

Office of the Scottish Charity Regulator

Report on the 2005-06 Audit

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 Executive and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds



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Executive Summary

Introduction

In 2005-06 we audited the financial statements of the Office of the Scottish Charity Regulator (OSCR) and looked at aspects of performance management and governance. This report sets out our key findings.

Financial Statements

We have given an unqualified opinion on the financial statements of the agency for 2005-06.

At the planning stage we identified nine main audit issues and risks which informed our audit procedures. From our audit work we can conclude that these issues and risks are being satisfactorily managed by OSCR.

Governance

OSCR's corporate governance and control arrangements operated satisfactorily in the period under review as reflected in the Statement on Internal Control. We have also found the work of the internal audit service to be satisfactory and continue to place formal reliance on its work.

Performance Management

During 2005-06 we completed a baseline analysis of larger organisations' management arrangements for achieving Best Value and an overview of their management arrangements in relation to the requirements of the Scottish Executive's Efficient Government Initiative. OSCR was not included in either of these exercises.

I would like to record my thanks to management and staff for their co-operation and assistance.

Alastair Reid, Senior Audit Manager, 17 November 2006

Introduction

Scope of the Audit

1. This report summarises the findings from our 2005-06 audit of OSCR. The scope of the audit was set out in our Audit Plan which was submitted to OSCR in March 2006. This plan described the work we planned to carry out on financial statements, governance and performance.
2. This report to management sets out our findings from the review carried out. The weaknesses outlined are only those which have come to our attention during the course of our normal audit work and are not necessarily, therefore, all the weaknesses which may exist. Although we include a number of specific recommendations in this report to strengthen internal control, it is the responsibility of management to determine the extent of the internal control system appropriate to OSCR. We would stress, however, that an effective internal control system is an essential part of the efficient management of any organisation.
3. The contents of this report have been agreed with relevant officers to confirm factual accuracy.
4. This report will be submitted to the Auditor General for Scotland and will be published on our website at www.audit-scotland.gov.uk.

Outcome on Issues and Risks Identified in the Audit Plan

5. Nine audit issues and risks were identified at the planning stage. The outcome of our reviews of these issues is summarised at Appendix A. We can conclude from the results of our work on these issues and risks that they are being satisfactorily managed by OSCR and do not indicate areas of material concern.

Prior Period Follow Up

6. Two issues were identified in our Report on the Audit of the 2004-05 accounts. We note that progress has been made in improving creditor payment systems but that training is still needed on SEAS report writing.

Management Action

7. Audit recommendations, together with management comments, on those areas where further improvements could be achieved are included in the action plan at Appendix B of this report.

Financial Statements

Our Responsibilities

8. We audit the financial statements and give an opinion on whether:

- they give a true and fair view, in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers, on the state of affairs of the Office of the Scottish Charity Regulator as at 31 March 2006 and of its net operating cost, recognised gains and losses and cash flows for the year then ended
- they and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers
- in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

9. We also review the Statement on Internal Control by:

- considering compliance with Scottish Executive guidance
- considering the adequacy of the process put in place by the Accountable Officer to obtain assurances on systems of internal control
- assessing whether disclosures in the Statement are not inconsistent with the information emerging from our normal audit work.

Overall Conclusion

10. We have given an unqualified opinion on the financial statements of OSCR for 2005-06. We are able to conclude that the financial statements of OSCR give a true and fair view of the financial position for the year from 1 April 2005 to 31 March 2006 and that, in all material respects, the expenditure and receipts shown in the financial statements were incurred or applied in accordance with applicable enactments and relevant guidance.
11. Following discussion with the head of Resource Management, a date of 7 July 2006 was agreed for the provision of the accounts for audit. Accordingly audit work was scheduled to achieve a certification date that would permit the laying of the accounts before the Scottish Parliament by the

end of October. Accounts were duly submitted on the agreed date and the completion timetable largely achieved.

Financial Performance

12. OSCR's operating cost statement for the year records net operating costs of £1.706 million.

Statement on Internal Control

13. The Statement on Internal Control was signed by the Chief Executive on 15 November 2006. This set out the arrangements operated for risk identification and review, management of identified risks and assurance of effectiveness.

14. We are satisfied that the Statement complies with Scottish Executive guidance, the process put in place by the Accountable Officer to obtain assurances on systems of internal control is adequate and the contents of the Statement are not inconsistent with the information emerging from our normal audit work.

ISA 260: Communication of Audit Matters to Those Charged with Governance

15. My responsibilities in relation to the communication of audit matters to those charged with governance are covered in International Standard on Auditing 260 and outcomes against the requirements of the Standard were reported in a letter to the Accountable Officer on 1 November 2006.

16. There are no significant judgements included in the accounts on which we wish to comment.

17. As part of the audit process we did not identify any accounting adjustment that was required.:

18. A number of other minor errors were identified that did not require adjustment:

- Fixed assets are understated by £1,000 as VAT on a fit-out invoice was incorrectly treated as recoverable;
- As a result of the de-minimus of £10,000 set by the Scottish Executive for accruals, there is an estimated understatement of £20,000

19. There are no other significant points arising out of the letter.

Issues Arising

20. We would like to draw attention to the following issues arising from our audit of the financial statements:

- accruals levels

Action point 1

- development of year end procedures

Action Point 2

- furniture capitalisation

Action Point 3

- version control

Action Point 4

Governance

Introduction

21. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of an organisation. This section sets out the main findings arising from our review of OSCR's corporate governance as it relates to:

- fraud prevention and detection arrangements
- systems of internal control
- review of internal audit.

Overall Conclusion

22. During our audit we reviewed the governance systems operating at OSCR. In general, we are content that they are soundly based.

Fraud Prevention and Detection Arrangements

23. OSCR's arrangements for preventing and detecting fraud and corruption were assessed during the audit and found to be satisfactory. No frauds were identified by OSCR in 2005-06.

Systems of Internal Control

24. See paragraph 20 for recommendations on systems of internal control.

Review of Internal Audit

25. OSCR recognises that internal audit is a key element of the internal control system set up by management. A strong internal audit function is necessary to ensure the continuing effectiveness of the internal control system that has been established. To maximise the reliance that external audit can place on internal audit and to avoid duplication of effort, the adequacy of internal audit is assessed each year.

26. Internal audit is provided by Scottish Executive Audit Services. Audit Scotland's Scottish Executive audit team carried out a review of the Executive's arrangements for internal audit as part of 2004-05 audit work. As part of 2005-06 audit work they have assessed Audit Services' progress in implementing the agreed action plan from 2004-05. Their review of Audit Services' working paper

files confirms that they continue to comply with Government Internal Audit Standards in adopting a risk based audit approach in planning and undertaking their work. As a result we intend to place reliance on a number of aspects of Audit Services' work during 2005-06 as was anticipated in our audit plans.

27. We planned to place formal reliance on the work of internal audit, in terms of the International Statement on Auditing 610 (considering the work of Internal Audit), for our financial statements audit work, in the following areas:
 - arrangements for setting and monitoring budgets, making payments and collecting income
 - financial reporting
 - procurement
 - travel and subsistence payments.
28. A report was produced by Scottish Executive Internal Audit during 2005-06. We reviewed the report. None of the observations and related risks precluded planned assurance from being taken for our financial statements audit.
29. The Head of Internal Audit provided the Chief Executive with substantial assurance on the adequacy and effectiveness of the system of internal control within the Agency.

Performance Management

Introduction

30. This section covers our assessment of the way in which organisations secure value for money in the use of their resources. This year we focussed on two main areas:

- Efficient Government
- Best Value.

Efficient Government

31. The Efficient Government initiative is a 5 year programme with the aim of reducing waste, bureaucracy and duplication in Scotland's public sector. The primary objective is to deliver the same services with less money or to enable frontline services to deliver more or better services with the same money. The Efficient Government Plan sets targets to achieve of £745 million (rising to £900 million) of cash-releasing savings and £300 million (rising to £600 million) of time-releasing savings, by 2007-08.

32. During 2005-06 Audit Scotland completed a management arrangements diagnostic on Efficient Government activities across a number of Central Government organisations. It aimed at providing baseline information on arrangements across a range of Efficient Government related topics. We concentrated on the largest organisations and did not include OSCR.

33. A detailed position statement of the sample of public sector organisations in Scotland is being produced by Audit Scotland and will be issued shortly.

Best Value

34. There is no statutory duty of Best Value in the wider public sector in Scotland (the Scottish Executive and its Executive Agencies, Executive NDPBs, and the NHS). Instead, the Scottish Executive issued high level guidance in May 2003, followed by more detailed draft secondary guidance in August 2003. This duty can be described as:

- to make arrangements to secure continuous improvement in performance (while maintaining an appropriate balance between quality and cost)
- to have regard to economy, efficiency and effectiveness, and the equal opportunity requirements
- to contribute to the achievement of sustainable development.

35. In May 2005, Ministers decided that they would not bring forward legislation which extends Best Value in the wider public sector. However, as Ministers do wish to encourage and embed the principles of Best Value across the wider public sector, revised guidance was issued in May 2006.
36. For 2005-06 Audit Scotland reviewed how well advanced arrangements are in place by public bodies across the central government sector to demonstrate Best Value, and to identify areas of good practice. As part of this review we completed a Best Value analysis to establish baseline information on the management arrangements in place within the larger organisations. The overall aim of this analysis was to establish the organisations' arrangements for taking forward the Best Value agenda and demonstrating continuous improvement. We concentrated on the largest organisations and did not include OSCR.
37. The results of the review across the wider public sector are currently under review and will be published by Audit Scotland during 2006.

National Studies

38. The Central Government team within the Performance Audit division of Audit Scotland has recently published on behalf of the Auditor General a study entitled "Relocation of Scottish Executive Departments, agencies and NDPBs".
39. The report notes that 28 public sector bodies have been, or will be, either relocated or established under the Scottish Executive's relocation policy, introduced in 1999. 1,653 posts have been transferred from Edinburgh and a further 1,164 posts have been created outside the city. Audit Scotland examined the implementation of location and relocation in Scotland. It reviewed the process and management of relocation and looked at evidence of the impact of the moves. Around 34,000 public sector employees (six per cent of the public sector workforce) are in posts which could be considered for relocation under the policy.
40. Audit Scotland found that most of the reviews arose from the creation or restructuring of organisations, or from breaks in property leases. Only two of 38 reviews were the result of potential efficiency improvements identified by the organisations in their business plans. In most cases, it was not clear whether relocation would deliver wider policy objectives.
41. The Auditor General for Scotland, Robert Black said: "The Executive has plans to evaluate the impact of the policy but little has been done to date. For this reason it is difficult to determine whether relocations are good value for money."

42. Key findings in the report include that:

- there is some limited evidence of efficiency gains from relocation, such as lower staff turnover and reductions in sick leave in specific relocations, but wider benefits have not so far been measured
- the estimated cost per job for the relocation of individual organisations range between a saving of £33,000 per job and a cost of £45,000 per job
- the Executive does not have explicit targets for relocation and it has not identified areas of the country expected to benefit from its policy
- In some cases, new or revised criteria to identify potential sites for relocation were introduced late in the review process.

43. Robert Black said: “I would encourage the Scottish Executive to define more clearly the measures of success that it is applying to its relocation policy and to develop its plans for evaluating the benefits of relocation.”

44. OSCR was one of the organisations surveyed and details were provided in Appendix 3: Case study narratives. No comments were made on the process or management of the relocation to Dundee.



Appendix A: Outcome on Issues and Risks Identified in the Audit Plan

| Audit Issues and Risks | Outcome |
|--|---|
| <p>1. The accounting records are maintained by the Scottish Executive on the Scottish Executive Accounting System (SEAS). In previous years several adjustments had to be made to the draft financial statements to correct mis-postings made.</p> | <p>There remain issues with the provision of information by the Scottish Executive. Additional training is to be provided to OSCR staff to ensure in future they can access the required reports.</p> |
| <p>2. Several employees have been seconded from other organisations, with OSCR being issued invoices for their salary costs, it must therefore be ensured that the full cost for the period of service is included in the financial statements</p> | <p>There were no issues with the allocation and recording of costs for seconded employees.</p> |
| <p>3. The organisation is in its second full year of operation and the system of internal control is still evolving, and will continue to do so with the organisation's transition to a non-ministerial department from 2005/06;</p> | <p>Scottish Executive Internal Audit report concluded that OSCR has made 'significant progress in developing good governance systems', and that 'substantial assurance' can be provided that OSCR is able to meet its objectives.</p> |
| <p>4. The Audit Committee was only established in October 2004 with non-executive directors only being appointed in November 2004.</p> | <p>The Scottish Executive Internal Audit report was positive about the developments in this area, with the Terms of Reference being in line with the Scottish Public Finance Manual.</p> |
| <p>5. To enable both executive and non-executive directors to fully discharge their duties, it is important that they receive adequate induction and on-going training. Within OSCR, the director training programme is still evolving;</p> | <p>The formal training programme is currently being developed. All new staff are issued with an induction pack.</p> |

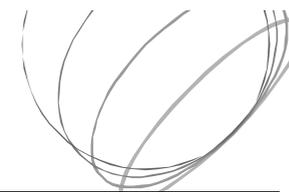
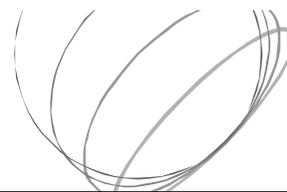


| Audit Issues and Risks | Outcome |
|--|---|
| 6. Risk register is not regularly reviewed and updated | The risk register is reviewed quarterly by the SMT. All staff were issued with a copy in August 2005, and it is proposed that an annual meeting will be held to enable staff to become involved with the identification and review of risks. |
| 7. Better coordination of desk procedures and standing financial instructions is required. | OSCR continues to rely on guidance issued by the Scottish Executive, together with specific guidance. It was suggested by Internal Audit that this could be better collated. Audit Scotland has recommended the introduction of year end procedures. <i>See paragraph 20 and action plan point 2</i> |
| 8. Changes to the accounts format, particularly the Annual Report, are required under the Financial Reporting manual (FReM); | The revised requirements of FReM were included in the 2005-06 accounts. Audit Scotland provided advice on the contents. |
| 9. Changes to the accounting personnel preparing the accounts | Most of the accounts preparation was completed by the outgoing Finance Manager. Audit Scotland liaised with the new Finance Manager and continuity was successfully maintained. |

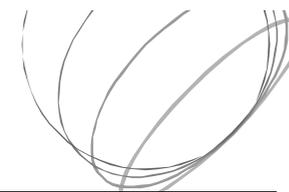
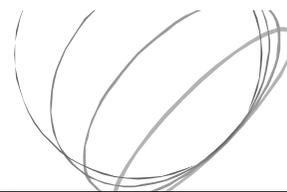


Appendix B: Action Plan: Recommendations for Further Improvements

| Action Point | Para. No | Issue, Risk and Audit Recommendation | Importance | Management Response | Responsible Officer | Target Date |
|--------------|----------|---|------------|--|--------------------------------|-------------|
| 1 | 20 | <p>Accruals</p> <p>In line with Scottish Executive guidelines the level set for inclusion as an accrual was £10,000. This has resulted in an understatement of which is not considered to be material to this year's accounts.</p> <p>There is a risk that there could be a material misstatement to expenditure figures in the accounts.</p> <p>We recommend that consideration should be given to reducing the de-minimis for inclusion within Office of the Scottish Charity Regulator to more accurately reflect the financial position at the year end.</p> | Medium | We will consider reducing the de —minimis as part of our work in respect of the preparation of the 2006/07 Annual Report and Accounts. | Anne Monk — Finance Manager | 31.03.07. |



| Action Point | Para. No | Issue, Risk and Audit Recommendation | Importance | Management Response | Responsible Officer | Target Date |
|--------------|----------|---|------------|---|--------------------------------|-------------|
| 2 | 20 | <p>Year end procedures</p> <p>OSCR does not currently have written procedures for the production of its annual accounts. It relies partly on the procedures of the Scottish Executive. The information in the accounts comes from a number of sources both internal and external to OSCR.</p> <p>There is a risk that component parts of the accounts may not be completed on time. The move to a Non Ministerial Department in 2006-07 may require additional accounts consultation. There is also a risk that OSCR may not have sufficiently efficient procedures to implement the 'faster closing' agenda.</p> <p><i>We recommend that OSCR draws up year end procedures for its 2006-07 accounts in consultation with the Scottish Executive</i></p> | Medium | Noted. We had recognised this as an issue, particularly in light of our NMD status, and the Finance Manager's targets for 2006/07 include the development of year-end procedures in respect of annual accounts. | Anne Monk — Finance Manager | 31.03.06 |



| Action Point | Para. No | Issue, Risk and Audit Recommendation | Importance | Management Response | Responsible Officer | Target Date |
|--------------|----------|---|------------|---|--------------------------------|-------------|
| 3 | 20 | <p>Fixed Asset Accounting</p> <p>A review of the fixed assets identified a discrepancy in the treatment of some items of furniture. The accounting policies note that <i>'In line with the Scottish Executive policy OSCR does not capitalise furniture and fittings and the full cost is included in the Operating Cost Statement in the year of acquisition.'</i> Testing identified that several items had been grouped together and included in the Fixed Asset register and although the total amount is only £1,000 it results in an overstatement of the fixed assets at the year end.</p> <p>There is a risk that fixed assets and subsequently depreciation could be overstated in the accounts.</p> <p><i>We recommend that staff should be reminded of the relevant treatment of these items in the asset register.</i></p> | Medium | Noted. We had already identified the need to consider and refine our arrangements in respect of Fixed Assets, and specifically the maintenance and review of the Fixed Asset Register, and included this in the Finance Manager's workplan. | Anne Monk — Finance Manager | 31.12.06 |



| Action Point | Para. No | Issue, Risk and Audit Recommendation | Importance | Management Response | Responsible Officer | Target Date |
|--------------|----------|--|------------|--|-----------------------------|-------------|
| 4 | 20 | <p>Final Account Version Control</p> <p>During the audit, there was confusion over the versions of draft accounts supplied to Audit Scotland.</p> <p>There is a risk that errors identified during the course of the audit may not be corrected at the final stage if the wrong draft is used.</p> <p><i>We recommend that OSCR agree the form of version control that will operate with electronic drafts. We also recommend that OSCR consider using the properties function of Microsoft Word to record the version details.</i></p> | Medium | <p>The draft accounts were stored on the Objective eRDM system in July 2006. At that point the system had been operational for only a limited time, and staff were still learning how to effectively store and retrieve documents, and how to ensure effective version control. To address this point, a procedures/guidance note on this subject will be drafted and circulated to all staff.</p> | Head of Resource Management | 30.11.06 |



Appendix C: Auditor General for Scotland published reports

Auditor General for Scotland

Relocation of Scottish Executive departments, agencies and NDPBs (published 21/9/2006)

1,653 posts have been transferred from Edinburgh and a further 1,164 posts have been created outside the city. Audit Scotland found that most of the reviews arose from the creation or restructuring of organisations, or from breaks in property leases. Only two of 38 reviews were the result of potential efficiency improvements identified by the organisations in their business plans. In most cases, it was not clear whether relocation would deliver wider policy objectives.

Accounts Commission and Auditor General for Scotland

No hiding place: the National Fraud Initiative in Scotland (published 17/05/2006)

Scotland's councils have worked with other public bodies to identify £15m worth of fraud and errors in a national detection exercise.

Auditor General for Scotland

Leadership development: How Government Works (published 17/11/2005)

Scotland's public sector has good examples of investment in leadership but many individual organisations do not have clear policies and most are unable to link the spending to improvements in their performance. Public bodies need to do more to track the £5m they invest each year in leadership development and make sure it results in better managed organisations and better public services, says Audit Scotland.

Auditor General for Scotland

Scottish Executive: supporting new initiatives. How Government Works (published 10/11/2005)

Last year the Scottish Executive launched new initiatives amounting to £1.4 billion. The management of these projects is generally sound, but making changes could help to improve control of the funding and allow better assessment of whether the money is helping to achieve policy aims.



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