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INFRASTRUCTURE, GOVERNMENT AND HEALTHCARE

VisitScotland

Annual audit report to VisitScotland and the Auditor General for Scotland 2007-08

21 October 2008

AUDIT

AUDIT ▪ TAX ▪ ADVISORY

Contents

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Executive summary

This report summarises our work for 2007-08 and our findings in relation to our audit of the financial statements, corporate governance and performance management arrangements.

Management arrangements

From our audit perspective, management of the organisational change process established project management arrangements, including risk management and communication.

110 members of staff applied for voluntary severance and 79 staff were successful. The cost was £3.5 million, which is in line with the original forecast of £3.4 million.

VisitScotland's obligation in respect of lease dilapidations and early exit costs resulting from management's decision to terminate leases totals £1.3 million.

VisitScotland spent £5.3 million on the restructuring exercise, 6% more than the ring-fenced funding of £5 million allocated by the Scottish Government.

VisitScotland's share of eTourism Limited's losses and provision for non-recovery of the loan and associated interest due from eTourism Limited increased net operating costs by £3.2 million. Management has initiated discussions with eTourism Limited to secure its long-term sustainability.

VisitScotland did not meet its financial target, set by the Scottish Government, and reported a deficit of £2.6 million due to the impact of provisions for non-recovery of amounts due from eTourism Limited.

Corporate governance

Corporate governance arrangements have been designed and implemented appropriately.

The statement on internal control highlights areas for improvement in the system of internal control highlighted by internal audit and that VisitScotland is not yet fully compliant with statutory public sector equality duties.

Internal audit completed their plan during the year and issued their annual report of 16 September 2008. This report concludes that "*the organisation generally has an adequate framework of control over the systems we examined … subject to implementation of the recommendations*".

Internal audit reported a recommendation in respect of ensuring compliance with the procurement policy and consistency of documentation relating to tenders below the EU threshold. Subsequent testing confirmed that management addressed this weakness in early 2008.

Audit of the financial statements

We have issued unqualified opinions on the financial statements.

The financial statements reflect potential non-recovery of a proportion of outstanding claims for European funding.

Performance management

VisitScotland achieved or exceeded 10 out of 18 key performance indicators, but the annual performance report needs to be more consistent in its consideration of performance against targets and identify specific future actions.

An internal review reported that VisitScotland is 'well developed' in eight of the nine areas of Best Value. Equal opportunities is the remaining area for development of processes to achieve and demonstrate Best Value and this is reflected in management's action plan.

VisitScotland exceeded its target of £1 million and reported cash releasing efficiency savings of £1.8 million.

Introduction

Audit framework

This year was the second of our five-year appointment by the Auditor General for Scotland as external auditors of VisitScotland. This report to VisitScotland and the Auditor General provides our opinion and conclusions and highlights significant issues arising from our work.

In accordance with Audit Scotland's Code of Audit Practice ("the Code") the scope of the audit was to:

- provide an opinion on VisitScotland's financial statements and the regularity of its transactions;
- review and report on:
  - corporate governance arrangements as they relate to: review of systems of internal control; the prevention and detection of fraud and irregularity; standards of conduct, and prevention and detection of corruption; and VisitScotland's financial position
  - VisitScotland's arrangements to achieve Best Value
  - other aspects of arrangements to manage performance, as they relate to economy, efficiency and effectiveness in the use of resources.

We outlined the framework under which we operate, under appointment by Audit Scotland, in the audit plan for the year discussed with VisitScotland's audit committee.

Overview

The Tourist Boards (Scotland) Act 2006 received Royal Asset in November 2006 and required the following:

- the Scottish Tourist Board to be renamed VisitScotland;
- dissolution of Scottish Network 1 and 2 Tourist Boards on 1 April 2007; and
- transfer of assets, liabilities and staff to VisitScotland at that date.

From 1 April 2007, EventScotland ceased to be a joint venture between the former Scottish Executive and VisitScotland, is now a fully integrated directorate of VisitScotland.

On 26 September 2007 the Cabinet Secretary for Finance and Sustainable Growth announced the government's economic strategy for Scotland. There is to be a focus on better and closer working with the agencies that have responsibility for the Scottish economy. A strategic forum has been created that includes ministers, together with the chair and chief executives from VisitScotland, Scottish Enterprise, and Highlands and Islands Enterprise to promote integration and collaboration.

VisitScotland's core purpose remains to maximise the economic impact of tourism to Scotland through the core activities of marketing, information and inspiration, and quality assurance. To ensure that VisitScotland is making the best possible contribution to the Scottish Government's 50% growth ambition and is meeting the needs of its customer groups, it introduced a number of changes to improve the customer focus of the organisation. The organisation restructured along the regional areas adopted by the enterprise organisations and realigned teams to customer-focused directorates. The new 'customer first' structure has four directorates, reflecting the customer groups: visitor engagement; business engagement; strategic partners; and corporate services supporting internal customers.

Responsibilities of VisitScotland and its auditors

External auditors do not act as a substitute for VisitScotland's own responsibilities, through its accountable officer, for putting in place proper arrangements to account for its stewardship of resources made available to it and its financial performance in the use of those resources, to ensure the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the effectiveness of those arrangements and, through accountable officers, to make arrangements to secure Best Value.

We have structured the report around the headings management arrangements, governance arrangements, audit of the financial statements and efficient government and Best Value arrangements.

Acknowledgement

We wish to record our appreciation of the continued co-operation and assistance extended to us by your staff.

Management arrangements

- From our audit perspective, management of the organisational change process established project management arrangements, including risk management and communication.
- 110 members of staff applied for voluntary severance and 79 staff were successful. The cost was £3.5 million, which is in line with the original forecast of £3.4 million.
- VisitScotland's obligation in respect of lease dilapidations and early exit costs resulting from management's decision to terminate leases totals £1.3 million.
- VisitScotland spent £5.3 million on the restructuring exercise, 6% more than the ring-fenced funding of £5 million allocated by the Scottish Government.
- VisitScotland's share of eTourism Limited's losses and provision for non-recovery of the loan and associated interest due from eTourism Limited increased net operating costs by £3.2 million. Management has initiated discussions with eTourism Limited to secure its long-term sustainability.
- VisitScotland did not meet its financial target, set by the Scottish Government, and reported a deficit of £2.6 million due to the impact of provisions for non-recovery of amounts due from eTourism Limited.

Customer first

On 26 September 2007 the announced the government's economic strategy for Scotland. In response to the Cabinet Secretary for Finance and Sustainable Growth's announcement in September 2007, VisitScotland decided to organise its activities around six regions, aligned to Highland and Islands Enterprise and Scottish Enterprise regions, and three island areas. This simplified structure was operational from 1 April 2008.

The restructuring process commenced in 2007-08 when VisitScotland introduced a number of changes to improve the customer focus of the organisation through a restructuring process referred to as 'customer first'. The new structure's four directorates reflect VisitScotland's customer groups:

- visitor engagement – the customer journey from deciding on Scotland as a destination, through booking and travelling, to getting the best out of their experience and keeping in touch after they have gone;
- business engagement – helping businesses join up with customers by providing routes to markets and giving quality advice, consultancy and assessments;
- strategic partners – communications and strategic engagement with stakeholders; and
- corporate services – designed to support internal customers.

'Customer first' included a review of the staffing structure to assess whether it remained suitable for VisitScotland's new responsibilities and the requirement for closer working with other organisations and the need to reduce costs through shared service initiatives prompted a strategic review of the property portfolio.

Project team

The senior management team acted as the steering group and was responsible for timely approval of decisions and actions. The chief executive was project sponsor and responsible and accountable for ensuring the project delivered against its objectives. Allocation of specific tasks to responsible individuals ensured that there was accountability for delivery of project goals.

Risk management

In line with good practice, the project risk register included a description of risks, likelihood and impact scores, total risk rating, preventative action, mitigation or resolution, owner, updates and percentage complete. Assignation of risk owners ensured that there was clarity over responsibilities and a mechanism to hold officers accountable for the project.

Communication

The main communication method deployed was via a specific page on VisitScotland's intranet dealing with the customer first project. This operated in conjunction with a cascade process, whereby the senior management team agreed communications and cascaded these to staff through heads of department. VisitScotland's strategy, partnerships and communications division managed external communications through liaison with the press and via the VisitScotland corporate website.

Human resources

110 members of staff applied for voluntary severance and, during 2007-08 and the early months of 2008-09, 79 staff left through the voluntary severance scheme, including two directors.

Management followed a robust system for assessing applications to the scheme and for calculating the cost of the scheme to the organisation, but the process for retaining evidence to demonstrate the timing of decisions should be improved. The cost of the voluntary severance scheme is £3.5 million, which is in line with the original forecast of £3.4 million. The majority of payments to staff were processed in April 2008 and management correctly recognised these costs as an accrual in the 2007-08 financial statements.

The 2007-08 draft financial statements included accruals of £120,000 relating to goods and services received in 2008-09, primarily relating to 'customer first' training courses for staff in the summer of 2009. These transactions do not meet the requirements of accounting standards and, as a result of the audit process, management adjusted the financial statements and reduced expenditure by £120,000.

Property portfolio

Senior management identified a number of criteria to prioritise property leases under review and implemented a weighted scoring system to be assess criteria on a consistent and formal basis.

The initial review identified 13 properties for consideration. During March 2008 the customer first project team completed these reviews and engaged third party property advisors to calculate the cost of any refurbishment – lease dilapidations - required by individual leases at the time of termination. The financial statements include accruals of £1.3 million to reflect VisitScotland's obligation in respect of lease dilapidations and early exit costs resulting from management's decision to terminate leases.

Finance

The Scottish Government provided an additional £5 million of non-recurrent grant-in-aid funding to assist VisitScotland with meeting the costs of restructuring. Spend against this allocation is shown below.

	£'000
Property costs	1,351
Voluntary severance	3,488
Consultancy	224
Staff training and development	105
Research, legal and other costs	134
	5,302
Non-recurring grant-in-aid funding	5,000
Surplus / (deficit) against restructuring ring-fenced funding	**(302)**

Source: VisitScotland (September 2008)

Summary

From our audit perspective, management of the organisational change process established appropriate project management arrangements, including risk management and communication.

visitscotland.com

VisitScotland's wholly owned subsidiary, TourCo Limited, owns 36% of the share capital of eTourism Limited. The 'visitscotland.com' website is operated by eTourism Limited and provides information and booking services to tourists.

VisitScotland previously loaned £1.875 million to TourCo Limited, which in turn provided a loan of £1.85 million to eTourism Limited. The loan is repayable by eTourism Limited and is dependant on the profitability of eTourism Limited, which has been and is loss making. The earliest date repayment of the loan was due to commence was 2008, but the current financial position, including net liabilities of £6.2 million, means that repayments will not commence until later.

A new strategic partnership agreement between shareholders of eTourism Limited in September 2006 aligned shareholdings in eTourism Limited and aimed to secure a range of benefits, including improving the technology platform for the website, and the financial stability of e-Tourism Limited. However, eTourism Limited continues to report annual losses of £1.4 million (prior year: £3.1 million).

TourCo Limited took the decision, based on consideration of eTourism Limited's financial statements and forward business plan, to provide in full against recovery of its loan in its 2007-08 financial statements. In addition, the financial statements include a provision of £0.9 million against loan interest due to VisitScotland. These provisions are subsequently reflected in full in the VisitScotland group financial statements.

The operating cost statement also includes the VisitScotland group's share of eTourism Limited's losses of £454,000 (2006-07: £1,034,000). During 2007-08 VisitScotland management and the board have maintained close contact with the board of eTourism Limited and initiated discussions to secure its long-term sustainability.

2007-08 financial outturn

An analysis of the 2007-08 financial performance is summarised below.

	Expenditure £'000	Funding £'000	Outturn £'000
Core grant-in-aid (including capital)	43,379	43,351	(28)
Customer first	5,302	5,000	(302)
Non-cash	1,037	1,580	543
Total before provision for non-recovery of intra-group loans	49,718	49,931	213
Provision for non-recovery of intra-group loans	2,787	-	(2,787)
Overall outturn for the year	**52,505**	**49,931**	**(2,574)**
Scottish Government targets			
Cash	51,468	48,351	(3,117)
Non-cash	1,037	1,580	543
Overall outturn for the year	**52,505**	**49,931**	**(2,574)**

Source: VisitScotland

VisitScotland did not meet its cash target and the surplus against the non-cash target was insufficient to cover the cash shortfall. Consequently, VisitScotland did not meet its overall financial target, set by the Scottish Government, and is reporting a deficit of £2.6 million. The reasons for the 'cash' overspend are a provision for non-recovery of intra-group loans of £2.8 million and £0.5 million from the VisitScotland group's share of eTourism Limited's operating loss.

After consultation with the board, Scottish Government and external auditors, management's decision to provide for non-recovery of the loan and interest due from eTourism Limited during the year increased total planned expenditure by £2.8 million.

Group reserves increased during the year by £1.5 million (2006-07 decrease of £4.7 million), primarily due to the excess of expenditure over income being offset by a £5 million decrease in pension liabilities. The table below shows the movements in reserves.

	2007-08 £'000	*2006-07 £'000*
Group reserves at 1 April	**4,414**	*9,133*
Net expenditure	(51,819)	*(45,951)*
Scottish Executive funding	48,351	*45,226*
Net impact of restructuring the group's shareholding in eTourism	-	*1,124*
Actuarial movement on pension liabilities	5,172	*(5,435)*
Net movement on the government grant reserve	(160)	*(112)*
Net movement on the revaluation reserve	(6)	*429*
Group reserves at 31 March	**5,952**	*4,414*

Source: VisitScotland

The actuarial movement on pension liabilities is outwith VisitScotland's control, but it has a significant impact on the reserves reported in the financial statements. The net movement on reserves, before the impact of the actuarial movement is a decrease of £3.6 million (2007: increase of £0.7 million) attributed to factors outlined in the table above.

2008-09 financial plan

The financial plan reports a balanced outturn for the year ended 31 March 2009. Management are currently performing a detailed mid-year review and reforecast to revise assumptions underpinning the financial plan, including the impact of decreasing:

- local authority income;
- visitor numbers in tourist information centres, but partially offset by a small increase in average customer spend; and
- other operating income.

Following completion of the income reforecast management will revise expenditure plans to ensure that the financial plan continues to forecast a breakeven position.

Corporate governance

- The corporate governance arrangements have been designed and implemented appropriately.
- The statement on internal control highlights areas for improvement in the system of internal control highlighted by internal audit and that VisitScotland is not yet fully compliant with statutory public sector equality duties.
- Internal audit completed their plan during the year and issued their annual report of 16 September 2008. This report concludes that "*the organisation generally has an adequate framework of control over the systems we examined … subject to implementation of the recommendations*".
- Internal audit reported a recommendation in respect of ensuring compliance with the procurement policy and consistency of documentation relating to tenders below the EU threshold. Subsequent testing confirmed that management addressed this weakness in early 2008.

Introduction

Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all bodies.

Through its chief executive, VisitScotland is responsible for establishing arrangements for ensuring the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. The Code requires auditors to review and report on corporate governance arrangements as they relate to:

- reviews of systems of internal control, including reporting arrangements;
- the prevention and detection of fraud and irregularity;
- standards of conduct and arrangements for the prevention and detection of corruption; and
- financial position.

Management is responsible for establishing arrangements for the conduct of its affairs, including compliance with applicable guidance, ensuring legality of activities and transactions and monitoring the adequacy and effectiveness of these arrangements in practice.

Corporate governance framework

The board consists of the chairman, five non-executive directors, the chief executive and four executive directors. The board delegates powers to three sub-committees: audit, remuneration and EventScotland, each of which have formal terms of reference. The terms of reference meet expectations and detail committee membership, procedures for meetings, reporting, responsibilities, and information requirements.

VisitScotland's directors are responsible for preparation of board and committee papers in advance of each meeting. We consider the contents of board and committee papers, particularly in relation to financial reporting, but also customer first and restructuring, operational performance, pay awards and remuneration, and other areas where decisions may impact the financial statements. A number of papers, particularly those relating to financial performance, are 'high level' and provide summary information. The content of papers should be revised to provide detailed analysis and consideration of risks to the organisation (financial and operational) and the impact on future plans.

Minutes of board and committee meetings should record the discussion and decision-making process as well as the final decision. The minutes of board and audit and remuneration committee meetings during 2007-08 did not, on a number of occasions, provide sufficient detail to allow the reader to understand fully discussions and decisions.

Non-executive directors completed a board survey in the summer of 2008 and the chairman reported the results to the board in July 2008. These results include the need for board papers to provide more clarity on the level of engagement expected of board members and increased discussion on strategy rather than operational issues.

Recommendation 1

The number of executive directors decreased from six to four during the year during the restructuring exercise. The senior management team, consisting of executive directors, head of human resources and EventScotland chief operating officer, supports the board at an operational level.

The Ethical Standards in Public Life etc. (Scotland) Act 2000 requires VisitScotland to implement a code of conduct for board members, outlining their responsibilities. In line with the model code, the VisitScotland code contains rules of conduct on:

- general conduct;
- confidentiality requirements;
- registering and declaring interests;
- declaration of gifts and hospitality;
- use of public body facilities;
- appointment to partner organisations; and
- lobbying and access to members of public bodies.

We have considered the corporate governance arrangements and, combined with the work of internal audit, concluded that the corporate governance framework is appropriate and fully documented.

Statement on internal control ("SIC")

The SIC for 2007-08 provides details of the internal control environment and risk management and control framework. Management highlight that the system of internal control is based on an ongoing process designed to identify the principal risks to the achievement of the organisation's policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically.

The chief executive submitted a certificate of assurance to the deputy director of whisky legislation and tourism division at the Scottish Government in April 2008. Completion of an internal checklist supports the assurances provided to the Scottish Government on the following areas business planning, major investment, project management, finance, procurement, human resources, equality, information technology, health and safety, risk management, and regulatory compliance.

The SIC notes that recent internal audit reviews have highlighted some areas for improvement in the system of internal control, including cash and credit card controls in tourist information centres, and that these are being addressed. In addition, a number of prior year internal audit recommendations relating to equality and environmental compliance, payroll and human resources reconciliations, validation of ticket sales, and documentation of payroll procedures remain outstanding. The SIC also highlights that VisitScotland is not yet fully compliant with statutory public sector equality duties, particularly in relation to assessment of the impact of key policies and activities. Management developed an action plan to ensure compliance with these requirements in the future. The content of the SIC is consistent with our understanding.

Risk management

VisitScotland’s risk management policy includes standard sections such as the requirement for formal documentation of a risk management strategy and approach, the roles and responsibilities of key parties (including the chairman, chief executive, board members, audit committee, internal audit and the head of finance), the key aspects of the system of internal control and risk management, and reporting procedures. The policy was last updated in August 2007 and is available to all staff on the intranet.

The policy requires that management perform a formal annual review of risks and report the results to the board. During the year, management report new, amended and deleted risks to the board. The risk register documents the nature of risks, including likelihood and impact, mitigating action plans, responsible officer and the implementation date. In line with good practice, a number of local risk registers, including information technology, EventScotland and the ‘customer first’ project, support the corporate risk register at an operational level.

Internal audit

Our planned audit approach seeks, wherever possible, to place reliance on the work completed by internal audit to minimise duplication of effort and ensure maximum benefit from the combined audit resource. To support this, in accordance with International Standard on Auditing 610, we have again formally considered VisitScotland’s internal audit arrangements. Our evaluation incorporates consideration of both the organisational and operational aspects of the function, including the scope of work, the independence of the function, arrangements to secure due professional care and quality of work performed and reporting mechanisms.

We performed detailed file reviews in areas where we formally placed reliance on the work of internal audit. This confirmed that we could again place reliance on internal audit’s work. We placed reliance on the work performed on tendering and procurement processes and took into account the findings from other work completed by internal audit to inform our approach to the audit, including business continuity, financial fraud risk management and the IT data centre.

Internal audit completed their plan during the year and issued their annual report of 16 September 2008. This report concludes that “*the organisation generally has an adequate framework of control over the systems we examined … subject to implementation of the recommendations*”.

Internal controls

Drawing on the work of internal audit, we carried out detailed testing in relation to both organisation-wide and key financial controls. Our work in this area included consideration of the principal accounting systems to assess whether the related controls were designed appropriately and operating effectively to prevent or detect a material misstatement of the financial statements and review of the IT control environment. The organisation is in the process of improving business continuity and disaster recovery arrangements and information security.

We concluded that, overall, the design and implementation of organisation-wide and IT general controls was effective, and that key financial controls, with the exception of some minor observations relating to journal entries, fixed assets, the provision for doubtful debts and supplier statement reconciliations, were operating effectively. We made some recommendations to enhance the efficiency and effectiveness of the control framework.

Prevention and detection of fraud and irregularity

Fraud policy

The fraud response plan sets out what to do on suspicion of fraud or other irregularities. The plan details the role of the fraud response coordinator, membership of the fraud response group, processes to be followed during investigations, and reporting mechanisms.

A whistle-blowing policy supports the fraud response plan and documents the process for staff raising concerns relating to unlawful conduct, financial malpractice or dangers to the public or to the environment. The audit and compliance manager reports significant frauds to the audit committee. There were no material instances of fraud reported during 2007-08.

Regularity

In accordance with our responsibilities within *the Code*, we provide an opinion on VisitScotland's financial statements and, as required by relevant authorities, the regularity of transactions.

In order to gain assurance over the regularity of expenditure we have updated our understanding over the processes in place to receive Scottish Government circulars, register, allocate and distribute responsibility for action points and monitor and follow up these action points.

To ensure completeness, management should ensure that all circulars are recorded in a spreadsheet based register to allow it to be sorted by reference. The circulars register should be regularly reviewed with reminders to responsible officers of the need to respond to action points in a timely manner. Responsible officers should be reminded of the importance of evidencing the timely actioning of the circulars by signing and dating the responses. We reported similar weaknesses in policies and procedures and regularity in 2006-07 and recommendations were accepted by management. Implementation dates of 31 December 2007 and 30 September 2007 were respectively agreed with management, but progress was still required to complete these actions. Earlier this year management agreed an implementation date of 31 December 2008 to fully implement these actions.

Procurement

Internal audit reported a recommendation in respect of ensuring compliance with the procurement policy and consistency of documentation relating to tenders below the EU threshold. We relied on the work completed by internal audit in the period to October 2007 and carried out additional testing over subsequent contracts. We did not identify any errors and satisfactory tendering arrangements were in place for all contracts with a value over the EU threshold, including appropriate advertising in the Official Journal of the European Union, sufficiently clear pre-qualification questionnaires and tendering documents and a clear process with regard to the final decision.

For projects under the EU tendering threshold, internal audit reported that there was not a structured process in place to ensure that documentation was in place to support compliance with VisitScotland policy. In order to improve this process, VisitScotland plans to use standardised documentation for all contracts under the EU tendering threshold, which should ensure compliance with the policy in all cases.

State aid

State aid refers to forms of assistance from a public body given to an undertaking on a discretionary basis, with the potential to distort competition and affect trade between member states of the European Union.

Internal audit undertook a review of state aid restrictions during 2006-07 in order to assess the effectiveness of VisitScotland's controls to monitor compliance with state aid rules. One control weakness rated as "high" by internal audit relating to the absence of a formal, documented policy and procedure in place with respect to VisitScotland's approach to state aid. To address the risk that inappropriate payments are made, which could have potential state aid implications resulting in penalties for recipient firms and the UK government, management introduced a state aid policy. The audit committee ratified this policy in January 2008.

From November 2007, additional wording was inserted to the standard EventScotland contract providing for an event of default if "*the award is determined to be illegal by any court or regulatory authority*". Contracts issued by VisitScotland in the last quarter of 2007-08 used the revised standard contract.

VisitScotland continues to respond to requests for information from the European Commission in relation to a claim lodged with the European Commission in 2006 in relation to payments made to a UK limited company, which may have State Aid implications.

Audit of the financial statements

- We have issued unqualified opinions on the financial statements.
- The financial statements reflect potential non-recovery of a proportion of outstanding claims for European funding.

Reporting arrangements and timetable

Management provided draft group financial statements on 4 August 2008 and narrative statements, including the management commentary and remuneration report, on 19 August 2008. We have separately reported to management a number of performance improvement recommendations in relation to the financial statements preparation process.

Audit opinion

Following approval in October 2008 we issued an audit report expressing an unqualified opinion on the financial statements for the year ended 31 March 2008 and on the regularity of transactions reflected in those financial statements.

We bring the following issue to your attention.

European Union funding

VisitScotland has claimed £9 million of funding from the European regional development fund during the period 2002 to 2008 and submitted claims for the final £0.5 million in July 2008. Management has identified a risk that the audit trail for interim and final claims may not be complete and has commenced an internal review of all supporting documentation during 2008-09. The 2007-08 financial statements prudently reflect the potential risk of non-recovery of a proportion of outstanding claims. Management should implement a formal monitoring process during 2008-09 to monitor the likelihood of non-recovery or repayment in line with the requirements of accounting standards.

Recommendation 2

Performance management

- VisitScotland achieved or exceeded 10 out of 18 key performance indicators, but the annual performance report needs to be more consistent in its consideration of performance against targets and identify specific future actions.
- An internal review reported that VisitScotland is 'well developed' in eight of the nine areas of Best Value. Equal opportunities is the remaining area for development of processes to achieve and demonstrate Best Value and this is reflected in management's action plan.
- VisitScotland exceeded its target of £1 million and reported cash releasing efficiency savings of £1.8 million.

Key performance indicators

The corporate plan details VisitScotland's key performance indicators. As part of the 2007-08 corporate planning process management agreed to reduce the number of corporate key performance indicators to 18. Members of the senior management team 'own' individual objectives to ensure accountability and responsibility for performance. The board received a six-month progress report and a year-end progress report on the outturn against these targets. Management reported to the board in May 2008 that 10 out of 18 targets were achieved or exceeded:

- Give strategic direction to the industry – the two key performance indicators achieved scores of 45% and 44% against targets of 55% and 65% respectively.
- Attract visitors by building a successful Scottish tourism – four of the five targets were achieved, with 'increasing visitor propensity to visit Scotland' an area for development in 2008-09.
- Engage and work in partnership with the tourism industry and other stakeholders – 'industry income from business customers' exceeded the target, but 'partner sector leverage in marketing challenge funding' and 'local authority funding received' fell short of expectations.
- Enhance the visitor experience through the provision of quality assurance to visitors and quality advice to industry – the proportion of business in the quality assurance scheme increased by 83% against a target of 85% and the target increase of 10% in membership of the green tourism business scheme was achieved.
- Enhance the visitor experience through the provision of information – the tourist information centres did not meet two return on investment targets, but retail spend per visitor increased by 17.8% and the use of new channels to service enquiries exceeded budget by 37%.
- Manage our business efficiently and effectively – efficiency savings and financial reporting targets were achieved.

The board report summarising performance for the year does not fully document the reasons behind achievement or non-achievement of targets. Formal documentation and reporting of the reasons behind non-achievement of targets would provide management with information on which to make decisions on future action. The annual performance report clearly links named directors to individual performance, but, in some cases, does not identify specific actions to be performed in 2008-09. To allow the board to hold directors to account for specific actions, these should be formally documented in the performance reports.

Management should fully document analysis and consideration of performance against targets, including identifying specific future actions, in a similar way to the six-month progress report.

Recommendation 3

The board is considering use of the single outcome agreement in future years as the basis for measuring organisational performance and is discussing a potential set of indicators with the Scottish Government, Scottish Enterprise and Highlands and Islands Enterprise.

Best Value

During 2005-06 Audit Scotland undertook a baseline assessment of VisitScotland's position in relation to Best Value. Six out of the nine areas were found to be 'under development' to secure Best Value, with the remaining three areas regarded as 'well developed' (commitment and leadership, accountability and joint working).

The audit and compliance manager led a review of arrangements to embed Best Value in the organisation based upon the self-assessment questionnaire issued by the Scottish Government for use by public sector organisations. This review, which concluded in August 2008, found that VisitScotland is 'well developed' in eight of the nine areas and 'under development' in equal opportunities. Management identified actions to progress developments in respect of equal opportunities, including appointment of a diversity manager, introduction of an equality annual report and more visible inclusion in the corporate reporting process.

2008-09 onwards

Audit Scotland has been committed to extending the Best Value audit regime across the whole public sector for some time now, with significant amounts of development work having taken place during the last year. Using the Scottish Government's nine best value principles as the basis for audit activity, Audit Scotland has selected five areas as priority development areas (use of resources, governance and risk management, accountability, review and option appraisal, and joint working). Audit Scotland is currently developing a series of toolkits that auditors will be required to use from 2008-09. Completion of these toolkits will require a detailed examination of arrangements in specific areas. The focus of this work in 2008-09 will be on the use of resources, including efficiency, information management, procurement, asset management, performance management and people management. It is anticipated that national reports may be prepared by Audit Scotland.

Efficient government

The efficient government plan was published in November 2004 and outlines the Scottish Government's strategy for improving the efficiency of the Scottish public sector. It contains measures to deliver at least £745 million of annually recurring cash-releasing efficiency gains and at least £300 million of recurring time-releasing efficiency gains.

VisitScotland reported cash releasing efficiency savings of £1.8 million during the year. This comprises £1 million of recurring savings from the full year effect of savings implemented in 2006-07 and an additional £0.8 million of new savings from improved procurement opportunities, and co-location and rationalisation of activities across the network.

The Scottish Government has set a combined target of £16 million of efficiency savings in 2008-09 from VisitScotland, Scottish Enterprise, and Highlands and Islands Enterprise.

Appendix – action plan

Priority rating for performance improvement observations raised		
Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of VisitScotland or systems under consideration. The weakness may therefore give rise to loss or error.	**Grade two** (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items that may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.	**Grade three** (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations that would assist us as auditors. The weakness does not appear to affect the availability of the controls to meet their objectives in any significant way. These are less significant observations than grades one and two, but we still consider they merit attention.

No.	Issue and performance improvement observation	Management response	Officer and due date
1	Non-executive directors completed a board survey in the summer of 2008 and the chairman reported the results to the board in July 2008. These results include the need for board papers to provide more clarity on the level of engagement expected of board members and increased discussion on strategy rather than operational issues. *(Grade two)*	Management will endeavour to provide greater clarity in papers presented to the board and its committees.	Director of corporate services Ongoing
2	The 2007-08 financial statements prudently reflect the potential risk of non-recovery of a proportion of outstanding European funding claims. Management should implement a formal monitoring process during 2008-09 to monitor the likelihood of non-recovery or repayment in line with the requirements of accounting standards. *(Grade two)*	Management highlighted this issues and plans to undertake a data verification programme to support the ERDF claims.	Head of finance 31 March 2009

No.	Issue and performance improvement observation	Management response	Officer and due date
3	The board report summarising performance for the year does not fully document the reasons behind achievement or non-achievement of targets and, in some cases, does not identify specific actions to be performed in 2008-09. Management should fully document analysis and consideration of performance against targets, including identifying specific future actions, in a similar way to the six-month progress report. *(Grade two)*	The content of the papers will be written in a more consistent manner, incorporating greater detail to allow informed discussion and review.	Director of strategic partnerships 31 March 2009

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