limited reliance could be placed on the system due to a number of weaknesses in key controls during the period.

Performance

Best Value

Audit Scotland carried out a baseline review to establish the arrangements in place across the central government and NHS sectors which support Best Value and continuous improvement, and to identify areas of good practice. Within this, a separate review was carried out at the Scottish Executive covering corporate functions and all departments. The results of these reviews were presented to each individual organisation, and a summary was provided to the Executive for internal management purposes.

The Executive has demonstrated a strong corporate commitment to Best Value and introduced a number of major initiatives to support continuous improvement, both in core departments and across the wider public sector. The findings from the review across the core departments and corporate centre indicated, however, that arrangements are generally still under development, as are the management information systems to demonstrate and monitor continuous improvement.

Audit Scotland is considering what type of audit approach might be appropriate for non-statutory Best Value in the public sector. The results from the recently published review of the audit and inspection regime in Scotland by Professor Crerar will inform our thinking. Thereafter we will consult with the Scottish Government on our proposals.



Efficient Government

In 2005/06 the Executive claimed savings of £441 million against a target of £405 million. These savings were reviewed by Audit Scotland, and the Auditor General provided a report to Parliament under Section 23 of the Public Finance and Accountability (Scotland) Act 2000. The review concluded that progress had been made in the measuring and monitoring techniques used to identify and quantify savings, however there was still further work to be done to make the savings auditable.

In the context of future financial constraints, failure to achieve sustainable efficiencies may impact adversely on the quality of public services. The outturn results against the 2006/07 targets will be published shortly. Early indications are that the reported savings figure will substantially exceed the target.

e-Procurement

In 2006/07 we undertook a second follow-up review of the eProcurement Scotland (ePS) programme. We concluded that progress has been made in addressing the risk areas identified during our earlier audit, although there are a number of areas where further work is required. In relation to achievement of Efficient Government targets, there remains a high risk that anticipated efficiency savings will not be fully achieved, although this is a general issue for the Public Procurement Reform Board rather than ePS specifically. We will continue to monitor progress in this area.

Looking Forward

The final part of our report notes some specific key risk areas for the Scottish Government going forward. Restructuring and revised governance arrangements in the process of being introduced after the election present particular risks during the period of transition. In addition, the tight financial settlement increases the need to ensure that robust financial management processes are in place. These and the other issues outlined will be considered further as part of our risk assessment and audit planning process for the 2007/08 audit.



Introduction

1. This report summarises the findings from our 2006/07 audit of the Scottish Executive. The scope of the audit was set out in our Departmental and Summary Audit Plans which outlined the key business risks facing the Executive and individual Departments and described the work we planned to carry out on:
 - financial statements;
 - governance; and
 - performance.
2. This report completes our audit by giving an overview of the work we carried out and a summary of our key findings. We have structured the main body of the report to cover the three topics listed above, as well as our view on emerging risk areas for 2007/08.
3. During the year we undertook a range of reviews including a high level follow up of financial management, review of all core financial systems and substantial work on the financial accounts systems. Other risk areas and related planned management actions have or are being separately reported to the Executive in the relevant topical reports.
4. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officials and non-executives of the Executive during the course of our audit. This report will be published on our website, www.audit-scotland.gov.uk.



Financial Stewardship

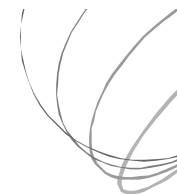
5. In this section we summarise key outcomes from our audit of the Scottish Executive consolidated financial statements for 2006/07, and comment on significant financial management and accounting issues.

Our Responsibilities

6. Our audit plan sets out our responsibilities in detail. In summary, we audit the consolidated financial statements and give an opinion on:
 - whether they give a true and fair view of the financial position and 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; and
 - the regularity of the expenditure and receipts.
7. We also review the Statement on Internal Control by considering the adequacy of the process put in place by the Principal Accountable Officer to obtain assurances on the overall system of internal control and assess whether disclosures in the statement are consistent with our knowledge of the organisation.

Overall Conclusion

8. We have concluded that the financial statements of the Scottish Executive give a true and fair view of the state of affairs of the Scottish Executive and the consolidation of the entities within the departmental accounting boundary at 31 March 2007.
9. We have also concluded that:
 - 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, the Budget (Scotland) Act covering the financial year and sections 4 to 7 of the Public Finance and Accountability (Scotland) Act 2000; and
 - the sums paid out of the Scottish Consolidated Fund for the purpose of meeting the expenditure shown in the financial statements were applied in accordance with section 65 of the Scotland Act 1998.



10. A small number of adjustments for financial misstatements were made to the draft Consolidated Accounts presented for audit. The Accounts were not adjusted to correct a number of financial misstatements which, individually and cumulatively, were not sufficiently material to impact on the audit opinion. In accordance with auditing standards, the unadjusted errors have been separately reported to the Audit Committee and Principal Accountable Officer in our International Auditing Standards (ISA) 260 report.
11. Our review of the Statement on Internal Control concluded that it complies with the relevant guidance and is not inconsistent with other information we are aware of from our audit.

The Financial Position

12. The Budget (Scotland) Act 2006 prescribes, for the financial year 2006/07, both the financial limits on the use of resources by the Departments of the Scottish Executive and how these resources can be used. The final approved net resource budget for the Scottish Executive was £25,920 million. The net outturn for the year ended 31 March 2007 was £25,664 million (2005/06: £23,901 million), resulting in an overall underspend of £256 million (2005/06: £296 million). The split of the underspend between resource and capital was £169 million and £87 million respectively. The net outturn by Departments is highlighted in the following Exhibit.

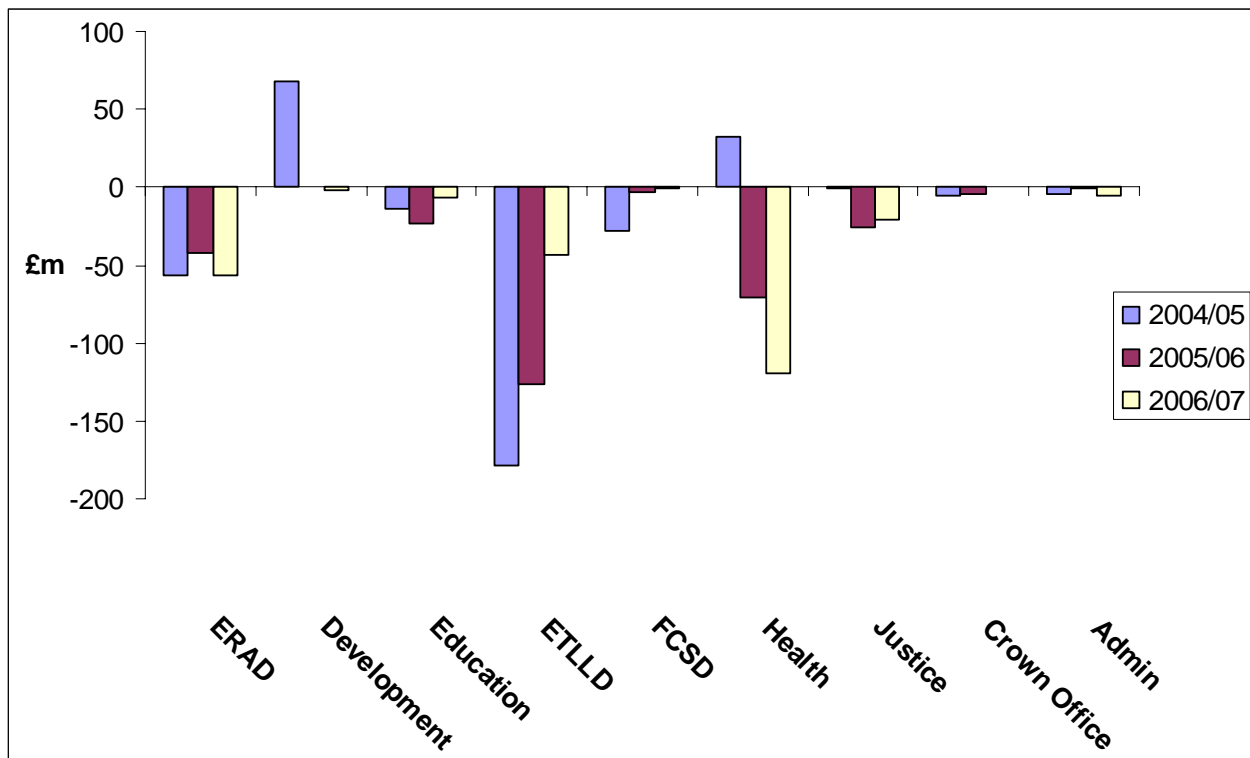
Exhibit 1 – Performance against Resource Budget 2006/07

Department	Resource Outturn £m	Capital Outturn £m	Total Outturn £m	Budget £m	Variance £m
Environment and Rural Affairs	555	43	598	655	57
Development	1,507	8	1,515	1,517	2
Education	1,027	2	1,029	1,036	7
Enterprise, Transport and Lifelong Learning	4,853	312	5,165	5,209	44
Finance and Central Services	7,770	1	7,771	7,772	1
Health	7,425	324	7,749	7,868	119
Justice	1,396	89	1,485	1,506	21
Crown Office	89	10	99	99	0
Administration	239	14	253	258	5
Total	24,861	803	25,664	25,920	256



13. The Scottish Executive met all nine departmental expenditure limits prescribed in the Budget (Scotland) Act 2006. The underspends incurred by the Departments over the period 2004/05 to 2006/07 are highlighted in Exhibit 2.

Exhibit 2 – Departmental Under/Overspends 2004/05 to 2006/07



14. The most significant underspends in 2006/07 were incurred by the Health Department, the Environment and Rural Affairs Department (ERAD) and the Enterprise, Transport and Lifelong Learning Department (ETLLD) which incurred underspends of £119 million, £57 million and £44 million respectively.
15. The Health Department underspends mainly relate to slippage in general expenditure and capital projects at Health Boards and lower than expected expenditure on GP premises. The most significant element for ERAD is the lower than estimated borrowing by Scottish Water to support its capital investment programme. For ETLLD there were a number of significant offsetting variances with underspends being incurred on rail infrastructure (£18 million), slower uptake of capital grants by third parties (£27 million), and delays in the rollout of the younger persons concessionary scheme and the smartcard project (£22 million). These underspends were offset by increases in road maintenance (£58 million) and the additional purchase of land for the M74 scheme (£15 million).



16. Total operating income generated by the Scottish Executive was £3,040 million of which £245 million could not be used and required to be surrendered to the Scottish Consolidated Fund. Of this, £99 million was for designated receipts, such as fines, fees and forfeitures, which require to be surrendered under the Designated Receipts Order. The remaining £146 million related to excess receipts being generated which were not covered by Budget (Scotland) Act 2006 authority, and therefore by default require to be surrendered to the Scottish Consolidated Fund. These excess receipts relate to National Insurance receipts for the Health Department.
17. The total consolidated assets of the Executive as at 31 March 2007 are £24.8 billion, an increase of just under £1.5 billion on the previous year. The majority of the assets of the Executive are categorised under 3 main areas:
 - land and buildings £4.7 billion (2005/06: £4.6 billion) most of which comprises the NHS and Prisons Estate;
 - the roads network £13.1 billion (2005/06: £12.5 billion); and
 - investments £4.0 billion (2005/06: £3.8 billion) of which 45% is represented by student loans.
18. With respect to the total liabilities of £4.6 billion, the most significant individual items are instalments due in over one year on National Loans Fund loans and provisions made against student loans. These were £787 million and £659 million, a decrease of 3% and increase of 6% respectively on the prior year.

Wider Financial Management

19. In June 2007 the Cabinet Secretary for Finance and Sustainable Growth announced that the Executive had unspent balances of approximately £1.5 billion which were held by the Treasury on Scotland's behalf. This balance comprises accumulated underspends against the Scottish budget block carried forward using the End Year Flexibility (EYF) process since devolution and includes earmarked funding for individual portfolios which is held within the Central Unallocated Provision (CUP).
20. The CUP was established in September 2004 to provide a more flexible mechanism for managing spend between financial years. The balance as at 31 March 2007 was £1,180 million (31 March 2006: £965 million). The balances in the CUP over the last 3 years for the **core** Scottish Executive Departments are highlighted in Exhibit 3.



Exhibit 3 – Departmental CUP Balances 2004/05 to 2006/07

Department	SE CUP Year End Balances		
	2004/05	2005/06	2006/07
	£000	£000	£000
Finance and Central Services	46,883	78,941	88,889
Education	68,506	140,168	146,827
Development	97,000	135,977	91,463
Enterprise, Transport and Lifelong Learning	82,926	328,283	271,210
Health	20,000	(14,554)	(14,554)
Justice	8,404	8,310	60,928
Environment and Rural Affairs	198,155	254,821	485,169
Administration	10,664	3,564	14,196
Crown Office and Procurator Fiscal Service	0	1,391	2,473
Total	532,538*	936,901*	1,146,601*

* Totals exclude Forestry Commission, National Archives and a number of other bodies outwith the core Scottish Executive

21. The majority of balances held in the CUP are allocated to specific spending plans which have not yet been brought before Parliament for approval. They form part of the Executive's financial management processes and cannot be used without Parliamentary approval. As balances in the CUP relate to financial planning activity, they are not disclosed within the Executive's Consolidated Accounts and are not covered by our audit opinion. Changes to the balances held in the CUP are reported through Budget documents which are subject to parliamentary scrutiny, however the cumulative total reserves are not shown.

22. The CUP was introduced as a means of both ensuring that budgets approved annually by the Scottish Parliament would be taut and realistic and to provide a mechanism to ensure that budget provision would be in place to meet spending plans as and when required. The CUP balances have fluctuated across the Departments but there has been a general upward trend, with the total balance increasing significantly over the period. The diminution of the purchasing power of these reserves over time, combined with the opportunity cost from not using the funds, results in a consequential risk that better value could have been achieved through earlier use.

23. It is intended that approximately £650 million of the £1.5 billion end year flexibility (EYF) balance held by HM Treasury will be utilised in 2007/08, with the remaining balance available to supplement what has long been anticipated as a much tighter spending review settlement for the period 2008/09 to 2010/11. The Scottish Government has recently agreed full access to these funds with HM Treasury and factored this into its proposed spending plans aimed at delivering its targets and priorities.



Issues Arising from the Audit

Accounts Preparation

24. The draft schedules for the core Scottish Executive Departments were submitted for audit on 13 June and the draft consolidated account was received on 17 August, both in line with the agreed timetable. There has been continued improvement in the timeliness of the accounts presented by the Finance Group and the Executive should be commended for the presentation of draft consolidated accounts in advance of the previous year.
25. There are a number of matters arising from the final accounts process that we would wish to highlight. The key issues are:
- problems with the completion of the payroll, accounts payable and VAT reconciliations, which apart from payroll, had not been encountered in the previous year. Whilst all year end reconciliations were eventually completed there were significant delays, impacting on the audit process. We would also stress that regular reconciliations completed timeously during the year are fundamental components of good internal control;
 - the number of minor suspense accounts maintained by the Executive that are not subject to clearance, with balances remaining unchanged over a period of years. Whilst the Executive has made significant efforts to encourage the clearance of suspense accounts by Departments there are still a number that require to be reviewed and cleared routinely;
 - deficiencies across the organisation in the level of understanding of accruals and other accounting transactions required to support the production of the accounts. There was also evidence of varying use of the financial accounting system as a tool for the management of expenditure, with some divisions maintaining independent local records; and
 - the draft Statement on Internal Control was not received until 3 October due to delays in the receipt of Certificates of Assurance from Departments.

Group Audit

26. The consolidated resource accounts of the Executive consolidate the accounts of the core Executive, the Crown Office, Executive Agencies and NHS Health Boards, including for the first time Transport Scotland as an individual entity.
27. In previous years we have reported issues in the preparation and completion of the NHS sub-consolidation and the roads valuation (now the responsibility of Transport Scotland). We are pleased to report that no significant difficulties were encountered this year. In relation to roads, it is important that for future years, with more new road schemes coming on line, that this continues as any delays in the completion and audit of Transport Scotland's accounts could have a knock on effect on the completion of the Scottish Government's Consolidated Accounts.



28. With respect to the Executive Agencies consolidated a number of issues arose, specifically:
- **Accountant in Bankruptcy (AiB)** – the preparation and production of the AiB draft accounts was not in line with the consolidation timetable agreed by the Executive with its agencies, with further delays in the presentation of complete draft accounts for audit. The very late submission of the consolidation pack caused problems for the consolidation process and its schedule.
 - **Fisheries Research Service (FRS)** – there were issues with the quality of the draft accounts submitted for audit and subsequently a large number of revisions to the accounts. This also led to delay in submission of the draft consolidation pack to Finance.
 - **Scottish Agricultural Science Agency (SASA)** - the auditors withdrew from the audit until revised draft accounts were received because the initial draft accounts and supporting information were not considered to be of sufficient quality to enable the audit to proceed. There was also a delay in submission of the draft consolidation pack to Finance.
29. Whilst these issues have not impacted on the completion of the Consolidated Accounts this year issues such as these could have potential impact in future years, particularly if the faster closing agenda is taken forward. It is therefore important that senior management within all agencies ensure that appropriate attention is given to the production of robust financial statements in line with the Scottish Government consolidation timetable.
30. The Crown Office presented their accounts in line with their planned timetable which enabled the certification of their accounts by the end of September. The Crown Office has a separate outturn statement and Budget Act limit disclosed within the Scottish Executive Consolidated Accounts. However, with the faster closing agenda aim of finalising the Scottish Government's Consolidated Accounts towards the end of September there is a need for the Crown Office and its external auditors to review its timetable.
31. Aside from the presentation and preparation issues highlighted above, there are a number of other issues arising from these audits. Those that are considered significant or material to the Consolidated Accounts have been reported separately to the Audit Committee and Principal Accountable Officer in our International Auditing Standards (ISA) 260 report. However there is one wider issue which we wish to highlight in respect of the governance arrangements in place within the Mental Health Tribunal for Scotland Administration. As highlighted in Appendix B on Section 22 reports issued by the Auditor General, appropriate governance and accountability arrangements are still not in place and there are a number of key areas that require to be developed as a priority within this body.



Faster Closing

32. The accounts and the audit of the consolidated financial statements were completed two weeks earlier than in 2005/06 which continues to highlight progress by all parties in taking forward the faster closing agenda, particularly in light of the significant changes that have occurred over the last six months. However, faster closing still represents a key challenge for the Scottish Government and Audit Scotland going forward.
33. We have prepared a draft paper on the processes, barriers and benefits from the Westminster experience, and further afield, following discussion with the National Audit Office. This has been passed to the Scottish Government and discussions are ongoing on taking this agenda forward through a joint project team.

Register of Interests and Related Parties Disclosure

34. As highlighted in last year's report, the Ethical Standards in Public Life etc (Scotland) Act 2000 requires that relevant public bodies maintain a register of members' interests. This supports the promotion of the highest standards in public life and helps to ensure that potential conflicts of interest are avoided. Whilst the Act does not specifically cover the Scottish Executive, and in particular its non-executive members, good practice would be to maintain a register of interests covering the management group. The Executive indicated that it would consider this issue further but as yet no action has been taken.
35. The Government Financial Reporting Manual (FReM) requires the Executive to disclose within its financial statements material transactions with related parties, including senior managers and non-executives. At present the Executive has not undertaken a specific review and does not disclose any transactions in its Consolidated Accounts, although a number of potential related parties transactions have been identified by audit. The Scottish Government need to address this issue to ensure that there is appropriate transparency and, in our view, this would be supported by the maintenance of a Register of Interests.
36. The FReM also now requires the disclosure of related party transactions with Ministers. Again, the Executive has not undertaken a specific review for any such potential transactions and therefore none are disclosed within the financial statements although the Ministers' register of interest can be found on the Parliament's website.



Other Matters Arising

37. In line with normal practice a number of issues were discussed and resolved with officers during the course of the audit. We have presented our International Auditing Standards (ISA) 260 report to those charged with governance and a separate report to the Director of Finance is being prepared which provides details of issues arising from the financial statements audit which do not need to be reported here. We are also in the process of preparing summary reports for each Department on the audit and the specific issues relating to them.

Statement on Internal Control

38. The Principal Accountable Officer is required to provide a signed statement on internal control which he signs as part of the Scottish Executive Consolidated Resource Accounts. He is supported in this by Departmental Accountable Officers who provide Certificates of Assurance covering their portfolio responsibilities. The Certificates of Assurance are themselves based on an assurance framework which is detailed in the Scottish Public Finance Manual. As highlighted earlier in this report, the draft statement of internal control was not received by us until 3 October 2007 due to delays in the receipt of Certificates of Assurance from Departments.
39. The Statement on Internal Control provided by the Principal Accountable Officer reflected the Certificates of Assurance provided by the Departmental Accountable Officers, the report from the Head of Internal Audit and the main findings from external audit work. Our review of the Statement concluded that it complies with the relevant guidance and is not inconsistent with other information we are aware of from our audit.

Regularity Assertion

40. The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors 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 addressed this requirement through a range of procedures, including receipt of written assurances from the Executive as to their own views on adherence to enactments and guidance. No significant issues were identified for disclosure.

Scottish Consolidated Fund

41. We have confirmed that the Scottish Consolidated Fund (SCF) financial statements properly present the receipts and payments of the SCF and the balance held at 31 March 2007, and have been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers. We have also confirmed that in all material respects, the sums paid out of the SCF were in accordance with Section 65 of the Scotland Act 1998.



42. During the financial year the SCF received receipts of £23,841 million, representing an increase of 4% on the prior year. Receipts from the Department of Constitutional Affairs under section 64(2) of the Scotland Act 1998 (£21,752 million) and from Non-Domestic Rate income (£1,884 million) account for the significant majority of SCF receipts. The SCF made payments of £24,635 million representing an increase of 11% on the prior year. Payments under Budget (Scotland) Act documents account for 99% of all payments made. At the financial year end the SCF reported a deficit of receipts over payments of £794 million and balance of £58.4 million.
43. With respect to the SCF audit, there is only one issue that we would wish to highlight. In 2001 cash balances of £41.6 million relating to NHS Trusts were surrendered to the SCF. The Scottish Executive agreed with the Treasury, at that time, that this cash could be used by the Executive to meet the costs of repayment of housing debt to a Council when it transferred its housing stock to community ownership. From our audit of that Council, we are not aware of any immediate plans that it has to transfer its housing stock to community ownership and consideration should be given to alternatives.

Non Domestic Rating White Paper Account

44. We have confirmed that the Non Domestic Rating (NDR) financial statements properly present the receipts and payments of the Scottish Ministers in respect of Non-Domestic Rating for the year ended 31 March 2007 and the balance held at that date, and have been properly prepared in accordance with Schedule 12 of the Local Government Finance Act 1992 and directions made thereunder by the Scottish Ministers.
45. We have also confirmed that the receipts and payments shown in the accounts were incurred or applied in accordance with any applicable enactments and guidance issued by Scottish Ministers, sections 4 to 7 of the Public Finance and Accountability (Scotland) Act 2000, and the sums paid out of the Scottish Consolidated Fund for the purpose of meeting the expenditure shown in the accounts were applied in accordance with Section 65 of the Scotland Act 1998.
46. Total contributions for 2006/07 were £1,909 million with an additional £108 million relating to prior years. The total sums distributed amounted to £1,884 million for 2006/07 and £17 million for prior years. The surplus carried forward at the year end was £12.1 million compared to a deficit of £104.2 million at the previous year end. There are no significant issues to report.



UK Statement of European Funds

47. Following an announcement made by the then Economic Secretary to the Treasury, the Treasury has prepared a UK Consolidated Statement on the use of EU Funds for the financial year 2006/07, which is to be laid before the Westminster Parliament. The purpose of this statement is to enhance audit and parliamentary scrutiny of the UK's use of EU funds, help detect any irregularities and generally improve financial management.
48. The National Audit Office lead on the audit of this statement and our role is to support the audit of expenditure incurred in Scotland included within the statement. The draft statement to which Scotland contributed has only just been received from the Treasury and is now in the process of being audited.

Fraser Investigation Final Costs Statement

49. The Executive asked Audit Scotland to carry out an audit of the final costs statement for the Fraser investigation. The statement was received for audit on 10 October 2007 and the audit is now underway and is expected to be completed shortly.

Auditor General Reports on Accounts

50. The Auditor General has concluded that there are no matters arising from the 2006/07 audit of the Executive's accounts which require to be reported to Parliament under Section 22(3) of the Public Finance and Accountability (Scotland) Act 2000.
51. Appendix B contains a brief summary of the Auditor General's Section 22(3) reports on the accounts of the Executive's bodies which have been or are soon to be laid this year.



Governance

52. This section sets out our main findings arising from our review of the Executive's governance arrangements. We focused on:

- review of the key systems of internal control;
- following up our financial management and budgetary control report;
- review of internal audit; and
- specific joint reviews with other inspectorates.

53. We also discharged our audit responsibilities as they relate to prevention and detection of fraud and irregularity, standards of conduct and the Executive's financial position.

Corporate Governance

54. In 2005/06 we reviewed corporate governance arrangements within the Executive. The Executive indicated that the issues raised in the report would be considered as part of the Taking Stock review, and we planned to follow-up the report findings and recommendations as part of the 2006/07 audit. The significant changes in accountability and governance arrangements since the election means that this work is best deferred until the new arrangements are embedded. We will therefore follow-up our report as part of a review of the newly established arrangements in the 2007/08 audit.

Financial Management and Budgetary Control

55. Last year we also reviewed Financial Management and Budgetary Control (FMBC). Following the review, we prepared a report that was subject to extensive discussion with Executive officials. The Scottish Executive Audit Committee (SEAC) considered the report in October 2006, and again in February 2007.

56. During 2006/07, a number of the recommendations aimed at operational improvements have been taken forward by the Finance Directorate. In the meantime, the key strategic findings have subsequently been endorsed and re-enforced by high-level, external exercises commissioned by the Executive:

- Taking Stock: Fit for Future review;
- Financial Management Review (this has still to be finalised); and
- Howat Report.



57. Follow-up work has been undertaken on the key strategic issues highlighted in our original report, and a draft report is with the Permanent Secretary for comment. It highlights our continuing concerns about the role and status of the finance function and the organisational barriers that impact on its ability to operate more strategically and efficiently across the organisation. This presents particular risks in the period of transition following the May election, with new governance and accountability arrangements being introduced. It also presents equally significant risks for an organisation with an annual budget of more than £30 billion, as the Scottish Government faces an increasingly challenging financial environment. These risks increase the importance of having an authoritative, and professionally led, strategic finance function capable of supporting strategic change, improved decision making, sound monitoring, and taking a lead role in co-ordination and challenge on all financial matters across the organisation. Further work is planned as part of the 2007/08 audit to follow up all the report findings, particularly operational issues.
58. A specific review of the re-organisation of financial management within the Health Department was also undertaken. We considered the progress on the merger of the previously distinct finance functions into one new division. We found that significant progress had been made in undertaking a risk based approach to monitoring the financial performance of the Department and NHS bodies. These changes are being delivered through re-organisation of staff and teams, changes in working practices and through the ongoing professionalisation of the Health Finance Division.

Internal Audit

59. The establishment and operation of an efficient and effective internal audit function forms a key element of effective governance and stewardship. During the year we carried out a comprehensive review of the Scottish Executive Internal Audit Division ("Internal Audit"). The review covered:
- the extent of Internal Audit's compliance with Government Internal Audit Standards (GIAS) in planning and undertaking their work; and
 - a detailed evaluation of specific internal audit work to determine the extent to which we can rely on this work for the purposes of our audit.
60. From our review we were able to conclude that Internal Audit comply with GIAS in adopting a risk based audit approach in planning and undertaking their work. We identified a number of areas of good practice, including the separation of the Head of Internal Audit role from other responsibilities within the Finance Directorate, as well as a few areas for improvement in the management and governance arrangements for the internal audit function. However, none of these affected our overall assessment and we were able to place reliance on the work of Internal Audit for the purposes of our audit of the Scottish Executive.



Systems of Internal Control

61. As part of our audit we reviewed the high level controls in a number of the Scottish Executive's systems that impact on the financial statements. 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. Our audit covered central financial systems, specific departmental systems and Information and Communication Technology.

Central Financial Systems

62. We reviewed the following key systems:

- the operation of the main accounting system (SEAS);
- accounts payable systems (including the operation of EASEbuy);
- the central aspects of the accounts receivable system, and cash and banking systems (including the reconciliation of the main bank account);
- the central aspects of the operation of the Britannia fixed asset system; and
- the central aspects of the operation of the payroll and subsistence systems.

63. Excluding payroll, our overall conclusion is that key controls across the Executive's central systems and procedures are operating adequately. However, a number of the recommendations made in previous reports, particularly in relation to SEAS and cash income and banking, have not been implemented or only partially implemented. In addition, issues were identified over controls that have previously been operating satisfactorily. Findings include:

- a number of weaknesses in the segregation of duties across the Executive's financial systems; and
- issues with key year end reconciliations including delays in the completion of reconciliations, limited evidence of timely completion or management review and unexplained or unresolved differences.

64. With respect to Executive's payroll system (ePayFact), we have obtained sufficient assurance for our audit opinion. We were required to obtain the majority of our assurance from increased transaction testing as we were only able to place limited assurance on the key controls operating within the system. The same conclusion was reached in our 2005/06 audit. Action to address the majority of the risks and issues previously identified was not due to take place until after 31 March 2007, therefore limited progress had been made for the 2006/07 financial year.



65. The weaknesses identified in the key controls present an increased risk of error or fraud occurring. Audit testing, however, did not identify any incidences of error or fraud.

Departmental Systems

66. We reviewed the high level controls for a range of key departmental programme expenditure areas and their underlying systems within the Scottish Executive which impact on the financial statements. These included:

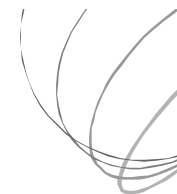
- Student Awards, Graduate Endowment and Individual Learning Accounts (excluding controls operated by Learndirect Scotland);
- European Structural Funds;
- Supporting People; and
- Common Agricultural Policy Market Support.

67. We initially intended to place reliance on the controls in place for Regional Selective Assistance. Due to the introduction of a new grant management system during the year, we decided that direct testing of the grant payments would provide more efficient and effective assurance for our audit of the financial statements. We have undertaken a review of the computer application controls which is highlighted later in this report and we will complete a full review of the control environment in 2007/08 once the system has bedded down.

68. Our review of controls over Common Agricultural Policy Market (CAPM) Support expenditure is carried out in order to provide assurance for both the audit of the Scottish Executive's Consolidated Accounts and the European Guarantee Account¹ audit. Our audit work on the CAPM focuses on the systems and procedures operated by the Environment and Rural Affairs Department to support payments under the 2007 European Guarantee Account and to carry out substantive testing of a sample of payments made to producers.

69. This work is still ongoing and the results will be reported in detail separately to the Scottish Government and European Commission. Testing of the control environment is not complete, although it is expected that reliance will be placed on it, including the controls over the Single Farm Payment Scheme (SFPS). This will represent good progress from last year when significant issues were raised. Sufficient assurance has been obtained for payments made up to 31 March 2007 through detailed transaction testing.

¹ EAGGF 2006 accounting year - 16 October 2005 to 15 October 2006



70. For the other departmental programme expenditure areas and their underlying systems we have concluded that key controls operated satisfactorily.

Information and Communication Technology

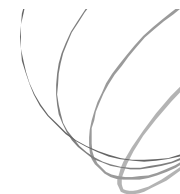
71. As part of our 2006/07 audit our specialist computer auditors have undertaken a number of reviews of ICT controls at the Scottish Executive including:
- Computer Services Review;
 - Central financial systems, in particular SEAS and Payroll;
 - the e-Procurement Scotland programme;
 - Review of eRDM Scanning Solutions within Executive Business Areas;
 - Information security;
 - CMAS (Innovation Support); and
 - Grant Aid for Scottish Student System (GRASS).

Computer Services Review

72. The Executive's ICT services division, ISIS, provides a shared service data networking infrastructure to the Executive and a number of Executive Agencies. ISIS supports the infrastructure and core systems such as eRDM, Parliamentary Questions, PA-BRIX and services such as the Internet, Intranet and email.
73. We carried out a high level Computer Services Review (CSR) at the Executive. We identified a number of areas of good practice and areas where improvement could be made, including the formalisation of the corporate Information Management Strategy developed in 2005 and the development of departmental business continuity plans.

eRDM - Scanning

74. Last year we carried out a high level review of the Executive's Electronic Records and Document Management (eRDM) system's scanning procedures. This initial review identified a number of risks and, during 2006/07, we have followed up on the agreed actions to assess whether these risks have been adequately addressed. We surveyed a number of staff about their practical experience with scanning as part of this follow-up review.
75. We found that scanning procedures have become business as usual in many areas and that user confidence has increased. While not all risk areas have been fully addressed, overall progress has been good.



Information Security

76. As part of our work to support the European Guarantee Account audit we are required to report annually on IT Security within the Environment and Rural Affairs Department. To a large extent this means that we are required to consider IT security across the Executive as the Department is subject to corporate IT security arrangements and uses corporate financial systems for processing European Guarantee Account payments.
77. The detailed results from our work are recorded in the formal European Guarantee Account 2006 report. Overall we found that the information systems security of the Environment and Rural Affairs Department is generally well organised and maintained. Strong central controls and guidelines are available, designed to provide appropriate security protection. However, whilst there has been improvement in performance since last year, further work is still required to demonstrate full compliance with ISO 17799 by 2008 as required by the EU.

Grant Aid for Scottish Student System (GRASS)

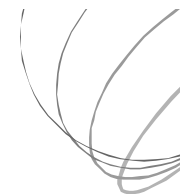
78. The GRASS system is a grant administration system for processing student award applications. Our review identified a number of areas of good practice, although some areas were identified where action was required to mitigate risks, including security in web applications, the over reliance on a few key staff and the limited management information available.

CMAS (Innovation Support)

79. CMAS (Case Management and Administration system) is the grant management application system which has recently been developed in-house to support the management of the Regional Selective Assistance (RSA) programme and the Business Growth and Innovation (BGI) grant schemes. Again our review identified a number of areas of good practice and some areas of increased risk, including the over reliance on one systems analyst/developer and incomplete system development documentation.

Other Specific Reviews

80. As part of our audit of the Executive we have also carried three specific reviews of voluntary sector organisations in receipt of funding from the Education portfolio. These were joint reviews carried out in conjunction with Her Majesty's Inspectorate of Education. The reviews covered:
- Young Scot;
 - Scottish Youth Parliament; and
 - Youthlink Scotland.



Young Scot

81. Young Scot's specific role is to act as the national youth information agency for Scotland. Our review considered how Young Scot discharged their role, including the corporate and financial governance of the organisation. The joint review concluded that Young Scot has a number of key strengths and is an effectively managed organisation. Specifically:

- Young Scot is continuously seeking to improve the key outcomes and impacts of its work with young people and other stakeholders;
- management and leadership are effective; and
- quality improvement arrangements are effective and Young Scot has the capacity to continue to improve.

Scottish Youth Parliament

82. This review followed up the report published in March 2004 by HMIE to assess the progress made in addressing a number of significant issues. The follow up work identified that although good progress had been made, further work is still required. As many of the changes have only recently been implemented and SYP are working to further improve their financial operations, HMIE will make a follow-up visit in 2008 to report on further progress.

Youthlink

83. The review followed up the report published in March 2006 and identified that, in the short period since the original review, there had been a number of significant changes to Youthlink including the appointment of a new Chief Executive, extensive re-structuring of the organisation and consultation on the national youth work strategy. Future progress will continue to be monitored.



Performance

84. 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 annual 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.
85. Accountable Officers have a duty to ensure resources 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.

Best Value

86. There is no statutory duty of Best Value in the wider public sector in Scotland covering the Scottish Executive and its Executive Agencies, Executive NDPBs, and the NHS. However, Ministers wished to encourage and embed the principles of Best Value across the public sector, and further guidance was issued in May 2006.
87. Following this, Audit Scotland carried out a baseline review to establish the arrangements in place across the central government and NHS sectors which support Best Value and continuous improvement, and to identify areas of good practice. Within this a separate review has been carried out at the Scottish Executive covering corporate functions and all departments. The results of these reviews were presented to each individual organisation, and a summary was provided to the Executive for internal management purposes. This provided an assessment of how each organisation's arrangements compared with those described under the nine characteristics from the Best Value guidance. Examples of existing good practice were also provided. This allows organisations to undertake a gap analysis and prepare an appropriate action plan.
88. The findings from the review across the core departments and the corporate centre indicated that the Executive's arrangements for securing best value are generally still under development, as are the systems in place to demonstrate and monitor continuous improvement.
89. Departmental business plans were highlighted as the key mechanism for demonstrating continuous improvement, within the overall corporate framework of the Partnership Agreement, Building a Better Scotland and the Big Picture. The Executive has demonstrated a strong corporate commitment to Best Value, and has introduced a number of major initiatives designed to support continuous improvement, both in core departments and across the wider public sector. However, there was a perceived overlap between branded initiatives, including Public Service Reform, Efficient Government, sustainable development, and the Big Picture, and there was a perceived difficulty in adequately accommodating such a wide range of branded initiatives in departmental business plans.



90. It should be emphasised that our review did not represent a best value audit of the Executive, the NHS or Agencies and NDPBs. Audit Scotland is considering what type of audit approach would be appropriate for non-statutory Best Value. The results from the recently published review of the audit and inspection regime in Scotland by Professor Crerar will inform our thinking. Thereafter we will consult with the Scottish Government on our proposals for the audit of Best Value in the wider public sector.

Public Performance Reporting

91. Public Performance Reporting is a fundamental component of Best Value, since it underpins the development of a culture of customer focus and continuous improvement, and demonstrates openness and accountability. Whilst the Scottish Executive annual accounts for 2006/07 contain an Annual Report, Operating and Financial Review (OFR) and Public Interest Report these have been prepared to meet the basic requirements of FReM and do not provide a comprehensive review of the performance of the Executive.

92. The Scottish Government needs to consider developing its annual corporate reporting mechanisms to ensure that it effectively reports its performance annually, as well as comprehensively meeting the requirements of FReM. The Annual Report, Operating and Financial Review (OFR) and Public Interest Report contained within the annual accounts may provide one appropriate mechanism for this. At a minimum the annual accounts should contain summarised information with cross-references made to other annual performance report documents.

93. To meet the requirements of FReM more comprehensively the main issues the Scottish Government should consider are:

- a more detailed review of the Scottish Government's business, including description of activities, objectives and strategies for achieving them, details of risks and uncertainties and future developments;
- disclosure of the CUP and its management;
- the disclosure of performance against key performance indicators and whether the present cross reference to other reports is sufficient on an annual basis. This is emphasised this year by the fact the Annual Evaluation report has not been produced;
- increased analysis on significant movements on operating costs and assets and liabilities in the OFR;
- details of the executive policies on sustainability, including the policies on social and community issues; and
- the action taken to maintain or develop the provision of information to, and consultation with, employees.



Efficient Government

94. In 2005/06 the Executive claimed savings of £441 million against a target of £405 million. These savings were reviewed by Audit Scotland and the Auditor General provided a report to Parliament under Section 23 of the Public Finance and Accountability Act 2000. Essentially the review concluded that although progress had been made in the measuring and monitoring techniques used to identify and quantify savings, there was still further work to be done to make the savings auditable.
95. The outturn results against the 2006/07 targets will be published shortly by the Scottish Government. Early indications are that the reported savings figure will substantially exceed the target.

eProcurement

96. In 2006/07, we undertook a second follow-up of our 2004/05 review of the eProcurement Scotland (ePS) programme. During this follow-up, we sought to update our assessment of the risk areas in the control environment and monitor progress in the roll-out of the project across the public sector. We concluded that progress has been made in addressing the risk areas identified during our earlier review, although there are a number of areas where further work is required. In relation to achievement of Efficient Government targets, there remains a high risk that anticipated efficiency savings will not be fully achieved, although this is a general issue for the Public Procurement Reform Board rather than ePS specifically.
97. Given the high profile nature of this project throughout the public sector, we will continue to monitor progress.

National Studies

98. The Public Reporting Group within Audit Scotland has carried out a number of studies during the year. Details of those published recently are included at Appendix C along with details of the forward study programme at Appendix D.



Looking Forward

99. The Scottish Government is responsible for delivering policy and managing public expenditure in a complex and dynamic environment. The public have rising expectations of improved performance in securing high quality, customer focused services and in the achievement of Best Value and efficiency in the use of resources.

100. There are a number of challenges facing the Scottish Government over the coming year and beyond including:

- **Restructuring and revised governance arrangements** – The Scottish Government has and is undergoing significant change in its structure and governance arrangements. Ensuring that these arrangements bed down and are robust will be critical over the coming period.
- **Taking Stock: Fit for the Future and the Financial Management Review** – Continuing to take forward the key outcomes from these reviews in light of the new organisational arrangements will continue to be important for the Scottish Government in its efforts to achieve continuous improvement.
- **Financial Governance** - The restructuring of the Scottish Government has resulted in significant changes for the monitoring of expenditure as the departmental management boards no longer exist. This presents a potential gap in the financial governance of the organisation and there is a risk that financial monitoring and accountability arrangements will not be as robust as they were previously until new governance and management arrangements are embedded.
- **Spending Review and Outcome Agreements** – The outcomes from the spending review and the introduction of outcome agreements will present significant challenges. Given the tight financial settlement, ensuring robust financial management processes are in place will be imperative.
- **Business Planning, Risk and Performance Management** – The development of the business planning and the risk and performance management frameworks will be important in helping to support the delivery of strategic objectives through an outcome based approach.
- **Public service reform** – The new administration has intimated a desire to de-clutter the public sector delivery landscape. Taking forward this agenda and encouraging the development of our public services is a significant challenge for the public sector as a whole.
- **International Financial Reporting Standards (IFRS)** – The Scottish Government is required to prepare accounts for 2008/09 in accordance with IFRS. The Scottish Government will need to ensure that all consolidated bodies are prepared to enable effective implementation. A project is in place to manage implementation within the Scottish Government and its consolidated bodies.



- **Procurement** – The development of procurement in the public sector continues to face key challenges to address the issues and recommendations contained in the 2006 report “The Review of Public Procurement in Scotland”. It will be important that the recommendations continue to be acted upon to improve performance in the public sector and that the benefits of the e-procurement strategy are fully realised.
- **Best Value** - The Scottish Government will need to ensure that it has mechanisms in place that enable it to demonstrate continuous improvement and that the principles of Best Value are embedded. Over the next year Audit Scotland will be developing and refining the approach to the audit of public bodies’ arrangements to secure economy, efficiency and effectiveness in the use of resources.
- **Efficient Government** - In the context of future financial constraints, failure to achieve sustainable efficiencies may impact adversely on the quality of public services. Regardless of the precise nature of the future direction of the Efficient Government Initiative, the importance of efficiency and its role in the achievement of Best Value will continue.
- **European Structural Funds closure and restructure** –The implementation of the Structural Funds for the programming period 2007 to 2013, and the closure of the 2000-2006 programme period, will continue to present the Scottish Government with a number of challenges and risks which it will require to manage.
- **Demand led policies** – The Scottish Government is implementing a number of significant demand-led policies. There are risks that demand may outstrip the estimated take up and funding provided, creating risks to service delivery and increased financial pressure on the Scottish Government.

101. Our planning process for the 2007/08 audit will incorporate a review of the effectiveness of the Scottish Government’s arrangements for managing these and other identified risk areas.



Appendix A: Action Plan

Action Point	Issue	Response and Agreed Action
Accounts preparation		
1	Processes and procedures should be reviewed to ensure the timely and accurate completion of all key processes. In particular, procedures for preparing year-end reconciliations should be improved.	The Finance Directorate will review processes and procedures in this area.
Group Audit		
2	The Scottish Government, in conjunction with Audit Scotland, should direct and encourage the timely and accurate production of financial statements of consolidated bodies for audit to support the consolidation processes and the faster closing agenda.	The Scottish Government already has a process in place for directing and encouraging the production of consolidated bodies financial information via meetings of the Consolidation Working Group, on-going communication and detailed guidance. We will continue to stress the importance of meeting group deadlines to the consolidation process, especially to senior management. We would also stress the need for audit processes to align with these objectives.
Faster Closing		
3	The Scottish Government, in conjunction with Audit Scotland, needs to develop a clear project plan to take forward the Faster Closing initiative in the short and longer term, both internally and across the consolidated bodies.	The Scottish Government are fully committed to the faster closing initiative. Meetings have been held with Audit Scotland and a paper has been tabled at the 23 October SGAC meeting outlining the joint Faster Closing project's aims. The SG will be putting together a Project Board to manage the Faster Closing project.
Register of Interests		
4	The Scottish Government should consider maintaining a register of interests for members of the Strategic Board and other senior managers, and in particular non-executives, to provide transparency in the Scottish Government's governance arrangements and support compliance with FReM.	A report will be prepared to allow the Strategic Board to consider this proposal and the Scottish Government will consider cross referencing the accounts to registers of interests for Ministers and Senior Management.



Action Point	Issue	Response and Agreed Action
Statement on Internal Control and Certificates of Assurance		
5	<p>The Scottish Government should ensure that the assurance framework that is in place to provide certificates of assurance is complied with in a robust and timely manner to enable the timely presentation of the draft Statement on Internal Control.</p>	<p>There is an assurance framework in place which is defined by the requirements set out in the Scottish Public Finance Manual. The Finance Directorate will review the guidance for 2007-08 including communication of requirements and key deadlines. Senior Management will be reminded of the importance of robust and timely completion.</p>
Public Performance Reporting		
6	<p>The Scottish Government needs to consider developing its annual corporate reporting mechanisms to ensure that it effectively reports its performance as well as comprehensively meeting the requirements of FReM.</p> <p>To meet the requirements of FReM more comprehensively the main issues the Scottish Government should consider are:</p> <ul style="list-style-type: none"> ▪ a more detailed review of the Scottish Government's business including description of activities, objectives and strategies for achieving them, details of risks and uncertainties and future developments; ▪ disclosure of the CUP and its management; ▪ the disclosure of performance against key performance indicators and whether the present cross reference is sufficient on an annual basis; ▪ increased analysis on significant movements on operating costs and assets and liabilities in the OFR; ▪ details of the executive policies on sustainability, including the policies on social and community issues; and ▪ the action taken to maintain or develop the provision of information to, and consultation with employees. 	<p>Finance Directorate will consider as part of its 2007-08 Accounts planning process, where the contents of various reports within the Annual Accounts could usefully be improved to provide more information to the public.</p> <p>Any wider reporting of Scottish Government activities needs to be considered corporately and we need to consider whether the annual accounts would be the appropriate place.</p>



Appendix B: Auditor General for Scotland Section 22(3) Reports

102. Paragraphs 103 to 111 present a brief summary of the Auditor General's reports on accounts which have been or are about to be laid this year. These issues have been considered in the context of the audit of the Scottish Executive and it was concluded that no action was necessary in relation to the audit opinion, or the need for a separate reference in a S22 report on the Executive's accounts.

Western Isles Health Board

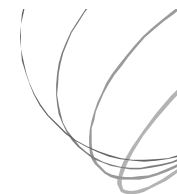
103. The Auditor General's report drew attention to the Board's failure to meet a financial target and continuing issues around governance arrangements. This is the third consecutive year that a report has been prepared on the accounts of the Western Isles Health Board. While the Board has developed a financial recovery plan, there are concerns that the targets appear unrealistic and planned savings are unlikely to be achieved. The report also indicates that the lack of financial management expertise and financial focus at Board level may result in insufficient scrutiny and monitoring of progress towards the achievement of financial recovery.

104. Serious weaknesses concerning the Board's corporate governance arrangements are also highlighted. Some progress has been made to strengthen the Board's corporate governance arrangements, but there continue to be significant concerns. The Board's Internal Audit Service has concluded that, as in the previous year, the Board did not have an adequate or effective system of internal controls in place during 2006/07.

Scottish Arts Council (SAC)

105. The auditor's report on the regularity of expenditure was qualified because of payments to the SAC's former chief executive which were not properly approved. The auditor's report on the accounts of the SAC's National Lottery Fund is similarly qualified.

106. The remuneration report in SAC's financial statements for 2006/07 refers to payments totalling £70,000 made to its former chief executive. The former chief executive voluntarily resigned from his post with effect from February 2007 in exchange for a payment of £40,000 in lieu of taxable salary for outstanding notice and an ex-gratia payment of £30,000.



107. SAC must comply with the Scottish Public Finance Manual (SPFM) issued by Scottish Ministers.

Under SPFM rules compensation is only payable in exceptional circumstances to staff who resign from their post voluntarily. Such payments must also be approved by Scottish Executive finance officials before any offer is made. In March 2007, the Minister for Tourism, Culture and Sport wrote to SAC's Chairman noting that SAC had considered options in terms of costs and effectiveness of the organisation during the period of transition to Creative Scotland but noting that action in relation to the chief executive's departure represented a breach of the SFPM. The auditor found no evidence of Scottish Executive approval and concluded that SAC had not complied with Ministerial guidance in this respect and qualified the regularity opinion.

Scottish Water

108. The Auditor General's report highlighted that Scottish Water made significant improvements in its efficiency and customer service in the period March 2002 to April 2006 and has reported that it continued to do so in 2006/07. Scottish Water reported that taken together, these improvements mean that the average household water bill is £100 less than it otherwise would have been.

109. Scottish Water still faces significant challenges in the years ahead. The Scottish Water Commission for Scotland's new targets covering the four-year period to March 2010 will require Scottish Water to contain its operating expenditure such that customers' bills will rise at less than the rate of inflation and to deliver the third capital investment programme at a cost of £2.15 billion (in 2003/04 prices). It is vitally important therefore, that Scottish Water continues to pay close attention to its operating costs and capital investment programme, not least so that it can respond when the supply of water and sewerage services to non-household customers is opened to competition from April 2008. The Auditor General will continue to monitor Scottish Water's performance in the years ahead and may consider a further report to Parliament in due course. The Commission is also expected to report on Scottish Water's performance for 2006/07 in the autumn.

Mental Health Tribunal for Scotland Administration (MHTSA)

110. The 2005/06 audit of MHTSA included a review of its governance and accountability framework. This review concluded in August 2006 that appropriate governance was not in place for MHTSA and it needed to be developed as a priority.

111. In August 2007, follow-up work on governance was completed as part of the 2006/07 audit. The overall conclusion was that although MHTSA had made progress in some areas, there remained a need to improve to meet good governance standards.



Appendix C: Auditor General for Scotland published reports

Accounts Commission and Auditor General for Scotland

Police Call Management (published 27/09/2007)

112. Scotland's police receive almost 16,000 calls a day and people are generally satisfied when they call 999 or a non-emergency number. The report indicates that forces recently reorganised how they manage calls but a lack of performance information means they cannot show whether the new systems are delivering the intended benefits or providing value for money.

Sustainable Waste Management (published 20/09/2007)

113. The report indicates that recycling rates have risen significantly, but further increases will be harder to achieve and will cost more. Because of slow progress in developing facilities to deal with waste that is not recycled it is unlikely that Scotland will be able to reduce landfill to the levels required by the EU. Urgent decisions now need to be made.

Managing long-term conditions (published 16/08/2007)

114. The NHS in Scotland can improve the care it gives to people with long-term illnesses by better targeting resources, further developing community-based services and driving a national strategy.

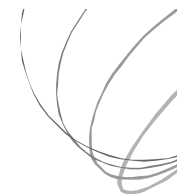
Auditor General for Scotland

Estate management in higher education (published 13/09/2007)

115. The report recommends that there should be a sustained commitment to maintaining and developing the estate, which is worth almost £5 billion.

Dealing with offending by young people: performance update (published 23/08/2007)

116. Increased funding and a stronger focus on youth justice services over recent years have delivered some positive changes. However, the report says that it is still not possible to demonstrate clearly that resources provide value for money and are being used effectively.



Primary care out-of-hours services (published 16/08/2007)

117. The report indicates that most patients are satisfied with NHS out-of-hours care. However fewer GPs are working during the out-of-hours period and there is a significant risk the service is unsustainable in its current form.

Edinburgh transport projects review (published 20/06/2007)

118. This report provides details on the Auditor General's review of the arrangements for managing the delivery of the Edinburgh trams and Edinburgh Airport Rail Link (EARL) projects.

Value For Money in public sector corporate services: A joint project by the UK Public Sector Audit Agencies (published May 2007)

119. Audit Scotland in conjunction with the other UK audit bodies launched indicators which will enable comparisons to be made between the performance of public bodies on corporate matters such as sickness absence and finance.

Planning ward nursing - legacy or design? A follow-up report (published 25/01/2007)

120. The report highlights that progress has been made towards improving the planning and management of ward nursing. Many of the recommendations in Audit Scotland's 2002 report on ward nursing are being addressed. The NHS now needs to build on progress made and ensure it has the information needed to manage the workforce well. The use of bank and agency nurses also needs to be kept under review.

The Efficient Government Initiative: a progress report (published 19/12/2006)

121. The report on the Efficient Government Initiative has found a commitment to improve efficiency, but says the Executive needs to do more to provide assurance on the levels of savings and their impact on service delivery.

Overview of the financial performance of the NHS in Scotland (published 14/12/2006)

122. This report looks at the financial performance of the NHS in Scotland in the 2005/06 and the outlook for the future. It finds that there are record levels of funding going into the health service and the NHS ended the 2005/06 year in surplus. However strong long-term planning is needed as the service faces financial pressures.



Catering for patients: a follow-up report (published 30/11/2006)

123. Hospital catering services are improving, with patients having more choice and the NHS getting better at responding to their preferences. However the report indicates that health boards need to focus more on making sure patients get the nutritional care they need. This report follows up on progress made since Audit Scotland last investigated hospital catering in 2003.

Managing IT to deliver information in the NHS in Scotland (published 23/11/2006)

124. The report indicates that the Scottish Executive must continue to improve the way it manages information technology to support care in the NHS in Scotland, however doing this involves a major cultural shift and will take time.

Performance management in the Scottish Qualifications Authority (published 9/11/2006)

125. The report highlights the progress made by the Scottish Qualifications Authority since 2000, when problems in processing exam results led to incomplete and inaccurate results for 17,000 candidates.



Appendix D: Future Studies Programme

Accounts Commission and Auditor General for Scotland

Studies	Indicative Publication Date
Improving Scotland's school estate	Autumn 2007
Free personal care	Winter 2007/08
Civil contingency planning	Summer 2008
Mental health services	Winter 2008
Strategic procurement	Spring 2009
Delivering an integrated transport system	Summer 2009
Follow-up Studies	
Community equipment and adaptations	Winter 2008
Road maintenance	2008
The Teachers' Agreement	2009
Community Planning	2009



Auditor General for Scotland

Studies	Indicative Publication Date
NHS performance and financial overview	December 2007
Palliative care	Winter 2007/08
How government works - major capital projects	Spring 2008
Prisoner population	Spring 2008
How government works – use of consultants	Spring 2008
General Medical Services contract	Spring 2008
Rail franchise monitoring	Summer 2008
Overview report 1	Summer 2008
Diagnostic services	Summer 2008
Promoting renewable energy	Autumn 2008
NHS asset management	Autumn 2008
NHS financial overview	December 2008
Overview report 2	Winter 2008/09
How government works (topic to be confirmed)	Spring 2009
Follow-up Studies	
Using medicines in hospital	Winter 2008

Further detail on the forward study programme can be found on our website at the following link:

<http://www.audit-scotland.gov.uk/audit/forwardwork.htm>

Scottish Executive

Report on the 2006/07 audit

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