Scottish Public Pensions Agency
NHS Pension Scheme (Scotland)
Scottish Teachers Pension Scheme
2022/23 Annual Audit Report

Prepared for the Scottish Public Pensions Agency and the Auditor General for Scotland

December 2023

Contents

Key messages

2022/23 annual report and accounts

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2 Material adjustments were made to the SPPA annual report and accounts as a result of the audit process.

3 There were no material misstatements in the NHSPSS and STPS annual reports and accounts.

Financial management and sustainability

4 Although SPPA overspent its 2022/23 budget there was evidence of sound financial management and regular communication with the Scottish Government.

5 The NHSPSS and STPS pension schemes both overspent and this was not formally communicated to the Scottish Government until late in the audit process. Fortunately the overspend could be managed due to underspends elsewhere in the Scottish Administration but could have had significant consequences.

6 SPPA forecasts funding shortfalls over the next six years but has not yet developed a strategy to support financial sustainability.

Vision, leadership and governance

7 SPPA has a clear vision but requires a coherent financial strategy to support it. While we recognise that progress has been made with workforce planning there is a need to finalise the framework and embed the key principles.

Use of resources to improve outcomes

8 Effective quarterly performance reporting is provided to the Management Advisory Board against SPPA's strategic objectives.

9 The Pension Platform Project remains on-track but modified solutions have been required for the Remedy project.

Introduction

1. The Scottish Public Pensions Agency (SPPA) is an executive agency of the Scottish Government and is responsible for administering the NHS Pension Scheme (Scotland) (NHSPSS) and Scottish Teachers' Pension Scheme (STPS). This report summarises the findings from the 2022/23 annual audit of SPPA, NHSPSS and STPS. This report is addressed to the board of SPPA (which acts as scheme manager for NHSPSS and STPS) and the Auditor General for Scotland and will be published on Audit Scotland's website www.audit-scotland.gov.uk in due course.

2. The scope of the audit was set out in an Annual Audit Plan presented to the 27 June 2023 meeting of the Audit and Risk Committee (ARC). This Annual Audit Report comprises significant matters arising from an audit of SPPA's, NHSPSS' and STPS' annual reports and accounts and conclusions on the following wider scope areas that frame public audit as set out in the Code of Audit Practice 2021.

Audit appointment from 2022/23

3. Carole Grant was appointed by the Auditor General as auditor of SPPA, NHSPSS and STPS for the period from 2022/23 until 2026/27. The 2022/23 financial year was the first of the five-year appointment which coincides with the new Code of Audit Practice introduced for financial years commencing on or after 1 April 2022.

4. We would like to thank board members, ARC members, executive team members, and other staff, particularly those in finance, for their cooperation and assistance in this year and we look forward to working together constructively over the course of the five-year appointment.

Responsibilities and reporting

5. SPPA has primary responsibility for ensuring the proper financial stewardship of public funds (including those relating to NHSPSS and STPS). This includes preparing annual report and accounts that are in accordance with the account's direction from the Scottish Ministers. SPPA is also responsible for establishing appropriate and effective arrangements for governance, propriety, and regularity.

6. The responsibilities of the independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice 2021, and supplementary guidance and International Standards on Auditing in the UK.

7. This report contains an agreed action plan at Appendix 1. Weaknesses or risks identified are only those which have come to our attention during our normal audit work and may not be all that exist. Communicating these does not absolve management of SPPA from its responsibility to address the issues we raise and to maintain adequate systems of control.

Auditor Independence

8. We can confirm that we comply with the Financial Reporting Council's Ethical Standard. We can also confirm that we have not undertaken any non-audit related services and therefore the 2022/23 combined audit fee of £164,190, covering SPPA, NHSPSS and STPS, as set out in our 2022/23 Annual Audit Plan remains unchanged. We are not aware of any relationships that could compromise our objectivity and independence.

9. We add value to SPPA by:

- identifying and providing insight on significant risks, and making clear and relevant recommendations
- providing clear and focused conclusions on the appropriateness, effectiveness and impact of corporate governance arrangements to ensure the best use of resources and financial sustainability
- sharing intelligence and good practice identified.

1. Audit of 2022/23 annual report and accounts

Public bodies are required to prepare annual reports and accounts comprising financial statements and other related reports. These are principal means of accounting for the stewardship public funds.

Main judgements

Audit opinions on the annual report and accounts of SPPA, NHSPSS and STPS are unqualified.

Material adjustments were made to the SPPA annual report and accounts as a result of the audit process.

There were no material misstatements in the NHSPSS and STPS annual reports and accounts.

Audit opinions on the annual report and accounts are unqualified

10. Our audit opinions on the annual report and accounts of Scottish Public Pensions Agency (SPPA), NHS Pension Scheme (Scotland) (NHSPSS) and Scottish Teachers' Pension Scheme (STPS) are unqualified. The SPPA annual report and accounts for the year ended 31 March 2023 were considered by the SPPA Audit and Risk Committee on 20 September 2023 before being approved by the Management Advisory Board (MAB) and signed on 26 October 2023. The annual report and accounts for NHSPSS and STPS were signed on 12 December 2023 following consideration and approval by the Audit and Risk Committee and MAB on 11 December 2023. As reported in the independent auditor's reports:

- each of the financial statements give a true and fair view and were properly prepared in accordance with the financial reporting framework
- all expenditure and income were incurred or applied in accordance with applicable enactments and guidance
- the audited part of the SPPA remuneration and staff report was prepared in accordance with the financial reporting framework

- the SPPA performance report and governance statement were consistent with the financial statements and properly prepared in accordance with the relevant legislation and directions made by Scottish Ministers
- the audited part of the NHSPSS and STPS report of the scheme manager and governance statement were all consistent with the financial statements and properly prepared in accordance with the relevant legislation and directions made by Scottish Ministers.

Materiality for SPPA, NHSPSS and STPS was reviewed and revised on receipt of the unaudited annual report and accounts

11. Broadly, the concept of materiality is applied by auditors to determine whether misstatements identified during the audit could reasonably be expected to influence the economic decisions of users of the financial statements, and hence impact their opinion set out in the independent auditor's report. Auditors set a monetary threshold when considering materiality, although some issues may be considered material by their nature. It is ultimately a matter of the auditor's professional judgement.

12. Our initial assessment of materiality was carried out during the risk assessment phase of the audit. This was reviewed and revised on receipt of the unaudited annual report and accounts as summarised in Exhibit 1.

Exhibit 1
Materiality values

SPPA Materiality level	Planning	Final
Overall materiality	£0.44 million	£0.5 million
Performance materiality	£0.26 million	£0.3 million
Reporting threshold	£25,000	£25,000

NHSPSS Materiality level	Planning	Final
Overall materiality	£31.8 million	£35.0 million
Performance materiality	£19.1 million	£21.0 million
Reporting threshold	£250,000	£250,000

STPS Materiality level	Planning	Final
Overall materiality	£23.6 million	£24.0 million
Performance materiality	£14.2 million	£15.0 million
Reporting threshold	£250,000	£250,000

Source: Audit Scotland

13. The overall materiality threshold was set with reference to gross expenditure, which we judged as the figure most relevant to the users of the financial statements.

14. Performance materiality is used by auditors when undertaking work on individual areas of the financial statements. It is a lower materiality threshold, set to reduce the probability of aggregated misstatements exceeding overall materiality. Performance materiality was set at 60 per cent of overall materiality for all three audits, reflecting the level of errors found in 2021/22 and ongoing staffing issues within the finance team during 2022/23.

15. It is our responsibility to request that all misstatements, other than those below our reporting threshold, are corrected, although the final decision on making the correction lies with those charged with governance.

Significant findings and key audit matters

16. Under International Standard on Auditing (UK) 260 we communicate significant findings from the audit to the board, including our view about the qualitative aspects of the body's accounting practices.

17. The Code of Audit Practice also requires all audits to communicate key audit matters within the annual audit report under International Standard on Auditing (UK) 701. These are matters that we judged to be of most significance in our audit of the financial statements.

18. The significant findings and key audit matters are summarised in Exhibit 2.

Exhibit 2
Significant findings and key audit matters from the audit of the annual report and accounts

Issue	Resolution
SPPA only	
1. Police and fire balances Police and fire balance represent amounts which have been paid on behalf of the police and fire schemes by SPPA and are due to be refunded by the Scottish Police Authority and the Scottish Fire and Rescue Services. Through our review we found the following issues: • The receivables balance includes cash in transit of £16.7 million. From review we found that this is due to the prepayment of payrolls due on 1 April 2023 which were paid on the 31 March 2023. The classification as a receivable is therefore incorrect. • In 2021/22 SPPA found that it had overpaid HMRC by £7.9 million. It opted to disclose this within the existing payables balance with HMRC, thereby off-setting the full amount. Given that the receivables balance relates to different underlying transactions, this should be disclosed separately. • Identified mis-postings within the police and fire receivables balance means it is overstated by £3.3 million. Residual opening credit balance in event reporting (tax) code in the ledger of £1.3 million that could not be explained.	Following discussion, SPPA agreed to: • Reclassify £17.0 million of the cash-in-transit balance as a prepayment (contained within other receivables which has a footnote confirming this relates to police and fire pension schemes). • Separately identify the outstanding overpayment with HMRC of £7.9 million within other receivables and to add a footnote to explain its inclusion. Including a prior-period adjustment to the 2021/22 comparator accounts in relation to the HMRC overpayment. • Post an adjustment to the receivables balance by £2.0 million in respect of general mis-posting and the residual balance in event reporting code. This is the net of the corrections for mis-postings of £3.3 million and unexplained credit balance within event reporting of £1.3 million. These adjustments were confirmed in the revised set of accounts provided by SPPA. **Recommendation 1**
2. Property revaluation mis-postings Our review of property revaluations and the fixed asset register found the following issues: • The gross book value was incorrectly adjusted with a revaluation gain of £0.4 million. Our testing found that it should have been adjusted with a revaluation loss of £0.4 million. • The accumulated depreciation should have been adjusted to remove all balances at the point of revaluation. This had not been properly	Following discussion SPPA agreed to: • Adjust the gross book value by £0.8 million. • Adjust the accumulated depreciation by £0.8 million. • Review and update postings in the FAR for 2023/24 and accept an unadjusted misstatement of £0.1 million in 2022/23 in terms of misclassification issue and a further £0.1 million in terms of the omitted depreciation.

<table>
<tr><th>Issue</th><th>Resolution</th></tr>
<tr><td>accounted for resulting in an overstatement of £0.8 million.

The combination of these misstatements resulted in no change to the net book value.

Our review also found some inaccuracies between the ledger and the fixed asset register (FAR). These included:

• Additions of £0.2 million in the ledger which do not appear in the FAR.
• A possible mis-classification of additions of £0.1 million in the ledger (as differently categorised in the FAR)
• The revaluation adjustments were not dated as 31 March 2023 in the FAR which will create an issue in 2023/24 in terms of depreciation calculations.
• Further additions in 2022/23 of £0.1 million which appear in the ledger but not in the FAR.
• As a result of the omitted additions on the FAR there is an understatement in depreciation, estimated to be £0.1 million.

Given we selected our audit samples from the ledger, we are satisfied that these did not lead to any other material misstatement.</td><td>The agreed adjustments were confirmed in the revised set of accounts provided by SPPA.

Recommendation 2</td></tr>
<tr><td>3. Assets under construction mis-classified

SPPA is currently preparing to deliver the 2015 McCloud remedy which affects multiple schemes. SPPA is also developing a new pension platform programme. As part of this ongoing work, new software is being developed including pension calculators.

As part of our audit, SPPA confirmed that at 31 March 2023, £0.3 million had been spent on the preparation of these assets and disclosed as operational when they still related to assets under construction. As assets under development should not be amortised, there was a consequential overstatement of £0.1 million in the amortisation charge for 2022/23.</td><td>Following discussion, SPPA agreed to:

• Reclassify £0.3 million of operational tangible operational asset additions as intangible assets under development.
• Reduce depreciation on tangible assets by £0.1 million.

These adjustments were confirmed in the revised set of accounts provided by SPPA.

Recommendation 2</td></tr>
</table>

Issue	Resolution
4. Fair pay calculation The financial reporting manual (FReM) requires disclosures regarding fair pay. This includes providing a ratio of the mid-point of highest paid director's remuneration to the staff member in the lower quartile (i.e. 25th percentile), median (i.e. 50th percentile) and upper quartile (i.e. 75th percentile). Our review of the calculations for the median and quartile pays found that they did not include any agency staff. HM Treasury guidance (applicable as per the FReM) requires agency staff to be included. As per the remuneration and staff report within the accounts, there were agency costs of £2.7 million in 2022/23, representing 16 per cent of total staff costs.	The original calculations, which did not incorporate agency staff costs, were prepared by the Scottish Government. The calculations were revised by SPPA following the audit recommendation resulting in changes to all ratios as set out below: • 25th percentile changed from 3.20 to 3.66 • Median ratio changed from 3.30 to 3.40 • 75th percentile changed from 2.80 to 2.81. These adjustments were confirmed in the revised set of accounts provided by SPPA.
NHSPSS and STPS	
5. Combined scheme budget position As reported in the financial statements for both bodies, the combined accrued resources are covered by one limit in the Budget (Scotland) Act. In 2022/23 the combined position was in excess of the stated budget. NHSPSS overspent the budget by £135.6 million. STPS overspent the budget by £39.3 million. Due to this overspend position we had to consider the implications of this for our audit opinion and assess whether it would result in a regularity qualification.	The overspend occurred after taking account of adjustments provided by the Government Actuarial Department. On a cash basis, the schemes did not overspend. We concluded that the overspend did not impact on our regularity opinion as the Public Finance and Accountability (Scotland) Act refers to cash overspends. We also considered the wider implications of the overspend and confirmed that this could be accommodated due to underspends elsewhere in the Scottish Administration. However we did note that this was not actively communicated to the Scottish Government to enable it to be managed as part of the wider financial management regime. This is covered further in the section on Financial Management. **Recommendation 3**

Issue	Resolution
NHSPSS only	
6. Reversal of prior year accruals Our audit procedures identified an overstatement of £23 million in Benefits Paid. Prior year accruals had not been processed using an automatically reversing journal, and as a result some 2021/22 related benefits were accounted for again in the 2022/23 financial statements.	SPPA Officers agreed with the error and processed an adjustment to the financial statements. This increased the actuarial gain recorded in Other Comprehensive Expenditure. The amount identified was the total possible error of this nature and we carried out further audit procedures to gain assurance that a similar issue was not affecting the STSS accounts. We are satisfied that the error was an isolated incident likely a result of the financial capacity issues reported in the prior year.

Source: Audit Scotland

Our audit work responded to the risks of material misstatement we identified in the annual report and accounts

19. We have obtained audit assurances over the identified significant risks of material misstatement to the financial statements we identified in our 2022/23 Annual Audit Plan. It also summarises the further audit procedures we performed during the year to obtain assurances over these risks and the conclusions from the work completed.

Exhibit 3
Significant risks of material misstatement in the annual report and accounts

Audit risk	Assurance procedure	Results and conclusions
1. Risk of material misstatement due to fraud caused by management override of controls As stated in International Standard on Auditing (UK) 240, management is in a unique position to perpetrate fraud because of	• Assess the design and implementation of controls over journal entry processing. • Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual journal activity.	**SPPA, NHSPSS and STPS** Our testing of journals, year-end transactions, accruals and prepayments did not identify any incidents of management override of controls. The methods and assumptions used to prepare

Audit risk	Assurance procedure	Results and conclusions
management's ability to override controls that otherwise appear to be operating effectively. This is presumed to be a significant risk in every audit. (**SPPA, NHSPSS and STPS**)	• Test journals at the year-end and post-closing entries and focus on significant risk areas. • Consider the need to test journal entries and other adjustments during the period. • Evaluate significant transactions outside the normal course of business. • Assess any changes to the methods and underlying assumptions used to prepare accounting estimates compared to the prior year. • Substantive testing of income and expenditure transactions around the year-end to confirm they are accounted for in the correct financial year. • Focused testing of accounting accruals and prepayments.	accounting estimates were confirmed to be reasonable and consistent with prior years. We are satisfied that there is no material misstatement arising from this risk.
2. Estimation in the valuation of land and buildings SPPA held land and buildings with a NBV of £4.8 million as at 31 March 2022. There is a significant degree of subjectivity in the valuation of land and buildings which is based on specialist and management assumptions. Changes in assumptions can result in material changes to valuations. (**SPPA only**)	• Review the information provided from SPPA to the external valuer to assess for completeness. • Review detailed working papers to support asset reviews and impairments. • Evaluate the competence, capabilities, and objectivity of the external valuer. • Obtain an understanding of management's involvement in the valuation process to assess if appropriate oversight has occurred. • Critically assess management's approach to ensuring that assets not	**SPPA only** We confirmed that SPPA engaged appropriately with the valuer to allow the valuation process to proceed effectively. We assessed the valuer and confirmed that they are competent and appropriately qualified for their role. We identified some misstatements which have been corrected and have made a recommendation to support improvement. We did not identify any land and buildings not subject to a valuation in year.

Audit risk	Assurance procedure	Results and conclusions
	subject to external valuation are not materially misstated. • Review the appropriateness of the reconciliation between the financial ledger and the fixed asset register.	We are satisfied that the valuation of property assets is not materially misstated.
3. Information supporting scheme valuations Decisions taken by SPPA for the schemes are reliant on the work of the Government Actuary Department (GAD). The actuarial valuation methodology relies on significant judgements and assumptions in relation to financial, mortality and demographic factors. There is a risk that the actuarial information for valuing the schemes is affected by incomplete or inaccurate information, or the use of unreasonable judgements and assumptions. (**NHSPSS and STPS only**)	• Review of the work of GAD, focusing on reliability, professional competence, and capability. • Meet with GAD to discuss work practices, validation processes and quality review arrangements to determine whether reliance can be taken in relation to GAD's internal processes. • Review reports to GAD supporting valuation data. • Commission review of GAD by independent expert.	**NHSPSS and STPS only** We performed a review of GAD and confirmed that it is a reliable, competent and capable organisation and that the individuals involved are appropriately qualified. Supporting this, we commissioned a review of GAD by an independent accountancy firm with appropriate expertise in relation to both schemes. This found that the key processes and assumptions were reasonable and in line with guidance. We met with GAD at two points during the year to discuss progress of work, key underlying assumptions, the quality of data provided and movements in the liabilities. No issues were found from this. The reports prepared by GAD were consistent with our discussions and we confirmed that they were consistent with the unaudited accounts provided by SPPA for both schemes.

Source: Audit Scotland

20. In addition, we identified an "area of audit focus" in our 2022/23 Annual Audit Plan where we considered there to be a risk of material misstatement to the financial statements. The area of specific audit focus related to the Police Service of Scotland and Scottish Fire and Rescue Service year end balances within the SPPA financial statements. Our findings from this work are captured in Exhibit 2.

There were four non-material misstatements identified within the SPPA financial statements, three within NHSPSS and none in STPS

21. In terms of SPPA, other than the three corrected material misstatements detailed as significant findings in Exhibit 2, our audit identified some other non-material misstatements above our reporting threshold. These related to the employee benefit accrual and some expenditure items which had not been accrued properly. Both of these were below materiality (cumulatively totalling £0.1 million) and were adjusted for.

22. We identified two further non-material misstatements which were not corrected by management in the audited accounts for SPPA. Details of the uncorrected misstatements for SPPA are included in Exhibit 2, item 2 and totalled £0.2 million.

23. As documented in Exhibit 2, item 6, we identified one error caused by a failure to reverse prior year accruals in NHSPSS. This was subsequently adjusted by officers, resulting in a £23 million increase in the actuarial gain recorded as Other Comprehensive Expenditure. The error breached our performance materiality threshold, we undertook additional audit procedures and were satisfied that we have identified the total extent of this error within both sets of scheme accounts.

24. We also identified two misstatements which were not corrected in the NHSPSS accounts in relation to two accrued balances. These total to £3.74 million and reflect an overstatement in total comprehensive expenditure and net liabilities for the same amount. SPPA opted not to make these adjustments.

25. We considered the size, nature and circumstances leading to all uncorrected misstatements, individually and in aggregate, and concluded that those identified above were not material.

The unaudited annual report and accounts were received in line with the agreed audit timetable

26. The unaudited SPPA annual report and accounts were received in line with our agreed audit timetable on 7 July 2023. Following that, the unaudited annual report and accounts for both NHSPSS and STPS were provided on 11 August 2023.

27. Although these dates are later than as stated in our Annual Audit Plan, the revised dates were agreed with the audit team and have allowed us to complete our audit work within the statutory timescales. While some amendments were required, the standard of the annual report and accounts, and supporting papers, was generally good.

28. This outcome represents significant progress on the situation in 2021/22. New members of the finance team were appointed in spring 2023 and have performed well as evidenced by the improved situation. Even although the Head of Finance left her post at the end of June 2023, the finance team delivered satisfactory sets of accounts and support to the audit process.

Reasonable progress was made on prior year recommendations

29. SPPA has made progress in implementing the audit recommendations identified last year. As detailed in Appendix 1.

2. Financial management

Financial management means having sound budgetary processes, and the ability to understand the financial environment and whether internal controls are operating effectively.

Conclusion

Although SPPA overspent its 2022/23 budget there was evidence of sound financial management and regular communication with the Scottish Government.

The NHSPSS and STPS pension schemes both overspent and this was not communicated to the Scottish Government until it was raised as part of the audit process. Fortunately the overspend could be managed due to underspends elsewhere in the Scottish Administration but could have had significant consequences.

Audit testing found some improvement in the financial control environment but there remains scope for the controls to be further enhanced.

SPPA overspent its budget in 2022/23, but this was clearly communicated to the Scottish Government

30. The main financial objective for SPPA is to ensure that the financial outturn for the year is within the budget allocated by Scottish Ministers. The initial capital budget was subject to significant revision reducing from £4.6 million to £0.6 million. This was due to SPPA opting to use a cloud-hosted solution for Pension Platform Programme (PPP) rather than an in-house option. The funding was offered back to the Scottish Government with the associated non-cash budget.

31. SPPA reported an outturn of £25.1 million against its overall budget for 2022/23 with an overspend of £0.5 million. During the audit process SPPA provided evidence of discussions with the Scottish Government regarding the overspend, which was attributed to costs associated with the Remedy project. This confirms that sound financial management was being applied despite the final overspend position. The financial performance against fiscal resources is shown in Exhibit 4.

Exhibit 4
Performance against fiscal resource in 2022/23

	Initial budget £m	Final budget £m	Outturn £m	Overspend £m
Resource	23.7	23.9	24.4	0.5
Capital	4.6	0.6	0.6	0.0
Total	**28.3**	**24.5**	**25.1**	**0.5**

Source: SPPA Annual Report and Accounts 2022/23

NHSPSS and STPS exceeded their 2022/23 combined budget limit

32. NHSPSS and STPS are funded by Scottish Government annual managed expenditure (AME) to cover the cost of pension payments to retired members. The main financial objective of NHSPSS and STPS is to ensure that financial outturn for the year is within the budget allocated by Scottish Ministers.

33. NHSPSS and STPS' accrued resources are covered by one budget limit of £6,966.1 million, but the total accrued resources for 2022/23 were £7,140.9 million an overspend of £175.8 million as shown in Exhibit 5. The overspend was mainly due to back dated pay awards that were agreed during the year but not factored in when the budget was set. We have received correspondence between SPPA and the Scottish Government which confirms that the overspend can be absorbed due to underspends elsewhere in the Scottish Administration.

Exhibit 5
Performance against AME in 2022/23

	Initial budget £m	Final budget £m	Outturn £m	Overspend £m
NHSPSS	4,468.8	4,657.8	4,793.3	135.5
STPS	2,002.2	2,308.3	2,347.6	39.3
Total	**6,471.0**	**6,966.1**	**7,140.9**	**175.8**

Source: Scottish Budget: 2022/23, NHSPSS and STPS Annual Report and Accounts 2022/23

The Scottish Government was not promptly advised of the overspends for NHSPSS and STPS

34. Both the SPPA's resource budget and the budgets for the pension schemes' were increased as part of the revision process. However this did not prevent all three budgets being overspent. In the case of the schemes this was primarily due to an in-year pay award agreed at a late date, while the Remedy project was largely responsible for the SPPA result.

35. While we are satisfied that the explanations provided are reasonable, SPPA should ensure more active engagement with the Scottish Government as part of the budgeting process to ensure that the risk of any potential overspends can be managed. Correspondence from the Scottish Government has highlighted the need for earlier notification of overspends, while confirming that the schemes' overspend could be absorbed due to underspends elsewhere in the Scottish Administration.

Recommendation 3

SPPA should ensure that the Scottish Government is promptly advised of changes in the forecast outturn position.

Financial controls have improved, but need further investment to support a robust control environment

36. We identify and assess the key internal controls in those accounting systems we regard as significant to produce the financial statements. Our objective is to gain assurance that SPPA, NHSPSS and STPS have systems of recording and processing transactions which provide a sound basis for the preparation of the financial statements.

37. Last year we identified a number of financial control issues including the lack of a check on reconciliations. This year we have found that the situation has improved but that there remains room for further improvement. We have found evidence of controls in place, however these controls are not as strong as they could be. We have set out the issues we found below:

- Comparison reports are used to check data between the administration and payroll elements of Altair (the pension administration system) for both NHSPSS and STPS. Our review found that these reports were being prepared on a monthly basis, but there was no evidence that they were being regularly checked and differences investigated. We tested samples of pension calculations for both schemes and did not identify any significant issues. We also checked details from a sample of employers and found no issues when comparing to Altair.

- Our testing of the Epicor system (used to manage contributions from employers) found issues with the monthly bank account reconciliation process. We were informed that due to capacity issues, the May 2022 and December 2022 reconciliations were not completed as at March 2023. SPPA stated that mitigating controls such as the daily checks remained in place during this time. During our financial statements audit we confirmed that the balances had been duly reconciled at year-end. However, there was a lack of an audit trail regarding who checked the reconciliation.

- We found a lack of evidence to confirm that management / exception reports from the Epicor system were being routinely checked during the year by an appropriately senior officer. Although we were advised that the reports were routinely prepared and checked there was a lack of an audit trail to support this.

- Access to the Epicor system is controlled and SPPA was able to demonstrate that only appropriate users currently have access. However records are not retained when a user is granted access.

Recommendation 4

SPPA should ensure that financial management controls are routinely carried out during the year and that appropriate evidence of management review is retained.

38. Last year we also identified an issue with one individual who left SPPA and was not removed from its payroll in a timely manner. Our testing did not find any such issues in 2022/23 with leavers appropriately removed. Similarly, our audit testing this year did not identify any issues regarding changes to suppliers' details. Finally, last year we also flagged an overpayment to HMRC which indicated weaknesses within the internal control process. This is covered in more detail in Exhibit 2, item 1.

Standards of conduct and arrangements for the prevention and detection of fraud and error are appropriate

39. In the public sector there are specific fraud risks, including those relating to tax receipts, welfare benefits, grants and other claims made by individuals and organisations. Public sector bodies are responsible for implementing effective systems of internal control, including internal audit, which safeguard public assets and prevent and detect fraud, error and irregularities, bribery and corruption.

40. Last year we highlighted this as an area for improvement. We noted that the counter-fraud policy had not been updated since 2014 and a regular fraud report is not provided to the ARC.

41. During 2022/23 we confirmed that SPPA has still to update the counter-fraud policy. We have been advised that SPPA feel that is remains functional but recognises there are elements that are out-dated. SPPA intend to review this during 2023/24 to align with the UK government's counter fraud functional standard and Scottish Government best practice.

42. While a dedicated report on fraud has not been prepared, it does now feature as a standing item at ARC meetings and is covered verbally. Given the low number of frauds found by SPPA, this is felt to be appropriate.

Recommendation 5

SPPA should ensure that it reviews its counter-fraud policy so that it is appropriately up to date and complies with best practice.

3. Financial sustainability

Financial Sustainability means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs.

Conclusion

SPPA forecasts funding shortfalls over the next six years and has not yet developed a strategy to support financial sustainability.

Changes in scheme contributions are being introduced to keep pace with the changing environment.

SPPA forecasts funding shortfalls over the next six years but has still to develop a financial strategy

43. In June 2023, SPPA provided a strategic approach to budgeting (SAB) return to the Scottish Government. This outlined resource shortfalls over a six-year period from 2023/24 to 2028/29 totalling £36.8 million. Looking ahead to 2023/24, SPPA forecast a shortfall of £2.7 million. About £1.7 million of this is attributable to projects, these being Remedy and the PPP.

44. A report to SPPA's MAB in October 2023 is now forecasting a deficit of £2.2 million for 2023/24. SPPA is looking at options to reduce spend such as recruitment controls and letting of space within the Tweedbank office. These actions are not expected to prevent SPPA overspending its allocation in 2023/24.

45. Last year we recommended that SPPA prepare a financial strategy demonstrating how it will manage its finances and meet future funding challenges. SPPA is still preparing its financial strategy. Giving the ongoing funding pressures, SPPA should prioritise the finalisation of this key strategic document.

Recommendation 6

SPPA should prioritise developing a financial strategy to identify how it will meet future challenges and pressures.

Both pension schemes saw a significant reduction in liabilities in 2022/23

46. The 2022/23 annual report and accounts of NHSPSS and STPS show that NHSPSS has net liabilities of £54.5 billion (£40.6 billion decrease) and STPS has net liabilities of £31.4 billion (£22.0 billion decrease).

47. These large decreases are due to a large increase in the discount rate regarding the pension scheme liability. This movement is consistent with movements seen in other pension schemes across the public sector. The figures are prepared by the Government Actuarial Department (GAD).

48. As part of our audit we carry out a review of GAD and its assumptions. We found no issues as part of this review, which included the use of an auditor's expert, in the form of an accountancy firm with the required specialist knowledge and skills.

49. GAD's assessments of current service cost are based on movement in the discount rate in the previous twelve-month period (April 2021 to March 2022 for 2022/23). As such, the current service cost has not changed in line with the scheme liability.

50. In addition to that, pay awards agreed late in the year resulted in an increase in the liability. This is particularly the case for NHSPSS. The increased current service costs for both schemes resulted in the combined spend being greater in 2022/23. Overall the spend was £175.8 million over budget (see Exhibit 5).

Changes in schemes contributions are being introduced to keep pace with the changing environment

51. Moving forward, the 2020 valuations for both schemes are due to be finalised in the near future. The valuation is being prepared by GAD and will involve a review of employer contributions. Any changes to contributions will come into effect on 1 April 2024.

52. The review will also consider issues such as McCloud, guaranteed minimum pension (GMP) and the Goodwin case. SPPA is undertaking work on each of these to better understand what they mean for the schemes.

53. In addition, SPPA is actively reviewing how both schemes operate. New contribution rates were agreed for NHSPSS following discussion with the relevant scheme advisory board (SAB). These new rates came into effect on 1 October 2023 and aim to achieve the target yield of 9.8 per cent. In recent years the actual yield has been slightly below this at 9.6 per cent.

54. The STPS SAB set up a working group to carry out a review of the scheme's eligibility rules. The review is nearing completion and will require approval from HM Treasury. As with the other reviews, this is necessary as the environment in which these schemes operate is ever changing.

4. Vision, leadership and governance

Public sector bodies must have a clear vision and strategy and set priorities for improvement within this vision and strategy. They work together with partners and communities to improve outcomes and foster a culture of innovation.

Conclusion

SPPA has a clear vision but requires a coherent financial strategy to support it.

Although there has been changes to the Executive Team, it is now feeling more settled.

SPPA has made progress with workforce planning but further work is required to finalise the framework and embed the key principles.

SPPA has a clear vision but requires a coherent financial strategy to support it

55. As we reported last year, SPPA launched Our Corporate Plan 2022-27 in March 2022. This details the agency's purpose, vision and strategic aims and sets out its aims and objectives for the next five years.

56. Supporting this, the 2022/23 Business Plan details ten priorities for the year and identifies key performance indicators. Progress against the ten priorities were subsequently reported in the 2022/23 annual report and accounts.

57. A business plan is also in place for 2023/24. This sets out five priorities and describes how they will be measured. The plan also identifies performance indicators that are being reported to the MAB using a RAG (red, amber, green) status. The most recent report was provided on 30 October 2023, with no areas highlighted as red.

58. This provides evidence that SPPA has a clear vision supported by effective prioritised corporate and operational planning. The lack of a financial strategy and delays in workforce planning though must be addressed to support the overall delivery of the Corporate Plan.

There have been some changes to the Executive Team, but generally it is now more settled

59. Last year we reported that the post of Chief Operating Officer (COO) had been vacant for a period of time. This situation arose in October 2022, with interim arrangements in place. A new COO was appointed in March 2023 which meant that the Executive Team was fully resourced at the end of the financial year.

60. After the end of the year however, the Head of Finance left her post (on 30 June 2023). Interim arrangements were put in place during the financial statements audit process, with a new appointment made on 30 October 2023. Generally we are satisfied that the Executive Team is more settled.

61. Supplementing this, SPPA also has other managerial appointments, including a specialist Programme Director to manage the Remedy and PPP projects. It will be important to maintain this situation over the coming years, given the significance of these two projects and to support SPPA in tackling the ongoing financial challenges.

SPPA has made progress with workforce planning but further work is required

62. While the Executive Team is more settled and the finance team is better resourced, work is still ongoing to develop robust workforce planning across the organisation. This should be performed in tandem with the financial strategy given the forecast pressures for 2023/24 and beyond. SPPA estimates that it faces a challenge of £0.9 million on its staff costs alone.

63. While it will be important for SPPA to reduce its pay costs, it should still be able to provide a quality service. A workforce plan would better position the organisation to deliver that. Work has commenced and a workforce planning group has been set up (as we reported last year). This includes representatives from across the organisation, including finance.

64. A workforce planning framework was presented to the People Committee in August 2023 alongside an action plan. This sets out the key stages towards the development of the framework. The initial timescale for completion of the action plan was December 2023, but through discussion with SPPA we understand that this will not be met.

Recommendation 7

SPPA should finalise its workforce planning framework and associated action plan and ensure aligns with other plans being developed such as the financial strategy.

Governance arrangements are appropriate

65. SPPA's governance arrangements have been set out in the Governance Statement in the annual accounts. We have reviewed these arrangements and concluded that they are appropriate and effective. Scrutiny arrangements are generally working well in SPPA with both the ARC and MAB performing annual self-assessments.

66. There is scope to strengthen SPPA's approach to openness and transparency by making the papers for the MAB and ARC meetings available on the website. Currently only minutes are available. Providing supporting papers could include financial and performance information and detail decisions made which are of public interest.

Climate change arrangements

67. The Scottish Parliament has set a legally binding target of becoming net zero by 2045 and has interim targets including a 75 per cent reduction in greenhouse gas emissions by 2030. The public sector in Scotland has a key role to play in ensuring these targets are met and in adapting to the impacts of climate change.

68. SPPA is currently preparing a Sustainability and Environmental Plan for the period from 2023-2028. This is scheduled to be finalised in December 2023 and will be necessary to set out how the agency will meet its climate change targets. We will follow this point up in future years.

69. The Auditor General and Accounts Commission are developing a programme of work on climate change. This involves a blend of climate change-specific outputs that focus on key issues and challenges as well as moving towards integrating climate change considerations into all aspects of audit work.

5. Use of resources to improve outcomes

Public sector bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities.

Conclusions

SPPA has developed an appropriate framework to support the assessment of the delivery of Best Value.

Effective quarterly performance reporting is provided to the MAB against SPPA's strategic objectives.

PPP remains on-track but modified solutions have been required for the Remedy project.

SPPA has an appropriate Best Value framework

70. Ministerial guidance to Accountable Officers for public bodies and the Scottish Public Finance Manual (SPFM) sets out the accountable officer's duty to ensure that arrangements are in place to secure best value. The guidance sets out the key characteristics of best value and states that compliance with the duty of best value requires public bodies to take a systematic approach to self-evaluation and continuous improvement.

71. Last year we reported how the 2022/23 business plan sets key performance indicators for each of the new business priorities. Further we identified that these measures aimed to help SPPA to demonstrate how it is securing Best Value. This year we have seen how these priorities have been reported ultimately in the 2022/23 annual report and accounts.

72. Further, the 2022/23 annual report and accounts identify how SPPA uses a range of mechanisms to obtain feedback from its customers and stakeholders. Examples include the various pension boards which have member and employer representatives, targeted groups, desk-top research and complaint feedback. The accounts also refer to benchmarking with other pension providers which SPPA is currently undertaking.

Effective quarterly performance reporting arrangements are in place

73. The MAB received quarterly performance reports during 2022/23. These reported on the KPIs (key performance indicators as set out in the 2022/23 business plan), linked to strategic objectives. The report used a RAG status to identify progress against each of these targets.

74. This approach is effective as it provides the MAB with the necessary information to gauge and challenge the performance of the organisation. The approach has been taken forward in 2023/24 with quarterly reports describing progress against the 2023/24 business plan.

PPP remains on-track but modified solutions have been required for the Remedy project

75. Last year we provided an update on the progress of SPPA's two main projects, Remedy and PPP. We reported that PPP aims to deliver a comprehensive digital solution for pensions and payroll administration and was due to be in place by 2025. Remedy meanwhile aims to deliver the regulatory changes to pension schemes required by an age discrimination legal judgement.

76. Regular update reports on both projects are provided by the Programme Director at meetings of the MAB and the ARC. In October 2023, the Remedy project was assessed as amber. This was due to a delay in providing automated solutions (i.e. pension calculators) which impacted on all schemes.

77. The intention is to provide members with two calculations which would allow them to select the preferred option. However, this is not possible at present. Due to the delay with the calculators, SPPA has put in place modified manual solutions. These meet with regulations (as they currently stand) but will not provide a dual calculation for members.

78. PPP has a longer timeframe and is currently assessed as amber / green. There was a delay in the contractor signing the contract, but this was ultimately completed in June 2023. Another notable achievement was the migration of data for the police and fire schemes to the cloud in September 2023.

79. Although the projects are separate, they are not mutually exclusive. The automation being prepared for Remedy will also be incorporated into PPP in due course. As such, it is important that the issues with Remedy are corrected swiftly. PPP is particularly fundamental given ongoing funding issues and the level of manual intervention required in the current system (Altair).

Appendix 1. Action plan 2022/23

2022/23 recommendations

Issue / risk	Recommendation	Agreed management action / timing
1. Police and fire balances Police and fire balances represent amounts which have been paid on behalf of the police and fire schemes by SPPA and are due to be refunded by the Scottish Police Authority (SPA) and the Scottish Fire and Rescue Services (SFRS). There is also a payables balance for tax on any pension payments which have not been paid to HMRC at year-end. This is matched by an element within the receivables balance. Through our review we found issues regarding a mis-classification of the reported cash in transit balance of £16.7 million; the transparency of disclosures regarding an overpayment to HMRC of £8.0 million; mis-postings within the police and fire receivables balance of £3.8 million: and an unexplained residual balance in event reporting tax code in the ledger of £1.3 million. Risk – SPPA materially mis-states its balances in relation to police and fire pension schemes.	SPPA should ensure that appropriate management checks are carried out on year-end balances regarding the police and fire pension schemes. In addition, SPPA should confirm these year-end balances with SPA and SFRS. SPPA should also consider whether the provision of a service auditor would provide greater assurance to all relevant parties. Exhibit 2, item 1	SPPA has employed two financial accountants. SPPA will ensure that appropriate management checks are carried out on year-end balances regarding the police and fire pension schemes. In addition, SPPA will confirm these year-end balances with SPA and SFRS. SPPA will consider whether the provision of a service auditor would provide greater assurance to all relevant parties. SPPA Financial Accountant June 2024

Issue / risk	Recommendation	Agreed management action / timing
2. Asset accounting SPPA's unaudited accounts reported total non-current assets of £6.9 million made up of £5.6 million of property, plant and equipment and £1.3 million of intangible assets. During our audit we found issues in terms of how revaluations were accounted for, how intangible assets under development were classified and differences between the fixed asset register and the ledger (relating to asset additions and revaluations). Risk – SPPA materially misstates its non-current assets.	SPPA should ensure that there are appropriate management checks on year-end revaluation adjustments. SPPA should also ensure that assets are appropriately classified and that the fixed asset register is updated appropriately (including post-dating any adjustments relating to prior-years' correctly). SPPA should also ensure that the fixed asset register reconciles to the general ledger (SEAS). Exhibit 2, items 2 and 3	SPPA has employed two financial accountants. SPPA will ensure that there are appropriate management checks on year-end revaluation adjustments. SPPA will also ensure that assets are appropriately classified and that the fixed asset register is updated appropriately (including post-dating any adjustments relating to prior-years' correctly). SPPA will also ensure that the fixed asset register reconciles to the general ledger (SEAS). SPPA Financial Accountant June 2024
3. Combined scheme resource position The accrued resources for NHSPSS and STPS are covered by one limit in the Budget (Scotland) Act. In 2022/23 the combined position was in excess of the stated budget. The overspend occurred after taking account of adjustments provided by GAD. On a cash basis, the schemes did not overspend. SPPA did not inform the Scottish Government about the overspend until 27 September 2023, although it was known since 5 June 2023. Risk – The overspend within the schemes cannot be absorbed by overspends elsewhere in the Scottish Administration.	SPPA should ensure that the Scottish Government is promptly advised of changes in the forecast outturn position. Exhibit 2, item 5 Paragraph 35.	SPPA has employed two financial accountants. SPPA will ensure that the Scottish Government is promptly advised of changes in the forecast outturn position. SPPA currently advises HM Treasury and SG Reporting of the NHSPSS and STPS on monthly basis. SPPA Financial Accountant June 2024

Issue / risk	Recommendation	Agreed management action / timing
4. SPPA management controls Financial controls provide management with assurance that the underlying systems are working appropriately. Testing of SPPA controls regarding the Altair and Epicor systems found that there was a general lack of audit trail in terms of management review. Risk – The key financial systems are not robustly controlled resulting in unidentified errors and increasing the risk of fraud.	SPPA should ensure that financial management controls are routinely carried out during the year and that appropriate evidence of management review is retained. Paragraph 37.	SPPA will ensure that financial management controls will routinely be carried out during the year and that appropriate evidence of management review will be retained. SPPA Financial Accountants/ Financial Controller March 2024
5. Counter fraud policy A counter fraud policy sets out how an organisation deals with potential acts of fraud. They are a key control to ensure that any allegations are reported and properly investigated. The SPPA counter fraud policy has not been updated since 2014. Risk – The organisation is not supporting staff in the reporting and management of fraud.	SPPA should ensure that it reviews its counter-fraud policy so that it is appropriately up to date and complies with best practice. Paragraph 41. 42.	SPPA Counter Fraud Policy will be reviewed by relevant internal stakeholders and updated as required. SPPA Risk & Control Officer March 2024
6. Financial strategy It is important that organisations plan to meet financial challenges over a multi-year period, covering at least three to five years. SPPA is forecasting deficits over the next four years. Although it is taking some mitigating actions, there is currently no comprehensive strategy or plan to support this. Risk – SPPA is unable to achieve financial balance.	SPPA should prioritise developing a financial strategy to identify how it will meet future challenges and pressures. Paragraph 45.	In October 2023, Pension Board Chairs jointly wrote to the Minister for Public Finance and Community Wealth to outline concerns regarding the budget constraints facing the SPPA, with a formal response and acknowledgement being received very shortly thereafter. Such resource demands have been reflected in SPPA's budget request to Scottish Government. Accordingly, SPPA remains committed to prioritising the finalisation of its financial

Issue / risk	Recommendation	Agreed management action / timing
		strategy, aligning to its Corporate Plan (5 years), and this will be undertaken once 2024/25 budget allocations to portfolios are published by the Scottish Government in December 2023. SPPA CEO/ CFO Agreed date: October 2024
7. Workforce planning An organisation should have a plan or framework in place which sets out its workforce needs. This should be closely aligned to other plans such as the corporate plan and financial strategy. SPPA has made progress and has developed a workforce framework and action plan. It had hoped to achieve the action plan by the end of 2023 but this won't be achieved. Risk – SPPA is not adequately resourced to carry out its functions.	SPPA should finalise its workforce planning framework and associated action plan and ensure it aligns with other plans being developed such as the financial strategy. Paragraph 64.	The workforce planning framework and process is in place, subject to continuous review and refinement by the HR and Finance teams. The internal workforce planning process will change substantially following the full implementation of the new Oracle system in 2024, which is anticipated to improve functionality, data accessibility and analysis. Responsible officer: HR Manager Agreed date: October 2024 A workforce strategy has been commissioned setting out planned changes to the workforce aligned to the high level business plan and developing digital strategy. It will address how automated processes should be integrated into the workforce and adaptation to budget constraints. Responsible officer: Head of People Agreed date: August 2024

Follow-up of prior year recommendations

Issue / risk	Recommendation	Agreed management action / timing
b/f 1. Submission of annual report and accounts	Whilst acknowledging that SPPA is trying to secure additional capacity in the finance team, this should be progressed urgently. This should ensure that the team has the resources needed to prepare annual reports and accounts in a timely manner and to support the audit.	The 2022/23 annual report and accounts were provided in accordance with the agreed timeline. The audit team received good support from finance enabling the audit to be delivered in accordance with the original timescale. **Complete**
b/f 2. Financial controls	SPPA should ensure that it retains evidence of appropriate management checks regarding reconciliations, changing suppliers' details, significant payments and for people leaving the organisation.	Although there has been some progress, there is still a lack of evidence of management review on moany controls. **Ongoing – see Recommendation 4**
b/f 3. Fraud arrangements	SPPA should finalise its review of the counter fraud policy and regular fraud reports should be submitted to the ARC, which should also incorporate results from NFI exercises.	SPPA has yet to review and update its counter-fraud policy. **Ongoing – see Recommendation 5**
b/f 4. Financial sustainability	SPPA should continue to develop a financial strategy demonstrating how it will manage its finances and meet future funding challenges	SPPA has still to fully develop its financial strategy. It is vital that it does this to manage known resource shortfalls in the coming years. **Ongoing – see Recommendation 6**
b/f 5. Workforce planning	SPPA should continue developing workforce planning to ensure it addresses longer-term strategic aims as well as meeting more immediate customer and business needs.	SPPA has made progress and has developed a framework and action plan to address this point. It had hoped to achieve the action plan by the end of 2023 but this has not been achieved. **Ongoing – see Recommendation 7**

Issue / risk	Recommendation	Agreed management action / timing
b/f 6. Performance reporting	SPPA should fully embed and enhance improvements made to the 2021/22 performance report to ensure that it meets with FReM requirements and best practice.	The performance report in the 2022/23 annual report and accounts met the FReM requirements after some audit adjustments. There are always opportunities to further improve performance reporting and we will work with SPPA during the audit appointment. **Complete**
b/f 7. Leadership	SPPA should prioritise filling the post of Chief Operating Officer and continuously review strategic capacity for major change programmes.	The Chief Operating Officer post was filled in March 2023. While the Head of Finance post was vacant for 4 months in 2023, this has now been filled and the executive team is more settled. **Complete**

SPPA, NHSPSS and STPS

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