



## Care Inspectorate

Annual audit report 2014/15

September 2015

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This report will be published on our website after it has been considered by the audit committee. The information in this report may be used by Audit Scotland in any reporting to the Scottish Parliament.

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# Key Messages

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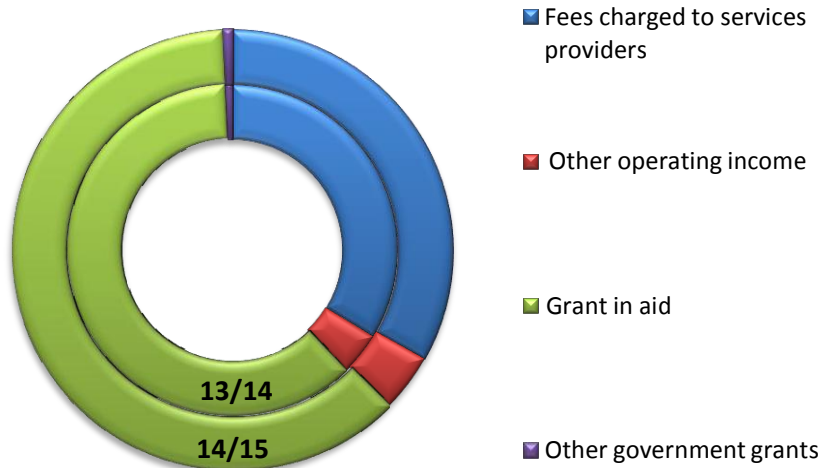
<p>Audit of financial statements</p>	<ul style="list-style-type: none"><li>• Unqualified independent auditor's report on the 2014/15 financial statements.</li><li>• Working papers were of a high standard and officers provided excellent support which enabled the audit team to complete on-site fieldwork by the planned target date.</li><li>• Only presentational and disclosure adjustments required to the financial statements presented for audit.</li></ul>
<p>Financial management and sustainability</p>	<ul style="list-style-type: none"><li>• The Care Inspectorate operated within its resource budget for 2014/15.</li><li>• The financial position remains stable. A balanced budget of income and expenditure is projected for a 3 year period to 2017 based on continuing Scottish Government funding.</li><li>• The Care Inspectorate faces a challenge to keep operating costs within its budget in the medium to long term.</li></ul>
<p>Governance and transparency</p>	<ul style="list-style-type: none"><li>• Overall we found that the Care Inspectorate had sound governance arrangements.</li><li>• Systems of internal control operated effectively during 2014/15.</li><li>• The register of interests extends to all Care Inspectorate board members and is renewed annually.</li></ul>

# Introduction

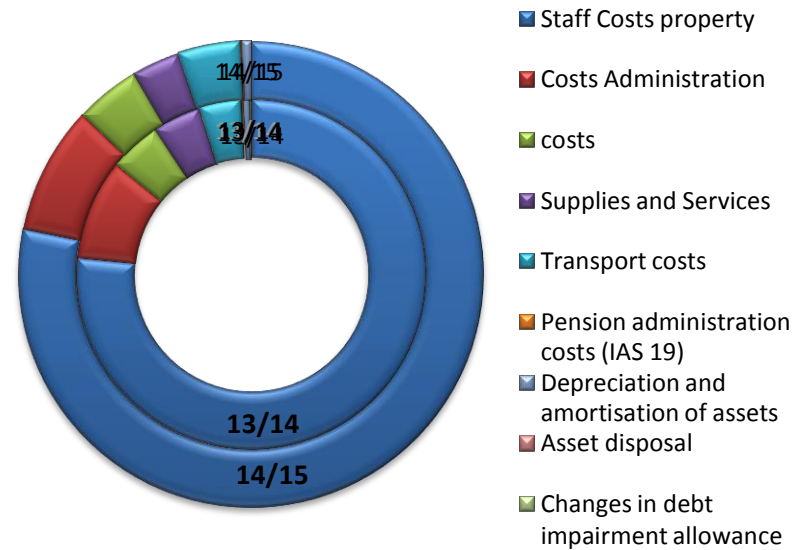
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1. This report is a summary of our findings arising from the 2014/15 audit of the Care Inspectorate.
2. The management of the Care Inspectorate is responsible for:
  - preparing financial statements which give a true and fair view, in accordance with the relevant financial reporting framework
  - ensuring the regularity of transactions, by putting in place systems of internal control
  - maintaining proper accounting records
  - preparing and publishing with their financial statements an annual governance statement and a remuneration report
  - preparing consolidation packs.
3. Our responsibility, as the external auditor of the Care Inspectorate, is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.
4. An audit of financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements; that have been prepared by management with the oversight of those charged with governance. This does not relieve management of their responsibility for the preparation of financial statements.
5. A number of reports, both local and national, have been issued by Audit Scotland during the course of the year. These reports are summarised at [appendix II](#) and [appendix III](#).
6. [Appendix IV](#) is an action plan setting out our recommendations to address the high level risks we have identified from the audit. We recognise that not all risks can be eliminated or even minimised. What is important is that the Care Inspectorate understands its risks and has arrangements in place to manage these risks. The committee should ensure that they are satisfied with proposed action and have a mechanism in place to assess progress and monitor outcomes.
7. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures; consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.
8. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

### Income/ Funding £35.8m (£35.2m)



### Expenditure £38.0m (£36.6m)



The financial statements show that income and Scottish Government net funding for 2014/15 was £35.824 million, an increase of £0.600 million (1.7%) from 2013/14. Expenditure increased by £1.4 million (3.7%) to £38 million in 2014/15. Staff costs within the expenditure for 2014/15 includes the impact of IAS 19 actuarial pension valuation adjustment of £2.189 million.

# 2014/15 financial statements

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## Financial Statements

- The financial statements of the Care Inspectorate for 2014/15 give a true and fair view of the state of the body's affairs and of its net expenditure for the year.
- We confirm that the financial statements have been properly prepared in accordance with the 2014/15 FReM and the requirements of the Public Services Reform (Scotland) Act 2010.

## Regularity

- In all material respects, the expenditure and income in the financial statements were incurred or applied in accordance with applicable enactments and guidance.

## Other prescribed matters

- The remuneration report to be audited has been properly prepared in accordance with the requirements of the Public Services Reform (Scotland) Act 2010.
- The information in the management commentary is consistent with the financial statements.

### Submission of financial statements for audit

9. We received the unaudited financial statements on 26 June 2015 in accordance with the agreed timetable. The working papers were of a high standard and the staff provided good support to the audit team and we completed our fieldwork on 5 August 2015. Next year will present a specific challenge due to the significant changes outlined at paragraph 22.

### Overview of the scope of the audit of the financial statements

10. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual Audit Plan presented to the Audit Committee on 18 March 2015.
11. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken any non-audit related services. The 2014/15 agreed fee for the audit was set out in the Annual Audit Plan and, as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.
12. The concept of audit risk is of central importance to our audit approach. During the planning stage of our audit we identified a number of key audit risks which had the greatest effect on the audit strategy, resources and effort. We set out in our

Annual Audit Plan the audit work we proposed to undertake to secure appropriate levels of assurance. [Appendix I](#) sets out these significant audit risks and how we addressed each risk in arriving at our opinion on the financial statements.

13. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

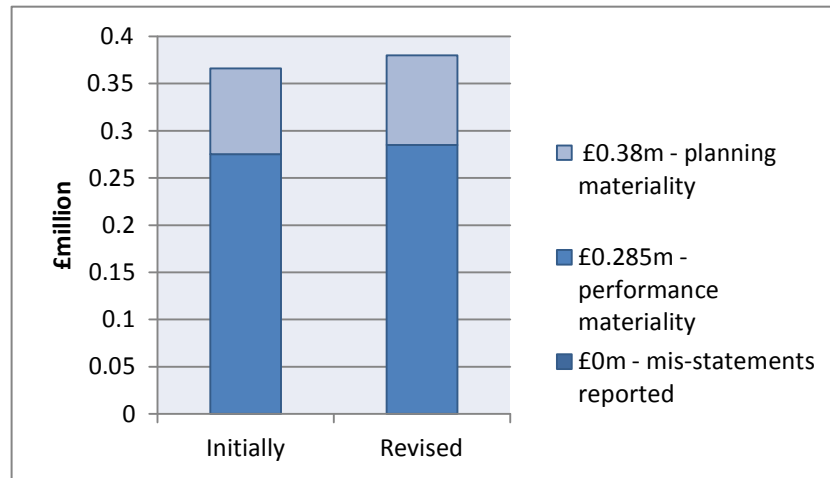
### Materiality

14. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other qualitative reasons (for example an item contrary to law).
15. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
16. We summarised our approach to materiality in our Annual Audit Plan. Based on the unaudited financial statements, we revised our planning materiality for 2014/15 to £0.380 million (1% of gross expenditure). Performance materiality of £0.285



## Audit of the 2014/15 financial statements

million is determined to ensure that uncorrected and undetected audit differences do not exceed our planning materiality level. We report all misstatements greater than £4,000.



## Evaluation of misstatements

17. There were no misstatements identified during the audit which exceeded our misstatement threshold. Therefore, no amendments have been made to the financial statements which impact upon either the net expenditure for the year or the net assets position at 31 March 2015.

## Clearance process

18. The issues arising from the financial statements audit were discussed with the Head of Finance and Corporate

Governance at a meeting on 6 August 2015.

## Significant findings from the audit

19. International Standard on Auditing 260 requires us to communicate to you significant findings from the audit:
  - the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and disclosures.
  - significant difficulties encountered during the audit.
  - significant matters arising from the audit that were discussed, or subject to correspondence with management.
  - written representations requested by the auditor.
  - other matters which in the auditor's professional judgment, are significant to the oversight of the financial reporting process.
20. There are no significant findings from the audit that we require to bring to your attention. However, it should be noted that the Care Inspectorate was unable to obtain the pension details for one member of the Executive Team. As a result, a footnote has been added to the relevant table in the remuneration report to highlight that this information could not be obtained from the Tayside Pension Fund.

## Audit of the 2014/15 financial statements

21. We recommended a number of changes to the presentation of the management commentary and remuneration report in the financial statements due to changes in the 2014/15 FReM. The recommended changes have been processed by management and there are no unadjusted misstatements to report.

### Refer Action Plan no. 1

## Significant findings from the audit in accordance with ISA260

22. There are no issues or audit judgements that, in our view, require to be communicated to you in accordance with ISA260.

## Future accounting and auditing developments *Revisions to the Financial Reporting Manual (FReM)*

23. The financial statements are prepared in accordance with the Government financial reporting manual (FReM). Two significant revisions will apply from 2015/16:
- Simplification and Streamlining Project – changes to the form and content of the annual report and accounts.
  - Adoption of IFRS13 *Fair value measurement* for the first time – this also includes IAS 16 and IAS 38 adaptations.
24. **Restructuring of the annual report and accounts:** the 2015/16 FReM has been extensively re-written to require the annual report and accounts to include:

- a performance report which will give a fair, balanced and understandable analysis of performance and will include an overview section and a performance analysis section.
- an accountability report incorporating the following three main sections:
  - corporate governance report consisting of a directors' report, a statement of the Accountable Officer's responsibilities and a governance statement
  - remuneration and staff report which will cover a number of prescribed disclosures including remuneration policy, payments to directors, staff numbers and sickness absence rates
  - parliamentary and accountability report which will include information on the regularity of expenditure and the independent auditor's report.

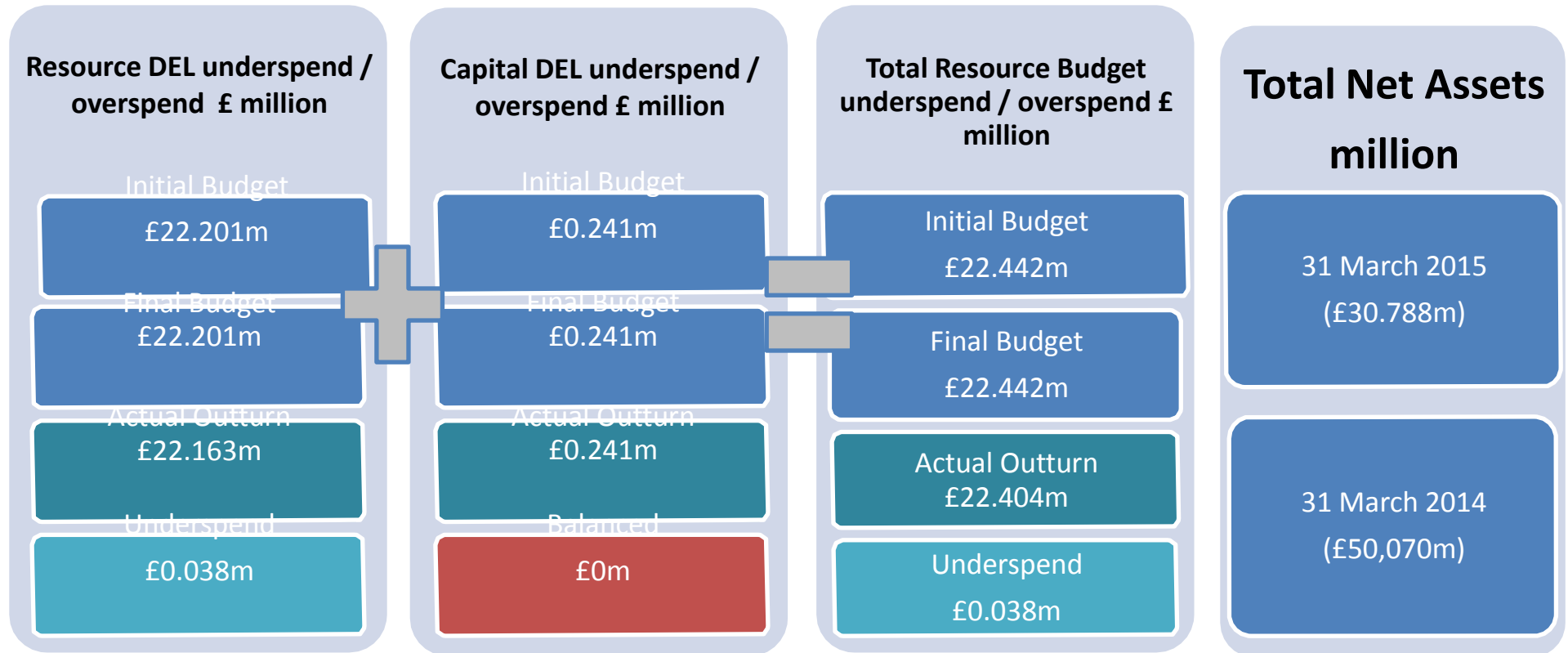
### Refer Action Plan no. 2

25. **International Financial Reporting Standards - IFRS13 Fair value measurement:** sets out the requirements for assets to be valued at fair value and is applied in full by the FReM only to assets that are not held for their service potential (i.e. investment properties and assets held for sale). It also applies to operational assets which are surplus to requirements where there are no restrictions on disposal which would prevent access to the market.

## Audit of the 2014/15 financial statements

26. IFRS 13 does not apply to operational assets which are in use delivering front line services or back office functions, and surplus assets with restrictions on their disposal. These will be valued in accordance with the adaptations to *IAS (International Accounting Standard) 16 property, plant and equipment*.

# Financial management and sustainability



## Financial management and sustainability

27. The main financial objective for the Care Inspectorate is to ensure that the financial outturn for the year is within the resource budget allocated by Scottish Ministers.
28. The Scottish Government sets a resource budget for the year for the Care Inspectorate which originates from the spending review settlement and is subsequently approved in the Budget Bill. During the year, any revisions are approved in the autumn and spring.
29. The Care Inspectorate received a total final resource budget of £22.442 million for 2014/15 which was internally split between revenue (£22.201 million) and capital (£0.241 million) as detailed above.
30. Spending on operating costs was within the final budget set, mainly as a result of in-year expenditure monitoring where budget adjustments, slippages and efficiencies have been used to balance within the overall allocation. We have concluded that the Care Inspectorate budget setting and monitoring arrangements are satisfactory, and we noted that senior management and the Board received relevant monitoring reports timeously.
31. The target level of efficiencies to be achieved by the Care Inspectorate in 2014/15 was £1 million. This was a challenging target when set against an existing background of extensive use of shared services and a high uptake of collaborative procurement opportunities over the years. For the period 2014/15, the Care Inspectorate has internally reported

efficiency savings of £1.368 million which can be regarded as a positive outcome for the year. Savings have mainly arisen from:

- estates rationalisation
- procurement
- pulse system administration
- staff savings

32. The financial position of the Care Inspectorate remains stable with the body operating within its available funding (on an accounting and resource basis).

## Financial management

33. As auditors we need to consider whether bodies have established adequate financial management arrangements. We do this by considering a number of factors, including whether:
  - the Director of Corporate Services and Head of Finance and Corporate Governance have sufficient status to be able to deliver good financial management
  - standing financial instructions and standing orders are comprehensive, current and promoted within the body
  - reports monitoring performance against budgets are accurate and provided regularly to budget holders
  - monitoring reports do not just contain financial data but are linked to information about performance

## Governance and transparency

- members provide a good level of challenge and question budget holders on significant variances.
34. Our review noted that the Director of Corporate Services and Head of Finance and Corporate Governance have sufficient status to deliver good financial management to the Care Inspectorate.
  35. Our review of the Care Inspectorate's financial regulations concluded that they are comprehensive and current. The financial regulations are available on the website.
  36. Regular reporting on budget monitoring and key performance indicator updates are provided to relevant board and resources committee members on a regular basis throughout the year.
  37. Based on our accumulated knowledge, our review of board papers and through our attendance at committees we conclude

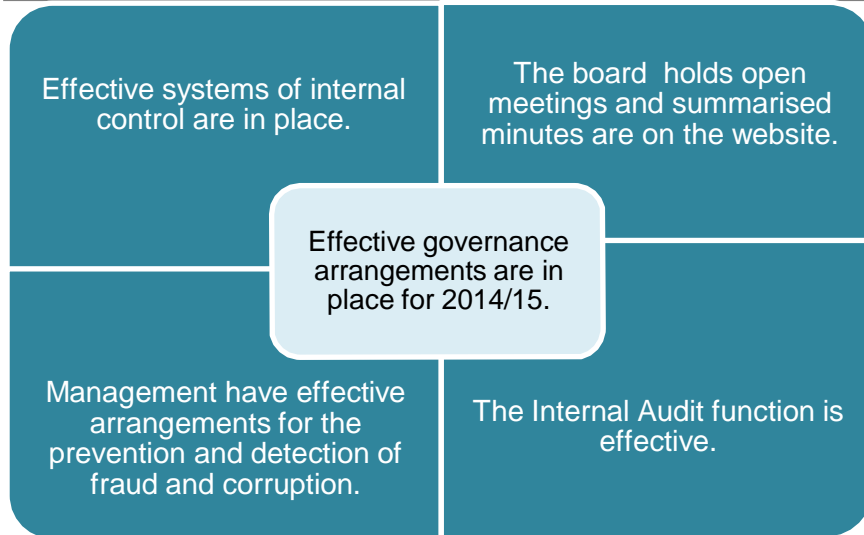
that the Care Inspectorate has strong financial management arrangements in place.

## 2015/16 and beyond

38. The Care Inspectorate's Scottish Government funding allocation for 2015/16 is consistent with the funding allocated in 2014/15. However, longer term efficiencies, budget reductions or funding increases are required to manage the anticipated budget deficits of £1.388 million (2016/17) and £2.099 million (2017/18). This a very challenging budget reduction target for the Care Inspectorate.

**Refer Action Plan no. 3**

# Governance and transparency



## Corporate governance

39. The board and Accountable Officer are responsible for establishing arrangements for ensuring the proper conduct of the affairs of the Care Inspectorate and for monitoring the adequacy of these arrangements.
40. The Care Inspectorate is managed by a board of non-executive directors and is accountable through the Scottish Ministers to the Scottish Parliament. The board's Chair and non-executives are appointed by the Scottish Ministers.

41. The board is supported in its role by the audit committee, policy committee and resources committee. The committees meet on a regular basis throughout the year to consider relevant matters.
42. The Care Inspectorate has effective overarching and supporting governance arrangements which provide an appropriate framework for organisational decision making.

## Transparency

43. The Scottish Government's "On Board" guidance (<http://www.gov.scot/Publications/2015/04/9736/0>), for board members of public bodies was updated and reissued in April 2015. On Board states that boards should demonstrate high standards of corporate governance at all times including openness and transparency in decision making. It recommends boards should consider:
  - holding an annual open meeting
  - holding board meetings in public unless there is a good reason not to
  - publishing summary reports and/or minutes of meetings
  - inviting evidence from members of the public in relation to matters of public concern

## Governance and transparency

- consulting stakeholders and users on a range of issues
  - making corporate plans and the annual report widely available.
44. Audit Scotland advocates in transparency of financial reporting within the annual report and accounts including:
- a clear reconciliation between expenditure and the outturn against Scottish Government Resource budgets.
  - identification of, and explanation of, any significant movements in budget during the year.
45. The Care Inspectorate makes available a range of information on their website, such as the Corporate Plan 2014/18. While we acknowledge that there are aspects of meetings that are confidential and sensitive in nature, the Care Inspectorate's board meetings are open to the public and summarised minutes are made available on the website. Overall we conclude that the arrangements in this area are soundly based.

## Accounting and internal control systems

46. While auditors concentrate on significant systems and key controls in support of the opinion on the financial statements, their wider responsibilities require them to consider the financial systems and controls of audited bodies as a whole. However, the extent of this work should also be informed by their assessment of risk and the activities of internal audit.
47. No material weaknesses in the accounting and internal control

systems were identified during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

48. Internal audit is an important element of the Care Inspectorate's governance structure. In the interests of an efficient audit approach we also rely on assurances received from the auditor of the Scottish Government on work performed on the Scottish Government central systems that are used by the Care Inspectorate. This approach ensures we are delivering an efficient co-ordinated audit that avoids unnecessary duplication and expense.
49. The central systems assurance letter provided by the auditor of the Scottish Government provided unqualified audit opinion on the financial services assurance report.
50. As we have raised in previous years, the project to implement Pulse, the Care Inspectorate's payroll and human resources information system, continues to have ongoing system development issues. These issues affect the implementation of specific human resources modules which would help to ensure benefits realisation of the new system is achieved.

**Refer action plan No. 4**

## Internal audit

51. Internal audit provides the audit committee and accountable officer with independent assurance on the overall risk



## Governance and transparency

management, internal control and corporate governance processes. We are required by international auditing standards to make an assessment of internal audit to determine the extent to which we can place reliance on its work. To avoid duplication, we place reliance on internal audit work where possible.

52. Our review of internal audit concluded that the internal audit service (provided by Scott Moncrieff) operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place. Therefore, we were able to place reliance on the following reviews during 2014/15:

- business continuity
- corporate planning
- efficiency savings
- performance management
- payroll
- shared services.

## ICT audit

53. ICT is a key area of control because it underpins all systems used by the Care Inspectorate. As part of our planning process we carried a high level review of ICT covering a number of areas. There is one area of improvement required relating to business continuity management. The Care

Inspectorate has made good progress in developing their business continuity arrangements and staff training and physical and desktop testing of the plans have now commenced. We plan to review progress with management during 2015/16.

## Arrangements for the prevention and detection of fraud

54. We assessed the arrangements for the prevention and detection of fraud during the planning phase of our audit. This involved reviewing the Counter Fraud Strategy, Counter Fraud Policy, Fraud Response Plan and Whistleblowing Policy and Procedures. We conclude that there are effective arrangements for the prevention and detection of fraud.

## National Fraud Initiative in Scotland

55. The National Fraud Initiative (NFI) in Scotland is a counter-fraud exercise led by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different financial systems, to identify circumstances (matches) that might suggest the existence of fraud or error

56. Auditors are required to assess the arrangements that bodies have put in place to prevent and detect fraud, including how they approach the NFI exercise itself.

## Governance and transparency

57. As part of this year's NFI exercise, the Care Inspectorate submitted payroll and creditors data to the Cabinet Office. However, no NFI matches have been received to date for further investigation. As a result, we will monitor the Care Inspectorate's progress during 2015/16 in following up NFI matches.

### Arrangements for maintaining standards of conduct and the prevention and detection of corruption

58. The Care Inspectorate has in place a range of activities designed to maintain standards of conduct including Codes of Conduct for officers and members.

59. An area of good practice undertaken by the Care Inspectorate relates to board members completing register of interests' forms. This process would highlight where there may be a potential conflict of interest and is updated annually.

60. Based on our review of the evidence we concluded that there are appropriate arrangements in place for the prevention and detection of corruption and we are not aware of any specific issues that we need to record in this report.

### Acknowledgements

61. We would like to express our thanks to the staff and members of the Care Inspectorate for their help and assistance during the audit of this year's financial statements which has enabled us to provide an audit report within the agreed timetable.

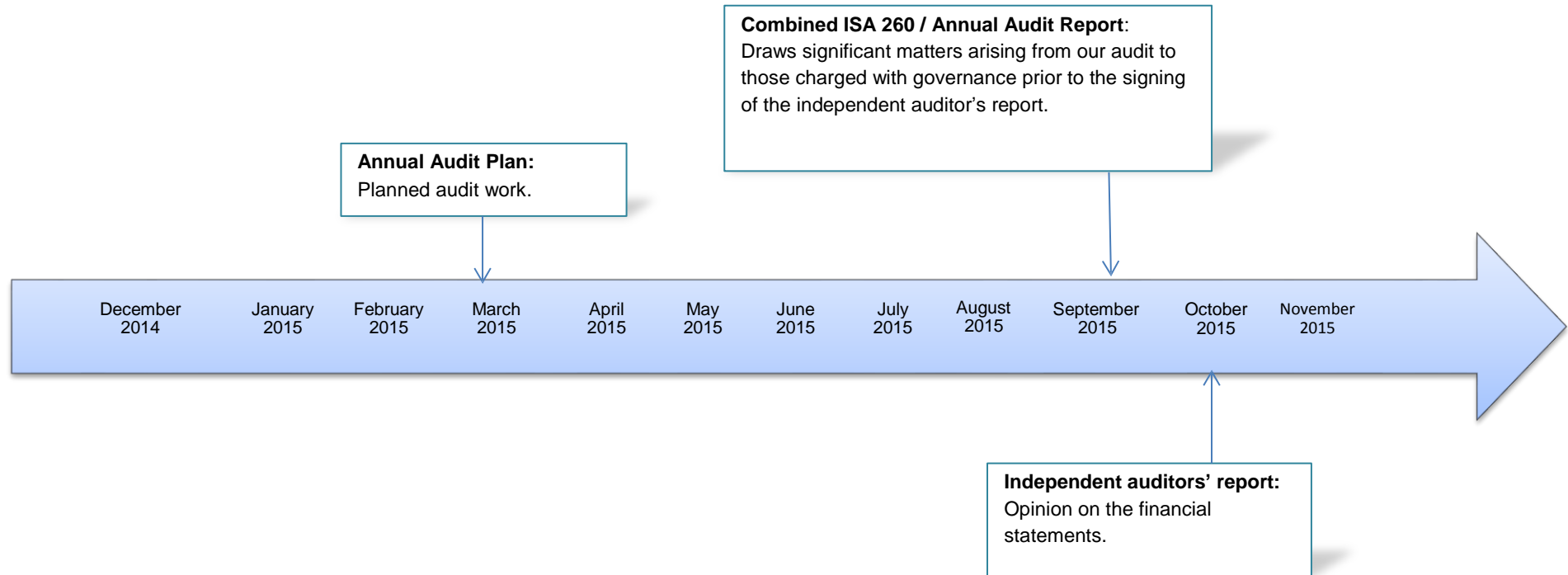
## Appendix I – Summary of local audit reports

The table below sets out the audit risks, how we addressed each risk and our judgement in arriving at our opinion on the financial statements.

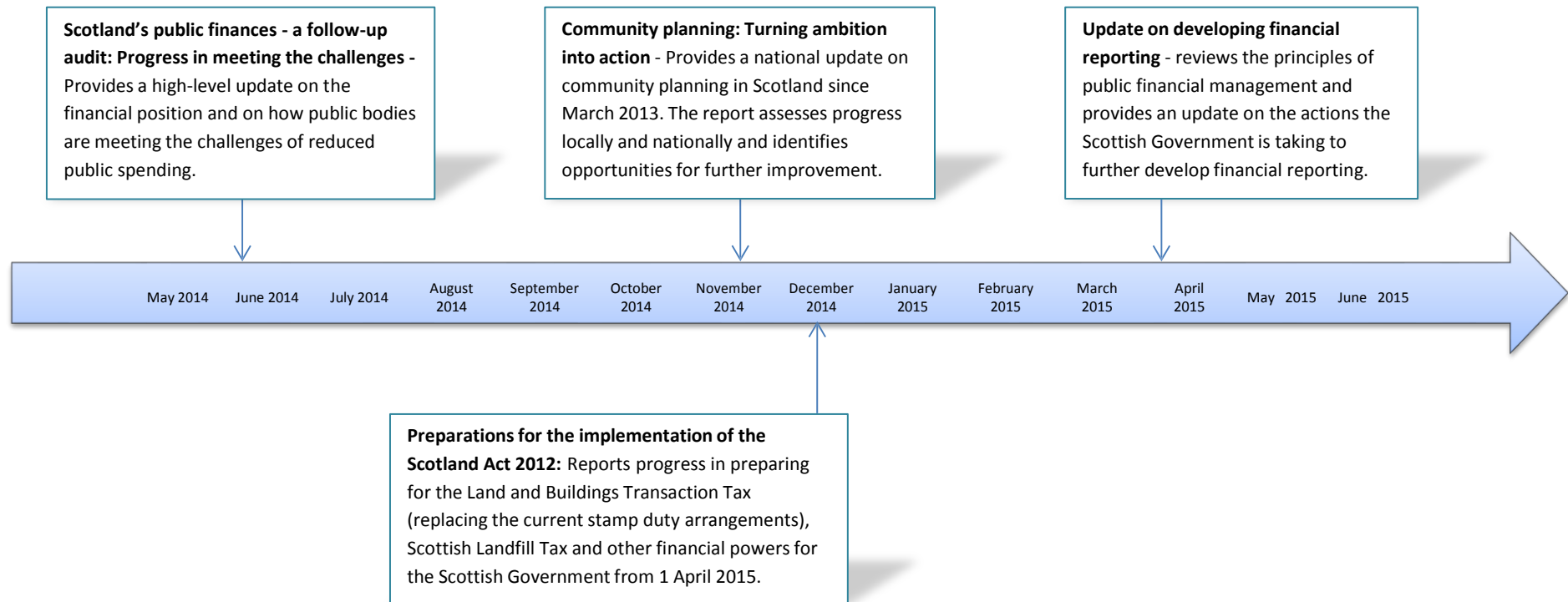
Audit Risk	Assurance procedure	Results and conclusions
<b>Risk of material misstatement</b>		
<p><b>Income</b></p> <p>The Care Inspectorate receives a significant amount of income in addition to Scottish Government funding.</p> <p><i>The extent and complexity of income means that there is an inherent risk that income could be materially misstated.</i></p>	<ul style="list-style-type: none"> <li>• Analytical procedures on income streams.</li> <li>• Detailed testing of revenue transactions focusing on the areas of greatest risk.</li> </ul>	<p>We undertook detailed testing of income streams and did not identify any evidence of fraudulent activity or significant weaknesses in related controls.</p>
<p><b>Management override of controls</b></p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p>	<ul style="list-style-type: none"> <li>• Detailed testing of journal entries.</li> <li>• Review of accounting estimates.</li> <li>• Focused testing of accruals and prepayments.</li> <li>• Evaluation of significant transactions that are outside the normal course of business.</li> </ul>	<p>We undertook detailed testing of journal entries, accruals and prepayments. We also reviewed accounting estimates and transactions for appropriateness.</p> <p>We did not identify any incidents of management override of controls.</p>

## Appendix I – Summary of local audit reports

Audit Risk	Assurance procedure	Results and conclusions
<p><b>Change to SPFM</b></p> <p>The section of the SPFM on 'severance, early retirement and redundancy terms' now requires central government bodies to consult with the Scottish Government before offering or entering into any settlement agreement.</p> <p><i>Failure to obtain the required approval for any such payments could impact on our regularity audit opinion.</i></p>	<ul style="list-style-type: none"> <li>Ensure that the new SPFM requirements are consistent with those set out in the Scottish Government framework document.</li> </ul>	<p>We reviewed relevant supporting documentation for early voluntary severance payments made during the year as part of the 2014/15 financial statements audit. No issues were identified.</p>
<p><b>Payroll and Human Resources Service - Pulse</b></p> <p>Although the Pulse system payroll module is operational, there are ongoing system development issues.</p> <p><i>System processes may not be fully implemented resulting in control weaknesses or user requirements not being met or benefits failing to materialise</i></p>	<ul style="list-style-type: none"> <li>Analytical review of payroll streams will be used to confirm completeness and identify any unusual transactions or variations.</li> </ul>	<p>We undertook a review of payroll streams during the year and did not identify any evidence of significant weaknesses in related controls.</p>



# Appendix III – Summary of local audit reports 2014/15



## Appendix IV – Action plan

Para/page	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
<b>Financial audit issues</b>				
1 7/20	<p><b>Issue:</b> We identified formatting and consistency issues during our review of the management commentary and remuneration report in the annual report and accounts due to changes with the FReM.</p> <p><b>Risk:</b> Ongoing issues with the financial statements provided for audit may require additional resource and effort from both audit and Care Inspectorate staff.</p> <p><b>Recommendation:</b> Management should ensure that adequate arrangements are in place to ensure that the draft Annual Report and Accounts submitted for audit are complete, correctly formatted and proof read.</p>	<p>Considerable effort is made to ensure the draft Annual Report and Accounts submitted for audit are complete, correctly formatted and proof read. This effort will be maintained in future years.</p>	<p>Head of Finance and Corporate Governance</p>	<p>June 2016</p>

Appendix IV – Action plan

Para/page	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
2 23/8	<p><b>Issue:</b> The 2015/16 FReM contains changes that will require action by officers to ensure they are fully reflected in the 2015/16 unaudited financial statements.</p> <p><b>Risk:</b> There may be ongoing issues with the financial statements provided for audit and they may require additional resource and effort from both audit and Care Inspectorate staff to ensure compliance with the FReM.</p> <p><b>Recommendation:</b> Officers should review the changes, discuss key areas with the audit team and put arrangements in place to ensure full compliance with the FReM</p>	<p>As part of our planning process a meeting has been arranged with Audit Scotland to identify the action prior to drafting the 2015/16 Annual Report and Accounts</p>	<p>Head of Finance and Corporate Governance</p>	<p>June 2016</p>



## Appendix IV – Action plan

Para/page	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
<b>Wider audit issues</b>				
3 37/11	<p><b>Issue:</b> A funding solution has been agreed for 2015/16 which is consistent with previous years. However, a longer term funding/ efficiencies solution is required to manage the identified budget deficits in future years.</p> <p><b>Risk:</b> Without a longer term solution, the Care Inspectorate may not be able to deliver the key objectives and outcomes agreed within the corporate plan.</p> <p><b>Recommendation:</b> The Care Inspectorate should clarify future funding arrangements and continue to identify and implement efficiencies in order to reduce costs and have a balanced budget in-line with Scottish Government funding and anticipated income streams.</p>	<p>We are working closely with the Sponsor to secure a longer term funding solution. A three year indicative budget has been prepared. Resources Committee is monitoring the development of the medium term financial plans and has incorporated this as a standing item on its agenda.</p> <p>A regime of Best Value reporting has been agreed for 2015/16 onwards. Resources Committee has agreed this will supersede the annual efficiencies report.</p>	Chief Executive	31 March 2016

Appendix IV – Action plan

Para/page	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
4 49/13	<p><b>Issue:</b> The project to implement the Pulse system has ongoing system development issues affecting the implementation of some human resources modules.</p> <p><b>Risk:</b> There is a risk that the users' requirements are not met and benefits are not materialised.</p> <p><b>Recommendation:</b> Management should keep the board and Audit Scotland up to date on progress to deliver the outstanding system modules.</p>	<p>Internal Audit carried out a review of the payroll system and reported to Audit Committee in November 2014. The controls in place were considered robust and on the whole are operating effectively. This report was made available to Audit Scotland and all relevant information provided during their fieldwork.</p> <p>Corporate Services Management Team (CSMT) will continue to oversee further development of additional functionality to ensure that the benefits of Pulse are fully realised.</p>	Director of Corporate Services (as Chair of CSMT)	31 March 2016