

Scottish Public Pensions Agency

Scottish Teachers' Superannuation Scheme

NHS Superannuation Scheme, Scotland

Report on the 2007/08 Audit



19 December 2008



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# Executive Summary

## Introduction

In 2007/08 we looked at the key strategic and financial risks faced by the Scottish Public Pensions Agency (SPPA). We audited the financial statements of the Scottish Public Pensions Agency, the Scottish Teachers' Superannuation Scheme and the NHS Superannuation Scheme (Scotland), and we also considered aspects of performance management and governance. This report sets out our key findings.

## Financial Position – Scottish Public Pensions Agency

During financial year 2007/08, the Scottish Public Pensions Agency recorded income of £0.1 million from operating activities and received financing of £12.1 million from the Scottish Government. The Agency incurred a net operating cost of £8.3 million against a budget of £8.5 million; a net underspend of £0.2 million on operating costs. There was a net underspend of £0.9 million against the capital budget of £4.4 million (£3.5 million outturn capital expenditure).

The Agency faces an increasingly tight financial settlement for 2008-11, including the need to achieve 2% year on year efficiency savings, and will be expected to deliver pension reform changes in addition to business as usual.

## Financial Position – NHS Superannuation Scheme (Scotland)

The NHS Superannuation Scheme (Scotland) had net outgoings for the year of £1,033.3 million, an increase of 1.1% (£11.1 million) from 2006/07 (£1,022.2 million).

Scheme liabilities have decreased by £0.8 billion (3.6%) from £21.9 billion to £21.1 billion. During the financial year 2007/08, new regulations came into force which made changes to retirement benefits and the Government Actuary's Department has estimated that the effect of these changes is to reduce the pension liability. Consequently, £440.0 million has been credited to the operating cost statement as a negative past service cost.

## Financial Position – Scottish Teachers' Superannuation Scheme

The Scottish Teachers' Superannuation Scheme had net outgoings for the year of £1,142.3 million, an increase of 107% (£590.8 million) from 2006/07 (£551.5 million). The largest contributory factor to this increase was a negative past service cost of £340 million that arose in 2006/07. This negative cost occurred as a consequence of changes to scheme terms and conditions and had the effect of significantly reducing 2006/07 outgoings. Scheme liabilities have increased by £0.6 billion (3.2%) from £18.7 billion to £19.3 billion.



## **Financial Statements**

We have given unqualified opinions on the financial statements of the Scottish Public Pensions Agency, the Scottish Teachers' Superannuation Scheme and the NHS Superannuation Scheme (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.

## **Overpayments of Pension**

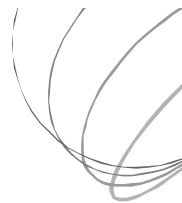
During the year an error in the indexation of some pensions was identified which affected a number of pension schemes in Scotland, England and Wales. The error affected pensioners in receipt of a guaranteed minimum pension and resulted primarily from deficiencies in information passed to the Scottish Public Pensions Agency and its predecessor body from HM Revenue and Customs in the period since 1978. In consultation with the Scottish Government, the Agency has decided in principle to write off overpayments which total £5.67 million made by both schemes to 6,009 pensioners between 1978 and 31 March 2008. The Scottish Public Pensions Agency will be taking action in December to contact all those affected.

We are satisfied that the action taken to correct the overpayments by the Agency is reasonable and that the appropriate disclosures have been included in the financial statements. Although sizeable, the overpayments are not material to our overall opinion on the regularity of expenditure included in the financial statements.

## **Governance**

Corporate governance is concerned with the structures and process for decision making, accountability, control and behaviour at the upper levels of an organisation. Overall the corporate governance and control arrangements for the Agency operated satisfactorily during the year, as reflected in the Statement on Internal Control. During the year there was an incident resulting in temporary loss of personal data which led to tightening of procedures.

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 and to mitigate the risks of material misstatement of the accounts, error or fraud.



## **Performance**

The Scottish Public Pensions Agency operated within its combined operating costs and capital budget for 2007/08 for the Agency and for the two schemes. The Agency met all five of its original key targets outlined in the corporate plan for 2005-08, and 4 out of the 6 targets added since the corporate plan was drawn up. Details of performance are reported in the Annual Report.

## **Best Value**

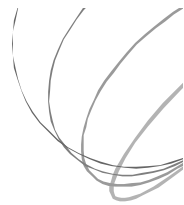
Achieving best value is about ensuring sound governance, good management and public reporting on performance and we comment on aspects of the Scottish Public Pensions Agency's arrangements in this report. Audit Scotland is committed to ensuring that best value auditing across the public sector adds value to existing arrangements, is proportionate and risk-based. We intend to adopt an audit framework that is consistent across central government, health and local government, although the application will vary to reflect different accountability arrangements. Development will continue during 2008/09 and will include consultation with stakeholders.

## **Looking forward**

The final part of our report notes some key risk areas for the Scottish Public Pensions Agency going forward. We consider the implementation of the AXISE pensions administration IT system for the NHS Superannuation Scheme (Scotland) and the development of satisfactory arrangements for the National Fraud Initiative represent significant challenges for the Scottish Public Pensions Agency in the coming year.

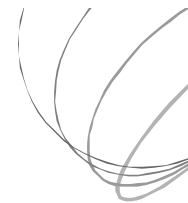
The assistance and co-operation given to us by Board members and staff during our audit is gratefully acknowledged.

**Audit Scotland**  
**19 December 2008**



# Introduction

1. This report summarises the findings from our 2007/08 audit of Scottish Public Pensions Agency (SPPA), the Scottish Teachers' Superannuation Scheme and the NHS Superannuation Scheme (Scotland). The scope of the audits was set out in our Audit Plan, which was presented to the Audit Committee on 16 January 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. This report completes our audit by giving an overview of the work we carried out and a summary of the key findings.
2. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officers and members of the SPPA 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](http://www.audit-scotland.gov.uk).



# Financial Position - SPPA

3. In this section we summarise key outcomes from our audit of the SPPA 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

4. We audit the financial statements and give an opinion on:
  - whether they give a true and fair view of the financial position of the SPPA and its expenditure and income for the period in question;
  - whether they and the part of the Remuneration Report to be audited 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 and the unaudited part of the Remuneration Report included in the Annual Report, with the financial statements, and
  - the regularity of the expenditure and receipts.
5. 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 the SPPA.

## Overall conclusion

6. We have given an unqualified opinion on the financial statements of the SPPA for 2007/08.
7. The unaudited financial statements were provided to us on 16 June, supported by a comprehensive working paper package.



## Financial Position

### Outturn 2007/08

8. The SPPA is required to work within the resource budget set by the Scottish Government Economy Directorate. The Agency underspent its operating costs budget by £0.2 million and its capital budget by £0.9 million (overall position is £1.1 million underspend) – see exhibit 1 below.

**Exhibit 1 – Performance against Resource Budget 2007/08**

Resource Allocation (£ million)	Budget	Actual Outturn	Difference
Operating	8.5	8.3	0.2
Capital	4.4	3.5	0.9
<b>Total</b>	<b>12.9</b>	<b>11.8</b>	<b>1.1</b>

9. Operating outturn decreased by £0.5 million from £8.8 million (2006/07) to £8.3 million (2007/08). This was due to reductions in administrative costs.

### 2008/09 Budget

10. Scottish Ministers have agreed a resource budget for the SPPA of £14.1 million for 2008/09.

**Exhibit 2 – 2008/09 Resource Budget**

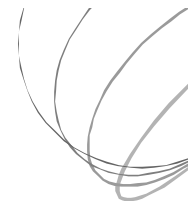
	£ million
Operating	<b>10.5</b>
Capital	<b>3.6</b>
<b>Resource Budget</b>	<b>14.1</b>

11. SPPA have indicated that they are on course to keep both operating and capital expenditure within the published budget figures.

## Issues arising from the audit

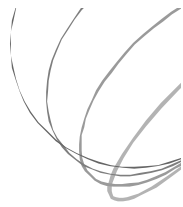
12. As required by auditing standards we reported to the Audit Committee on 15 July 2008 the main issues arising from our audit of the financial statements. There were no significant issues to be brought to the Audit Committee's attention.
13. A separate **management letter** will be sent out in December. All items have been discussed with management. The matters covered include recommendations regarding fuller discussion of financial performance in the Management Commentary and accounting for the disposal of fixed assets.





## Regularity Assertion

14. 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 the Scottish Ministers. We have been able to address 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 items were identified for disclosure.



# Financial Position – NHSSS and STSS

15. In this section we summarise key outcomes from our audits of the NHS Superannuation Scheme (Scotland) and the Scottish Teachers' Superannuation Scheme financial statements for 2007/08, and comment on the key financial management and accounting issues faced.

## Our responsibilities

16. We audit the financial statements and give an opinion on:
- whether they give a true and fair view of the financial position of the NHS Superannuation Scheme (Scotland) and the Scottish Teachers' Superannuation Scheme and their 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 Report of the Managers and the Report of the Actuary, with the financial statements; and
  - the regularity of the expenditure and receipts.
17. We also review the statements 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 statements are consistent with our knowledge of the NHS Superannuation Scheme (Scotland) and the Scottish Teachers' Superannuation Scheme.

## Overall conclusion

18. We have given unqualified opinions on the financial statements of the NHS Superannuation Scheme (Scotland) and the Scottish Teachers' Superannuation Scheme for 2007/08.
19. As agreed, the unaudited financial statements were provided to us on 28 July 2008, supported by working papers. The high standard of the supporting papers and the timely responses from SPPA staff allowed us to conclude our audit within the agreed timetable and provide draft opinions to the Audit Committee on 14 October. The receipt of final, signed financial statements was delayed until December pending resolution of the issue concerning guaranteed minimum pension overpayments referred to in paragraphs 26 to 31.



## Financial Position – NHS Superannuation Scheme (Scotland)

### Outturn 2007/08

20. The NHS Superannuation Scheme (Scotland) had net outgoings for the year of £1,033.3 million, an increase of 1.1% (£11.1 million) from 2006/07 (£1,022.2 million).
21. Scheme liabilities have decreased by £0.8 billion (3.6%) from £21.9 billion to £21.1 billion. The discount rate applied from 31 March 2008 was 2.5% real, an increase from 1.8% real from the previous year. The increase in the liability for the prior period was £5.7 billion (35.1%). During the financial year 2007/08, new regulations came into force which made changes to retirement benefits. The Government Actuary's Department has estimated that the effect of these changes is to reduce the pension liability. Consequently £440.0 million has been credited to the operating cost statement as a negative past service cost.
22. In accounting for pensions, Financial Reporting Standard 17 (Retirement Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if actual payment will be made in future years. This requirement results in very large future liabilities being recognised in financial statements. In summary, the FRS17 liability has moved as follows since the standard was first introduced in 2003/04:

	2003/04 £billion	2004/05 £billion	2005/06 £billion	2006/07 £billion	2007/08 £billion
FRS 17 Liability	11.6	12.7	16.2	21.9	21.1

## Financial Position – Scottish Teachers' Superannuation Scheme

### Outturn 2007/08

23. The Scottish Teachers' Superannuation Scheme had net outgoings for the year of £1,142.3 million, an increase of 107% (£590.8 million) from 2006/07 (£551.5 million). The largest contributory factor to this increase was a negative past service cost of £340 million that arose in 2006/07. This negative cost occurred as a consequence of changes to scheme terms and conditions and had the effect of significantly reducing 2006/07 outgoings.
24. Scheme liabilities have increased by £0.6 billion (3.2%) from £18.7 billion to £19.3 billion. The discount rate applied from 31 March 2008 was 2.5% real, an increase from 1.8% real from the previous year. The increase in the liability for the prior period was £4.1 billion (28.4%).



25. In summary, the FRS17 liability has increased as follows since 2003/04:

	2003/04 £billion	2004/05 £billion	2005/06 £billion	2006/07 £billion	2007/08 £billion
FRS 17 Liability	10.7	12.4	14.6	18.7	19.3

## Overpayments of pension

26. During 2008 an error in the indexation of some pensions was identified which affected a number of pension schemes in Scotland and in England and Wales. The error resulted from a breakdown in the flows of information from the National Insurance Contribution Office (NICO) at HM Revenue and Customs (and its predecessors) and pension scheme administrators. About 5% of current pensions in the Scottish Teachers' Superannuation Scheme and the NHS Superannuation Scheme (Scotland) were indexed up incorrectly at the start of each financial year, in the period 1978 to 1997, leading to overpayments of pensions over a significant period of time and some current individual pension levels being higher than they should be.
27. This arose as a result of the contracting out arrangements introduced in the late 1970s when some employees became entitled to a guaranteed minimum pension. Details of these people were maintained by the NICO and this information should have been passed by the NICO to pension administrators to enable them to correctly determine the rate of indexation to be applied to pensions at the beginning of each financial year. The receipt of this information from NICO would lead to pension administrators abating the indexation applied to the pensions of those people who were entitled to the guaranteed minimum pension.
28. Pension administrators received this information correctly from the NICO for the majority of people; however it has been identified that for a small percentage the information has not been correctly forwarded. For this small percentage the pensions have been indexed by greater levels than they should have been, with the impact being cumulative year on year.
29. In December 2008 the SPPA, in consultation with the Scottish Government, decided in principle to write off these overpayments which totalled £5.67 million (NHSSS £1.54 million, STSS £4.13 million) that had been made by the schemes to 6,009 pensioners (NHSSS 3,148, STSS 2,861) since 1978. SPPA have identified that there were no individual losses or special payments in excess of £250,000 which would require separate disclosure during the year to 31 March 2008, or that have been



recognised since that date. Scottish Ministers have been informed prior to the signing of the accounts of the wording proposed in the accounts and the action planned.

30. Information on these overpayments has been reflected in the accounts in the Report of the Managers, the Statement on Internal Control, and Note 24 Losses and Note 25 Post Balance Sheet Event. Further write-offs will be required in relation to the 2008/09 accounts and these are anticipated to be approximately £1.66 million (NHSSS £0.56 million, STSS £1.10 million). We have agreed that the wording used reasonably describes the situation and that the actions proposed by SPPA are appropriate.
31. SPPA will be taking action in December to write to all pensioners in the two schemes.

## Issues arising from the audit

32. As required by auditing standards we reported to the Audit Committee on 14 October 2008 the main issues arising from our audit of the financial statements of the two schemes. The key issues reported were:
33. **Early retirement costs debtor:** The NHS Superannuation Scheme (Scotland)'s accounts include a debtor of £14.5 million for early retirement costs recoverable from the Scottish Government Health Directorate (SGHD). SPPA issue recharge reports to the SGHD to recover these costs. There is, however, an unreconciled difference of £308,000 between the debtor included in the accounts and the supporting documentation. The Audit Committee agreed that this difference should be investigated and resolved prior to the end of financial year 2008/09.

*Action plan 1*

34. **Unreconciled bank balance:** Our audit of the SPPA bank reconciliation identified an unreconciled balance of £109,000 at the year end. There were comparable unreconciled balances of £290,000 in 2006/07 and £235,000 in 2005/06 on this account at the end of the financial year. Although SPPA undertook to investigate and resolve these balances prior to the end of the 2007/08 financial year, this has not yet been completed. The Audit Committee asked for this to be completed as a matter of urgency.

*Action plan 2*

35. **Annual return reconciliations** are not yet in place for Teachers and Main Health Authorities. Last year we were informed that the changes arising out of the implementation of new pensions' administration software will allow a reconciliation to contributions received from larger employers. In 2008/09 this issue will be implemented for STSS as the AXISe system was introduced in September 2008. However NHSSS reconciliations may not be possible as delays have meant that



implementation of AXISe for the NHSSS may be delayed until early 2009. We will monitor the situation and the effect on operations.

36. **Update of pension increase factors:** We identified a number of errors relating to the payment and calculation of the pensions increase, particularly in relation to STSS. Although the number of errors is limited, SPPA staff have been unable to ascertain the reason for these system failures.

*Action plan 3*

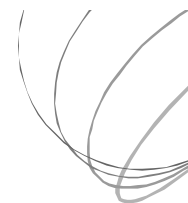
37. **Capitalised receipts:** Poor communication between the Scottish Government Health Directorate and the SPPA resulted in income and the corresponding debtor being omitted from the NHS Scheme accounts. The amount was £1 million which, although a significant sum, was not material in the context of the financial statements as a whole.

*Action plan 4*

38. A separate management letter will be sent out in December. All items have been discussed with management and none are sufficiently material to warrant inclusion in this report.

## Regularity Assertion

39. 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 the Scottish Ministers. We have been able to address 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. Apart from overpayments relating to the guaranteed minimum pension scheme, no significant issues were identified for disclosure.



# Governance

## Overview of arrangements

40. This section sets out our main findings arising from our review of the SPPA governance arrangements including those covering the Scottish Public Pensions Agency Account, the Scottish Teachers' Superannuation Scheme and the NHS Superannuation Scheme (Scotland). This year we reviewed:
- key systems of internal control;
  - internal audit; and
  - aspects of information and communications technology (ICT).
41. 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. Our overall conclusion is that arrangements within the SPPA are sound and have operated through 2007/08.

## Systems of internal control

42. Key controls within systems should operate effectively and efficiently to accurately record financial transactions and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In their annual report for 2007/08 internal audit provided the opinion that, based on the internal audit work undertaken during the year, there was substantial assurance on the adequacy and effectiveness of the systems of internal control.
43. As part of our audit we reviewed the high level controls in a number of SPPA systems that impact on the financial statements of both the SPPA account and the two Pension Scheme accounts. In addition to the work done on the SPPA's own systems we also drew assurance from work done by Audit Scotland's Scottish Government team on the Scottish Executive Accounting System (SEAS) used by the SPPA.
44. Our overall conclusion was that key controls were operating effectively.

## Statement on Internal Control

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



## Prevention and detection of fraud and irregularities

46. The SPPA 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.
47. SPPA was one of 74 public bodies to take part in the latest National Fraud Initiative (NFI 2006/07). This exercise is undertaken as part of the audit of the participating bodies. The NFI brings together data from councils, health bodies, police, fire and rescue boards and other agencies including SPPA, to help identify and prevent a wide range of frauds against the public sector. These include housing benefit fraud, occupational pension fraud and payroll fraud.
48. The NFI has generated significant savings for Scottish public bodies (£9.7 million from the 2006/07 exercise and £37 million including previous exercises). Where fraud or overpayments are not identified in a body, assurances can usually be taken about internal arrangements for preventing and detecting fraud.
49. In May 2008 Audit Scotland released its report *National Fraud Initiative in Scotland 2006/07*. A full copy of the report is available on Audit Scotland's website [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk). The report highlighted a range of areas where prevention and detection of fraud had been enhanced.
50. Although the SPPA has made some good progress in dealing with the 2006/07 NFI matches since our last review, it still has a number of cases under investigation. This includes the significant overpayment cases highlighted in the national NFI report.

### *Action plan 5*

51. Looking forward, Audit Scotland is working to widen the scope of the NFI in line with the rest of the UK. Public bodies provided information again in October this year as part of their 2008/09 audits, with the output expected in early 2009. We shall continue to monitor the Agency's progress.





## Internal Audit

52. 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 the SPPA internal audit function (provided by Scottish Government Internal Audit Division). We concluded that the internal audit service operates in accordance with the Government Internal Audit Manual and therefore placed reliance on their work in the areas of:

- Administrative cost expenditure;
- Awards;
- Payments and benefits statements;
- Risk management, governance and best value;
- Pension sharing on divorce;
- Taxation;
- Handling of sensitive data.

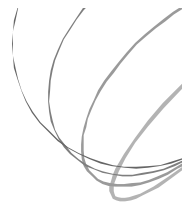
## Data handling

53. On 23 November 2007 the Cabinet Secretary for Finance announced to the Scottish Parliament that a package containing personal details was unaccounted for after being sent from SPPA to NHS Greater Glasgow. SPPA investigations subsequently ascertained that the package had been delivered safely to Stobhill Hospital. Loss of sensitive data has been recorded as a risk in the agency risk register. One of the steps taken by the agency to address this risk was to arrange an internal audit review of the controls established to manage the risks associated with handling/processing of sensitive items of mail. Internal audit were able to provide substantial assurance over risk and control arrangements. We have reviewed the work of internal audit and conclude that the actions taken by SPPA were satisfactory.

## Information and Communication Technology

### Issues arising out of Scanning Solutions review

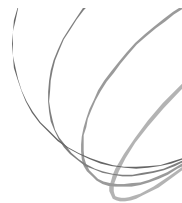
54. As part of our interim testing and Internal Audit's review of superannuation awards and payments, we identified issues with the completeness and quality of scanned documentation within both the Comino and EDM On-line systems. As a result, we carried out a review of the scanning process used by SPPA for recording documentation relating to pension payments.



55. We identified an aspect of good practice involving the back-scanning workstream performed by the EDM Group. The organisation is certified with ISO9001:2000 accreditation and, as part of this accreditation, scanned documents are required to comply with the code of practice for legal admissibility and evidential weight of information stored electronically.
56. We also identified significant areas where improvements can be incorporated into current operational practice, in particular by:
- implementing a records management policy;
  - updating operational procedures and providing staff with refresher training;
  - undertaking proof in total testing before formally signing off future data cleansing and migration tests;
  - implementing “poly pockets” for storing and transferring documents to the mailroom;
  - implementing further housekeeping procedures to ensure that “unknown” case folders are investigated timeously and reasons for deletion of case folders are noted and formally authorised.

### **Computer services review update**

57. In July 2008 we reported the results of our Computer Services Review of the SPPA together with an action plan agreed with management. SPPA has implemented the following actions to address the risks that were reported in our initial reviews:
- documenting and approving an ICT Strategy and IT security policy;
  - agreeing disaster recovery and ESCROW arrangements for new systems;
  - setting up a test site for the implementation of the Heywood system;
  - receiving an updated service catalogue for the use of the SCOTS network from ISIS;
  - updating all access and password procedures;
  - approving and testing their business continuity plan.
58. The Agency has also made good progress in implementing the actions to address the remaining risks reported in the initial review. We will follow up these outstanding issues in 2009.



# Performance Management

59. Public audit is more wide-ranging than in the private sector and covers the examination of, and reporting on, performance and value for money issues. 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.
60. 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

61. 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 (i.e. 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. 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.
62. Audit Scotland is committed to extending the Best Value audit regime across the whole public sector and significant development work is taking place. Our guiding principles are to ensure that best value auditing adds value to existing arrangements, is proportionate and risk-based. We intend to adopt a framework that is consistent across central government, health and local government, although the application will vary to reflect different accountability arrangements. Development will continue during 2008/09 and will include consultation with stakeholders.
63. In essence, achieving best value is about ensuring sound governance, good management and public reporting on performance and we comment on aspects of the Agency's arrangements throughout this report.

## Efficient Government

64. This was the last year of the three year efficiency programme. In 2007/08, SPPA achieved savings of £1.246 million against a target of £0.635 million. Over the three years SPPA has achieved overall savings of £2.144 million against targets totaling £1.67 million. A 2% target has been set for future years. This will be tight in view of current economic constraints.



**Exhibit 3 – Efficiency Savings 2005/06 to 2007/08**

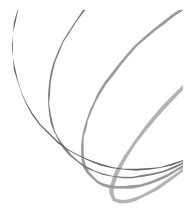
	Target £ million	Actual £ million
2005/06	0.400	0.410
2006/07	0.635	0.488
2007/08	0.635	1.246
<b>Total</b>	<b>1.670</b>	<b>2.144</b>

## Performance Management

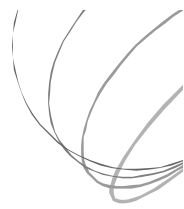
65. The SPPA is required to publish a corporate plan every three years. The last plan was published in 2005 and covered the period 2005-08, including the period of these accounts. This plan sets out 9 key performance targets, which have subsequently been revised to improve the measurement of the Agency's performance in key areas.
66. The SPPA operated within its combined operating costs and capital budget for 2007/08 for the Agency and for the two schemes. The Agency met all five of its original key targets outlined in the corporate plan for 2005-08, and 4 out of the 6 targets added since the corporate plan was drawn up. Details of performance are reported in the Annual Report. A new corporate plan covering 2008-11 has been published.

## National Studies

67. The Audit Scotland report: *'How Government Works: major capital projects'* was published on 24 June 2008. The study presented a picture of how Scottish Government, agencies and NDPBs have been and are delivering major capital projects. It provided Parliament with the first wide view report on the delivery of major capital projects to time, cost and quality. Key messages arising out of the report were as follows:
- In general, the achievement of cost and time targets improved significantly as projects progressed;
  - Early cost and time estimates at project approval stage were too optimistic for many major projects;
  - Performance against cost and time estimates is better after contracts are awarded, as plans are more certain and risks clearer;
  - Most completed projects have successfully delivered the required roads, hospitals and other assets, and all current projects are forecast to do so. However, few projects have been evaluated to demonstrate that they have delivered the expected wider benefits which originally justified the investment;



- Nine current projects examined had awarded the main construction contract, which should increase cost certainty. However, four projects had significant increases in estimated cost before reaching this stage; and
  - Project management and governance arrangements within individual projects are broadly effective, although room for improvement remains. A more strategic approach to managing the programme of capital projects could improve value for money.
68. The report made a number of recommendations for both the Scottish Government and public bodies. It recommended that the Scottish Government should report in public on the performance of projects, particularly any reasons for changes to costs and timing and what lessons can be learned from completed projects. It also made several recommendations to public bodies about strengthening business cases, improving project management and governance arrangements, and post project reviews. Although the Agency was not directly involved in this report, the pensions IT system is mentioned in the appendix.
69. In the overall interest of promoting the most effective management of projects by public bodies, Audit Scotland has recently produced a good practice checklist to complement this report. It aims to help decision makers identify key issues and potential challenges that public bodies should be aware of during the course of any major project and whether improvements are needed for management and governance. The main audiences for the checklist include governing bodies and audit committees, senior management and the senior responsible owners of projects.
70. The SPPA has contributed to the Audit Scotland report: *'Promoting and improving energy efficiency in the public sector'* by completing a survey and supplying key documents. This study was published on 11 December 2008 and reviewed how well the public sector is promoting and improving energy efficiency across their estates.



# Looking Forward

71. The Scottish Public Pensions Agency 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 has 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. 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 based on the outcome based 'Virginia-style' model of performance measurement and reporting. 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 the SPPA 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 PFI, leases and infrastructure accounting. The challenge for the SPPA is to prioritise spending, identify efficiencies and review future commitments to ensure delivery of key targets and objectives.
- **New Pension Administration System for NHS Superannuation Scheme (Scotland)** – SPPA introduced a new IT system, AXISe for the administration of Scottish Teachers' Superannuation Scheme during 2008 and has proposed to introduce the same IT system for the NHS Superannuation Scheme (Scotland) in mid 2009. A number of difficulties were encountered in implementing the system for STSS and consequently SPPA has been cautious about introducing the next phase of its development at a time of the year when the Agency is under other pressures. We will monitor the project management arrangements in place to deliver the next phase in this key project.



- **National Fraud Initiative** – Public bodies will provide information again in October this year to the National Fraud Initiative as part of their 2008/09 audits, with the output expected in early 2009. SPPA has increased the resources available but still faces a challenge in investigating significant overpayment cases. Audit Scotland is working to widen the scope of the NFI in line with the rest of the UK and we will continue to monitor the Agency's progress.

# Appendix A: Action Plan

## Key Issues and Planned Management Action

Action Point	Risk Identified	Planned Action	Responsible Officer	Target Date
1.	<p><b>Early retirement costs debtor</b></p> <p>Following a recommendation made in the 2006/07 audit report, SPPA established procedures in 2007/08 for producing recharge reports for early retirement costs recoverable from the Scottish Government Health Directorate (SGHD). A debtor of £14.5 million is included in the NHS superannuation scheme's accounts in respect of these costs. There is, however, an unreconciled difference of £308,000 between the debtor in the accounts and the supporting documentation and therefore a risk that the debtor could be mis-stated.</p> <p><i>We recommend that:</i></p> <p><i>(a) Early retirement cost recharge reports should be produced and issued to SGHD on a regular basis throughout the financial year.</i></p> <p><i>b) SPPA should approach SGHD to ensure that information is provided to SPPA on time to enable regular reconciliation of the early retirement costs debtor to the supporting recharge reports.</i></p>	<p>SPPA along with Health Boards continue the task of repairing payroll data migrated from Paymaster.</p> <p>SGHD is relying on SPPA to provide accurate and timely recharge reports to calculate debtors. The action above will allow SPPA to do this. There is no information coming from SGHD.</p>	Ian Clapperton /Chris Fenton	31 March 2009



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2.	<p><b>Unreconciled bank balance</b></p> <p>The SPPA bank reconciliation had an unreconciled balance of £109,000 at the year end. There were comparable unreconciled balances of £290,000 in 2006/07 and £235,000 in 2005/06. Although SPPA undertook to investigate and resolve these balances prior to the end of the 2007/08 financial year, this has not yet been completed. The Audit Committee asked for this to be completed as a matter of urgency.</p> <p><i>We recommend that the reconciliations are completed before the end of the 2008/09 financial year.</i></p>	<p>There is a misunderstanding of this process. SPPA demonstrated that all bank receipts were accounted for, and that the bank and ledger accounts were fully reconciled. Not all receipts were fully identified; 109k was the balance in the suspense account which was not allocated to a receipt heading in SEAS. This represents a very small proportion of the £1.4 billion received. £109k is the smallest balance in recent years. SPPA will attempt to allocate all receipts where possible but there must be an acceptable tolerance.</p>	Christopher Fenton	31 May 2009
3.	<p><b>Update of pension increase factors</b></p> <p>We identified a number of errors relating to the Pensions Increase on the STSS. Errors related both to the calculation of pension increases and to the payment of pension increases. We were unable to find out the reason for these system errors.</p> <p><i>We recommend that controls over the calculation and payment of pension increases are reviewed as soon as possible.</i></p>	<p>SPPA is transferring the PI action for STSS to Resourcelink in time for April 2009. Additional checks which will also be introduced to test outcomes.</p>	Ian Clapperton	31 May 2009

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4.	<p><b>Capitalised receipts</b></p> <p>An amount of £1 million was omitted from the accounts due to poor communication between the SGHD and SPPA. The income and corresponding debtor were not adjusted as the amount was considered not material to the accounts. There were significant delays by SGHD in confirming the amount due to SPPA.</p> <p><i>We recommend that SPPA approach SGHD to ensure that information on capitalised receipts due to the SPPA is notified on a more timely basis.</i></p>	<p>SPPA relies on SGHD to provide details of cases capitalised. This year the information was received from the SGHD in October; SGHD have given assurances that this will be dealt with promptly at the end of the financial year 2008 – 09.</p>	<p>Christopher Fenton</p>	<p>Complete</p>
5.	<p><b>National Fraud Initiative</b></p> <p>The SPPA has made some progress in dealing with the 2006/07 National Fraud Initiative (NFI) matches since our last review. Although recently there have been additional resources devoted to NFI investigations, there are still a number of cases under investigation. These include significant overpayment cases highlighted in the national NFI report.</p> <p>There is a risk that cases under investigation may not be processed sufficiently quickly to ensure recovery of all overpayments.</p> <p><i>We recommend that a timetable is established for the resolution of outstanding cases.</i></p>	<p>Accepted. A timetable will be introduced. In addition the Agency has prepared a new Overpayment recovery policy for introduction in 09/10.</p>	<p>Ian Clapperton/ Chris Fenton</p>	<p>30 June 2009</p>