

The Scottish Housing Regulator

**Report on the 2009/10 Audit to The Scottish Housing
Regulator and the Auditor General for Scotland**

October 2010



 **AUDIT SCOTLAND**



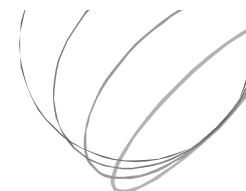
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Key messages

In 2009/10 we looked at the key strategic and financial risks being faced by The Scottish Housing Regulator (SHR). We audited the financial statements and we also reviewed the use of resources and aspects of performance management and governance. This report sets out our key findings.

Financial statements

We gave an unqualified opinion on the financial statements of SHR for 2009/10 and 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.

Financial position and use of resources

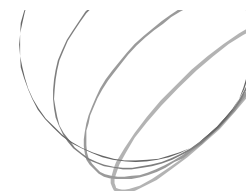
Scotland's economy is in recession and the public sector is under the greatest financial pressure since devolution ten years ago. It will be very challenging to maintain current levels of public services and meet new demands when resources are tight. It remains unclear what impact the current recession will have beyond 2010/11. The Scottish budget is likely to reduce in real terms but the full extent of this is not yet known. Two per cent efficiency savings will not be sufficient beyond 2011 to bridge the gap between public spending and the smaller budget available. In the current economic climate difficult decisions will have to be made across the public sector about priority spending programmes.

SHR's outturn for 2009/10 was £3.978 million compared to an original budget of £4.682 million. During the year £700,000 was returned to the Scottish Government primarily due to reduced staff costs arising from vacancies in the first six months of the year and SHR's strategic decision not to recruit later in the year due to the forthcoming changes under The Housing (Scotland) Bill. The 2010/11 budget is £4.330 million, which, while 7.5% less than the 2009/10 original budget, is greater than 2009/10 outturn. The decreased budget is part of the Scottish Government's reduction in funding to scrutiny bodies.

Payroll and staff-related costs account for over 80% of costs and operating within current vacancy levels may be unsustainable in the longer term. While SHR has under spent in the past two years for the future it has to assess a number of priorities and their workforce-planning implications, particularly around supporting the Scottish Government on The Housing (Scotland) Bill and assessing the workload for SHR under increased interventions powers the new Housing Bill provides to SHR. In light of anticipated future budget allocations SHR are carrying out financial scenario planning exercises looking at the impact of differing financial settlements from 2011/12.

Governance and accountability

Corporate Governance is concerned with the structures and process for decision making, accountability, control and behaviour at the upper levels of an organisation. The former Chief Executive left in October



2009 to join the Scottish Government and the Head of Inspection was appointed as acting Chief Executive thereby allowing continuity of management to staff and stakeholders.

The Housing (Scotland) Bill was introduced to the Scottish Parliament in January 2010; royal assent is expected in November 2010 and the new legislation is expected to come into force in April 2011. The Bill intends to give SHR statutory operational independence under its own Board, with Board members being appointed by Ministers. It will also give SHR a more flexible range of intervention powers. To manage the process through to April 2011 a Transition Advisory Group was established, with representation from Scottish Government and trade unions, and a Transition Plan prepared in February 2010.

As 2009/10 was SHR's second year of operation, SHR continued to focus on refining and embedding controls established in their first year. Overall the corporate governance and control arrangements for SHR 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.

Performance

SHR's priorities for 2009/10 included supporting the Scottish Government on the new Housing Bill, taking extra steps to provide assurance on the financial viability of Registered Social Landlords and working with other scrutiny bodies on the new shared risk assessment process for all local authorities.

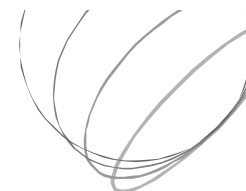
The 2009/10 SHR business plan included 30 activities and 78 targets under six strategic objectives. Due to resources spent on the above priorities, during 2009/10 SHR re-scheduled 14 targets into 2010/11 or allocated them to the separate Transition Plan. Of the remaining 64 targets at the year-end, 57 targets had been achieved or related to on-going activity, with the remaining seven being reviewed and re-scheduled by the EMT. As SHR assess the impact of future budget changes, they should continue to review their business plan, for example by considering whether they have too many targets and if they still reflect the priorities for the organisation.

Looking forward

The final part of our report notes some challenges for SHR going forward, including the Housing Bill, scrutiny co-ordination and financial pressures on SHR. We will continue to monitor developments in these areas.

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

Audit Scotland
September 2010

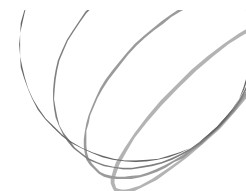


Introduction

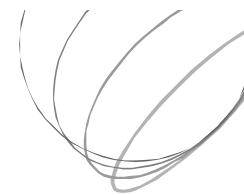
1. This report summarises the findings from our 2009/10 audit of The Scottish Housing Regulator. The scope of the audit was set out in our Audit Plan in accordance with the Code of Audit Practice, which was presented to the Audit Committee on 17 March 2010. This plan set out our views on the key business risks facing the organisation and described the work we planned to carry out on financial statements, performance and governance.
2. We have issued three 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. Best value duties apply across the public sector and are a formal duty on all accountable officers. Audit Scotland has adopted a generic framework for the audit of best value across the public sector and this has been further developed during 2009/10 with the completion of its bank of best value Toolkits which, although primarily designed for audit use, are available to all public bodies for reference.

Exhibit 1: Framework for a best value audit of a public body





4. A linked development here has been the Scottish Government's work to refresh its 2006 best value Guidance for Public Bodies. This latter initiative, due for issue later in 2010, will result in clearer guidance to public bodies, and particularly those in the Central Government and Health sectors, on securing continuous improvement in performance, with due regard to the balance between cost and quality.
5. Throughout this report we comment on aspects of SHR's arrangements in this area. Our comments are made on the basis of information made available in the course of the annual audit. We do not make an overall best value judgement because we do not yet have enough evidence to conclude on all relevant areas. Our intention is to build up the corporate assessment over time. This report represents a further step towards that goal.
6. Another building block for our assessment of best value is the national study programme carried out by Audit Scotland on behalf of both the Auditor General for Scotland and the Accounts Commission. Where these have a bearing on the activities, risks or performance of SHR we make reference to these reports in this document. Full copies of the study reports can be obtained from Audit Scotland's website, www.audit-scotland.gov.uk.
7. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by management and members of SHR during the course of our audit. This report will be submitted to the Auditor General for Scotland and will be published on our website.



Financial Statements

8. In this section we summarise key outcomes from our audit of SHR's financial statements for 2009/10 and the 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

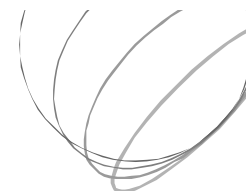
9. We audit the financial statements and give an opinion on:
 - whether they give a true and fair view of the financial position of SHR and its expenditure and income for the period in question
 - whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements
 - the consistency of the information which comprises the About Us, Performance against our six strategic objectives and the management commentary included with the Annual Report
 - the regularity of the expenditure and receipts.
10. We also review the statement on internal control by:
 - considering the adequacy of the process put in place by the Acting Chief Executive as Accountable Officer to obtain assurances on systems of internal control
 - assessing whether disclosures in the statement are consistent with our knowledge of SHR.

Overall conclusion

11. We have given an unqualified opinion on the financial statements of SHR for 2009/10.
12. As agreed the unaudited accounts were provided to us on 17 May 2010, supported by a comprehensive working paper package. We concluded our audit within the agreed timetable and provided our opinion to the Audit Committee on 23 June 2010 as timetabled.

Issues arising from the audit

13. As required by auditing standards we reported to the audit committee on 23 June 2010 the main issues arising from our audit of the financial statements. The key issues were:
 - **Balances with the Scottish Government:** SHR use the Scottish Government accounting system. The accounts of SHR include small balances with the Scottish Government which are



accounting errors relating to transferred assets and funding which require to be cleared out. SHR will work with the Scottish Government in 2010/11 in clearing the errors.

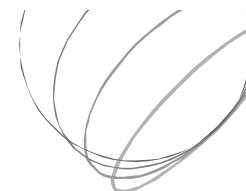
- **Non-current additions** – during the year SHR compared the physical assets held with records provided by the Scottish Government on transfer but the impact of the review was not clearly separated from other movements in non-current assets in the accounts. The accounts were adjusted to disclose the results of the asset review separately and SHR now have quarterly meetings to reconcile SHR asset listing with Scottish Government figures.

Regularity

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 issues were identified for disclosure.

International financial reporting standards (IFRS)

15. UK Government departments and other public sector bodies prepared their accounts in accordance with International Financial Reporting Standards (IFRS) for the first time in financial year 2009/10. The transition arrangements to IFRS required bodies to prepare IFRS shadow accounts for 2008/09, including revised opening balances as at 1 April 2008.
16. During 2009/10 we were required to review the shadow accounts and report on them to SHR by December 2009. The purpose of this exercise was to consider whether the shadow accounts had been properly prepared and report any matters that might prevent them forming a reliable basis for the first set of IFRS based accounts in 2009/10.
17. The shadow accounts and supporting documentation for the 2008/09 financial year were submitted by SHR for audit for review by the deadline date of 30 September. We made some recommendations for the production of the 2009/10 accounts and considered progress on these when we audited the 2009/10 accounts. These included consideration of segmental reporting analysis and identification of intangible assets; the 2009/10 accounts presented for audit met reporting requirements under IFRS.



Use of Resources

18. Sound management and use of resources (people, money and assets) to deliver strategic objectives is a key feature of best value. This section sets out our main findings from a review of SHR's financial position and financial sustainability.

Financial Position

Outturn 2009/10

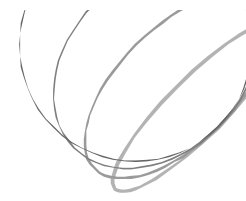
19. SHR is required to work within its resource budget set by the Scottish Government. SHR reported a net under spend of £704,000 in 2009/10. This is the difference between the operating costs for the period of £3.978 million and the budget set by the Scottish Government of £4.682 million. In quarter four £700,000 was returned to the Scottish Government giving a revised budget of £3.980 million. Outturn against the revised budget resulted in an under spend of £4,000. The under spend against the original budget was due to a lower than expected level of take-up of the Scottish Government severance scheme and reduced staff costs arising from vacancy rates (15-18%) in the first six months of the year.

Exhibit 2 – Performance against resource budget 2009/10 (£ million)

Limits	Original Budget	Revised Budget	Actual Outturn
Operating	4.682	3.982	3.978
Capital	Nil	Nil	Nil
Total	4.682	3.982	3.978

Scotland's public finances

20. The Auditor General's report on *Scotland's public finances, published in November 2009*, contained an overview of the financial environment in Scotland and the pressures and challenges facing the public sector. The aim of this report was to help to inform the debate on the future of public finances in Scotland. The key messages from this report were:



Extract from Auditor General's report *Scotland's public finances*

The public sector is coming under the greatest financial pressure since devolution.

- Scotland's economy is in recession and the public sector is under the greatest financial pressure since devolution ten years ago. It will be very challenging to maintain current levels of public services and meet new demands when resources are tight.
- The Scottish Government and the wider public sector need to work together to develop better activity, cost and performance information. This information is needed to enable informed choices to be made between competing priorities, and to encourage greater efficiency and productivity.

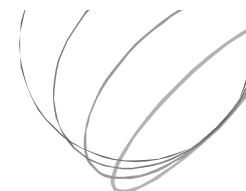
The Scottish Government faces significant challenges in balancing the budget while also delivering on its commitments and meeting increasing demands for public services.

- It remains unclear what impact the current recession will have beyond 2010/11. The Scottish budget is likely to reduce in real terms but the full extent of this is not yet known.
- In many cases, the public sector uses income from various sources to pay for services. Income levels anticipated before the recession are unlikely to be realised, reducing the amount available to spend.
- The Scottish public sector faces significant challenges in balancing its budget while also delivering on its commitments. Changes in Scotland's population and rising unemployment rates will increase demand for public services.
- Two per cent efficiency savings will not be sufficient beyond 2011 to bridge the gap between public spending and the smaller budget available.

In the current economic climate difficult decisions will have to be made about priority spending programmes.

- The Scottish Government's annual budget is largely developed on an incremental basis which involves making adjustments at the margin to existing budgets. This approach is not suitable for budgeting in a financial downturn because it does not easily allow informed choices to be made about priorities, based on robust information about activity, costs and performance.
- The Scottish Parliament has an important role in scrutinising the government's spending plans. Better information linking spending to costs, activities and service performance, and a rolling programme of performance reviews, would support the Scottish Parliament in fulfilling this role.

21. While SHR has under spent in the past two years, primarily due to unfilled vacancies, it has a number of priorities to review and consider the workforce-planning implications. It has to review activities and consider the workload under the new Housing Bill and manage the implications if there are any delays with legislation being implemented. SHR's priorities include providing assurance about the financial viability of Registered Social Landlords (RSLs); SHR has to respond to increased financial risk of RSLs which could lead to additional work to provide that assurance. RSLs are having to manage an increased demand for services when trying to finance increased interest charges. SHR also has to plan for the changed approach to scrutiny work under the National



Scrutiny Plan for Local Government. These pressures impact on staff costs and SHR's overall financial position.

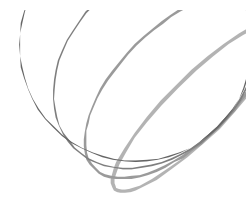
Financial sustainability and the 2010/11 budget

22. Scottish Ministers have agreed a resource budget for SHR of £4.330 million for 2010/11, which covers all expenditure. This is 7.5% less than the 2009/10 original budget but 8.8% above the 2009/10 outturn of £3.978 million.

Exhibit 3 – 2010/11 Resource Plan

Limits	Budget
	£million
Operating	4.330
Capital	nil
Total	4.330

23. Given the nature of SHR's organisation and activities it does not undertake large capital projects.
24. Salaries and related employee costs account for over 80% of the 2010/11 budget. Providing services and supporting delivery of reforms, while absorbing pay inflation and other cost pressures represents an on-going challenge for the organisation. SHR has forecast a balanced budget for 2010/11 and been preparing contingency plans for any future budget cuts. In addition the Scottish Government is seeking requests from staff to leave under early retirement and severance schemes which SHR may have to fund but the impact of the scheme on SHR is unknown at this time.



Governance and Accountability

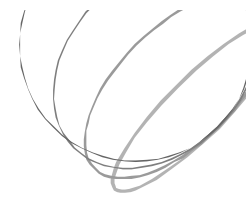
25. High standards of governance and accountability, with effective structures and processes to govern decision-making and balanced reporting of performance to the public, are fundamental features of best value. This section sets out our findings arising from a review of SHR arrangements.
26. Increasingly services are being delivered across the public sector through partnership working, sometimes involving complex governance and accountability arrangements. Best value characteristics also include effective partnership working to deliver sustained improvements in outcomes.

Overview of arrangements

27. This year we reviewed:
 - key systems of internal control
 - internal audit
 - arrangements for the prevention and detection of fraud and irregularity, including standards of conduct.
28. In October 2009 the former Chief Executive left SHR to join the Scottish Government and the Head of Inspection was appointed as Acting Chief Executive; the Head of Inspection post was back-filled, also in an acting capacity. This provides continuity of management to staff and stakeholders during the period towards implementation of The Housing (Scotland) Bill.
29. Our overall conclusion is that arrangements within SHR are satisfactory and have operated through 2009/10.

Housing (Scotland) Bill

30. The Housing (Scotland) Bill was introduced to the Scottish Parliament on 13 January 2010; royal assent is expected in November 2010 and the new legislation is expected to come into force in April 2011. The Bill will give SHR statutory operational independence under its own Board, with Board members being appointed by Ministers. It will also give SHR a more flexible range of intervention powers.
31. To manage the process through to April 2011 a Transition Advisory Group was established, with representation from Scottish Government and trade unions, and a Transition Plan prepared, which



covers governance arrangements and organisational change. The Head of Policy and Corporate Services provides progress updates to each Regulation Board meeting.

Systems of internal control

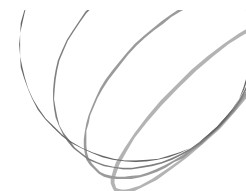
32. Key controls within systems should operate effectively and efficiently to accurately record financial transactions and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In their annual report for 2009/10 Scottish Government Internal Audit the internal auditors, provided their opinion that, based on the internal audit work undertaken during the year, there was substantial assurance on the adequacy and effectiveness on the systems of internal controls.
33. As part of our audit we reviewed the high level controls in a number of systems that impact on the financial statements. This audit work covered a number of areas including payroll, non-current assets and trade payables. We did identify a small number of areas where controls could be strengthened and agreed an action plan of improvements with management. This will be followed up in 2010 to confirm that improvements have been made.
34. We also rely on assurances received from the auditor of the Scottish Government on work performed on shared systems that operate at SHR, hosted by the Scottish Government. This supports our approach to deliver an audit without unnecessary duplication.
35. The shared systems assurance letter provided by the auditor of the Scottish Government concluded that there was adequate assurance for all systems except payroll. Adequate assurance is where key controls and procedures are operating to enable reliance to be placed on the system. Limited assurance was provided for the payroll system operated by the Scottish Government and we therefore carried out additional work locally to achieve our audit objectives. There is no impact on our overall audit opinion on the financial statements.

Statement on Internal Control

36. The Statement on Internal Control (SIC) reflected the main findings from both external and internal audit work. The SIC recorded management's responsibility for maintaining a sound system of internal control and set out SHR's approach to this.

Internal Audit

37. 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 2009/10 audit we assessed whether we could place reliance on SHR's internal audit function. We concluded that the



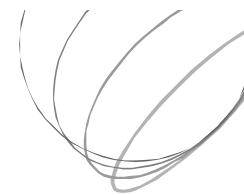
Scottish Government Internal Audit Division operates in accordance with the Government Internal Audit Manual and therefore placed reliance on their work in number of areas during 2009/10, as we anticipated in our annual audit plan. This included reliance on aspects of internal audit's systems work to avoid duplication of effort.

Prevention and detection of fraud and irregularities

38. During the audit we examined client procedures for recording staff expenditure (e.g. travel), gifts and hospitality. We also reviewed SHR's Code of Conduct, which is based on the Scottish Government model. We are satisfied that SHR 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.

National Studies

39. In September 2010, Audit Scotland will be publishing a national study on *The Role of Boards* which will be relevant to the governance of SHR, particularly when it becomes a non-ministerial department. Boards play a crucial role in ensuring that governance standards are maintained in public sector organisations and we will review the results of this study and consider any risks for SHR for the future.



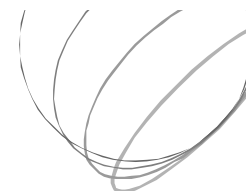
Performance

40. 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. Key features of best value include:
- setting a clear vision of what the organisation wants to achieve, backed up by plans and strategies to secure improvement, with resources aligned to support their delivery
 - a performance management culture which is embedded throughout the organisation and a performance management framework which is comprehensive and supports the delivery of improved outcomes.
41. In this section we comment on:
- SHR's corporate plan
 - scrutiny co-ordination
 - performance against targets
 - performance management arrangements
 - SHR's efficiency programme.

Vision and strategic direction

Corporate Plan

42. SHR agreed its corporate plan for 2008 – 2010 with Scottish Ministers in September 2008. The plan focuses on six strategic objectives:
- to hold regulated bodies to account for securing better service outcomes
 - to provide assurance about the financial viability of Registered Social Landlords (RSLs) and challenge all landlords to deliver better asset management and value for money
 - to secure good governance and accountability
 - to engage tenants and other service users in our work
 - to inform, and respond to, the Scottish Government's policy and investment priorities
 - to be a responsive and best value organisation.
43. In May 2010 SHR published their 2010/11 Corporate Plan. The original six strategic objectives per the 2008-2010 Corporate Plan, as described above, remain for the year through to April 2011. The plan also includes objectives for the transition process. SHR will:

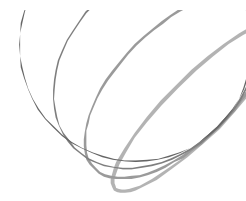


- manage the transition into an organisation fit for its new purpose, reflecting its new status and powers, and ensure that staff are fully engaged in the transition process
- ensure it is fully prepared for commencement of the new statutory duties and powers
- continue to regulate effectively through the period of change. Regulation will continue around principles of risk and proportionality.

44. SHR have a separate Transition Plan with milestones and target dates through to August 2012. SHR plan to deliver the transition process through work streams of governance and accountability; regulation policy; organisational structure and staffing; and business systems and continuity. Communications and stakeholder management will be a key strand running throughout all these work streams.
45. The delivery of the corporate plan objectives will be particularly challenging given the level of change for the body and the developments in the social housing sector over the same period of tight financial constraints. This is an area we will keep under review during our appointment.

Scrutiny Co-ordination

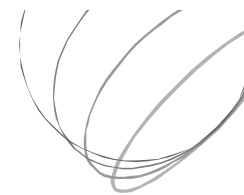
46. Following the publication of the Crerar report in September 2007, the Scottish Government's response stated its aim of establishing a simplified and coherent approach to delivering local government scrutiny. A key aspect of this agenda is to better coordinate and streamline scrutiny and achieve greater effectiveness, whilst at the same time protecting the independence of scrutiny bodies.
47. In February 2008, the Accounts Commission was asked to take on the transitional gatekeeping role in respect of the scrutiny of local government. The local government scrutiny coordination strategic group was established to set priorities and oversee development activity. The following key priorities were subsequently agreed:
 - improving the planning and scheduling of scrutiny activity
 - developing a single corporate assessment
 - implementing a shared risk assessment framework.
48. The strategic group established an operational group to carry out the necessary detailed work in respect of these priorities. The group is made up of representatives from SHR and other scrutiny bodies including Audit Scotland, Care Commission, COSLA, HM Inspectorate of Education, NHS Quality Improvement Scotland and Social Work Inspection Agency.



49. On 1 July 2010 the National Scrutiny Plan for Local Government 2010/11 was published, which sets out the strategic scrutiny work to be under taken and moves towards a more streamlined and proportionate approach to local government scrutiny. It is supported by a local Assurance and Improvement Plan for each council. Effective self-evaluation is seen as being central to reduced scrutiny but that independent challenge must continue to maintain public assurance The National Scrutiny Plan commits to further streamlining of scrutiny to bring efficiencies and to review the processes to ensure consistency and promote sharing of good practice.
50. These developments have been taking place during a time of significant reorganisation for scrutiny bodies. SHR have participated in establishing and developing LANs across all 32 councils. We will continue to monitor SHR's involvement in this important initiative.

Performance overview

51. The SHR 2009/10 Annual Report and Accounts provide details of performance, including outturn against key performance indicators, under each of the six strategic outcomes. Each year SHR conduct a financial health check of each RSL but with a difficult financial climate for the sector, in 2009 SHR reviewed business planning at a number of RSLs. Seeing the need for improvement SHR issued their report "Business Plan Guidance" to help RSLs.
52. A significant publication for SHR in 2009/10 was "Social Landlords in Scotland: Shaping up for Improvement" which comments on the performance of social landlords over the last five years and concludes that just under half of housing services provided were either poor or only adequate but that the sector was overall relatively financial stable. Where necessary SHR continue to make external Board appointments to RSLs to provide skills and experience during periods of significant change or difficulty.
53. The 2009/10 business plan, which is used internally to monitor performance, splits down the six strategic objectives into 30 activities and 78 targets with timescales. This compares to 2008/09 business plan which had 39 detailed objectives and over 100 targets, however, many of the 2008/09 targets related to SHR recruiting specific posts and establishing governance arrangements in the first year.
54. During the year the business plan was updated to reflect 14 targets being either transferred into the transition plan or rescheduled in 2010/11. In May 2010 the Regulation Board were updated on progress that the majority of the targets were achieved or related to on-going activity and the Executive Management Team were reviewing and rescheduling the remaining seven targets.
55. SHR has spent much time and resources on supporting the introduction of the Housing Bill and assessing the impact for the future and have had to prioritise workloads so that, as described above,



some targets have had to be re-scheduled e.g. reviewing complaints handling; develop a new approach to records and information management and develop a new intranet site. While the Annual Report explains the priorities for 2010/11 SHR should consider its public reporting on those areas that require to be carried forward until resources allow the work to be started.

Performance management

56. In 2008/09 SHR adopted the balanced scorecard approach to performance management but in early 2009/10 concluded that its complexity outweighed its practicality and SHR sought to develop an alternative reporting mechanism. For 2009/10 SHR set activities and targets under the six strategic objectives with set timescales and key performance indicators (KPIs) were established e.g. sickness absence and response times to Parliamentary requests. Progress against the business plan is reviewed by the Executive Management Team monthly and every quarter the Regulation Board are provided with:

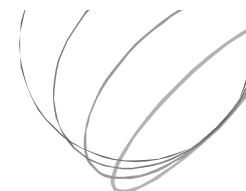
- KPI statistics for the quarter
- progress against activities on an exceptions basis
- progress against the Transition Plan. SHR deliberately keep the Transition Plan and business plan reporting separate to distinguish 'business as usual' activity from change activity.

57. SHR continue to develop their performance management framework. The SHR 2010/11 Business Plan includes 28 activities with 93 tasks and SHR have reduced the number of status categories from six to four. As change activities under the transition plan become 'business as usual' activity and SHR assess the impact of future budget changes, SHR should continue to review their business plan, for example by considering whether they have too many tasks and if they still reflect the priorities for the organisation. We will continue to monitor developments in the performance management framework.

Risk management

58. In our 2008/09 Annual Report on the Audit we noted that internal audit had concluded that in SHR's first year of operation it has made considerable progress in establishing a risk management framework. In 2009/10 the risk register, which detail activities to manage the risk, continues to be reviewed and updated as necessary at meetings of the Executive Management Team and the Regulation Board.

59. Some risks continue from last year particularly with respect to changing scrutiny environment and SHR's response to failing RSLs. Further risks have been added regarding the impact of the Housing Bill and SHR's related Transition Plan.



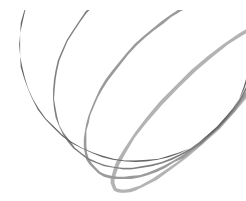
Improving public sector efficiency

60. The Audit Scotland report *Improving public sector efficiency* was published on 25 February 2010. It provided a position statement on the first year (2008/09) of the Efficient Government Programme (the Programme), which aims to deliver £1.6 billion efficiency savings over the three years to 2010/11. It also gave an update on how the Scottish Government and public bodies have addressed the recommendations made in the 2006 report about the previous efficiency programme.
61. The report found that Scottish public bodies reported more efficiency savings than the Government's two per cent target. But there are serious financial challenges ahead – the biggest since devolution – and making the required savings through efficiency will become increasingly difficult.
62. The report recommended that to deal with reduced future funding and increase savings, public bodies need to consider fresh approaches to improving efficiency and productivity. They must take a more fundamental approach to identifying priorities, improving the productivity of public services, and improving collaboration and joint working.
63. The drive to improve efficiency and productivity is not just an exercise for managers and service providers. It requires strong leadership and engagement from the very top of public bodies. Leaders and senior decision-makers within an organisation have a responsibility to check, challenge, monitor and support their organisations in delivering efficiency and productivity improvements. The report's recommendations highlighted areas that public bodies' key decision makers should look at to assess their organisation's development and to challenge existing arrangements (see below):

Extract from Audit Scotland report *Improving public sector efficiency*

In order to improve the delivery of efficiency savings public bodies should:

- ensure they have a priority-based approach to budgeting and spending
- continue to improve collaboration and joint working, overcoming traditional service boundaries
- consider using alternative providers of services, if these providers can improve the efficiency, productivity or quality of services
- improve information on costs, activity, productivity and outcomes, including setting baselines to measure performance against
- give greater urgency to developing benchmarking programmes
- maintain the momentum of activities and initiatives to improve purchasing and asset management and extend shared services
- ensure there is a joined-up approach to efficiency savings across the public sector, avoiding duplication
- ensure that plans are in place to deliver savings, clearly setting out what action will be taken, the level of savings to be delivered and how these will be measured
- strengthen the involvement of front-line staff, service providers and users in redesigning public services
- reduce reliance on non-recurring savings to meet financial targets and generally use these as part of a wider and longer term strategy
- report efficiency savings consistently.

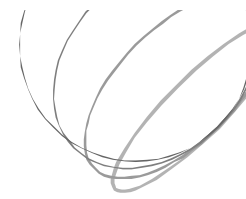


64. To support these high-level recommendations, Audit Scotland, the Northern Ireland Audit Office and the Wales Audit Office have drawn on their combined experience to develop a detailed good practice checklist. The checklist is intended to promote detailed review and reflection and, if necessary, a basis for improvement. We recommend that those responsible for leading efficiency and improvement work should consider assessing themselves against each question, and recording the results.
65. SHR's budget for 2010/11 is £4.330 million, which is 7.5% less than the 2009/10 original budget but 8.8% above the 2009/10 outturn, as demonstrated below:

Exhibit 4 – Outturn v budget 2008/09- 2010/11 (£ million)

Limits	Original Budget £m	Revised Budget £m	Actual Outturn £m
2010/11	4.330	-	-
2009/10	4.682	3.982	3.978
2008/09	4.575	4.346	3.908

66. Under spends in the past two years have primarily been due to reduced staff costs arising from delays in recruitment in year one and working with vacancy levels of 15 -18% in year two.
67. In response to the budget allocations SHR are carrying out financial scenario planning exercises looking at the impact of differing financial settlements. Payroll and staff-related costs account for over 80% of costs and SHR has a number of priorities and the related workforce-planning challenges to manage, as described earlier, and operating with current vacancy levels may be unsustainable in the longer term.
68. Also, in 2009/10 SHR recruited a procurement specialist to set up procurement frameworks for legal services and social housing specialists and these should be in place later in 2010. This should reduce SHR's need to contract for housing specialists under single tender/ non-competitive actions, which happened in 2008/09 when resources were required urgently.



Looking Forward

69. SHR faces a number of challenges in 2010/11, which include:

- **Efficiencies and future funding** - Scottish public bodies reported more efficiency savings than the Government's two per cent target in 2008/09, but there are serious financial challenges ahead – the biggest since devolution – and making the required savings through efficiency will become increasingly difficult. To deal with reduced future funding and increase savings fresh approaches to improving efficiency and productivity must be considered, taking a more fundamental approach to identifying priorities, improving the productivity of public services, and improving collaboration and joint working. The challenge for SHR is to prioritise spending, identify efficiencies and review future commitments to ensure delivery of key targets and objectives.
- **Financial management and affordability** – Scottish Government spending is set to decline significantly in the next few years as UK public finances come under increasing pressure. Effective budget monitoring and reporting arrangements will be crucial to SHR achieving its financial targets within tighter funding settlements. We will consider SHR's financial management arrangements as part of our 2010/11 audit.
- **Housing Bill** - The Housing (Scotland) Bill was introduced to the Scottish Parliament on 13 January 2010 with royal assent expected in November 2010. The bill would affect SHR by giving it statutory operational independence under its own Board, with Board members being appointed by Ministers. SHR has a transition plan in place linking the progression of the Housing Bill with SHR's key activities through to 2012. SHR will continue to support the Scottish Government as the Housing Bill progresses through Parliament.
- **Scrutiny Co-ordination** – 2010/11 is the second year of the joint scrutiny plan for local government in Scotland. Implementation of the shared risk assessment arrangements progresses and we will continue to monitor the impact of these developments on SHR.
- **Best Value** - The concept of best value is seen as a key driver of modernisation and improvement in public services. Audit Scotland has continued its commitment to extending the best value audit regime across the whole public sector and significant development work has taken place over the last year including the finalisation of its best value toolkits. This has been matched by the Scottish Government's commitment to refreshing its Best Value Guidance for Public Bodies. SHR should continue to respond to this important initiative as it develops. While SHR's sixth strategic objective is to be a responsive and best value organisation a challenge for SHR is to consider how they can demonstrate overall that arrangements have been made to secure best value.