



OFFICIAL REPORT
AITHISG OIFIGEIL

Scottish Commission for Public Audit

Wednesday 18 December 2024

Session 6

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SCOTTISH COMMISSION FOR PUBLIC AUDIT 2nd Meeting 2024, Session 6

COMMISSION MEMBERS

- *Colin Beattie (Midlothian North and Musselburgh) (SNP) (Chair)
- *Jamie Greene (West Scotland) (Con) (Deputy Chair)
- Daniel Johnson (Edinburgh Southern) (Lab)
- *Richard Leonard (Central Scotland) (Lab)
- *Mark Ruskell (Mid Scotland and Fife) (Green)

*attended

THE FOLLOWING ALSO PARTICIPATED:

- Vicki Bibby (Audit Scotland)
- Stephen Boyle (Auditor General for Scotland)
- Colin Crosby (Audit Scotland)
- Stuart Dennis (Audit Scotland)
- Martin Walker (Audit Scotland)

LOCATION

The Adam Smith Room (CR5)

Scottish Commission for Public Audit

Meeting of the Commission

Wednesday 18 December 2024

[The Chair opened the meeting at 11:15]

Decision on Taking Business in Private

The Chair (Colin Beattie): Good morning, everybody, and welcome to the second meeting in 2024 of the Scottish Commission for Public Audit.

The first item on the agenda is a decision on whether to take agenda item 3 in private. Do we agree to take that item in private?

Members *indicated agreement.*

Audit Scotland Budget Proposal 2025-26

11:15

The Chair: Our next agenda item is to take evidence on Audit Scotland's budget proposal for 2025-26. Members can find a copy of the budget proposal, along with the covering letter from the Auditor General, in paper 1 of the meeting papers.

I welcome to the meeting Stephen Boyle, Auditor General for Scotland; Colin Crosby, chair of the Audit Scotland board; and, from Audit Scotland, Vicki Bibby, chief operating officer, Martin Walker, director corporate support, and Stuart Dennis, corporate finance manager. I welcome Colin Crosby to his first meeting as chair.

I invite Colin Crosby and then the Auditor General to make short introductory statements.

Colin Crosby (Audit Scotland): Thank you, everybody, for your time today. As the chair has pointed out, I have recently been appointed to the post of chair of Audit Scotland and this is my first formal meeting with the commission, so I look forward to talking to you today and to working with you all over the coming years.

As with all public bodies and services, we are operating in the context of significant challenges and risks. The fiscal environment is the most difficult that it has been for decades. Put simply, public services are not sustainable without major reforms to the financial structures behind them and the ways in which they are delivered.

At the same time, the demands on and regulatory expectations for audit are increasing. For example, a knock-on effect is that Britain's corporate sector has seen audit fees almost double over the past seven years, and English local government bodies are facing a 9.5 per cent rise this year, after an increase of 150 per cent two years ago.

In that context, it is crucial that Audit Scotland delivers in three key areas. The first is the delivery of high-quality independent audit that provides assurance about public spending and probity, gives insights that drive improvement and acts as an early-warning system about emerging problems.

The second area is to ensure the effectiveness of public audit, not only now but in the long term. That way, we can sustain a high-quality service that adds maximum value to and positively affects the outcomes for and experiences of all Scotland's people.

The third area is to show leadership and play our part in the face of the financial challenges.

That means making sure that we are efficient and that we use our publicly funded resources as prudently and effectively as possible.

Our budget proposal seeks to strike a careful balance between enabling us to modernise, as we must, to continually improve and to maintain quality, while also managing risks and delivering efficiencies and savings where we can.

My closing comment is that the proposal, along with everything that makes up the proposal, has undergone significant scrutiny from Audit Scotland's internal systems and by my board during its development. I hope that you can see the rigour that is in it, and I look forward to your questions and the discussions today.

I will hand over to Stephen Boyle, the accountable officer for Audit Scotland.

Stephen Boyle (Auditor General for Scotland): Many thanks, Colin. Good morning, chair and members.

Over the past year, Audit Scotland has delivered annual audits of almost 300 public sector entities in Scotland, as well as performance audits on matters of significant public interest. Through our quality assurance regime, we know that we have continued to deliver high-quality work, while also improving our performance as an organisation. We have made significant progress in our multiyear programme to recover the timeliness of our audit delivery, which was interrupted as a result of the pandemic.

None of that is straightforward. As ever, I express my thanks to all my colleagues in Audit Scotland for their hard work and, equally, to the colleagues who work in the audit firms with which Audit Scotland contracts.

Colin Crosby has spoken about the need for balance that we look to achieve through the budget proposal. I hope that you will see from our submission and from this morning's discussion that we can assure you and provide insights on how we plan to modernise how we deliver public audit so that it is fit for the future, while continuing to deliver efficient and high-quality public audit.

You will see from our submission that our resource requirement for 2025-26 is £14.6 million, which is an increase of £1.4 million. The three key elements to that are our core costs, increased employer national insurance contributions and the funding that we are looking for from the commission to support our audit modernisation software.

We have managed to contain the rise in our core costs to 1.4 per cent. That is against the context of UK inflation levels of 2.6 per cent that were announced yesterday, together with our planned 3.8 per cent pay award in 2024-25 and a

4.2 per cent uplift in our costs through our contract with audit firms. A significant part of achieving that was through £2 million in efficiencies and savings by closely managing our costs and making strategic decisions in areas such as our office estate.

As with all employers, we have had to quickly assess the impact of the recently announced increase in national insurance contributions. Through this budget, we are asking for the Parliament's assistance to meet that unanticipated additional expenditure.

As members will know, we are modernising how we deliver public audit in Scotland. A key step in that will be the procurement of new audit software during 2025-26. Modernisation is a crucial element in ensuring that public audit is effective and sustainable in the longer term. By investing now, we will reap efficiencies and improvements in the medium and longer term.

Our audit modernisation proposal reflects a programme of work in that area that started in the past 18 months. As Colin Crosby has mentioned, there is an onus on us to reflect the challenges that are facing the wider public sector in Scotland in addressing fiscal pressures. Our proposal does that by looking at every area of our organisation where we can deliver efficiencies while maintaining high quality and modernising. Achieving that means that, in this budget proposal, we are looking to accept a higher level of risk than we have done in previous years. We are clear that there are mitigations and approaches to those risks, but we think that that is the right approach and one that all public bodies are grappling with.

As our chair said, we very much look forward to the discussion that we will have with the commission this morning and to answering your questions.

The Chair: Thank you for that opening statement. I will open up to members for questions, and I will bring in Mark Ruskell first.

Mark Ruskell (Mid Scotland and Fife) (Green): Good morning. I want to ask you about productivity, particularly in relation to the move from a 37-hour week to a 35-hour week. I suppose that it is a bit of a chicken-and-egg question. Have you been able to increase productivity to the point at which you feel comfortable reducing working hours to a 35-hour week, or do you think that a reduction to a 35-hour week will enhance productivity to the point that it is beneficial for your work in the organisation? I am interested to know about your decision making in that space and its relationship with productivity more generally.

Stephen Boyle: That is an important area. You will see peppered throughout our submission our approach to productivity and the dynamics of the

move to a 35-hour week. I will bring in Vicki Bibby, as she led much of our engagement with trade union partners in arriving at the proposal

I will speak first about productivity in more general terms. Productivity is not a nebulous factor, but is reflected in our results. We are seeing an increase in our audit delivery timescales, as we are progressing through recovery of audit deliverables, and Martin Walker might want to set some of that out for the commission.

All our national health service audits are on time and so are almost all our central Government audits. We are recovering the pace of delivery of our financial audits in local government, too.

Vicki Bibby can say more about the 35-hour working week. It will be a change in how we operate as an organisation—that is true. However, distilled down, that change will equate to 15 minutes a day for colleagues. It is very clearly a matter of significant importance for our colleagues and their trade unions in terms of their requirements of us as an employer, and it mirrors the move that many organisations will be taking, including the Scottish Government and, indeed, the Parliament, in due course. We understand that it is an important accommodation and right, and we must strike the right balance between the conditions that we offer our colleagues and how they translate into productivity.

I will bring in Vicky, because she has been involved closely in the issue.

Mark Ruskell: That is good. Vicky, can you say how that change relates to the staff survey work? Is there a package of other measures around that work that fits with the 35-hour working week? What impact will it have on the organisation?

Vicki Bibby (Audit Scotland): It is quite a complex dynamic, which we are very alive to. I will bring in a couple of points to cover what you are looking for.

We are on a 36-and-a-quarter-hour week, so we are not moving from 37 to 35 hours. The 35-hour working week will come in on 1 April. In our pay negotiations with the unions, they were very clear—it was for them a red line—that they would not agree a pay deal with us without the introduction of a 35-hour working week. We wanted to work with the unions on delivering that anyway, but it was a key factor for them in the pay negotiations. We think that we have negotiated a very fair package for our workforce.

With regard to that change, we also made clear in the discussions that it was to be cost neutral. We could not be in the environment of increasing our staff numbers to accommodate the loss of hours. A lot of internal discussion was required

about how that was going to be delivered. I say that it is a complex dynamic because we are also in the environment of recovering our audit delivery timescales, and we have to think about staff wellbeing as well. The purpose of the 35-hour working week is to increase staff wellbeing by giving staff more time, so there was discussion with the unions about the need to increase productivity.

We will have to carefully watch what happens. That is the position that we are taking. We are not bringing in any extra staff. As Stephen Boyle said, this is about 15 minutes a day, so we are looking at simple measures such as saying, “If you are to have an hour-long team meeting, could you make it 50 minutes and focus some rigour on ways of working that could help you manage that?”

Equally, we need to look at what that looks like for staff. We operate a flexi system, which enables us to see if there are extra hours being worked. We will closely monitor that, because we do not want to have a 35-hour working week but have staff balances increasing on the flexi side. We are working closely with human resources and the unions to monitor that, and we will need to see how it manifests.

We are feeling positive about the change. As we approach it, we think that it is a good thing. It is what our staff and the unions were looking for in order to increase wellbeing, and we are entering into it in that spirit. However, we will be closely monitoring it and do not want to be complacent.

Mark Ruskell: That is a useful answer. As you say, it is quite a marginal change—15 minutes a day. My team in Parliament operates on a 30-hour week, and that does put a lot of pressure on productivity.

I just wonder how that change and a package of other measures might impact on your recruitment and retention. You are projecting a 5 per cent vacancy rate. Is it difficult for you to pin down what the vacancy rate will be? Are you working towards bringing that down and towards an outcome where you are more competitive? It might be difficult to match the salaries in the private sector, but what is the attractive package that you can offer?

For somebody who has caring responsibilities, 35 hours a week is better than 37 but it is not 32; it does not take half an hour off of each day to enable them to pick up the kids or go and see an elderly parent.

I am thinking about people who are making career choices to go with you rather than the private sector and about bringing down the vacancy rate. Is the reduction competitive alongside other actions that you are taking? How does it impact your budget? That is a bit of a holistic question.

11:30

Stephen Boyle: I will start, and I am sure that Vicki Bibby will want to contribute as well.

I do not want to underplay the fact that, for us as an organisation, there is risk in reducing the working week, and benefits, too. As Vicki mentioned, our trade unions were absolutely clear about how important it was to staff wellbeing, primarily. It gives people the ability to juggle multiple responsibilities that they have in their lives beyond working in what we hope is a satisfying, dynamic place to work in Audit Scotland.

You can see from our proposal that we have increased the vacancy factor to 5 per cent this year. We have had engagement with the commission over the past couple of years about the right level for us. On the face of it, moving to a 5 per cent vacancy factor generates an efficiency saving at the start of the proposal. It is not an insignificant one—about £1.2 million. The point is that we have to deliver it, so we are bringing in some new arrangements—what we call a recruitment board—to support the delivery of that vacancy factor.

It has been absolutely clear that achieving that vacancy factor will involve slowing down to a degree the pace at which we fill vacancies. Some of that might happen organically. Many of the people whom we recruit will be on a three-month notice period and, when somebody who is leaving works their notice period for Audit Scotland, that never syncs equally with bringing in somebody else. That will be one factor to manage.

Broadly, the totality of the package that we offer people who work with us is competitive. Our turnover rates are not historically high and we are still able to bring people into the organisation at all grades, from the executive team to a successful trainee package. Typically, we do not compete in pure financial terms with what somebody might be able to earn in the private sector. However, with the shorter working week, together with the flexible working that Vicki Bibby mentioned and a significant public sector pension—defined benefit schemes are now rare in the private sector—we think that we offer the right balance of reward package that can help us to deliver that vacancy factor and, more fundamentally, still be an attractive place for people to stay working with us and join us in the years to come.

Vicki Bibby: Stephen Boyle covered all the key points that I would have made. I add that we work closely with other audit agencies across the United Kingdom on their packages and any recruitment issues that they have. The environment has been competitive.

Relatively, we are in a good place in Scotland. Our package is competitive, but, equally, we do

not want to be complacent about that, so we always keep an eye out. We are doing a lot of work on our future target operating model. We are looking at bringing in more graduates. We are pivoting around our school leavers programme and modern apprenticeship programme with an eye to the future. We are continually benchmarking against the private sector and other public sector employers in Scotland and at the UK level.

Mark Ruskell: Okay. I will stay with questions on productivity. You have identified one relatively minor best practice change within the organisation in relation to time. Will you take further actions in the next year to improve efficiency and productivity? We will come to questions about the audit modernisation project later, but can you point to anything else on productivity and efficiency that you are working on that benefits staff and helps them to do their jobs?

Stephen Boyle: Yes. Vicki Bibby might want to say more, and perhaps Martin Walker.

We are working to targets, which is the main thing. We are also benefiting from the fact that we are moving into the third year of the audit appointment cycle. By dint of that cyclical nature, we typically see more efficiency as auditors become more familiar with the public bodies, which benefits the pace of delivery and the depth and quality of reporting and auditors' findings.

Pace is most fundamental. The commission will be familiar with Audit Scotland's programme of phased recovery from the disruptive effect of the pandemic on the delivery of financial and performance audits—you may recall that, four years ago, we paused the performance audit programme, which severely impacted the timeliness with which we were able to deliver financial audits. We are on the right path with that.

Audit modernisation will be fundamental, but it is not the only factor. We are continuing to invest in learning and development for our colleagues, which naturally benefits productivity.

Our targets are there, and we are keen to chat about them. With regard to the investment that we are making in our colleagues and the throughput from it, for me, those are the headlines.

Vicki Bibby: One of the key factors for us in measuring productivity is the project to improve our resourcing model and bring in new software to allocate resources to and know the costs of audits. We are looking at that right across the organisation. That is a key function for us—to have the real data at each level in the organisation, to set productivity targets for each level and to know the true cost of each audit.

At the moment, our data is not as robust—or, rather, we have the data, but a lot of manual interventions are required to get that information, so we have quite a lag and we are not getting it in real time. That investment is key to giving us a better idea of our productivity. We are also working on a project with the National Audit Office on its levels of productivity so that, once we have the data, we can benchmark it and challenge where we are against that right level.

One of the other things around productivity is our impact reporting and work planning. The Auditor General and the Accounts Commission, with the team, regularly review which pieces of work will have the most impact. That is done more so on the performance audit side. We have a keen eye on opportunity costs: working on a certain project means that we are not doing something else. We are bringing cost information into all our audits, so that we have all the data to make decisions about productivity and impact.

Stephen Boyle: Mr Ruskell, I wonder whether I might bring in Colin Crosby, as he mentioned in his opening remarks the scrutiny of productivity that the board provides, which is a regular feature. Rather than me trying to persuade you that we are focused on productivity, the chair might want to do that.

Colin Crosby: Thank you, Auditor General. I am glad that you think that my powers of persuasion will be bigger than yours.

There are some interesting bits about productivity. Vicki has commented on the better data that is sought through the resource and management information software, which will go in in the next short while.

The board is, funnily enough, as vexed about productivity as your question would indicate that the commission is. There is an interesting perception, in the way that one speaks, that somebody comes in, starts auditing at 9 o'clock and finishes at the end of the day. However, meetings and training and all that kind of stuff—essentially non-audit work, but work, nonetheless—must be taken into account.

The board is seeking more and more clarity as to how efficient our training is. We might have allocated 18 days to it, but could it all be done in 15 days if we trained in a different way? Similarly, could meetings be shorter and sharper, and does everybody who is at a meeting have to be there? Are those members of staff who are working at the coalface getting the appropriate support to maximise the time that they are spending for the sort of productivity that you are referring to? What support can we put in to better streamline the other processes? That is work in progress. Colleagues, including the chair of the Accounts

Commission and the chairs of the HR and remuneration committees, are very hot on the subject, because they see the scope to improve that further. Fifteen minutes might well be a challenge, but we are actually looking for rather more than that in terms of the amount of time that can be driven towards the job in hand.

Mark Ruskell: That will obviously benefit staff as well. Thank you.

Jamie Greene (West Scotland) (Con): Good morning. You will be relieved to hear that I will ask my questions in two tranches and I will come back in later with the second tranche.

The first area that I will cover is basically about people. At the end of the day, audit work is about people, as much as we talk about automation and software. Let us look at some of your numbers. On page 12 of your budget proposal, you summarise the position on costs and you propose that your people costs will be £25.8 million for 2025-26. To give me an idea of how you perform against budget expectations, can you let me know what the result of last year's budget is likely to be for people costs? What I am looking for is what you thought you would spend on people in 2024-25 versus what you expect to spend, just to give me an idea of how on track you are with the budget.

Stephen Boyle: I am happy to do that. I will ask Stuart Dennis to share the precise detail with the commission. We had a session with our colleagues yesterday on our forecast; as we move into quarter 4 of the financial year at the start of January, we are focusing really carefully on that. There will be a degree of estimation in some of the numbers that we will share with you as regards where we think that we will land, but Stuart can set that out if we have that detail with us this morning.

Your overall premise is right, Mr Greene. People costs are the driver for Audit Scotland, given that 67 per cent of our costs relate to people, and that inevitably does not include the work that firms carry out on our behalf. Some 20 per cent of the remaining costs relate to firms, and that money is for people as well, so getting that right is fundamental.

I will bring in Stuart Dennis to track the extent to which we are on target.

Stuart Dennis (Audit Scotland): Good morning, everyone. As you can see, in the table that Mr Greene referred to, the people costs for 2024-25 are £24.6 million. The current projection, which is based on the information that we have, is that we will have an underspend in the region of £300,000 against that. We still have another three months to go and the figures will reflect turnover, so the costs could get a bit higher, but we are working with a projected £300,000 underspend.

Jamie Greene: When was the £24.6 million adjusted? How does it match up with what you forecast at the beginning of the financial year that you would spend on people?

Stuart Dennis: The £24.6 million figure is exactly the same figure that was put to the commission this time last year, so there is no real change in the people costs budget. The column is called “Adjusted Budget”, but that is mainly to take into account the adjustments that are required for leasing and things. It becomes a more transparent process whereby you can compare like with like, but the people costs did not change.

Jamie Greene: Okay. I presume that any underspend on people costs at the end of the financial year is set. There is no rolling over of budget for people, for example.

Stephen Boyle: We have no provision to retain any underspends from one year to the next. Any underspends in Audit Scotland’s budget will be returned to the consolidated fund.

Jamie Greene: That is interesting, bearing in mind what we are looking at for next year and you asks there. I presume that the increase includes year 2 of the pay deal that was agreed, which involves an increase of 3.8 per cent. However, does it include or exclude the national insurance contribution increases? I presume that they were not factored into your initial projections for 2025-26.

11:45

Stephen Boyle: You are quite right: 3.8 per cent is the increase in the second year of the two-year pay deal that we agreed with our trade union partners. It was 4.2 per cent in the first year. As we refer to in our proposal, that mirrors the arrangement that the Scottish Parliament reached with its colleagues.

As I mentioned in my introductory remarks, the national insurance increase for employers was not one that we had anticipated as we compiled our budget. I will bring in Stuart Dennis to say why we have sought to ring fence that, rather than make any assumptions. That is primarily for transparency, but also because of the engagement that we have had with the Scottish Government finance directorate, with which we liaise as part of the preparation and submission of Audit Scotland’s budget, which the Parliament considered in the round as part of the draft budget proposal.

Jamie Greene: You have come to the table asking for a 10 per cent increase overall, which is substantial. I am trying to break it down into the constituent parts to make it easier to scrutinise. A big chunk of that is the national insurance

contribution. I am trying to find out why Audit Scotland felt that this was the mechanism to try to recuperate that money.

Stephen Boyle: It would be helpful for Stuart Dennis to set out our engagement with the Scottish Government on what feels like a live issue in terms of the negotiations and engagement between the UK Government and the Scottish Government on the extent to which the increase in national insurance contributions will be funded, either in totality or partly. With that level of uncertainty, and until we have clarity, our view, which was supported by our board, is that NICs should be kept as a separate item for engagement with the SCPA today.

The national insurance increase equates to an additional £520,000 on our cost base. We have options. In the event that the Parliament chooses not to support our proposal, our only other options would be to reflect that in fee increases or, on the other side of the balance sheet, reflect it in our cost base by doing something differently in how we deliver our audit work—to vary the pace and so forth.

I will bring Stuart in. It would be useful for the commission to hear about not the direction that we have had from the Government, but the steer or engagement that we have had about how we best reflect that in our proposal.

Jamie Greene: Sorry to interrupt, but when you answer, I would really like to hear why you have chosen not to go down the fee increase route.

Stuart Dennis: Our perspective is purely a transparency perspective. It is quite easy. If we went down the fee route, we would obviously have to increase our fees, which would then be just under 3.5 per cent more than what we have in the report.

The approach that we have taken, through the board and its scrutiny, is based on what the impact is to Audit Scotland. Although in the grand scheme of things, the cost is not a lot, it is a lot to Audit Scotland. If NICs are costing us more, what is the impact of the increase in employer national insurance to Scotland as a whole? We could absorb that cost by increasing fees, but I expect that the bodies that we charge the fees to would not be getting an uplift in their grant or funding to cover that. That is why we took that route this year. It was basically to say, “This is an extra pressure and we really need funding for it.” It is a more transparent approach to say, “This is what the cost to Audit Scotland will be for this,” and we feel that that should be reflected in the funding. In my discussions with the finance director at the Scottish Government, they were content with our approach.

Jamie Greene: In your opening statement, Auditor General, you said that you audit 300 public bodies. Half a million pounds spread across hundreds of bodies would not be a huge cost increase for them, would it? Is that not a fairer approach? Ultimately, it is a pass-on cost. Again, there is a slight domino effect to all of this, and we do not really know where all those things will land in the next couple of months. However, it is not as if you are turning up at a public authority and asking for hundreds of thousands of pounds per authority, for example.

Stephen Boyle: You are right. There are options. As Stuart Dennis and I have set out, our preference is that that would be funded from the consolidated fund, given the uncertainty of it all. There is additional complexity, in that audit fees are not chargeable for all the audits that we undertake, so we have to map through all those arrangements as well.

We thought that we had got ourselves to a reasonable and stretching place in the core fee increase of 1.9 per cent. That was below inflation, a bit lower than where we had been in previous years on fee increases for public bodies—as the commission will recall—and lower than the pay award. I recognise stretching targets in the efficiencies that we have touched on to an extent. In the absence of clarity and detail from the Scottish and UK Governments on how that would be funded—Stuart Dennis has mentioned what it might mean, and there will be variability within sectors and we cannot cross-subsidise within sectors—this was our preference for the funding model from the consolidated fund. However, I do not deny that there would be alternative options, if that was the commission's preference.

Jamie Greene: Audit firms will incur increased national insurance costs for their own staff. Is that factored into the increase that you have agreed with them for the work that they undertake, or will there have to be an NIC increase over and above what you have agreed?

Stephen Boyle: Vicki Bibby might want to say more, but it is not our understanding that that will be an additional fee for the audit firms. We have a five-year contractual model with the firms that we appointed for the start of the 2022-23 audit year. The contract prices are inflated by Audit Scotland's pay award—which will be 3.8 per cent—and it will be for firms to absorb the NIC increase in their own cost base.

One slight caveat, if it is helpful, is that the prices vary over and above that figure for any other material changes, such as a new auditing standard that is required to be reflected. We would have to engage with the firms on such things, but it is not our understanding that employers' NICs will be a separate addition.

Jamie Greene: Something else that struck me about that table on page 12 is the staff projections. Please do not take this in any way as a criticism, but it jumped out at me. For the years 2024-25, 2025-26, 2026-27 and 2027-28, you have projected pretty much the same number of staff. It is very unusual in an organisation to have such certainty, year on year. In addition—maybe this is a question for the board—does having the same numbers of people scream of efficiency and productivity improvements? Do you suspect that the volume of work will be the same? Will you need more people to do more work, because of the change in working hours? I am trying to get my head around this, because it strikes me as such an unusual forecast in a big organisation.

Stephen Boyle: There are various factors. You are right—I am sure that the chair will want to comment, as will Vicki Bibby, who has led some of the thinking on our target operating model, which you have mentioned.

There are a lot of variables. As has been mentioned, there is an opportunity to discuss further the audit modernisation approach. Part of that—not the first phase—is that we expect that the application of artificial intelligence will change how we deliver our audit work. We see that already in the wider profession. Audit Scotland is already adopting aspects of audit automation. We have spoken with the commission previously about our ability to look at vastly increased numbers of transactions. Although we will still sample test—auditors will still go out to test samples of transactions—we anticipate that, before very long, and as we do in some audits already, we will be able to drill down, in a way, across a population.

The staff projections are our best estimate of what our people requirements will be. Those are quite short term—2027-28 is not terribly far off for us—and take us only to the first year of the new audit appointment arrangements.

Before I bring in Vicki Bibby and Colin Crosby, I want to mention the other variable, which is that the number of bodies that we audit is changing. This year, we will audit at least two new public bodies, one of which is Zero Waste Scotland. Yesterday, we heard that we will also be the auditor of the Scottish pubs code adjudicator, which is a small body, but all such bodies still require an audit.

The numbers point to an emphasis on productivity. To an extent, we can absorb such additional work as a result of some of our efficiency models. I hope that that answer is helpful as a starter.

Vicki Bibby: We want to flatline at a relatively high level, recognising that there is growth in

demand for what we do. We do not want to be linear—as we audit more bodies, we want to keep the cost base down. It would be a bit of a crude assessment to take a high-level look at whole-time equivalents. We are looking at our target operating model, which is linked to our business plan. We might replace a more senior post with a junior post and pivot where we have our workforce. Having that link with our business planning is where we want to get to.

As the audit modernisation project develops, we will need different skills. In some areas, we might need fewer auditors but more data analysts. We want to be able to break that down at different levels and different grades. We have information about where we want to be in our target operating model. That is very much linked with our audit modernisation work. The world is changing and, like every other organisation, we want to be on the front foot and to look at our skill set.

Colin Crosby: I think that that is my cue to state where the board is on that. Vicki Bibby has covered a number of the points, but although we have a flat number for staffing, there will be movement in what those staff will do over the next period of time. As the commission is aware, a number of staff members are delivering the audit modernisation project. One could see a situation in which, at the end of that process, we could repeat the question and ask what they would do then, but the reality is that there will be an on-going level of change, which will be managed to enhance the efficiency of the audit process.

The board is on a drive to have more productivity and efficiency, but it is also conscious that there is a moving feast from the point of view of the number of audits that are being done, the complexity of those audits and the public's appreciation of what an audit should comprise. In a changing world, there is a need to combine all those elements. You can ask, "How can the staff numbers be static?", and we could ask exactly the same question. However, in order to deviate from that static position, we would have to be able to predict, 24 months ahead, that we would need more or fewer people.

Vicki made a point about the staff mix. Over time, the private sector has realised that it needs more people at a more senior level to discharge the work, because more judgments are being made. Therefore, the model will change over time. That will not necessarily reduce the cost, because we will have more expensive people who are better skilled to make the judgments that are now being called for.

Your observation was absolutely correct. We are dealing with a moving situation. The flat position on staff is a best guess over a relatively short period of time. That will be constantly

reviewed by the board, because we are keen for more efficiency to be achieved. Why do I say that? That is one of the benefits of having non-execs on the board. They are quite hawkish about this. They are very supportive, but they are quite hawkish, I think.

12:00

Jamie Greene: Good—so they should be.

That is very helpful. I appreciate that there are a number of moving parts, and that complexity makes it difficult to take a snapshot in relation to a budget ask and present it in that way. For future years, it might be helpful to get a snapshot of those moving parts in order to see, for example, how the average salary is changing and to get a feel for the number of people that you have and, relatively, how much that costs.

In effect, year on year, you come back to ask for more money for people. That seems to be off the back of annual pay rises as opposed to fluctuations in the types or number of people that you have. The other side of that is marrying that up with the type of work that you are doing and the implementation of automation and AI, for example. I am looking for more of a medium-term strategy, rather than this annual snapshot that we seem to get. However, perhaps that is for another session on another day.

I am glad that modernisation has been mentioned a few times, because I want to talk about that. I have a specific question on this year's budget ask. Apart from national insurance contributions, the biggest chunk of your 10 per cent year-on-year increase relates to your request for £672,000 for audit modernisation. Why is that a people cost? The commission assumed that that would be a cost for consultancy, an agency, software or development work or some form of pre-implementation cost, but that budget line seems to be a cost for people. Why is that?

Stephen Boyle: I will clarify that. The figure of £672,000 is to meet the development and implementation costs of the replacement audit software. In our submission to the commission, we sought to show where that is going in terms of cost and impact, which you mentioned in your earlier question. That is our best estimate because, inevitably, it will be quite a complex information technology project. We need the right level of programme management, which is part of our delivery costs, so that we have the right skills to deliver, and support the implementation of, Audit Scotland's most fundamental change programme of the past 10 to 15 years. In the budget submission, we have set out where we think that that money—the £672,000 for 2025-26 and a

further £1,544,000 across 2026-27 and 2027-28—will go.

I am looking to see whether any of my colleagues wants to comment on the figure of £672,000.

Vicki Bibby: Those are revenue costs. We are not going down a capital project route of buying something in; the costs will be the licensing costs for the development of what we are doing. The people costs are largely being absorbed in our budget—Colin Crosby spoke about us pivoting some of our resources. The costs are linked very much to the costs of working with the other national audit agency, procuring its software and the implementation process. It is a revenue cost—not a capital cost.

Jamie Greene: In essence, you are saying that your current cost estimate for the modernisation project is about £2.2 million—that is a back of a fag packet analysis—and you are splitting that over three financial years, with the first tranche being an ask of £672,000 for next year and an expectation of £1.5 million over the following two years' budgets. Is that correct?

Vicki Bibby: That is correct.

Jamie Greene: How reliable is that estimate? With the greatest respect, public bodies do not have the best track record in forecasting budgets for software and modernisation projects. I am concerned that, although £672,000 this year is a big chunk, you might be loading the costs towards the end of the project and that, in a year or two, we will find that you come back to ask for £2 million or £3 million, because the cost of the whole thing has just ballooned.

Stephen Boyle: Given the organisation that we are, and noting that we have reported many times over the years on unsuccessful IT projects in other public bodies, we are very alert to that risk, and we do not want to find ourselves in a place where we have not successfully anticipated costs or timescale drifts, or where we do not have the expertise.

It might be helpful to set out some of the safeguards that we have so that we do not find ourselves in that place. We have assurance arrangements through the board, and we have what we call a strategic improvement board, which oversees progress with the project. We have had an internal audit review of our arrangements, and we have engaged the Government gateway process, where the Government brings in technical experts to assess our intentions and pace and whether we have got it right. We have gone through all those processes, and I suggest that the figures and timescales that we are presenting are robust.

We are following the Treasury guidance on the delivery of projects, which captures whether we have the right or wrong pitch in terms of optimism bias. As you will know, Mr Greene, with many projects, people can assume that they will be in one place—particularly the owners of the project—so as to get it off the ground, but that may not transpire. We have tried to capture all the variables and risks and to present them to the executive governance arrangements and our Audit Scotland governance, so that we are projecting in the right way.

We have some strong certainty that our preferred model is to partner with the National Audit Office—and Vicki Bibby might want to say a bit more about that. That avoids leaving us at the mercy of a tender exercise. Our engagement with prospective suppliers could suggest one thing, but the tender price that arrives might be materially different. We broadly know what it will cost as we engage with the National Audit Office, which has been very supportive and accommodating. I express my thanks to the NAO for the engagement that we have had so far.

Vicki Bibby: Stephen Boyle has covered a lot of the governance aspects that I would have mentioned, so the only thing for me to add is that we have got some certainty, as the project is not a capital project: we are not building something ourselves; it involves software and licensing. The NAO has been through all that, so we have a bit of certainty there.

The risk that comes with the project lies in the implementation timescales, and we want to monitor that closely. We cannot hold reserves for funding projects. We are relatively certain and confident about the totality of the funds over a three-year period, but the questions are around what the risk will be, monitoring whether we are on track for implementing the project within the timescale and how the costs fall across the three financial years. The gateway reviews have been really helpful and very positive, and they have usefully highlighted areas that we need to examine to ensure that we are on track.

Jamie Greene: I guess that it is important not to look at the project through the prism of a single-year ask. Even though we are talking about just the first year of that three-year spend and the money is being spread out, you are essentially asking for sign-off of the whole project. We have spoken a lot about how much the project will cost and how much you need to do it, but we have not heard a huge amount about what comes out the other end. What are the savings involved? We probably do not have time to go into all that today, so I will park that there.

I would like to see a breakdown of the overall cost, particularly the £670,000 for this year, to

understand the terminology of “resource” versus “capital” and so on. In providing that, you could perhaps paint a rosier picture of why spending £2 million on modernisation will save money down the line.

Stephen Boyle: I will bring in our chair, who will be keen to set out some of that. We will present a clear picture of that. In fact, I am happy to come back to the commission in writing with more detail on the analysis of the anticipated cost of the audit modernisation project, if you would find that helpful.

To manage expectations ever so slightly, I should say that we do not have a strong or fundamental expectation that the project will, at its heart, be a cash-releasing programme of investment. It is more about readying Audit Scotland for the future, so that we can continue to deliver what we believe to be high-quality, impactful audit work on behalf of the Parliament and the people of Scotland. The further out we go, the more variables there are. The pace of the development of technologies such as artificial intelligence is likely to mean that what we have anticipated today could be different in three to five years' time.

I hope that, with the commission's support, we will be in a place where we can invest incrementally in technology, in a way that we have not done previously. I could show you some of the systems that we are operating, which are at the end of their lives. That means that we are not equipping the people who deliver public audit with the tools that they need to continue doing so. Manual interventions are required and, as Vicki Bibby said, we are not getting the information that we need to run Audit Scotland as efficiently as we would like to.

Lastly, before I bring in Colin Crosby, that system is also increasing our cyber risk. There is no panacea, but one thing that really attracted us to the partnering arrangement with the NAO was that it is readying the system so that it can be developed over time, with a bolt-on for artificial intelligence. We have really been playing catch-up and think that that would allow us to move to a place where we can keep pace as we invest.

I am certainly keen to share some of our underlying information with the commission and will be glad to do so.

Colin Crosby: That is a difficult topic to cover and I note that Stephen Boyle has volunteered to come and attempt to talk about the full scope of that at a different time.

From the board's perspective, there are a few strands to the audit modernisation project. It is going through the Government gateway process at the moment, which I will come back to. It has also

gone through an internal audit process regarding how it has been procured, and we have had an offline deep dive into AI audit and assurance best value in all sorts of guises. The board has been instrumental in that to ensure that it fully understands the issue.

Somewhat unfortunately, I was number 1 in the recent gateway review process. I thought that I would be last and could sweep up, but I actually had to be on the front foot. One interesting issue is that the single biggest risk in all of this is not the software but the process of change that will have to take place following implementation. That is why there is a significant people part to the process—it is because we are changing entire ways of working.

Stephen Boyle spoke about obsolescence. As I understand the position at the moment, at a simple level, a previous year's audit cannot be used to self-populate the following year's audit with a heap of standing information. If one changes the practice, there is significant scope to save time in setting up the next audit, which leads to Mr Ruskell's comments about efficiency.

There are whole processes in that but, by and large, processes need people to buy into them. Change is welcome in some quarters but not in others, so one really has to deal with those who do not welcome it, because you need the totality of colleagues to come on board. In some ways, the software part appears to be less costly than the people part in the totality of the project.

The board has been very keen to ensure that we are not doing this as a stand-alone purchase or—even worse—development of software. We wanted to find working models where, if it made sense for procurement purposes, we could partner with others, so that they, and not us, would take the heat of the software cost.

I hope that we can combine all that with flexibility and things such as AI. There is scope for the whole process of sampling to be done away with, in time, and for us to get to 100 per cent review of transactions using automated systems. You can then identify the exceptions, so that you spend more time dealing with those than sampling, which in some ways should improve the quality. That is when you need judgment. It is where you begin to get the total change, from a situation in which somebody does the sampling to produce a set of data to a situation in which the data appears and you then interpret it.

12:15

Getting to that point over the next two or three years is a complex project, and the board is keen to get it done faster than the team wants to do it, because we do not quite see why it should take so

long. There is pressure to get it done quickly, but we are very conscious that, if you do it quickly, it could fall over, because of a reluctance to change. Therefore, we have to moderate the pace to ensure that everybody is taken with us as we go along.

Why do I take time in doing this? Because it is the background, and we have to distil it down into a budget so that the commission can go through it line by line and say, "Why is this and why is that?" There is quite a lot of thought going on, which the board is involved with, and there have been a number of deep dives. The project has been through various committees, all in a pretty challenging way—at least, I hope that the team think that it has been a challenging way, but constructively so. We are fully committed to doing it, because it will improve the audit product.

Jamie Greene: That is much appreciated—thank you.

Richard Leonard (Central Scotland) (Lab): I want to pick up a couple of loose ends from the previous two rounds of questions. Of course, our job is to challenge, so, for the record, I note that not all of us believe in the inevitability of downsizing as an approach, and I think that you have described why there are times when you need to expand and reshape the skill sets that you have. Your responses on that have been very useful for us as a commission to understand what is happening with your overall staffing cost.

Stephen Boyle: Thank you, Mr Leonard. Mr Greene has pointed out, quite rightly, that, with the best information that we have, and given the volume of variables that we are operating with, we are anticipating a static workforce in the organisation.

However, the variables are significant. Artificial intelligence might bring downsizing, but, equally, as our chair has mentioned, it might require us to bring in different types of jobs—Vicki Bibby touched on data analysts and so forth. The pay and grading of those jobs is to be confirmed, because the market will dictate that. Audit Scotland operates in a market in which people can move quite readily to other public bodies or firms, so we have to pitch ourselves at the right point.

The other variable that you might want to explore, which I am happy to do, is what our roles and responsibilities will be in public audit in the years to come. Climate change, specifically, might very well require a different contribution from Audit Scotland as we move into the 2030s and 2040s; the progress that the public sector in Scotland makes towards net zero might require Audit Scotland to start to do different things. That will be a further variable. However, the estimate that we

are presenting to the commission is the best estimate for today.

Vicki Bibby: In our workforce planning and target operating model, we are considering whether we need more specialists in certain areas such as climate change, and we know that some of the other audit agencies have done that. We are also considering where we can partner—for example, we might not need to bring in a specialist if we have a reciprocal arrangement. There are opportunities to garner from linking in with the NAO, which is a much bigger organisation, through our audit modernisation project.

On our overall workforce, we take quite seriously our role as a public sector anchor institution. We have been increasing our budget for modern apprentices, for example. There is quite a lot of pivoting within the numbers. I am very happy, as Mr Greene requested, to give you more detail in the future.

Richard Leonard: Thank you. Again, that will be helpful in informing our decision making today, which, after all, is to decide whether or not to agree your budget.

There is a second point that I want to make, following the questions that Mark Ruskell asked. An old trade union organiser thought went through my head—do any of the staff who you employ work on contracts that provide for them to be paid overtime?

Stephen Boyle: As an organisation, we do not pay overtime. As Vicki Bibby has mentioned, we have had flexible working for at least 20 years, and flexitime has been the model through which people can claim back time when they have worked beyond their contracted weekly hours.

Richard Leonard: Okay, that is fine. It is just that we were talking about the potential exposure to risk and the importance of us challenging the model that you are describing, and I just wanted to understand that point. I acknowledge that you have given a categorical reply.

Stephen Boyle: If you will allow me to develop the point slightly, one of the things that we are focusing on across the piece is striking the right balance between delivery and wellbeing. That has been a recurring theme over the past five years or so, particularly during the pandemic. The management team looks closely at annual leave and flexi balances, and we have taken a couple of steps to encourage people to get the right balance by using their annual leave and not accruing significant flexi balances that become unmanageable.

Notwithstanding Vicki Bibby's well-made point about our management information not being brilliant, we look closely at that issue, and we have

seen a real downward trajectory over the past year, with a reduction in unused annual leave and lower flexi balances.

Richard Leonard: I am glad to hear it.

I will move on from staffing issues to other areas. In your proposal document, there is a section headed “Other operating costs”. In that section, you itemise what you call the “main areas of movement”—by “movement”, I think that you mean “increase”. I want to probe some of the areas that you have highlighted.

You talk about “Resource system implementation”. Forgive me if you covered this earlier, with a different descriptor, but could you perhaps tell us a little bit more about what that work is and how it is being delivered? Is it being delivered in-house? Is it externalised? Are you bringing in people to do that through an outsourced model? If you could begin by telling us what it is, that would be helpful.

Stephen Boyle: I am delighted to do so. That is our organisational response to the topic that we have just touched on. We do not have good enough information, and we do not have the necessary tools to deploy people on audits. Somewhat regrettably, we are still using spreadsheets to allocate people and teams to different audits.

We have known about the need to resolve the issue for many years, but we never quite got the right solution off the ground. For the past couple of years, we have been engaging with other audit agencies in the UK and speaking to audit firms about what we can learn and what the right solution for Audit Scotland might be. We have created a project under the banner of internal governance to give it the right structure and scrutiny, and, as part of our productivity and efficiency thinking, we have looked to procure a system to support the delivery of a way to better deploy people in the organisation.

Vicki Bibby might want to say a bit more about this, because we are at a pivotal moment in the project. We are in the throes of work on contracts, so there might be some boundaries to what we are able to set out for you this morning. However, the intention is that Audit Scotland equips itself with a system that allows us to deploy people much more efficiently and successfully than we can currently.

Vicki Bibby: The project is absolutely complementary to our audit modernisation. We are treating it as a separate project to manage it in the context of the enormity of audit modernisation. As we have raised with you before, our cost information is based on audit days—that is, on the number of days that it takes to deliver an audit. The cost of a day of an audit director is different from the cost of a day of an audit junior. To get

that information, which is important in order to understand the costs of audit, as well as charging, a lot of manual intervention is required. That means that, when we get the information, there is quite a lag time. Therefore, we want a system that links in with our people system and our flexi system and which gathers the information that we need in order to set a budget for an audit and then be clear about what the gross resource allocation is. At the moment, an audit director’s time is involved in allocating staff to audits, which we believe is quite inefficient, so we want a system that will do it. This is very much a spend to save.

We wrote to the commission previously about how the pension reduction that we had in the budget would fund the project for three years. After that period, however, we will have on-going licensing costs, which will be self-funded through the efficiencies of staff being taken away to fund the on-going project. We very much see it as a spend to save that is necessary for efficiency.

Richard Leonard: Okay, and you have systems in place to make sure that it is delivering value for money.

Vicki Bibby: Yes.

Richard Leonard: There is some kind of governance system that has oversight.

Stephen Boyle: Absolutely. It is one of the two or three projects that we are running—audit modernisation is the largest one—that are subject to on-going scrutiny by what we are calling our strategic improvement programme board. There are regular reports on progress and our Audit Scotland board is also informed of that.

We think that we have the right oversight of the project. Most fundamental to that is value for money; with the right rigour, we will not progress with a project, regardless of how tempting it is, if it is not going to deliver value for money.

Richard Leonard: Let me move on to another area that crops up in the “Other operating costs” section of your proposal, which is an expectation that, certainly compared to two years ago, you are looking at a significant increase in legal fees. Can you explain the occasions that Audit Scotland requires to procure legal support externally? What areas do you take legal advice on?

Stephen Boyle: I am happy to start on that, but Stuart Dennis might want to say a bit more beyond my thoughts on how we go about doing that and in what type of circumstances.

As auditors, we work in a legislative environment. We often have to explore whether a piece of legislation applies to a public body and whether that body has complied with the legislation. At times, that rubs up against the boundaries of our expertise, so we take guidance

on our roles, responsibilities and powers. Sometimes, in very specific examples, we will take guidance on particular parts of the act that govern us. Our access to information can also be a pinchpoint at times, so we have taken advice on that.

You might see one other aspect of some of our legal and professional work in forward projections—the work that we do in the national fraud initiative will also be captured under the broad heading of legal and professional fees.

That is a general reflection, but it is a feature of our work that we need to bring in the advice of others at times. Is that fair, Stuart? Do you want to add anything?

Stuart Dennis: Not really. We have a legal framework for the four legal firms that we deal with. We put the work out to them, and it varies. We will need guidance in respect of, for example, the estates strategy and leases and contracts, and we will ask for advice on human resources. As well as the audit side of things, we would also need them for the core operational things.

In addition to professional fees, we have an occupational health contract that is due for renewal, and that is related to staff and contractor wellbeing. We have that provided as an external support. Those are just natural increases as part of the contracts that we work with.

Martin Walker (Audit Scotland): It is worth noting a few other things. We are a relatively small organisation, so we do not have in-house experts in certain fields—we do not have a legal team. Lawyers are not employed directly by Audit Scotland. All those legal services are drawn down from that contract arrangement that Stuart Dennis talked about.

In the projections for the year ahead, we are also bearing in mind a couple of the projects that we have just been talking about and recognising that, when it comes to setting up memorandums of understanding and the licensing arrangement for the audit modernisation project and so on, it is important to get those things right, so part of the costs that we are talking about is also related to that kind of stuff. It is very much a range of different sources, as has been said, but I thought that those were two other things worth mentioning this morning.

12:30

Richard Leonard: Again, that is helpful. Stuart Dennis alluded in passing to the estates strategy. In previous years, when looking at the budget, we have discussed your plans to change the distribution of your staff—where they work from and so on. In broad terms, that was about

reducing the head count and your footprint in Edinburgh and increasing those in Glasgow. You say in your submission that that has netted savings overall. Therefore, are those savings still on track and how is the estates strategy going?

Stephen Boyle: We are really pleased about where we have reached. We have completed the project to modernise our estate in our Edinburgh and Glasgow offices. As you rightly point out, we are about half the size that we were in our Edinburgh office and we have, as it were, moved that capacity to Glasgow in the existing office building, which will result in efficiency savings of £281,000 over the course of the years to come. It has been a successful project for the organisation, which gives us an estate that allows us to be a flexible organisation.

People are still working remotely, but our offices are being used appropriately when they are needed. We have changed the number of our team meeting facilities. It is about striking the right balance. We do not have a desk for everybody, if everybody wanted to turn up at the same time, but that reflects how we operate as an organisation. People are still working the length and breadth of Scotland, delivering public audits. We have retained our office in Inverness and our base for colleagues in the north-east of Scotland, which uses Aberdeenshire Council facilities. That all gives us the right modern facilities but, appropriately, it also generates some cash efficiencies.

Vicki Bibby: On the positives, one of our key things is that, as a training organisation, we want to ensure that we bring staff in to be together and to learn from each other. That has proved to be really successful, particularly in the Glasgow office. On the demographics, our staff complement in the west is a bit younger, and those staff probably work more on the financial audit side, so teams are coming into the office to work together, and they have a really good space to do that in, which is a really important part of people's work experience and training for learning.

Stephen Boyle: I should probably mention—this possibly speaks to the point that Mr Ruskell raised earlier—that these developments demonstrate our physical investment in the environment that people are working in in Audit Scotland. That will serve us well in relation to the people who are already with us, but it will also show prospective hires that the organisation will continue to invest in training and development and it demonstrates the general learning and work experience that people get.

The Chair: In paragraph 41 of your paper on page 10, you talk about “another UK public audit agency”. What is that agency?

Stephen Boyle: It is the National Audit Office.

The Chair: You propose to use its audit software as part of the modernisation process.

Stephen Boyle: Yes, that is correct.

The Chair: There will be some software development, which I presume will be the bulk of the cost, although you say that there are minimum system requirements. Where will the data reside?

Stephen Boyle: First, you are right that the cost will be mostly for software licences. We were very clear that we did not want to go down the route of developing the system, because that brings enhanced risk and additional cost as well as timescale issues. Martin Walker mentioned some of the advice that we are taking. We have a very good relationship with the National Audit Office and we are partners in the Public Audit Forum. However, this is still a commercial transaction, so we need to ensure that the contracts are properly structured and that the memorandum is drafted effectively. Part of that covers the data.

The most important thing, which Vicki Bibby might want to talk about, is that Audit Scotland meets its obligations, so we will control the data for the audits that we are undertaking.

The Chair: Therefore, the data will reside in Scotland.

Stephen Boyle: Yes. We will own that data, and we as a public body also have data retention obligations, which mean that we must retain data and audits for seven years. We will ensure that that is properly reflected, not just in the custom and practice but in the legal underpinning.

Vicki Bibby: Although we are using the NAO's system, it is not passing on its sunk costs in terms of what it has invested in developing in the system. It recognises that it is part of the public sector. However, we are working with a third-party provider on the process of taking that system and implementing it in Scotland. Therefore, the system will be licensed, but it will be our own system that we will use as we would have used it, had we procured it from someone else. That is why we have the third-party arrangement. We can provide more detail on that, but the NAO will not hold and own all our data.

The Chair: Does the licensing arrangement include upgrades? The NAO will not be standing still—it will be constantly upgrading its system—so will we benefit from that?

Stephen Boyle: Yes, absolutely. One of the key attractions of the arrangement was that the system will evolve—we have touched on artificial intelligence, for example. Audit Scotland can move at the same pace as the NAO, or at the pace that

is appropriate for us, through the system's development and implementation.

On your previous point, chair, I should, for absolute clarity, say that this is a cloud-based system, much like all new systems these days, which means that we are not investing in new data servers and so forth to store the information. We touched on that in response to Mr Greene's line of questioning. However, access to and security of that information are clear issues, and we are keen to come back to you in writing with more detail if that would be helpful.

The Chair: With the licensing, is there a contractual period of, say, five or 10 years? How do you envisage that working?

Stephen Boyle: Vicki Bibby might want to say more about the specifics of the contractual arrangement, which we are still working through, but as I have mentioned, the arrangement is attractive to us as it allows us to move at a pace of evolution over the years to come. With this proposal, we have set out investment over a three-year period, but I hope that I can be clear with the commission that, having gone through a period of not investing in our digital estate to deliver our audit work, we are moving to a more reasonable position or expectation that this will be a period of on-going investment. That investment might not be at the scale that we are setting out for the next three years but, as we move to that modern public audit provision, we will need to continue to invest in our IT capability in a way that we have not done in years gone by.

The Chair: What other systems did you evaluate?

Stephen Boyle: Vicki Bibby might want to set this out, but we looked at a range of alternatives and engaged with a number of providers in this environment, and we assessed them against the criteria of functionality, cost and so forth, before arriving at our preferred option of partnering with the National Audit Office. We might not be able to go into the detail of that in public session, but we are happy to share it, as appropriate, with the commission.

Vicki Bibby: The team looked at a lot of options. We engaged with the other national audit agencies—not just the NAO but some of the private sector firms. The big four, for example, invest a lot globally in developing their own systems. We were clear with the board at the start that going down the route of developing our own system would be quite risky, because of the need for on-going development and the associated costs.

The NAO took a number of years and spent millions developing its own system, so it was attractive to join in with it, because that work had

been done. We could not join in with one of the big four firms, as they would not be able to do the same thing. The other option was off-the-shelf packages, which do not lend themselves to the needs of public audit.

The team undertook a lot of investigation work on the options and reported to the board. That is why the board agreed to go with the NAO.

The Chair: Staying on the same page of your document, I have a question about paragraph 48. I am always a bit nervous when I see savings being made by reducing the contingency budget. How big is that budget?

Stephen Boyle: The contingency budget in the current financial year is £500,000.

The Chair: So you have halved it.

Stephen Boyle: Indeed. You might remember that, with the SCPA's support, Audit Scotland increased its contingency budget around the time of the Covid-19 pandemic, in light of the volatility of the environment in which we were all operating and the fact that we are not able to hold reserves. That gave us a sufficient buffer to deal with unexpected matters that came our way during the financial year.

Given where we are in the cycle, although halving the contingency budget increases our risk—I am clear on that—it also feels like an appropriate step to take so that we are clear on top of our cost base what efficiencies we can offer. The proposal that we have come to is to reduce it by half.

The Chair: I guess that I am being simplistic, but you asked for an increase in the contingency budget, which you received. However, you are now offering half of it back as a saving.

Stephen Boyle: The move to £250,000 broadly reflects where Audit Scotland was over the longer term. It is more reflective of the contingency that we need to operate, given how we are structured financially. We cannot run a deficit in any year. There is a degree of volatility about the progress of our work and the income recognition that goes alongside work in progress, so halving that budget feels broadly like the right context for us. There is a pay dynamic, too, but Vicki Bibby might want to say more about that.

Vicki Bibby: The larger contingency helped us over the recent period of more volatile pay settlements. Because such settlements were annualised, we did not quite know what they would be, and, indeed, they have been above inflation.

Do not get me wrong: I would like a larger contingency but, after reflecting on where public services are and wanting to ensure that we play our own part in that, we felt that we could absorb

some of the risk, because we have settled ahead of the year. We know that there will be a 3.8 per cent pay increase, and it has been built into the budget. In previous years, our budget just contained assumptions for pay, and, because in those years the settlements were above budget, we used the contingency to absorb them.

The Chair: For my last question, I come back to the audit modernisation project and how it will be paid for. All audited bodies will benefit from a successful roll-out of the project, but why has Audit Scotland not shared its overall resource requirement for 2025-26 across all audited bodies? There is an argument that, because you have not done so, central Government and sponsored bodies are cross-subsidising other parts of the public sector's audit fees. I know that you are conscious of that issue; indeed, in the past, we have had discussions about avoiding it.

Stephen Boyle: I am glad that you have raised that issue, chair, because you are absolutely right. We are clear—and the legislation is such—that we do not cross-subsidise between different sectors. That has been a theme of discussion with the SCPA in previous years, when we looked at some of the fee increases and how we arrived at them.

In the longer term, the benefits will evolve and change. Broadly speaking, we do not currently anticipate that the audit modernisation project will be a significant cash-releasing programme—we will see. The pace of change might result in significant change to our cost base. However, I think that, at the moment, we are adopting the right balanced approach, which is that modernisation will allow us to become a more effective and impactful organisation and to better respond to some of the changes in auditing standards and so forth. That is broadly our central premise for the audit modernisation project.

12:45

Vicki Bibby: This was a significant discussion at the executive team and with the board. As the investment phase peaks over the next three years, we wanted those costs to be clearly ring fenced and transparent, and we wanted to ask for central funding for them. Once we have finished implementation and are purely on the recurring licensing, we will want to build that cost into our core audit fee model. However, we want pump priming for the investment bit.

Again, as has been said, I am happy to provide more formal information on this, but as far as efficiencies are concerned, I should point out that the trajectory of audit costs is quite steep—there is quite a significant increase. Therefore, we do not anticipate significant cash savings, but we will not be on the sort of trajectory that we have seen in

the profession of 9 per cent, 14 per cent or even 150 per cent increases, as has been mentioned. We are reducing the baseline when it comes to the costs, so we think that after three years we will be able to baseline the licensing fee and include it in our fees. However, for the three years of the investment, we want to be transparent on ring fencing and on asking for central funding.

As Stephen Boyle has said, and as is the case with national insurance, we could build different options into fees now. However, in coming before you today, we felt that this was our preferred proposal.

Colin Crosby: Chair, in a previous forum, the point was succinctly put that what we were doing in the first stage was infrastructure and that, as such, it was partly about the need for Audit Scotland to be able to service both Scottish Government and non-Scottish Government audits. Once we are through that phase, the costs will be distributed among all the parties, which will pay fees in the appropriate way. The board is content with that.

The Chair: Thank you. I am conscious of time but members can come in if they have a brief question.

Jamie Greene: I had been saving up this question for when we came on to the fees issue, but I note that a third of your auditing is undertaken by external firms. I appreciate that you have a multiyear deal with them and that you are obliged to increase their fees to you—by 4 per cent this year, if I am not mistaken.

Stephen Boyle: That increase has been put in place with reference to the Audit Scotland pay award as the uplift from one year to the next.

Jamie Greene: That follows on nicely from the chair's line of questioning with regard to your passing on the uplift in fees, which is much lower than what you are being charged by external companies. What is the strategy in that respect? For example, given that a small handful of very big companies perform the lion's share of such audit work, is there a risk that, in future, they might simply not bid for it in light of the relatively low margins for such work or the nature of the bodies that they are required to audit?

Stephen Boyle: Yes. That is a very live issue for us as we move into the next phase of public audit. Generally, we operate to a five-year cycle; in addition to the requirements of the underpinning legislation, the Accounts Commission and I produce a code of audit practice, which sets out our requirements of auditors that carry out public audit and which goes alongside the procurement of audit services. We are starting the next phase of that programme now and are looking at the future of public audit in Scotland.

We will engage in much more detail with the SCPA and the Public Audit Committee over the course of 2025, but there are signs that the market for public audit in Scotland will become more challenging for firms in the years to come. For that view, we are drawing on some of the experience elsewhere in the UK and the fact that some firms that currently provide services to us have pulled out of other markets, not just for public audit but for audit entirely.

Therefore, we do not have certainty on providers or price yet. Of course, we have a fallback, which is that Audit Scotland could do all the work if it so wished. However, that would require investment and growth in the number of people working for Audit Scotland. We need to weigh all of that up, but we will absolutely be going through that rigorous process over the next 12 to 18 months.

Jamie Greene: Could Audit Scotland provide better support to small and medium-sized auditing firms in Scotland that are more localised to their clients and which are spread across your four geographic office areas? After all, four very big international companies are soaking up huge amounts of public money here.

Stephen Boyle: Both points are true. We operate with six providers, so we have appointed some medium-sized firms. I can assure you that, last time round, we actively sought to encourage additional bids from small and medium-sized accountancy firms. Indeed, I think that the chair of the board has a strong perspective on the matter, too, if you have time to hear it.

We will absolutely be doing the same thing this time round, too, but I recognise that there are barriers to entry and opportunity costs in providing public audit—you have quite rightly homed in on that. What we can pay to carry out public audit can be matched and, in some cases, bettered by the fees for providing private audit services, so there will be a trade-off in that respect. We want to cast our net wide; most fundamentally, we want to marry affordability and quality, and that will be the driver as we go forward with the programme.

Colin Crosby: As Stephen Boyle has mentioned, the process of doing the next code of audit practice has just kicked off, and the board is, quite correctly, involved in that work. There is significant challenge, not in the sense of hostility but in how we slice and dice the audit market. The perception is that public audit is nothing but public audit under the rules and regulations, and that applies to a certain part of the work. Indeed, that is in itself quite a specialised piece, because there are completely different rules for public audits and accounts as opposed to those in the private sector.

However, I should point out that the portfolio ranges from banks to Scottish Water, which is a quasi-FTSE company, through to charities, which are another specialist area. For Audit Scotland to expand into all those areas, we would have to recruit people with the skill set to do that; however, we would perhaps not have the amount of work that was needed to keep a particular sector fully skilled.

When I attended one of the annual planning meetings, I saw that there was a trade-off here, because there are skill sets that informally lie with the private sector and skill sets that informally lie with the public sector. However, both can come together quietly, to an extent, to exchange experiences and skills.

It is not a given that Audit Scotland cannot do that work, but I think that there is a projection somewhere that shows that we would need to employ another 100 people to perhaps not do the work as well as parts of the private sector would. It is not a black-and-white situation, but it is under review.

The Auditor General also mentioned earlier that there are people out there who might be even better skilled at doing, say, a green audit than a conventional auditor would. The point is that everything about how this is done is open for examination.

The Chair: If no other members have any brief questions that they want to ask, I thank Colin Crosby, the Auditor General, Vicki Bibby, Martin Walker and Stuart Dennis for their evidence this morning.

We now move into private session.

12:54

Meeting continued in private until 13:09.

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