

# ANNUAL REPORT AND ACCOUNTS

13/14

Year ended 31 March 2014

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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# Welcome

## Chair's welcome

Welcome to Audit Scotland's annual report for 2013/14.

The past year has been one of ongoing change for Scotland's public sector. We have seen major reform, such as the launch of the new single police and fire forces, the reorganisation of Scotland's further education colleges, and new legislation that will change the way public bodies work and deliver services to the people of Scotland. This is at a time of growing demands and reducing resources.

One of the strengths of having a public audit model is that we understand the environment in which we and the bodies we audit operate. As the times change Audit Scotland must respond and adapt. So we have been examining how we ourselves work and what the people of Scotland, public bodies and decision-makers expect of us and what we produce for the Auditor General and the Accounts Commission. This will help ensure we are targeting the right areas, working effectively and efficiently, and that we reach the different audiences for our work in ways that reflect their needs and how they access and use information.

We have done much over recent years to reduce our costs and become a more efficient, streamlined organisation. I am pleased that throughout this we have maintained a high standard of performance and audit service.

The Board sets and monitors the strategic direction of Audit Scotland while overseeing Audit Scotland's work and striving for excellent governance and management. The board's focus has been on making sure we use the resources we have to maximise the quality and impact of our work, while identifying and preparing for the challenges of the future.

This has also been a year of considerable change for the Audit Scotland Board itself. We said goodbye to John Baillie, who served for nine years, including three as chair, and also to Katharine Bryan who completed a three-year term with us. My thanks go to both of them for their significant and distinctive contributions.

This is my last annual report as Chair of Audit Scotland's Board. During my time in the post, I have been struck by the enthusiasm, dedication and commitment to quality of Audit Scotland's staff. It has been a pleasure to work with people who not only understand the importance of what they do, but take pride in doing it and doing it well. I would like to thank them and my fellow board members for their work and support over 2013/14 and the preceding years.

**Ronnie Cleland, Chair of Audit Scotland Board**

## Accountable Officer's report

The financial environment for Scotland's public bodies continues to change. Clear comprehensive financial reporting is more important than at any time I can remember. Neither can I think of a more exciting or demanding time to be involved in public audit, nor for audit to make more of a contribution to the effective use of public resources.

From next year, the Scotland Act 2012 will start coming into effect, devolving new tax and borrowing powers to the Scottish Parliament, with the aim of increasing autonomy and strengthening accountability. This will bring opportunities and challenges regardless of the outcome of the independence referendum this September.

During 2013/14, we explored both how we as an organisation need to prepare for this and also considered how Scotland's public sector can prepare. We also promoted the need for better reporting of public finances. Financial management and reporting in Scotland is starting from a strong base – for example, it is relatively rare for us to have to highlight accounting issues in a body's accounts to the Scottish Parliament or the Accounts Commission – but there are gaps such as the lack of a complete picture of the public sector's assets and liabilities. Comprehensive, transparent and reliable financial reporting is vital to holding public bodies to account, improving confidence in public finances, and providing important information for decisions about public services. We will continue to highlight where there is room for further improvements in financial reporting.

I am very conscious of the need to demonstrate that Audit Scotland itself provides value for money and makes a real contribution to public services. We have delivered on our promise to reduce the cost of audit by at least 20 per cent in real terms over the four years to 2014/15, in fact making a 23.5 per cent reduction. We cut audit fees to public bodies by six per cent in the last completed audit year (2012/13). In 2013/14, we delivered £1.6 million of efficiency savings, against a target of £0.8 million. This figure represented 6.8 per cent of our budget. Over recent years we have reshaped our workforce and reduced our costs. Our focus during 2013/14 was on strengthening our structure, skills and technology to ensure we have the capacity needed to deliver our responsibilities, particularly through the merger of two of our directorates and through increased opportunities for professional and personal development.

During all of this, we remain committed to world-class audit work that improves the use of public money. This report provides you with detail of the many pieces of work we produced in 2013/14 that have contributed to improving and reshaping Scotland's public services so that they are fit for the future. I would like to thank my colleagues at Audit Scotland and my fellow board members for their strong support and hard work.

**Caroline Gardner, Accountable Officer**

# Who we are

## About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our reports to the Auditor General for Scotland and Accounts Commission for Scotland, we provide independent assurance to the people of Scotland that public money is spent properly and provides value for money. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations for improvement, and following these up.

## Who we are

Audit Scotland is a statutory body that carries out audits and investigations for the Auditor General and the Accounts Commission. Together, we shape and deliver public audit in Scotland.

The Auditor General secures the audit of the Scottish Government and other public bodies in Scotland, except local authorities, and is independent of the Scottish Government and the Scottish Parliament.

From 1 April 2013, Police Scotland and the Scottish Fire and Rescue Service will be audited by the Auditor General. The police and fire boards they replace were previously audited by the Accounts Commission.

The Accounts Commission is the public spending watchdog for local government. It holds councils in Scotland to account and helps them improve. It operates impartially and independently of councils and the Scottish Government and meets and reports in public.

Our stakeholders are the people of Scotland, the Scottish Parliament, the Scottish Government, and all Scottish public organisations.

Audit Scotland is governed by its board and held to account by the Scottish Commission for Public Audit - see page 18 for details.

## Our resources

- 258 whole-time equivalent staff as at 31 March 2014.
- £17.5 million from audit fees from public bodies, bank interest, and miscellaneous income.
- £6.6 million direct funding from the Scottish Parliament.
- Seven private firms of accountants appointed to carry out about half of the annual audits.

## Our performance

Reducing the cost of audit (in real terms)	2013/14	2012/13	2011/12
Audit fee reduction by audit year*	-2.00%	-6.45%	-9.25%

Note: \* An audit year runs from November to October and bridges two financial years. The 2012/13 audit year was started in financial year 2012/13 and completed in financial year 2013/14.

Objectives	2013/14	2012/13	2011/12
Annual audit of public bodies	208	214	211
10 – 12 performance audits	16	14	15
5 – 8 Best Value audits	4	8	12
Community Planning Partnership audits*	0	4	n/a
32 risk assessments in local government	32	32	32
Coordinating scrutiny across local government	✓	✓	✓
National Fraud Initiative (biennial)	n/a	✓	n/a
Housing benefit audits	✓	✓	✓

Notes:

\* Following an independent evaluation, our approach to these audits has now been developed further and we are planning a series of individual CPP reports during 2014/15.

# Our work

As public bodies face increasing demands on services, in many cases combined with decreasing funding, they need to make important decisions about their spending and their services.

During 2013/14 we provided high-quality financial audits that gave accurate, transparent and comprehensive information to public bodies about factors such as assets, arm-length external organisations and major projects so that decisions about future spending are well informed.

We also produced performance audits on behalf of the Auditor General and the Accounts Commission, covering specific themes or topics, or particular sectors. For this aspect of the work, we consult internally and externally before finalising our forward work programme. We do this via our website, and by taking the proposed programme for this work to the Public Audit Committee of the Scottish Parliament. It is then approved by the Auditor General and the Accounts Commission.

We report on all of these areas in more detail below, and a full list of our published work appears on page 23.

## The financial audit

Number of bodies audited by sector	2013/14	2012/13	2011/12
Scottish Parliament	1	1	1
Central government	75	76	72
NHS	23	23	23
Further education	32	37	38
Local government	77	77	77
<b>Total</b>	<b>208</b>	<b>214</b>	<b>211</b>

Financial auditors - both from Audit Scotland and those from the private firms of accountants appointed to carry out the annual audits - work closely with public bodies. As well as holding them to account for their use of public money, the auditors support improvement in organisations, and provide feedback and recommendations on their performance.

The vast majority of opinions given by appointed auditors are unqualified which means that we are able to provide an assurance that an organisation's financial statements offer a true and fair view of its financial position. However, where auditors disagree or wish to refer to any limit of scope of that opinion, they will qualify their opinion. This year, one qualification was issued on the Scottish Consolidated Fund Account.



We carry out comprehensive financial audits across the public sector to the highest auditing standards, with a continued focus on accurate, transparent reporting. Most accounts are prepared under International Financial Reporting Standards, the same standards applied to listed companies. We use International Standards on Auditing, the standards used in the private sector, and our work is undertaken in accordance with the Code of Audit Practice approved by the Auditor General and the Accounts Commission.

Auditors completed all the audits of health, central government, further education and local authority bodies on time.

Annual audit reports cover the full range of audit work done in the year and can be found on Audit Scotland's website.

In the coming year, our financial auditors will audit a number of local government charities for the first time. They are also preparing for the audit of new integrated health and social care joint boards and a significant extension in the scope of our work on European agricultural funds.

## Highlighting issues from accounts

We bring significant issues from the annual audits to the attention of the Scottish Parliament and the Accounts Commission. This helps to ensure effective scrutiny of the use of public funds.

The Auditor General can issue reports to the Scottish Parliament under section 22 of the Public Finance and Accountability (Scotland) Act 2000. In 2013/14 we issued one section 22 report, on Adam Smith College.

For local authorities, the Controller of Audit issues statutory reports to the Accounts Commission. These include Best Value and Community Planning Partnership reports (see page 12 for details). Two other reports were also produced during 2013/14 on Highland Council's Caithness Heat and Power project, and on a number of issues arising at Argyll and Bute Council.

## Identifying fraud and errors

Audit Scotland coordinates the National Fraud Initiative (NFI) in Scotland, a data-matching exercise that brings together auditors and public bodies to identify public sector fraud and error.

We compare information from the public sector in areas such as housing benefits, payrolls, pensions, disabled parking permits and council tax records. Since the NFI started in 1996, it has helped bodies identify overpayments made through fraud and error worth £94 million in Scotland and over £1 billion across the UK. Effective anti-fraud arrangements can also act as a deterrent. We will publish a report on the latest NFI exercise in June 2014.

The Accounts Commission has responsibility for auditing housing benefit services in Scotland. Through our benefits performance audit, we use a risk-based approach to hold councils to

account and help them to improve their benefits services. During 2013/14, we carried out ten housing benefit risk assessments and agreed action plans with councils to address risks identified. After reviewing those action plans, we requested updates from four councils to review the progress being made.

## Performance and Best Value reports

Audit sector	2013/14	2012/13	2011/12
Cross-sector (including CPPs)	4	6	8
NHS	2	3	3
Central government	6	3	1
Local government	4	6	3
Best Value in local government	4	8	12
<b>Total*</b>	<b>20</b>	<b>26</b>	<b>27</b>

Note:\* the total number of reports carried out in any one year will reflect a number of factors such as the length/type of report.

We are able to carry out performance audits across the entire public sector for the Auditor General and the Accounts Commission, and we report on these in public. This year, report topics included:

- Modern apprenticeships
- Reshaping care for older people
- Police reform
- Renewable energy
- Scotland's colleges
- Housing in Scotland
- Scotland's key transport infrastructure projects
- Managing early departures from the Scottish public sector

For a full list of our published reports see pages 23 and 24.

This work enables the Auditor General and the Accounts Commission to highlight areas where services could improve, how bodies can plan for the future and where money can be saved without reducing or affecting the quality of public services. For instance, in 2013/14, we reviewed the government's 10-year project to improve health and social services for people aged 65 or over. The report made recommendations aimed at helping accelerate change, particularly given the growing pressure on services and the integration of health and social care.

*Scotland's colleges 2013*, provided an update on the sector's financial standing and reviewed recent progress towards the structural reform of colleges. It recommended that the Scottish Government and Scottish Funding Council will need to assess and manage the impact on their finances of colleges becoming public bodies. They will also need to monitor the savings and other benefits from mergers, and the impact that prioritising younger students and full-time courses has on the opportunities for older people.

The report *Police reform in Scotland* reviewed the process of creating a single national police service. It made recommendations aimed at helping the new service achieve its intended savings of £1.1 billion by 2026 and at improving the reporting on police performance to help in the scrutiny of the service.

Also during 2013/14 we highlighted the need for more comprehensive and clearer public reporting on the costs of public projects and on public finances. For example, our review of five major transport infrastructure projects found that while the stated public cost of building them was £3.8 billion, the actual total of public money committed is £7.5 billion over the next 30 years.

Our report on developing financial reporting in Scotland made recommendations on improving the transparency of public reporting. It suggested having a clearer picture of the public sector's assets and liabilities ahead of Scotland receiving new tax and borrowing powers.

We also emphasised the need for public bodies to start planning how they will deliver services in the future. Our review of NHS finances said the current model of services was not sustainable and we suggested health boards improve their long-term financial planning to help in redesigning services. We also produced guidelines on good practice for public bodies when letting staff leave in early release schemes.

In December, we reported on work following up our February 2013 report on waiting list management. We found that NHS boards had acted on the recommendations we had made to improve management and scrutiny of lists.

Reports for the Auditor General and joint reports for the Auditor General and the Accounts Commission are considered by the Scottish Parliament.

## Scottish Parliament

The Auditor General presented 12 performance audits to the Scottish Parliament's Public Audit Committee (PAC). In 2013/14, the committee held evidence sessions on six of these:

- Scotland's key transport infrastructure projects
- Developing financial reporting in Scotland
- Scotland's colleges 2013
- NHS financial performance 2012/13
- Police reform: Progress update 2013
- Management of patients on NHS waiting lists.

The committee called relevant accountable officers from the Scottish Government and other public bodies to give evidence and answer questions about issues raised. For example, the PAC heard from the Health Secretary and key Scottish Government officials following publication of two of our reports on the health service.

In addition we gave evidence to the PAC on audit arrangements for the Scottish rate of income tax and to other committees including Finance, and Local Government and Regeneration.

Audit Scotland also helped the Accounts Commission present evidence to the Local Government Committee and jointly with the Auditor General to the Public Audit Committee.

## Best Value

During 2013/14 we continued to deliver Best Value (BV) audits of local authorities for the Controller of Audit. We now target our work based on the risk assessments we carry out annually in partnership with other scrutiny bodies. In 2013/14 we published reports on the audits of four councils: City of Edinburgh; Moray; Aberdeenshire; and South Ayrshire. The Accounts Commission published findings on these four audits and on two Controller of Audit statutory reports on Highland Council's Caithness Heat and Power project, and on a number of issues arising at Argyll and Bute Council. The Accounts Commission publishes a separate annual report on its work.

We also continued the 'How councils work' series of publications for the Accounts Commission aimed at supporting improvement. We published two reports on: charging for services and options appraisal, which provided advice to councils on how best to consider different ways of providing goods and services.

## Community Planning Partnerships

Following a request from the Cabinet Secretary for Finance, Employment and Sustainable Growth to the Accounts Commission, Audit Scotland worked with its scrutiny partners and other key stakeholders in developing an audit framework for supporting improved performance and accountability of Community Planning Partnerships (CPPs). The audit methodology was tested in three early audits carried out in Aberdeen City, Scottish Borders and North Ayrshire. Their audit reports were published in 2013 along with a national overview report drawing on the common messages from the three reports. Following an independent evaluation, our approach to these audits has now been developed further and we are planning a series of individual CPP reports during 2014/15. These are produced jointly by the Controller of Audit and the Auditor General.

## Scrutiny co-ordination

Audit Scotland, on behalf of the Accounts Commission, continues to work with other scrutiny bodies to make sure that the scrutiny of local government is better targeted and more proportionate to identified risks. The Accounts Commission is responsible for co-ordinating and facilitating scrutiny in local government.

This year we again produced individual assurance and improvement plans (AIPs) for each council. From these, we have drawn up a scrutiny plan showing what scrutiny activity we will seek to ensure the council keeps on track with what it is trying to do and any improvements it needs to make. Details of our current national scrutiny plan are on our website.

## Quality

Audit Scotland places great emphasis on achieving high quality in all our audit work. The board leads this through approving a Corporate Quality Framework which sets out the key elements of the approach.

Our business groups apply quality control processes to all their work and reports, which are backed up by independent reviews. For example, we give a selection of our performance audit reports to other UK audit agencies – the National Audit Office, the Wales Audit Office and the Northern Ireland Audit Office – for peer review each year. We then use any improvements identified in future work.

Our financial audit work has been reviewed by the Institute of Chartered Accountants of Scotland (ICAS) who looked at six audits chosen to cover a range of audited bodies. The reviews assess the quality of audit work and compliance with auditing and ethical standards as well as progress made against findings from the previous review. We are pleased with the positive assurance provided by the ICAS work and the relatively small number of areas for improvement identified.

We also regularly seek feedback from public bodies on the quality of our audit work. This year we surveyed local and central government bodies, with positive responses about the overall quality of our service from 97 per cent and 94 per cent of each sector respectively and which also highlights areas where we can still do better.

Each year we produce a Transparency and Quality Report which describes our arrangements for achieving high-quality audit work in more detail. This is available on our website.

## Impact

To measure and report impact, we use a framework which sets out the four broad areas where we expect our work to make a difference. These are: financial sustainability, value for money, governance and financial management and transparency of reporting. They have been collectively identified by Audit Scotland as the public sector audit dimensions and are used to plan, report and measure the impact of our work. We publish a report on this which is available online.

When we asked audited bodies about the contribution our work made across the four public sector audit dimensions, they reported that the biggest contribution was in improving governance and financial management.

## Ethical standards

The independence of public audit helps ensure its effectiveness. Audit Scotland has adopted the principles of the Financial Reporting Council's ethical standards for auditors. While the standards only apply to financial audit work, we apply them to all our work. The Assistant Auditor General performs the role of ethics partner and provides advice on applying the standards. This year we have extended the formal annual declarations of potential conflicts of interest and ethical issues to all staff, in order to be able to demonstrate the same high standards being applied across all our work and to support increased flexible working across the organisation.

## Technical guidance and assistance

Audit Scotland contributes to improvements in accounting, financial reporting and auditing in the public sector through the technical guidance and assistance we provide to appointed auditors. We also make this via this our website to finance professionals across the Scottish public sector. We published 15 in-depth guidance notes and four bulletins explaining technical developments.

We added 240 documents to our online technical reference library, and responded to 596 technical enquiries from auditors and stakeholders. We also contributed to the preparation of externally produced codes and manuals.

## Working with other countries

The work of Audit Scotland is valued by other countries and this is reflected in requests for assistance and visits from overseas organisations. In 2013/14, we continued to participate in the audit of the United Nations in partnership with the UK National Audit Office, provided mentoring and technical advice to the Office of the Auditor General of Kosovo and are currently helping the development of modern, accountable services at the Serbian Ministry of the Interior and Police. We hosted seven international delegations, presented a paper on auditing economic activities to the October 2013 European Organisation of Regional External Public Finance Audit Institutions (EURORAI) conference and we will be hosting the October 2014 EURORAI conference in Edinburgh. A separate report on our work with other countries is available on our website.

# Our organisation

## Our business

In 2013/14, we continued to reduce the cost of audit while ensuring we prepare for the future. This reflects the responsibility we have to be as efficient as possible with our own use of resources, and our response to the difficult circumstances faced by the public bodies we audit.

The cumulative fee reduction since 2009/10 is now 23.5 per cent in real terms, which is above our target of reducing fees by at least 20 per cent by April 2014. In the last completed audit year (2012/13), while continuing to provide a high-quality service, we reduced audit fees to public bodies by six per cent, and will continue with reductions in the 2013/14 audit year.

We are also preparing for the future, both in our workforce planning and in the priorities we have set for changing the way we work. In 2013 we launched three key projects: review of the expectations of audit; streamlining audit; and audit intelligence, and we are continuing these projects into 2014/15. Together, these will ensure we are: targeting the right areas with our work; doing it as effectively and efficiently as we can; and the outputs we produce reflect the audiences for our work, developments in information technology and the way people access, digest and use information.

As part of our continuous efforts to streamline our work, we also merged our Performance Audit and Best Value directorates, and reduced the size of our management team.

## Workforce planning and staff development

Over the past four years, through our voluntary early release scheme and natural turnover, we have reduced our whole-time equivalent staff numbers from 293 to 258, which is ahead of schedule in our workforce plan. At the same time, we have changed our grade mix to achieve a more effective balance of skills. During 2013/14 we targeted recruitment to ensure we have the skill mix and the capacity to maintain our current work and carry out developments and improvements.

We have continued our commitment to staff development and engagement. We launched our Personal Development and Growth initiative during 2013, along with an internal online learning portal, and in early 2014 started our healthy working lives initiative. Our Performance Appraisal and Development (PAD) scheme helps all our staff maintain and develop their skills. During 2013/14, staff received an average of 12.7 days each of training and personal development (compared with 7.81 days in 2012/13).

We also run one of the largest public sector accountancy training schemes in Scotland. We had 35 trainees and staff working towards CIPFA and ICAS qualifications. Six trainees successfully completed their qualifications during the year. We recruited 10 new graduate trainees.



We held a series of 'Re:Connect' sessions involving all colleagues and used that time to discuss the various scenarios to which audit might have to respond over the next three years. We also staged a series of 'knowledge cafes' for staff, bringing in experts from across Scotland to help us understand and respond to some of the challenges facing Scotland.

This year we kept our status as 'One to watch' in the Best Companies survey of workplaces. We have a partnership forum for regular consultation with our staff trade union.

We continued our office rationalisation programme, moving our West of Scotland office to central Glasgow and beginning our planning to merge our two Edinburgh offices into one.

Staff information	2013/14	2012/13	2011/12
Staff (whole-time equivalent)*	258	260	255
Staff turnover	9.98%	8.6%	12.27%
Sickness absence/person**	5.99 days	5.95 days	4.77 days
Male/female staff%	49.3/50.7	50/50	49.8/50.2
Male/female Board members%	60/40	60/40	80/20
Male/female Senior Management%	33.3/66.7	28.5/71.5	28.5/71.5

Notes: \*At 31 March

\*\*Public sector average is nine days/person.

## Diversity and equality

Our approach to diversity and equality is led by a steering group comprising colleagues from all our business groups. We published our equality outcomes and a report on how we are mainstreaming equalities in April 2013, as required under new equalities legislation. Our steering group regularly monitors our progress against our equalities outcomes and will prepare a report on this in April 2015. In the meantime we have published an interim update which is available on our website.

Our equality outcomes and approach to mainstreaming equalities are on our website.

## Community, social and human rights

We are committed to conducting our work to the highest standards and building positive relationships with communities in Scotland. We have established a Giving Something Back group to consider ways that Audit Scotland can help colleagues to give something back to the community. We currently have three members of staff who undertake public duties under our Public Duties policy. Over 2013-14 we had five people involved in the Pilotlight scheme which matches skilled business leaders with charities and social enterprises. Audit Scotland staff took part in 'DoNation' which helps people drive down their carbon footprint; we had 131 pledges which will save 8 tonnes of CO<sub>2</sub>.



## Responding to public concerns

Audit Scotland receives enquiries from a wide range of people about the bodies we audit. Where appropriate, we may carry out further audit work in response. In 2013/14, we received 267 items of correspondence raising concerns (compared with 177 in 2012/13).

We receive many routine requests for information on a daily basis. Where the requests are non-routine, complex or are submitted under the Freedom of Information (Scotland) Act 2002 we record them. This year we received and recorded 63 Freedom of Information requests (38 in 2012/13). There was one data subject access request, which was later withdrawn, under the Data Protection Act, and no Environmental Information Regulations (EIR) requests.

Our complaints process records how Audit Scotland has dealt with complaints from members of the public about the way their concerns have been dealt with. In 2013/14, we investigated three such complaints from members of the public (two in 2012/13).

The Public Services Reform (Scotland) Act 2010, which came into force on 1 October 2010, places duties on public bodies to provide and publish information on certain expenditure and exercise of functions. The information for 2013/14 is available on our website.

## Managing our resources and sustainability

In our Carbon Management Plan we aimed to reduce our carbon footprint by 20 per cent, or 107 tonnes of CO<sub>2</sub>, by 2014. By the end of last year we had already significantly surpassed that five-year reduction target. This was achieved through rationalising our offices, the impact of lower car travel mileage and the introduction of a greener fleet.

We continued to demonstrate improved performance across a range of fronts in our Carbon Management Performance during 2013/14. This gives us a good platform upon which to build as we develop our next Carbon Management Plan for 2015/20 which will be focusing on:

- Travel and energy use (ICT and Buildings)
- Waste reduction
- Staff behaviour change
- Mainstreaming environmental performance management.

Our report on sustainability is available on our website.

## Internal audit and risk management

Audit Scotland's audit committee supports our board in its responsibilities for risk, control and governance, and associated assurance. The committee strengthened its membership by co-opting a new member, for a term of one year. The committee met four times in 2013/14 and considered ten internal audit and advisory reports.

Most internal audits in 2013/14 achieved 'substantial assurance', the highest standard available, from our internal auditors BDO LLP. A follow-up report confirmed that we were making excellent progress in applying previous recommendations.

## Our governance and management

### Our board

Our board sets and monitors the strategic direction of Audit Scotland while overseeing Audit Scotland's work and striving for high standards of governance and management.

In addition to considering reports on streamlining the business and expectations of audit, the board also considered the implications for Audit Scotland of The Scotland Act 2012 and other constitutional change. The board continued to gain an understanding of the views and expectations of clients and stakeholders on the role of public audit.

The board has an audit committee which recommends the appointment of our internal auditors and receives our annual accounts and internal audit reports. The committee has started the procurement process for the next three-year appointment of internal auditors to Audit Scotland (for the period 2014-17).

The board met nine times during the year, and the Audit Committee four times.

The board also has a remuneration and human resources committee which sets and reviews the salaries of senior staff (excluding the Auditor General, whose salary is agreed by the Scottish Parliamentary Corporate Body) and the main terms and conditions for all staff. The Remuneration and Human Resource Committee met four times this year.

The board has agreed on a framework which sets out the principles of partnership working between the Auditor General, the Accounts Commission and Audit Scotland. The framework is designed to make sure the parties work together to deliver their vision for public audit.

### Our board members are:

- Ronnie Cleland - Chair of the board
- Douglas Sinclair - Chair of the Accounts Commission (from 1 December, 2013)
- Caroline Gardner - Auditor General and Accountable Officer for Audit Scotland
- Katharine Bryan - Independent non-executive member (until 31 March 2014)
- John Maclean - Independent non-executive member.

Ian Leitch joined our Board on 1 April 2014.

Our audit committee consists of John Maclean (chair), Douglas Sinclair and Katharine Bryan (until 31 March 2014). In January 2014, Heather Logan joined us as a co-opted member.

Our remuneration and human resources committee consists of Katharine Bryan (chair - until 31 March 2014), Douglas Sinclair and John Maclean.

John Baillie was a member of our board, audit committee and remuneration and human resources committee until 30 November 2013 in his capacity as then Chair of the Accounts Commission.

## Scottish Commission for Public Audit

Audit Scotland is held to account by Parliament through statutory arrangements put in place by the Scotland Act 1998 and through the Public Finance and Accountability (Scotland) Act 2000. The Scottish Commission for Public Audit (SCPA) is central to these arrangements. The SCPA consists of five MSPs and meets in public. It appoints our non-executive board members and chair, scrutinises our budget, annual report and accounts, and produces reports on these. It appoints our external auditors, currently Alexander Sloan Chartered Accountants.

## Our senior management

Our senior management team oversees the day-to-day operations of Audit Scotland's work, with each member taking responsibility for a specific area.

The members of the Management Team are:

- Caroline Gardner - Auditor General and Accountable Officer for Audit Scotland
- Diane McGiffen - Chief Operating Officer
- Russell Frith - Assistant Auditor General
- Fraser McKinlay - Director of Performance Audit and Best Value (PABV), and Controller of Audit
- Fiona Kordiak - Director of Audit Services
- Lynn Bradley - Director of Corporate Programmes and Performance.

Barbara Hurst was a member of the Management Team as Director of Performance Audit until 3 July 2013.

# Our finances

## Financial summary

Audit Scotland is required to produce annual accounts detailing the resources acquired, held or disposed of during the financial year and the way in which they were used. The Auditor General for Scotland has been appointed as Accountable Officer and is responsible for the preparation of these accounts.

Audit Scotland's accounts are independently audited on behalf of the Scottish Commission for Public Audit (SCPA), which appointed Alexander Sloan Chartered Accountants to carry out the audit.

During the year, HMRC confirmed Audit Scotland's VAT status. On behalf of the Accounts Commission, Audit Scotland continues to recover input tax in respect of external auditor fees and expenses incurred in the delivery of local authority audits.

The following section provides a summary from the accounts. The full accounts are published on pages 30 to 62 and are available on our website.

## A summary of income and expenditure

Direct funding from Parliament	2013/14		2012/13	
	Actual £000	Budget £000	Actual £000	Budget £000
Expenditure - total resource requirement	24,141	24,233	23,965	24,061
Income	17,493	16,851	16,783	17,103
<b>Net Operating (Cost)</b>	<b>(6,648)</b>	<b>(7,382)</b>	<b>(7,182)</b>	<b>(7,048)</b>

In 2013/14, Audit Scotland spent £24.1 million on services for the Auditor General and the Accounts Commission. Of these costs, £17.5m were recovered through charges to audited bodies and miscellaneous income. The balance of expenditure £6.6m was met from direct funding provided by the Scottish Parliament.

In 2013/14, we delivered £1.6m of efficiency savings against a target of £0.8m. This was 6.8% of our budget. The majority of savings came from reductions in staff, external consultancy, printing and stationery and property costs.

## 2013/14 financial results

In 2013/14, income earned from audited bodies and miscellaneous income was £17,493k. Expenditure in the same period was £24,141k. The resulting Net Operating Cost of £6,648k

was £734k less than the estimated net resource requirement (budget) of £7,382k provided by the Scottish Parliament. Income earned in the year was £642k more than budget while expenditure was £92k less than budget.

## Analysis of expenditure

Expenditure	2013/14		2012/13	
	£000	% total	£000	% total
Staff and members' costs	14,755	61	14,131	59
Fees and expenses paid to appointed auditors	5,193	21	5,036	21
Buildings, rent and depreciation	1,625	7	1,698	7
Operating costs	2,560	11	3,089	13
<b>Gross Administration costs</b>	<b>24,133</b>	<b>100</b>	<b>23,954</b>	<b>100</b>
Corporation Tax	8	-	11	-
<b>Total resource requirement</b>	<b>24,141</b>	<b>100</b>	<b>23,965</b>	<b>100</b>

## Sources of income

Income	2013/14		2012/13	
	£000	% total	£000	% total
Fees paid by local authorities	11,665	67	11,419	68
Fees paid by health bodies	3,750	21	3,506	21
Fees paid by further education colleges	629	4	538	3
Fees paid by Scottish Government and sponsored bodies	1,957	11	1,780	11
<b>Total fee income</b>	<b>18,001</b>	<b>103</b>	<b>17,243</b>	<b>103</b>
Bank interest	41	-	52	-
Miscellaneous	164	1	43	-
Other finance income (pensions)*	(713)	-4	(555)	-3
<b>Total</b>	<b>17,493</b>	<b>100</b>	<b>16,783</b>	<b>100</b>

Note: \* Other finance income is comprised of the expected interest income from the local government pension scheme assets less the interest payable on the scheme liabilities. The 2012/13 figure has been restated to reflect compliance with the revised International Accounting Standard 19 on employee benefits.

## Comparison with previous year

Expenditure in 2013/14 was £176k more than in the previous year.

Staff costs in 2013/14 increased by £624k of which £391k of the increase was attributable to charges arising from compliance with International Accounting Standard 19 (IAS19) on employer benefits - the increased charge related to pensions and is driven by the ongoing impact of low interest rates and their effect on the net discount rates used to value pension liabilities and charges. The remainder of the increase due to the employment of two additional members of staff (+£102k), and the impact of pay growth (+1%).

Fees and expenses paid to appointed audit firms were £157k higher than the previous year as a result of annual contractual increases (1%) and impact of additional audit work. completed in the year.

The increases recorded for staff costs and fees and expenses paid to appointed audit firms were offset by cost reductions recorded for buildings, rent and depreciation, £73k, and operating cost, £532k.

A total of £356k of the operating cost reduction was attributable to VAT - in 2012/13 a provision of £204k for outstanding VAT was made while this year's results include a credit of £152k. Reduced use of external consultants generated a further £319k reduction in cost. We increased investment in staff training by £154k.

Income in 2013/14 totalled £17,493 and was £710k higher than recorded the previous year. Last year fee income was reduced by £1,036k of fee rebate. When offset with the positive impact of fee reductions made for the 2012/13 audit year this resulted in a year-on-year increase in fee income of £758k.

Miscellaneous income earned from staff on secondment to other organisations and from supporting United Nations audit work was £121k higher than in the previous year. This partly offset a £158k reduction in other finance income (IAS19 pension returns) - the result of increased interest costs on pension liabilities.

### **Comparison with budget**

Net operating costs were £734k less than budget. The agreement of our outstanding VAT registration liability at levels below the sums provided in previous years contributed £152k to the underspend. Staff costs, inclusive of agency costs and net of secondment income, were £314k lower than budget.

Fee income net of sums paid to appointed firms was £231k greater than budget mainly as a result of both an increase in agreed fees compared with budget and lower levels of expenses paid to appointed firms.

Further savings were recorded in ICT expenditure, £94k, and in the use of external consultants, £167k. An expenditure contingency of £250k was not used during the year.

Investment in staff training and development totalled £527k (£154 more than in the previous year) and was £106k more than budget. Recruitment costs were £48k more than budget. A provision of £350k was made to meet the costs of five staff who have accepted voluntary early retirement and severance - as a result annual savings of £233k will accrue from April 2015.

# Reports published in 2013/14

## Annual audits

- Scottish Parliament
- 75 Central government
- 23 NHS
- 32 Further education
- 77 Local government

## Performance reports

- Modern apprenticeships
- Reshaping care for older people
- Management of patients on NHS waiting lists - audit update
- Scotland's public sector workforce
- Police reform
- NHS financial performance 2012/13
- Renewable energy
- Scotland's colleges
- Housing in Scotland
- Developing financial reporting in Scotland
- Scotland's key transport infrastructure projects
- Managing early departures from the Scottish public sector
- Maintaining Scotland's roads
- Overview of local government in Scotland

## Section 22 reports for the Auditor General

- The 2011/12 audit of Adam Smith College

## How councils work series

- How councils work: an improvement series for councillors and officers - Options appraisal: are you getting it right?
- How councils work: an improvement series for councillors and officers - Charging for services: are you getting it right?

## **Controller of Audit reports to the Accounts Commission**

- South Ayrshire Council
- Aberdeenshire Council
- The Moray Council
- The City of Edinburgh Council
- The Highland Council: Caithness Heat and Power: Follow-up statutory report
- Argyll & Bute Council

## **Scrutiny improvement**

- National Scrutiny Plan for local government
- Assurance and improvement plans 2013 - 16 (one for each of the 32 councils)

## **Accounts Commission publications**

- Accounts Commission Strategy
- Accounts Commission Annual Report 2012/13 and Action Plans
- Accounts Commission Equality Outcomes
- Accounts Commission Mainstreaming Equalities
- Statutory Performance Indicators Direction 2013

## **Audit Scotland publications**

- Audit Scotland Annual Review 2012/13
- Audit Scotland Annual Report and accounts 2012/13
- 2012/13 Transparency and Quality report
- 2012/13 report on working with other countries
- Scrutiny Board - Annual Report 2012/13
- Audit Scotland Equality Outcomes
- Audit Scotland Mainstreaming Equalities
- Audit Scotland corporate plan 2012-15 - Priorities for 2014



# Remuneration report

## Remuneration and human resources committee

The membership and remit of the committee are set out in Standing Orders as follows:

‘The remuneration and human resources committee will consist of a member or members of the board who are not employees of Audit Scotland. The board may appoint persons who are not members of the board to be members of or advisers to the remuneration and human resources committee, and may pay them such remuneration and expenses as the board decided.’

In relation to members of Audit Scotland’s Management Team, the responsibilities of the committee are to:

- review and approve all terms and conditions of employment, including job descriptions, all pay and benefit reward elements associated with each post
- ensure remuneration policy and strategy is aligned to the relevant public sector policies being implemented by the UK and Scottish Governments
- set and review the overall reward structure, including the value of pay ranges and general annual pay award strategy
- assure itself that effective arrangements are followed for performance assessments in respect of Audit Scotland’s Management Team, including any changes to pay and benefits arising from the assessment of performance during the review period
- review talent management and succession planning arrangements
- approve remuneration packages for newly appointed members of the Management Team
- recommend appointments and changes affecting Management Team to the board
- decide on applications for early retirement and determine compensation payments for loss of office
- agree, oversee and review the operation of expenses policy and review the expense claims of the Accountable Officer on an annual basis.

In relation to other staff employed by Audit Scotland, responsibilities are to:

- determine the remuneration policy governing all terms and conditions of employment, including pay, benefits, retirement policy and other policies relating to compensation for loss of office
- ensure remuneration policy and strategy is aligned to the relevant public sector policies being implemented by the UK and Scottish Governments
- approve the parameters for the annual pay award cycle
- review, not less than annually, the application of remuneration policy
- assure itself about any issues relating to the overall performance of employees.

Although the salary and pension contributions of the Auditor General for Scotland are paid by Audit Scotland, they are set by the Scottish Parliamentary Corporate Body.

The members of the remuneration and human resources committee during the year were:

- Chair – Katharine Bryan
- Member – John Baillie (until 30 November, 2013)
- Member – Douglas Sinclair (from 1 December, 2013)
- Member – John Maclean
- Member – Caroline Gardner.

In setting salary levels, the committee has regard to:

- the need to recruit, retain and motivate suitably able and qualified people to exercise their different responsibilities
- the performance of individual managers
- regional/local variations in labour markets and their effects on recruitment and retention
- government policies for improving public services including the requirement to meet the output targets for the delivery of services and other relevant Government policies and targets
- the funds available subject to any expenditure limits.

The information on pages 27 to 29 is covered by the audit opinion.

## Audit Scotland Board

Under the provisions of schedule 2 of the Public Finance and Accountability (Scotland) 2000 Act the Auditor General, the Chair of the Accounts Commission and any employee of Audit Scotland or member of the Accounts Commission are not entitled to any remuneration in respect of their membership of the Audit Scotland Board.

The Audit Scotland Board has three independent members including the chair of the board. The annual remuneration for independent members of the board is set by the Scottish Commission for Public Audit (SCPA). All independent board member appointments are part-time and non-pensionable. Independent board member remuneration was as follows:

	Remuneration banding	
	2013/14 £000	2012/13 £000
Chair – Ronnie Cleland	10 - 15	10 - 15
Independent board members	5 - 10	5 - 10

## Senior Management

The salaries (excluding employer's superannuation and national insurance contributions), benefits in kind and pension entitlements of the Management Team are shown in the following tables. Information is presented for the whole year to 31 March 2014. Further information on the pensions payable to Audit Scotland staff, including senior management, can be found in note 3 to Audit Scotland's Annual Accounts (page 45).

Single total remuneration		2013/14	2012/13	2013/14	2012/13	2013/14	2012/13	2013/14	2012/13
		Salary	Salary	Benefit in kind	Benefit in kind	Pension benefit	Pension benefit	Total	Total
Note		£000	£000	£	£	£000	£000	£000	£000
<b>Caroline Gardner</b>	(iii)	135 - 140	100 - 105	-	-	55	42	190 - 195	145 - 150
Auditor General for Scotland from 1 July 2012									
<b>Russell Frith</b>		110 - 115	110 - 115	-	-	9	15	120 - 125	125 - 130
Assistant Auditor General									
<b>Diane McGiffen</b>		105 - 110	105 - 110	-	1,200	17	11	126 - 130	115 - 120
Chief Operating Officer									
<b>Lynn Bradley</b>		90 - 95	90 - 95	2,500	2,800	3	7	90 - 95	90 - 95
Director of Corporate Programmes & Performance									
<b>Barbara Hurst</b>	(iv)	25 - 30	90 - 95	-	-	10	15	35 - 40	105 - 110
Director of Performance Audit									
<b>Fiona Kordiak</b>		90 - 95	90 - 95	5,300	4,700	2	7	95 - 100	105 - 110
Director of Audit Services									
<b>Fraser McKinlay</b>		100 - 105	90 - 95	-	-	19	24	120 - 125	115 - 120
Director of Performance Audit and Best Value, and Controller of Audit									

The highest paid member of senior management was the Auditor General for Scotland. Her annualised remuneration before pension benefits was 3.4 times the £41,664 median remuneration paid to Audit Scotland's staff in 2013/14 (2012/13 – 3.4 X £41,050).

**Pensions**

		Accrued	Accrued	Real	Real	CETV at	CETV at	Real
		Accrued	lump sum	increase	increase	31 March	31 March	increase
		pension at	at 31	in annual	in lump	2014	2013	in CETV
		31 March	March	pension	sum	note (v)	note (v)	note (v)
		2014	2014					
		£000	£000	£000	£000	£000	£000	£000
	<i>Note</i>							
<b>Caroline Gardner</b>	<i>(iii)</i>	65 - 70	NIL	2.5 - 5.0	NIL	796	28	-12
Auditor General for Scotland - from 1 July 2012								
<b>Russell Frith</b>		25 - 30	80 - 85	0 - 2.5	0 - 2.5	540	499	6
Assistant Auditor General								
<b>Diane McGiffen</b>		30 - 35	65 - 70	0 - 2.5	0 - 2.5	514	472	5
Chief Operating Officer								
<b>Lynn Bradley</b>		30 - 35	70 - 75	0 - 2.5	0 - 2.5	524	492	-4
Director of Corporate Programmes & Performance								
<b>Fiona Kordiak</b>		30 - 35	70 - 75	0 - 2.5	0 - 2.5	520	488	-4
Director of Audit Services								
<b>Fraser Mckinlay</b>		10 - 15	10 - 15	0 - 2.5	0 - 2.5	127	109	3
Director of Performance Audit and Best Value, and Controller of Audit								

Notes:

(i) The estimated value of benefits in kind relates to the provision of vehicles. Values to the nearest £100.

(ii) The value of pension benefits accrued during the year is calculated as the real increase in pensions and applying the HMRC methodology multiplier of 20 plus the real increase in any lump sum. The real increases exclude increases due to inflation and are net of contributions made by the individual.

(iii) Caroline Gardner was appointed Auditor General for Scotland from 1 July 2012. As Auditor General for Scotland her pension benefits are provided through access to the Principal Civil Service Pension Scheme. No lump sum is payable. The accrued pension and CETV at 31 March 2014 include benefits earned in a previous employment and transferred to the Principal Civil Service Pension Scheme during 2013/14.

(iv) Barbara Hurst left Audit Scotland in July 2013 under the terms of our Voluntary Early Release Arrangements. A payment of £60k was made to Lothian Pension Fund to secure early access to pension benefits. No cash compensation was paid.

(v) A CETV is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the scheme including any benefit transferred from another scheme and not just their service in a senior capacity to which the disclosure applies. The real increase in CETV reflects the increase in CETV effectively funded by the employer. It does not include the increase in accrued pension benefits due to inflation, contributions paid by the employee and uses common market valuation factors for the start and end of the period.

## Service contracts

Senior managers hold appointments which are open-ended until they retire. Early termination, other than through misconduct, would result in the individual receiving compensation.

The Auditor General for Scotland is not an employee of Audit Scotland but is a Crown appointment following nomination by Parliament. Her appointment is for a fixed term of eight years from 1 July 2012. Salary is determined by the Scottish Parliamentary Corporate Body.

## Accounts Commission for Scotland

Members of the Accounts Commission are appointed by Scottish ministers who also set their remuneration. Commission members are not employed by Audit Scotland and detail of their remuneration is not required under the policy outlined in the Financial Reporting Manual. The following details are included for information and to assist the reader of the report.

The average number of members of the Commission throughout the period was 12 (2012/13 – 12) and their remuneration was as follows:

	Remuneration banding	
	2013/14 £000	2012/13 £000
Chair – John Baillie (until 30 November 2013)	25 - 30	40 - 45
Chair – Douglas Sinclair (from 1 December 2013)	10 - 15	-
Depute Chair – Douglas Sinclair (until 30 November 2013)	5 - 10	10 - 15
Commission members	5 - 10	5 - 10

Note: All Commission appointments are part-time and non-pensionable.

**C Gardner**  
**Auditor General and Accountable Officer**  
 10 June 2014

# Foreword to the accounts

## Statutory background

Audit Scotland was formed on 1 February 2000 (and commenced operations on 1 April 2000), following the transfer of staff and property from the Accounts Commission and National Audit Office, under the Public Finance and Accountability (Scotland) Act 2000. Part 2 of the Public Finance and Accountability (Scotland) Act 2000 established Audit Scotland as a body corporate.

## Basis of accounts

These are the accounts of Audit Scotland for the year ended 31 March 2014. The accounts have been prepared in compliance with a direction given by Scottish ministers in accordance with section 19(4) of the Public Finance and Accountability (Scotland) Act 2000.

## Sources of funding

Audit Scotland may, under Part 2 of the Public Finance and Accountability (Scotland) Act 2000, make reasonable charges to audited bodies in respect of the exercise of its functions. Audit Scotland must seek to ensure that, taking one year with another, its charges for certain types of work are broadly equivalent to its expenditure. Any expenditure not met from charges is payable out of the Scottish Consolidated Fund.

## Post balance sheet events

There were no important events occurring after the year-end which fall under the definition of a post balance sheet event.

## Pensions and early departure costs

Details of the organisation's pension and early retirement costs are included in the notes to these accounts.

## Board and Management

Details of the board and Management Team are in the Management Commentary and the Remuneration Report.

## Staff relations and equal opportunities

Audit Scotland is committed to ensuring that recruitment and management of employees is carried out on merit on the basis of equal opportunity for all. Full and fair consideration is given to applications for employment from disabled persons where they have the skills and abilities to perform the job. Audit Scotland has a single equality scheme.

Audit Scotland recognises the importance of good industrial relations and effective communication with its entire staff. Regular meetings are held with staff representatives to discuss matters of mutual interest.

### **Payment to suppliers**

In line with the CBI Prompt Payment Code Audit Scotland has a policy to pay all invoices not in dispute in 30 days or the agreed contractual terms if otherwise specified: 98% (99% - 2013) of all invoices for the year were paid on or before the due date.

We also monitor our performance against the Scottish Government's target of payment of trade invoices within ten days. In 2013/14, 86% (2013 - 92%) of trade invoices were paid within ten days.

### **Auditors**

Accounts prepared by Audit Scotland must, under section 19 of the Public Finance and Accountability (Scotland) Act 2000, be sent to the Scottish Commission for Public Audit (SCPA) for auditing. The SCPA appointed Alexander Sloan Chartered Accountants, as auditors to Audit Scotland for a three-year period commencing March 2011. In December 2013 the SCPA agreed to extend the appointment of Alexander Sloan Chartered Accountants as Auditors to Audit Scotland by one year.

So far as I am aware, there is no relevant audit information of which Audit Scotland's auditors are unaware, and I have taken all the steps that I ought to have taken to make myself aware of any relevant audit information and to establish that Audit Scotland's auditors are aware of that information.

**C Gardner**  
**Auditor General and Accountable Officer**  
10 June 2014

# Statement of Accountable Officer's responsibilities

Under section 19(4) of the Public Finance and Accountability (Scotland) Act 2000, Audit Scotland is required to prepare resource accounts for each financial year, in conformity with the direction of the Scottish ministers, detailing the resources acquired, held, or disposed of during the year and the use of resources by Audit Scotland during the year.

The resource accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of Audit Scotland, the net resource outturn, comprehensive net expenditure, cash flows and movement in taxpayers' equity for the financial year.

The Scottish Commission for Public Audit has appointed the Auditor General for Scotland as Accountable Officer for Audit Scotland, with responsibility for preparing the accounts of Audit Scotland and for submitting them for audit to the Scottish Commission for Public Audit.

In preparing the accounts, the Accountable Officer is required to comply with the Financial Reporting Manual (FReM) and in particular to:

- observe the accounts direction including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis
- make judgements and estimates on a reasonable basis
- state whether applicable accounting standards, as set out in the FReM, have been followed; and disclose and explain any material departures in the accounts
- prepare accounts on a going concern basis.

The responsibilities of the Accountable Officer, including responsibility for the propriety and regularity of the public finances for which an Accountable Officer is answerable, for keeping proper records and for safeguarding assets, are set out in the *Accountable Officer's Memorandum* which is available at [www.scotland.gov.uk/Resource/Doc/1069/0084581.doc](http://www.scotland.gov.uk/Resource/Doc/1069/0084581.doc)



# Governance statement

As Accountable Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of Audit Scotland's policies, aims and objectives. I am also responsible for safeguarding the public funds and assets assigned to Audit Scotland, in accordance with the responsibilities set out in the *Accountable Officer's Memorandum*.

## Purpose of the system of internal control

The system of internal control is based on an ongoing process designed to identify the principal risks to the achievement of the organisation's policies, aims and objectives; to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically. This process has been in place for the year ended 31 March 2014 and up to the date of approval of the annual report and accounts.

The system of internal control is designed to manage rather than eliminate the risk of failure to achieve Audit Scotland's policies, aims and objectives. It can therefore only provide reasonable and not absolute assurance of effectiveness.

The processes within the organisation have regard to the guidance to public bodies in Scotland issued by Scottish ministers and set out in the Scottish Public Finance Manual.

## Governance framework

As Accountable Officer, I also have responsibility for reviewing the effectiveness of the systems of internal control. The following processes have been established to inform my review.

The board of Audit Scotland meets regularly to develop and monitor the plans and strategic direction of the organisation. The board which has three independent non-executive members, including the chair, also includes the Auditor General for Scotland and the Chair of the Accounts Commission for Scotland. The board has agreed a framework which sets out the principles of partnership working between the Auditor General for Scotland, the Accounts Commission and Audit Scotland. The board met nine times in 2013/14.

The board has an audit committee which recommends the appointment of our internal auditors and receives our annual accounts and internal audit reports. The audit committee considers the risk management arrangements, receives regular updates on the corporate risk register, and reviews the annual assurances provided by management. The audit committee undertakes an annual review of our principal governance policies (Standing Orders, Financial Regulations and Scheme of Delegation). The audit committee also considered annual assurance reports on Health and Safety, Information Risk and Security, Transparency and Quality, Risk Management, Hospitality and Gifts, Whistleblowing, and Bribery and Fraud. In 2013/14, a review of the Corporate Risk Management Policy and Strategy was undertaken. During the year the audit committee was strengthened through the appointment of a co-opted member. This appointment will ensure continuity of the committee's work during a period of

change of members on the Audit Scotland Board. The audit committee, which is chaired by a non-executive board member, met four times in 2013/14. The chair of the audit committee submits an annual Statement of Assurance to the board.

The board also has a remuneration and human resources committee which sets and reviews the salaries and the main terms and conditions for all staff. The committee which is chaired by a non-executive board member met four times in 2013/14.

Audit Scotland has a Management Team which normally meets on a weekly basis. The Management Team comprises the Auditor General for Scotland as Accountable Officer of Audit Scotland and five executive directors of the organisation. It considers regular reports from the managers within the organisation on progress towards meeting the organisations' performance objectives.

Audit Scotland has a risk strategy and policy which sets out the approach to risk management in the organisation. The corporate risk register, which identifies the key risks facing the organisation, the likelihood and impact of the risk crystallising, the controls in place, the way in which the risk is monitored and any actions to further reduce the risk, is regularly reviewed by the Management Team and by the audit committee. Information risk is covered by the normal risk management arrangements and monitored by the Knowledge, Information and Technology Governance Group. In addition, Audit Scotland is committed to information management and security and improving our arrangements for data sharing.

The system of internal financial control is based on a framework of regular management information, administrative procedures and a system of delegation and accountability. In particular it includes:

- detailed budgeting processes with an annual budget approved by the board
- regular reviews by the board and the Management Team of financial reports covering progress towards financial targets
- annual reviews and updates to standing orders, scheme of delegation and financial regulations
- quarterly reviews of the corporate risk register.

### Review of effectiveness of internal control and risk management

As Accountable Officer, I have responsibility for reviewing the effectiveness of the system of internal control and risk management arrangements. My review is informed by:

- an assurance framework established in accordance with the Scottish Public Finance Manual that provides certificates of assurance from executive directors and senior managers who are responsible for developing, implementing and maintaining internal controls across their delegated areas
- the work of the internal auditors which is directed through an audit plan agreed by the audit committee and focuses on identified control risk areas. The internal auditors submit regular reports on the adequacy and effectiveness of the organisation's systems of internal control together with recommendations for improvement

- quarterly reviews by the audit committee of the organisation's corporate risk register and the work of internal audit in assessing the effectiveness of risk management arrangements
- comments made by the external auditors in their management letters and other reports.

During the financial year to 31 March 2014 and to the date of this statement, no significant control weaknesses or issues have arisen, and no significant failures have arisen in the expected standards for good governance, risk management and control.

## Information security

Audit Scotland has privileged and wide-ranging access to data and information to support the discharge of the audit function and ensure that reports to Parliament are factual, accurate and complete. Audit Scotland has a duty to respect this privileged access and to ensure that the personal information entrusted to it is safeguarded properly.

In order to reinforce the importance of this, training on data security is included in the induction process for all staff and during 2013/14, staff were required to complete 'Protecting Information' refresher training. Also this year Audit Scotland produced and distributed to staff:

- a guide to sending information securely
- a data protection update
- data protection and information security reminders to staff dealing with client information.

There have been no incidents of personal data loss which required to be notified to the Information Commissioner.

## Significant issues

I am able to report that there were no significant weaknesses in Audit Scotland's system of internal controls in 2013/14 which affected the achievement of Audit Scotland's key policies, aims and objectives.

**C Gardner**  
**Auditor General and Accountable Officer**  
10 June 2014

# Summary of Resource Outturn

Year ended 31 March 2014

	Note	2014 £000	Restated 2013 £000
Net Operating (Cost) - actual		<u>(6,648)</u>	<u>(7,182)</u>
Estimate - year to 31 March 2014		<u>(7,382)</u>	
Net Cash Requirement <i>(see Cash flow statement )</i>		<u>7,326</u>	<u>8,453</u>

# Statement of Comprehensive Net Expenditure

Year ended 31 March 2014

	Note	2014 £000	Restated 2013 £000
<b>Administration costs</b>			
People costs	2	(14,755)	(14,131)
Other administration costs	4	(9,378)	(9,823)
<b>Gross administration costs</b>		<b>(24,133)</b>	<b>(23,954)</b>
Operating income	5	18,206	17,338
Other finance income	6	(713)	(555)
<b>NET (EXPENDITURE)</b>		<b>(6,640)</b>	<b>(7,171)</b>
Corporation Tax (payable)		(8)	(11)
<b>NET OPERATING (COST) and TOTAL COMPREHENSIVE NET (EXPENDITURE)</b>		<b>(6,648)</b>	<b>(7,182)</b>

# Balance sheet

As at 31 March 2014

	Note	2014 £000	2013 £000
<b>Non-current assets</b>			
Property, plant and equipment	7	704	836
Intangible assets	8	70	51
<b>Total non-current assets</b>		<b>774</b>	<b>887</b>
<b>Current assets</b>			
Trade and other receivables	9	2,632	2,196
Cash and cash equivalents	10	1,072	1,199
<b>Total current assets</b>		<b>3,704</b>	<b>3,395</b>
<b>Total assets</b>		<b>4,478</b>	<b>4,282</b>
<b>Current liabilities</b>			
Trade and other payables	12	2,703	3,065
Provision for early retirement	14	564	557
Other provisions	16	251	79
<b>Total current liabilities</b>		<b>3,518</b>	<b>3,701</b>
<b>Non-current assets plus/less net current assets/liabilities</b>		<b>960</b>	<b>581</b>
<b>Non-current liabilities</b>			
Deferred liabilities	13	(52)	(22)
Provision for early retirement	14	(1,796)	(1,912)
Other provisions	16	(279)	(489)
Net funded pension (liability)	3	(17,528)	(13,607)
<b>Total non-current liabilities</b>		<b>(19,655)</b>	<b>(16,030)</b>
<b>ASSETS LESS LIABILITIES</b>		<b>(18,695)</b>	<b>(15,449)</b>
<i>Represented by:</i>			
<b>TAXPAYERS' EQUITY</b>			
Net funded pension (liability)	3	(17,528)	(13,607)
General fund		(1,167)	(1,842)
		<b>(18,695)</b>	<b>(15,449)</b>

**C Gardner**

**Auditor General and Accountable Officer**

10 June 2014

# Cash flow statement

Year ended 31 March 2014

	Note	2014 £000	Restated 2013 £000
<b>Cash flows from operating activities</b>			
Net operating (cost)		(6,648)	(7,182)
<i>Adjustment for non-cash items:</i>			
- Depreciation	7, 8	365	423
- Pension scheme - net revenue debit		1,196	427
(Increase) / Decrease in trade and other receivables		(436)	373
(Decrease) in trade / other payables / deferred liabilities		(350)	(1,016)
(Decrease) / Increase in provisions for early retirement		(109)	150
(Decrease) in other provisions		(38)	(7)
Adjustment for cash balance due to the Consolidated Fund	12	(1,072)	(1,199)
<b>Net cash outflow from operating activities</b>		<b>(7,092)</b>	<b>(8,031)</b>
<b>Cash flows from investing activities</b>			
Purchase of property, plant and equipment	7	(212)	(418)
Purchase of intangible assets	8	(40)	(17)
Less movement in accrued expenditure		18	13
		<b>(234)</b>	<b>(422)</b>
<b>Cash flows from financing activities</b>			
Opening cash balance payable to the Consolidated Fund		1,199	1,951
From Consolidated Fund (Supply)		6,000	5,750
		<b>7,199</b>	<b>7,701</b>
<b>Net (decrease) in cash and cash equivalents in the period</b>		<b>(127)</b>	<b>(752)</b>
Cash and cash equivalents at the beginning of period		<b>1,199</b>	<b>1,951</b>
Cash and cash equivalents at the end of period		<b>1,072</b>	<b>1,199</b>
<b>Net cash requirement</b>			
Cash flows from financing activities		7,199	7,701
Decrease in cash		127	752
		<b>7,326</b>	<b>8,453</b>

# Statement of Changes in Taxpayers' Equity

Year ended 31 March 2014

	Note	Net funded pension £000	General fund £000	Total £000
<b>2012/13 restated</b>				
<b>Balance at 1 April 2012</b>		<b>(9,698)</b>	<b>(1,589)</b>	<b>(11,287)</b>
Transfers between reserves				
Transfer to net fund pension liabilities	2	38	(38)	0
Net return on pension assets		(465)	465	0
Actuarial remeasurements (losses)	3	(3,482)	-	(3,482)
Net operating (cost)		-	(7,182)	(7,182)
Net funding from the Scottish Parliament	11	-	6,502	6,502
<b>Balance at 31 March 2013</b>		<b>(13,607)</b>	<b>(1,842)</b>	<b>(15,449)</b>
<b>2013/14</b>				
<b>Balance at 1 April 2013</b>		<b>(13,607)</b>	<b>(1,842)</b>	<b>(15,449)</b>
Transfers between reserves				
Transfer to net fund pension liabilities	2	(571)	571	0
Net return on pension assets		(625)	625	0
Actuarial remeasurements (losses)	3	(2,725)	-	(2,725)
Net operating (cost)		-	(6,648)	(6,648)
Net funding from the Scottish Parliament	11	-	6,127	6,127
<b>Balance at 31 March 2014</b>		<b>(17,528)</b>	<b>(1,167)</b>	<b>(18,695)</b>



# Notes to the accounts

## 1. Statement of accounting policies

The accounts have been prepared in accordance with the accounts direction issued by Scottish ministers under section 19(4) of the Public Finance and Accountability (Scotland) Act 2000 and also in accordance with the Financial Reporting Manual (FReM) applicable for the year. The accounting policies contained in the FReM apply International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector context. Where the FReM permits a choice of accounting policy, the accounting policy which is judged to be most appropriate to the particular circumstances of Audit Scotland for the purpose of giving a true and fair view has been selected. The accounting policies adopted by Audit Scotland are described below. They have been applied consistently in dealing with items considered material in relation to the accounts.

### a) Basis of accounting

The accounts have been prepared under the historical cost convention. In accordance with the principles of resource accounting, the gross funding received from the Scottish Consolidated Fund is recorded directly within the General Fund and is not included in the operating income received in the year in the Statement of Comprehensive Net Expenditure.

In common with similar public bodies, the future financing of Audit Scotland's liabilities will be met by future grants of Supply and the application of future income, both to be approved annually by the Scottish Parliament. The approval of amounts for 2014/15 has already been given and there is no reason to believe that future approvals will not be forthcoming.

Accordingly it is considered appropriate to adopt a going concern basis for the preparation of these financial accounts.

### b) Non-current assets

All property occupied by Audit Scotland is leasehold. The minimum level of capitalisation for a non-current asset is £5,000 for individual or group purchases. Non-current assets are held at fair value. Depreciated historic cost has been used as a proxy for fair value due to the low value and short life of the assets held.

### c) Depreciation

Depreciation has been provided at a rate calculated to write off cost in equal annual instalments over the estimated useful lives of assets.

Asset cost is written off as follows:

Leasehold premises	remaining period of lease (from 2 - 10 years)
Furniture and fittings	5 years
Computer equipment	2- 5 years
Software	2- 5 years

### d) Amortisation of rent-free periods

The benefit of rent-free periods on leases of premises is amortised over the period of the lease or over the period to a lease break point when this is the most probable end of lease, whichever is the shorter.

### e) Operating income

Operating income relates directly to the audit activities of Audit Scotland. It principally comprises fees and charges for services provided on a full cost basis to audited bodies.

### f) Work in progress

Work in progress is valued on the basis of a proportion of the agreed fee earned by the balance sheet date less an allowance for any foreseen losses. This calculation is based on an assessment of the amount of audit work completed by the balance sheet date as a proportion of the total expected amount of audit work. Payments received on account of work in progress in excess of or below the value of carrying out the relevant work are included in creditors or debtors as appropriate.

### g) Operating leases

The total cost of operating leases is charged to revenue in equal instalments over the life of the lease.

Estimates of likely costs in respect of obligations under our property leases for dilapidations, reinstatement and property decorations are charged to revenue in equal instalments over the life of the lease or the period to a planned early termination of the lease whichever is the shorter.

## **h) Value Added Tax (VAT)**

Input tax in respect of external auditor fees and expenses incurred in the delivery of Local Authority audits is reclaimed from HMRC on behalf of the Accounts Commission and is used to offset audit fees payable by Local Authorities. All other input tax is charged to the Statement of Comprehensive Net Expenditure. Audit Scotland is registered for VAT in respect of business activities. During 2013/14 we reached agreement with HMRC in respect of the effective date of this registration at March 2003. As a result of the agreement overpaid VAT has been recovered from HMRC and has generated a net credit of £152k in 2013/14 (£204k charge in 2013).

## **i) Pension arrangements**

Audit Scotland complies with the requirements of IAS 19 for the year ended 31 March 2014. Audit Scotland makes pension provision for present and former employees through two pension schemes. Employees joining Audit Scotland after 1 April 2000 and those transferring to Audit Scotland from the Accounts Commission have benefits provided through the Local Government scheme. Employees transferring to Audit Scotland at 1 April 2000 from the NAO are covered by the provisions of the Principal Civil Service Pension Scheme. The Auditor General for Scotland has benefits provided through the Principal Civil Service Pension Scheme.

## **j) Revised Accounting Standard - IAS 19 (Employee Benefits)**

Revisions to IAS 19 (Employee benefits) came into effect from 1 January 2013 for accounting periods starting after that date. The revised standard has been applied in this year's Annual Report and Accounts. The revised standard restricts the estimated rate of return to be earned on pension assets to a level equivalent to the discount rate used in assessing future pension liabilities. In our accounts, the comparator figures for 2012/13 have been restated to reflect this change. The impact of the change reduced expected return on pension assets by £529k - see note 6 to the accounts.

## 2. People costs and numbers

People costs comprise:

	<b>2014</b>	<b>2013</b>
	£000	£000
<b>Administrative staff</b>		
Salaries	10,931	10,681
National Insurance	964	953
Superannuation	1,888	1,879
Pensions in payment (see note 3c)	23	83
Provision for early retirement and severance costs (see note 14)	350	313
Movement in early retirement costs	(105)	113
Adjustment for retirement benefit scheme costs (see below)	571	(38)
	<b>14,622</b>	<b>13,984</b>
<b>Accounts Commission members</b>		
Salaries	112	117
National Insurance	9	14
Travel and subsistence	12	16
	<b>133</b>	<b>147</b>
	<b>14,755</b>	<b>14,131</b>

The average number of directly employed whole time equivalent (w.t.e.) staff during the period was 262 (2013 – 260). The average number (w.t.e.) for agency and seconded staff used during the year was nine (2013 – 8).

### Analysis of local government retirement benefit scheme costs:

	<b>2014</b>	<b>2013</b>
	£000	£000
Current service costs	3,010	2,303
Past service costs	94	73
	<b>3,104</b>	<b>2,376</b>
Less: Employees' contributions	(731)	(709)
<b>Charge to revenue</b>	<b>2,373</b>	<b>1,667</b>
Employer contributions	(1,802)	(1,705)
Adjustment for retirement benefit scheme costs	<b>571</b>	<b>(38)</b>

### 3. Pension assets and liabilities

In accordance with International Accounting Standard No 19 (IAS 19), Audit Scotland is required to disclose certain information concerning assets, liabilities, income and expenditure related to pension schemes for its employees. Audit Scotland operates two main pension schemes: the Local Government Scheme, administered by the Lothian Pension Fund, and the Principal Civil Service Pension Scheme (PCSPS). Audit Scotland is not required to record information related to the PCSPS as the scheme does not identify assets and liabilities by employer. In addition, until June 2012, Audit Scotland operated a 'by analogy' scheme for the previous Auditor General for Scotland.

#### a) Local government scheme

Audit Scotland has an agreement with The City of Edinburgh Council under which all staff are eligible to enter the Lothian Pension Fund (the name of the Local Government Superannuation Scheme managed by the council) in accordance with its rules. It is a defined benefit scheme providing pension benefits and life assurance for all permanent staff.

The following valuations have been provided by Hymans Robertson LLP, the independent actuaries to Lothian Pension Fund. The financial and actuarial assumptions used for the purposes of their IAS 19 calculations as at 31 March 2014 were as follows:

	<b>2014</b>	<b>2013</b>
Salary increases	<b>5.10%</b>	5.10%
Pension increases	<b>2.80%</b>	2.80%
Discount rate	<b>4.30%</b>	4.50%
The assumed average life expectancy for a retiral at age 65 are as follows:		
	<b>Male</b>	<b>Female</b>
	years	years
Current pensioners	<b>20.4</b>	22.8
Future pensioners	<b>22.6</b>	25.4

Liabilities are valued on an actuarial basis using the projected unit method, which assesses the future liabilities of the fund discounted to their present value. The valuations at 31 March 2014 have been prepared by Hymans Robertson LLP.

The movement in the funded part of the net pension liability for the year to 31 March 2014 is as follows:

	Period ending 31 March 2014		
	Assets	Obligation	Net (Liability) / Asset
	£000	£000	£000
Fair value of employer assets	61,499	0	61,499
Present value of funded liabilities	0	75,106	(75,106)
<b>Opening position as at 1 April 2013</b>	<b>61,499</b>	<b>75,106</b>	<b>(13,607)</b>
Current service cost	0	2,279	(2,279)
Past service cost	0	94	(94)
<b>Total service cost</b>	<b>0</b>	<b>2,373</b>	<b>(2,373)</b>
Interest income on plan assets	2,794	0	2,794
Interest cost on defined benefit obligation	0	3,419	(3,419)
<b>Total net interest</b>	<b>2,794</b>	<b>3,419</b>	<b>(625)</b>
<b>Total defined benefit cost recognised in Statement of Comprehensive Net Expenditure</b>	<b>2,794</b>	<b>5,792</b>	<b>(2,998)</b>
Employee contributions	725	725	0
Employer contributions	1,802	0	1,802
Benefits Paid	(1,339)	(1,339)	0
<b>Total cashflows</b>	<b>1,188</b>	<b>(614)</b>	<b>1,802</b>
<b>Expected closing position</b>	<b>65,481</b>	<b>80,284</b>	<b>(14,803)</b>
Change in financial assumptions	0	3,669	(3,669)
Other experience changes	0	(30)	30
Return on assets excluding amounts included in net interest	914	0	914
<b>Total remeasurements recognised in Other Comprehensive Income</b>	<b>914</b>	<b>3,639</b>	<b>(2,725)</b>
Fair value of employer assets	66,395	0	66,395
Present value of funded liabilities	0	83,923	(83,923)
<b>Closing position as at 31 March 2014</b>	<b>66,395</b>	<b>83,923</b>	<b>(17,528)</b>

Information in respect of the defined benefit obligation

	Liability split		Duration
	£000	%	Years
Active members	52,027	62.0%	25.3
Deferred members	9,705	11.6%	23.3
Pensioner members	22,191	26.4%	12.2
<b>Total</b>	<b>83,923</b>	<b>100.0%</b>	<b>21.6</b>

The increase in net pension liabilities was mainly due to a reduction in the real discount rate used to value pension liabilities. The impact of increased liabilities was partly offset by increased asset values as a result of higher than expected investment returns.

The movement in the funded part of the net pension liability for the year to 31 March 2013 was as follows:

	Period ending 31 March 2013		
	Assets	Obligation	Net (Liability) / Asset
	£000	£000	£000
Fair value of employer assets	52,396	0	52,396
Present value of funded liabilities	0	62,094	(62,094)
<b>Opening position as at 1 April 2012</b>	<b>52,396</b>	<b>62,094</b>	<b>(9,698)</b>
Current service cost	0	1,594	(1,594)
Past service cost	0	73	(73)
<b>Total service cost</b>	<b>0</b>	<b>1,667</b>	<b>(1,667)</b>
Interest income on plan assets	2,535	0	2,535
Interest cost on defined benefit obligation	0	3,000	(3,000)
<b>Total net interest</b>	<b>2,535</b>	<b>3,000</b>	<b>(465)</b>
<b>Total defined benefit cost recognised in Statement of Comprehensive Net Expenditure</b>	<b>2,535</b>	<b>4,667</b>	<b>(2,132)</b>
Employee contributions	708	708	0
Employer contributions	1,705	0	1,705
Benefits Paid	(1,541)	(1,541)	0
<b>Total cashflows</b>	<b>872</b>	<b>(833)</b>	<b>1,705</b>
<b>Expected closing position</b>	<b>55,803</b>	<b>65,928</b>	<b>(10,125)</b>
Change in financial assumptions	0	9,260	(9,260)
Other experience changes	0	(82)	82
Return on assets excluding amounts included in net interest	5,696	0	5,696
<b>Total remeasurements recognised in Other Comprehensive Income</b>	<b>5,696</b>	<b>9,178</b>	<b>(3,482)</b>
Fair value of employer assets	61,499	0	61,499
Present value of funded liabilities	0	75,106	(75,106)
<b>Closing position as at 31 March 2013</b>	<b>61,499</b>	<b>75,106</b>	<b>(13,607)</b>

Assets are valued at fair value, principally market value for investments, and consist of:

Asset Category	At 31 March 2014				At 31 March 2013			
	Quoted Prices in Active Markets £000	Prices not quoted in Active Markets £000	Total £000	%	Quoted Prices in Active Markets £000	Prices not quoted in Active Markets £000	Total £000	%
<b>Equity Securities:</b>								
Consumer	10,061.5	0.0	10,061.5	15%	7,881.2	0.0	7,881.2	13%
Manufacturing	9,063.1	0.0	9,063.1	14%	7,587.1	0.0	7,587.1	12%
Energy and Utilities	7,388.1	0.0	7,388.1	11%	4,444.0	0.0	4,444.0	7%
Financial Institutions	4,624.8	0.0	4,624.8	7%	6,695.2	0.0	6,695.2	11%
Health and Care	4,529.8	0.0	4,529.8	7%	3,226.5	0.0	3,226.5	5%
Information Technology	4,319.2	0.0	4,319.2	7%	3,762.8	0.0	3,762.8	6%
Other	2,933.7	0.0	2,933.7	5%	1,846.1	0.0	1,846.1	3%
<b>Debt Securities:</b>								
Corporate Bonds (investment grade)	2,146.4	0.0	2,146.4	3%	2,365.6	0.0	2,365.6	4%
Corporate Bonds (non-investment grade)	322.8	0.0	322.8	0%	202.2	0.0	202.2	0%
UK Government	2,259.5	0.0	2,259.5	3%	2,336.5	0.0	2,336.5	4%
Other	56.7	0.0	56.7	0%	60.4	0.0	60.4	0%
<b>Private Equity:</b>								
All	541.1	7,513.2	8,054.3	12%	0.0	7,070.2	7,070.2	11%
<b>Real Estate:</b>								
UK Property	0.0	4,625.9	4,625.9	7%	0.0	4,247.7	4,247.7	7%
Overseas Property	0.0	537.9	537.9	1%	0.0	582.6	582.6	1%
<b>Investment funds and Unit trusts:</b>								
Equities	688.9	246.7	935.6	2%	4,131.1	1,246.6	5,377.7	9%
Bonds	0.0	283.6	283.6	0%	0.0	309.5	309.5	1%
Commodities	0.0	225.6	225.6	0%	0.0	390.3	390.3	1%
Other	0.0	215.8	215.8	0%	0.0	202.0	202.0	0%
<b>Derivatives:</b>								
Other	7.0	0.0	7.0	0%	6.7	0.0	6.7	0%
<b>Cash and cash equivalents:</b>								
All	3,803.7	0.0	3,803.7	6%	2,904.6	0.0	2,904.6	5%
<b>TOTALS</b>	<b>52,746</b>	<b>13,649</b>	<b>66,395</b>	<b>100%</b>	<b>47,450.0</b>	<b>14,048.9</b>	<b>61,499</b>	<b>100%</b>



The sensitivities regarding the principal assumption used to measure the funded scheme liabilities are set out below:

<b>Sensitivity analysis at March 2014</b>	<b>Approx.% increase to employer obligation</b>	<b>Approx. monetary amount £000</b>
0.5% decrease in real discount rate	12%	9,943
1 year increase in member life expectancy	3%	2,518
0.5% increase in salary increase rate	4%	3,633
0.5% increase in pension increase rate	7%	6,074

During the year ended 31 March 2014, Audit Scotland's contribution to the pension fund represented 14.4% (2013 – 14.4%) of contributing employees' pensionable pay. In addition a lump sum payment of £343k (2013 – £343k) was paid to meet past service cost deficits. Under Superannuation Regulations, contribution rates are set to meet 100% of the overall liabilities of the fund. In their valuation, as of December 2011, Hymans Robertson LLP recommended employers' contributions be set at 14.4% of pensionable pay plus an annual lump sum payment of £343k to meet past service cost deficits for 2012/13 to 2014/15. Hymans Robertson estimate that employer contributions in 2014/15 will be approximately £1,786k.

## **b) PCSP scheme**

Employees of the NAO transferring to Audit Scotland on 1 April 2000 and the Auditor General for Scotland from 1 July 2012, have pension benefits provided through the Principal Civil Service Pension Scheme (PCSPS). Audit Scotland makes payments of superannuation contributions to PCSPS at rates set by the Government Actuary.

The PCSPS is an unfunded multi-employer defined benefit scheme; however, Audit Scotland is unable to identify its share of the underlying assets and liabilities. The last full actuarial valuation was carried out at 31 March 2007.

Total liabilities at 31 March 2007 were estimated at £128.8 billion. Further details may be found at <http://www.civilservice.gov.uk/pensions/governance-and-rules>

During the year ended 31 March 2014, Audit Scotland paid an employer's contribution of £177k (2013 – £212k) into the PCSPS at rates between 18.8% and 24.3% of pensionable pay (2013 – 18.8% to 24.3%). Audit Scotland has been informed that contributions in 2014/15 will remain at the rates paid in 2013/14. Employer contribution rates are reviewed every three years following a scheme valuation by the Government Actuary. The contribution rates reflect benefits as they are accrued, not when costs are actually incurred, and they reflect past experience of the scheme.

### c) By analogy scheme

R W Black retired as Auditor General for Scotland, on 30 June 2012. Until that time his pension benefits were provided by analogy to the Local Government pension scheme. In 2013/14, pension payments of £23k were made (2013 - £83k including a lump sum).

### d) Early departure costs

Certain costs arising from the early retirement of staff are payable by Audit Scotland. These relate to the early payment of pensions which employers must make to the pension fund and severance costs.

## 4. Other administration costs

	£000	2014 £000	2013 £000
<b>Fees and expenses to appointed audit firms:</b>			
Local authorities	2,600		2,530
National Health Service bodies in Scotland	1,199		1,131
Further education colleges	575		503
Scottish Government and sponsored bodies	819		872
	—————	<b>5,193</b>	<b>5,036</b>
<b>Other Costs:</b>			
Rent and rates	747		678
Other accommodation costs	513		597
Travel and subsistence	889		894
Legal and other professional fees	441		760
Stationery and printing	179		181
Training	527		373
Staff recruitment	148		165
Communications (telephone, postage)	61		51
Insurance	75		79
Information technology	277		293
Internal Audit	27		26
External Audit - financial accounts	25		29
Other	(89)		238
Non-cash items: Depreciation - tangible assets (see note 7)	344		352
Depreciation - intangible assets (see note 8)	21		71
	—————	<b>4,185</b>	<b>4,787</b>
		<b>9,378</b>	<b>9,823</b>

Rent and rates includes £542k in respect of property leases (2012/13 – £482k) - see note 15.

Other includes a credit of £152k (2012/13 – £204k charge) in respect of refunds received for VAT charged to previous accounting periods.

## 5. Operating income

	<b>2014</b>	<b>2013</b>
	£000	£000
Fees and charges payable:		
- by Local authorities	11,665	11,419
- by National Health Service bodies in Scotland	3,750	3,506
- by Further education colleges	629	538
- by Scottish Government and sponsored bodies	1,957	1,780
	<b>18,001</b>	<b>17,243</b>
Bank interest	41	52
Miscellaneous income	164	43
	<b>18,206</b>	<b>17,338</b>

## 6. Other finance income

	<b>2014</b>	<b>Restated</b>
	£000	2013
		£000
Interest income on pension scheme assets	2,794	2,535
Interest cost on pension scheme defined obligations	(3,507)	(3,090)
	<b>(713)</b>	<b>(555)</b>

## 7. Property plant and equipment

	Leasehold premises	Furniture and fittings	Computer equipment	Total
<b>Cost</b>	£000	£000	£000	£000
At 1 April 2013	1,815	147	1,306	<b>3,268</b>
Additions	4	-	208	<b>212</b>
<b>At 31 March 2014</b>	<b>1,819</b>	<b>147</b>	<b>1,514</b>	<b>3,480</b>
<b>Depreciation</b>				
At 1 April 2013	1,185	116	1,131	<b>2,432</b>
Charge for the year (note 4)	255	8	81	<b>344</b>
<b>At 31 March 2014</b>	<b>1,440</b>	<b>124</b>	<b>1,212</b>	<b>2,776</b>
<b>Net Book Value</b>				
<b>At 31 March 2014</b>	<b>379</b>	<b>23</b>	<b>302</b>	<b>704</b>
<b>Analysis of asset financing</b>				
Owned	<b>379</b>	<b>23</b>	<b>302</b>	<b>704</b>
<b>Prior year</b>				
<b>Cost</b>	£000	£000	£000	£000
At 1 April 2012	1,546	121	1,330	<b>2,997</b>
Additions	269	26	123	<b>418</b>
Disposals	-	-	(147)	<b>(147)</b>
<b>At 31 March 2013</b>	<b>1,815</b>	<b>147</b>	<b>1,306</b>	<b>3,268</b>
<b>Depreciation</b>				
At 1 April 2012	957	100	1,170	<b>2,227</b>
Charge for the year (note 4)	228	16	108	<b>352</b>
Depreciation on disposals	-	-	(147)	<b>(147)</b>
<b>At 31 March 2013</b>	<b>1,185</b>	<b>116</b>	<b>1,131</b>	<b>2,432</b>
<b>Net Book Value</b>				
<b>At 31 March 2013</b>	<b>630</b>	<b>31</b>	<b>175</b>	<b>836</b>
<b>Analysis of asset financing</b>				
Owned	<b>630</b>	<b>31</b>	<b>175</b>	<b>836</b>

Non-current assets are held at fair value. Depreciated historic cost has been used as a proxy for fair value due to the low value and short life of the assets held.

## 8. Intangible assets

	<b>Software</b>	
	<b>2014</b>	<b>2013</b>
<b>Cost</b>	£000	£000
At 1 April	680	696
Additions	40	17
Disposals	-	(33)
<b>At 31 March</b>	<b>720</b>	<b>680</b>
<b>Depreciation</b>		
At 1 April	629	591
Charge for the year ( <i>note 4</i> )	21	71
Disposals	-	(33)
<b>At 31 March</b>	<b>650</b>	<b>629</b>
<b>Net Book Value</b>		
<b>At 31 March</b>	<b>70</b>	<b>51</b>

## 9. Trade and other receivables

	£000	<b>2014</b>	<b>2013</b>
		£000	£000
Amounts falling due within one year:			
Trade receivables:			
- Central Government bodies	37		-
- Local authorities	13		33
- NHS bodies in Scotland	1		-
- Bodies external to government	40		6
	<u>40</u>	91	39
Work in progress in advance of billing		1,842	1,615
VAT		200	-
Prepayments		499	542
		<b>2,632</b>	<b>2,196</b>

There are no trade and other receivables due after one year.

## 10. Cash and cash equivalents

	2014 £000	2013 £000
Balance at 1 April	1,199	1,951
Net change in cash and cash equivalents	(127)	(752)
<b>Balance at 31 March</b>	<b>1,072</b>	<b>1,199</b>
The following balances at 31 March were held at:		
Commercial banks	<b>1,072</b>	<b>1,199</b>

## 11. Net funding from the Scottish Government

	2014 £000	2013 £000
Opening cash balance payable to the Consolidated Fund	1,199	1,951
Funding received from the Consolidated Fund	6,000	5,750
Closing cash balance payable to the Consolidated fund	(1,072)	(1,199)
<b>Net funding from the Scottish Parliament</b>	<b>6,127</b>	<b>6,502</b>

## 12. Trade payables and other current liabilities

	£000	2014 £000	2013 £000
Amounts falling due within one year:			
Trade payables:			
- Central Government	-		5
- Local authorities	-		59
- NHS bodies in Scotland	-		4
- Bodies external to government	236		205
	<u>236</u>	236	273
- Cash balance payable to Consolidated Fund		1,072	1,199
- Deferred income		445	420
- VAT		-	111
- Corporation Tax		8	19
- Accruals		276	404
- Staff benefits - untaken holidays		632	603
- Rent free period on premises – current liability (note 13)		34	36
		<b>2,703</b>	<b>3,065</b>

The cash balance payable to the Scottish Consolidated Fund is based on accounting conventions adopted for resource based accounting.

### 13. Deferred liabilities

Audit Scotland rents premises in various locations in accordance with its operational requirements. During the years ended 31 March 2003, 31 March 2012 and 31 March 2013 various leases were negotiated with rent-free periods.

	2014	2013
	£000	£000
<b>Opening balance at 1 April</b>		
Current	36	9
Deferred	22	19
	<b>58</b>	<b>28</b>
Additions	64	50
Released during year	(36)	(20)
	<b>86</b>	<b>58</b>
<b>Closing balance at 31 March</b>		
Whereof:		
Current	34	36
Deferred	52	22
	<b>86</b>	<b>58</b>

### 14. Provision for early retirement and severance

The provision represents the actuarially computed liabilities for early retirement added years, pension strain (early payment of pension) and severance liabilities. The movement during the year was as follows:

	2014	2013
	£000	£000
<b>Opening balance at 1 April</b>	<b>2,469</b>	<b>2,319</b>
Additions	350	313
Utilised in year	(437)	(364)
Revaluation	(22)	201
	<b>2,360</b>	<b>2,469</b>
<b>Closing balance at 31 March</b>		
Payable within 1 year	564	557
Payable after 1 year	1,796	1,912
	<b>2,360</b>	<b>2,469</b>
Discount rate used	4.3%	4.5%

## Early retiral and severance

During January to March 2014, Audit Scotland offered staff access to voluntary early release arrangements as part of a four-year business restructuring programme. The terms of the arrangement offered staff a termination payment and/or early access to pensions. As at 31 March 2014, five staff had indicated a willingness to accept terms to leave Audit Scotland in the period April to December 2014. A further provision of £350k has been made in the accounts for the year ended 31 March 2014 to meet the costs of early departures.

In the year to March 2014, nine staff left Audit Scotland under a voluntary early release arrangement. Under the arrangement staff were entitled to a termination payment and/or early access to pension. The total cost of the arrangements was £302k.

	Number of arrangements	
	2014	2013
< £10,000	3	2
£10,000 - £25,000	3	-
£25,000 - £50,000	1	2
£50,000 - £100,000	2	1
£100,000 - £150,000	-	2
Total number of arrangements	9	7
<b>Total cost (£000)</b>	302	386

## Former Local Government Ombudsmen

Prior to establishment of the Public Services Ombudsman's office, Audit Scotland provided support services including payroll and finance for the Scottish Local Government Ombudsman. The related liabilities were assumed to transfer to the new Ombudsman following the enactment of the Scottish Public Services Ombudsman Act 2002. However, following a review of the implementation of the Act it was determined that the liability for pensions of former Local Government Ombudsmen and their staff did not transfer to the new Ombudsman's office. Since 31 March 2007 Audit Scotland has recognised the pension liability for staff previously employed by the Scottish Local Government Ombudsman. The liability as at 31 March 2014 was £280k (31 March 2013 – £441k).



## 15. Commitments under leases

During the period to 31 March 2014, the amounts charged to revenue in respect of operating leases for premises and vehicles were as follows:

	2014 £000	2013 £000
Premises (note 4)	542	482
Vehicles	473	467
	<b>1,015</b>	<b>949</b>

Obligations under operating leases – total minimum amounts payable for each of the following periods:

	2014 £000	2013 £000
<b>Premises - lease expiry</b>		
Within one year	490	535
Later than one year and not later than five years	426	852
Later than five years	199	254
	<b>1,115</b>	<b>1,641</b>
<b>Vehicles - lease expiry</b>		
Within one year	355	416
Later than one year and not later than five years	405	306
	<b>760</b>	<b>722</b>

In April 2014, Audit Scotland agreed an 11 month extension to the lease for 110 George Street, Edinburgh from 1 February 2015 to 31 December 2015. The amount payable in respect of this extension is £204k. These sums are in addition to those disclosed above.

Audit Scotland has no finance leases.

## 16. Other provisions

Other provisions comprise property dilapidations.

Audit Scotland leases four properties across Scotland. Each lease contains provisions in respect of obligations for property dilapidations, reinstatement and decoration. Estimates of likely costs in respect of obligations under our property leases for dilapidations, reinstatement

and property decorations are charged to revenue in equal instalments over the life of the lease or the period to a planned early termination of the lease, whichever is the shorter.

The movement in the property dilapidations provision during the year was as follows:

	<b>2014</b>	<b>2013</b>
	£000	£000
<b>Opening Balance at 1 April</b>	568	575
Provided in year	40	43
Utilised in year	(78)	(50)
<b>Closing Balance at 31 March</b>	<b>530</b>	<b>568</b>
Payable within 1 year	251	79
Payable after 1 year	279	489
	<b>530</b>	<b>568</b>

## 17. Related party transactions

Audit Scotland is a statutory body funded by the Scottish Parliament. The latter is regarded as a related party. Audit Scotland's income arises principally from audit fees and charges levied on public sector bodies. During the period, none of Audit Scotland's management staff has undertaken any material transactions with related parties.

## 18. Contingent liabilities

At 31 March 2013 Audit Scotland was in discussion with HMRC in respect of its VAT liabilities and a contingent liability of £160k was noted in the accounts in respect of output VAT. Agreement has now been reached with HMRC and all outstanding sums have been paid.

At 31 March 2014 there were no contingent liabilities.

## 19. Capital commitments

At 31 March 2014, there were no contracted capital commitments payable in 2014/15.

## 20. Segmental reporting

Audit Scotland is considered to have just one operating segment and therefore no segmental information is produced.

# Direction by the Scottish ministers

## In accordance with section 19(4) of the Public Finance and Accountability (Scotland) Act 2000

1. The statement of accounts for the financial year ended 31 March 2006 and subsequent years, shall comply with the accounting principles and disclosure requirements of the edition of the Government Financial Reporting Manual (FReM) which is in force for the year for which the statement of accounts are prepared.
2. The accounts shall be prepared so as to give a true and fair view of the net resource outturn, resources applied to objectives, recognised gains and losses and cash flows for the financial year, and of the state of affairs as at the end of the financial year.
3. This direction shall be reproduced as an appendix to the statement of accounts. The direction given on 25 April 2001 is hereby revoked.

**Signed by the authority of the Scottish ministers**

**17 January 2006**

# Independent auditors' report

## To the Scottish Commission for Public Audit

### (Under section 25(3) of The Public Finance Accountability (Scotland) Act 2000)

#### Audit Scotland

We have audited the accounts of Audit Scotland for the year ended 31 March 2014 which comprise the Summary of Resources Outturn, Statement of Comprehensive Net Expenditure, Balance sheet, Cash flow statement, Statement of Changes in Taxpayers' Equity and the related notes 1 to 20. We have also audited the relevant disclosures in the Remuneration Report as required under the direction of the Scottish ministers. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the 2013/14 Government Financial Reporting Manual (the 2013/14 FReM) and directions made by Scottish ministers.

The report is made solely to the Scottish Commission for Public Audit, as a body, in accordance with Section 25 of the Public Finance and Accountability (Scotland) Act 2000. Our audit work has been undertaken so that we might state to the Scottish Commission for Public Audit those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Scottish Commission for Public Audit as a body, for our audit work, for this report, or for the opinions we have formed.

#### **Respective responsibilities of directors and auditor**

As explained more fully in the Statement of Accountable Officer's responsibilities, set out on page 32, the Accountable Officer is responsible for the preparation of the accounts in conformity with the Directions of Scottish ministers and for being satisfied that they give a true and fair view. The Accountable Officer is responsible for the propriety and regularity of the public finances, for keeping proper books and for safeguarding assets, as set out in the *Accountable Officer's Memorandum*.

Our responsibility is to audit and express an opinion on the accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

We report to you on the matters set out in section 22(1)(a) and (b) of the Public Finance and Accountability (Scotland) Act 2000 and our opinion as to whether the Resource Accounts give a true and fair view and are properly prepared in accordance with section 19(4) of that Act.

### **Scope of the audit of the accounts**

An audit involves obtaining evidence about the amounts and disclosures in the accounts sufficient to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to Audit Scotland's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by Audit Scotland; and the overall presentation of the accounts.

In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect or inconsistent based on the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

We read the other information contained in the Governance statement, and consider whether it is consistent with the audited accounts. As auditors we are not required to consider whether the Accountable Officer's Governance statement covers all risks and controls, nor are we required to form an opinion on the effectiveness of the risk and control procedures. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

### **Opinion on the accounts**

In our opinion the accounts:

- give a true and fair view of the state of Audit Scotland as at 31 March 2014 and of its net resource outturn for the year then ended
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2013/14 FReM
- have been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and Directions by Scottish ministers issued thereunder.

### **Opinion on regularity**

In our opinion in all material respects:

- the expenditure has been incurred and the receipts have been applied in accordance with section 22(1)(a) and (b) of the Public Finance and Accountability (Scotland) Act 2000
- the sums paid out of the Scottish Consolidated Fund for the purpose of meeting the expenditure shown in the accounts were applied in accordance with section 65 of the Scotland Act 1998.

## Opinion on other matters

In our opinion:

- the information specified by Scottish ministers on remuneration and other transactions has adequately been disclosed
- the information given in foreword and the management commentary is consistent with the accounts.

## Matters on which we are required to report by exception

We are required to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the accounts are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the Accountable Officer's Governance statement contains any apparent misstatements or material inconsistencies with the accounts.

We have nothing to report in respect of these matters.

**Alexander Sloan**  
**Chartered Accountants**  
**Statutory Auditors**  
**38 Cadogan Street**  
**Glasgow G2 7HF**

10 June 2014

# ANNUAL REPORT AND ACCOUNTS

Year ended 31 March 2014

This report is available in PDF and RTF formats at:  
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