

# Her Majesty's Inspectorate of Education

Report on the 2007/08 Audit

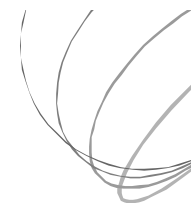


August 2008



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# Executive Summary

## Introduction

In 2007/08 we looked at the key strategic and financial risks being faced by Her Majesty's Inspectorate of Education (HMIE). We audited the financial statements and we also reviewed governance arrangements and aspects of performance management. This report sets out our key findings.

## Financial Position

HMIE received £14.3 million in funding from the Scottish Government during the year to 31 March 2008. HMIE also received income from fees and charges totalling £1.172m (2006/07: £1.212m) whilst income from other sources in 2007/08 was £0.140m (2006/07: £0.464m). Gross Administration costs for 2007/08 were £15.999m (2006/07: £15.162m), with the main element being staff costs of £11.153m (2006/07: £10.758m). Other administration costs for the year were £4.551m (2006/07: £4.076m); the most significant factor in the increase being this year's expenditure reflecting fuller costs for Reports and Inspections.

Scottish Ministers have agreed a resource budget for HMIE of £15.8 million for 2008/09.

## Financial Statements

We have given an unqualified opinion on the financial statements of HMIE for 2007/08. We have also concluded that, in all material respects, the expenditure and receipts shown in the financial statements were incurred or applied in accordance with applicable enactments and relevant guidance, issued by Scottish Ministers.

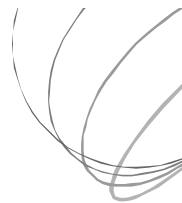
## Governance

Corporate Governance is concerned with the structures and process for decision making, accountability, control and behaviour at the upper levels of an organisation. Overall the corporate governance and control arrangements for HMIE operated satisfactorily during the year, as reflected in the Statement on Internal Control.

We examined the key financial systems which underpin HMIE's control environment. We concluded that financial systems and procedures operated sufficiently well to enable us to place reliance on them.

## Performance

As recorded in their annual report, HMIE achieved a high degree of success in meeting their targets. For example, quantitative targets for numbers of inspections carried out and reports published were either achieved or exceeded; and good progress or achievements were reported against qualitative targets.



## Best Value

As part of the 2006/07 audit we reviewed the outcome of HMIE's self assessment of its arrangements against the benchmark criteria for the 9 Best Value characteristics. Overall arrangements were assessed as well developed and we reported that this compared favourably with the results of baseline assessments for central government bodies (January 2007). In 2007/08 we followed up this work, noting that in relation to the "sustainable development" characteristic HMIE have made good progress on meeting their environmental targets. Also, relevant to a range of Best Value characteristics, in June 2008 HMIE were successful in the renewal of their Charter Mark status.

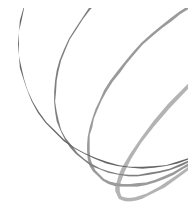
## Looking forward

The final part of our report notes some key risk areas for HMIE going forward, for example the impact of:

- **International Financial Reporting Standards (IFRS)** – and the need to manage the transition from existing arrangements to accounts prepared under IFRS.
- **Scotland Performs, the National Performance Framework and outcome agreements** – which will require the frequency of school inspections to increase.
- **The Scottish Government's response to Professor Lorne Crerar's review** - which could have a potentially significant effect on scrutiny bodies such as HMIE.
- **Future funding** – budgets for 2008/09 and the immediate future will need to be managed within a tighter funding regime.
- **Data handling** – monitoring the outcome of the review of data handling arrangements in Scotland and HMIE's response to the findings..

The assistance and co-operation given to us by Board members and staff during our audit is gratefully acknowledged.

**Audit Scotland**  
**August 2008**



# Introduction

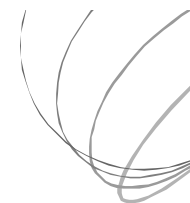
1. This report summarises the findings from our 2007/08 audit of Her Majesty's Inspectorate of Education (HMIE). The scope of the audit was set out in our Audit Plan, which was presented to the Audit Committee on 31 January 2008. The plan set out our views on the key business risks facing the organisation and described the work we planned to carry out on financial statements, governance and performance.
2. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officers and members of HMIE during the course of our audit. This report will be submitted to the Auditor General for Scotland and will be published on our website, [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

# Financial Position

3. In this section we summarise key outcomes from our audit of HMIE financial statements for 2007/08, and comment on the key financial management and accounting issues faced by the Agency. The financial statements are an essential means by which the Agency accounts for its stewardship of the resources available to it and its financial performance in the use of those resources.

## 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 HMIE and its expenditure and income for the period in question;
  - whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements;
  - the consistency of the information which comprises the Management Commentary with the financial statements, and
  - 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 HM Senior Chief Inspector as Accountable Officer to obtain assurances on systems of internal control, and



- assessing whether disclosures in the statement are consistent with our knowledge of HMIE.

## Overall conclusion

6. In relation to the above responsibilities we have given an unqualified opinion on the financial statements of HMIE for 2007/08.
7. As agreed the unaudited accounts were provided to us on 28 April, supported by a comprehensive working paper package. The good standard of the supporting papers and the timely responses from HMIE staff allowed us to conclude our audit within the agreed timetable and confirm our opinion to the Audit Committee on 30 May as timetabled.

## HMIE's Financial Position

### Outturn 2007/08

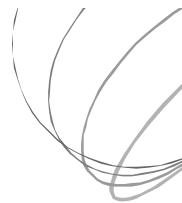
8. HMIE had net operating costs for 207/08 of 14.687 million (2006/07: 13.486 million). Payroll is the main expenditure item at £11.153 million (206/07: £10.758 million) and the movements within it are consistent with the staff movements. Other administration costs for the year were £4.551 million (2006/07: £4.076 million); the most significant factor in the increase being fuller costs associated with reports and inspections.
9. The net asset position decreased slightly to £0.614 million (2006/07: £0.875 million). There have been no significant movements in fixed assets, as expected.
10. Income from fees and charges during 2007/08 was £1.172 million (2006/07: £1.212 million), while income from other sources decreased to £0.140 million (2006/07: £0.464 million). Most of the income received under fees and charges is from the Service Level Agreement with the Scottish Funding Councils.
11. Overall HMIE operated within budget in 2007/08. HMIE were allocated a budget of £15.2 million for 2007/08, but returned £0.5 million of this during the year to allow it to be utilised for other projects. This related to work on developing the Inspection of Services for Children Development, which is expected to be completed in the near future and costs will increase accordingly in future years.

### 2008/09 Budget

12. The Scottish Ministers have set the budget for HMIE for 2008/09 at £15.8 million. No further increases are expected unless the Agency is requested to undertake further work on behalf of Ministers.

## Issues arising from the audit

13. As required by auditing standards we reported to the audit committee in May 2008 the main issues arising from our audit of the financial statements. Less significant matters are recorded in a letter to



management. We had no significant exceptions to report to the Committee and were pleased to note the improvement in key financial processes and controls, particularly the further development of reconciliations between the payroll and accounting systems. We also welcome HMIE's intention to further develop arrangements for budget monitoring and reporting in 2008/09.

## Regularity Assertion

14. 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.

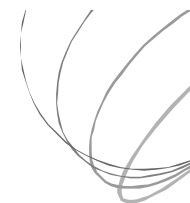
# Governance

## Overview of arrangements

15. This section sets out our main findings arising from our review of HMIE's governance arrangements. Our assessment of governance arrangements covers key systems of internal control and internal audit. 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. This year we also comment on strategic change at HMIE and aspects of information and communications technology (ICT). Our overall conclusion is that arrangements within HMIE are sound and have operated through 2007/08

## Strategic change

16. There are two key developments that HMIE are having to respond to:
  - The Concordat between the Scottish Government and the Convention of Scottish Local Authorities (COSLA), which is underpinned by an outcome agreement and a National Performance Framework. This will require the frequency of school inspections to increase.
  - The Scottish Government's response to Professor Lorne Crerar's report on the review of regulation, audit, inspection and complaints handling of public services in Scotland, which could have a potentially significant effect on scrutiny bodies such as HMIE.



17. HMIE are key participants in these processes and their management arrangements, such as the business planning tool and risk management, mean that they are well placed to establish new models of inspection and to assess any other implications as they emerge. For example, HMIE's school inspections are changing to build more directly on self evaluation and be more proportionate to ensure the Inspectorate can cope with the increased frequency of school inspections with the same resources and to allow reporting in line with Government priorities.

## **Systems of internal control**

18. Key controls within systems should operate effectively and efficiently to accurately record financial transactions and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In the annual report for 2007/08, the head of internal audit provided his opinion that, based on the internal audit work undertaken during the year, there was reasonable assurance on the adequacy and effectiveness on the systems of internal control.
19. As part of our audit we reviewed the high level controls in a number of HMIE's systems that impact on the financial statements. Our overall conclusion was that key controls were operating effectively. We note that HMIE uses the ICT network and main systems operated by the Scottish Government. These systems have been reviewed by our Scottish Government audit team. Whilst some areas for improvement have been identified, the review concluded that the main accounting system is operating satisfactorily.

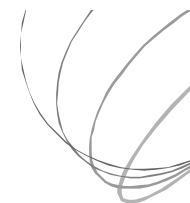
## **Prevention and detection of fraud and irregularities**

20. HMIE has appropriate arrangements in place to prevent and detect fraud, inappropriate conduct and corruption, including policies and codes of conduct for staff and Board members.

## **Internal Audit**

21. 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 2007/08 audit we assessed whether we could place reliance on HMIE's internal audit function. We concluded that the internal audit service, which is provided by the Scottish Government Internal Audit Division, operates in accordance with the Government Internal Audit Manual and therefore placed reliance on their work in number of areas during 2007/08, as we anticipated in our annual audit plan.





## **Audit and Risk Committee**

22. The Committee conducted a preliminary review of its existing arrangements in light of the updated draft guidance issued for consultation by the Scottish Government during the year. The Committee agreed that proposals should be brought forward to a future meeting to allow consideration of how arrangements may change in light of the new guidance.

## **Statement on Internal Control**

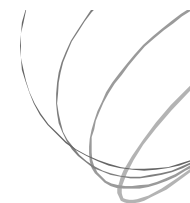
23. The Statement on Internal Control (SIC) included within HMIE's annual accounts summarises the Accountable Officer's responsibilities for maintaining a sound system of internal control and the measures put in place to achieve this. The internal control systems and governance arrangements have been reviewed by internal audit and found to be generally satisfactory. The findings from our audit work have not identified any matters that are inconsistent with the statements and conclusions recorded in the SIC.

## **Information and Communication Technology**

24. The Scottish Government carried out a review of data handling arrangements in Scotland, in response to failures in UK government bodies procedures and practices during 2007. The review considered current policies and procedures on data protection, consistency with government standards and local arrangements for implementation of procedures. HMIE participated in this exercise. An interim report published in April 2008 made some initial recommendations and a final report is expected soon.

# **Performance Management**

25. 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.
26. 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.

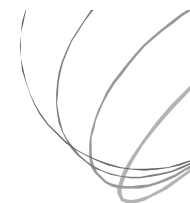


## Best Value developments

27. HMIE carried out a Best Value self assessment exercise in 2006/07, which was subject to audit review. Overall arrangements were assessed as well developed at the time, and we reported that this compared favourably with the results of baseline assessments for central government bodies (January 2007). Of the 9 Best Value characteristics, HMIE considered that their arrangements covering 7 were well developed, with only “equal opportunities” and “sustainable development” being under development.
28. HMIE’s strategic priority 4 is: “Securing our own continuous improvement.” Among other aspects and particularly relevant to sustainable development, the annual report records progress against environmental targets. All targets except that for paper usage were met and in some cases exceeded by a significant margin.
29. In June 2008 HMIE’s arrangements were independently reviewed as part of the renewal of their Charter Mark status. The resulting report of the assessment is very positive, confirming:
  - the Award of Charter Mark
  - that there were no areas of non-compliance
  - many areas of good practice – for example, “One could not report on HMIE without promoting in the strongest terms the excellent practice that has resulted in How Good Is Our School?” (the HMIE guidance on self evaluation / quality indicators).
30. Over the next year we will 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 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.

## Performance Management

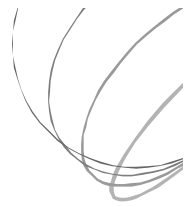
31. As recorded in their annual report, HMIE achieved a high degree of success in meeting their targets. For example, quantitative targets for numbers of inspections carried out and reports published were either achieved or exceeded; and good progress or achievements were reported against qualitative targets.



# Looking Forward

32. HMIE faces a number of challenges in 2008/09, some of which are recorded earlier in this report, but which we summarise at this point:

- **International Financial Reporting Standards (IFRS)** – As part of the UK Budget 2007 the Chancellor announced that the timetable for IFRS implementation was to be extended by a year with central government accounts in Scotland to become IFRS compliant with effect from the 2009/10 financial year. The Scottish Government have notified central government bodies that they will be required to produce shadow IFRS based accounts for the financial year in 2008/09, including a restated balance sheet as at 1 April 2008. A detailed timetable and list of requirements is awaited from the Scottish Government. This process may require significant resource to complete and it will be important that the restatement of the 1 April 2008 balance sheet is tackled early in 2008/09, together with creating a plan to manage the transition from existing arrangements to accounts prepared under IFRS.
- **Scotland Performs** – The Scottish Government is continuing to develop its approach to performance management based on a National Performance Framework and outcome agreements. The National Performance Framework is based on the outcome based 'Virginia-style' model of performance measurement and reporting. In support of this the Scottish Government has developed a new electronic tool and website to communicate to the public on Scotland's progress. This will include progress on overall delivery of the administration's purpose for Government, the five strategic objectives for Scotland and other aspects of the outcomes based National Performance Framework. In this context, earlier in the report we noted that the Concordat between the Scottish Government and the Convention of Scottish Local Authorities (COSLA) and outcome agreements will require the frequency of school inspections to increase. We will consider how HMIE is addressing this and other aspects of these developments as part of the 2008/09 audit.
- **Future funding** – Budgets for 2008/09 and the immediate future will need to be managed within a tighter funding regime. This includes significantly less scope for the application of end of year flexibility for the Government, with HM Treasury, until the next Spending Review; no option to transfer funds from capital to revenue; and the potential impact of the introduction of International Financial Reporting Standards (IFRS), particularly on PFI, leases and infrastructure accounting (although this latter aspect should not have a significant direct impact on HMIE). The challenge for HMIE, together with Scottish Government colleagues, is to manage this tighter funding regime against the background of changing the inspection process



and finalising/ implementing the arrangements for the Inspection of Services for Children Development. In this regard HMIE's intention to further develop arrangements for budget monitoring and reporting in 2008/09 is timely.

- **Data handling** – The Scottish Government carried out a review of data handling arrangements in Scotland, in response to failures in UK government bodies procedures and practices during 2007. The review considered current policies and procedures on data protection, consistency with government standards and local arrangements for implementation of procedures. An interim report published in April 2008 made some initial recommendations and a final report is expected soon. We will monitor HMIE's response to the review and action taken as part of our 2008/09 audit.