Government and Public Sector Assurance

June 2011

Mental Welfare Commission

Annual Report to Commissioners and the Auditor General for Scotland 2010/11

PRICEWATERHOUSECOOPERS

Contents

The principal objective of our audit procedures is to enable us to express our opinion, in line with the requirements of the Audit Scotland Code of Audit Practice, on the financial statements as a whole. Our audit opinion does not guarantee that the financial statements are free from misstatement. Our audit responsibilities and their limitations are explained in our letter of appointment. Any oral comments made in discussions with you relating to this report are not intended to have any greater significance than explanations of matters contained in the report. Any oral comments that we make do not constitute oral advice unless we confirm any such advice formally in writing. The matters raised in this and other reports that will flow from the audit are only those which have come to our attention arising from or relevant to our audit that we believe need to be brought to your attention. They are not a comprehensive record of all the matters arising, and in particular we cannot be held responsible for reporting all risks at the SAS or all internal control weaknesses. This report has been prepared solely for your use and should not be quoted in whole or in part without our prior written consent. No responsibility to any third party is accepted as the report has not been prepared for, and is not intended for, any other purpose.

1. Executive Summary

Introduction – Section 2

Our overall responsibility as external auditors of the Mental Welfare Commission (MWC) is to undertake our audit in accordance with the principles contained in the Audit Scotland Code of Audit Practice ("the Code"), revised and published in March 2007.

We have a dual reporting responsibility for the audit: to the Board of MWC and to the Auditor General for Scotland.

Financial Statement and Audit Opinions – Section 3

The financial statements of MWC for the year ended 31 March 2011 have been prepared to comply with accounting requirements contained in the NHS Board Accounts Manual for Directors' Report and Accounts of NHS Boards and for Scottish Financial Returns, and supplementary guidance, as issued by the Scottish Government Health Directorates (SGHD) and approved by Scottish Ministers.

We are pleased to report that our **true and fair opinion** and **regularity opinion** on the financial statements for the year ended 31 March 2011 are **unqualified.**

We also provide a view as to whether those parts of the Remuneration Report subject to audit have been properly prepared. Our opinion on the relevant parts of the **Remuneration Report is unqualified**. It should be noted that our audit opinion does not extend to other parts of the Annual Report.

Basis of Preparation – International Financial Reporting Standards
The accounts are prepared under International Financial Reporting Standards (IFRS) and the 2010/11 NHS Scotland Boards Accounts Manual as detailed above.

Accounting Issues
A number of accounting issues were discussed with management during the audit. The most significant of these are set out below:

- Accounting implications for additional pension contributions
- Assessment of going concern – net liability position

Financial Performance 2010/11 – Section 4

MWC is required to meet three targets each year as set by the Scottish Government Health Directorate (SGHD). All three of these were achieved in the year.

Governance and Performance 2010/11 – Section 5

We reviewed MWC's overall governance arrangements in place during the year 2010/11 including a review of the new Board and Committee structures and minutes, financial reporting to the Commission/ Board and risk management. We consider that appropriate arrangements and reporting were in place. We have also reviewed MWC's overall systems of internal control including a review of IT general controls (ITGCs); and internal audit arrangements.

The new Board structure took effect from 1st April 2011 with the appointment of the new Chair and other members. The role of the Board is to govern and set MWC's strategic direction with the role of service provision undertaken by Commission Visitors. Appropriate arrangements and reporting were noted.

2. Introduction

Purpose of this report

The Annual Audit Report which follows is designed to set out the scope, nature and extent of our audit, and to summarise our opinion and conclusions on issues arising. Specifically, this will direct your attention to matters of significance that have arisen out of the 2010/11 audit process and to confirm what action is planned by management to address the more important matters identified for improvement.

Scope, nature and extent of our audit

Our overall responsibility as external auditors of MWC is to undertake our audit in accordance with the principles contained in the Code of Audit Practice issued by Audit Scotland in March 2007. In this regard, the Code sets out the need for public sector audits to be planned and undertaken from a wider perspective than in the private sector involving not only assurance on the financial statements but also consideration of areas such as regularity, propriety, performance and the use of resources. It also sets out the need to recognise that the overall audit process is a co-ordinated approach involving the "appointed auditor", the Auditor General for Scotland and other auditors such as Audit Scotland's Health Performance and Public Reporting Group. Our audit has been planned and conducted to take account of these wider perspectives. Under the requirements of International Standard on Auditing (UK and Ireland) ('ISA') 260: "*Communication of audit matters to those charged with governance*", we are required to communicate audit matters arising from the audit of the financial statements to those charged with governance of an entity. This Annual Audit Report to Members, together with previous reports to the Audit Committee throughout the year, discharges the requirements of ISA 260.

Acknowledgment

We would like to formally extend our thanks to all MWC managers and staff for the assistance they have given us during the current year's audit process and to thank them for the courtesy and cooperation extended to us throughout our tenure as external auditors which now concludes.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Glasgow
17 June 2011

3. Financial Statement and Audit Opinion

Audit opinion

Our audit opinion concerns both the true and fair statement of the MWC's financial results for the year ended 31 March 2011 and the regularity of its income and expenditure for the year.

We are pleased to report that our opinion on the true and fair view on the financial statements and on the regularity of income and expenditure is **unqualified**. We also provide a view as to whether those parts of the Remuneration Report subject to audit have been properly prepared. Our opinion on the Remuneration Report is **unqualified**. Our audit opinion does not extend to any other part of the Directors' Report.

Audit Process

The financial statements and supporting schedules were presented to us for audit within the agreed timetable. The quality of working papers provided by management was of a high standard. Overall, an efficient audit process was achieved through an effective working relationship with your staff.

Basis of Preparation

The financial statements were prepared in accordance with the accounting requirements contained in the NHS Scotland Board Accounts Manual for Directors' Report and Accounts of NHS Boards and for Scottish Financial Returns, and supplementary guidance, as issued by the Scottish Government Health Directorates (SGHD) and approved by the Scottish Ministers.

Approval

The Financial Statements were submitted to MWC's Audit Committee on 17 June 2011 and are to be approved and adopted at the Board meeting on 28 June 2011.

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Unadjusted misstatements

Under ISA 260 - "Communication of audit matters to those charged with governance", we are required to report to you all unadjusted misstatements which we have identified during the course of our audit, other than those which we deem to be of a trivial nature.

As a result of our work, we proposed a small number of measurement and disclosure adjustments all of which have been processed by management in the finalised version of the 2010/11 financial statements.

Accounting Issues

Lothian Pension Fund

The decision was taken to make additional contributions to the Lothian Pension Fund to address the liability and potential costs on cessation. PwC's Pension Actuarial team provided advice on the accounting treatment for these payments whereby the payments cost should be classified as expenditure in the year and not charged against the actuarially determined balance sheet liability. These additional contributions will be reflected in the future actuarial valuation.

The 2010/11 under-spend position was higher than originally budgeted due to the change in the statutory measure of inflation used in the actuarial assumptions from RPI to CPI in accordance with Central Government guidance on accounting for pensions. This resulted in a realisation of around £129k to account for the reduction in value of the pension liability. The Commission has agreed with the Scottish Government to make additional contributions to the Lothian Pension Fund totalling £317k of which £120k was paid during 2010/11 and £197k accrued as at 31 March 2011 to be paid over in during 2011/12.

Going Concern

MWC's balance sheet discloses net liabilities of £730k at 31 March 2011 (2009/10: £641k), meaning that the Commission is technically insolvent. The primary reason for this position at 31 March 2011 is the Lothian Fund pension liability although this has reduced from the prior year due to the change in pension assumptions noted above. Additional contributions to reduce the pension liability have been made with accruals totalling £197k included within Accounts Payable. Under the current accounting arrangements as set out in the Financial Reporting Manual (FReM), MWC must show liabilities on its balance sheet without drawing down the equivalent cash to fund them. However, as the liabilities fall due, the cash will be drawn down from the SGHD to meet the payments.

We are satisfied that the accounts have been correctly prepared on a going concern basis.

Cost of capital

It should be noted that MWC are no longer required to recognise a cost of capital charge for 2010/11 and going forward. In accordance with guidance issued by the Scottish Government, this change is treated as a voluntary change in accounting policy thus requiring restatement of prior year figures. The prior year comparator within the Statement of Comprehensive Net Expenditure has been restated to £4,042k.

Prepayments and accruals

An annual schedule of prepayments and accruals is maintained to identify adjustments at the year end. It was noted through audit testing that a number of low value transactions had not been identified as prepayments or accruals resulting in a net position where expenditure had been understated. We have agreed an adjustment with management to correct the financial statements and a recommendation has been raised within the action plan at Appendix A to update the schedules as appropriate.

Action 1

4. 2010/11 Performance

Financial Results 2010/11

2010/11 Outturn	£'000	£'000
Recurring income	3,700	
Recurring expenditure (before savings)	(3,700)	
Recurring savings	0	
Underlying recurring surplus / (deficit)		**0**
Non-recurring income	81	
Non-recurring expenditure (before savings)	(81)	
Non-recurring savings	0	
Non-recurring surplus/(deficit)		**0**
Financial surplus for the year		**0**
Underlying recurring surplus / deficit as a percentage of recurring income		**0**

At the start of the 2010/11 financial year, the Scottish Government confirmed an allocation of £3.7 million for MWC for 2010/11 with an additional £27k to be received for National Dementia Standards and £54k relating to distinction awards.

The balance sheet position as at 31 March 2011 decreased from the prior year £730k (2009/10: £641k). The pension liability reduced in the year but additional amounts totalling £197k were accrued for contributions to reduce the cessation value of the Lothian Pension Fund as described at Section 3 above.

At the end of the year, MWC reported a break even result as surplus amounts were used to reduce the Commission's pension liability in the Lothian Pension Fund.

Performance against Key Financial Targets

MWC is required to meet three targets each year as set by the Scottish Government Health Directorate (SGHD). MWC has achieved all three of its financial targets in the year as follows:

	Limit set by SGHD £'000	Actual Outturn £'000	Variance (over)/under £'000
Revenue Resource Limit	3,781	3,781	nil
Capital Resource Limit	nil	Nil	nil
Cash Requirement	3535	3535	nil

Creditors – Creditors Payment Days

The Financial Statements at 31 March 2011 report a decrease in creditor payment days from 14 days in 2009/10 to 11 days. The reported days are within the targets set by the Scottish Government.

5. Governance and Control

Overall Governance Arrangements

As from 1st April 2011, the new governance structure has been implemented in response to the requirements of the Public Services Reform Act 2010. The Full Commission and six Standing Committees have been replaced by a new Board and one standing Committee. The Board has responsibility for the strategic direction and corporate governance of the organisation. All part time Commissioner posts ceased on 31 March 2011.

We have not formally assessed the new governance structure as part of the audit but noted the changes which had taken place prior to our final audit visit during May 2011.

Service redesign and sustainability

During 2010/11 the role of MWC was changed in accordance with the Public Services Reform Act 2010 and this is reflected in the reduced budget allocation for the year. The Social Care and Social Work Improvement Scotland (SCSWIS) and Health Improvement Scotland (HIS) are now responsible for general service improvement. The role of MWC is to safeguard the rights of individuals with a focus on legal and ethical issues in care and treatment. MWC is required to communicate areas of concern to HIS and SCSWIS who, in turn, have a duty to report to MWC on legal and ethical practices in the delivery of mental health services.

Systems of Internal Control

The results of our audit work on systems of internal control were communicated to Audit Committee in our Interim Management Letter on 25th February 2011 The report contained two new recommendations to improve controls, neither of which was graded as higher risk. Furthermore, no risks were identified that could be considered business critical in nature. MWC has completed an action plan detailing those individuals responsible for implementing our recommendations and the timetable for completion.

Statement of Internal Control

The Code of Audit Practice requires us to review and report on MWC's Statement on Internal Control. MWC has used the correct format for its Statement and has outlined the processes it has employed to identify and evaluate risks. In addition, key elements of the MWC's control framework have been highlighted. Based on our normal audit procedures, we do not disagree with the disclosures contained in the Statement.

Follow up of outstanding recommendations

We followed up progress in implementing recommendations made in the prior year during our interim visit. Our Follow up Report was considered at the Audit Committee meeting on 25th February 2011. At the time of reporting, of the 9 agreed actions, progress was as follows:

Status	Follow Up of prior period reports
Action implemented	7
Action in progress	2
Limited/Little progress to Date	-
Not yet due	-
No longer applicable	-
Total	**9**

Appendix A: Action Plan

Recommendation and Risk Rating	Management Response, Responsible Officer and Implementation Date
Action 1 An annual schedule of prepayments and accruals is maintained to identify adjustments at the year end. It was noted through audit testing that a number of low value transactions had not been identified as prepayments or accruals resulting in a net position where expenditure had been understated. We recommend, going forward, that the schedule of accruals and prepayments be updated to include those items identified during the final audit fieldwork visit and any additional missing entries. **Risk rating -**	**Management Response:** Agreed **Responsible Officer:** Finance Manager **Implementation Date:** Immediate

Recommendation and Risk Rating	Management Response, Responsible Officer and Implementation Date
Action 2 For tangible and intangible assets, additions and yearly depreciation charges are not cleared to zero at the start of the year and amounts moved to opening cost and opening depreciation/amortisation. As such the individual general ledger account codes do not directly agree to the accounts. We recommend that in future, the above account codes are cleared at the start of each financial year so that movements on the codes correctly reflect transactions undertaken in the year. **Risk rating -**	**Management Response:** The overall Fixed Asset position reconciles to the accounts. The approach has been to post depreciation charges and additions to cumulative accounts only and not to 'in year' accounts followed by another journal to clear balances to the cumulative accounts. We will review our current approach in the light of Scottish Government guidance during the coming year. **Responsible Officer:** Finance Manager **Implementation Date:** 30th September 2011

Appendix B – Communications to Management

International Standards on Auditing ("ISA") (UK&I) 260 – Reporting to those charged with Governance, requires that the External Auditor communicates certain matters to those charged with governance. Those charged with Governance is taken to be the Members of the Audit Committee with responsibility discharged through the regular meetings of the Audit Committee during the year. Summarised below are the requirements set out within ISA 260 together with reference to the relevant communication with you during 2010/11 or comments as appropriate.

Communication Required under ISA 260	Reference/Comment
Engagement letters	Signed Engagement Letter with Audit Scotland at the start of our 5 year appointment and updated annually.
Independence	Audit Planning document reported to the Audit Committee on 25 February 2011 confirmed no member of audit team has any direct interest, financial or otherwise, in MWC.
Audit Approach and Scope	Audit Planning document (reported to Audit Committee on 25 February 2011)
Accounting Policies/Practices with a Material Effect on the Financial Statements	Sections 3 of this Annual Report to Commission Members and the Auditor General for Scotland.
Potential Effects of Material Risks and Exposures	Audit Planning document (reported to Audit Committee on 25 February 2011).
Audit Adjustments	Section 3 of this Annual Report to Commission Members and the Auditor General for Scotland.
Material Uncertainties relating to Going Concern	None identified.
Disagreement with Management about Matters that could be Significant to the Financial Statements	Not applicable.
Expected Modifications to the Auditor's Report	No modifications identified. A true and fair opinion provided
Letter of Representation	Signed by management on 28 June 2011.
Material Weaknesses in Internal Control	Reported separately in our Interim Management Letter to Audit Committee 25 February 2011.
Fraud	Discussed fraud arrangements with the Audit Committee (25 February 2011) and management throughout the audit process.

Communication Required under ISA 260	Reference/Comment
Laws and Regulations	We have not identified any material braches of laws and regulations in the period which impact on the 2010/11 Financial Statements.
Audit materiality	Included in Audit Planning document – presented to Audit Committee in 25 February 2011.
Fair Value Measurement and Disclosure	Included in representation letter, signed by management dated 28 June 2011.
Related Parties	Other than those transactions disclosed in the financial statements we have not identified any further transactions requiring disclosure.

Formal Reporting to Management during 2010/11

During the year we have presented a number of formal reports to Management and the Audit Committee and produced certain outputs. Our principal outputs during 2010/11 are summarised below:

Formal Output	Timing
Audit Plan	25 February 2011
Detailed Timetable for 2010/11 Financial Audit	25 February 2011
Interim Management Letter	25 February 2011
Annual Report to Board Members and the Auditor General for Scotland	17 June 2011
Audit Opinions 1. True and fair value on the financial statements ✓ 2. Regularity of income and expenditure ✓ 3. Remuneration Report (sections) ✓ Unqualified Audit Opinions	28 June 2011