



cutting through complexity™

Scottish Legal Aid Board

Annual audit report to Scottish Legal Aid Board
and the Auditor General for Scotland

Year ended 31 March 2011

27 July 2011



Contents

The contacts at KPMG in connection with this report are:

Grant Macrae

Director, KPMG LLP

Tel: 0131 527 6611

Fax: 0131 527 6666

grant.macrae@kpmg.co.uk

Michael Wilkie

Manager, KPMG LLP

Tel: 0141 300 5890

Fax: 0141 204 1594

michael.wilkie@kpmg.co.uk

Jon Tyler

Assistant manager, KPMG LLP

Tel: 0131 527 6790

Fax: 0131 527 6666

jonathan.tyler@kpmg.co.uk

	Page
Executive summary	2
Priorities and risks	4
Financial statements	6
Use of resources	7
Governance	10

About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the Code").

This report is for the benefit of the Scottish Legal Aid Board and is made available to Audit Scotland (together "the beneficiaries"), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes, but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scope and objectives section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the beneficiaries) for any purpose or in any context. Any party other than the beneficiaries that obtains access to this report or a copy and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the beneficiaries.

This report summarises our work for 2010-11 and our findings in relation to our audit of the financial statements, corporate governance and performance management arrangements.

Financial statements

Following chief executive approval in July 2011, we issued an audit report expressing an unqualified opinion on the financial statements for the year ended 31 March 2011 and on the regularity of transactions reflected in those statements.

The financial statements of the Fund report net operating costs of £170.565 million (2009-10: £147.601 million) and net liabilities as at 31 March 2011 of £68.134 million (2009-10: £59.135 million).

Grant-in-Aid reports net operating costs of £15.548 million on an accruals basis (2009-10: £14.999 million) and net liabilities of £40.660 million as at 31 March 2011 (2009-10: £44.545 million).

No numerical audit adjustments were made to the financial statements.

The 2010-11 reportable spend for Grant-in-Aid on a cash basis, including capital and revenue, shows a net underspend of £0.220 million against a budget of £13.390 million. This has been achieved through an underspend on staff costs of £0.112 million and an underspend on capital costs of £0.063 million. The Fund, which is not cash limited, on a cash basis reports actual spend of £161.4 million against an anticipated net expenditure of £160.0 million.

Total provisions in the Fund as at 31 March 2011 are £75.580 million (2010 : £64.796 million). The main reason for the movement is the increase in VAT in year and increases to solicitor fees notably in relation to civil legal aid and criminal solemn legal aid.

Net liabilities at 31 March 2011 for Grant-in-Aid are £40.660 million (2010: £44.545 million). The main reason for the movement in net liabilities is the movement in the pension liability in year £42.134 million (2010: £45.731 million). This movement is due largely to a change in financial assumptions agreed with the Board's actuaries and the change in inflation assumption from RPI to CPI.

Governance and accountability

We considered corporate governance arrangements as they relate to systems of internal control, the prevention and detection of fraud and irregularity, standards of conduct and arrangements for the prevention and detection of corruption, and its financial position.

The annual internal assurance programme supports the assessment of the operation of the system of internal control. Responsible officers provide a statement of assurance to the chief executive to assist in his preparation of the statement.

Our testing of the design and operations of controls over entity level controls and significant risk points in key financial processes confirms that, controls are designed appropriately and operating effectively.

Performance

The Scottish Legal Aid Board ("SLAB") continues to have strong performance management arrangements in place, and performance is measured on an annual basis against key performance indicators. A number of key performance indicators have been set, with the primary measures combining individual timeliness and accuracy targets for each legal aid type. In 2010-11 SLAB hit seven out of eight of the headline performance targets. The Board did not achieve its timeliness target for criminal legal aid due to a particularly tight online service standard. The target for 2011-12 has been extended in recognition of the fact that it was particularly challenging.

SLAB forecast efficiency savings for the Fund in 2011-12 of £11.9 million and is required to meet savings of £1.1 million on the Grant-in-aid budget. Detailed plans are in place for how these savings are to be realised.



Executive summary

Headlines

Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practice* ("the Code"). This specifies a number of objectives for our audit.

This report summarises our work for the year ended 31 March 2011.

We wish to record our appreciation of the continued co-operation and assistance extended to us by Scottish Legal Aid Board staff during the course of our work.

Priorities and risks

Management has made significant progress to identify savings that can be realised to meet the 2011-12 cash reduction of the Legal Aid administration budget.	Page 4
--	--------

The Board is aware of significant risks in respect of delivery and legislative and regulatory reform to legal aid; that these changes do not materialise in order to allow the Board to deliver required savings. In our view the Board has taken appropriate mitigating action within their powers although it remains a significant risk.	Page 5
---	--------

Financial statements

We have issued unqualified audit opinions on the 2010-11 financial statements and the regularity of transactions reflected in those financial statements.	-
---	---

A number of technical accounting matters were considered during the audit process; management provided good quality analysis and no adjustments were required.	Page 6
--	--------

Use of resources

SLAB met its financial targets recording an under spend for Grant-in-aid against the budget of £0.175 million.	Page 7
--	--------

We assessed management's response to Audit Scotland's national report on procurement. Management has taken reasonable action to mitigate risks and improve processes at a local level.	Page 9
--	--------

Governance

There have been no significant changes and the statement on internal control continues to confirm the existence of a comprehensive framework of internal control.	Page 10
---	---------

Internal audit completed their plan and did not report any significant risk recommendations.	Page 10
--	---------

Arrangements to prevent and detect fraud are embedded in internal controls, including processes to comply with requirements in respect of the National Fraud Initiative.	Page 10
--	---------

Recommendations

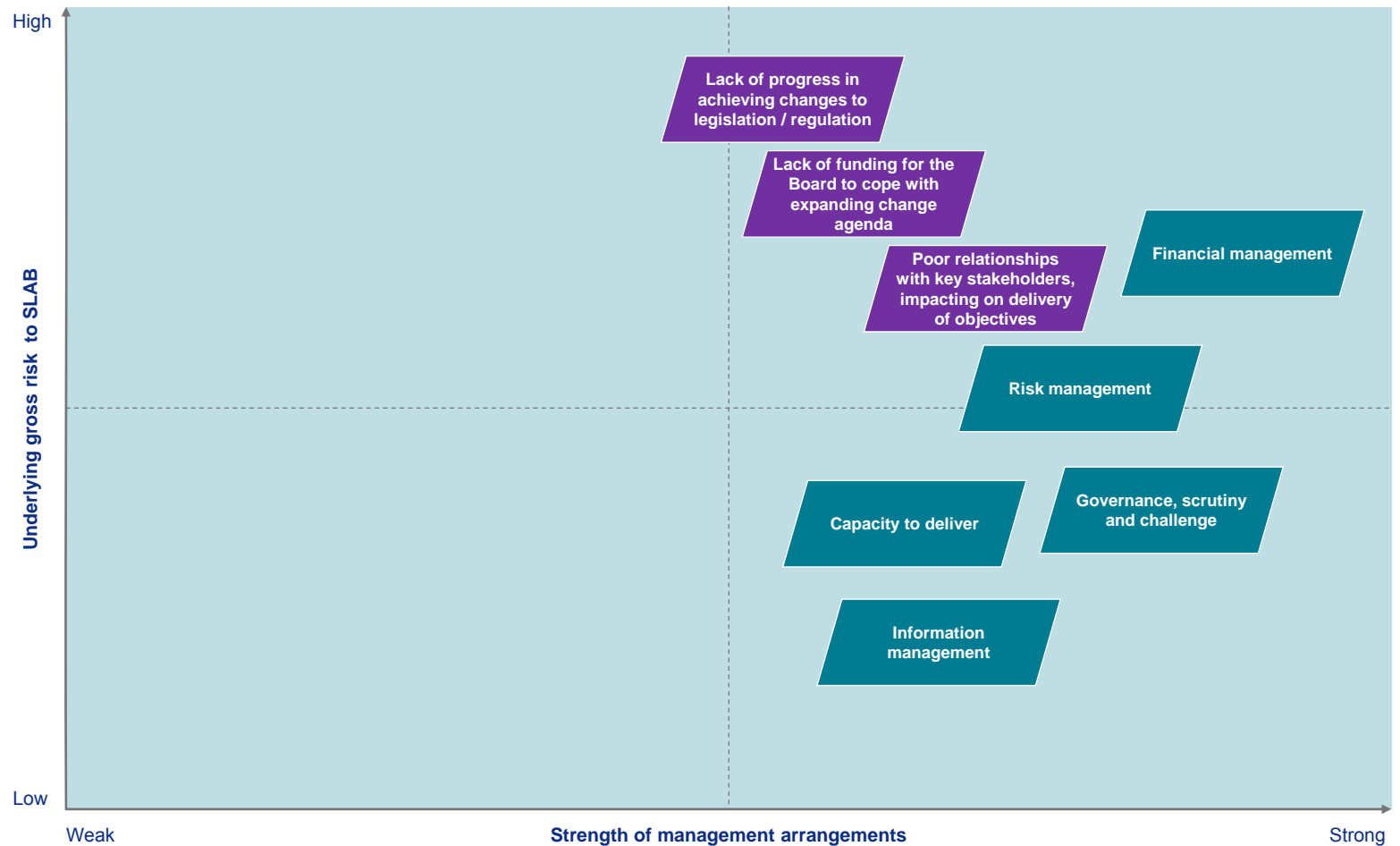
We have not raised any specific recommendations for improvement in key controls or processes but note that the Board continues to improve efficiency through greater use of electronic systems. We recommend continued concentration on increasing the use of IT to reduce paper and manual processes and appreciate the Board continues to progress this.	-
--	---

Priorities and risks

Summary of arrangements

Competing risks and pressures continue to present new and recurring challenges. Overall, the impact of sector priorities present a high risk.

The diagram summarises the potential underlying risks to achievement of strategic objectives, compared to the strength of management arrangements to mitigate these risks. The following pages summarise the areas where we believe that significant risks are present, together with how management arrangements are likely to mitigate or eliminate these risks to a greater or lesser extent.



Priorities and risks

Assessment of significant risks

Arrangements in respect of relations with key stakeholders are likely to mitigate the impact of significant risks.

Management's approach to the risk of lack of progress in achieving changes to legislation / regulation, is limited in its capacity to mitigate the risk posed to Fund forecast cash savings.

Poor relations with key stakeholders, impacting on ability to deliver key objectives or importing difficulties into working practices	<p>To reduce the risk, management has identified the following key stakeholders; the Law Society, the Crown Office and Procurator Fiscal Service, legal profession, sheriffs and the Glasgow Bar Association and assessed appropriate communication arrangements in place with each group. The Board's communication strategy approved for 2011-14 which focuses on these stakeholders.</p>	<p>In our view, risk reduction measures in place are sufficiently robust to mitigate risks around maintaining positive working relations with key stakeholders.</p> <p>We understand that the Board is in continued dialogue with the Glasgow Bar Association.</p>
Lack of progress in achieving changes to legislation / regulation to improve legal aid and achieve efficiency savings	<p>Delay to the delivery of regulatory changes could impact upon the forecast savings packages. To mitigate this risk, SLAB has developed a Scottish Government and SLAB joint programme management board which helps with the early identification and communication of requirements from the government</p> <p>In the April 2011 risk update to the audit committee, it was noted that the lack of programme board meetings was a concern that had been raised with the Scottish Government.</p>	<p>SLAB has previously demonstrated their ability to liaise closely with the Scottish Government in respect of legislative change and to subsequently adapt their business in response to changes. This has been evident over the last year.</p> <p>The Board recognises the risk that legislative change does not occur which could impact ability to deliver savings and has taken appropriate action to mitigate the risk as far as possible.</p>
Lack of funding for the Board to cope with the expanding change agenda	<p>The Board was aware for some time that a cash reduction on the 2011-12 administrative budget was likely. Progress with legal aid online, including a substantial increase in take up by solicitors and the implementation of other digital systems are likely to help meet the budgetary requirements.</p> <p>The most significant savings will be realised in areas of staff costs and running costs.</p>	<p>Controls to identify savings and thus mitigate the risk of funding cuts have been implemented and a designed to meet the 2011-12 budget.</p>
	<p>■ In our view risks exist but actions have been identified to address these risks.</p>	

Risks were anticipated around provisions and net liabilities; no audit adjustments were required and matters were concluded in a timely manner.

Areas of HIGH audit risk			
Area	Value (£'000)		KPMG comment
	2011	2010	
Provision for legal aid costs	75,580	64,796	<p>The level of provision has increased by £10.784 million in year. This movement is due predominantly to the increase in VAT in 2010-11 and increases to solicitor charge rates with regards to civil and solemn criminal legal aid. With regards to solemn criminal legal aid cases, there has been a higher number of cases being referred to the high court, thus increasing the costs provided for.</p> <p>We reviewed the underlying basis of the provision, the model used for calculation and management's underlying assumptions and concluded that the provision as at 31 March 2011 was not materially misstated.</p> <ul style="list-style-type: none"> ■ No adjustment to the financial statements was necessary. ■ Financial statement disclosures in this respect are complete and accurate.
Net Liabilities	40,660	44,545	<p>Provisions for liabilities and charges and pension scheme liabilities have been accounted for under International Accounting Standard 37 'Provisions, Contingent Liabilities and Contingent Assets' and International Accounting Standard 19 'Employee Benefits' respectively. We have reviewed a 'letter of comfort' provided by management, originating from the Scottish Government confirming that cash will be available in future years to fund the settlement of these obligations as and when they fall due.</p> <ul style="list-style-type: none"> ■ No adjustment to the financial statements was necessary. ■ Financial statement disclosures in this respect are complete and accurate.
Systems and controls			
Preparation of the financial statements			
<ul style="list-style-type: none"> ■ Draft financial statements and supporting documentation were provided between 6 June and 17 June, which was in line with the agreed timetable. ■ The schedules and supporting documentation were prepared to a high standard and submitted for audit both in electronic and paper format. 			
Control environment			
<ul style="list-style-type: none"> ■ Overall, management's approach to preparing the financial statements is efficient. Management worked consistently to the audit timetable which built in time for internal review before schedules were submitted for audit. 			

Financial position

Actual performance in 2010-11 against Scottish Government funding allocations was as follows:

	Scottish Government Budget £000s	Other funding Sources £000s	Total Funding available £000s	Cash Expenditure £000s	Net Operating Costs (accruals basis) £000s
Scottish Legal Aid Fund	160,000	228	160,228	161,451	170,565
Scottish Legal Aid Board Administrative Budget	12,894	496	13,390	13,170	15,548

Scottish Legal Aid Fund

The nature of legal aid and complexity of relevant legislation means that expenditure is demand led and therefore unpredictable in timing and volume. Section 40 of the Legal Aid (Scotland) Act 1986 states that “*The Secretary of State shall pay to the Board out of moneys provided by Parliament ... such sums as are required ... to meet payments out of the Fund under this Act*”. This means that expenditure is driven by legislation and is not cash limited to the funding allocation of £160.0 million. As a result of this, the Fund’s expenditure is not limited by budget but is rather regularly monitored throughout the year by management submitting a monthly vote monitoring return detailing cash drawn down to date and forecast cash required to 31 March 2011 in line with Scottish Government Justice Department requirements. The Fund drew down £161.400 million in cash during the year, which is consistent with correspondence from the Scottish Government Justice Department, which together with a further £228,000 of pension related amounts comes to the figure of £161,628 million shown as grant-in-aid received in the cash flow statement. The total cash expenditure, reflecting both cash drawn down and the movement in bank balances was £161.451 million. Timing differences between expenditure being incurred on the accrual basis and cash payouts for legal aid can vary and along with depreciation charges and results in a significant difference between cash and accruals based expenditure.

Administrative budget

The total funding available of £13.390 million for the Board’s administrative budget combines the Scottish Government’s core grant-in-aid with sums the Board is entitled to retain from the collection of superannuation contributions from staff; with the Scottish Government’s funding of pension costs above an agreed baseline sum. At £13.170 million, net cash expenditure for the year is within that total available cash funding. The higher accruals based expenditure primarily relates to non-cash pension scheme service and finance costs and depreciation.

The Board is given a budget allocation by the Scottish Government each year. An extensive annual process of budget preparation, in which each cost centre is examined, is undertaken annually. Internal audit reviewed the accounting and budgeting processes during the year upon and they concluded that the controls in place were satisfactory.

The Board meets eight times a year. Financial performance is discussed in detail at these meetings, and any concerns over or risks to the financial plan are discussed. During the year, the Board keeps the sponsor division informed about the projected outturn against budget. Any amendments to that budget would be reflected in the Scottish Government’s proposals to Parliament for autumn and spring budget revisions.

Financial plans 2011-12 and beyond

The Scottish Government has been allocated a resource and capital budget which will reduce by 6.8% in 2011-12 and 38.4% in real terms by 2014-15.

Scottish Legal Aid Fund

In November 2010, the Cabinet Secretary for Finance and Sustainable Growth announced the Scottish Government's draft budget for 2011-12. This indicated an expectation of significant financial savings from the Legal Aid Fund. The Fund is demand led and as such making significant reductions to the cost of Legal Aid generally requires legislative or regulatory change. The Board has subsequently agreed savings packages with the necessary stakeholders which amount to near to the 8% reduction in expenditure anticipated by the Scottish Government. However, it is thought likely that a gap will remain between SLAB's net forecast and current Scottish Government funding. Forecast savings for 2011-12 total £11.9 million. The Scottish Government's published budget acknowledged this gap and undertook to manage these demands throughout the year.

Scottish Legal Aid administrative budget

In its budget plans, the Scottish government indicated that there would be a cash reduction in the grant-in-aid budget of £1.1 million in 2011-12, a reduction of 8.5% on prior year total funding available.

To meet this challenge, the Board identified at an early stage a range of savings across the administrative budget. Most significant savings will be in staff costs and the Board does not believe these savings will require compulsory redundancy. Other significant savings have been identified in running costs, predominantly since some computer maintenance costs were accelerated into 2010-11.

Key risks

Achievement of the financial plan will be challenging due external pressures. The key risks identified are similar to the prior year and are summarised in the table below.

Key risks identified

- Failure to identify trends forecasts in legal aid and take appropriate actions; and
- Lack of progress in achieving changes to legislation / regulation to improve legal aid and achieve efficiency savings.

Audit Scotland national studies

Audit Scotland periodically undertakes national studies on topics relevant to the performance of central government bodies. While the recommendations from some of the studies may have a national application, elements of the recommendations are also capable of implementation at board level, as appropriate.

Audit Scotland's corporate plan 2009-12 reinforces a commitment to maximising the impact of their work and demonstrating this impact. As part of this process, external auditors are required to provide information on how bodies respond to national performance audit reports.

Management has procedures in place to consider individual reports. In addition, where appropriate, management will carry out a self-assessment against the national study and implement local action plans as required.

In 2010-11 a more targeted follow-up was to be completed by auditors in respect of SLAB's actions following publication of the joint Accounts Commission / Auditor General for Scotland report, "Improving Public Sector Purchasing" published in July 2009.

Our work centred around the answers to three questions to facilitate analysis of the Board's arrangements. Overall, taking into account the size and nature of the Board, we found that processes are appropriate and mitigate the issues highlighted by the report. We noted that in the two procurement capability assessments that SLAB had participated in in 2009 and 2010, SLAB had been graded as 'conformant' and that an action plan has been put in place to take forward improvements suggestions identified in the process.

We have provided a separate report to management and Audit Scotland in respect of this follow-up work.

The audit committee receive a quarterly detailed update and presentation on the Board's consideration of Audit Scotland national studies. The updates include consideration of whether studies were applicable, and the lessons and actions that could be taken from any element of the reports.

This is an example of best practice.

Over-arching and supporting corporate governance arrangements remain primarily unchanged and provide a sound framework for organisational decision-making.

Corporate governance framework	<p>Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour. The three fundamental principles of good corporate governance – openness, integrity and accountability – apply to all bodies. Through its chief executive, the Board 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:</p> <ul style="list-style-type: none"> - the Board's reviews of its systems of internal control, including its reporting arrangements; - the prevention and detection of fraud and irregularity; and - standards of conduct and arrangements for the prevention and detection of corruption.
Statement on internal control	<p>The statement on internal control provides details of the purpose of the framework of internal control, along with an analysis of its effectiveness. This statement is in compliance with guidance issued by the Scottish Government.</p>
Internal controls	<p>Our testing, combined with that of internal audit, of the design and operation of financial controls over significant risk points confirms that controls are designed appropriately and operating effectively.</p>
Internal audit	<p>Internal audit have submitted all of their planned reports for the year. We have relied on a number of reports, including those in respect of receipts and payments, procurement BPIs, accounting and budgeting, risk and best value. These reports do not make any 'critical' recommendations.</p> <p>Internal audit's 2010-11 annual report concludes that <i>"based on this work, in my opinion, the Scottish Legal Aid Board has a generally sound framework of control which provides reasonable assurance regarding the effective and efficient achievement of the Board's objectives. Accordingly, I am of the opinion that there is nothing which would warrant the Accountable Officer not signing the standard form of the Statement of Internal Control in the Board's report and accounts for the year to 31 March 2011, and I do so recommend."</i></p>
Fraud and irregularity	<p>SLAB participated in the National Fraud Initiative (NFI) exercise in the year and has a low number of matches which are being investigated.</p>



© 2011 KPMG LLP, a UK Limited Liability Partnership, is a subsidiary of KPMG Europe LLP and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (KPMG International), a Swiss entity.
All rights reserved.

The KPMG name, logo and 'cutting through complexity' are registered trademarks or trademarks of KPMG International Cooperative (KPMG International).