

## Key Issues Memorandum

Office of the Scottish Charity Regulator

For the year ended 31 March 2010

*10 June 2010*

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# Grant Thornton

To the Management and Audit Committee of the Office of the Scottish  
Charity Regulator (OSCR) and to the Auditor General for Scotland

The purpose of this memorandum is to highlight the key issues affecting  
the results of OSCR and the preparation of the financial statements for the  
year ended 31 March 2010. It is also used to report to management to meet  
the mandatory requirements of International Standard on Auditing (UK &  
Ireland) 260.

We take responsibility for this memorandum, which has been prepared on  
the basis of the limitations set out in 'The small print' (Section 5).

We would like to take this opportunity to record our appreciation for the  
kind assistance provided by Anne Monk and other staff during our audit.

Grant Thornton UK LLP  
10 June 2010

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# 1 Executive summary

<b>Financial statements</b>	
Audit opinion	<ul style="list-style-type: none"> <li>• We intend to issue an unqualified audit report.</li> </ul>
Financial statements	<ul style="list-style-type: none"> <li>• No audit adjustments were identified and the accounts and working papers were of a high standard.</li> </ul>
IFRS conversion	<ul style="list-style-type: none"> <li>• The 2009-10 accounts are in compliance with the FReM.</li> </ul>
<b>Governance</b>	
Risk management	<ul style="list-style-type: none"> <li>• OSCR have good risk management arrangements.</li> </ul>
Financial planning	<ul style="list-style-type: none"> <li>• The financial planning and budgetary processes are well-developed and effective.</li> </ul>
Procurement	<ul style="list-style-type: none"> <li>• OSCR follows Scottish Government procurement guidelines in the award of contracts.</li> </ul>
National performance reports	<ul style="list-style-type: none"> <li>• OSCR has effective arrangements for considering Audit Scotland national performance reports.</li> </ul>
<b>Performance and best value</b>	
Best Value and Performance	<ul style="list-style-type: none"> <li>• OSCR is fully committed to the principles of Best Value and is open and transparent about its performance. OSCR did not meet its business plan objective target "to determine whether bodies are charities" and this will be explained in the annual report.</li> </ul>
Efficiencies	<ul style="list-style-type: none"> <li>• OSCR exceeded its efficiency savings targets for the year.</li> </ul>

## 2 Financial statements

### 2.1 Findings and conclusions

OSCR is required to produce financial statements under an Accounts Direction issued by the Scottish Ministers. The Accounts Direction requires OSCR to prepare its financial statements in line with the accounting principles and disclosure requirements of the 2009-10 FReM.

We audit the financial statements and give an opinion on whether they give a true and fair view. Our opinion also covers whether 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.

We also review the Statement on Internal Control and consider OSCR's compliance with Scottish Government guidance, the adequacy of the process put in place by the Accountable Officer to obtain assurances on

systems of internal control and assess whether disclosures in the Statement are consistent with the information emerging from our normal audit work.

The draft financial statements and supporting working papers were presented for audit prior to the fieldwork and were of a high standard. As a result, no audit adjustments have been recommended following the audit procedures. We have no recommendations to make on financial systems internal controls.

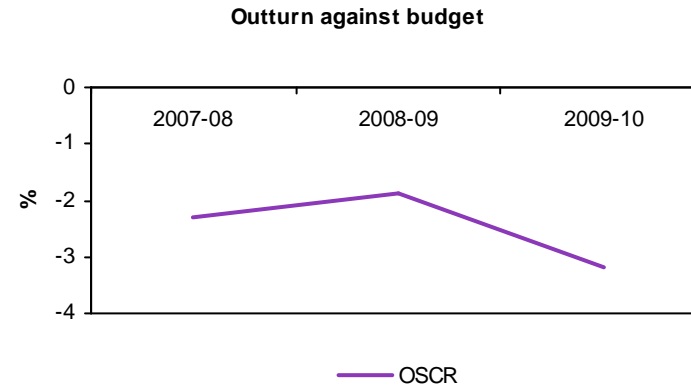
We intend to give an unqualified opinion on both the financial statements of OSCR for 2009-10 and on the regularity of transactions undertaken during the financial year.

Specific issue identified in the AAM	Response
<p><b>IFRS implementation</b> This is the first full year in which central government bodies are required to prepare their accounts on the basis of IFRS. We reviewed and reported on the 2008-09 shadow accounts in January 2010.</p>	<p>We carried out a review of the draft 2009-10 accounts, which have been prepared under IFRS, against the requirements of the 2009-10 FReM and conclude that the accounts are in compliance.</p>

**2.2 Outturn against budget**

In 2009-10, OSCR's expenditure was £99,000 below its budget of £3,100,000 (3%) leaving OSCR within the regularity limit.

This result has been achieved through efficiency savings - particularly efficient procurement - and a longer lead time than budgeted for filling staff vacancies.



### 2.3 Operating cost statement

In addition to the budget savings identified above, there has been a 3.7% reduction in operating costs from 2008-09. The reduction in costs is analysed as follows:

Increase in staff costs                    £114,000

offset by -

Decrease in other admin costs    (£111,000)

Decrease in depreciation            (£112,000)

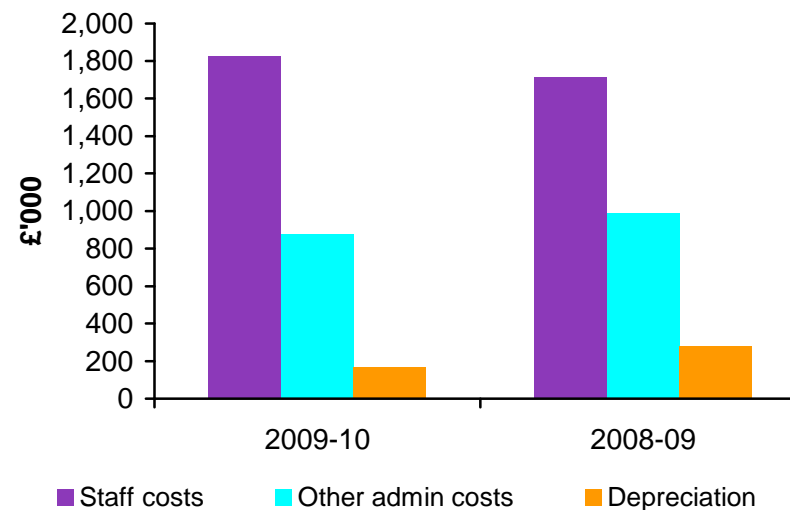
The staff costs increase is attributed to the higher average number of staff throughout the year, the majority of which were taken on at the end of 2008-09. A further analysis of staff numbers is provided below:

Year	Actual Staff Numbers*
2008-09	50
2009-10	55
Staff Establishment at 31 March 2010	58

*\*full time equivalent and including secondments and temporary staff*

The cost savings in other admin costs relate to the different regulatory activities being carried out this year including a reduction in the number of major research projects and publications from the prior year.

### Expenditure analysis



## 3 Governance

### 3.1 Introduction

Corporate governance is the system by which organisations direct and control their functions and relate to their stakeholders, and incorporates the way in which an organisation manages its business, determines strategy and objectives and goes about achieving those objectives. It is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of the organisation.

### 3.2 Audit Approach

As part of our 2009-10 audit, we assessed the adequacy of OSCR's governance arrangements against good practice standards for the public sector.

We examined:

- risk management procedures
- financial planning, including sensitivity analysis
- procurement procedures followed
- outcome of the 'Board Effectiveness Review'
- OSCR's procedures for considering Audit Scotland national performance reports.

Specific issue identified in the AAM	Response
<p><b>Risk management</b></p> <p>OSCR faces reputational risk should there be a regulatory failure or should a high profile charity fail. The impact of the economic downturn has increased the need for charities' services but at the same time has put constraints on the funding available.</p>	<p>We reviewed the risk management procedures in place and found them to be robust with no deficiencies to report. The risk of reputational failure has been addressed by through a recent publication on the OSCR website: Charities in Financial Difficulties. This sets out the liability of OSCR for the failure of a charity and clearly states that OSCR is not the 'guarantor of financial viability'.</p>
<p><b>Financial planning</b></p> <p>The economic recession is likely to result in significant cuts in public sector funding as the UK Government faces material reductions in tax receipts, higher welfare payments and higher loan repayment costs. In the Scottish public sector, recent estimates indicate a potential reduction of between 5% and 15% in public sector funding from 2011-12.</p>	<p>The budget for 2010-11 is confirmed at £3.6m (2009-10 £3.1m) and OSCR has prepared a budget to demonstrate that it can manage its spend within this limit.</p> <p>We also reviewed the results of a review of budget sensitivities for 2011-12 that has been reported to the Board and conclude that OSCR is taking reasonable steps to address the risk of budget cuts and to budget for any additional responsibilities it is asked to take on in future years.</p>



Specific issue identified in the AAM	Response
<p><b>Procurement</b> OSCR seeks to follow Scottish Government guidelines on procurement. We planned to review the procedures in place including a small sample of recent contracts tendered.</p>	<p>We reviewed OSCR's procurement procedures against the Scottish Government guidelines. OSCR follows the Scottish Government procurement procedures which are available on the Scottish Government website <a href="http://www.scotland.gov.uk/Publications/2008/12/23151017/0">http://www.scotland.gov.uk/Publications/2008/12/23151017/0</a>. It also implements its own procurement procedures to ensure staff are in compliance with the Government manual. These procedures contain revised limits which are lower than the Government requirements.</p> <p>We examined two contracts in more detail - Resilience research project and phase 2 of the integrated reporting process. The second is still going through the procurement process. We found that OSCR followed Scottish Government guidelines in both cases and keeps detailed records of decisions taken and processes followed at each stage of the procurement process.</p>
<p><b>Board effectiveness</b> Audit Scotland visited OSCR in September 2009 as part of their study on the Role of Boards. The study aims to assess the role and effectiveness of boards in public bodies and is due to be published in April 2010.</p>	<p>The report is now unlikely to be issued before the conclusion of our audit. We will follow up the report's findings as part of our 2010-11 audit</p>
<p><b>Audit Scotland national performance reports</b> Audit Scotland require auditors to provide feedback to them on the response by public bodies to national performance reports. Where we find that OSCR has not adequately considered a relevant national study report and/or has not prepared an action plan to implement relevant recommendations, we discuss this with you and make recommendations where appropriate.</p>	<p>We found that OSCR has procedures which ensure that relevant national performance reports are discussed at board and audit committee meetings and that action plans are prepared if required. We submitted a progress report to Audit Scotland in February 2010 in line with this conclusion, and are required to submit a further report by 31 August 2010. The national performance report of most relevance that has been published recently is "Improving Public Sector Efficiencies" published in February 2010 and OSCR will have considered this study by the time of our final report to Audit Scotland.</p>

## 4 Performance and best value

### 4.1 Introduction

All public bodies in Scotland have a duty to secure Best Value and continuous improvement. The public sector is facing a period of significant financial austerity, with budget cuts likely to be in the region of 5-15% in real terms by 2013-14. In many areas this means that the current

level of service provision is unsustainable. Public pressure to deliver services as efficiently and cost effectively as possible means that being able to demonstrate that the organisation delivers Best Value is more important than ever.

Specific issue identified in the AAM	Response
<p><b>Best value</b> OSCR is required to operate effectively and efficiently and demonstrate a commitment to the principles of Best Value.</p>	<p>A new plan for 2009-11 was developed at the start of the year and OSCR has graded itself very well developed in 5 of the key areas and well developed in the remaining 4. We conclude that OSCR is demonstrating a continuing commitment to the principles of Best Value.</p>
<p><b>Performance indicators</b> OSCR has revised its Key Performance Indicators (KPIs) from 2009-10 to provide more relevant and new information on OSCR's functions.</p>	<p>OSCR publishes on its website a comparison of KPIs for the current year against the previous year. In the first draft 2009-10 accounts it listed achievements against the target KPIs but did not explain the results. OSCR achieved the majority of its KPIs with the exception of those relating to the business objective "to determine whether bodies are charities" and we agreed that management would provide commentary relating to that in the annual report.</p> <p>Our review of KPIs indicates that they are mainly process or input related and there may be scope to review performance reporting to focus more on reporting against the outcomes or impact of OSCR's activities for stakeholders.</p>

Specific issue identified in the AAM	Response
<p><b>Efficient government</b>            The Scottish Government has set OSCR a target to achieve £70,000 in efficiency savings each year from 2007-08 to 2010-11. Last year, our review of 2008-09 found that OSCR has put in place arrangements for capturing, monitoring and reporting efficiency and progress against the efficiency savings target. Further, cost savings of £72,000 were made.</p>	<p>We examined the quarterly efficiency reports prepared by management and are able to conclude that OSCR has good arrangements with comprehensive processes in place for capturing and regularly reporting on efficiency savings.</p> <p>OSCR had a target of £70,000 for 2009-10 and exceeded this target by £3,000 or 4%. So it has achieved its target for both years to date.</p>

## 5 The small print

ISAUK 260 requires communication of:

- relationships that have a bearing on the independence of the audit firm and the integrity and objectivity of the engagement team
- nature and scope of the audit work
- the form of reports expected

### Purpose of memorandum

This Key Issues Memorandum has been prepared for the benefit of discussions between Grant Thornton, the Audit Committee and the Board.

The purpose of this memorandum is to highlight the key issues affecting the results of OSCR and the preparation of the organisation's financial statements for the year ended 31 March 2010.

This document is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

We would point out that the matters dealt with in this report came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements of the organisation.

This memorandum is strictly confidential and although it has been made available to management to facilitate discussions, it may not be taken as altering our responsibilities to the organisation arising under the Code of Audit Practice.

The report will be submitted to the Auditor General for Scotland and will be published by him on his website at [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

### Responsibilities of the Board, Accountable Officer and auditors

The Board and Accountable Officer are responsible for the preparation of the financial statements and for making available to us all of the information and explanations we consider necessary. Therefore, it is essential that the Board and Accountable Officer confirm that our understanding of all the matters in this memorandum is appropriate, having regard to their knowledge of the particular circumstances.

### Clarification of roles and responsibilities with respect to internal controls

OSCR's management is responsible for the identification, assessment, management and monitoring of risk, for developing, operating and monitoring the system of internal control and for providing assurance to the Board and Accountable Officer that it has done so.

The Board and Accountable Officer are required to review the organisation's internal financial controls. In addition, they are required to review all other internal controls and approve the statements included in the annual report in relation to internal control and the management of risk.

The Board and Accountable Officer should receive reports from management as to the effectiveness of the systems they have established as well as the conclusions of any testing conducted by internal audit or ourselves.

We have applied our audit approach to document, evaluate and assess your internal controls over the financial reporting process in line with the requirements of auditing standards.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you.

In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify.

We would be pleased to discuss any further work in this regard with the Board and Accountable Officer.

### Independence and robustness

Ethical standards require us to give you full and fair disclosure of matters relating to our independence.

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

In accordance with best practice, we analyse our fees below:

	£ incl VAT
Grant Thornton UK LLP	13,000
Audit Scotland fixed charge	1,400
<b>Total</b>	<b>14,400</b>