

# ***Children's Hearings Scotland***

Annual Report to Board Members and  
the Auditor General for Scotland

Board Meeting

17 September 2012

141 Bothwell Street  
Glasgow  
G2 7EQ

For the attention of the Board  
Childrens Hearings Scotland  
Ladywell House  
Ladywell Road  
Edinburgh  
EH12 7TF

17 September 2012

Dear Sirs,

We are pleased to enclose our Annual Report to Board Members and the Auditor General for Scotland for the external audit of the year ended 31 March 2012. This report also discharges our obligations under International Standards of Auditing ("ISA") 260: Reporting to those charged with Governance.

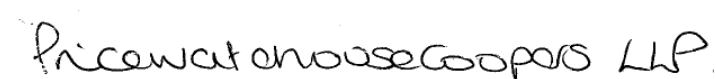
The primary purpose of this report is to communicate the significant findings arising from our external audit that we believe are relevant to those charged with governance and to meet our obligations, as set out within the Audit Scotland Code of Practice.

The scope and proposed focus of our audit work was summarised in our audit plan, which we presented to the Audit and Risk Committee. The procedures we have performed in response to our assessment of significant audit risks are detailed within the Key Areas of Audit Focus section of this report.

We have completed our year end external audit work on the financial statements and expect to issue an unqualified audit opinion, following the meeting of the Children's Hearings Scotland Board on 17 September 2012 to approve the financial statements, subject to final review of the updated financial statements.

We would like to take this opportunity to thank Children's Hearings Scotland staff and management for their cooperation and assistance throughout the audit process.

Yours faithfully



PricewaterhouseCoopers LLP

17 September 2012

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# Section 1: Introduction

We have pleasure in presenting this report relating to our audit of the financial statements of the Children's Hearings Scotland ('CHS') for the year ended 31 March 2012.

We have discussed this report with the Director of Finance and Corporate Services as part of our audit process. The purpose of this report is to update the CHS Board on the output of the audit and of any significant matters that have arisen during the course of our work.

## Scope, nature and extent of our audit

Our overall responsibility as external auditor of CHS is to undertake our audit in accordance with the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011. 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" and the Auditor General for Scotland.

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 financial statements to those charged with governance of an entity. This Annual Audit Report to Board Members discharges the requirements of ISA 260.

## Management responsibility

It is the responsibility of the Board and the National Convenor/Chief Executive, as Accountable Officer, under Section 136(3) of the Local Government Etc. (Scotland) Act 1994, to prepare financial statements for each financial year in the form and on the basis determined by the Scottish Ministers. This means:

- acting within the law and ensuring the regularity of transactions by putting in place systems of internal control to ensure that financial transactions are in accordance with the appropriate authority;
- maintaining proper accounting records;
- preparing financial statements timeously which give a true and fair view of the financial position of CHS and its expenditure and income for the year ended 31 March 2012; and
- preparing Management Commentary, a Governance Statement and a Remuneration Report.

## Auditor's responsibilities

We audit the financial statements and the part of the Remuneration Report to be audited and give an opinion on:

- whether they give a true and fair view of the financial position of Children's Hearings Scotland and its expenditure and income for the year to 31 March 2012;
- whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements;
- whether the information which comprises the annual report included with the financial statements is consistent with the financial statements; and
- whether expenditure and receipts have been incurred and applied in accordance with guidance from Scottish Ministers (the regularity opinion).

We also review the Governance Statement by considering the adequacy of the process put in place by the National Convenor/Chief Executive as Accountable Officer to obtain assurances on systems of internal control; and assess whether disclosures in the statement are consistent with our knowledge of the organisation and in line with guidance.

## Status

Our audit work on the draft financial statements 2012 was undertaken the week commencing 13 August 2012. We have completed our year end external audit work on the financial statements and have issued an unqualified audit opinion.

## The audit process

We received a complete draft set of financial statements within the timetable we agreed. All necessary CHS staff were available to assist us complete our year end testing, and all issues identified were discussed and resolved on a timely basis.

A number of disclosure amendments were discussed and agreed with Management and these have been reflected in the final financial statements.

## Opinion

We have completed our year end external audit work on the financial statements and have issued an unqualified audit opinion. Our opinion is also unqualified in respect of the Remuneration Report and of consistency of the Board Report with the financial statements.

## Significant auditing and accounting matters

Section 4 contains other matters for the attention of those charged with governance, including elements of communication required under International Standard on Auditing "Communication with those charged with governance". This section includes communication regarding identified misstatements, a summary of which is included in **Appendix 1**.

## Staff Assistance

We would also like to take this opportunity to express our thanks for the co-operation and assistance we have received from management and staff throughout our work.

## Section 2: Financial performance

### Financial performance 2011/12

	<b>2011/12 (actual)</b>	<b>2011/12 (forecast)</b>	<b>Variance</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>
<b>EXPENDITURE</b>			
Staff costs	221	266	(45)
Board	51	76	(25)
Property	0	23	(23)
Travel	2	5	(3)
Other Operating Charges	238	301	(63)
Direct Support for Panel	16	65	(49)
<b>NET OPERATING EXPENDITURE*</b>	<b>528</b>	<b>735</b>	<b>(207)</b>
<b>INCOME</b>			
Grant-in-aid	750	750	-

\* extracted from the 2011/12 Operating Cost Statement of the financial statements and budget information.

CHS was established on 4 July 2011 under the Children's Hearings (Scotland) Act 2011. Accounts have been produced for the first time for the year ended March 2012 without prior year comparatives.

The 2011/12 forecast figures were derived by management based on actual year to date figures to February 2012 plus forecasted expenditure for March 2012. This forecast was submitted to the CHS Board in March 2012 for discussion.

The results for the year show Net Operating Expenditure of £0.528million with an under spend of £0.207m against forecast resulting primarily from approximately £0.145million. The under spend is due primarily to the Scottish Government agreeing to account for approximately £0.145million of start up expenditure originally incurred by CHS. Prior to January 2012, CHS did not have their own general ledger in place. As a result, both the Scottish Government and the Scottish Children's Reporter Administration (SCRA) were recording expenditure on CHS's behalf. Upon successful creation of their ledger, CHS was recharged all expenditure incurred by SCRA on their behalf. However an agreement was reached between CHS and the Scottish Government whereby the Scottish Government agreed to absorb the initial start up cost it has incurred on behalf of CHS.

The remaining under spend on operating costs (approximately £0.062million) was mainly derived from slippage of expenditure into 2012/13 (£0.023million).

Grant-in-aid from the Scottish Government for 2011/12 was £0.750 million, which CHS has drawn down in full. This was allocated on the assumption that Government expenditure committed on behalf of CHS would be top-sliced from the grant-in-aid. However, as the Scottish Government have now agreed to account for these expenses, CHS has an under spend of £0.222million for 2011/12. We understand that the Scottish Government have agreed that CHS may carry this forward into 2012/13 and as such this has been recognised in CHS's reserves balance.

## Financial outlook – 2012/13 and beyond

The Financial Memorandum of the Children's Hearings (Scotland) Act provides the estimated cost distribution for new arrangements under the Children's Hearing Bill. This includes the allocation set aside for CHS from 2012/13 until 2014/15.

The 2012/13 budget was initially approved by the Board on 28 March 2012. The budget was prepared on the basis of an anticipated Grant-in-Aid figure of £4.16million, which included a provisional £1.2million for training. CHS' shadow period has been extended and the organisation will now be fully operational in June 2013, and not September 2012 as originally anticipated. The Scottish Government has also confirmed that they will wholly fund training costs until September 2013. On this basis, the Grant-In-Aid figure was revised to £3million.

The Board approved the revised revenue budget for 2012/13 on 13 June 2012.

	<b>2012/13 (CHS approved revised Budget)</b>
	<b>£m</b>
<b>EXPENDITURE</b>	
Staff costs	0.673
Board	0.095
Property Costs	0.074
Travel and Subsistence	0.015
Corporate Services	0.426
Direct Support for Panel	1.717
<b>NET OPERATING EXPENDITURE</b>	<b>3.000</b>

Staff costs are budgeted based on 11 establishment posts. CHS is not operating at its full establishment as the decision to recruit a further three further Panel and Area Support roles has been deferred pending the outcomes of a panel training options appraisal.

Budgeted property costs include committed expenditure for the year based on the agreed Memorandum of Terms of Occupation for CHS' headquarters. A further provisional sum of £0.015million has been included to fund an option to increase CHS's floor area and provide a visitor's waiting area

£0.07million has been budgeted within corporate services for the shared services agreement with SCRA. SCRA provide CHS with corporate support in particular key finance and HR functions. This includes hosting CHS's general ledger system and performing all payroll services, including the calculation and payment of CHS staff on their behalf.

The three year financial position for 2012-2015 shows a reduction in the funding position year on year. In order to provide the desired level of resources for recruitment, training and support of panel members and area support teams, CHS have identified corporate services as an area where costs could potentially be minimised in future years. However, CHS have also recognised that in addition to controlling expenditure on corporate services, efficiencies will have to be realised in the delivery of direct support to panel members. It is anticipated that efficiencies can be realised through effective procurement, contract management and use of alternative training delivery methods.



## Section 3: Key areas of audit focus

Our audit followed the strategy set out in our Audit Plan which was presented to the Audit and Risk Committee. We confirm that there has been no cause for us to vary the planned scope of our work.

### Our response to the areas of audit focus identified in the audit plan:

Risk identified/area of audit focus	Audit response
Management override of controls	<p>In accordance with our audit plan, we have reviewed management’s overall fraud arrangements and policies. We have reviewed a sample of journal entries and examined management’s accounting estimates for bias. We also incorporated unpredictability into our testing of income and expenditure</p> <p>This work did not identify any errors that required adjustment to the financial statements.</p>
Recognition of operating expenditure	<p>We performed substantive testing on a sample of expenditure transactions and reviewed management’s estimates of future expenditure, such as accruals. We have undertaken specific cut-off testing to identify potentially unrecorded liabilities.</p> <p>This work did not identify any errors that required adjustment to the financial statements.</p>
Professional scepticism	<p>As auditors, we are required to display professional scepticism when we plan and perform our audits. This involves providing challenge to management in areas such as critical assumptions, judgements, explanations and inconsistencies.</p> <p>During this audit, we have displayed professional scepticism in a range of areas including, for example,</p> <ul style="list-style-type: none"> <li>• <b>Recognition of all CHS expenditure:</b> We discussed with management the agreement in place between CHS and the Scottish Government in relation to accounting for CHS start-up costs to confirm which expenditure should be included within CHS’s Financial Statements; and</li> <li>• <b>Journals:</b> We performed testing over a sample of manual journals processed to ensure adjustments were appropriate, amounts recorded agreed to supporting documentation and there was evidence of segregation of duties. We included immaterial journals within our sample to introduce an element of unpredictability.</li> </ul>

# Section 4: Significant audit and accounting matters

## Required communications on significant matters

The following table contains communication required under ISA 260 (revised and re-drafted) “Communication with those charged with governance”.

Requirement	Delivery of requirement
Uncorrected and corrected misstatements	We identified no financial misstatements to bring to your attention. A number of disclosure adjustments were identified and agreed with management.
Significant accounting principles and policies	Significant accounting principles and policies are disclosed in the notes to the financial statements. We will ask the accountable officer to represent to us that they have considered the accounting policies and that there have not been any material changes in the accounting principles and policies used during the year.
Significant qualitative aspects of accounting practices and financial reporting, management’s judgments and accounting estimates	We reviewed management’s judgements and accounting estimates in respect of accruals. We are satisfied with management’s methodology. We will continue to review the assumptions used in estimating these so that it remains appropriate in future years.
Deficiencies in the internal control environment	The purpose of our audit was to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that were appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. No deficiencies were noted during our year end work performed.
Details of material uncertainties related to events and conditions that may cast significant doubt on CHS's ability to continue as a going concern	We have not encountered any material uncertainties which cast doubt upon the ability of CHS to continue as a going concern. CHS is a Non-Departmental Public Body (NDPB), which was established under the Children’s Hearings (Scotland) Act 2011. The organisation is going through a ‘shadow’ period and is expected to be fully by June 2013.
Significant difficulties encountered during the audit	No significant difficulties were encountered during our audit which we require to bring to your attention.
Confirmation of audit independence	We confirm that, in our professional judgment, as at the date of this document, we are independent auditors with respect to CHS within the meaning of UK regulatory and professional requirements and that the objectivity of the audit engagement leader and the audit staff is not impaired.

# ***Section 5: Governance, accountability and internal control***

As part of our wider external audit remit, stemming from our responsibilities under Audit Scotland's Code of Audit Practice, we are required to consider CHS's governance and accountability arrangements in our audit work. We gained an understanding of CHS's existing governance arrangements as they concern:

- corporate governance and systems of internal control;
- the prevention and detection of fraud and irregularity; and
- standards of conduct and arrangements for the prevention and detection of corruption.

We provide brief comment on CHS's governance systems and structures below.

## **Corporate governance and internal control**

The Board is responsible for ensuring that CHS fulfils the aims and objectives set by Scottish Ministers. The role of the Board includes establishing the overall strategic direction, monitoring performance against agreed objectives and ensuring that statutory requirements for the use of public funds are complied with.

The Board is supported by the Audit and Risk Committee, which has responsibility for monitoring risk and internal control, and the Remuneration and Appointment Committee, which considers matters such as planning, human resources and remuneration.

As your external auditors, we are required to review the governance statement before publication and report as to whether the statement complies with relevant guidance, is misleading, or is inconsistent with other information obtained during the audit. We do not consider whether the statement covers all risks and controls, or form an opinion on the effectiveness of internal control or risk management arrangements. We have reviewed the governance statement and confirm that there are no matters to report.

We have considered internal control as it concerns the key financial systems and to an extent based on our audit risk assessment. The purpose of our audit is for us to express an opinion on the financial statements. This includes consideration of internal control relevant to preparation of the financial statements in order to design appropriate audit procedures. It does not extend to expressing an opinion on the effectiveness of internal control.

We are required by ISA 265 to report to those charged with governance and management deficiencies in internal controls that the auditor has identified during the audit and that, in the auditor's professional judgment, are of sufficient importance to merit their respective attentions.

We have not identified any significant weaknesses in the current system of internal controls.

## **Prevention and detection of fraud**

Audited bodies are responsible for establishing arrangements to prevent and detect fraud and other irregularity. As part of our external audit, we have reviewed CHS's high level arrangements for preventing and detecting instances of fraud and corruption. There are no matters we wish to bring to your attention concerning fraud.

All employees are required to read and sign a code of conduct upon commencing employment as part of their induction. This provides guidance on how employees are expected to behave and their ethical responsibilities as CHS employees. A financial manual is also in place, which details the processes which CHS employees should follow in order to ensure value for money and compliance with Scottish Government policies are maintained

when entering into contracts and standing orders on behalf of CHS. CHS also have a whistle blowing policy in place.

## Standards of conduct

Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and have proper arrangements in place for implementing and monitoring compliance with standards and codes of conduct, standing orders and financial instructions. We have not become aware of any issues concerning CHS's arrangements that we need to identify in this report. All employees sign up to a code of conduct upon commencing employment outlining their responsibilities and ethical responsibilities.

## Risk Assessment

CHS has invested time developing their risk assessment and management process and interim arrangements have been in place since January 2012. The stated purpose of the process is to identify and prioritise risks to the achievement of the CHS's policies, aims and objectives; to evaluate the likelihood of those risks being realised and the impact should they be realised; and to manage them efficiently, effectively and economically.

The primary mechanism for monitoring risk is through the strategic risk register which CHS adopted based on the format prescribed by the Scottish Government, reviewed by the Audit and Risk Committee in January 2012. In addition, a comprehensive risk management policy has been developed and was approved by the CHS Board in May 2012.

The Audit and Risk Committee oversee, on behalf of the Board, the risk management process through monitoring the implementation of the risk management policy. This includes reviewing the strategic risk register annually and as necessary, reviewing the work undertaken on identified high risk areas and the action plans to mitigate the effects of such risks.

## Internal Audit

As described in our Annual Plan, International Standard on Auditing (UK and Ireland) 610: "Using the work of internal auditors" requires us to:

- Consider the activities of Internal Audit and the extent that their work can be relied upon for external audit procedures;
- Obtain sufficient understanding of internal audit activities and the effectiveness of the function to enable us to identify areas of risk and develop an effective and targeted audit approach; and
- Evaluate and test the quality and timeliness of internal audit work, where we seek to rely on the findings, in order to confirm its adequacy for our purposes.

Internal audit completed one review within 2011/12 'Shared Services and governance Statement Review', which we reviewed as part of our work.

Due to the area of internal audit focus for 2011/12 we did not place specific reliance on the report issued during the year, but they did assist us in our understanding of the risks facing CHS and key activities.

# *Appendices*

# **Appendix 1: Summary of corrected and uncorrected misstatements**

In the course of our audit work, we record the errors or misstatements we find except those that are clearly trivial, which in the case of CHS are those considered to be less than £500 (this represents 5% of our overall materiality level as set out in our External Audit Planning document presented to the Audit and Risk Committee).

No financial adjustments were identified during the course of our work. However, we have proposed a number of disclosure adjustments to the draft financial statements, primarily to ensure all disclosures were in line with the required standards which have been discussed and agreed with management.



*This report has been prepared for and only for the Children's Hearings Scotland in accordance with the terms agreed with Audit Scotland in our engagement letter and for no other purpose. We do not accept or assume any liability or duty of care for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.*

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