



Scottish Prison

Service

Annual audit report 2014/15

August 2015

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This report will be published on our website after it has been considered by the audit committee. The information in this report may be used by Audit Scotland in any reporting to the Scottish Parliament.

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Key messages

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|  <p>Audit of financial statements</p> | <ul style="list-style-type: none"> • Unqualified independent auditor's report on the 2014/15 financial statements. • On 26 January 2015 the Cabinet Secretary for Justice announced that the plans for a female prison in Inverclyde would not go ahead. The decision resulted in the write off of design costs of £1.3 million and an impairment of the land value of £3.0 million. |
|  <p>Financial management and sustainability</p> | <ul style="list-style-type: none"> • The total underspend, including non-cash DEL, AME and ODEL expenditure, was £29.5 million against a budget of £366.0 million. The majority of this underspend arose from impairment reversals as a result of increases in tender price indices provided by the District Valuer. • The total budget for 2015/16 has increased by £27.1 million to £393.1 million. This includes a capital budget of £40.0 million which has not yet been fully allocated. SPS will need to continue to tightly manage the operating and capital budget to ensure it is able to operate within the total allocation. • We have concluded that SPS has reasonable financial management arrangements in place. |
|  <p>Governance and transparency</p> | <ul style="list-style-type: none"> • SPS recognises it requires to improve its overall governance arrangements and has commenced a short life governance review to address these issues. • A Corporate Risk Manager was appointed in March 2015. Immediate priorities include the implementation of a revised corporate risk register and the preparation of a risk management policy. • SPS systems of internal control operated effectively during 2014/15 with the exception of the payroll system. • There is scope to improve openness and transparency. |

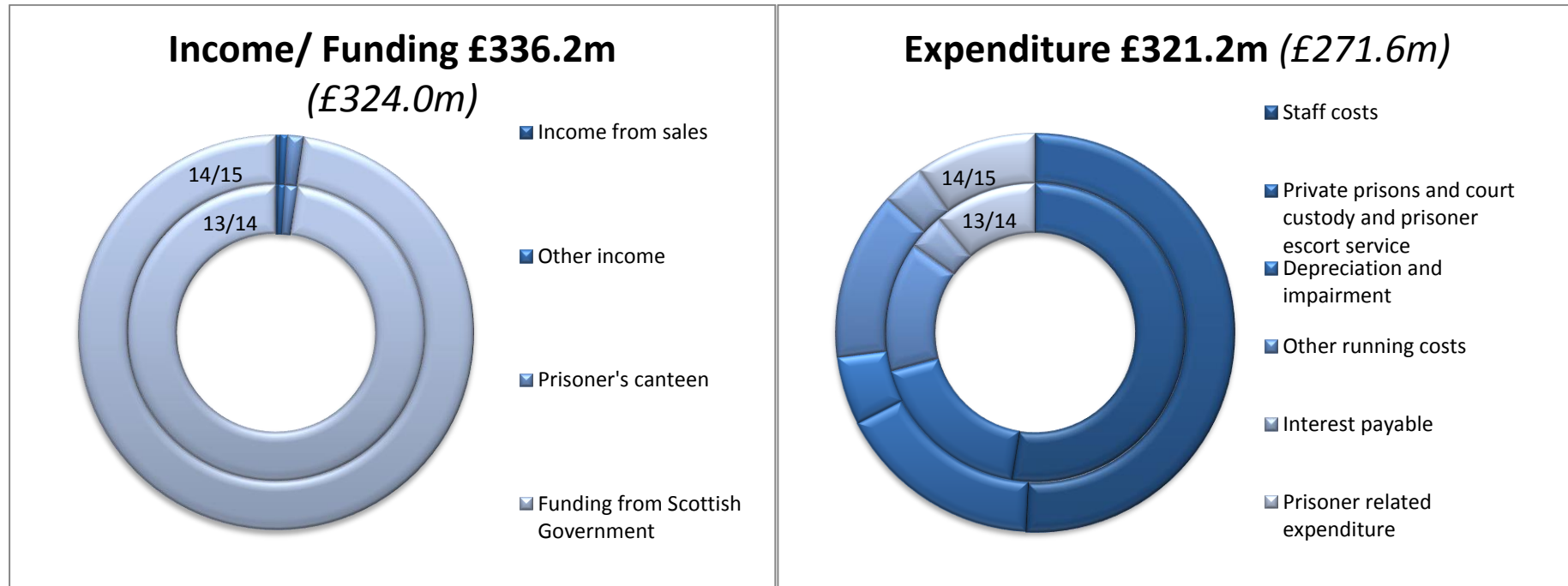
Key Messages

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|  <p>Value for money</p> | <ul style="list-style-type: none">• There has been limited progress in implementing the recommendations from our review of the prison estate capital investment programme.• We will conduct a local study to review workforce planning during autumn 2015. |
|  <p>Outlook</p> | <ul style="list-style-type: none">• SPS should continue to develop its corporate governance model and internal corporate governance framework, including improving organisation-wide risk management arrangements.• Implementation of the change programme arising from the organisational review should remain a key priority.• The Cabinet Secretary for Justice announced the strategy for the management of women offenders on 22 June 2015. SPS needs to work with the Scottish Government and other partner organisations to develop plans for its estate that enable the strategy to be effectively implemented . |

Introduction

1. This report is a summary of our findings arising from the 2014/15 audit of Scottish Prison Service (SPS).
2. The management of SPS is responsible for:
 - preparing financial statements which give a true and fair view, in accordance with the relevant financial reporting framework
 - ensuring the regularity of transactions, by putting in place systems of internal control
 - maintaining proper accounting records
 - preparing and publishing with their financial statements an annual governance statement and a remuneration report
 - preparing a Scottish Government consolidation pack.
3. Our responsibility, as the external auditor of SPS, is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.
4. An audit of 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; that have been prepared by management with the oversight of those charged with governance. This does not relieve management of their responsibility for the preparation of financial statements.
5. A number of reports, both local and national, have been issued by Audit Scotland during the course of the year. The reports relevant to SPS are summarised at [appendices II](#) and [III](#) respectively and include recommendations for improvements.
6. [Appendix IV](#) is an action plan setting out our recommendations to address 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 "Management action/response". We recognise that not all risks can be eliminated or even minimised. What is important is that SPS understands its risks and has arrangements in place to manage these risks. The RMAC should ensure that they are satisfied with proposed action and have a mechanism in place to assess progress and monitor outcomes.
7. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures; consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.
8. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

2014/15 financial statements



Cash funding from the Scottish Government comprises 97% of total income and funding. Scottish Government funding of £328.7 million in 2014/15 is £12.2 million (4%) more than 2013/14 (£316.5 million).

Expenditure in 2014/15 was £321.2 million, an increase of £49.6 million compared to 2013/14 (£271.6 million). The main increases related to staff costs (+£12.8million) and depreciation and impairment (+£32.1 million).

The increase in staff costs was due to the additional staff employed and a one-off payment of £6.5 million.

The increase in depreciation and impairment charges was the result of a reduction in net impairment reversals. In 2014/15 there was an overall depreciation and impairment charge of £17.8 million. In 2013/14 the impairment reversals resulted in a credit of £14.3 million to expenditure.

Audit of the 2014/15 financial statements

Audit opinions

Financial Statements

- The financial statements of SPS for 2014/15 give a true and fair view of the state of the body's affairs and of its net expenditure for the year.
- We confirm that the financial statements have been properly prepared in accordance with the 2014/15 Government Financial Reporting Manual (FReM).

Regularity

- In all material respects, the expenditure and income in the financial statements were incurred or applied in accordance with applicable enactments and guidance.

Other prescribed matters

- The remuneration report to be audited has been properly prepared in accordance with the requirements of the FReM.
- The information in the strategic report and directors' report is consistent with the financial statements.

Audit of the 2014/15 financial statements

Submission of financial statements for audit

9. We received the unaudited financial statements on 19 May 2015 in accordance with the agreed timetable. The working papers were of a satisfactory standard and the staff provided good support to the audit team and we completed our on-site fieldwork on 12 June 2015.

Overview of the scope of the audit of the financial statements

10. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual audit plan presented to the RMAC on 6 March 2015.
11. 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 2014/15 agreed notional fee for the audit was set out in the Annual audit plan and, as we did not carry out any work additional to our planned audit activity, the notional fee remains unchanged.
12. The concept of audit risk is of central importance to our audit approach. During the planning stage of our audit we identified a number of key audit risks which had the greatest effect on the audit strategy, resources and effort. We set out in our Annual audit plan the audit work we proposed to undertake to secure appropriate levels of assurance.

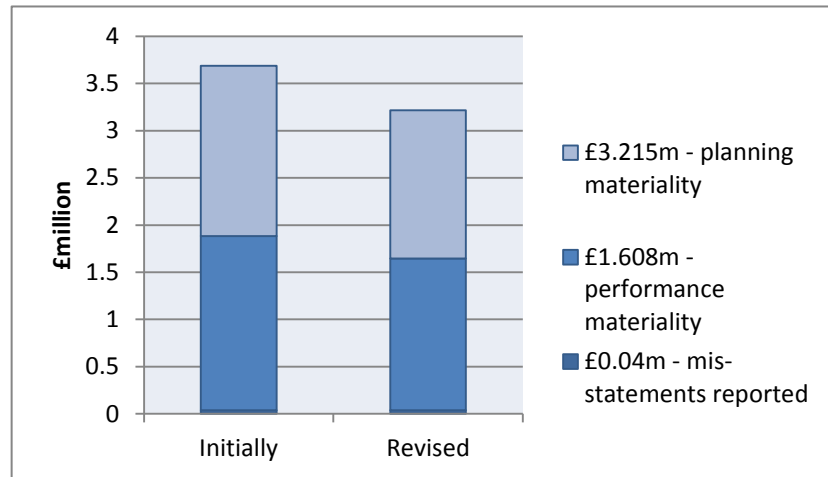
13. [Appendix I](#) sets out the significant audit risks identified at the planning stage and how we addressed each risk in arriving at our opinion on the financial statements.
14. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

Materiality

15. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other qualitative reasons (for example an item contrary to law).
16. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
17. We summarised our approach to materiality in our Annual audit plan. Based on the financial statements, we revised our planning materiality for 2014/15 to £3.2 million (1% of gross expenditure). This reflects a decrease in gross expenditure

Audit of the 2014/15 financial statements

from the Autumn Budget Revision, (the basis of our planning materiality), compared to gross expenditure reported in the financial statements. Performance materiality of £1.6 million is determined to ensure that uncorrected and undetected audit differences do not exceed our planning materiality level. We report all misstatements greater than £40,000.



Evaluation of misstatements

18. All misstatements identified during the audit, which exceeded our misstatement threshold, have been amended in the financial statements.

Significant findings from the audit

19. International Standard on Auditing (ISA) 260 requires us to communicate to you significant findings from the audit:

- the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and disclosures
- significant difficulties encountered during the audit
- significant matters arising from the audit that were discussed, or subject to correspondence with management
- written representations requested by the auditor
- other matters which in the auditor's professional judgment, are significant to the oversight of the financial reporting process.

20. One monetary adjustment and a number of presentational matters were identified within the financial statements during the course of our audit. These were discussed with relevant officers who agreed to amend the unaudited financial statements. The overall effect of the adjustment made to the financial statements is to decrease total comprehensive net expenditure by £0.3 million. Net assets as recorded in the statement of financial position have increased by £0.3 million.

21. A summary of the significant issues that, in our view, require to be communicated to you in accordance with ISA 260 are contained in the following table. As the monetary adjustment referred to above is not significant, this is reported in the section on other accounting issues.

Significant findings from the audit in accordance with ISA260

22. Strategy for the management of female offenders: On 26 January 2015 the Cabinet Secretary for Justice announced that the plans for a female prison in Inverclyde would not go ahead as this did not fit with his vision of how to address female offending in Scotland. As a result, the Scottish Government and SPS undertook an extensive consultation with partners and communities with a view to the development of specific proposals. Given the uncertainty surrounding these proposals at 31 March 2015, the prison estate has been valued on the basis of the position at that time. The Women's Regional Unit at HMP Edinburgh was placed on hold whilst the new proposals were being developed and expenditure incurred to 31 March 2015 (£0.4 million) is included within assets under construction. Land purchased for the development of the female prison in Inverclyde has been valued on the assumption that it is surplus to operational requirements. The remaining life of HMP Cornton Vale was revised from one year to four years, with effect from the February 2015, on the basis that the prison will continue to be used in the short term. On 22 June 2015 the Cabinet Secretary for Justice announced his plans for the future of the custodial estate for women. The announcement confirmed that there would be a new national facility on the site of HMP Cornton Vale and a number of new community custody units across Scotland. The announcement also confirmed that existing plans for the Women's Regional Unit at HMP Edinburgh would not go ahead. The financial statements were updated to include disclosure of this post balance event.

Resolution: We carried out sample testing of land and building valuations, including consideration of the valuation bases adopted for the women's estate. On the basis of the evidence available, we are satisfied that the valuation of the prison estate as at 31 March 2015 is correctly stated. We are also content that the announcement on 22 June 2015 has been appropriately disclosed as a non adjusting post balance sheet event in accordance with *International Accounting Standard (IAS) 10 Events after the reporting period*. SPS should revisit the valuation of the prison estate, in 2015/16, to ensure that it reflects the Cabinet Secretary's confirmed strategy for the management of women offenders.

Refer Action Plan no.1

Significant findings from the audit in accordance with ISA260

23. HMP Inverclyde adjustments: The impact of the ministerial announcement in January 2015 resulted in the write off of design costs for the new female prison in Inverclyde of £1.3 million. Expenditure on design costs up to the date of the announcement were deducted from the value of assets under construction and charged to the Statement of Comprehensive Net Expenditure. Expenditure on demolition and enabling works of £3.3 million was transferred from assets under construction and added to the purchase cost of the land (£2.9 million) on which the new prison was intended to be built, resulting in a value of £6.2 million. The District Valuer carried out an independent valuation of the land, as at 31 March 2015, which resulted in a decrease in the total land value of £3.0 million. This decrease has also been charged to the Statement of Comprehensive Net Expenditure. The total adjustment of £4.3 million is included within the impairment charge disclosed in Note 9 to the accounts.

Resolution: We reviewed the adjustments in relation to the expenditure on design, demolition and enabling works for the female prison in Inverclyde, with reference to *IAS 36 Impairment of assets* and the FReM. We are satisfied that the correct accounting entries have been made and the adjustments have been adequately disclosed.

24. Financial performance: The financial performance information included in the management commentary identifies a total underspend of £29.5 million (8%) against a budget of £366.0 million. The majority of this underspend arises from a negative Annually Managed Expenditure (AME) outturn of £22.2 million against a nil budget. The AME underspend includes net impairment reversals of £16.3 million identified in the impairment analysis at Note 9 to the financial statements. The £4.3 million impairment charge in respect of HMP Inverclyde is excluded from the AME outturn of £16.3 million, which increases the reported net impairment reversals in the financial performance information to £20.6 million. Net impairment reversals were the result of a rise in tender price indices provided by the District Valuer, which determines valuation and indexation movements. The remaining £1.6 million AME underspend relates to miscellaneous provisions.

Resolution: We have carried out sample testing on the valuation movements. We are satisfied that the net impairment reversals are correctly stated in the Statement of Comprehensive Net Expenditure and financial performance disclosures are appropriate.

Significant findings from the audit in accordance with ISA260

25. **One-off operational payment:** Total net staff costs of £163.0 million include a one off payment of £2,000 to each operational member of staff in pay ranges C, D and E. The cost of this payment, excluding national insurance contributions, was £6.5 million. These payments were made to prison officers and operational first line managers following an agreement reached between the Prison Officers Association (Scotland) and SPS. This agreement commits both parties to participate in the development of the prison officer role over the next two years and is intended to avoid the risk of any significant disruption during this period.

Resolution: We reviewed the nature of this expenditure and carried out testing on a sample of payments. We also considered related disclosures in the management commentary and notes to the accounts. We are satisfied that the operational payment has been correctly calculated and has been adequately disclosed in the financial statements.

Other accounting issues

Capital accounting

26. **Assets under construction:** We identified a number of issues in respect of SPS' capital accounting processes and the disclosure of assets under construction movements relating to property, plant and equipment and intangible assets as follows:

- the year-end review of assets under construction to identify completed assets, carried out by finance staff, identified a number of items that should be classified as revenue expenditure. SPS should strengthen controls in relation to the initial recognition and capitalisation of assets under construction

- adjustments to remove revenue items from assets under construction are disclosed as disposals and charged to maintenance costs. Assets under construction which are written off to revenue should be disclosed as impairments
- all building, dwelling and information technology (IT) additions are disclosed as assets under construction additions even where there is no further construction work and the addition is completed within the same year. We were informed that this is because all building and IT enhancements are treated as part of a bigger project even although this might not be the case in practice
- there is inconsistency in relation to the application of component accounting. SPS should follow the NHS capital accounting manual which provides further guidance on the application of IAS 16 *Property, plant and equipment* in

Audit of the 2014/15 financial statements

relation to the identification of significant and shorter life building elements.

27. We are satisfied that none of the disclosure points have an impact on the closing balance in respect of total non current assets or individual asset categories as at 31 March 2015. Capital accounting processes and assets under construction disclosures should be reviewed during 2015/16.

Refer Action Plan no.2

Provisions

28. **Secundee provision:** The unaudited financial statements included a provision for £0.3 million for net expenditure arising from the estimated cost of retrospectively applying VAT on payments for inward secondees and invoices for outward secondees, the majority of which were with other government departments. SPS agreed to remove the provision on the basis that there was not sufficient certainty to meet the definition of a constructive obligation as defined in IAS 37 *Provisions, contingent liabilities and contingent assets*. The fact that there may be a possible future charge and recharge in respect of VAT being applied to previous invoices for inward and outward secondments is disclosed as a contingent liability.

Scottish Government accounts consolidation pack and whole of Government accounts information

29. SPS is required to complete a Scottish Government consolidation pack that we are required to audit. This pack includes a section to provide information for the whole of government accounts (WGA), which are the consolidated financial statements for all branches of government in the UK. We are not required to audit this section of the pack as SPS falls below the de-minimis level for audit of £350 million of gross expenditure.
30. SPS is required to submit an audited consolidation pack to the Scottish Government prior to the deadline of 17 July 2015. We have received the unaudited consolidation pack and expect to meet the Scottish Government timetable.

Future accounting and auditing developments

Revisions to the FReM

31. The financial statements are prepared in accordance with the FReM that is in force for the year for which the financial statements are prepared. Two significant revisions will apply from 2015/16:
- adoption of International Financial Reporting Standard (IFRS)13 *Fair value measurement* for the first time – this

Audit of the 2014/15 financial statements

also includes IAS 16 and IAS 38 adaptations

- simplification and streamlining project – changes to the form and content of the annual report and accounts.

32. IFRS 13 Fair value measurement: sets out the requirements for assets to be valued at fair value and is applied in full by the FReM only to assets that are not held for their service potential (i.e. investment properties and assets held for sale). It also applies to operational assets which are surplus to requirements where there are no restrictions on disposal that would prevent access to the market.

33. IFRS 13 does not apply to operational assets that are used for delivering front line services or back office functions, and surplus assets with restrictions on their disposal. These will be valued in accordance with the adaptations to IAS 16 *Property, plant and equipment*.

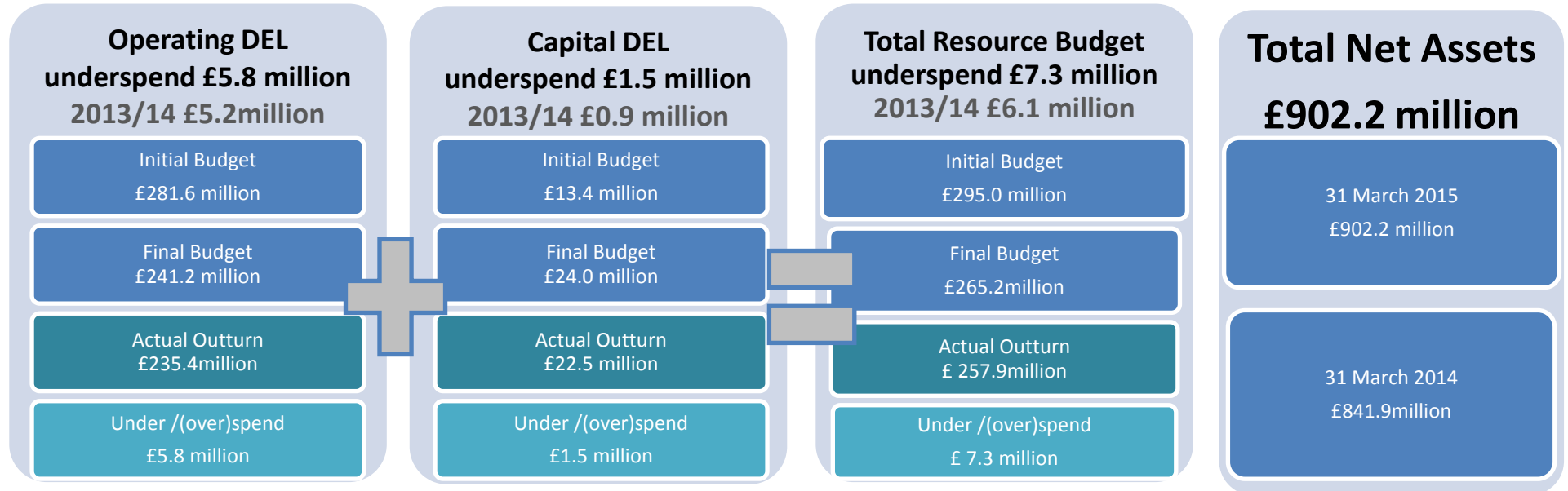
34. Restructuring of the annual report and accounts: the 2015/16 FReM has been extensively re-written to require the annual report and accounts to include:

- a performance report which will give a fair, balanced and understandable analysis of performance and will include an overview section and a performance analysis section
- an accountability report incorporating the following three main sections:

- corporate governance report consisting of a directors' report, a statement of the Accountable Officer's responsibilities and a governance statement
- remuneration and staff report which will cover a number of prescribed disclosures including remuneration policy, payments to directors, staff numbers and sickness absence rates
- parliamentary and accountability report which will include information on the regularity of expenditure and the independent auditor's report.

35. SPS should ensure that the amendments to the FReM are fully considered when preparing the 2015/16 annual report and accounts.

Financial management and sustainability



In addition to its resource budget above, SPS had a non-cash DEL budget, an ODEL budget and an AME budget. The underspends in respect of the non-cash and AME budgets were £0.2 million (2013/14: £1.8 million) and £22.2 million (2013/14: £56.5 million) respectively. The ODEL budget was overspent by £0.2 million (2013/14: £1.2 million underspend).

36. The main financial objective for SPS is to ensure that the financial outturn for the year is within the resource budget allocated by Scottish Ministers. The Scottish Government sets a resource budget for the year which is determined by the spending review settlement and is subsequently approved in the annual budget bill. During the year revisions are approved in the autumn and spring budget revisions.
37. Departmental Expenditure Limits (DEL) are firm plans for three

Financial management and sustainability

years and comprise the majority of the budget that covers programme expenditure and running costs of the Scottish budget. DELs are divided into operating and capital budgets.

38. SPS also has a budget “outside” DEL (ODEL) to reflect a technical adjustment in respect of the privately managed contracts for the operation of HMP Kilmarnock and HMP Addiewell and the contract for the court custody and prisoner escort service carried out by G4S.
39. Annually Managed Expenditure (AME) is generally less predictable and controllable than DEL expenditure.
40. SPS is expected to manage its budget in accordance with its framework document and the Scottish Public Finance Manual (SPFM). SPS operated within the resource budgets for 2014/15 as detailed above.

2014/15 financial position

41. The total budget in 2014/15 was £366.0 million, which comprises an operating budget of £342.0 million and a capital budget of £24.0 million.
42. The operating budget is made up of DEL cash £241.2 million, DEL non cash £32.0 million, and ODEL £68.8 million.
43. The out-turn for the year was £336.5 million which resulted in an underspend of £29.5 million (8%) against the total budget of £366.0 million. The majority of this underspend arises from a negative Annually Managed Expenditure (AME) outturn of

£22.2 million against a nil budget. The AME underspend is made up net impairment reversals of £20.6 million and miscellaneous provisions of £1.6 million.

44. The remaining £7.3 million underspend comprises operating DEL of £5.8 million and capital DEL of £1.5 million. The underspend in operating DEL relates to pay and prisoner related costs. The underspend in capital DEL is the result of a delay in a project to relocate the lock store and the site acquisition for HMP Highland being delayed to 2015/16.
45. The Scottish Government agreed to transfer £10.6 million of revenue funding to capital at the spring budget revision. In addition, net savings of £13.2 million were surrendered from the SPS operating budget to other Scottish Government priorities. These transfers are reflected in the final budget of £366.0 million. Savings arose from underspends in pay due to vacant posts, service credits in relation to the court custody and prisoner escort contract and funding for additional prisoner places in respect of the private prison contracts not being required.
46. At 31 March 2015, SPS’ statement of financial position shows an increase in total assets of £60.3 million. This can be attributed to the increase in the value of property, plant and equipment arising from valuation and indexation movements.
47. The 2015/16 budget was approved by the Scottish Parliament in February 2015. The total budget of £393.1 million comprises an operating budget of £353.1 million, an increase of

Financial management and sustainability

£11.1 million, and a capital budget of £40.0 million which represents an additional £16.0 million compared to 2013/14.

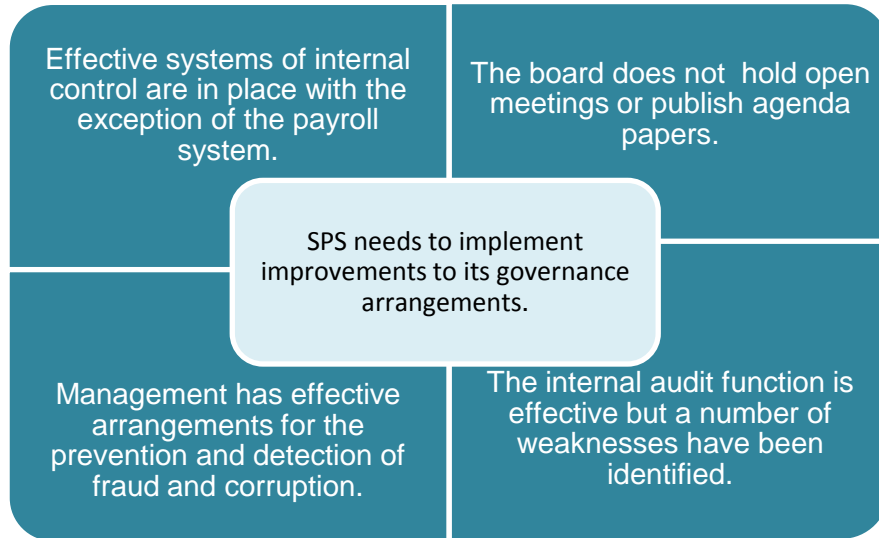
48. The £40.0 million capital budget includes a £10.0 million technical switch from revenue to capital. The capital budget has not been fully allocated at the present time. The Chief Executive requested that this transfer was not reversed whilst SPS awaited confirmation, from the Cabinet Secretary for Justice, of the future strategy for the women's prison estate. The capital programme will be updated following the announcement on the future of the custodial estate for women in June 2015. The Scottish Government has advised SPS that the capital budget can be revisited during the biannual budget revision process.
49. The spending review for 2016/17 will commence later in the year.

Financial management

50. As auditors we need to consider whether bodies have established adequate financial management arrangements. We do this by considering a number of factors, including whether:
 - the Head of Finance has sufficient status to be able to deliver good financial management
 - standing financial instructions and standing orders are comprehensive, current and promoted within the body

- reports monitoring performance against budgets are accurate and provided regularly to budget holders
 - monitoring reports do not just contain financial data but are linked to information about performance
 - non executive directors provide a good level of challenge and question budget holders on significant variances.
51. Our review of SPS governance arrangements (see Governance and transparency section) noted that there is a regular financial report to the Board. However, the information is summarised and the Board did not consider the 2014/15 budget setting process. We observed that reports on performance are ad hoc in nature and there is a lack of purpose in respect of some items. We recommended that scheduled items in respect of finance, performance, risk and other key issues would help to provide focus for the Board.
 52. The regular finance report has been revised and an update on the SPS budget and budgetary process for 2015/16 was provided to the Board in March and May 2015 respectively.
 53. Based on our accumulated knowledge, our review of board papers and through our attendance at the RMAC we conclude that SPS has reasonable financial management arrangements in place.

Governance and transparency

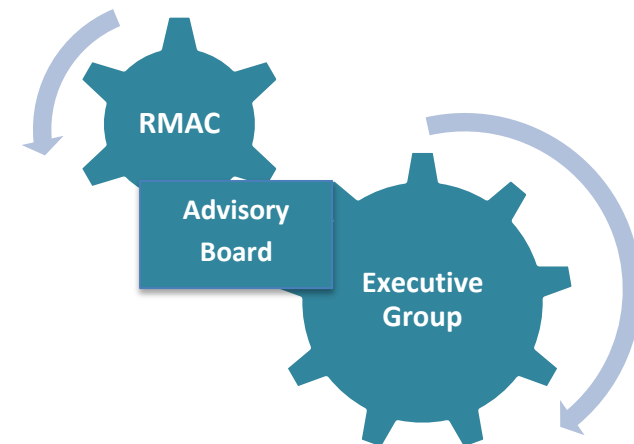


Advisory Board to support this role. As at 31 March 2015 the Board comprised three executive directors and four independent non-executive directors appointed by the Chief Executive. During 2014/15 there were a number of changes to non-executive directors. Four of the five non-executive directors left the Board and three new members were appointed.

- 56. The Advisory Board met on six occasions during 2014/15. The Advisory Board is supported by the Executive Group and RMAC.

Corporate governance

- 54. SPS is headed by a Chief Executive who is responsible to Scottish Ministers, within the terms of the Agency's framework document with the Scottish Government, for its management, performance and future development. The Chief Executive is responsible for all operational matters as delegated by the Director General Learning and Justice.
- 55. The Chief Executive has a responsibility to ensure the Agency effectively delivers ministerial policies and he chairs an



Governance and transparency

57. The Executive Group, which comprises the executive directors and is attended by a number of other senior staff, meets on a fortnightly basis. At 31 March 2015 the RMAC had four members, comprising two non executive directors and two independent members. One non executive director and one independent member were new appointments during 2014/15. The RMAC is chaired by an independent member and met on four occasions during the year.
58. During 2014/15, we carried out a local study which reviewed SPS governance arrangements and reported our findings to the RMAC in March 2015. We were informed that the report would also be distributed to members of the Advisory Board, however this has still to be actioned.
59. Our review considered the role and effectiveness of the SPS Advisory Board, RMAC and SPS risk management procedures. We reported that, in general, the SPS Advisory Board and RMAC are operating with a good level of challenge. There is evidence of a positive change in the organisation's response to scrutiny and a willingness to implement change and to pursue continuous improvement. However, there is a need to implement a more formal governance structure in terms of process and support systems.
60. Key findings, in relation to the role and effectiveness of the SPS Board and RMAC, were:
- the SPS framework document was last formally updated ten years ago. It is out of date and the contents do not fully reflect the requirements of Scottish Government guidance
 - the nature of an Advisory Board can result in uncertainty over its role and the responsibilities of its members. As a result, the responsibilities of Board members and the respective roles of the Board and RMAC need to be clarified
 - a lack of succession planning has resulted in a large turnover of members and pressure to make appointments to ensure there is sufficient membership of the Board and RMAC
 - there is no appraisal process for non executive directors and independent members and improvements are required to induction and training procedures
 - the Board does not carry out a formal review of its own performance on a regular basis. There is no standardised structure to the Board agenda and the purpose of some papers presented to members is unclear.
61. In respect of risk management we reported that there is no formalised approach to the Board's consideration of risk management arrangements. There is no risk management strategy for the organisation and the corporate risk register has not been subject to a formal review for almost two years.
62. We followed up progress on the implementation of the 24 recommendations included in our report during May and

Governance and transparency

June 2015. Overall, we are satisfied that some progress is being made. However only a few of the recommendations have been fully implemented in accordance with the agreed target dates. The following paragraphs outline some of the improvements underway.

63. New non executive directors and independent RMAC members were appointed during the third quarter of 2014/15. These appointments are for a period of three years with the option to extend up to a further three years, which gives scope to vary termination dates and assist with succession planning.
64. The skills mix of Board and RMAC members is currently being reviewed in order to create a structured training and development programme. Arrangements for implementing a formal appraisal system for Board and RMAC members are being progressed.
65. A project manager has been appointed to the Office of the Chief Executive to undertake a project reviewing and co-ordinating corporate governance across the organisation. This short life governance review will develop an SPS corporate governance model and internal corporate governance framework. We have been advised that the review will ensure the recommendations in our report are fully implemented.
66. An additional RMAC meeting is scheduled for September 2015 to consider how the committee works. An update, from SPS,

on the progress made in implementing the recommendations included in our governance report will be provided to the November 2015 RMAC meeting.

67. SPS appointed a Corporate Risk Manager in March 2015. To date, a draft risk appetite statement has been produced and a risk management policy is currently being prepared. Risk scoping meetings have been undertaken or are being scheduled at SPS establishments and a risk workshop with members of the Board and Executive Group is under development.
68. SPS should continue to make progress in improving risk management arrangements during 2015/16. These include;
 - revising the format and content of the corporate risk register
 - implementing organisation-wide risk management arrangements
 - preparing and implementing a risk management policy
 - developing a consistent approach to directorate/ establishment risk registers
 - providing risk management training
 - clarifying formal reporting mechanisms.
69. We will continue to monitor the implementation of the recommendations included in our report and the progress of the SPS short life governance review.

Refer Action Plan no.5 and 6

Organisational review

70. The SPS 2014-17 corporate plan, which sets out its strategic priorities, was published during the year. The corporate plan is supported by the 2014/15 annual delivery plan, which identifies the tasks required to ensure delivery of priority areas.
71. Implementation of the change programme arising from the organisational review should remain a key priority for the service. Sufficient organisational capacity, staff development and effective leadership will influence the organisation's ability to deliver the change programme and business as usual activity.
72. Ongoing vacancies continued to be an issue during 2014/15. The Chief Executive is supported by three executive directors; Director of Corporate Services, Director of Operations and Director of Strategy and Innovation. The Director of Operations is currently on extended absence and a short term solution has been to create two interim posts to cover his duties.
73. The Corporate Change Unit (CCU) has a key role in the transformation of the service. A permanent head of the CCU, who reports to the Chief Executive, was appointed in January 2014 but only held this post for five months. The post has since been covered by two acting heads. There is no timetable

to fill the post on a permanent basis.

74. SPS needs to ensure that it has adequate succession planning in place to provide the required capacity and expertise to both fill and provide support at a senior management level.

Refer Action Plan no.7

Transparency

75. The Scottish Government's [On Board](#) guidance for board members of public bodies was updated and reissued in April 2015. The guidance states that boards should demonstrate high standards of corporate governance at all times including openness and transparency in decision making. It recommends boards should consider:
 - holding an annual open meeting
 - holding board meetings in public unless there is a good reason not to
 - publishing summary reports and/or minutes of meetings
 - inviting evidence from members of the public in relation to matters of public concern
 - consulting stakeholders and users on a wide range of issues
 - making corporate plans and the annual report widely available.
76. SPS holds all Board meetings in private. Board minutes are

Governance and transparency

available on the SPS website. Our review of governance arrangements noted that restricted access to Board papers and the RMAC terms of reference impacts on the openness of the organisation. SPS maintain a register of interests of directors and Governors which is held centrally. This register is not published.

77. Organisational transparency will be reviewed as part of the SPS short life governance review and the On Board guidance should be considered as part of this process.

Refer Action Plan no.8

Internal control

78. As part of our audit we reviewed the high level controls in a number of systems key to the preparation of the financial statements. Our objective was to obtain sufficient audit evidence to support our opinion on the financial statements.
79. With the exception of the payroll system, no material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the organisation's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.
80. We have carried out additional substantive testing of payroll transactions to provide assurance on the reliability of the figures reported in the financial statements.

81. Weaknesses were also identified from our review of prisoner funds at HMP Cornton Vale. We visited this prison to review a sample of systems as a result of internal audit reporting limited assurance in respect of financial management and controls. Additional assurance was obtained from reviewing internal audit working papers, which considered prisoner funds at a further three establishments (see below), and by carrying out substantive testing on all prisoner fund balances as part of our year end audit.
82. We reported our findings in our Report on interim testing which was presented to the RMAC on 22 May 2015.

Statements of assurance

83. Twice yearly statements of assurance supported by a memorandum on year end issues are reported to the RMAC. These statements are prepared by the executive directors and other senior staff and cover the main systems for which they are responsible.
84. The Chief Executive has identified three significant control issues in the 2014/15 governance statement:
- HMP Grampian (see appendix I)
 - strategy for the management of women in custody (see significant findings from the audit)
 - information technology - digital procurement and HR facilities (see ICT audit).

Governance and transparency

85. It was noted by members, at the May 2015 meeting of the RMAC, that the statements of assurance did not highlight these matters as significant issues. There were a number of other matters in the paper presented to the RMAC that appeared to be relevant for the purposes of reporting in the governance statement. Members were informed that the information in respect of some of these issues was out of date and/ or the fact that they were not considered a major risk was not fully articulated in the paper. It was also noted that the annual report from the Head of Audit and Assurance Unit (AAU) should feed into the formal assurance process for the purpose of identifying significant control issues in the governance statement.
86. The statements of assurance process should be reviewed to ensure that there is a clear link between the statements provided by the executive directors, the Head of AAU's annual report and the significant control issues identified by the Chief Executive in the annual governance statement.

Refer Action Plan no.3

Internal audit

87. Internal audit provides the RMAC and Accountable Officer with independent assurance on the overall risk management, internal control and corporate governance processes. We are required by international auditing standards to make an assessment of internal audit to determine the extent to which we can place reliance on its work. To avoid duplication, we place reliance on internal audit work where possible.
88. The SPS internal audit service is carried out by the Audit and Assurance Unit (AAU). Our review of internal audit concluded that the internal audit service operates in accordance with the Public Sector Internal Audit Standards (PSIAS).
89. The internal audit plan for 2014/15 was materially complete although there was slippage in some areas as detailed in the Head of AAU's Annual Report to the RMAC in May 2015. The areas in which slippage was reported did not impact on our work. We were able to place formal reliance on aspects of internal audit work on prisoner funds and capital accounting.
90. In order to place formal reliance on the two areas noted above we carried out a detailed review of the internal audit working paper files. Discussions held with the Head of AAU, as part of our audit planning, indicated that the internal audit files would be available for review prior to 31 March 2015. We did not receive the files for review until May 2015. A number of issues were identified from our review of these files:
- there is not an agreed methodology for sample size selection
 - sampled items were not spread across the year to date
 - it was sometimes difficult to identify the items selected for testing
 - it wasn't always clear what control was being tested

Governance and transparency

- there was a lack of supporting evidence in the files to support errors.
91. Internal audit working papers should be prepared to a consistently high standard and audit testing should be carried out in accordance with a predetermined methodology.
92. We acknowledge that 2014/15 has been a challenging year for the AAU. We understand that one financial auditor remains on long-term sick leave and another financial auditor has recently left the section. To ensure that the AAU continues to operate in accordance with PSIAS, the Head of AAU should ensure that adequate resources are in place to deliver the audit work programme.

Refer Action Plan no.4

Information and communications technology (ICT audit)

93. As part of our 2014/15 audit we met with the Head of Information Systems and Strategy (ISS) to consider the continuing and emerging challenges facing the ISS management team.
94. **Digital strategy:** The SPS Digital Strategy, which takes account of the organisational review and supports the aims of the national Digital Strategy for Justice, was approved by the Executive Group in July 2014.
95. There is no detailed plan to support delivery of the strategy. The challenge of taking on increased responsibility, in conjunction with the infrastructure updates identified from planning the data recovery test (see below) have affected the resources available to develop detailed plans. This is an area we will keep under review as part of our 2015/16 audit.
96. **Business continuity (BC) and disaster recovery (DR):** A new business continuity and disaster recovery facility was created following relocation of the SPS data centre services. An annual test of the IT BC/ DR facilities was due to take place in July 2014. A full test of these facilities has still to be performed. However, the detailed planning of this exercise is identifying issues that are being resolved. A revised deadline of September 2015 has been provided by the Head of ISS.
97. **Digital procurement and HR facilities:** SPS intends to deliver digital procurement and HR capabilities to provide additional functionality and enhance business efficiencies. An e-procurement system is also required to meet an EU Directive requiring all public purchases to move to full e-procurement by mid 2016.
98. The e-procurement project is currently on hold following a Scottish Government Gateway Review. SPS has considered the findings from the review and, as a result, the governance regime for the project was reviewed and the ISS section was given increased responsibility. SPS has identified the need to initiate a project to reconsider the business case and develop a

Governance and transparency

detailed action plan. A business analyst was appointed in June 2015 to progress this work.

99. Concerns emerging in relation to the e-procurement project, as well as the HR system which is behind schedule in relation to the roll out of full functionality, are identified as significant control issues in the 2014/15 governance statement.
100. SPS should ensure that the ICT delays noted above are addressed in accordance with an agreed timetable.

Refer Action Plan no.9

Arrangements for the prevention and detection of fraud

101. We assessed SPS' arrangements for the prevention and detection of fraud. This involved reviewing the SPS whistleblowing policy and the operation of the Fraud Response Group which was established in accordance with the SPS Fraud Response Plan. The Fraud Response Plan supports the SPS Fraud Prevention Policy. The Fraud Response Policy and Plan was refreshed and relaunched to SPS employees in February 2015. A report on the work of the Fraud Response Group is presented to the June meeting of the RMAC each year.
102. We conclude that there are effective arrangements for the prevention and detection of fraud.

National Fraud Initiative in Scotland

103. The National Fraud Initiative (NFI) in Scotland is a counter-fraud exercise led by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different financial systems, to identify circumstances (matches) that might suggest the existence of fraud or error.
104. Auditors are required to assess the arrangements that bodies have put in place to prevent and detect fraud, including how they approach the NFI exercise itself.
105. We have reviewed the progress that SPS has made in following up data matches identified for the purposes of the 2014/15 NFI exercise. We are satisfied that SPS has satisfactory arrangements in place for investigating and reporting data matches and is on target to meet the deadline for completion of the 2014/15 exercise.

Arrangements for maintaining standards of conduct and the prevention and detection of corruption

106. SPS has a range of procedures in place that are designed to maintain standards of conduct, including an employee code of conduct. We are continuing to monitor SPS progress in updating the code.

Governance and transparency

107. SPS is required to comply with the SPFM, which promotes good practice and high standards of propriety. In addition, the SPS Financial Policy and Procedures Manual provides guidance to ensure that assets are properly safeguarded, proper accounting records are maintained and compliance with current legislation and government financial procedures.
108. A Conduct Investigation Unit was launched in June 2010. It is an independent unit responsible for investigating allegations of gross misconduct involving SPS employees. An annual report, which summarises the work of the unit, is presented to the RMAC in June each year.
109. Based on our review of the evidence we concluded that there are appropriate arrangements in place for the prevention and detection of corruption and we are not aware of any specific issues that we need to record in this report.

Value for money

110. Accountable officers have a specific responsibility to ensure that arrangements have been made to secure Best Value.

Arrangements for securing best value

111. 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.

112. 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 SPS agree to undertake local work in this area.

Local performance audit reports

Review of capital investment programme

113. During 2014/15 we followed up the recommendations arising from our review of arrangements to establish and keep under review the prison estate capital investment programme, which

was reported to the RMAC in March 2014.

114. A number of recommendations to support improvement in the direction and delivery of SPS capital investment were made.

We reported that SPS should:

- develop and publish a strategy to set out the long term needs and constraints for capital investment in the prison estate in Scotland
- clearly outline governance arrangements for the capital programme
- improve the quality of information provided to the board on the capital programme
- continue to seek opportunities for joint working with justice partners, other public bodies, and councils to explore ways to improve the efficiency of the capital programme
- implement standard procedures for measuring, monitoring and reporting of the benefits for each major capital project
- carry out post-project evaluations following project completion in line with guidance issued by the Scottish Government.

115. Responsibility for implementing the majority of the management responses to the recommendations raised in our action plan were allocated to the Corporate Change Unit

Value for money

(CCU). We understand that a number of capital projects fall within business as usual activity which are monitored by the Directorate programme boards.

- 116. Overall, there has been limited progress in implementing the recommendations made in our review of the capital investment programme. SPS has confirmed that plans to produce a long-term capital investment strategy are on hold until the Scottish Government sets a clearer direction in terms of a penal policy.
- 117. SPS should update the management responses to reflect organisational responsibilities for implementing the capital programme and provide revised management actions as appropriate.

Refer Action Plan no.10

Review of governance arrangements

- 118. We carried out a review of governance arrangements during 2014/15. The findings from this review are summarised in the section on Governance and accountability.

Review of workforce planning

- 119. We have agreed that we will conduct a local study to determine if SPS has effective workforce planning in place. We will establish whether SPS has produced a workforce strategy and plan and whether these ensure there are sufficient skills and capacity to deliver the recommendations in the organisational

review. We will consider how SPS plans to achieve its overall workforce strategy and whether there are effective arrangements in place for the scrutiny of workforce planning and implementation activity.

- 120. A scoping document was presented to the RMAC in May 2015. This review will be carried out in October 2015 and we will report our findings in November 2015. A summary of the key outcomes will be included in our 2015/16 Annual audit report.

National performance audit reports

- 121. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2014/15, a number of reports were issued which are of direct interest to SPS. These are outlined in [appendix III](#).
- 122. SPS has confirmed that arrangements are being made to review the forthcoming publications section on the Audit Scotland website in order to identify reports which are relevant to the Agency. Published national performance reports will be considered and included as an agenda item for the RMAC and/or SPS Advisory Board as appropriate.
- 123. **Reducing reoffending in Scotland - impact report:** This report, which was published in May 2014, summarised the impact of the Reducing reoffending in Scotland national performance report. The impact report identified that:

Value for money

- the Scottish Government set up a working group to look at the cost of Criminal Justice Social Work Services and the unit cost of Community Payback Orders
- the Scottish Government is proposing major changes to how community justice services are planned and delivered
- the Scottish Government changed how community justice services were funded
- the Scottish Government is developing a national performance framework for community justice and reducing reoffending.

124. **Scotland's public finances – a follow up audit: Progress in meeting the challenges:**

This report was published in June 2014 and commented that, in setting budgets, public bodies need to focus more on their priorities, making clearer connections between planned spending and the delivery and measurement of outcomes. It highlighted the importance of public bodies developing and maintaining long-term (5-10 year) financial strategies to direct and control their finances.

125. **Update on developing financial reporting:**

This update report, published in March 2015, reviewed the principles of public financial management and provided an update on the actions the Scottish Government is taking to further develop financial reporting.

126. The report concludes that the Scottish Government and the public sector generally, have a good record of financial

management and reporting. The Scottish Government has continued to improve and develop its financial reporting framework since the previous report was published. The report highlights that consolidated accounts for the whole of the Scottish public sector would help provide an overall picture of its financial position to strengthen understanding and transparency.

Appendix I – Significant audit risks

The table below sets out the audit risks, how we addressed each risk and our judgement in arriving at our opinion on the financial statements.

| Audit risk | Assurance procedure | Results and conclusions |
|--|---|---|
| Financial audit Issues | | |
| <p>PFI contracts <i>(Statement of Comprehensive Net Expenditure, Statement of Accounting Policies ,Note 17)</i></p> <p>There is a risk the PFI costs of the contract for HMP Kilmarnock and HMP Addiewell become unaffordable. SPS have commissioned PwC to look at both PFI contracts (HMP Kilmarnock and HMP Addiewell) in terms of value for money, cost and affordability.</p> | <ul style="list-style-type: none"> Review as part of our planned capital programme follow up work. | <p>SPS have received the completed report on the PFI contracts from PwC. We have been informed that the report identifies a number of concerns which will be considered in consultation with the Cabinet Secretary for Justice.</p> <p>The Chief Executive has confirmed that the issues identified have no impact on the figures reported in the 2014/15 financial statements.</p> <p>We are unable to conclude on this risk at this time and will continue to monitor any implications arising from the findings contained in the PwC report.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|--|--|---|
| <p>Management override of controls <i>(Statement of Comprehensive Net Expenditure, Statement of Accounting Policies)</i></p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p> <p>There is a risk of management override of controls.</p> | <ul style="list-style-type: none"> Financial statements work – detailed sample testing of journals, review of accounting estimates and evaluation of significant transactions that are outside the normal course of business. | <p>Financial statements audit work covered the planned assurance procedures. No issues were identified.</p> |
| <p>Format of SoCNE <i>(Statement of Comprehensive Net Expenditure, Statement of Accounting Policies)</i></p> <p>The format of the Statement of Comprehensive Net Expenditure (SoCNE) in the SPS accounts does not comply with the FReM as illustrated in the proforma accounts for Agency Pink.</p> <p>Agency Pink requires the statement to allocate staff costs, other costs and income between administration and programme elements.</p> <p>There is a risk that the SoCNE does not comply with the FReM.</p> | <ul style="list-style-type: none"> Review of revised SoCNE. | <p>We sought further technical advice in relation to this matter and concluded that no amendment to the SoCNE was required.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|--|---|--|
| <p>Land and Building valuations <i>(Statement of Financial Position, Statement of Accounting Policies, Note 6)</i></p> <p>A material error occurred at the 31 March 2012 valuation of SPS land and buildings (in respect of the land at HMP Barlinnie) resulting in a prior year adjustment in the 2013/14 accounts.</p> <p>In addition, the 31 March 2014 valuations of HMP Aberdeen and HMP Peterhead, which were non operational properties required to be revised as a result of audit work.</p> <p>There is a risk valuations provided by the District Valuer are inaccurate.</p> | <ul style="list-style-type: none"> • Review additional process implemented by SPS. • Additional analytical review work. | <p>The Head of Finance met with the District Valuer to discuss SPS' requirements prior to the year end valuation exercise. There was ongoing correspondence between the District Valuer and finance staff throughout the financial year. We have been informed that there were benefits gained, in respect of clarity and timeliness, from this approach.</p> <p>We carried out additional analytical procedures as part of our year end testing of asset valuations. This included reviewing the changes in year end asset values in respect of assets valued by the District Valuer and identifying significant variances. Explanations were received in respect of these movements and we are satisfied that valuations provided by the District Valuer are accurate.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|--|--|---|
| <p>Accounting and disclosure of impairments <i>(Statement of Comprehensive Net Expenditure, Statement of Accounting Policies, Notes 4, 6, 9)</i></p> <p>Significant impairment reversals were required in 2013/14 due to an increase in tender price indices (TPIs).</p> <p>In prior years, audit work identified errors in respect of accounting for valuation movements.</p> <p>TPIs are subject to change between the forecast used for the preparation of the accounts and the actual index after the year end.</p> <p>This resulted in a late amendment, to disclose the change in accounting estimate, in the 2013/14 accounts.</p> <p>There is a risk that impairments are accounted for incorrectly.</p> | <ul style="list-style-type: none"> Review accounting treatment for impairments – including verification of impairment reversals and whether impairment reversals are caused by an in-year change or a change in the forecasted TPI and the actual index at the year end. Sample testing of impairment charges and/or reversals to include calculations, accounting entries and disclosure in the financial statements. | <p>Net impairment reversals of £16.3 million are disclosed in the 2014/15 financial statements. This net figure is comprised of impairment reversals of £20.7 million and impairment charges of £4.4 million. £6.0 million of the net amount was the result of a revision to the opening index.</p> <p>We carried out sample testing of these calculations and reviewed disclosures in the financial statements. We are satisfied that impairments are accounted for correctly.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|---|--|--|
| <p>Reduction in capital budget <i>(Management Commentary – Financial Performance)</i></p> <p>There has been a reduction in the capital budget in 2014/15 with an £11 million overspend currently forecast.</p> <p>There is a risk that insufficient capital funding could lead to failure of delivering the capital programme.</p> | <ul style="list-style-type: none"> • Review as part of our planned capital programme follow up work. • Review of capital programme monitoring reports. | <p>Refer to comments in respect of our follow up work on our report on the SPS capital investment programme in the value for money section.</p> <p>We reviewed capital programme monitoring reports during the year. The Scottish Government agreed to transfer £10.6 million of revenue funding to capital at the spring budget revision to address the forecast overspend. There was an underspend of £1.5 million (6%) against a final capital budget of £24.0 million in 2014/15.</p> <p>A capital budget of £40.0 million is available in 2015/16. This budget is not yet fully allocated.</p> <p>We are satisfied that sufficient funding is available to deliver the capital programme in the short term.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|--|---|--|
| <p>HMP Inverclyde <i>(Statement of Comprehensive Net Expenditure, Statement of Financial Position, Statement of Accounting Policies, Notes 4, 6, 9)</i></p> <p>Plans to build a new women’s prison at HMP Inverclyde have been terminated. Demolition and enabling work had progressed and were due to be completed by April 2015.</p> <p>There is a risk that expenditure incurred on enabling work and procurement is not accounted for correctly.</p> | <ul style="list-style-type: none"> Review accounting treatment of expenditure on HMP Inverclyde to ensure costs incurred are properly accounted for. | <p>Refer to the section on significant findings from the audit in accordance with ISA260.</p> <p>We are satisfied that the correct accounting entries have been made and the adjustments have been adequately disclosed.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|--|---|---|
| Wider audit issues | | |
| <p>HMP Grampian <i>(Governance Statement)</i></p> <p>A number of issues culminated in a disturbance at HMP Grampian in May 2014, two months after the prison was opened. Following the conclusion of the incident, a decision was taken to limit capacity to approximately 250 prisoners in the medium term.</p> <p>The issues identified are not fully resolved and the prison continues to operate at a reduced capacity.</p> <p>There is a risk that weaknesses in the SPS methodology for designing and building the prison and a failure to adequately define the concept of a community facing prison are repeated in respect of future capital projects.</p> | <ul style="list-style-type: none"> Review as part of our planned capital programme follow up work. | <p>Refer to comments in respect of our follow up work on our report on the SPS capital investment programme in the value for money section.</p> <p>The operational issues relating to HMP Grampian were addressed during the year and a long-term plan is being implemented to ensure its stability. The prisoner population at HMP Grampian has gradually increased since the incident in May 2014, with a date for full occupancy still to be determined. Work is on-going to address the issues surrounding the recruitment and retention of staff at HMP Grampian.</p> <p>The issues noted above are reported as a significant matter in the 2014/15 governance statement.</p> <p>We have been informed that a “lessons learned” report in relation to HMP Grampian will be presented to the RMAC in June 2015.</p> <p>We are satisfied that SPS has reflected on the problems that arose at HMP Grampian and these will be taken into consideration when planning future capital projects.</p> |

Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|---|---|--|
| <p>Organisational review <i>(Governance Statement)</i></p> <p>Although developments have been made, there is a risk that management arrangements to deliver the organisational review are not fully embedded on a timely basis. Ongoing vacancies and a failure to implement staff development activities could impact on the organisational capacity to deliver the organisational review recommendations.</p> <p>There is a risk that organisational policies and procedures are not being updated due to the prioritisation of organisational review recommendations.</p> | <ul style="list-style-type: none"> • Review of workforce planning. • Review of Board and other committee minutes. • Regular meetings with the Chief Executive. • Obtain and review action plan for delivery of the organisational review and measure progress against it. | <p>Refer to comments on the organisational review in the governance and transparency section.</p> <p>We have reviewed Board and other minutes during the year and met with the Chief Executive on a number of occasions.</p> <p>We discussed progress with the implementation of the recommendations raised in the organisational review with the Acting Head of CCU. We understand that a report on progress to date will be presented to the June 2015 meeting of the RMAC.</p> <p>An update on the organisational review is disclosed in the 2014/15 governance statement as a follow up to the comments made in the significant matters section of the 2013/14 governance statement. An updated whistleblowing policy and a revised staff code of conduct are expected to be published in 2015/16.</p> <p>We will continue to monitor developments in relation to updating organisational policies and procedures and delivery of the change programme arising from the organisational review.</p> <p>We will carry out a review of workforce planning in autumn 2015.</p> |

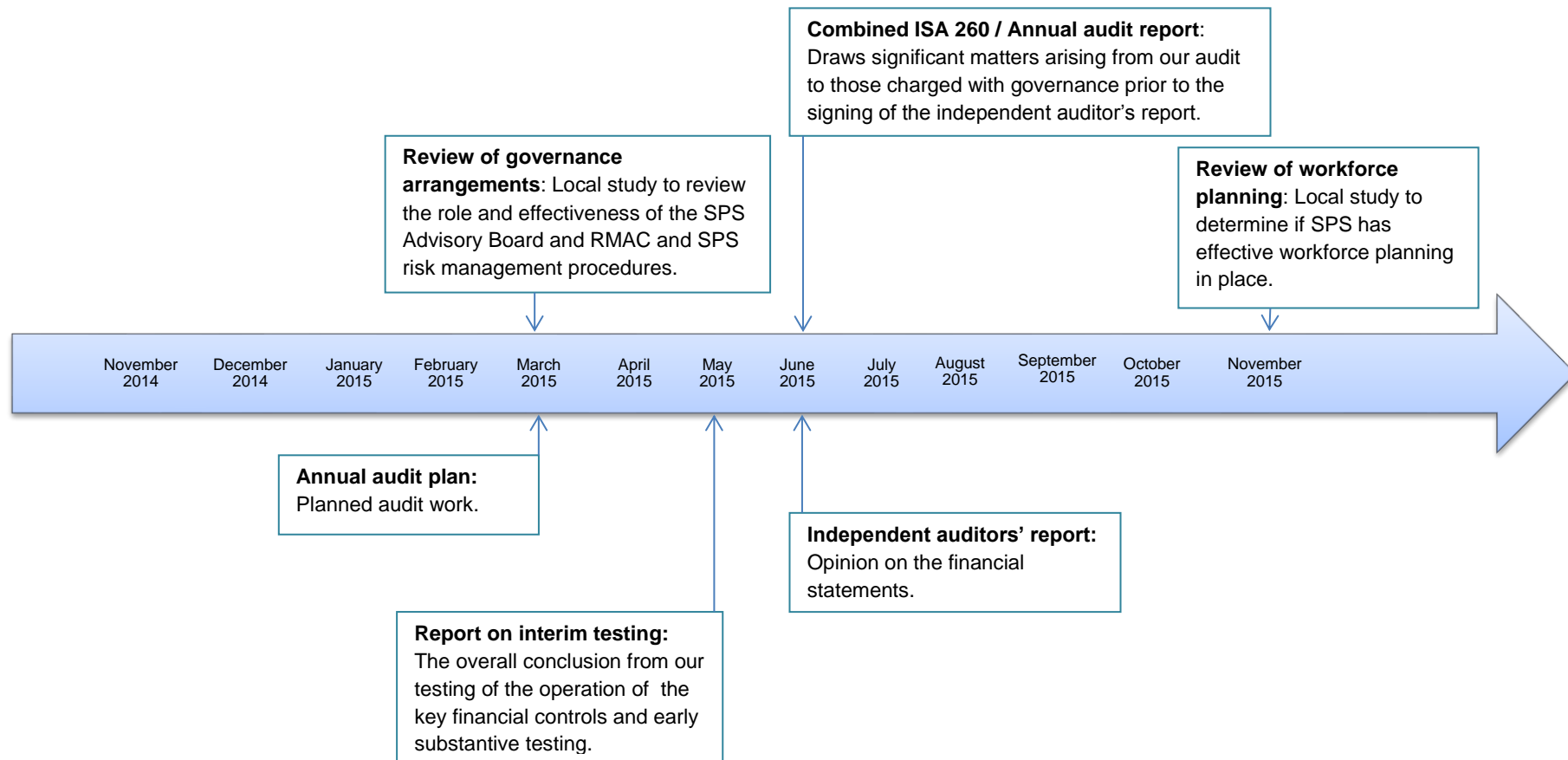
Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|--|--|--|
| <p>Governance arrangements <i>(Governance Statement)</i></p> <p>A number of risks were identified and reported as part of our review of governance arrangements in respect of the role and effectiveness of the SPS Advisory Board and RMAC. These have been grouped into four areas as follows:</p> <ul style="list-style-type: none"> • framework document • roles and responsibilities • appointment, induction and assessment of NEDs and independent members • Board and RMAC effectiveness. | <ul style="list-style-type: none"> • Review as part of our planned follow up work on governance arrangements. • Review of Board and other minutes. • Regular meetings with Chief Executive. | <p>We have reviewed Board and other minutes during the year and met with the Chief Executive on a number of occasions.</p> <p>Refer to the findings from our review of governance arrangements in the governance and transparency section. Progress has been made in a number of areas and a short life governance review has been commissioned by the Chief Executive. Further work is required to fully implement the recommendations contained in our report.</p> |

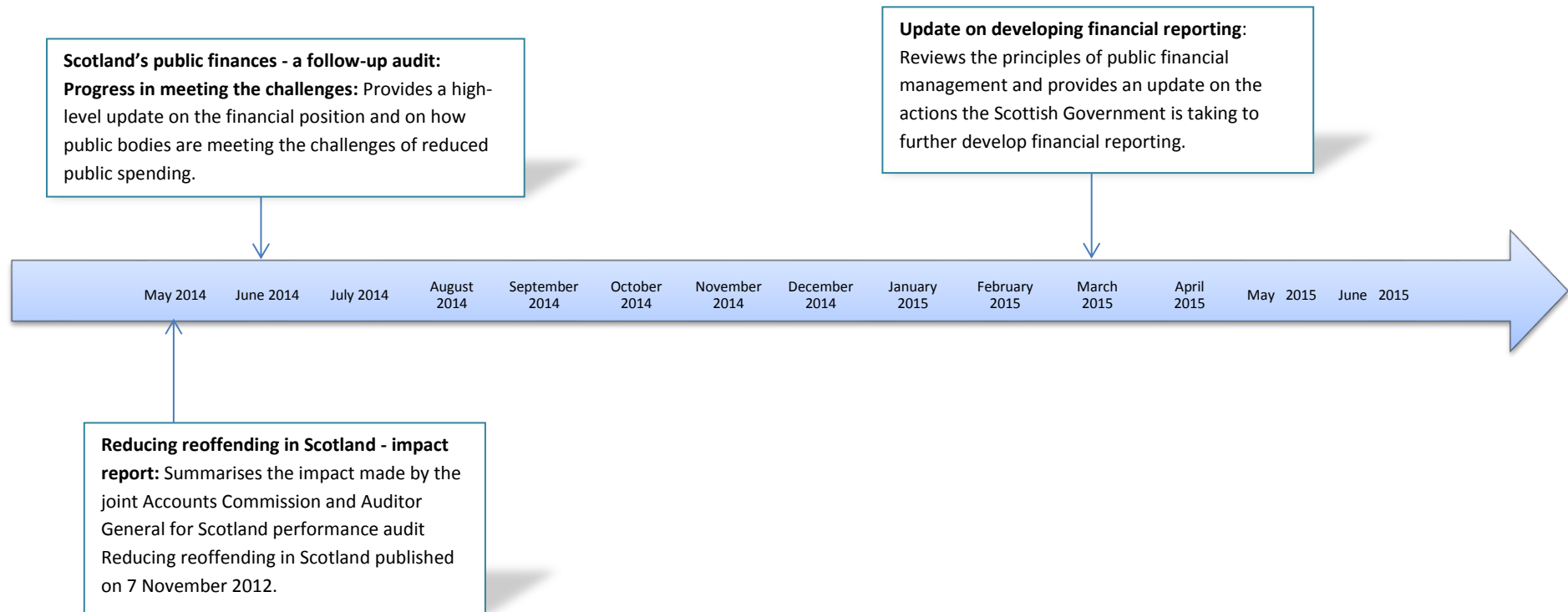
Appendix I – Significant audit risks

| Audit risk | Assurance procedure | Results and conclusions |
|---|--|--|
| <p>Risk management arrangements <i>(Governance Statement)</i></p> <p>The corporate risk register requires significant improvement to allow the members of the RMAC and SPS Board perform their assurance role in respect of the effective operation of organisational governance.</p> <p>Although a number of improvements to risk management have been planned, including the appointment of a Corporate Risk Manager, these improvements are not yet in place.</p> <p>There is a risk that risk management procedures are not sufficiently robust.</p> | <ul style="list-style-type: none"> • Monitor implementation of improved risk management arrangements including the appointment of a Risk Manager and progress with updating risk registers. • Review as part of our planned follow up work on governance arrangements. • Review of Board and other minutes. | <p>We have reviewed Board and other minutes during the year and met with the Chief Executive on a number of occasions.</p> <p>Refer to the findings from our review of governance arrangements in the governance and transparency section.</p> <p>We have commented on progress in implementing improved risk management arrangements in the governance and transparency section. A Corporate Risk Manager started work with SPS in March 2015 and has started to make improvements. Further work is required to fully implement the recommendations contained in our report and implement effective risk management arrangements.</p> |

Appendix II – Summary of local audit reports 2014/15



Appendix III – Summary of national reports 2014/15



Appendix IV – Action plan

| Paragraph/ action point | Issue/ risk/ recommendation | Management action/response | Responsible officer | Target date |
|-------------------------------|---|---|---------------------|-------------|
| Financial audit Issues | | | | |
| 22/ 1 | <p>Strategy for the management of female offenders</p> <p>As at 31 March 2015 the future strategy for the management of female offenders was the subject of ongoing consultation and asset valuations were based on the evidence available at that time. An announcement from the Cabinet Secretary for Justice, on 22 June 2015, confirmed the new proposals and the impact on the prison estate.</p> <p>Risk</p> <p>Asset valuations may not reflect the impact the plans for the future custodial estate for women have on the estate.</p> <p>Recommendation</p> <p>SPS should revisit the valuation of the prison estate, in 2015/16, to ensure that it reflects the Cabinet Secretary’s confirmed strategy for the management of women offenders.</p> | <p>Agreed.</p> <p>A valuation exercise will be carried out during 2015/16 as part of the normal rolling programme. Any announcements surrounding the women’s custodial estate will be taken into consideration during that process.</p> | Head of Finance | March 2016 |

Appendix IV – Action plan

| Paragraph/ action point | Issue/ risk/ recommendation | Management action/response | Responsible officer | Target date |
|-------------------------------|---|---|---------------------|-------------|
| 27/ 2 | <p>Assets under construction</p> <p>We identified a number of issues in respect of SPS' capital accounting processes and the disclosure of asset under construction movements in the financial statements.</p> <p>Risk</p> <p>There is a risk that assets under construction are not properly disclosed in the financial statements.</p> <p>Recommendation</p> <p>Capital accounting processes and asset under construction disclosures should be reviewed during 2015/16.</p> | <p>Agreed.</p> <p>A review of capital accounting procedures will be carried out during 2015/16.</p> | Head of Finance | March 2016 |

Appendix IV – Action plan

| Paragraph/ action point | Issue/ risk/ recommendation | Management action/response | Responsible officer | Target date |
|-------------------------------|--|--|--|-------------------|
| 86/ 3 | <p>Governance statement assurance process</p> <p>There is not a clear link between the statements of assurance provided by the executive directors, the Head of AAU's annual report and the significant control issues identified by the Chief Executive in the annual governance statement.</p> <p>Risk</p> <p>The governance statement may not reflect significant control issues within the organisation.</p> <p>Recommendation</p> <p>The statements of assurance process should be reviewed to ensure that it supports disclosures in the annual governance statement.</p> | <p>The Statement of Assurance process will be reviewed for 2015/16 and Executive Directors / Branch Heads will be requested to identify the main risks and performance issues within their locus of responsibility. In addition, each of the risks / issues identified will require to be individually scored on the likelihood / impact matrix. High risks will then inform the Corporate Risk Register (CRR) which will assist in identifying any significant control issues highlighted by the Chief Executive in the annual governance statement. The CRR also informs the AAU annual Audit & Assurance Plan which details reviews designed to test controls on high risk areas of the business. The Head of AAU Annual Report will highlight areas of control weakness found in the course of review and, if considered major, breaches of control will be reported in the Chief Executive's annual governance statement.</p> | <p>Head of Audit and Assurance</p> <p>Corporate Risk Manager</p> | <p>March 2016</p> |

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|-------------------------------|---|---|-----------------------------|---------------|
| 92/ 4 | <p>Internal audit</p> <p>A number of issues, relating to the quality of internal audit working papers, were identified from our detailed review of internal audit working paper files. The financial audit team within AAU is currently under resourced.</p> <p>Risk</p> <p>There is a risk that working papers don't provide sufficient evidence to support the conclusions reached and financial audits are not sufficiently resourced.</p> <p>Recommendation</p> <p>Internal audit quality standards, including the agreed sampling methodology, should be reinforced. Financial audits should be appropriately resourced and completed in accordance with an agreed schedule. This schedule should ensure that files are available for our review prior to the year end.</p> | <p>In the year under review, the financial audit team suffered a loss of resources due to serious long term illness of two key experienced members. The resourcing of the financial audit team has been reviewed and an additional qualified accountant post will be created and advertised. Filling of two other vacancies will be progressed in tandem with the recruitment of the new qualified post.</p> <p>Slippage in quality of working papers is acknowledged to an extent and will be addressed through the arranging of an "in house" Institute of Internal Auditors (IIA) training course for staff on producing quality audit work papers. Guidance on sampling methodology will be sought from Audit Scotland. In the reporting year, work scheduling was disrupted by staff sickness but given additional resourcing going forward Audit Scotland requests for specific AAU files should be met .</p> | Head of Audit and Assurance | December 2015 |

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| Paragraph/ action point | Issue/ risk/ recommendation | Management action/response | Responsible officer | Target date |
|-------------------------------|--|--|-------------------------------|---------------|
| Wider audit issues | | | | |
| 69/ 5 | <p>Corporate governance</p> <p>Our review of SPS governance arrangements identified a number of recommendations relating to the role and effectiveness of the Board and RMAC.</p> <p>Risk</p> <p>The Board and RMAC may not be fully effective in their governance and scrutiny roles.</p> <p>Recommendation</p> <p>SPS should continue to progress the implementation of recommendations included in our Review of governance arrangements report.</p> | <p>Following receipt and consideration of the Audit Scotland review of SPS governance arrangements, the Chief Executive confirmed that there would be a clear focus on reviewing and refreshing the organisation’s corporate governance arrangements in 2015/16. Work commenced on the review of the corporate governance arrangements at the beginning of May 2015 and is scheduled to conclude prior to Audit Scotland requesting a formal update in early 2016. As outlined in paragraph 62, Audit Scotland have been updated on progress with this review.</p> | Office of the Chief Executive | February 2016 |

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| Paragraph/ action point | Issue/ risk/ recommendation | Management action/response | Responsible officer | Target date |
|-------------------------------|---|--|--|---------------|
| 69/ 6 | <p>Risk management</p> <p>Our review of SPS governance arrangements review noted that risk management arrangements were not well developed and this remained the case throughout the financial year.</p> <p>Risk</p> <p>Risk management procedures are not sufficiently robust.</p> <p>Recommendation</p> <p>SPS should implement the agreed approach to organisation-wide risk management arrangements which is now being taken forward by the Corporate Risk Manager</p> | <p>Risk management arrangements have evolved significantly since March 2015. However, this is a continuing process which will require to be implemented over the longer term. Phases 1 and 2 of this implementation will be complete by December 2015 and included within these phases will be:</p> <ul style="list-style-type: none"> • production of Risk Management Strategy document and supporting user guidance • production of Risk Appetite Statement • revised and refreshed Corporate Risk Register reflecting real and relevant strategic threats to the business • production of likelihood and impact matrices • workshop sessions to improve risk awareness and inform better department, prison and / or project risk registers. | <p>Head of Audit and Assurance</p> <p>Corporate Risk Manager</p> | December 2015 |

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| | | Organisational wide risk management arrangements will not remain static and the above will remain under review to ensure that it remains appropriate for the business. | | |

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|-------------------------------|--|---|--------------------------------|--|
| 74/ 7 | <p>Organisational review</p> <p>The Chief Executive is currently supported by only two executive directors and the Head of CCU post is filled on a temporary basis.</p> <p>Risk</p> <p>Insufficient leadership capacity could impact on SPS' ability to deliver the change programme.</p> <p>Recommendation</p> <p>Succession planning should ensure that there are individuals, within the organisation, who have the appropriate skills to cover senior management positions in the absence of the permanent postholder. A timetable for the appointment of a permanent Head of CCU should be agreed.</p> | <p>Timetable for the appointment of a permanent Head of CCU</p> <p>This position is currently being assessed through Job Evaluation (at appeal stage). Once this is completed, recruitment can commence.</p> <p>Estimated timelines:</p> <ul style="list-style-type: none"> • conclusion of Job Evaluation – September 2015 • conclusion of recruitment process (provisional offer) – November 2015 • appointment to role – February 2016. <p>These timescales are dependent on line manager availability and candidate notice period.</p> <p>Succession planning</p> <p>An approach to assessing potential succession planning risks has been developed and has been identified as a corporate deliverable. Following pilot</p> | Director of Corporate Services | <p>Appointment of Head of CCU - February 2016</p> <p>Succession planning - December 2015</p> |

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| | | <p>work in Corporate Services Directorate, this will be rolled out to senior management positions (by Q3 2015/16). This approach will classify risk to allow appropriate targeting of resourcing to ensure that there are appropriate skills to cover senior management positions.</p> <p>This is being completed alongside wider commissioned project work to enhance succession planning and talent.</p> | | |

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|-------------------------------|---|---|-------------------------------|---------------|
| 77/ 8 | <p>Transparency</p> <p>SPS holds all Board meetings in private. There is restricted access to Board papers, the RMAC terms of reference and the Board members' register of interests.</p> <p>Risk</p> <p>There is a risk that SPS is not sufficiently open and transparent.</p> <p>Recommendation</p> <p>SPS should consider implementing the recommendations relating to openness and transparency in decision making contained in the Scottish Government's On Board guidance.</p> | <p>The review of corporate governance arrangements will consider all recommendations made in the Audit Scotland review of SPS governance arrangements. It is worth noting that it has been acknowledged that the Scottish Government's 'On Board' guidance does not translate easily into the Executive Agency environment. Discussions are on-going between the Scottish Government Delivery Bodies Group and the Public Bodies Unit to produce a revised version of On Board for Executive Agencies. SPS has been invited to and will participate in a short-life working group for this purpose.</p> | Office of the Chief Executive | February 2016 |

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| Paragraph/ action point | Issue/ risk/ recommendation | Management action/response | Responsible officer | Target date |
|-------------------------------|---|---|---------------------|---|
| 100/ 9 | <p>ISS projects</p> <p>There is no detailed plan to support delivery of the Digital Strategy for Justice. Business continuity and data recovery testing has been postponed. In addition, there have been delays with the implementation of digital procurement and HR facilities.</p> <p>Risk</p> <p>There is a risk that a number of ISS activities are subject to ongoing delays. This could result in a failure to address business needs including the implementation of e-procurement facilities in accordance with the EU Directive.</p> <p>Recommendation</p> <p>SPS should ensure that delays in the ISS activities identified above are addressed in accordance with an agreed timetable.</p> | <p>The business cases for the Digital Strategy for Justice have been received and will be considered at the Programme Direction Group meeting in August 2015. Due to the complexity of what is being proposed it is not possible to provide any estimated dates for the completion of a detailed plan to support delivery as they are fully dependent on decisions made at the Programme Direction Group.</p> <p>The digital procurement project was placed on hold following a Gateway Review. An options appraisal and action is being developed prior to baselining the project. A recommendation is expected late September.</p> <p>The e-HR project has been subject to various delays but has now passed across to ISS ownership since May 2015. The project has been re-baselined with the roll-out of</p> | Head of IT | <p>Detailed plan to support the Digital Strategy for Justice - subject to decisions made at the Programme Direction Group Digital procurement project – September 2015</p> <p>e-HR project – September 2015</p> |

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| | | <p>functionality scheduled to commence in September 2015.</p> <p>To assure delivery of the full portfolio of ISS activities in line with business expectations, all projects are now reporting into the Information Technology (IT) programme board.</p> | | |

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| 117/ 10 | <p>Capital investment programme</p> <p>Limited progress has been made in addressing the risks reported in our review of the SPS capital investment programme.</p> <p>Risk</p> <p>There is a risk that the prison estate is not fit for purpose and does not support the overall aims and objectives of SPS and national outcomes of the Scottish Government.</p> <p>Recommendation</p> <p>Our report on the capital investment programme should be revisited and the management responses updated to reflect organisational responsibilities for implementing the capital programme.</p> | <p>The report on the capital investment programme has been re-visited and the management responses and responsibilities have been updated.</p> | Chief Executive | July 2015 |