

Scottish Public Pensions Agency

Report on the 2011/12 Audits



Prepared for Scottish Public Pensions Agency and the Auditor General for Scotland
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Key messages

2011/12

The financial challenges facing the Scottish Public Sector are well documented, with public bodies facing deep and prolonged cuts in funding. In 2011/12 we assessed the key strategic and financial risks faced by the Scottish Public Pensions Agency (SPPA). We audited the financial statements of the Agency, the NHS Superannuation Scheme (Scotland) (NHSSS) and the Scottish Teacher's Superannuation Scheme (STSS). We also reviewed the use of resources and aspects of performance management and governance. This report sets out our key findings.

Financial statements

We have given unqualified opinions on the financial statements of all three accounts for 2011/12. There were no significant issues arising from our audit of the Agency accounts.

The Agency has made significant improvements to its arrangements to support the preparation of scheme accounts in the last year. These included improved oversight, better quality control and the development of staff capacity. There was also a greater focus on improvement and resolution of known issues, and better working relationships between directorates. This has contributed to a significant reduction in the volume and significance of issues identified in the course of our audits.

In October 2011 HM Treasury suspended all unfunded pension scheme valuations pending decisions by the UK Government on pension reform proposals. As a result, publication of full scheme valuations of both schemes has been delayed. Pension liabilities for both schemes have, nonetheless, been valued subsequently using the methodology applied to a full valuation as outlined in the actuarial reports. We are content these are fairly stated.

A prior year adjustment was made to the NHSSS accounts due to an understatement of the premature retirement provision. This resulted from coding errors in previous years. We are satisfied that appropriate adjustments have been made in the NHSSS financial statements.

Financial position and use of resources

SPPA and both scheme accounts operated within the 2011/12 budgets. We found SPPA's budget setting and monitoring arrangements to be satisfactory. SPPA anticipates that spending in 2012/13 will remain within budget.

Governance and accountability

In 2011/12 we concluded that the Agency had sound corporate governance structures in place. We examined the organisation's key financial systems underpinning the organisation's control environment and concluded that they operated sufficiently well for us to place reliance on them. Improvements are being made to the review of employer contributions.

Outlook

Pension reform will be a significant driver for the Agency's work in the next few years, presenting significant challenges both in supporting policy development and implementing the required administrative arrangements. The Agency will also require to respond to the new governance requirements for pension schemes likely to arise from the UK Public Service Pensions Bill.

Introduction

1. This report is the summary of our findings arising from the 2011/12 audits of the Scottish Public Pensions Agency (SPPA), the Scottish Teachers' Superannuation Scheme (STSS) and the NHS Superannuation Scheme (Scotland) (NHSSS). The purpose of the annual audit report is to set out concisely the scope, nature and extent of the audit, and to summarise the auditor's opinions (i.e. on the financial statements) and conclusions and any significant issues arising. The report is divided into sections which reflect the extent of our public sector audit model.
2. A number of reports have been issued in the course of the year in which we make recommendations for improvements (Appendix A). We do not repeat all of the findings in this report, but instead we focus on the financial statements and any significant findings from our wider review of SPPA.
3. Appendix B is an action plan setting out the high level risks we have identified from the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "planned management action". We do not expect all risks to be eliminated or even minimised. What we expect is that SPPA understands its risks and has arrangements in place to manage these risks. The Accountable Officer, and other members of the board, should ensure that they are satisfied with the proposed management action and have a mechanism in place to assess progress.
4. This report is addressed to SPPA and the Auditor General and should form a key part of discussions with the Audit and Risk Committee, as soon as possible after the formal completion of the audit of the financial statements. Reports should be made available to stakeholders and the public, where appropriate. Audit is an essential element of accountability and the process of public reporting.
5. This report will be published on our website after consideration by the Audit and Risk Committee.
6. The management of the audited body is responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems. Weaknesses or risks identified by auditors are only those which have come to our attention during our normal audit work, and may not be all that exist. Communication by auditors of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
7. The assistance and co-operation given to us during the course of our audit work is gratefully acknowledged.

SPPA financial statements

8. Audited bodies' financial statements are an essential part of accounting for their stewardship of the resources made available to them and their performance in the use of those resources.
9. We are required to audit financial statements in accordance with the timescales set by Audit Scotland, which may be shorter than statutory requirements, and give an opinion on:
 - whether they give a true and fair view of the financial position of audited bodies and their expenditure and income
 - whether they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements
 - the regularity of the expenditure and income.
10. We review and report on, as appropriate, other information published with the financial statements, including the Directors' Report and Management Commentary, Governance Statement and the Remuneration Report. Where required, we also review and report on Whole of Government Accounts returns. This section summarises the results of our audit on the financial statements.

Audit opinion

11. We have given an unqualified opinion that the financial statements of SPPA for 2011/12 give a true and fair view of the state of the body's affairs and its net operating cost for the year.
12. SPPA is required to follow the 2011/12 Government Financial Reporting Manual (the FReM) and we confirmed that the financial statements have been properly prepared in accordance with the FReM. We also confirmed that relevant parts of the remuneration report had been properly prepared and that information given in the Directors' Report and Management Commentary was consistent with the financial statements.
13. We also reviewed the Governance Statement and concluded that it complied with Scottish Government guidance.

Regularity

14. We confirmed that the expenditure and income in the financial statements were in accordance with applicable legislation and Ministerial guidance, the Budget Act for 2011/12 and legislation governing sums paid out of the Scottish Consolidated Fund.

Accounting issues

Accounts submission

The financial statements were submitted for audit on 31 May, in accordance with a pre-agreed timetable. The audit fieldwork was completed on 28 June. Issues arising from the audit were

reported to the Agency Finance Manager throughout the audit and reported to the Director of Finance at a clearance meeting on 28 June 2012. Our ISA 260 report was presented to the Audit and Risk Committee on 17 July, and the accounts were certified in line with the agreed timetable.

Whole of Government Accounts

The *Code of audit practice* requires appointed auditors to review and report on the Whole of Government Accounts (WGA) returns prepared by audited bodies. WGA is the consolidated financial statements for all branches of government in the UK. The main legislative authority for the preparation of WGA is the Government and Resources Accounts Act 2000. Although the Act does not apply in Scotland, the Scottish Government has agreed to provide Treasury with equivalent information. SPPA prepares a consolidation pack for the purposes of WGA. However, the amounts involved are below the threshold for audit involvement.

Outlook

15. There are no significant changes to the 2012/13 FReM that are expected to have an impact on SPPA's annual financial statements.

NHSS and STSS financial statements

Audit opinion

16. We have given unqualified opinions on the financial statements of STSS and NHSS for 2011/12.
17. The scheme accounts are prepared in accordance with International Financial Reporting Standards. The applicable standards are IAS 19 (employee benefits) and IAS 26 (reporting by retirement benefit plans). Further disclosure requirements are prescribed in the Financial Reporting Manual and we confirmed that the financial statements have been properly prepared in accordance with the FReM.

Regularity

18. We confirmed that the expenditure and income in the financial statements was in accordance with applicable legislation and Ministerial guidance, the Budget Act for 2011/12 and legislation governing sums paid out of the Scottish Consolidated Fund.

Accounting issues

Accounts submission

19. The financial statements were submitted for audit on 16 July, in accordance with a pre-agreed timetable. The audit fieldwork was completed on 5 October. The issues arising from the audit were reported to the Director of Finance and discussed at a clearance meeting on 29 August 2012. Minor issues were included in a matters arising schedule, the contents of which were discussed and agreed with the Programme Finance Managers on a regular basis throughout the audit.
20. Our ISA 260 report was presented to the Audit and Risk Committee on 9 October. The financial statements were signed by the Accountable Officer on 24 October and the auditor's opinions were signed on 26 October, in line with the agreed timetable.

Prior year adjustments

21. The NHSS premature retirement provision was re-valued at 31 March 2012 using new factors provided by the scheme Actuary. During this exercise coding errors in pension records were identified which have resulted in an understatement of the premature retirement provision for prior years. The financial statements for 2010/11 have been restated to reflect the correcting prior year adjustments. The effect of this is to increase the opening premature retirement provision as at 1 April 2011 by £9.2 million with an associated increase in the general fund liability. The premature retirement provision and the general fund liability

increased by a further £3.8 million during 2011/12 as a result of the adjustment. We are satisfied that appropriate adjustments have been made in the NHSSS financial statements.

Whole of Government Accounts

22. NHSSS and STSS are required to submit a return to HM Treasury for inclusion in the consolidation process for Whole of Government Accounts (WGA). This year's final WGA pack was received on 8 October for both schemes and we have confirmed that the information being provided to the WGA process is consistent with the audited accounts.

Issues arising from the audit

Valuation of scheme liabilities

23. The actuarial valuations prepared by the Government Actuary's Department (GAD) are the most significant input to the scheme accounts. They determine the pension liability in the balance sheet and the accrued pension costs reported in the revenue account.
24. In October 2011 HM Treasury suspended all unfunded pension scheme valuations pending decisions by the UK Government on pension reform proposals. As a result, publication of full valuations of both schemes has been delayed. Pension liabilities for both schemes have, nonetheless, been valued subsequently using the methodology applied to a full valuation as outlined in the actuarial reports.
25. Employer contribution rates are based on previously published full valuations - the 2004 valuation in the case of NHSSS and the 2005 valuation in the case of STSS. The financial statements of both NHSSS and STSS include disclosure of the circumstances of the suspension of the valuations and the impact on employer contribution rates.
26. We were content that the valuations of NHSSS and STSS are fairly stated and that details of the circumstances surrounding the delay in carrying out full valuations and the impact on employer contribution rates are satisfactorily disclosed.

Changes in actuarial roll forward methodology

27. The roll forward methodology used for the 2010/11 accounts relied on the assumption that the schemes' population will remain stable, in terms of the profile of the membership of each category of member over the roll forward period. For the 2011/12 accounts, a revised roll forward methodology, which is far less reliant on an assumption of stability, has been used. In the opinion of the Actuary, the revised methodology is likely to produce a more reliable estimate of the liabilities as at 31 March 2012.
28. The Actuary has identified that the revised method has some weaknesses. Notably, although the total liability should be reasonably reliable the liabilities attributed to actives, deferred pensioners and pensioners may not reflect the actual membership in each category at the roll forward date. Also, in times of significant change in scheme membership, material experience gains and losses will not be recognised until further data becomes available.

29. Changes in roll forward methodology and data and model corrections have resulted in an increase of £0.9 billion in the NHSS liability. The change in roll forward methodology and other miscellaneous effects have resulted in a decrease of £0.1 billion in the STSS liability.
30. Valuation methodology relies on judgement and assumptions for financial, demographic and mortality factors. We were satisfied that the revised methodology provides a reliable estimate of the NHSS and STSS liabilities as at 31 March 2012.

Progress against prior year issues

Capacity and accounts preparation processes

31. In 2010/11 we highlighted our concern about a high level of error identified during our audits that had continued over a number of years, and that many of these were related to system weaknesses and deficiencies in the accounts preparation processes on which we had previously reported. We also drew attention to weaknesses in the quality review arrangements for the financial statements.
32. We are pleased to report that significant progress has been made during 2011/12 in addressing these issues. The Agency has made significant improvements to its arrangements to support the preparation of scheme accounts. These included improved oversight, better quality control and the development of staff capacity. There was also a greater focus on improvement and resolution of known issues, and better working relationships between directorates. This has contributed to a significant reduction in the volume and significance of issues identified in the course of our audits.
33. Going forward, SPPA should ensure that improvements are maintained and developed on an on-going basis.

NHSS legacy refunds

34. When members leave the scheme with less than two years' qualifying service they have a finite period in which to transfer their service to another scheme or claim a refund ('undecided leavers'). After a period of two years they are only eligible to claim a refund ('legacy refunds'). The 2010/11 NHSS accounts included a liability of £10.9 million representing refunds due to members not entitled to pension benefits. We highlighted our view that SPPA had made limited progress in making these payments.
35. Since then SPPA have made good progress in clearing legacy refunds. As at 31 March 2012 the balance was £8.6 million. Reductions in the balance as a result of the claim and settlement of refunds are offset by new cases. Clearer procedures are needed for identifying when a member has reached the point where they should be moved from the 'undecided leavers' category to the 'legacy refunds' category to ensure that potential liabilities are recognised in the financial statements.

Refer Action Plan No. 1

Contributions reconciliations

36. The Agency receives around £1.5 billion each year in contributions, paid by approximately 1,200 employers, which is accounted for using the Epicor system. We have previously highlighted the need for improved controls over the completeness and accuracy of contribution income.
37. Over the last few years, SPPA have undertaken reconciliations of smaller, higher-risk NHSSS and STSS employers (2009/10) and of the main NHS Boards (2010/11) with plans to cover local authorities for 2011/12 in Q3 of 2012/13. The reconciliation exercises have proved difficult and time-consuming and the Agency were unable to reconcile contributions for teachers due to difficulties with leaver information. Despite this it is recognised that the reconciliation process plays an important contribution to controls over contribution receipts.
38. SPPA met with both internal and external audit and agreed that the existing process of reconciliations would continue, with targets and timescales agreed in consultation with Audit Scotland. In the longer term, consideration also needs to be given to the timing and content of employers' annual returns, taking account of relevant governance requirements imposed by the Pensions Regulator arising from pension reforms.

Refer Action Plan No. 2

SPPA financial position

39. Audited bodies are responsible for conducting their affairs and for putting in place proper arrangements to ensure that their financial position is soundly based.
40. We consider whether audited bodies have established adequate arrangements and examine:
- financial performance in the period under audit
 - compliance with any statutory financial requirements and financial targets
 - ability to meet known or contingent, statutory and other financial obligations
 - responses to developments which may have an impact on the financial position
 - financial plans for future periods.
41. These are key areas in the current economic circumstances. This section summarises the financial position and outlook for the organisation.

Financial results 2011/12

Annual outturn

42. SPPA's net operating costs during 2011/12 were £10.4 million and capital expenditure was £0.2 million. Net funding of £9.1 million was received from the Scottish Consolidated Fund.
43. Net operating costs have increased by £0.075 million in 2011/12. Increases in staff costs of £0.175 million and general administration costs of £0.073 million were partly offset by an increase in operating income of £0.116 million.

Budgetary control

44. Overall, SPPA operated within the budget limits set by the Scottish Government with a net underspend of £0.7 million (6%) against the budget of £11.3 million. See Exhibit 1 below.

Exhibit 1: Performance against resource budget 2011/12

Limits	Budget £ million	Outturn £ million	Difference £ million
Operating	10.8	10.4	0.4
Capital	0.5	0.2	0.3
Total	11.3	10.6	0.7

Source: SPPA annual accounts 2011/12

45. We have reviewed SPPA's budget setting and monitoring arrangements, which we found to be satisfactory. Senior management receive budget monitoring reports on a regular (monthly) basis and Director of Finance Reports are provided to each meeting of the External Management Board and the Audit and Risk Committee.

Financial position

46. SPPA's statement of financial position shows a net asset position of £5.3 million as at 31 March 2012. This compares to a net asset position of £6.3 million the previous year, reflecting the cost of depreciation charged on IT Software and the disposal of IT equipment.

Public reporting

47. Some commentary on the underlying financial picture is summarised in the annual report section of the annual report and accounts document. This is available on SPPA's website at www.sppa.gov.uk. There is scope to expand financial commentary in future years to explain more fully the financial pressures facing the organisation and how these have been managed during the year.

Financial planning to support priority setting

48. The Scottish Government publication *Spending Review 2011* sets out SPPA's spending plans for 2012-15. Provisional allocations indicate that SPPA will receive modest budget increases in both 2013/14 and 2014/15 as shown in Exhibit 2. The increase in budget recognises the significant challenges facing SPPA over the next few years as a result of the UK government's pension reform proposals.

Exhibit 2: SPPA's funding allocations 2012-2015

	2012/13 £ million	2013/14 £ million	2014/15 £ million
Running costs	11.5	11.9	12.6
Capital	0.5	1.1	1.2
Total	12.0	13.0	13.8

Source: Scottish Spending Review 2011

Workforce planning

49. A recent staffing review identified a number of emerging issues within the Agency, including:
- pressures in Policy and Finance Directorates arising from the pension reform agenda and the need to more proactively manage the audit/risk management and business improvement agendas

- over-reliance on key individuals in some specialist areas, particularly in Finance and Policy
 - succession planning issues which may impact on the ability to deal with the pension reform agenda and related governance issues as well as the loss of expertise at Senior Management Team level
 - the need to ensure that the Agency has sufficient resources to consider its role in a post referendum landscape which could fundamentally change the work of the SPPA.
50. In response to the increasing demands on the service, the Agency has received an increase in its revenue budget for the period up to 2014/15. This has allowed it to recruit a number of additional staff, helping it to build capacity and resilience.

Outlook

2012/13 budget

51. Scottish Ministers have agreed a resource budget for the SPPA of £12.0 million for 2012/13. This comprises operating expenditure of £11.5 million and capital expenditure of £0.5 million. This represents an increase of £1.4 million or 13.2% from 2011/12 (Exhibit 2).
52. During this period, operational caseloads are expected to increase as a result of increases in longevity and workforce changes within the NHS and teaching professions. The Agency therefore faces significant challenges in order to maintain the quality and effectiveness of its core pensions administration service during this period.
53. The task is made even more challenging by the scale and ambition of the pension reform agenda. The fundamental redesign of the way the schemes are structured, financed and governed will present significant policy and operational challenges for the Agency. The Agency will be required to develop appropriate business processes as well as ensure that its IT systems are sufficiently developed to deliver them.

Schemes' financial position

Financial results 2011/12 - NHSSS

Outturn 2011/12

54. The NHSSS had net expenditure for the year of £1,603 million, compared to net income of £1,671 million in 2010/11. This movement is due mainly to the change in indexation from retail price index (RPI) to consumer price index (CPI) in 2010/11 which resulted in a £3.3 billion reduction in the 2010/11 scheme liability. The scheme liability has increased by £1.2 billion (5.0%) from £24.1 billion to £25.3 billion. The increase is due largely to changes in actuarial assumptions, experience gains/(losses) on scheme liabilities and interest on scheme liabilities.
55. In accounting for pensions, International Accounting Standard 19 (Employee Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if actual payment will be made in future years. This requirement results in very large future liabilities being recognised in financial statements. In summary, the IAS 19 liability has moved as shown in Exhibit 3 since the standard was first introduced in 2003/04.

Exhibit 3: NHSSS IAS 19 liability (£ billion)

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
	£billion	£billion	£billion	£billion	£billion	£billion	£billion	£billion	£billion
IAS 19 Liability	11.6	12.7	16.2	21.9	21.1	19.4	28.2	24.1	25.3

Source: NHSSS published accounts from 2003/04 to 2011/12

Financial results 2011/12 - STSS

Outturn 2011/12

56. The STSS had net expenditure for the year of £1,375 million, compared to net income of £811 million in 2010/11. This movement is due mainly to the change in indexation from retail price index (RPI) to consumer price index (CPI) in 2010/11 which resulted in a £2.1 billion reduction in the 2010/11 scheme liability. The scheme liability has increased by £1.6 billion (7.3%) from £22.0 billion to £23.6 billion. The increase is due largely to changes in actuarial assumptions, experience gains/(losses) on scheme liabilities and interest on scheme liabilities.
57. In summary, the IAS19 liability has moved as set out in Exhibit 4 since 2003/04:

Exhibit 4: STSS IAS 19 liability (£ billion)

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
	£billion	£billion	£billion	£billion	£billion	£billion	£billion	£billion	£billion
IAS 19 Liability	10.7	12.4	14.6	18.7	19.3	18.4	24.4	22.0	23.6

Source: STSS published accounts from 2003/04 to 2011/12

Outlook

58. The pension schemes are funded from Annually Managed Expenditure, funded separately by Treasury from the Departmental Expenditure Limit settlement and, as such, variations in the scheme expenditure do not have to be balanced by adjustments elsewhere in the Scottish Budget. Budgets are subject to regular revision to meet the requirements of HM Treasury, the Office of Budget Responsibility and the Scottish Government.
59. In 2011/12 both schemes recorded an excess of payments over contributions of £306 million combined.

Pensions reform

60. The Hutton review of public sector pension schemes was commissioned by the UK Government and forms the basis of major reforms proposed by the government to all public sector schemes across the UK. The first of these changes has already been implemented, changing the annual indexation of pension payments and liabilities, from RPI to CPI. The government has also announced that employee contributions for some of the larger unfunded schemes should increase by an average of 3.2% of pay by April 2014, with the increase being implemented in stages commencing April 2012. These proposals are being applied to both STSS and NHSSS, with further major reforms anticipated.
61. The pension reform agenda presents a significant challenge for SPPA, especially in terms of resourcing the additional work load involved at a time when the public sector is under pressure to reduce costs. In recognition of these circumstances, the Scottish Government has agreed an increase in SPPA's budget provision over the current spending review period, with the possibility that additional funding may be required beyond that period. Nevertheless, the changes proposed will require strong financial and operational management within SPPA if they are to be delivered on time and within budget limits.

Governance and accountability

Corporate Governance

62. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all audited bodies, whether their members are elected or appointed, or whether they comprise groups of people or an individual accountable officer.
63. Through its chief executive or accountable officer, each body is responsible for establishing arrangements for ensuring the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies usually involve those charged with governance (including audit committees or similar groups) in monitoring these arrangements.
64. Consistent with the wider scope of public audit, we have a responsibility to review and report on audited bodies' corporate governance arrangements as they relate to:
 - corporate governance and systems of internal control
 - the prevention and detection of fraud and irregularity
 - standards of conduct and arrangements for the prevention and detection of corruption.
65. In this part of the report we comment on key areas of governance.

Overall effectiveness

66. We found that overall, corporate governance arrangements operated effectively during 2011/12. A recent review by Internal Audit of the governance structure and framework provided substantial assurance on the arrangements in place and made a number of minor recommendations for improvement. In particular, that SPPA should introduce a formal and rigorous assessment of the Board's performance to confirm that Members continue to discharge their duties effectively.

Management structure

67. The Chief Executive of SPPA is the Accountable Officer responsible for the administration of SPPA. The role of the Accountable Officer is supported by an External Management Board comprising four non-executive directors. There is also an Audit and Risk Committee (A&RC) comprising three non-executive directors. The Board and the A&RC meet four times annually.
68. There is also a Senior Management Team (SMT) comprising the directors of SPPA which is chaired by the Chief Executive. The SMT meets fortnightly as part of the Agency's formal monitoring and accountability processes.

Internal control

69. While we concentrate on significant systems and key controls in support of the opinion on the financial statements, our wider responsibilities require us to consider the financial systems and controls of audited bodies as a whole. The extent of this work is informed by our assessment of risk and the activities of internal audit.
70. Overall the systems of internal control were operating effectively during 2011/12. This enabled us to take the planned assurance on these systems for the audit of the financial statements. There were no major findings from our review of internal control systems, however, we identified a small number of control weaknesses where improvements could be made to existing arrangements. Management have responded positively to our findings.
71. As part of our risk assessment and planning process, the Scottish Government external audit team assessed the Scottish Government's Internal Audit Division who also acts as the SPPA's internal auditors. They concluded that internal audit operates in accordance with the Government Internal Audit Manual. In their annual report for 2011/12, internal audit were able to provide substantial assurance in respect of SPPA's risk management, control and governance arrangements.

Governance statements

72. In 2011/12 SPPA, NHSSS and STSS included a governance statement in their annual accounts for the first time. In accordance with Scottish Government guidance, this included description and assessment of the essential components of corporate governance and details of any significant risk-related matters arising during the period.
73. Arrangements to prepare the statements are generally satisfactory and include Directors submitting a certificate of assurance, supported by a completed checklist, to the accountable officer covering the key systems for which they are responsible. Assurances were also received from the Scottish Government's Director General Finance in respect of the financial systems shared with SPPA, and from the Scottish Government's Director General Governance and Communities in respect of the Scottish Government's HR and payroll systems that are shared with SPPA. This process provides management assurances to the accountable officer that there are no significant control weaknesses that should be reported in the statement. There are no significant exceptions reported in the governance statement.
74. The External Management Board and the Audit and Risk Committee have both carried out a self-assessment of their effectiveness during 2011/12 using criteria set by the Scottish Government. Both concluded that they were effective in carrying out their functions.

Prevention and detection of fraud and irregularities

75. SPPA is responsible for establishing arrangements to prevent and detect fraud and other irregularity. We review and report on these arrangements.
76. The SPPA has appropriate arrangements in place to help prevent and detect fraud and irregularities which follow Scottish Government's guidance. The Agency's Fraud Policy and

Whistleblowing Policy are available to all staff via the intranet. The Agency's website also includes a link for dealing with complaints and staff are aware of procedures to be followed when dealing with complaints, suspected fraud and breaches of proper standards.

- 77. The Agency communicates its Code of Conduct to staff in their contracts of employment and the Staff Handbook which is issued to new staff. Standards of conduct and the Disciplinary Policy are available on the intranet and reminders are issued to staff periodically or when changes are made.

NFI in Scotland

- 78. SPPA participates in the National Fraud Initiative (NFI). This is a counter-fraud exercise that uses computerised techniques to compare information about individuals held by different public bodies to identify circumstances that might suggest the existence of fraud or error (matches). Where matches are identified public bodies are expected to investigate these and if fraud and error has taken place, to stop payments and attempt to recover the amounts involved. The exercise also provides assurance on the effectiveness of arrangements and helps deter fraud. SPPA is well-organised in its approach to the NFI exercise and has built up considerable experience in investigating cases.
- 79. The value of overpayments identified by SPPA through the NFI exercise has fallen significantly over the course of the past four exercises as shown in Exhibit 5, as issues are identified and addressed. In the 2010/11 exercise a total of 5,749 cases were identified for consideration. After filtering, 1,574 cases were identified for further investigation. Of the data matches processed in respect of death information, 86 cases were identified with overpayments totalling £127k. Nine re-employment cases have been processed, involving overpayments of £38k. A further 22 re-employment cases remain under investigation.

Exhibit 5: SPPA NFI overpayments

	2004-05	2006-07	2008-09	2010-11
Overpayments identified	£5.3m	£2.3m	£565k	£127k

Source: Director of Finance Report to A&RC 17 July 2012

- 80. Using the industry-standard methods deployed under NFI, SPPA has estimated total and forward savings in 2010/11 of £4.4 million. This compares with £1.8 million in 2006/07, and £0.4 million in 2008/09. The spike in 2010/11 is the result of the inclusion for the first time of teachers in re-employment checks. To date no prima facie instance of fraud has been identified relating to payments by SPPA.
- 81. Results were published by Audit Scotland in May 2012 in a report on the NFI. This highlighted that fraud, overpayments and recoveries totalling £19.8 million had been identified across Scotland in the most recent exercise and outcomes of £78 million had been achieved since NFI was first introduced. The report also contained a self-appraisal checklist that all participants are recommended to use prior to the start of the next exercise in October 2012.

Standards of conduct and arrangements for the prevention/detection of bribery and corruption

82. 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 consider whether bodies have adequate arrangements in place.
83. SPPA has adequate arrangements in place to help ensure appropriate standards of conduct and to help prevent and detect bribery and corruption. We are not aware of any specific issues that we need to identify in this report.
84. The Audit and Risk Committee considered and approved the Agency's Bribery Policy on 3 April 2012 which is published on the intranet. A programme of staff awareness is being implemented, including the policy being explained to all staff through routine team meetings during the quarter ending 31 December. Staff will be made aware of the actions that they should take if they suspect bribery or fraud. A Register of Board Members' Interests is maintained by the Chief Executive's office and is available for public inspection. Arrangements are in place for Board Members to confirm their position annually.

Outlook

85. The current environment of significant organisational change, reducing resources and increasing expectations is one in which the organisation's governance and accountability arrangements are likely to be tested. It is important that the Agency maintains a proactive approach to reviewing and improving its governance and internal control arrangements and continues to work hard to address any identified weaknesses.

Best Value, use of resources and performance

86. Audited bodies have responsibility to ensure that arrangements have been made to secure best value. The Auditor General may require that we consider whether accountable officers have put in place appropriate arrangements to satisfy their corresponding duty of best value. Where such requirements are not specified we may, in conjunction with audited bodies, agree to undertake local work in this area.
87. As part of their statutory responsibilities, the Auditor General may procure, through Audit Scotland, examinations of the use of resources by audited bodies and publish reports or guidance. We may be requested from time to time to participate in:
- a performance audit which may result in the publication of a national report
 - an examination of the implications of a particular topic or performance audit for an audited body at local level
 - a review of a body's response to national recommendations.
88. During the course of our audit appointment we also consider and report on progress made by audited bodies in implementing the recommendations arising from reviews in earlier years. We may also consider the use of resources in services or functions, where the need for this is identified through local audit risk assessments.
89. This section includes a commentary on the best value and performance management arrangements within SPPA. We also summarise headline performance measures used by SPPA, highlight any relevant national reports and comment on the body's response to these.

Management arrangements

Best Value

90. Scottish Government guidance for accountable officers on best value in public services requires a systematic approach to self-evaluation and continuous improvement. The guidance identifies the themes an organisation needs to focus on in order to deliver the duty of best value, but notes that implementation should be appropriate and proportionate to the priorities, operating environment, scale and nature of the body's business.
91. The Agency's approach to Best Value is described in the Governance Statement. This highlights that Best Value principles are embedded in the Agency's planning, governance and business decision arrangements; and are communicated to staff through commitment, leadership and staff participation in the business planning process. It also highlights the contribution made by its participation in a variety of benchmarking activity.

92. The Agency is seeking to improve its arrangements across the range of its activities, including:
- the continuing integration of NHSSS and STSS Operational functions
 - development of an electronic pensions contributions interface with employers
 - development of web services for pensioners
 - development of a new automated process for handling death cases in payroll
 - a project to ensure that records of preserved members are accurate and up-to-date
 - a data cleanse project.

Overview of reported performance in 2011/12

93. The Agency reported that it had met 84% of the corporate targets set for 2011/12. When adjusted to exclude those targets which were not achieved as the result of circumstances outwith the Agency's control, for example policy decisions made by the UK Government, then the Agency reported that it had achieved 90% of its targets.
94. Reported performance at a Directorate level was more mixed. Operations met all of their targets except for one. Corporate Services met the majority of their targets with the exception of that relating to the provision of IT, which had been affected by a three day IT failure. Finance met 15 out of 18 targets. Policy missed a greater proportion of targets than other Directorates. The Agency reported that this was largely due to the volatile nature of the pension reform agenda and a significant increase in the amount of Ministerial correspondence.

National performance reports

95. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. Reports in the last year of direct interest are detailed in Exhibit 7.

Exhibit 7: A selection of national performance reports 2011/12

- | | |
|--|--|
| <ul style="list-style-type: none">• Managing ICT Contracts: an audit of three public sector programmes• The National Fraud Initiative in Scotland | <ul style="list-style-type: none">• Scotland's Public Finances - addressing the challenges |
|--|--|

Source: www.audit-scotland.gov.uk

Managing ICT contracts: an audit of three public sector programmes

96. Audit Scotland found significant weaknesses in the management of three public sector information and communication technology (ICT) programmes costing a combined £133 million so far. The report considers the management of important ICT programmes that were delayed, cancelled or overran on costs.

97. The report says many of the problems stemmed from a lack of specialised information technology skills and experience. But there were also weaknesses in basic project management and control, and the 'Gateway' system that the Scottish Government uses to provide assurance on the management of projects was not always effective. We recommended that the Scottish Government should consider the benefits that could be achieved by providing a central resource of specialised ICT expertise and advice for public bodies undertaking such programmes. The government also needs to comprehensively review how it can best support and oversee public bodies undertaking significant ICT programmes.
98. This report is of particular relevance to SPPA given the change agenda likely to result from pension reform and the potential for significant continuing ICT investment. SPPA should ensure that it makes use of the questions in Appendix 1 of the national report to help scrutinise and challenge the management of ICT programmes.

Arrangements to consider national performance reports

99. In line with best practice, national reports are considered by the Senior Management Team and presented to the External Management Board and A&RC where these are considered to be relevant to the activities of the Agency.

Outlook

100. In April 2011, the Equality Act 2010 introduced a new public sector 'General Duty' which encourages equality to be mainstreamed into public bodies' core work so that it is not a marginal activity but part and parcel of how public bodies operate. Following on from this the Scottish Government consulted on a set of 'Specific Duties' which came into force in May 2012. There are nine specific duties listed which aim to support public bodies to better perform against the 'General Duty,' including the duty to assess the impact of equalities in all policies and decisions as well as the requirement to publish a set of equality outcomes (and reporting requirements) no later than 30 April 2013.

Appendix A: audit reports

External audit reports and audit opinions issued for 2011/12

Title of report or opinion	Date of issue	Date presented to Audit Committee
Annual Audit Plan – SPPA, NHSSS, STSSS	22 March 2012	3 April 2012
Review of internal controls	31 May 2012	17 July 2012
Report on financial statements to those charged with governance - SPPA	4 July 2012	17 July 2012
Audit opinion on the 2011/12 financial statements-SPPA	4 July 2012	17 July 2012
Report on financial statements to those charged with governance -Schemes	2 October 2012	9 October 2012
Audit opinion on the 2011/12 financial statements-Schemes	2 October 2012	9 October 2012

Appendix B: action plan

Key Risk Areas and Planned Management Action

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1	<p>NHSSS legacy refunds</p> <p>The Agency should introduce procedures for identifying when a member has reached the point where they should be moved from the 'undecided leavers' category to the 'legacy refunds' category.</p> <p>Risk. The extent of potential liabilities may not be fully recognised.</p>	<p>SPPA will investigate the introduction of a report to identify those NHS members who have left the scheme with less than 2 years service and who may be due a legacy refund. These cases will be processed on an ongoing basis.</p>	Director of Operations	May 2013
2	<p>Contributions reconciliations</p> <p>SPPA recognises the importance of reconciling employers' actual contributions with data derived from employers' annual returns. As previously discussed, detailed proposals for undertaking reconciliations on a rolling basis should be prepared and formally agreed with both internal and external audit.</p> <p>Risk. Failure to formalise the process for reconciling contributions may mean these are given insufficient priority within the Agency, particularly when staff resources are under pressure.</p>	<p>SPPA will set out a detailed programme of 2012-13 reconciliations for completion by 31 March 2013, to be agreed with Audit Scotland and Internal Audit by 15 January 2013.</p>	Director of Finance	15 January 2013