



**OFFICIAL REPORT**  
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**DRAFT**

# **Scottish Commission for Public Audit**

**Wednesday 12 December 2018**

**Session 5**

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**Wednesday 12 December 2018**

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**SCOTTISH COMMISSION FOR PUBLIC AUDIT**

**2<sup>nd</sup> Meeting 2018, Session 5**

**COMMISSION MEMBERS**

- \*Colin Beattie (Midlothian North and Musselburgh) (SNP) (Chair)
- \*Bill Bowman (North East Scotland) (Con) (Deputy Chair)
- \*Alison Johnstone (Lothian) (Green)
- \*Rona Mackay (Strathkelvin and Bearsden) (SNP)
- \*Jenny Marra (North East Scotland) (Lab)

\*attended

**THE FOLLOWING ALSO PARTICIPATED:**

- Stuart Dennis (Audit Scotland)
- Caroline Gardner (Auditor General for Scotland)
- Ian Leitch (Audit Scotland)
- Diane McGiffen (Audit Scotland)

**LOCATION**

The Adam Smith Room (CR5)



## Scottish Commission for Public Audit

### Meeting of the Commission

*Wednesday 12 December 2018*

*[The Chair opened the meeting at 12:30]*

### Decision on Taking Business in Private

**The Chair (Colin Beattie):** Good afternoon and welcome to the second meeting in 2018 of the Scottish Commission for Public Audit. I remind everybody to switch off any electronic devices. As always, I ask members right at the outset to keep questions and answers concise and to the point.

Item 1 is a decision on taking business in private. I ask for members' agreement to take agenda items 4 and 5 in private. Is that agreed?

**Members** *indicated agreement.*

## Spring Budget Revision 2018-19

12:30

**The Chair:** Item 2 is consideration of Audit Scotland's spring budget revision for 2018-19, which members have a copy of in their meeting papers.

I welcome our witnesses from Audit Scotland. Ian Leitch, chair of the Audit Scotland board, is accompanied by Caroline Gardner, the Auditor General for Scotland; Diane McGiffen, chief operating officer; and Stuart Dennis, corporate finance manager. I invite Ian Leitch and the Auditor General to make short introductory remarks. Do you have any introductory remarks to make, Ian?

**Ian Leitch (Audit Scotland):** Not on this subject, chair. You know my views on this rather mysterious subject.

**The Chair:** Auditor General, do you have any introductory remarks?

**Caroline Gardner (Auditor General for Scotland):** Yes, thank you, chair.

As in previous years, the spring budget revision requests budget cover for the non-cash pension charge that will arise as a result of accounting adjustments in 2018-19. As members know, those adjustments are notional and do not generate cash movements. We are not able to plan for them in advance due to the timing of the information that we receive from our actuaries, and the Scottish Government has advised us to deal with them through the spring budget revision process. The amount involved this year is £2.918 million.

We will do our best to answer any questions that the commission has.

**The Chair:** Thank you. The obvious question is: what preliminary discussions have you had with the Scottish Government to confirm that the previously agreed arrangements with Her Majesty's Treasury with respect to the pension adjustment remain in place, and have you advised it of the amount of Audit Scotland's requirement?

**Caroline Gardner:** The answer to both questions is yes. We have had the usual discussions with the Scottish Government. It is aware of the amount involved, and it supports the submission that we are making to the commission today.

**The Chair:** No other members have questions or comments. I have one small additional question. Paragraph 19 on page 4 of your paper states:

“The expectation of continuing low interest rates in the next few years may require similar large accounting charge adjustments in 2019/20 and beyond.”

That is a little bit alarming really, but that has been the pattern for the past few years. I know very little about those things but, logically, one would think that, once you have plugged the gap, it will not keep reappearing.

**Caroline Gardner:** You have gone to the heart of why this is a complex matter. The accounting adjustments that we have to make are not about covering a deficit in a pension fund; they are to do with the accounting adjustments that are needed to cover the accounting entries that relate to the pension scheme. Stuart Dennis can talk you through the accounting entries if you would like to know more about them. This is not a funded scheme in which we are looking to plug the deficit; that is handled separately in the contributions that we make. This is about the accounting entries that are required to reflect the movements around the pension scheme as a whole. I will hand over to Stuart Dennis to explain the issue to members.

**Stuart Dennis (Audit Scotland):** There are three elements to the figure each year. There is the projected current service cost—that is, the cost in-year for the benefits that the staff get by the end of March each year—and, on top of that, there is the interest income on plan assets and the interest cost on defined benefits. Therefore, multiple things influence the figure. That is offset by the contributions that we make as an employer as part of the different valuation that Caroline Gardner mentioned in eventually plugging the gap at a future date. This is really about the in-year cost that we have.

**The Chair:** Thank you very much.

## Budget Proposal for 2019-20

12:35

**The Chair:** The next agenda item is evidence on Audit Scotland’s budget proposal for 2019-20. Members have a copy of the proposal in their meeting papers. We have the same witnesses so, without further ado, I ask Ian Leitch to give an introduction this time, followed by the Auditor General.

**Ian Leitch:** We will be happy to answer any questions that members have on the budget proposal. I thank the chair and members for the invitation to appear.

All members will be aware that we are in uncertain times—on reflection, that is pretty much an understatement about what is going on in the world. Like the public bodies that we audit, we have to navigate a course through that to run our business and manage risks and uncertainty. We attempt to do that while recognising that public resources are limited and keeping audit fees at a reasonable level.

At the same time, we are mindful of maintaining and improving the quality of audit just as further new financial powers and bodies are coming into being. We took those factors into consideration as much as we could in producing our budget proposal.

Our resource requirement is £7.564 million, which is an increase of £416,000 from 2018-19. The increase is 4.2 per cent in real terms and relates largely to people costs. It is in line with the long-term planned investment in the organisation that was set out to the commission in previous years. The 2019-20 aspects of that plan are detailed in the proposal.

After that brief introduction, and with your permission, chair, I will hand over to Caroline Gardner to speak in her capacity as accountable officer.

**Caroline Gardner:** New financial powers continue to be rolled out to the Scottish Parliament. As the commission knows, they include major new responsibilities, such as social security powers. Our budget proposal will enable us to continue to fulfil our statutory audit responsibilities; to take on the audit of the significant new expenditure and revenue-raising responsibilities; and to support the Scottish Parliament in its important role of holding the Government to account.

As we indicated last year, we have developed a four-year plan that reflects the implementation of the new financial powers. The 2019-20 proposal represents the second year of that plan.

As the chair of the board said, we are all working in an environment of great uncertainty. We reflected that in our proposal as well as we could at this stage, but we will keep a close eye on events as they unfold and keep in touch with the commission during that process.

As ever, we are happy to answer the commission's questions.

**The Chair:** I refer to the table on page 7 of your proposal and the further explanation on page 8, where Audit Scotland has advised that, following the approval of the 2018-19 budget in December 2017, a further £262,000 of cost pressures was identified. Will you provide more information on the sources of those additional cost pressures? Why were those pressures met solely from additional charges to audited bodies?

**Caroline Gardner:** Stuart Dennis will respond in detail, but the biggest movement involved increased audit fees for integration joint boards, which are new bodies that were established in 2016 and 2017 and which are gradually taking on significant new responsibilities for health and social care.

**Stuart Dennis:** As members are aware, we prepare the budget in July and August every year. We submitted last year's budget proposal before the Scottish Government budget was announced, so we based the pay award policy on the then ongoing 1 per cent cost-of-living increase.

As Caroline Gardner said, an additional element is that we cannot analyse fees until audits are completed, so work on the 2016-17 fees was not completed by the time that we built our budget. Once the fees had been calculated and the SCPA had approved our budget submission last year, we revisited the figures and made adjustments to the pay policy primarily and to the base fee increase because of the increased volume for integration joint boards.

**The Chair:** I throw the meeting open to members.

**Alison Johnstone (Lothian) (Green):** I want to move on to explore the additional work requirements and the impact that they will have. You have highlighted that, in 2019-20, because of increased financial and performance audit work on Social Security Scotland and further work with the National Audit Office in respect of Scotland's VAT share and Scotland's rate of income tax, you are proposing a further 4.5 whole-time equivalent staff at a cost of £285,000 to deliver that additional workload. When you presented your 2018-19 budget in December 2017, you suggested that one WTE would be required for the year 2019-20. I presume that additional information or a greater understanding of what will be required has meant that the figure has increased by 3.5 WTE.

**Caroline Gardner:** It is a timing difference rather than an increase. You might recall that our four-year plan suggested that, at the end of that period, we would have an additional 20 people in place to cover the full range of the new responsibilities of the Scottish Parliament and the Scottish Government. The exact timetable for the roll-out of the new financial powers is not fixed and keeps changing. For example, on social security, the Scottish Government has entered into an agreement with the Department for Work and Pensions to take on responsibility for some of the benefits sooner, which means that the audit work needs to run more quickly. I am just about to appoint an auditor to the new social security agency to cover that. In addition, we think that the timetable for the full devolution of the assignment of VAT revenues is about to be agreed. There are some other changes behind that, which I can ask Stuart Dennis to talk you through in a bit more detail. However, it is timing differences within the overall plan rather than changes to the plan that we are looking at.

**Alison Johnstone:** Okay. How do you estimate the time that will be required to complete financial and performance audit work for an entirely new body?

**Caroline Gardner:** An element of judgment is involved, as members would expect. We use our own audit experience of bodies of a similar size and look at the particular functions and responsibilities of the new body to see what we think is likely to be needed. My team has worked very closely with colleagues in the National Audit Office, who have a good deal of experience of auditing the Department for Work and Pensions, in order to get a better understanding of the systems that will need to be audited and the risks that will need to be taken account of. We are taking a phased approach to implementation, so we currently have a small team that is responsible for all our work on social security—the audit of the agency and the performance audit work—and we will build that up as the timetable for taking on the new responsibilities is firmed up and as we build up our own expertise and experience. We are therefore clear that 4.5 WTE is the right number for 2019-20, and there are two years of the plan after that that we can flex as the timetable unfolds.

**Alison Johnstone:** Given that Audit Scotland will work with the National Audit Office in relation to some audit work, how will you avoid duplication of audit effort and how can you demonstrate value for money in those circumstances?

**Caroline Gardner:** That is a good question, and one that we are now spending a lot of time working on with our colleagues in the National Audit Office. The devolution of those responsibilities to the Scottish Parliament does not

reduce the size of the National Audit Office's audit of the DWP, because of its scale and complexity. A memorandum of understanding is in place between the Comptroller and Auditor General and me at the United Kingdom level that sets out what work we will do to satisfy the needs of each of our Parliaments: the UK Parliament and the Scottish Parliament. The legislation includes some requirements for the C and AG to report to the Scottish Parliament. The expectation is that I will provide additional assurance through letting the Scottish Parliament know that its interests are being taken account of during that process and that I have no concerns about the work that is being done.

We are due to have an update of the audit accountability framework between the two Governments, which will set out how the process will work once all the new responsibilities have been devolved. That is still subject to discussion between the two Governments, but it is an important area in order to ensure that both Parliaments get the assurance that they require and that there is no overlap in the responsibilities that each of us carries.

**Alison Johnstone:** On the question of duplication and overlap, to what extent has Audit Scotland considered or discussed transferring resources between audit agencies where responsibility for audit work changes—for example, from the National Audit Office to Audit Scotland for social security?

12:45

**Caroline Gardner:** We have considered that question with colleagues in the National Audit Office, and it is fair to say that they are strongly of the view that the devolution of the new financial powers to Scotland does not reduce their audit requirement at all. The amount of money involved—about £3 billion a year—is very significant for Scotland, but it is very small in the context of the overall DWP budget. If anything, there is more complexity while the DWP continues to administer some of the benefits on behalf of the Scottish Government.

We will keep the issue under consideration, but at the moment it looks as though the overall volume of audit that is required will increase as a result of the devolution of the new powers.

**The Chair:** Jenny Marra has a supplementary.

**Jenny Marra (North East Scotland) (Lab):** I have a question about social security, although I realise that it might stray slightly into the Public Audit and Post-legislative Scrutiny Committee's jurisdiction. Will the audit include an assessment of the set-up costs of the social security system in Scotland?

**Caroline Gardner:** Yes, it will. The financial framework was clear about who would bear the set-up costs in relation to all the new financial powers, including on social security, and the contribution that the United Kingdom Government would make towards that. I look at that as part of my performance audit work, and I reported on it on an interim basis back in April. I am due to update that next year, and the Comptroller and Auditor General will look at that at the same time through the lens of the DWP. That information will be available to Parliament.

**Rona Mackay (Strathkelvin and Bearsden) (SNP):** On page 9 of your budget proposal, you set out your work programme for 2019-20, which is based on the five-year rolling programme of national performance audits. What role does the availability of resources play in deciding the priorities for that programme, bearing in mind what the chair has said about these uncertain times and the current financial unpredictability? Has that become a difficult task for you?

**Caroline Gardner:** The process is managed by Audit Scotland on behalf of me and the Comptroller and Auditor General. We aim to have a rolling five-year programme, which will involve having certainty over the next two years and an indicative programme for the years ahead, so that we can make the best use of our staff time and of the general intelligence gathering that we are doing to inform the programme. That will give the people we audit and Parliament a sense of what is coming.

**Rona Mackay:** So your programme is fairly secure for two years but, beyond that, it will depend on events.

**Caroline Gardner:** It is certainly more strongly committed in the first couple of years, because work that we will publish next summer will already be well under way. However, we aim to retain some flexibility so that we can respond to events. The obvious example is the impact of EU withdrawal and what will happen in that regard over the next 12 months, but other issues emerge from time to time.

**Rona Mackay:** My next question was about how you build in a safety net for events that might happen. Do you have enough resources to enable you to cope with anything that might crop up unexpectedly?

**Caroline Gardner:** We manage such situations within the programme, on the basis that it would not be appropriate for us to have a large chunk of uncommitted resource. We are talking about money that comes from other parts of the public sector, so we do not do that. As you know, we cannot carry forward reserves.



However, we are very clear about how we can flex the programme to respond to events. That will be possible to a limited extent over the next 12 to 18 months, and to a much greater extent for the remaining three years.

**Rona Mackay:** So you can move money around if you need to.

**Caroline Gardner:** That is exactly right. We now have a specific EU withdrawal category. We have committed some resources to that area without refining the scope of what will be looked at—there is too much uncertainty for us to be able to do that.

**Rona Mackay:** Thank you.

**Jenny Marra:** Your budget proposal contains a proposal to double the management contingency from £150,000 to £300,000. Why is that?

**Caroline Gardner:** It is a direct response to the uncertainty that we are now facing. We cannot carry forward reserves and, obviously, I am not prepared to risk overspending our budget. Therefore, for a long period, we have run a small contingency of £150,000, and that has been included in the proposal that we have brought to the commission in previous years. Given the extent of the uncertainty that we are now facing with regard to not just the work that we might need to carry out, which Ms Mackay explored, but what the impact might be on our costs in future, we propose to increase the contingency to £300,000. It is still a very small part of our budget—I think that it accounts for 1.2 per cent of our expenditure at the increased level—but we think that it is an appropriate buffer to have in place to avoid our having to come back to the commission if things turn out to have a big impact on our prices and costs next year.

**Jenny Marra:** I see Ian Leitch nodding. He obviously feels that this is quite important, given the current circumstances.

**Ian Leitch:** Yes, preparedness is a big issue, but the question is: preparedness for what? Guidance has been issued to the auditors who audit all the bodies about the questions that they should be asking to find out the state of preparedness, but every organisation is different.

**Jenny Marra:** Is it about preparedness for Brexit?

**Ian Leitch:** Yes, but what does that mean? I gave the example of the European agricultural fund audit, which is paid for through Europe—it comes through the National Audit Office to us—to the tune of £874,000 a year. Presumably, there will still be an audit and presumably, there will still be grants to farmers that will need to be audited, but what will the shape of that be and, more important, who will decide it? If it is a UK thing and

we do it as a sort of agent of the NAO, the resource should come from the NAO. If, on the other hand, it is devolved to the Scottish Government, arguably it would not be a chargeable item to the Scottish Government. As you know, we cannot charge for that audit, so the cost would have to be met through the commission approving it as a top slice from the consolidated fund. We do not know all those things; we do not know what flexing we have or what staff will be needed—18 staff members are involved in that work at the moment. The contingency fund and our staff movement—there is a 6 per cent turnover of staff—allow some flexibility.

We have tried to avoid taking too much from the pot of the consolidated fund, because if we top slice too much, we deny other parts of the public sector the use of those resources. At the end of the day, there is no point having it as a credit balance, because that means that somebody else does not have the opportunity to spend it on worthwhile public projects.

To lead on from the Auditor General's answer, I think that all those factors are about how we are trying to manage our budget within reasonable limits while giving us a degree of flexibility.

**Jenny Marra:** That makes sense. Of the £150,000 available in management contingency last year—or this year—how much has been used?

**Stuart Dennis:** Last year, we used half of it—about £75,000—in our actual accounts. As far as this year is concerned, there are still elements to be decided. It will probably not be used in full, but we do not know what will happen in the next three months, so it might well be.

**Jenny Marra:** Let us hope that next year we will be living in more certain times.

**Diane McGiffen (Audit Scotland):** An additional assurance for you is that we account for what we have spent out of the management contingency to the board and the commission at the final accounts stage. If the unexpected changes do not occur, we will be accounting for why we have not spent the management contingency as well as accounting for what we have spent. You and the board have that assurance at the other end of the process.

**Jenny Marra:** Moving on, we have picked up that the cost of audit to local authorities has increased by 4.2 per cent, while the cost of audits to other bodies such as the national health service and colleges has remained broadly the same. Can you explain why that is?

**Caroline Gardner:** I will ask Stuart Dennis to talk you through the detail in a moment, but first of

all it is worth reminding the commission that the board has encouraged us over the past few years to provide more transparency about the costs of each sector and how they are recovered through fees and to make sure that we balance each sector as well as the organisation as a whole, taking one year with another, so that there is more transparency in that regard. Stuart Dennis can talk you through the reason for the changes in the local government sector compared to the others.

**Stuart Dennis:** As the Auditor General has said, we do a sector analysis. We look to break even by sector. Included in that is apportionment of overheads, based on the data of completion of audits from the previous year. When we collect that data and redistribute it, that means that it moved around in volume where the work was done. That is where the fees and the apportionment of costs go, and that balances out.

**Jenny Marra:** Forgive me—I am not following that very well. I think that I understand it in accounting terms, but can you take us through it again?

**Stuart Dennis:** Yes, sure. Broadly, we look to break even by sector, so we take the number of audit days for each sector as the key driver for how we then distribute the costs in our budget across the sectors, allocating all the different overheads such as finance, human resources and information technology. It depends on where the work is. If that moves around—if the volume moves around slightly—there is more shifting of overheads, too.

**Jenny Marra:** What do you mean by the volume moving around?

**Stuart Dennis:** The volume is, in effect, the audit days.

**Jenny Marra:** Right. So, if there are more audit days for councils than there are for, say, colleges, it becomes more expensive.

**Stuart Dennis:** Yes.

**Jenny Marra:** My question, then, is: why are there more audit days for local authorities than there are for the other bodies?

**Stuart Dennis:** For a start, the local government sector includes the IJBs and, as we have highlighted, we had to increase the audit days based on the volume of audit days that we needed for the IJBs. That is one of the key areas.

**Caroline Gardner:** I think that what you are referring to, Ms Marra, is the income from charges to local government bodies on page 14, which has gone up, as you say, by 4 per cent as a result of the volume changes that Stuart Dennis has talked about.

It might help if I refer you to the fees and funding strategy on page 23 of our submission. You can see in table 1 that the charges to local government bodies have gone up by 0.5 per cent in real terms; in other words, the unit cost has gone up by 0.5 per cent. The volume overall has gone up by 4 per cent because of the change in the volume of work that is done.

**Jenny Marra:** Okay. So the cost of doing an audit of a council has gone up by—what did you say?

**Caroline Gardner:** That is not quite the right conclusion to draw. The unit cost—the fee—has gone up by 0.5 per cent in real terms on a like-for-like basis. That will vary for individual bodies depending on their circumstances, but that is the case across the sector.

The overall cost to local government has gone up by about 4 per cent, because of the change in the volume of the number of bodies that we are focusing on and the increase in the size of the IJB audits as the IJBs have taken on their full responsibilities. That is where the 4 per cent figure comes in. I apologise—it is a complex matter

**Jenny Marra:** I should apologise—I should be following this better. Who picks up the differential between what you charge and the actual cost?

**Caroline Gardner:** Local government pays for all the audit work in local government. All the annual audits, the performance audits and the best value audits are paid for by local government itself through the fees.

**Jenny Marra:** Thank you.

**Rona Mackay:** On page 24 of your submission, you set out the hourly rates used to cost audits, including staff costs. It is notable that the increases for certain grades of staff have been higher than others. For example, the hourly rate for audit managers has increased 8.6 per cent from £70 to £76, whereas the hourly rate for trainees has fallen 8.3 per cent from £48 to £44. Can you explain why that is?

**Caroline Gardner:** I will ask Stuart Dennis to talk you through that.

**Stuart Dennis:** The hourly rates are based on direct costs—that is, the actual pay, national insurance and pension contributions—and indirect costs such as property costs, IT and finance. An element of overhead involving indirect costs is included in the rates.

The figures are based on the budget at a particular time, and we take the mix of staff we have at that time. For example, the hourly rate for trainees has come down from £48 to £44, because of the mix of trainees and where they are on the pay scale. When the calculation was done for

2017-18, there would have been more trainees at the higher end of the pay scale than there were when we did the calculation for 2018-19.

**Rona Mackay:** So the rate is on a scale. It is not just a flat rate for trainees.

13:00

**Stuart Dennis:** It depends on where they are in their training programme. We have about 34 trainees; in 2017-18, more trainees were at a higher point of the pay scale than was the case in 2018-19. That is also a key driver for the allocation of the overheads; if that figure is reducing, it takes less of the overhead element. Audit managers will take more, because they are at a higher level, and the rate is based pro rata on the level that they are on.

**Rona Mackay:** Is that how it is normally done? Is that standard practice?

**Stuart Dennis:** Yes. As a finance forum, we benchmark with other audit agencies, and our levels are very similar to theirs.

**Rona Mackay:** They are comparable with those of other audit agencies.

**Stuart Dennis:** Yes.

**Bill Bowman (North East Scotland) (Con):** Do you have a budget for the hours?

**Caroline Gardner:** Each audit manager will have a budget for their audit, and that is expressed through the audit fee that is charged to the body and a standard make-up of the audit team. However, as you will know, the actual make-up of an audit team will vary, depending on the availability of resources and the requirements of a particular audit, and the breakdown of each grade will vary over time, too, depending on where people are on their pay scales.

**Bill Bowman:** Do you have a summary of all the teams to give a total hours budget for the organisation?

**Caroline Gardner:** The audit services team, which is the team responsible for doing the 70 per cent or so of the annual audits that are carried out, absolutely have that budget and manage it very closely for each of those audits. We manage the organisational staffing budget as a whole, including audit services, performance audit and best value and the corporate services group.

**Diane McGiffen:** Perhaps I can clarify something with regard to the previous question that connects with the current question. The table in paragraph 26 of appendix 3 reflects not the rates paid to trainees but the different mix of trainees. There has been a shift not in the salaries

of people but in the total cost of the audit at each grade.

**Rona Mackay:** Are you saying that, in effect, it is neither an increase nor a decrease?

**Diane McGiffen:** Our trainees are all paid on a set scale, and that has not changed. The mix of trainees that we had at the point when the table in paragraph 26 was produced changed from the mix that we had when the previous table was produced. At that time, more trainees were at the top end of their grade, but those people have now qualified and have gone on to other roles in the organisation. The table now reflects the fact that more people are starting their trainee journey with us. However, they are all being paid the same rate—that has not shifted.

**Rona Mackay:** Thank you. I understand that.

**Diane McGiffen:** I hope that that is helpful. I just thought that there might have been a bit of doubt about what the table is showing.

Coming back to Mr Bowman's point, I can tell him that we do have all that data for the audit services group, who manage the chargeable rates and the hourly allocations. That has built up, as you would expect.

**Bill Bowman:** Do you have a summary that shows the time that they say they have spent with clients, on training and so on?

**Diane McGiffen:** Yes. We have all those profiles and we work through that with the time recording system, which is what helps to build up the picture of what the costs should be. Stuart Dennis mentioned earlier the shift that we made in integration joint board charging, which was driven by the use of the time recording data to look from the planning assumptions being made about IJBs to the reality of how auditors were actually spending their time. As a result of that, we recognised that we needed to make a shift.

**Bill Bowman:** Can we see that summary?

**Diane McGiffen:** You can. Perhaps we can have a discussion afterwards about what form it might take. I can assure you, though, that the information is fed into the financial reporting and so on that the audit committee and the board review on a quarterly basis. I am very happy to share that.

**Bill Bowman:** Okay. We will come to that later then.

I have another question. I am pleased to see that quality is mentioned quite a lot in your budget proposal. Your quality report has within it a survey of the staff and their views. The 2017-18 quality report identified some areas where performance had fallen compared with performance in 2016-17—for example, in training and development.

What are the reasons for the fall in the number of positive responses from the number that was recorded in the previous year? Aside from having a staff survey, how does Audit Scotland assure itself that staff are well supported to deliver quality audits? You have £250,000 to invest in audit quality. How will you invest that to address the issues?

**Diane McGiffen:** I will start and, if I miss any of your three questions, I am sure that you will prompt me.

On the survey results, I assure you that the survey will be run again and that the commission will have the results at the end of the financial year when we publish the next annual quality report. This year's survey has not been conducted yet, so I do not know its results, but we will look at them closely.

Last year, there were increased pressures and increased commitments in parts of the organisation because of the volume of work—we talked about the audits of integration joint boards, for example. We looked closely at training and development and we made changes following that.

We changed how we organise professional support, which provides the technical and auditing support and training that help our auditors to be up to speed and up to date on all the technical matters that they deliver in their audits. We have focused on joining up professional support with our learning and development programme this year. We have offered more events and a huge range of topics, and we have involved external and internal providers. We have also worked with other audit agencies on a range of activities. At each event, we take feedback from colleagues who take part in learning and development. We also take stock of how teams feel about their ability to respond to demands.

We take short-term feedback all the way through the year. We will run the survey that the audit quality report refers to again, and we will soon have the results of another survey of staff, which is an anonymous survey. The participation rate in our Best Companies survey is very high—it is 84 per cent this year. That survey asks a series of questions about learning and development, so we await its results. Results from that survey go back 10 years, so we can carefully track what people have felt.

Audit Scotland's participation in the survey that the audit quality report refers to did not achieve a response rate of 84 or 85 per cent, which is the exceptionally high rate that we are used to. We are therefore working on the timing of that survey and thinking about how we can ensure that people participate.

We were disappointed by the results and we have been working hard to improve them. People and their skills are at the heart of the organisation. We want our people to have the time to devote to learning and development and to be supported in their learning and development, and we are working to make that as effective as possible. We have done lots of work on that and we will see what the next survey results tell us.

You asked what we will do for the audit quality team. We have a team of three people—when you read our audit quality report, you will have seen them pictured at the front. The team regularly reviews audit quality and reports on it to the Auditor General, the Accounts Commission and the audit committee of Audit Scotland's board. The team produces five reports every 12 months, including the annual report.

In addition to its own work, the team commissions work from the Institute of Chartered Accountants of Scotland, which means that the work of all auditors—those in Audit Scotland and the firms that we appoint—has an independent external review. This year, that work has just started. Through ICAS and the quality work that teams do individually, we will have reviews of about 11 per cent of the audits that we carry out. That is a significant percentage and an increase on last year.

As Audit Scotland, we are investing through our learning and development strategy to improve the quality of the work. We have a comprehensive programme of quality reviews, which we report on annually. We also have independent external reviews of work, which we publicly report on.

In a development that I think is unique across the audit agencies in the UK, we have extended the independent external reviews beyond the financial audits to include both the performance audits and our best value audits, and we are treading new ground in figuring out how to apply good, independent external reviews of two quite unique audit products. This year, we have much more quality review work on the go than we did last year and last year we made significant progress in the work that we reported. In the next annual quality report, the commission will be able to look at another set of results in relation to that review work.

**Bill Bowman:** For clarity, I should say that I am a member of ICAS, but just an ordinary member.

**Ian Leitch:** Quality is one of our key issues. As you know, across the country the profession is in somewhat dubious circumstances as a result of recent happenings with some of the companies and we are particularly keen that the public audit model in Scotland is the best that it can possibly be. That is why we have gone to all this trouble

and why we are concerned to make sure that we have the team to monitor it and that we have the independent review; it is why the board of Audit Scotland and its audit committee consciously seek those reports throughout the year. We have to assure ourselves first and then we have to assure the client groups, the commission and the Parliament that the audit quality is good.

**Bill Bowman:** Have the reports or reviews that you have done so far come up with anything that is concerning?

**Diane McGiffen:** No, not at this point. Last year's report highlighted a thread across all audit providers, which I think is highlighted in all reviews of audit, that sometimes better documentation is needed. We have been working on that, as have our partners in the firms, but as of today there have been no significant concerns.

**The Chair:** Do members have any other questions?

**Bill Bowman:** I have one or two more questions. I asked about the chargeable hours budget, which I think you will provide more information on. I do not think that you gave an actual cost or confirmed the number of hours that will be required to do the audit of the new Social Security Scotland.

**Caroline Gardner:** I did not but I am happy to come back to the commission after today's meeting with that information, if it would be useful.

**Bill Bowman:** Yes, thank you. There is a proposed capital budget of £150,000 for 2019-20, which is down from £175,000 for 2018-19. I think you have depreciation of somewhere around £300,000 elsewhere in the budget. I always thought, as a rule of thumb, that the capital should be at least the depreciation figure, to make up for the consumption of the assets. Is that not the case?

**Caroline Gardner:** It is changing because of how our IT is provided now. Most of the capital budget this year is for IT costs, both hardware and software, but the balance of our overall spend on IT is shifting from buying equipment and licences to buying subscriptions for cloud storage and cloud services. For example, this year we have moved to Office 365, so there is less capital investment to run the IT service than we have seen in the past. We are still depreciating past assets and, for our leases, we have provisions for dilapidations on the same basis.

**Bill Bowman:** So the staff have the correct equipment to do the job.

**Caroline Gardner:** That is absolutely our intention and it is what this year's capital budget is intended to do.

**Bill Bowman:** I know that different parliamentary committees receive reports from you when various things go wrong at organisations. Do those organisations get charged in some way and is a good organisation, which has done nothing wrong, in a better position than one that has had a number of reports?

**Caroline Gardner:** Yes, in relation to the chargeable audits that we carry out. The clearest example of an organisation getting charged over recent years is the Scottish Police Authority. For a range of reasons, we have had to do a lot of extra work to be able to provide an opinion on the financial statements and the SPA has been charged an additional fee for that work. That example is at the extreme end of the range of what has been needed, but it is the best example.

**Bill Bowman:** Does that cost appear somewhere in these reports?

**Caroline Gardner:** It is included in the fee income and it is often part of the answer that we give you when you ask why the fees for particular bodies have changed. I think we wrote to you last year with more information about the fees that had been higher than predicted—the difference between the budget and the actual amount. The cost does not appear on the face of the report because it generally involves a very small movement—something on the scale of the SPA example is unusual.

13:15

**The Chair:** I have a couple of small questions. I noticed that firms employed by Audit Scotland to perform audit functions received a 2 per cent increase in fees. Although this is not a comparison really, the average fee increases were 1.6 per cent. Will you confirm that the fees for the chargeable audit bodies cover the increase in the fees to the external providers?

**Caroline Gardner:** In total, yes. The mechanism for increasing the fees for the firms is set out in the contract that we have with each of them following the procurement process that happened two and a half or three years ago, which makes a provision that we will uprate the amount that we pay them in line with the base increase to our staffing costs. Two per cent is the assumption that we have for both our base increase to staffing costs and the fees.

**The Chair:** So that has been recovered on the other side.

**Caroline Gardner:** Absolutely, yes—by sector as well as across the budget as a whole.

**The Chair:** On page 5 of your submission, in paragraph 9, you talk about having a new team to audit Social Security Scotland. Where will the

expertise for that come from? Is special expertise needed?

**Caroline Gardner:** Certainly special expertise is needed. We have some expertise ourselves; we have been auditing housing benefits in local authorities for a number of years, which provides us with a good starting point. Since the Smith commission agreement and since the Scotland Act 2016 was first being developed we have recognised the need to build our capacity in this area and we have worked closely with our colleagues in the National Audit Office, who have many years' experience of auditing the Department for Work and Pensions and its predecessors. We have developed specialist training for the staff who are involved and have been building on that to make sure that we have the experience that we need. You are absolutely right, however, that it is quite a complex and specialised area, with particular risks in relation to the level of fraud that has been experienced in the UK as a whole. It is important to get it right for people who rely on benefit payments for their wellbeing. We absolutely recognise the importance of making sure that our teams are properly skilled to do that.

**Diane McGiffen:** We have been recruiting a lot this year. To date, we have had 19 new starts in the organisation. There is quite a lot of resourcing internally. We are looking at the mix of experience and skills that we have and the career opportunities that people want.

As you know, we have a strong commitment to our graduate training scheme and to growing our expertise. We took on an additional two graduates last year—above what we had notionally planned—to help make sure that a range of skills will flow through into the new social security work. There will be graduates, experienced staff and new people, so that we can get diversity in our teams, which will help us to make the most of the opportunity that we have to set up new teams and expand the organisation.

It is a challenging environment in which to create new teams, but it is also a real opportunity for us. We have been expanding slightly as an organisation, which has been welcome, with career opportunities for existing colleagues and new members who have joined.

**The Chair:** I get the impression that there is increasing specialisation in Audit Scotland in particular areas. For example, we have been talking about the special skills needed for social security. We have talked previously about the special skills needed for IT audits and so forth. Are we increasingly having to rely on people who are specialists in their areas and is that creating a silo effect within Audit Scotland?

**Caroline Gardner:** You are right that our work is becoming more complex and the range of bodies that we audit is increasing, as we are auditing such things as social security and tax-raising for the first time. We work hard to make sure that we have the balance right between having as much flexibility as we can in our resourcing and giving people the career development opportunities that Diane McGiffen referred to, while also having the real specialism that we need for particular areas such as social security. Our workforce plan is part of addressing that. It aims to make sure that we think ahead about the skills that we need so that we have the chance to develop them internally and to recruit people who have them.

However, the core that runs through all our work is audit skills. Ian Leitch referred to the staff who are working on the audit of the European agricultural funds—we have about 20 staff working on that. If that work finishes because of the way in which we leave the EU, the fact that they are all qualified auditors means that they will be able to work on other parts of our portfolio of work, so we are not running the risk of them not being able to be redeployed elsewhere. That is an example of the sort of balance that we try to maintain. The process does not always work smoothly in the short term, but that is our intention for the longer term.

**The Chair:** According to page 7 of your budget proposal, "People costs"—the number of staff—will go up, but your administrative costs will go down. How realistic is that?

**Caroline Gardner:** The reductions in "Other administrative costs" are all identified reductions; they involve a combination of savings and cost reductions. Stuart Dennis can give you a bit more detail about what is included. The important point to make is that we think that what we propose is realistic.

**Stuart Dennis:** Some of the reductions relate to property costs, which will come down. Depreciation was mentioned; that cost is coming down. Our travel and subsistence costs are coming down, too, because the car scheme that we had for staff ceased on 1 April 2017. As staff who were members of that scheme leave, the cost reduces. Everything that has been identified to reduce costs is achievable.

**The Chair:** The real decrease in costs is actually greater, because those costs are supporting more staff.

**Stuart Dennis:** Yes, the costs are coming down. Even though there are more staff, they will not benefit from the car scheme, for example. That is a genuine saving. The cost of our business rates has come down, too. All the savings that we

have identified are deliverable, even though staff numbers are increasing.

**The Chair:** I have one final question, which relates to appendix 2 on page 19. For some reason, I had never previously realised that local authorities pay only half the cost of the performance and best value audits.

**Caroline Gardner:** Are you looking at the "Performance and Best Value audit" line in the table on page 19?

**The Chair:** Yes—it is in appendix 2.

**Caroline Gardner:** Broadly, the total cost is nearly £3.9 million, of which local authorities pay a bit more than £2 million and the Parliament pays around £1.8 million. Local government pays for all the performance audit work in best value and all the best value audit work in local government. On the back of the fees and funding strategy that we agreed with the commission at the beginning of the process, the SCPA consolidated fund picks up the cost of all the performance audit work that is done in the NHS, central Government and the further education sector.

**The Chair:** Okay. As members have no further questions, we will move into private session. I thank the witnesses very much for attending.

13:23

*Meeting continued in private until 13:35.*





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