

The Scottish Housing Regulator

Annual report on the 2012/13 audit



Prepared for members of The Scottish Housing Regulator and the Auditor General for Scotland
September 2013

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. It provides services to the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Government and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

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Key Messages

2012/13

We have given an unqualified opinion that the financial statements of The Scottish Housing Regulator (SHR) for 2012/13 give a true and fair view of the state of the body's affairs and of its net expenditure for the year.

Expenditure for the year was £3.7m, which is less than the budget of £4m. During the year SHR identified savings and was able to return funding to the Scottish Government of £150,000.

In 2012/13 there were four Board members and this increased to eight from April 2013.

The early period of any new board requires time for non-executives to understand the business and both them and senior management to settle into the new roles. The level of challenge and discussion by non-executives on the Audit and Risk Assurance Committee has been high and relations among non-executives, officers and both internal and external audit are positive and constructive.

Overall SHR's arrangements for the prevention and detection of fraud were satisfactory during 2012/13. From our review of the key controls within the main financial systems, we concluded the systems of internal control are operating effectively.

In 2012 SHR agreed to carry out a series of seven best value reviews over the three-year period of the 2012-2015 Corporate Plan, with the first (Strategic Vision and Corporate Governance) being concluded and reported on back to the Audit and Risk Assurance Committee in April this year.

Outlook

The economic climate for social housing continues to be very difficult with growing demands on services due to welfare reform, alongside pressures on finances for registered social landlords. The regulatory work of SHR continues with a focus on service quality for all landlords and good governance and financial health for RSLs.

A priority for 2013/14 is the implementation of the replacement business intelligence system. SHR has been awarded additional funding for the project in 2013/14 and progress is monitored by a separate project board.

It will be a challenge to achieve the right balance of time and resources to manage delivery of both the regulatory work, in light of the pressures for the sector, and the internal IT project, as implementing IT systems has been shown to be difficult in other public sector organisations.

Introduction

1. This report is the summary of our findings arising from the 2012/13 audit of The Scottish Housing Regulator (SHR). The purpose of the report is to set out concisely the scope, nature and extent of the audit. It summarises our opinions (i.e. on the financial statements) and conclusions on significant issues arising.
2. The report also reflects our overall responsibility to carry out an audit in accordance with the public sector audit model which is based on the Code of Audit Practice prepared by Audit Scotland (May 2011). This sets out the wider dimensions of the public sector audit which involves not only the audit of the financial statements but also consideration of areas such as financial performance and corporate governance. An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements prepared by management; however this does not relieve management of their responsibilities in this respect. This report has been prepared for the use of SHR and no responsibility to any third party is accepted.
3. [Appendix A](#) 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 SHR understands its risks and has arrangements in place to manage these risks. Members should ensure that they are satisfied with the proposed management action and have a mechanism in place to assess progress.
4. This report is also addressed to the Auditor General for Scotland and will be published on our website after consideration by SHR's Audit and Risk Assurance Committee.

Financial statements

Conduct and scope of the audit

5. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in the Annual Audit Plan presented to the Audit and Risk Assurance Committee on 2 April 2013, and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in May 2011.
6. As part of the requirement to provide full and fair disclosure of matters relating to our independence we can confirm that we have not undertaken non-audit related services. The 2012/13 agreed notional fee for the audit was disclosed in the Annual Audit Plan and as we did not require to carry out any additional work outwith our planned audit activity this fee remains unchanged.

Audit opinion and accounting issues

7. We have given an unqualified opinion that the financial statements of SHR for 2012/13 give a true and fair view of the state of the body's affairs and of its net expenditure for the year. The audit opinion was formally issued and signed on 23 August 2013.
8. We received the unaudited financial statements on 13 May 2013 in accordance with the agreed timetable. The working papers (also received by 13 May) were of a high standard and the staff provided good support to the audit team and we completed our on-site fieldwork on 24 May 2013. SHR is required to follow the 2012/13 Government Financial Reporting Manual and we can confirm that the financial statements have been properly prepared in accordance with these accounting requirements.

Significant findings (ISA260)

9. During the course of the audit we identified no significant issues regarding the appropriateness of accounting policies or accounting estimates and judgements, the timing of transactions, the existence of material unusual transactions or the potential effect on the financial statements of any uncertainties.

Financial position

2012/13 Outturn

10. The main financial objective for SHR is to ensure that the financial outturn for the year is within the resource budget allocated by Scottish Ministers.
11. SHR operated within the resource budgets for 2012/13 as detailed in Table 1 below which also shows the budget changes that occurred during the financial year.

Table 1: Annual Budget

	Opening Budget	Revised Budget	Actual Outturn	Under / (Over) spend
Resource DEL	£4m	£3.85m	£3.7m	£0.15m

Source: SHR Annual Report and Accounts 2012/13; SHR budget monitoring reports

12. During the year the SHR Board was provided with regular budget monitoring reports which highlighted forecast year-end under-spends. The level of underspend reported to the March 2013 Board meeting (based on the period until the end of February) was circa £240,000 compared to the actual year-end position of £300,000, against the opening budget. The main area of under-spend related to staff costs due to the pace of recruitment being different from that anticipated.
13. In addition, SHR provided the Scottish Government with periodic updates on its forecast budget outturn position during the year, outlining at an early point in time that funding would be 'returned' in 2012/13. The Board approved the return of £100,000 in January 2013 and a further £50,000 in February.
14. This underspend was achieved in a year where a new staffing structure was agreed and implemented. In addition the planning stage for the replacement business intelligence system began and a number of stakeholder engagement events and training courses for staff were undertaken.
15. At the request of the Board, SHR commissioned an external firm of accountancy advisers to review the budget monitoring reports. This was reported back to the Board in January 2013 with a number of recommendations to enhance existing arrangements that are now being implemented.

2012/13 financial position

16. The Statement of Financial Position reports closing net liabilities balance of £463,000 (2011/12; £499,000). As noted in the accounting policies, this is because the accounts are based on an accruals basis whereas the funding from the Scottish Government is on a cash basis. Also, since SHR has a very small level of assets, it is always likely that a net liability position will be reported. The budget position referred to previously provides a more meaningful indicator, showing SHR are managing resources within their budget.

Public reporting

17. One of Audit Scotland's current priorities is to consider transparency and completeness of financial reporting to board members and the public and to consider if management commentaries in financial statements are used to clearly explain the financial position.

18. In our 2011/12 annual audit report we commented that the management commentary in the financial statements contains a short paragraph comparing current-year spend to the budgeted amount and that this could be expanded in future years to better explain financial performance.
19. For 2012/13, due to the nature of the movements from prior year, explanations against comparative agency costs were included directly below figures in the notes to the accounts. From 2013/14 officers will be able to report comparative information more simply allowing them to consider how the management commentary could be used to include explanations on financial spend across SHR's regulatory work and IT system implementation.

Refer to action plan no. 1

Financial planning

20. An initial 2013/14 budget report was submitted to the SHR Board in March 2013 for discussion and comment. A revised budget paper was then submitted to the next Board meeting in April where it was subsequently approved. The overall budget for the year is £3.8m as compared to a budget of £4.0m in 2012/13 (although as noted previously actual expenditure was only £3.7m). SHR reviewed its budget headings for 2013/14 in line with its priorities and the budget also includes a contingency element for IT costs for legacy systems.
21. SHR made a successful bid to Scottish Ministers for funding to develop a replacement business intelligence system. The new system is scheduled to go live from 1 April 2014.
22. From the 2013/14 revised budget paper (presented to the Board in April 2013) it was confirmed that a project budget will be monitored and reported on separately from other costs, given the nature and scale of the project.
23. Accounting for expenditure on large IT systems can be complex dependent on the stage of the project and classifications over what might be assessed as capital and revenue spend under accounting standards adopted for the financial statements. There is a risk that year-end financial accounting could be different from in-year management accounting; for example, some staff costs on the project might be included in capital additions and not staff costs through the operating cost statement. We will follow-up this issue with officers as part of our planning for 2013/14.

Refer to action plan no. 2

Corporate governance and systems of internal control

Overall governance arrangements

24. The Code of Audit Practice gives auditors a responsibility to review and report on audited bodies' corporate governance arrangements and overall we found SHR had good governance arrangements in place which included (in addition to the Board) an Audit and Risk Assurance Committee as well as a project board for the ongoing IT project to replace the current

business intelligence systems. These arrangements appear appropriate for a body such as SHR.

25. The early period of any new board requires time for non-executives to understand the business and both them and senior management to settle into the new roles. From an external audit perspective the level of challenge and discussion by non-executives on the Audit and Risk Assurance Committee has been found to be high. We consider the level of past experience and knowledge brought to the Committee by the non-executives was of a high standard and with good relevance to the work of SHR. The addition of two new members in 2013 added a greater level of financial expertise to the Board and the Audit and Risk Assurance Committee. Relations among non-executives, officers and both internal and external audit are positive and constructive.
26. The October 2012 Board meeting minutes record that staff observers found the challenge at Board level was good and were impressed by the different experience which members brought to the meetings. It was also noted that staff members found it useful to see connections between their work and the work of the Board.

Accounting and internal control systems

27. While auditors concentrate on significant systems and key controls in support of the opinion on the financial statements, their wider responsibilities require them to consider the financial systems and controls of audited bodies as a whole. However, the extent of this work should also be informed by their assessment of risk and the activities of internal audit. In addition, as SHR makes use of some of the financial systems provided by the Scottish Government, we have also considered the opinion of their external auditors (also Audit Scotland).
28. No material weaknesses in the accounting and internal control systems were identified during the audit of either SHR or Scottish Government which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.
29. SHR has been managing on-going business continuity risk to the regulation work as the current business intelligence systems (due to be replaced from 2013/14) continue to be used. Unforeseen problems are possible with such aged systems and this has been recognised by officers; contingency arrangements have been agreed, with a former Scottish Government IT officer now employed directly to work for SHR.
30. Internal audit is an important element of SHR's governance structure. Our review established that the work of internal audit is of a good quality allowing us to place reliance on their work on corporate governance. We liaised with internal audit throughout the year to avoid duplication of work.

Partnership working

31. In our 2011/12 annual audit report we raised a point about the lack of service level agreements with the Scottish Government for the range of services provided. We are aware

of the work by SHR's officers to engage with the Scottish Government in order to progress this issue but they are still not finalised. The unexpected increase in accommodation costs part way through 2012/13 highlight the risks to budgets of service level agreements not being in place.

Refer to action plan no. 3

Prevention and detection of fraud and irregularity

32. In our Annual Audit Plan we highlighted the responsibility audited bodies have for establishing arrangements to prevent and detect fraud and other irregularities. In our opinion SHR's overall arrangements for the prevention of fraud are satisfactory, although it should be noted that no system can eliminate the risk of fraud entirely. We have been informed that there have been no frauds in relation to the SHR in 2012/13.

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

33. 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. Auditors consider whether bodies have adequate arrangements in place. No issues have been identified by us for inclusion in this report.

Best value

Best value

34. Achievement of best value or value for money depends on the existence of sound management arrangements for services, including procedures for planning, appraisal, authorisation and control. Audited bodies are responsible for ensuring that these matters are given due priority and resources, and that proper procedures are established and operate satisfactorily. 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 SHR agree to undertake local work in this area.
35. In 2012 SHR agreed to carry out a series of seven best value reviews over the three-year period of the 2012-2015 Corporate Plan, with the first (Strategic Vision and Corporate Governance) being concluded and reported on back to the Audit and Risk Assurance Committee in April this year. These reviews have been developed locally by SHR with reference to the best value toolkits produced by Audit Scotland. We consider that this is a proportionate and appropriate approach.
36. The first self-assessment review reported SHR's position against a number of areas (with supporting evidence referred to) and highlighted improvement actions which had been identified including improving internal communication and recording and sharing lessons

learned from regulatory engagement activities. This style of reporting allows for detailed analysis of the work undertaken and supports any recommended actions which flow from the review.

National report - Housing in Scotland

37. In July 2013 the Accounts Commission and the Auditor General for Scotland published its report *Housing in Scotland* which highlighted that the supply of housing is not meeting current levels of need and Scottish Government housing budgets have fallen and funding for new homes has been particularly affected. SHR played an integral part in the study and the Director of Regulation, Finance & Risk Division was a member of the advisory group. The report concluded that effective leadership is required at a national and local level to ensure housing is well planned and linked to other policy areas and made a number of recommendations to both the Scottish Government and local authorities. Audit Scotland presented the findings to the August 2013 Board meeting; there were no specific recommendations for SHR but the Board discussed in detail the wider implications for the sector.

Acknowledgements

38. We would like to express our thanks to the staff of SHR for their help and assistance during the audit of this year's financial statements which has enabled us to provide an audit report within the agreed timetable.

Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1	19	<p>Public reporting</p> <p>The management commentary in the financial statements is an opportunity to explain financial movements and developments to enhance reporting of financial performance over and above the financial statements.</p> <p><i>Risk - for 2013/14 the management commentary is not developed to help explain the financial performance.</i></p>	Like for like comparisons in the management commentary in 2012/13 would have been difficult given our transition. We will be able to provide a fuller and more meaningful comparison in 2013/14.	Andy Munro, Head of Planning and Performance	May / June 2014 (for submission with draft accounts)
2	23	<p>Financial accounting for capital IT projects</p> <p>Financial accounting for large IT projects can be complex and may be different from in-year management accounting.</p> <p><i>Risk - Without early research into accounting for IT projects under International Financial Reporting Standards, SHR might not understand and plan for the different reporting of the IT costs.</i></p>	We are monitoring our revenue budget separately from our capital allocation from the Scottish Government for our business intelligence system, both for ongoing budget management purposes and for the annual accounts preparation.	Andy Munro, Head of Planning and Performance	May / June 2014 (for submission with draft accounts)

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
3	31	<p>Service Level Agreements with the Scottish Government</p> <p>As reported last year service level agreements which determine precisely what services are provided, and their cost, have not yet been agreed with the Scottish Government.</p> <p><i>Risk - There may be an unforeseen increase in the cost of services provided by the Scottish Government which is not budgeted for by SHR. There may also be a lack of support in the absence of a service level agreement with limited recourse to resolve issues.</i></p>	<p>SLAs are not common practice in the Scottish Government (SG), and effectively our work has been a pilot. We continue to make progress, and we now have outline SLAs from our IT services and our internal audit service and are working with both these SG services to firm up the SLAs. We are also engaging with the central SG team overseeing the SG corporate development of SLAs.</p>	Andy Munro, Head of Planning and Performance	March 2014