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Chair
Scottish Commission for Public Audit
The Scottish Parliament
Edinburgh
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Dear Chair

Thank you for the opportunity to give evidence to the Scottish Commission for Public Audit (SCPA) on 24 June 2024 in relation to the Audit Scotland Annual Report and Accounts 2023/24.

We are writing to you to provide additional information in relation to matters raised in the Commission's letter of 16 July 2024. We hope that this clarifies the areas where you and your fellow SCPA members have asked us to provide you with more detail.

Non cash resources

We note the Commission's disappointment that it was not advised of the £6.271 million of non-cash resource required to comply with the new technical requirements in relation to lease costs. We also note that the Commission has written to Audit Scotland's external auditor Alexander Sloan on this matter.

For the accounting period ending 31 March 2024 there is a requirement for Audit Scotland to account for leases in accordance with the International Financial Reporting Standard (IFRS) 16 in order to comply with the Government Financial Reporting Manual (FReM).The implementation of IFRS 16 requires the creation of a Right of Use asset on the balance sheet for the total value (a discounted cashflow model of lease payments) with an asset life equal to the term of the lease. This is then matched by the creation of a Lease creditor for the lease payment part of the Right of Use Asset calculation.

The IFRS 16 Accountancy and Budget Guidance Note issued by the Scottish Government Finance Directorate provided the transitional process to be adopted to enable discussion to take place with HM Treasury on the non-cash adjustments required. The full lease obligation is recognised as a non-cash Capital Departmental Expenditure Limit (CDEL) budget for the full value of the (potentially discounted) Right of Use Asset calculation for new, or extensions of existing, leases in the financial year they commence.

There was a requirement for a technical budget adjustment to be made in the Autumn Budget Revision (ABR), which was approved by Parliament on 7 November 2023. The approach adopted was based on the guidance received from the Scottish Government Finance Directorate who agree with the UK Treasury the total technical accounting adjustment required to comply with the IFRS 16 reporting standard.

Audit Scotland's requirement of £6.271 million was included in the Autumn Budget Revision (ABR) following engagement with the Scottish Government Finance Directorate. This enabled us to focus on reducing the size of the Edinburgh office, extend the size of the Glasgow office and replace expiring car leases.

While this was referred to in our budget proposal submitted 13 December 2023 (paragraphs 63-66), we recognise that the actual technical adjustment figures were omitted from the proposal. Please accept our apologies for this oversight and assurance this will be rectified for future budget submissions.

Please be assured that now there is a better understanding on how this technical adjustment impacts non-cash budgets and any future requirements for in-year CDEL adjustments for new or existing leases, these will be included in the annual budget submissions to the Commission.

Staff vacancy factor

Your letter notes that vacancy management provides a useful tool in the process of managing the budget. It is appropriate that the budget recognises that natural employee turnover means that we are unlikely to be operating at full complement 100% of the time in practice.

Excluding the accounting adjustments required under International Auditing Standard (IAS)19 for pension and untaken holiday costs, the people cost operational budget for 2023/24 was underspent by £514k (2.2%). This was principally as a result of the average vacancy level for the financial year being 9.4 whole time equivalents less than funded establishment.

The average vacancy factor for 2023/24 was 4.8 per cent compared to 6.1 per cent in 2022/23. Many internal colleagues have been successful in gaining promotions due to the recruitment activity during 2023/24. This had a knock-on impact on vacancies in band three and below.

The HR team works closely with the Corporate Finance team and business groups to ensure that any staffing changes occur within the overall approved financial envelope for the workforce.

On a planned basis, this can, at times, result in a below establishment position where positions are left vacant to ensure there is sufficient room for progression, for example in band one for our trainees, who progress through the band upon achieving exam qualification status.

The total turnover rate for 2023/24 was 9.33 per cent and the voluntary turnover rate was 5.83 per cent. This was a slight increase compared to the total turnover rate in 2022/23 of 9.02 per cent and a decrease in our voluntary turnover rate which was 6.62 per cent.

The turnover rates at Audit Scotland remain significantly below the headline measures of whole economy labour turnover, where the whole economy total turnover rate stands at 19.9 per cent and voluntary resignation rate is at 14.2 per cent[1].

We take some assurance from this that colleagues find Audit Scotland a good place to work. At the same time, we recognise that a degree of turnover is healthy, as it can bring in fresh ideas, talent and different perspectives. This supports our values of equality and innovation.

There will be some requirement to use the savings delivered by a higher turnover rate than budget to fund unbudgeted short-term agency appointments to ensure we continue to deliver essential operational requirements, most commonly in Audit Services and Corporate Services business groups.

[1] Source: XpertHR labour turnover rates September 2023

Audit Scotland’s Executive Team and Board monitor turnover and vacancies on a quarterly basis.

Currently we do not consider increasing the vacancy factor as a budget offset is prudent in the context of the volume of change and recruitment in the organisation. However, we will of course keep this under constant review.

We can confirm that Audit Scotland’s detailed vacancy factor assumptions will be provided for the Commission’s consideration of the 2025/26 budget proposal.

Additional audit fees

As highlighted in the annual report there are several factors that influenced the final outturn in respect of payments to external firms.

There were some residual costs relating to completion of 2021-22 audit work in financial year 2023-24 where no budget had been allocated. Usually the bulk of this audit work would have been completed in financial year 2022-23 but due to outstanding audit issues this moved into the new financial year. The cost of this was £200k.

The contract with the firms is uplifted in October each year based on the approved pay award for Audit Scotland staff. The budget in 2023-24 was based on a 3% pay award with the actual final settlement being 6% due to the cost of living pressures highlighted to the Commission at our budget scrutiny session in December 2022. The full year impact of this is £310k more than originally budgeted.

The financial year 2022-23 was ‘year one’ of the new appointments and this can have an impact on the amount of audit work required to ensure compliance with the new Code of Audit Practice and International Auditing Standards (IAS). The scale of the adjustments is difficult to predict until the new appointed auditor starts to engage with the public sector audited body, and at the time of the budget proposal it was estimated that any difference would not be significantly material to include in the budget.

The performance section in the annual report highlights that additional payments were required from some fee paying bodies due to a number of factors. These included the identification of a significant number of adjustments, the application of accounting standards and delays in auditors receiving accounts and working papers, and the quality of those documents. This is provided for within the appointment and contracts process and follows engagement between the appointed auditor and the audited body.

The Audit Quality and Appointments team in Audit Scotland manage the contract with the firms and hold regular contract management meetings with the lead partners within the firms. These meetings consider performance against the delivery timescale targets, while recognising that delivery should not be at the expense of the priority to deliver a high-quality audit.

The commencement of audit work in financial year 2023-24 is on budget and in line with the position from the previous years.

Budget underspends and overspends

The 2023-24 budget proposal was prepared in the context of uncertainty around the correct budgetary treatment for IFRS 16 leases (as outlined above) and was based on the best available information to support the proposal at the time.

Regular financial monitoring is undertaken by Audit Scotland’s Executive Team, the Board and the Audit Committee to ensure that we can evidence that we are delivering on our commitment to provide value for money.

In relation to **travel and subsistence** the total actual savings were £156k. The car lease scheme accounted for £124k of this. This is a closed scheme and the saving is due to the number of staff eligible for a lease car decreasing at a faster pace than planned due to promotions and leavers. Entitlement to membership of the car lease scheme ends if a colleague is promoted.

The IFRS 16 Leases standard also has an impact on the presentation of car lease expenditure in the annual accounts compared to our budget proposal. Under the standard we are now required to recognise the finance element of a car lease as a right-of use asset and depreciate over the duration of the lease. The accounts include this expenditure under the depreciation section, whereas in the budget proposal and our monitoring it appears within travel and subsistence. This is the reason why there is the potential for a large variance to occur if the annual accounts figures are directly compared to the figure submitted in our 2023-24 budget proposal. This situation also arises within the Rent and Rates heading.

In relation to **legal and professional fees** the 2023-24 approved budget was £752k and expenditure in the accounts was £531k, a variance of £221k. The main reasons for the underspend were due the release of prior year accruals in respect of housing benefit audit work, which, following examination, were identified as being no longer required. There was also a requirement to allocate the unused budget element of the audit modernisation project to fund a temporary project manager post within people costs. As mentioned at the evidence session, National Fraud Initiative (NFI) costs arise every two years and 2023-24 was a year where payment was not required and so this was the main reason for the movement compared to the previous year.

In relation to **IT costs**, the upgrade to the finance system was identified as a requirement after the Commission scrutinised our budget proposals in December 2022. In April 2023 we were advised by our Digital Service colleagues that the server hosting old finance system was no longer going to be supported by the end of 2023. This was identified as a significant risk that needed to be addressed. On evaluating the situation, and following robust forecasting, it was agreed that the most appropriate course of action would be to upgrade the finance software and migrate to a cloud based version, in line with our digital strategy. The finance system is one of our critical systems that requires robust security and protection. The decision to move to the cloud version was the most cost effective and appropriate course of action in the circumstances.

As advised at the evidence session in June, now that we have more clarity on the budgeting requirements under IFRS 16, we have requested the technical adjustment of £283k non-cash CDEL funding in addition to our approved 2024-25 budget as part of the Autumn Budget Revision process to enable us to comply with the FReM. We will be able to provide more detailed information to support the effective scrutiny of our future budget proposals.

Matters of concern about audited bodies

We receive correspondence from a range of people, including the public, Members of the Scottish Parliament (MSPs), Members of Parliament (MPs) and councillors. The correspondence covers a variety of matters about the bodies we audit and can be a valuable source of information for our audit work. We consider issues of concern as part of our Code of Audit Practice. The Code states that the key factor in determining whether we examine an issue of concern is its relevance to Audit Scotland's role and functions

Each year we publish a report on correspondence and whistleblowing. The most recent report, was published on 14 June 2024.

In 2023/24 we dealt with 301 items of correspondence. This was a three per cent increase compared to the 292 items dealt with in 2022/23. The correspondence in 2023/24 was comprised of:

- 195 new issues of concern, including 18 whistleblower disclosures and three objections to accounts
- 53 re-opened issues of concern
- 47 enquiries about our work
- six cases carried forward and completed from 2022/23.

Prior to 2021/22, our overall levels of correspondence were decreasing. We have received an increasing number of issues of concern over the past three years, while enquiries about our audit work have continued to fall over this period.

In 2023/24:

- 49% of the matters of concern related to Local Government (this proportion has increased over the period 2021/22 to 2023/24.)
- 35% related to Central Government
- 6% related to Health
- 9% related to bodies/ issues outside of our remit.

There are some recurring themes in the issues of concern raised with us in relation to local government. In 2023/24 the themes were:

- the transparency of decisions about education
- councils' governance and scrutiny arrangements
- council spend on local area projects
- officer and elected members' conduct and transparency
- planning/planning decisions.

In 2023/24, we received 88 issues of concern relating to central government bodies, compared to 103 in 2022/23. These issues of concern covered 20 central government bodies. Similar to previous years, around half of these concerns related to the Scottish Government and Transport Scotland. In 2023/24, we received seven concerns about colleges, compared to 18 concerns the previous year.

There were some recurring themes in the issues of concern raised about central government bodies. Similar to our two previous annual reports, ferries has remained one of the most common themes. This remains an area of audit interest for the Auditor General for Scotland. We also received a number of issues of concern related to the topics covered by our Decarbonising heat in homes report.

We continue to perform well in relation to target response times. In 2023/24, 97 per cent of correspondence was acknowledged within five working days and 98 per cent of correspondents received a final response within 30 working days.

Audit quality

In your letter you asked about the progress being made in relation to improvement actions identified in the Quality of Public Audit in Scotland 2022/23, and in particular on root cause analyses and learning and development in the Audit Services Group.

Auditors incorporate any relevant recommendations for improvement made in the annual Quality of Public Audit in Scotland reports into their own quality improvement action plans. Progress against these actions is monitored by the Audit Quality and Appointments team in Audit Scotland and an annual compliance report is prepared by each auditor to summarise their progress and actions in addressing the recommendations.

The actions arising from the audit quality reviews/ surveys/ root cause analysis (RCA) are monitored by the Quality and Ethics Committee and the Audit Committee. The audit quality action plan is updated and monitored on an ongoing basis. The most recent update report, considered by the Audit Committee in May 2024, advised that all improvement actions relevant to Audit Services were complete and that good progress was continuing in the actions planned within Performance Audit.

In August/September 2023 we carried out a root cause analysis in light of the 2022/23 staff survey findings on learning and development. The RCA was designed to get feedback from auditors on why they felt more support could be provided in delivering quality audits through learning and development.

The summarised results of the RCA and actions arising were discussed at Audit Scotland's Remuneration and Human Resources Committee at its meeting in November 2023.

The following table summarises the underlying causes of survey results identified from the RCA, the actions planned/taken and timescales:

Underlying cause	Action	Timescale
Learning activities are not scheduled appropriately (ASG only)	The Learning and Development Plan should specify learning activities throughout the year.	Initiated for the 2023/24 Learning & Development (L&D) Plan
	A schedule of events will be communicated for each quarter.	Quarterly L&D communication
	Timescales should be agreed with business groups on when training and materials and tools are required.	Project specific
Although colleagues like the availability of online materials, they miss the opportunity for discussion and questions	Where learning is delivered online or through videos, Professional Support and Learning (PS&L) will identify opportunities to support this learning through specific feedback and discussion sessions or attendance at Superteams.	Discussion sessions should aim to be delivered within 1 month of the related learning activity being available on the

Underlying cause	Action	Timescale
		Learning Management System (LMS).
Clearer presentation of an agreed audit approach with accepted interpretations. One example highlighted was the approach to revised ISA(UK) 315	The post implementation review of ISA (UK) 315 will look at lessons learned from the first year of implementing the new IT audit approach, and identify opportunities to further enhance the practical implementation of the underlying approach.	
Lack of time to attend learning activities.	It is important to set aside protected time for learning. The expansion of mandatory learning in the 23/24 L&D is the first step to helping protect time for learning	Expanded mandatory training included in 23/24 plan
Lack of clarity over what learning to focus on.	Development discussions should be used to identify and agree learning opportunities. Communications around the 23/24 3D process should emphasise the need to identify an individual learning plan. 3D participants should be encouraged to review learning needs and available materials in advance of 3D discussions	As part of communications on the L&D Plan (Sept/Oct) and 3D (performance review and development) process (Jan)

The results of the 2023/24 staff survey on quality were summarised in the 2023/24 Quality of Public Audit in Scotland report. The survey results showed that staff continue to be supported to deliver high quality audit work through training and development provision by audit providers. Results at Audit Scotland have improved from 54 per cent in 2022/23 to 62 per cent in 2023/24. This improvement follows actions taken from previous internal cold file reviews to provide guidance and training to auditors on aspects of the Audit Scotland Audit Approach alongside a more structured learning and development programme.

We remain committed to delivering high quality learning and development opportunities and support for our colleagues and the recently updated learning and development plan was published in August 2024.

We hope the above information is helpful. Please contact us if we can be of further assistance.

Yours sincerely

Stephen Boyle
Auditor General for Scotland
and Accountable Officer

Professor Alan Alexander
Chair