

Historic Scotland

Report on the 2007/08 Audit

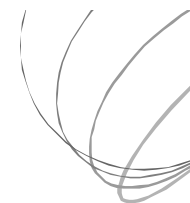


September 2008



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Executive Summary

Introduction

In 2007/08 we looked at the key strategic and financial risks faced by Historic Scotland. We audited the financial statements and we also reviewed aspects of performance management and governance. This report sets out our key findings.

Financial Position

Historic Scotland's outturn for 2007/08 was net expenditure of £50.2 million (2006/07: £44.1 million). This resulted in an overspend of £0.1 million against the resource budget allocated by the Scottish Government. This overspend was approved by the Scottish Government. In 2007/08 Historic Scotland's net assets increased by £624,000 to £25.621 million.

For 2008/09 Scottish Ministers have agreed resource cover for Historic Scotland of £51.7 million. This comprises £71.6 million to cover operating expenditure, £4.7 million of capital expenditure, less retained income and capital receipts of £24.6 million. Historic Scotland's initial internal budget for 2008/09 showed an over-commitment of £0.5 million against the original plans, similar to the initial position in 2007/08. However the current forecast for income for the year has reduced by £1.2 million, due to reduced visitor numbers, increasing the estimated over-commitment. Historic Scotland is currently developing plans to identify savings to reduce this over-commitment. This represents a significant challenge to the organisation.

Financial Statements

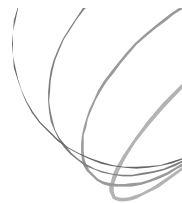
We have given an unqualified opinion on the financial statements of Historic Scotland for 2007/08.

We have also concluded 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 issued by Scottish Ministers.

Performance

Historic Scotland published its corporate plan in October 2005 for the period 2005-2008. Included in the plan is a summary of ten key performance targets against which the effectiveness of the corporate plan could be evaluated over the period. The Scottish Government's Internal Auditors reported that, in 2007/08, the last year covered by the corporate plan, Historic Scotland met or exceeded all ten key performance targets (2006/07: nine targets of the ten were achieved). This was a good performance for Historic Scotland.

A corporate plan for the period 2008-2011 has been drafted and was approved by the Scottish Ministers in September 2008. The new corporate plan details Historic Scotland's plans to contribute to the targets



and outcomes in the National Performance Framework and the Framework Document aims. The corporate plan lists nine key performance targets for the three-year period, each of which is supported by a number of business improvement targets.

Best Value

Historic Scotland completed a baseline review of Best Value arrangements in 2005/06. Since that time, the Agency has undertaken regular updates against self-assessment criteria and the majority of the recommendations arising from the 2005/06 review have been implemented, resulting in changes in Historic Scotland's governance and operational processes.

Governance

Corporate governance is concerned with the structures and processes for decision-making, accountability, control and behaviour at the upper levels of an organisation. Overall, the corporate governance and control arrangements for Historic Scotland operated satisfactorily during the year, as reflected in the Statement on Internal Control.

We examined the key financial systems which underpin the organisation's control environment. We concluded that financial systems and procedures operated sufficiently well to enable us to place reliance on them.

Looking forward

The final part of our report notes some key risk areas for Historic Scotland going forward. We highlighted a number of national issues which affect all public sector bodies including Historic Scotland, including the introduction of Scotland Performs; the impact of international financial reporting standards; and the review of data handling arrangement in public bodies across Scotland. Historic Scotland faces a number of other specific challenges over the next year to achieve its new efficiency target and its key performance target on income. We will continue to monitor the performance of Historic Scotland.

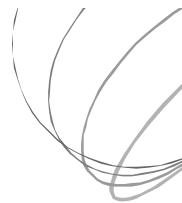
The assistance and co-operation given to us by board members and staff during our audit is gratefully acknowledged.

Audit Scotland
September 2008



Introduction

1. This report summarises the findings from our 2007/08 audit of Historic Scotland. The scope of the audit was set out in our Audit Plan, which was presented to the Audit Committee on 15 February 2008. This plan set out our views on the key business risks facing the organisation and described the work we planned to carry out on financial statements, performance and governance.
2. We have issued a range of reports this year, and we briefly touch on the key issues we raised in this report. Each report set out our detailed findings and recommendations and the board's agreed response.
3. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officers and members of Historic Scotland during the course of our audit. This report will be submitted to the Auditor General for Scotland and will be published on our website, www.audit-scotland.gov.uk.



Financial Position

4. In this section, we summarise key outcomes from our audit of Historic Scotland financial statements for 2007/08, and comment on the key financial management and accounting issues faced. The financial statements are an essential means by which the organisation accounts for its stewardship of the resources available to it and its financial performance in the use of those resources.

Our responsibilities

5. We audit the financial statements and give an opinion on:
 - whether they give a true and fair view of the financial position of Historic Scotland and its expenditure and income for the period in question;
 - whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements;
 - the consistency of the information which comprises the management commentary with the financial statements; and
 - the regularity of the expenditure and receipts.
6. We also review the statement on internal control by:
 - considering the adequacy of the process put in place by the chief executive as accountable officer to obtain assurances on systems of internal control; and
 - assessing whether disclosures in the statement are consistent with our knowledge of Historic Scotland.

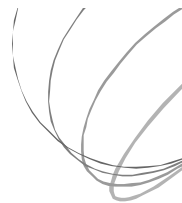
Overall conclusion

7. We have given an unqualified opinion on the financial statements of Historic Scotland for 2007/08.
8. As agreed, the unaudited accounts were provided to us on 12 May 2008, supported by a comprehensive working paper package. The good standard of the supporting papers and the timely responses from Historic Scotland staff allowed us to conclude our audit within the agreed timetable and provide our opinion to the Audit Committee on 16 June 2008, as timetabled.

Financial Position

Outturn 2007/08

9. Historic Scotland is required to work within its resource budget set by the Scottish Government. The budget covers both revenue and capital expenditure. The Scottish Government approved a total



expenditure budget for the year of £52.1 million, against which the Agency achieved a final outturn of £52.2 million. The overspend of £0.1 million on the resource budget mainly related to two major developments being completed during the year at Stanley Mills and Edinburgh Castle Visitor Reception centre and the subsequent related charge against the impairment budget. The overspend was approved by the Scottish Government.

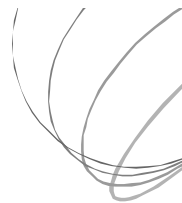
10. Historic Scotland's net assets increased by £0.624 million to £25.621 million in 2007/08.

2008/09 Budget

11. Scottish Ministers have set Historic Scotland's initial resource budget for 2008/09 at £51.7 million. This is in line with the 2007/08 budget when one off capital funding is excluded from the budget totals. The 2008/09 budget comprises:
 - a running costs budget of £39.6 million;
 - a programme costs budget of £32.0 million;
 - a capital budget of £4.7 million; and
 - an adjustment for retained income and capital receipts budget of £24.6 million.
12. Historic Scotland's initial internal budget for 2008/09 showed an over-commitment of £0.5 million against the original plans, similar to the initial position in 2007/08. However the current forecast for income for the year has reduced by £1.2 million, due to reduced visitor numbers, increasing the estimated over-commitment. Historic Scotland is currently developing plans to identify savings to reduce this over-commitment. This represents a significant challenge to the organisation. The budget is monitored throughout the year and budget adjustments will be sought if required. Senior management anticipate there will be no overspend at the year end, and the position managed to bring expenditure in within budget requirements.

Issues arising from the audit

13. As required by auditing standards, we reported to the Audit Committee in 16 June 2008 the main issues arising from our audit of the financial statements. One key issue was reported.
14. **Donated assets** – Historic Scotland received a donation of £165,000 from the Historic Scotland Foundation to help to fund the weaving of a tapestry, which was initially treated as income received in the year. Income from donations to fund expenditure on assets should be taken directly to reserves at the date of receipt and not treated as income. The accounting treatment was amended in the final accounts.



Regularity assertion

15. The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors that requires us to certify that, in all material respects, the expenditure and receipts shown in the accounts were incurred or applied in accordance with applicable enactments and guidance issued by Scottish Ministers. We have addressed the requirements of the regularity assertion through a range of procedures, including written assurances from the accountable officer as to his view on adherence to enactments and guidance. No significant issues were identified for disclosure.



Governance

Overview of arrangements

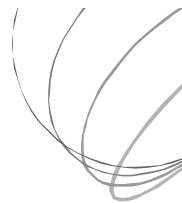
16. This section sets out our main findings arising from our review of Historic Scotland governance arrangements. This year we reviewed:
 - key systems of internal control;
 - internal audit; and
 - aspects of information and communications technology (ICT).
17. We also discharged our responsibilities as they relate to prevention and detection of fraud and irregularity, standards of conduct and the organisation's financial position (see paragraphs 9 to 10). Our overall conclusion is that arrangements within Historic Scotland are sound and have operated through 2007/08.

Corporate Plan

18. A revised Framework Document for Historic Scotland has been approved by Scottish Ministers which sets out the framework for the operation of the Agency. The new Framework Document defines three aims which will contribute to the Scottish Government's purpose of increasing sustainable growth. These aims are to care for; protect and enhance the historic environment; to secure greater economic benefits from the historic environment; and to help people value, understand and enjoy the historic environment.
19. A corporate plan for the period 2008-2011 has been drafted and was approved by the Scottish Ministers in September 2008. The new corporate plan details Historic Scotland's plans to contribute to the targets and outcomes in the National Performance Framework and the Framework Document aims. The corporate plan lists nine key performance targets for the three-year period, each of which is supported by a number of business improvement targets. The delivery of the corporate plan objectives will be particularly challenging given the tight financial constraints over the same period. This is an area we will keep under review during our appointment.

Systems of internal control

20. Key controls within systems should operate effectively and efficiently to record financial transactions accurately and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In his annual report for 2007/08, the Scottish Government Internal Audit Division's Audit Manager provided his opinion that, based on the internal



audit work undertaken during the year, there was substantial assurance given on the adequacy and effectiveness of the systems of internal control.

21. As part of our audit, we reviewed the high-level controls in a number of Historic Scotland systems that impact on the financial statements. Our overall conclusion was that key controls were operating effectively.

Prevention and detection of fraud and irregularities

22. Historic Scotland has appropriate arrangements in place to prevent and detect fraud, inappropriate conduct and corruption, including policies and codes of conduct for staff and board members.

Internal Audit

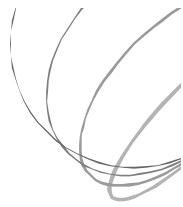
23. The establishment and operation of an effective internal audit function forms a key element of effective governance and stewardship. We therefore seek to rely on the work of internal audit wherever possible, and, as part of our risk assessment and planning process for the 2007/08 audit, we assessed whether we could place reliance on Historic Scotland's internal audit function. We concluded that the internal audit service operates in accordance with the Government Internal Audit Manual and therefore placed reliance on their work in number of areas during 2007/08, as we anticipated in our annual audit plan.

Statement on Internal Control

24. The Statement on Internal Control provided by Historic Scotland's Accountable Officer reflected the main findings from both external and internal audit work. This recorded management's responsibility for maintaining a sound system of internal control and set out Historic Scotland's approach to this.

Information and Communication Technology

25. As part of our 2007/08 audit, we planned to carry out a follow up review of the progress that Historic Scotland has made in implementing actions agreed during the 2006/07 review we carried out which provided a high-level risk based assessment of ICT services in Historic Scotland. As part of their follow-up work on their IT review, the Scottish Government Internal Audit Division are to include the follow-up of the agreed actions from our report and this work is scheduled to be carried out later this year.

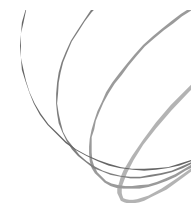


Performance Management

26. Public audit is more wide-ranging than in the private sector and covers the examination of, and reporting on, performance issues and value for money. As part of our audit, we are required to plan reviews of aspects of the arrangements to manage performance as they relate to economy, efficiency and effectiveness in the use of resources.
27. Accountable officers also have a duty to ensure the resources of their organisation are used economically, efficiently and effectively. These arrangements were extended in April 2002 to include a duty to ensure 'best value' in the use of resources.

Best Value developments

28. The positive impact of the best value concept in local government led Scottish Ministers to introduce a non-statutory Best Value duty on all public sector accountable officers (ie, across health and central government) in 2002. This was reinforced by refreshed Ministerial guidance in 2006, highlighting the importance that the Scottish Government places on Best Value as a means of supporting public service reform.
29. That position was again re-iterated in the Scottish Government's recent response to the Crerar scrutiny review which credited the Best Value regime as a key driver of modernisation and improvement in public services. Audit Scotland is committed to extending the Best Value audit regime across the whole public sector, and significant development work has taken place over the last year.
30. The framework for our proposed Best Value audit approach was agreed by Audit Scotland's Corporate Management Team in September 2007. It is based on the key principles of flexibility and proportionality, alignment and integration with our existing activities, being delivered within our existing resources and with an evolutionary implementation.
31. Using the Scottish Government's nine Best Value principles as the basis for our audit activity, we have identified five priority development areas (Use of Resources, Governance and Risk Management, Accountability, Review and Option Appraisal, and Joint Working) for our initial development work.
32. Currently, we are concentrating on the development of Use of Resources audit toolkits, focusing initially on Financial Management, Efficiency, and Information Management. These toolkits are being piloted in a sample of NHS and central government clients during 2007/08 and 2008/09. Developed toolkits will also be made available to public bodies to consider for self assessment.



33. Historic Scotland completed a baseline review of its best value arrangements in 2005/06. Since that time, there have been improvements in the governance of the Agency with a number of the changes suggested at the time of the initial review having subsequently been implemented. These include the recruitment of non-executive directors onto the Management Board and the Audit Committee; the restructuring of the Inspectorate of Ancient Monuments and Historic Buildings; the development of strategic policies via the Scottish Historic Environment Policy series; and the development of a systematic approach to risk management.

Efficiency

34. Specific targets had not been set under efficient government for Historic Scotland. However for the last six years, the organisation has been committed to the achievement of an annual key performance target of reducing non-cash expenditure by a percentage level set by the Scottish Government. The procurement unit within Historic Scotland had the overall responsibility to ensure delivery of this key performance target, and this year the target was to achieve one per cent efficiency gains on all non-grant expenditure. Against this target Historic Scotland achieved savings of £0.654 million against a target of £0.5 million. Over the three years, the Agency has achieved overall savings of £1.74 million against targets totalling £1.5 million, see Exhibit 1 below.

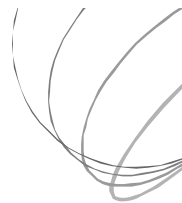
Exhibit 1 - Efficiency Savings 2005/06 to 2007/08

	Target %	Actual %
2005/06	1%	1.02%
2006/07	1%	1.07%
2007/08	1%	1.16%
Total		

35. For the next triennium, the key performance target has been revised to align with the efficiency targets set within the budget settlement for all public bodies; that is to achieve cash-releasing efficiency savings of two per cent on non-grant expenditure. This equates to £1 million per annum. This is a significant increase in the target and exceeds the savings achieved in previous years. It will be a challenging target for Historic Scotland to meet while absorbing pay and cost inflations.

Performance management

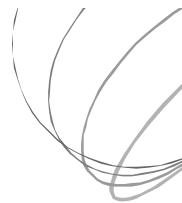
36. Historic Scotland published its corporate plan for the period 2005-2008. Included in the plan is a summary of ten key performance targets against which the effectiveness of the corporate plan could be evaluated over the period. The Scottish Government's Internal Auditors reported that, in 2007/08, the last year covered by the Corporate Plan, Historic Scotland met or exceeded all ten key performance targets (2006/07: nine targets of the ten were achieved). The targets included earned



income, scheduling of monuments, listing of buildings and performance rating from the Mystery Visit Programme.

National studies

37. Historic Scotland contributed to the Audit Scotland study on the use of consultancy services. This study is reviewing the use of consultancy services across central government. Historic Scotland is both a pilot site and a further case study site. The findings from the work will be reported in October 2008.



Looking Forward

38. Historic Scotland faces a number of challenges in 2008/09, which include:

- **International Financial Reporting Standards (IFRS)** – as part of the UK Budget 2007, the Chancellor announced that the timetable for IFRS implementation was to be extended by a year with central government accounts in Scotland to become IFRS compliant with effect from the 2009/10 financial year. The Scottish Government have notified central government bodies that they will be required to produce shadow IFRS-based accounts for the financial year in 2008/09, including a restated balance sheet as at 1 April 2008. A detailed timetable and list of requirements has been issued by the Scottish Government. This process may require significant resource to complete and it will be important that the restatement is tackled early in 2008/09, with a plan in place to manage the transition.
- **Scotland Performs** – the Scottish Government is continuing to develop its approach to performance management based on a national performance framework and outcome agreements. The national performance framework is modelled on an outcome-based 'Virginia-style' performance measurement and reporting tool known as Virginia Performs. In support of this, the Scottish Government has developed a new electronic tool and website to communicate to the public on Scotland's progress. This will include progress on overall delivery of the administration's purpose for Government, the five strategic objectives for Scotland, and other aspects of the outcomes-based national performance framework. We will consider how Historic Scotland is addressing this developing area as part of the 2008/09 audit.
- **Efficiency and future funding** – budgets for 2008/09 and the immediate future will need to be managed within a tighter funding regime. This includes significantly less scope for the application of end-of-year flexibility for the Government with HM Treasury until the next spending review; no option to transfer funds from capital to revenue; and the impact of the introduction of International Financial Reporting Standards (IFRS), particularly on Private Finance Initiative (PFI), leases and infrastructure accounting. Historic Scotland needs to achieve a new efficiency target of two percent of non-grant expenditure in 2008/09 which is a significant increase against achievements in the last three years. The challenge for Historic Scotland is to prioritise spending, identify efficiencies and review future commitments to ensure delivery of key targets and objectives.
- **Data handling** – the Scottish Government carried out a review of data handling arrangements in Scotland, in response to failures in UK government bodies' procedures and practices during 2007. The review considered current policies and procedures on data protection, consistency with government standards, and local arrangements for implementation of procedures. An interim report published in April 2008 made some initial recommendations and a final report is expected soon. We will monitor Historic Scotland's response to the review and action taken as part of our 2008/09 audit.



- **Key performance targets** – The income target for 2008/09 is calculated as a six per cent increase on the previous year's target. Although visitor numbers to the Agency's properties in care have increased over the previous year, the trend will need to continue in order to meet this challenging target. We will monitor achievement of this target in 2008/09.