



Scottish Government

2015/16 Annual audit
report

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Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively (www.audit-scotland.gov.uk/about/).

Mark Taylor, Assistant Director, Audit Scotland is the engagement lead for the external audit of the Scottish Government for 2015/16.

This report has been prepared for the use of the Scottish Government and no responsibility to any member or officer in their individual capacity or any third party is accepted.

The information in it may be used by the Auditor General in support of her wider responsibilities, including reporting to the Scottish Parliament.

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Key messages

Audit of financial statements

- The Auditor General's opinion on the 2015/16 financial statements is unqualified.

Financial management and sustainability

- Effective overall management of the 2015/16 budget.
- Spending in 2015/16 within the limits authorised by the Scottish Parliament.
- Effective financial management, with developments in progress as new financial powers take effect.

Governance and transparency

- Sound overall governance in 2015/16; governance review completed with new structure proposed.
- Systems of internal control operated effectively in 2015/16, with scope for improvements in some areas.
- Action on-going to secure sufficient resource for successful delivery of the internal audit plan.
- Commitments to continue to enhance financial transparency.

Performance and value for money

- Scope for greater alignment of resources and actions to the National Performance Framework.
- Clearer planning for change needed to facilitate the assessment of progress and measure success.
- Workforce capacity needs to be maintained and sufficient to meet current and future demands.

Introduction

1. This report is a summary of our findings arising from the 2015/16 audit of the Scottish Government.
2. Scottish Government officials are 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
 - publishing with the financial statements an annual governance statement and a remuneration report.
3. Our responsibility as external auditor 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 prepared by management with the oversight of those charged with governance. This does not relieve management of its 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. Officers have considered these and have agreed to take the specific steps in the column headed "Management action/response". We recognise that not all risks can be eliminated or even minimised. What is important is that the Scottish Government understands its risks and has arrangements in place to manage them. The Scottish Government Audit and Risk Committee, and the successor committee under the revised governance structure, should ensure that it is satisfied with proposed action and have mechanisms 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.
9. 2015/16 is the final year of the current five year audit appointment. From 2016/17 the auditor of the Scottish Government will continue to be the Auditor General for Scotland, who will be supported by Audit Scotland.

Audit of the 2015/16 financial statements

Audit opinions

Financial Statements	<ul style="list-style-type: none">• The Scottish Government's consolidated accounts for 2015/16 give a true and fair view of the state of its financial affairs and of its net expenditure for the year.• The financial statements have been properly prepared in accordance with the 2015/16 Government Financial Reporting Manual (the FReM) and the requirements of the Public Finance and Accountability (Scotland) Act 2000, and directions made thereunder by the Scottish Ministers.
Regularity	<ul style="list-style-type: none">• In all material respects, the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance.• The sums paid out of the Scottish Consolidated Fund were applied in accordance with section 65 of the Scotland Act 1998.
Other prescribed matters	<ul style="list-style-type: none">• The part of the Remuneration and Staff Report to be audited has been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers.• The information given in the Performance Report for the financial year is consistent with the financial statements.

Submission of financial statements for audit

10. We received the unaudited Scottish Government core financial statements on 9 June 2016 and the first version of the unaudited Scottish Government consolidated accounts on 29 July 2016, in accordance with the agreed timetable.
11. In a departure from previous years, the consolidated accounts did not include Scottish Government core-only balances and disclosures. Subsequent versions of the accounts contained further, significant presentational changes. These were made as part of the Scottish Government's programme to develop financial reporting and to align with the wider HM Treasury led *Streamlining and Simplifying Accounts* project.
12. We are content that the revised format of the accounts meets the requirements of the Government Financial Reporting Manual (the FReM). We are also of the view that the revised presentation of information on the use of resources improves the accounts.
13. The 2015/16 FReM introduced changes to the annual report section of the accounts. The accounts presented for audit did not include a complete annual report and we did not receive a full version until late in the audit process; there were also delays in completing the remuneration report.
14. Earlier notification of proposed changes to the form and content of the accounts would have allowed more time for us to consider the changes relative to the accounting and reporting standards, and

would have facilitated completion of the audit within the agreed timetable.

15. In a period of continuing change, the Scottish Government will wish to continue to reflect on the presentation of its accounts and related information. We recommend that the Scottish Government considers future changes to the accounts earlier in the process and would encourage early discussion with audit on its proposals.

Appendix IV – Action Plan Point 1

16. The working papers provided in support of the accounts were generally of a satisfactory standard. The Scottish Government staff provided good support to the audit team and we substantially completed our audit on 9 September 2016.

Overview of the scope of the audit of the financial statements

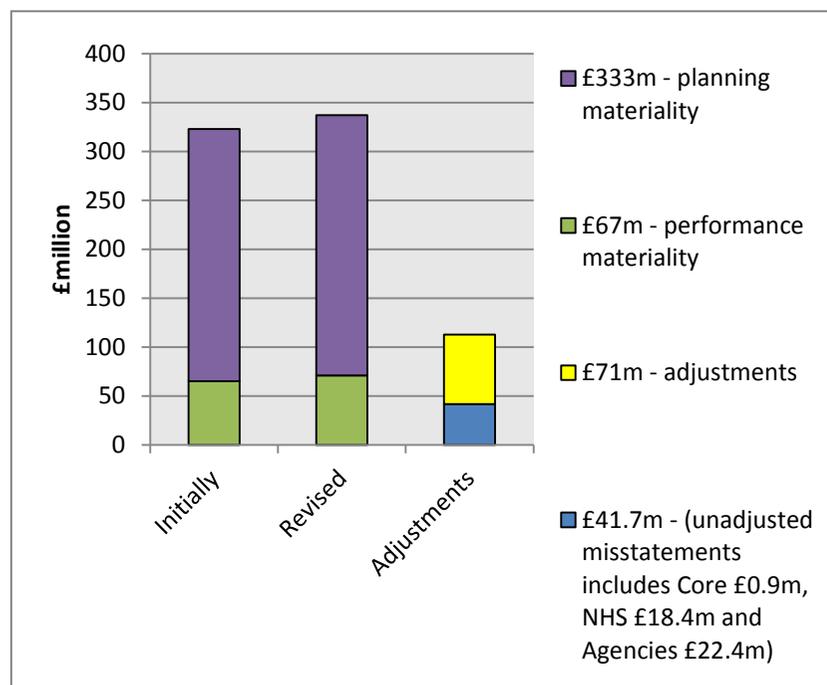
17. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our draft Annual Audit Plan presented to the Scottish Government Audit and Risk Committee (SGARC) on 17 March 2016.
18. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken any non-audit related services. The 2015/16 agreed notional fee for the audit was £987,100 and, as we did not carry out any work additional to our planned audit activity, the notional audit fee remains unchanged.

19. 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.
20. [Appendix I](#) sets out the audit risks identified at the planning stage and how we addressed each risk in arriving at our opinion on the financial statements.
21. 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.
24. We summarised our approach to materiality in our Annual Audit Plan. We revised our planning materiality for 2015/16 on receipt of the unaudited accounts to £333 million (1% of the total outturn).
25. We also set a lower level, known as performance materiality, when defining our audit procedures. This is determined to ensure that uncorrected and undetected audit differences do not exceed our materiality level. Performance materiality was set at £67 million (i.e. 20% of materiality) although in practice we work to lower materiality levels, meaning individual errors between £10 million and £20 million may be material depending on their nature and impact.
26. We report all misstatements greater than £100,000. No matters arose during the audit that required us to revise our materiality levels.

Materiality

22. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit procedures. We assess the materiality of uncorrected misstatements, both individually and collectively.
23. 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.

Exhibit 1: Overall materiality misstatements



Source: Audit Scotland: 2015/16 Annual Audit Plan and audit conclusions

Evaluation of adjustments

27. A number of presentational and monetary adjustments were identified during the audit. These were discussed with senior finance officials who agreed to make the necessary adjustments. Gross monetary misstatements totalled £71 million (Exhibit 1) were therefore corrected; the overall effect of these amendments was to increase comprehensive net expenditure by £19 million and decrease net assets by the same amount.

28. We are required to report to those charged with governance all unadjusted misstatements which we have identified during the course of our audit, other than those of a trivial nature. The total unadjusted misstatements identified during the audit were £41.7 million (gross), of which £0.9 million relates to the Scottish Government core financial statements, £18.4 million relates to the NHS and £22.4 million relates to Executive Agencies. If these adjustments had been made, the potential net impact would be to reduce total comprehensive net expenditure in the Scottish Government consolidated accounts by £4.5 million and increase net assets by £4.5 million.
29. We are content that no adjustment is required in relation to the core misstatement (which relates to 2016/17 expenditure included in the 2015/16 accounts). The auditors of the relevant NHS bodies and Executive Agencies were also content that no adjustments were required in relation to the misstatements in respective accounts. More information is provided in Table 1, paragraph 38.
30. The total value of adjustments exceeds our performance materiality level of £67 million and we have considered the implications of this for our audit. The largest adjustment of £33 million was a planned change to European Structural Fund (ESF) income and expenditure (no net impact on the accounts) to reflect the expected closure position of the programmes in light of the July 2016 declaration. A further adjustment of £14 million was made for the creation of two new provisions which also related to ESF (paragraph 34).

31. Overall, we are content that the adjustments are not representative of wider misstatement in the accounts. As a result there was no requirement for us to extend our audit work.

Significant findings from the audit

32. International Standard on Auditing 260 (ISA 260) requires us to communicate to you significant findings from the audit as detailed below:

- 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 that in the auditor's professional judgement, are significant to the oversight of the financial reporting process.

33. The following table details those issues or audit judgements that, in our view, require to be communicated to those charged with governance in accordance with ISA 260.

Table 1: Significant findings from the audit

Significant findings from the audit in accordance with ISA 260

European Structural Funds (ESF)

34. The financial statements include £92 million (representing a conversion of €117 million) of ESF funding receivable from the European Commission (EC), for expenditure the Scottish Government has declared in 2015/16 for programme funding. The three suspensions and one interruption of the four ESF programmes remained in place throughout the 2015/16 financial year. In order to lift the suspensions, the Scottish Government made self-corrections of €36 million to declared expenditure in its payment request to the EC in July 2016, which represents a permanent loss of grant of €14 million (£11 million), being the proportion of expenditure funded by the EC. This amount may increase if further ineligible areas of spend are identified in projects. The Scottish Government included a provision of £11 million in its accounts to reflect this position. A second provision of £3 million recognises that the Scottish Government has received £3 million more from the EC than the level of grant expenditure made.

The actual amounts involved will only be determined when final calculations for the 2007-13 programmes are completed in 2017. More details are provided at paragraphs 116 to 122 below.

Significant findings from the audit in accordance with ISA 260

Resolution – The 2015/16 accounts include two provisions totalling £14 million. We are content with the Scottish Government's accounting treatment. We will keep the accounting implications arising from the closure of these programmes under review in 2016/17.

Student Loans: restatement of opening balance

35. The financial statements include a £104 million restatement of opening balances relating to student loans. The effect of this was to decrease deferred income (in payables) by £104 million and decrease student loan investments (in financial assets) by the same amount. The restatement relates to amounts received from HMRC in prior years that were unallocated to individual student records by the Student Loans Company.

Amounts received from HMRC are based on a calculation by HMRC of Scotland's share of all receipts. The information provided to the Scottish Government from the Student Loans Company shows receipts matched to individual student records and is not as up to date as the information provided by HMRC on an overall level.

Resolution: The Scottish Government has included a note in its consolidated accounts to explain the reasons for the restatement and its impact. We are content with the Scottish Government's accounting treatment and disclosures.

Commitments under Service Concession Arrangements

36. Non-profit distributing (NPD), public private partnerships (PPP) and private finance initiative (PFI) transactions are accounted for in accordance with IFRIC 12: Service Concession Arrangements. Where the transaction is deemed to be 'on balance sheet', the substance of that contract is that the Scottish Government has a finance lease, with the asset recognised as a non current asset in the Scottish Government's statement of financial position. The contracts disclosed in the consolidated financial statements relate to the NHS bodies in Scotland, Transport Scotland and the Scottish Prison Service.

The Scottish Government has correctly accounted for these contracts in the statement of financial position. The FReM also requires the disclosure of commitments in respect of future capital payments and service charges in the notes to the financial statements. Future service charges are not disclosed in the Scottish Government's 2015/16 financial statements because the information is not included in

Significant findings from the audit in accordance with ISA 260

the audited financial statements of the NHS bodies. NHS bodies in Scotland are required to comply with the NHS Accounting Manual and the 2015/16 version did not reflect the current disclosure requirements of the FReM.

Resolution: We are content with the Scottish Government's non-disclosure of the future service charges on the basis that non-disclosure would not impact on the understanding of the overall financial position reported in the Scottish Government's consolidated financial statements. We understand that this matter will be considered as part of the update to the NHS Accounting Manual for 2016/17.

Transport Scotland – valuation of road network

37. To ensure that the depreciated replacement cost of the trunk road network reflects inflation, Transport Scotland uplifts the unit rates of each element of the network using a rate known as the Baxter index which is published by the Department for Business, Innovation and Skills. Due to the timing of this information, the figure for quarter three is routinely used to produce the year-end road network valuation for the annual financial statements. A further calculation is required each year when the quarter four figure is received, to assess whether applying this figure would materially affect the figures stated in the financial statements. In 2015/16 the Baxter index movement between Q3 and Q4 represented a 1.14% decrease, reducing the net book value of the trunk road network by £202 million.

A number of errors in the translation of road network data held on Transport Scotland databases onto the road asset valuation system (RAVs) resulted in the roads, land and structures values produced for the trunk road network valuation being incorrectly stated. Corrections resulted in the net book value of the trunk road network increasing by £581 million (i.e. £123 million increase in roads value, £381 million increase in land value and £77 million increase in net structures value).

Resolution: As the Baxter index movement is above the overall materiality level, an adjustment has been made in the final version of the Transport Scotland accounts to reduce the net book value of the trunk road network by £202 million. The corrections made to the data held on RAVs increased the trunk road network by £581 million. Therefore the resulting effect of these adjustments on Transport Scotland's accounts was to increase the value of the trunk road network by £379 million. Transport Scotland's auditors are content with the corrections applied.

Significant findings from the audit in accordance with ISA 260

Unadjusted misstatements in accounts

38. The total unadjusted misstatements in the accounts are £41.7 million (gross), with the two largest elements being in NHS bodies and agencies:
- NHS Grampian: Notified post year-end of a clinical negligence claim with an estimated value of £7.5 million. The Board disclosed this as a post balance sheet event in note 28 of their financial statements and has not adjusted the financial statements, as the overall net impact to the board is nil.
 - Transport Scotland's financial statements include an unadjusted misstatement of £20 million relating to the timing of trunk roads valuation of privately financed assets under construction.

Resolution: The potential net effect of the total misstatements would be to reduce total comprehensive net expenditure in the Scottish Government's consolidated accounts by £4.5 million and increase net assets by £4.5 million. Based on the work of the relevant external auditors we are content with the classification and treatment of the unadjusted misstatements.

NHS Ayrshire and Arran – additional support from the Scottish Government

39. In the accounts submitted for audit, the board recognised a prepayment of £1 million in the Balance Sheet, representing the costs of two March 2016 public holidays. The auditor's view is that the inclusion of this prepayment represented non compliance with accounting regulations. To avoid a modified audit opinion, the prepayment was removed from the accounts and service costs increased above the Revenue resource limit (RRL) target. The Director of Finance discussed this with the Scottish Government and the Scottish Government provided an additional allocation of £1 million in June 2016, to ensure NHS Ayrshire and Arran remained in financial balance.

The external auditors recommended that the Scottish Government should ensure that individual health boards have robust financial planning arrangements in place to prevent additional allocations of funding being required to achieve financial balance, and thereby reduce the financial risk to the Scottish Government.

Resolution: We note the explanation reported by the Health Board's external auditors. There is no impact on our audit of the Scottish Government's consolidated accounts.

Future accounting and auditing developments

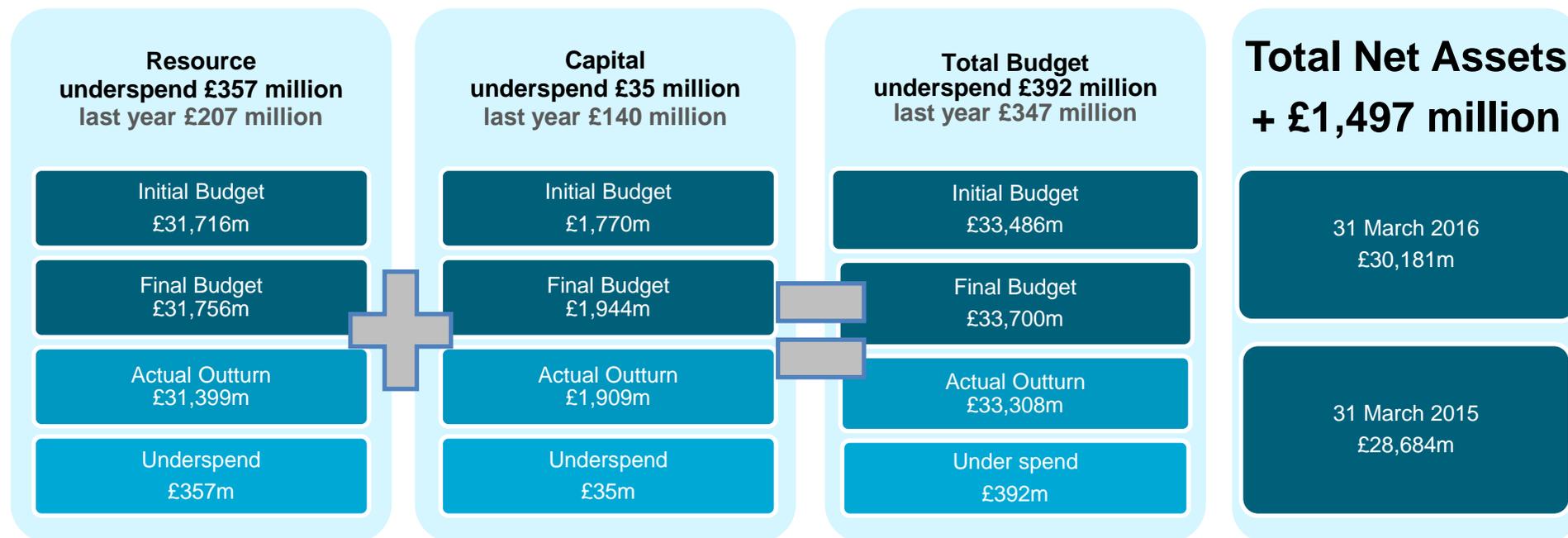
Code of Audit Practice

40. A new Code of Audit Practice applies to public sector audits for financial years starting on or after 1 April 2016. It replaces the Code issued in May 2011. It outlines the objectives and principles to be followed by auditors and is part of the overall framework for the conduct of public audit in Scotland.
41. The new Code increases the transparency of our work by making more audit outputs available on Audit Scotland's website. In addition to publishing all annual audit reports on our website, annual audit plans and other significant audit outputs will also now be made available online for all audited bodies. This is irrespective of whether the body meets in public or makes documents such as audit committee papers routinely available on its own website.
42. Also, under the new Code, appointed auditors are required to provide conclusions on the four dimensions of wider-scope public audit:
 - financial sustainability
 - financial management
 - governance and transparency, and
 - value for money.

Public Sector Internal Auditing Standard

43. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued a revised public sector internal auditing standard. We will assess the Scottish Government Internal Audit Directorate against this revised standard as part of our 2016/17 audit.

Financial management and sustainability



Financial planning

Budget management

44. The Scottish Government’s overall budget consists of the Scottish Block Grant determined within the framework of public expenditure control in the United Kingdom and other sources of income, mainly Non-Domestic Rates, funding connected with European programmes of financial assistance and receipts from the devolved taxes. The Block Grant is calculated using the Barnett formula which

adjusts the grant on the basis of a population share of changes in comparable programmes of expenditure in the rest of the UK. This was adjusted for the devolved taxes for the first time in 2015/16. The UK Parliament votes the necessary provision to the Secretary of State for Scotland who makes grants to the Scottish Government into the Scottish Consolidated Fund.

45. The Scottish Parliament approves the resources to be used by all the bodies whose expenditure is payable out of the Scottish Consolidated Fund by passing the annual Budget Act. The majority of the Scottish Budget relates to spending programmes and

administration costs covered by the Scottish Government consolidated accounts, but amounts are also allocated to other parts of the Scottish Administration and direct-funded bodies.

46. The Scottish Government is required to manage overall spending within both the Scottish Budget and UK Treasury limits. The consolidated accounts reflect the areas that it is directly responsible and accountable for. They include spending against the relevant components of the Scottish Budget. Separate accounts are prepared by other bodies to reflect their own accountability to Parliament.
47. Budget management during 2015/16 was effective in managing overall spending. The Scottish Government operated within its budget, resulting in an overall underspend of £392 million (1.2% of final budget) - resource by £357 million and capital by £35 million. Table 2 opposite, shows a summary of the amounts spent in each portfolio.
48. Information on variances in each portfolio is shown in the accounts. This, for example, shows that Health, Wellbeing and Sport overspent by £116 million, largely due to change in budgeting treatment of Non-Profit Distributing investment projects in Edinburgh and Dumfries (paragraph 53). Rural Affairs, Food and Environment overspent by £11 million, due to the provision of a loan scheme to compensate for the late payments to farmers of Common Agricultural Policy (CAP) subsidies (paragraph 107). The largest portfolio underspend was in Education and Lifelong Learning mainly due to technical adjustments to the student loan balance. The

underspend in Social Justice, Communities and Pensioners' Rights was mainly due to reduced capital and revenue spending in demand-led housing projects.

Table 2: Scottish Government outturn against budget 2015/16

Portfolio	Outturn £m	Budget £m	Over / (under) spend £m
Finance, Constitution and Economy	528	604	(76)
Health, Wellbeing and Sport	12,599	12,483	116
Education and Lifelong Learning	2,773	2,969	(196)
Fair Work, Skills and Training	268	270	(2)
Justice	2,374	2,399	(25)
Social Justice, Communities and Pensioners' Rights	11,454	11,617	(163)
Rural Affairs, Food and Environment	522	511	11
Culture, Europe and External Affairs	203	220	(17)
Infrastructure, Investment and Cities	2,290	2,321	(31)
Administration	183	192	(9)
Crown Office and Procurator Fiscal Service	114	114	-
Total	33,308	33,700	(392)

49. Total Managed Expenditure (TME) is the total budget agreed with HM Treasury, and is used by the UK Government to manage its spending on the Scottish Block. This varies slightly from the budget approved by the Scottish Parliament, largely for technical reasons reflecting differences between accounting rules and UK budget rules. A reconciliation is included at Note 21 to the Scottish Government's consolidated accounts.
50. TME is categorised as either Annually Managed Expenditure (AME) or Departmental Expenditure Limit (DEL). AME is not subject to firm multi-year limits and does not impact on the Scottish Government's spending power. DEL is subject to greater control, with a particular focus on fiscal DEL as a measure of real spending power. This excludes depreciation, some impairment and other technical accounting non-cash items.
51. In June 2016, the Cabinet Secretary for Finance and the Constitution announced the provisional outturn for 2015/16, reporting that the fiscal DEL budget was underspent by £115 million (£75 million resource and £40 million capital). The Scottish Government is able to carry forward the full amount into 2016/17.
52. The Scottish Ministers lay before Parliament a statement of total audited outturn for the preceding financial year against the final Budget for the Scottish Administration. This forms an important part of the Scottish Government's accountability to the Scottish Parliament.

NPD charges and capital borrowing

53. We reported in October 2015 that the Office for National Statistics (ONS) was considering how the Aberdeen Western Peripheral Route, which is a Scottish Non-Profit Distributing (NPD) investment project, should be classified in the National Accounts. In accordance with HM Treasury Consolidated Budgeting Guidance, budget treatment of these projects is determined by their position in the National Accounts. The ONS decided to classify the Aberdeen Western Peripheral Route as a public sector project. In view of the similarities in the structures of the funding models, the Scottish Government adopted a similar budget treatment for three further projects (Edinburgh Sick Kids Hospital, Dumfries & Galloway Royal Infirmary and the National Blood Centre). The effect of this was to require HM Treasury capital budget cover at the point of initial investment, rather than revenue budget cover for the annual payments over the lifetime of the contract.
54. This resulted in charges against fiscal DEL budgets of £109 million for 2014/15 and £283 million for 2015/16, which required to be managed within budget limits. This meant that initial spending plans had to be modified to accommodate £392 million (£328 million capital and £64 million resource¹) of NPD expenditure within overall budget limits. This effectively reduced the Scottish Government's spending power in 2015/16.

¹ The impact on resource arose because the £109 million charge for 2014/15 required to be met from the anticipated carry forward for that year: £45 million was met from the capital underspend and £64 million from the resource underspend.

55. The Scottish Government was successful in managing its planned spending in 2015/16 to remain within overall budget limits. It did this by reviewing its existing commitments and re-prioritising spending across its budgets, including the funding provided to a number of public bodies. The most significant consequences are reflected in the commentary on significant variances included in the consolidated accounts. Some further information is also included in the accounts of the public bodies affected.
56. Decisions about how to manage within the 2015/16 budget were taken by Scottish Ministers. This was achieved through the combination of measures. The most significant of these included:
- release of contingency from the Queensferry crossing programme – as the programme has proceeded, budget provisions for anticipated inflation and other contingencies have not been required for these purposes.
 - re-profiling of loans to Scottish Water – the Scottish Government funds Scottish Water's five year investment programme. Loans made during 2015/16 for this purpose were reduced from those originally anticipated, being delayed until nearer the point when Scottish Water needs this cash funding.
 - cancellation of the women's prison at Inverclyde - the Scottish Ministers have previously announced changes to plans for the prison estate. The consequential reduction in planned spending in 2015/16 was able to be deployed in managing the overall budget.
- postponement of uncommitted grants and lower than forecast expenditure on demand-led capital funding schemes - this had an impact over a number of portfolios, the most significant of which was in the Housing and Regeneration budget (within the Social Justice, Communities and Pensioners' Rights portfolio).
57. The initial budget for 2015/16 anticipated that new capital borrowing powers introduced by the Scotland Act 2012 would be used, and £306 million of the capital budget was established on this basis. HM Treasury agreed exceptional arrangements for 2015/16 so that the £283 million budget impact of the NPD classification was set against capital borrowing limits. In managing the overall position against budget the Scottish Ministers decided in the interests of prudent financial management that the £23 million balance was not required to finance capital spending.
58. Work on the existing four NPD projects is continuing, and the remaining capital budget charges associated with them will need to be managed within budgets in future years alongside capital expenditure postponed from 2015/16. The Scottish Government is considering options for financing its investment programme in the context of increased capital borrowing powers that will be available from 1 April 2017 as a result of the Scotland Act 2016.

2015/16 financial position

59. The Consolidated Statement of Financial Position summarises what is owned and owed by the Government. This shows taxpayers' equity – an accounting measurement of the amount invested by taxpayers that has continuing public benefit. It shows how much of

this has arisen from the application of revenues (including the Scottish Block Grant and devolved taxes) and that which has resulted through changes over time in the value of physical assets.

60. The Statement of Financial Position includes:

- items which are owned, have already been funded from revenues and will provide continuing economic benefit in future periods. These increase taxpayers' equity.
- items which are owed and expected to require to be funded from future revenues. These decrease taxpayers' equity.
- an analysis between amounts that will release or require funding within a year and those which will be carried into future years.

61. There are no significant concerns about the overall financial position. The performance report (which forms part of the annual report) contains commentary on the statement of financial position and its components and is a significant improvement this year.

Financial management

62. 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 DG Finance and other members of the finance function 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
- audit and risk committee members provide a good level of challenge and question significant variances.

63. Based on our audit work, our review of board and audit committee papers and through our attendance at the audit and risk committees we conclude that the Scottish Government has appropriate financial management arrangements in place.

Transparency of reporting

Budget reporting

64. The processes for setting, revising and reporting outturn against the Scottish Budget have remained broadly consistent for a number of years and are based on agreement between Scottish Government and the Finance Committee of the Scottish Parliament. The construction and management of the Scottish budget is becoming increasingly complex as new financial powers come into effect.

65. Our work in 2015/16 included a review of transparency of current budget reporting, assessing whether existing processes were applied consistently across financial years and portfolios. We will discuss our preliminary findings with the Scottish Government and thereafter produce a report to management.

Financial reporting

66. The Scottish Government has commenced a programme of work to review and broaden its financial reporting in the context of the new financial powers. This is considering the preparation and content of financial reports at all stages of the budget process - from preparation of the draft budget through to the suite of annual accounts that are audited and published.
67. As part of this work, the Scottish Government has reviewed the content of the 2015/16 consolidated accounts, to identify opportunities for improvement to explain how the Scottish Budget as a whole is funded and to make links with other accounts for the Scottish Consolidated Fund and the Devolved Taxes Account prepared by Revenue Scotland. It has also sought to streamline and simplify elements to the accounts to make them more accessible. These are welcome developments.
68. In a departure from the format of previous years' accounts, the consolidated accounts did not include Scottish Government core only balances and disclosures, as reported in paragraph 11.
69. In previous years the consolidated accounts reported a separate core statement of financial position and related notes. Information on staff numbers and costs was also reported. This information is no longer available. We are content that the revised format of the accounts meets the requirements of the FReM and overall improves the readability of the accounts.
70. As part of the Scottish Government's programme for improving financial reporting, it should consider how it can enhance transparency by including more detailed information on key aspects e.g. the value of the overall NHS estate.
71. The FReM sets out disclosures to be included in remuneration and staff reports. The following information has not been included in the Scottish Government's 2015/16 report:
 - Number of senior civil service staff (or equivalent) by band
 - Staff composition - analysis of the number of persons of each gender who were directors, senior civil servants (or equivalent) and employees of the company
 - Expenditure on consultancy
 - Off-payroll engagements - summary data on the use of off-payroll arrangements.
72. As the Scottish Government is required to comply with the principles of the FReM and not the detailed requirements, we concluded that there are no specific requirements for the information listed to be included in the consolidated accounts. The Scottish Government's decision on disclosure in this case is partly due to the availability of data and because of the wide-range of information already available on its website. This includes information on workforce, pay and diversity and the disclosure of individual items of expenditure as required by the Public Services Reform (Scotland) Act 2010.
73. There will be much still to do to develop financial reporting as further financial powers are introduced and to respond to the Parliament's

needs. The Scottish Government's programme of work is continuing. In its legacy paper, the Parliament's Public Audit Committee said that clear, transparent and comprehensive public sector financial and performance reporting is vital. Key elements for the Scottish Government to consider include:

- the draft budget and materials to support in-year budget revisions, so that these show how the key components of the budget have been established and how planned expenditure is expected to be funded overall. The Scottish Parliament's Finance Committee has announced a review of the budget process, involving parliamentary and government officials alongside a panel of external experts including the Auditor General.
 - continued development of the suite of annual accounts that contain detailed outturn information on the different components of the budget, so that the information provided is set in the context of the budget as a whole, and the overall position is clear.
 - accompanying performance reporting, so that it is clearer what spending is aiming to achieve and how this contributes to the Government's overall purpose and specific outputs and outcomes (see also paragraphs 75 and 76 below).
74. We have previously reported on the importance of consolidated accounts for the whole of the Scottish public sector. These would help provide an overall picture of the financial position. They would also provide the Scottish Parliament, taxpayers and others a fuller picture and understanding about public spending and the longer-

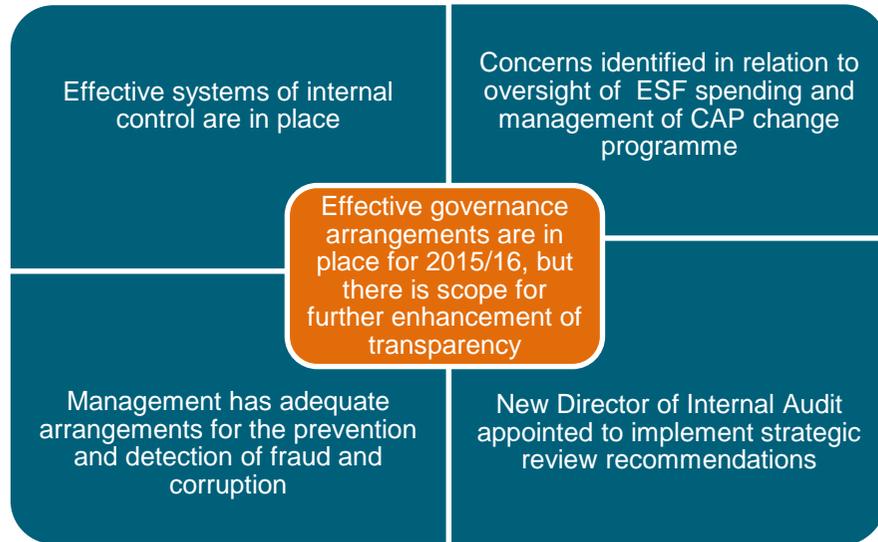
term implications for public finances. The Scottish Government has committed to continue to enhance financial transparency.

Performance reporting

75. The 2015/16 consolidated accounts comply with the principles of the FReM as they contain a performance report and an accountability report. The performance report summarises financial performance for the year, with particular emphasis on performance against budget. It also contains some specific performance information which is required by current guidance on supplier payment performance compared with policy targets and signposts where more information is available on sustainability and environmental performance. For information on the Scottish Government's progress towards its overall aims and objectives, users of the accounts are directed to the National Performance Framework.
76. Consequently, while the performance report provides analysis of some key aspects of financial performance, the consolidated accounts focus on the Government's finances. They do not report on the performance of the Scottish Government as a whole. A more rounded account of the Scottish Government's overall performance would enhance reporting to the Scottish Parliament and the public, and help strengthen accountability and scrutiny.

Appendix IV – Action Plan Point 2

Governance and transparency



Corporate governance

- 77. The Scottish Government, through its Principal Accountable Officer is responsible for establishing arrangements for ensuring the proper conduct of its affairs and for monitoring the adequacy of these arrangements.
- 78. The Scottish Government has effective overarching and supporting governance arrangements which provide an appropriate framework

for organisational decision-making. Risk management processes are well-developed and effective.

- 79. During 2015/16, the core Scottish Government was managed by a Strategic Board, chaired by the Permanent Secretary as Principal Accountable Officer. The Board met quarterly and was supported in its role by six corporate boards as illustrated below. All boards include non-executive directors as members appointed by the Permanent Secretary.



80. An overarching Scottish Government Audit and Risk Committee (SGARC) was supported by four portfolio-aligned audit and risk committees as illustrated below:



81. The audit and risk committees met at least quarterly to consider relevant matters. During 2015/16, 14 non-executive directors participated on the Scottish Government’s audit and risk committees and corporate boards. Their involvement provided challenge and support to senior management and brings an independent perspective.

82. During 2015/16, the Permanent Secretary commissioned a review to explore opportunities to streamline corporate governance arrangements while ensuring principles of effectiveness and transparency are maintained. It is good practice for organisations to carry out periodic reviews of governance to ensure they are fit for purpose and serve the quickly changing context and the continuing pressures on resources.
83. The Scottish Government’s review identified four key areas for improvement: structure; purpose; communication; and culture. The proposals provide the potential to achieve these aims; their effectiveness will depend on how the new arrangements are applied in practice, underpinned by the shift in organisational culture which the Scottish Government envisages.
84. The proposed structure which combines the corporate boards and portfolio audit and risk committees is illustrated below, which includes the Scottish Government Audit and Assurance Committee (SGAAC):



85. Notwithstanding the specific organisational arrangements that are implemented, culture and behaviour have a critical role. This will include the value everyone involved places on governance and accountability processes, including the importance of alternative views, perspectives and challenge and critical evaluation of performance. Non-executive directors play a key role in providing scrutiny and challenge as well as increasing transparency and accountability and improving decision-making. In implementing a revised approach it is also important to recognise the leadership role that the Scottish Government has for other public bodies.

86. We plan to review the effectiveness of the new arrangements as part of our on-going audit work.

Transparency

87. Good governance also involves making sure that all aspects of the decision-making process operate transparently within the organisation. This includes clarity about the activity that has taken place and appropriate record-keeping to capture the timing, substance and nature of discussions. How this operates in practice will be another measure of the success of the new governance arrangements.

88. Transparency of budget and financial reporting is also important, including a clear reconciliation between expenditure and the outturn against budgets and identification and explanation of any significant movements in budget during the year.

89. The Scottish Government includes information on resource and capital major variances in the consolidated accounts. This supports understanding of its activities during the year. As part of our audit, we highlighted areas where the explanations could be expanded and clarified to enhance transparency. We also set out some areas where we think financial and performance reporting could be further developed in paragraphs 66 to 76 above.

Minutes of board meetings

90. Systematic review of Scottish Government board minutes helps us build an understanding of the context for Scottish Government

business and is an important part of our processes for identifying matters that may have a bearing on the accounts and our audit. In our 2014/15 Annual Audit Report we reported delays in receiving minutes of management boards. These delays continued during the 2015/16 financial year.

91. We have now received minutes of boards covering the 2015/16 year. Some minutes of relevant board meetings required for the 2015/16 audit were not received until June 2016 onwards. We noted that the Strategic Board minutes provided to us, were as published and were not supplied on a timely basis e.g. the December 2015 minutes were published on the Scottish Government's website in July 2016. The risk remains that the audit team is not sighted on important information which may be relevant to amounts and disclosures in the accounts.
92. There are as yet no systematic arrangements for our access to board minutes on a regular and timely basis. We understand this is being taken forward as part of the implementation of the Scottish Government's governance review.

Appendix IV – Action Plan Point 3

Internal control

93. We carried out testing of internal controls on those accounting systems which we regard as significant for the production of the financial statements. We reported our findings to management in May 2016.

94. No material weaknesses in the accounting and internal control systems were identified during the 2015/16 audit which could adversely affect the organisation's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

Internal audit

95. We carry out an annual assessment of internal audit to determine the extent to which we can place reliance on its work. Our review this year concluded that the Scottish Government's Internal Audit Directorate (IAD) operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place.
96. We have reported previously on the pressures on IAD resources and the impact on its work programme; some public bodies receiving services from IAD had expressed concerns about IAD's capacity to deliver its plan and provide the assurance they require. IAD continued to face resource pressures in 2015/16 with further demands and competing priorities, particularly in relation to its European funding audit work.
97. The temporary Head of Internal Audit (HIA) undertook a strategic review of IAD and presented her findings to the Scottish Government Audit and Risk Committee in December 2015. The review identified the appointment of a director level HIA as critical to enable the changes required in internal audit. The Scottish Government moved quickly to appoint a new, substantive Director of

Internal Audit and the successful candidate took up post in April 2016.

98. The new Director of Internal Audit and her management team are working to ensure that the other strategic review recommendations are implemented, including those relating to structures and resources. IAD resources increased in 2015/16 and it was better placed to deliver against its plan.
99. The strategic review report signals a clear intention to review how the European funding audit work is arranged and resourced. Until resourcing is addressed fully, there is a risk to the successful delivery of the internal audit plan and the assurances that those charged with governance require.
100. With the extension of devolved powers and increased fiscal responsibility, it is critical that the Scottish Government's internal audit function is strengthened. It is also important that management continue to implement the findings of the strategic review to ensure resourcing issues are resolved.
101. We understand that the Scottish Government has requested the individual who carried out the strategic review of internal audit to return to undertake a review of the extent to which the recommendations have been implemented.

IT audit

102. While it is never possible for any organisation to completely eliminate the threat from a cyber-attack, it is important that

organisations demonstrate an awareness of good practice to minimise the risk. Overall the Scottish Government is aware of the risks associated with cyber security and is taking appropriate action to mitigate those risks.

103. A draft cyber strategy prepared during 2015 sets out a range of outcomes that the Scottish Government plans to deliver by 2020. Although this strategy remains to be formally approved, it has been used throughout 2015/16 to influence the activities of the Office of Protective Security (OPS). Although some of the strategic outcomes are being developed, the planned Security and Information Assurance Board (SIRAB) has not yet been formed. In the absence of SIRAB there is no clear governance process to monitor delivery of the strategy.
104. Processes and procedures have been implemented for the prevention and monitoring of cyber security threats. We note that the organisation operates the SCOTS Network that has achieved and maintains accreditation to the Public Services Network (PSN) and complies with the principles set by the International Information Assurance standard ISO/IEC 27001. These require organisations to demonstrate good practice in the operation of their overall information security arrangements. PSN accreditation represents a good achievement for the organisation that is supported by comprehensive information, communications and technology health checks that are conducted by external specialists including cyber security experts.

- 105. Our review, which was carried out as a joint exercise with internal audit, also highlighted some areas of improvement which will be set out in a report to management in due course.
- 106. Going forward as the threat from cyber security develops and attacks grow in magnitude and complexity it is essential that the Scottish Government continues to develop its approaches to cyber security.

Common Agricultural Policy Futures programme

- 107. The Scottish Government provides financial support to farmers and other rural businesses as part of the Common Agricultural Policy (CAP). The 2015/16 consolidated accounts include expenditure of £37 million on the Futures Programme, an IT-enabled change programme to implement CAP reforms in Scotland. Capital spending in 2015/16 was £27 million. The relevant amounts are reflected appropriately in the consolidated accounts.
- 108. The Governance Statement in the consolidated accounts notes that this programme has proved very challenging, with payments to farmers being made far later than in previous years. The Auditor General reported in May 2016 that the programme was managing its spend within the forecast cost of £178 million. This is 74 per cent above the amount included in the original business case. The report highlighted that the scope of the programme has significantly reduced and now aims only to deliver a system that is compliant with European Commission (EC) regulations, without all of the planned customer-focused enhancements and anticipated efficiencies. There is a risk that the programme budget will run out before a CAP compliant system is in place. As at 31 July 2016 the programme had spent £140.8 million, therefore a budget of £37.7 million remains. We do not expect the programme to achieve value for money.
- 109. The programme has not met key programme milestones or ministerial targets. As at 14 September, £329 million had been paid out to 17,864 farmers, crofters and rural business (97% of the estimated total number of claims), with 703 yet to receive full payment.
- 110. In the May 2016 report, the Auditor General highlighted the risk of penalties and disallowance if key deadlines were missed or the system was not fully compliant with EC regulations. In June 2016, the EC announced it was extending the payments deadline from 30 June 2016 to 15 October 2016. While this will help mitigate the risk of incurring penalties and disallowances, it does not help farmers get full payment quicker. There is still a risk of penalties and disallowances if the controls and systems in place for making payments do not meet the requirements of the regulations. Any penalties and disallowances will be subject to an assessment of specific circumstance by EC auditors, and its extent will not become evident until 2017.
- 111. To help farmers receive payments more quickly, the Scottish Government established schemes to loan funds from the Scottish budget while claims are being processed. The loans are made to farmers in advance of the claim being processed, the loan is then

repaid with the EU funds when the claim has been finalised and is paid. This introduced risk to the Scottish Government budget, including risk of duplicate or over-payments, and delays to other spending if the loans are not repaid when expected.

112. Three nationally funded loans schemes were initiated. The cash flow loan scheme and Less Favoured Area Support Scheme (LFASS) were introduced in March 2016, with the National Basic Payments loans scheme introduced in April 2016. Table 3 below summarises the amounts loaned to date and level of repayments.

Table 3: Loan payments and direct payments to farmers as at 14 September 2016

Type of scheme	Value
Cash flow loan scheme	£132,000 loaned, repayment amount being finalised.
LFASS loan scheme	£54 million loaned, no repayments to date.
National Basic Payment loan scheme	£92.9 million loaned, of which £85.1 million has been repaid.

Source: Scottish Government

113. The Cabinet Secretary for Rural Economy and Connectivity announced the launch of a new loan scheme on 13 September 2016. This will be open to all farmers and crofters who are eligible for the basic, greening or young farmer payments as part of the 2016 payment round. The deadline for applications is 12 October

2016. The Cabinet Secretary aims for the bulk of payments to be made in the first two weeks of November, and estimates loan payments of around £300 million.

114. The Auditor General concluded in the May 2016 report that programme governance had been ineffective. There had been little accountability in the programme for IT delivery leading to ineffective challenge and oversight. Management failed to deal with conflicts of interest effectively; actions were taken but these were inadequate and arrangements were not sufficient to ensure value for money.
115. This is a critical time for the programme and it is important that the Scottish Government learns from its experience of the 2015 payment year, and plans for the effective delivery of 2016 payments.
116. In his statement to the Parliament on 13 September, the Cabinet Secretary for Rural Economy and Connectivity accepted all the recommendations we made in our May 2016 report. The Cabinet Secretary has also written to the Auditor General providing an update on progress and summarising the actions that have been put in place in response to our recommendations. It is too early to assess whether these actions will be effective and we will continue to monitor progress.

European structural funds

117. The Scottish Government manages four European structural fund programmes (two programmes funded by the European Social Fund and two funded by the European Regional Development Fund).

These programmes provide financial assistance to, for example, help improve transport links, support business growth and improve skills. The 2015/16 consolidated accounts include £92 million structural fund expenditure and related funding.

118. The Governance Statement notes that three structural fund programmes for 2007-13 remained in 'suspension' during 2015/16; the fourth programme continued in 'interruption'. The European Commission (EC) procedures aim to avoid payments from the EC where there is a risk that the 'managing authority', in this case the Scottish Government, has not followed the rules on how funds are being spent. EC payments are stopped until it considers such risks have been removed:

- interruptions are relatively common across Europe and are applied where the EC considers that there may be a significant deficiency in the management and control system. Interruptions are usually resolved by the managing authority correcting expenditure declared as programme expenditure.
- suspensions represent an escalation where the EC considers that there is a serious deficiency in the management and control system or there is a serious irregularity in expenditure declared. This requires the managing authority to provide further assurances about the extent and effectiveness of controls, and correct declared expenditure.

119. The EC's action was in response to concerns and error rates reported by Scottish Government Internal Audit Directorate in its role as the 'audit authority' for structural funds. The auditors

highlighted a range of points, including the robustness of information retained by some grant recipients about how structural funds were spent.

120. The Scottish Government implemented an action plan to provide the EC with the assurances it requires about how it and the bodies in receipt of funds addressed the control weaknesses. The EC has recognised the actions taken to reduce control weaknesses and errors and, in August 2016, the suspensions for European Social Funds were lifted. In September 2016, the Scottish Government was notified by the EC of its decision to lift the remaining suspension for the European Regional Development Fund programme. Similarly, the interruption for the remaining European Regional Development Fund programme is expected to be lifted with confirmation from the EC for both to follow shortly.

121. In order to lift the suspensions, the Scottish Government made self-corrections which involved reducing declared expenditure by €36 million (approximately £30 million). Because the deadline for eligible expenditure under the 2007-13 programmes has passed, self-corrections cannot be 'recycled' to support other eligible projects. As a result, and taking into account the way in which individual projects are funded, the consolidated accounts contain a provision of £14 million to reflect a permanent loss of grant to the Scottish Government which it cannot now recover. As the suspensions and interruptions remained in place during 2015/16, amounts due from the EC accumulated. The consolidated accounts include £203 million receivable from the EC.

122. Full resolution of the 2007-13 programmes is likely to be finalised by March 2017 when the Scottish Government submits a final reconciliation to the EC which matches total grant received with total eligible project expenditure. Further audits on amounts declared are on-going and may identify further disallowable expenditure. This could have further financial consequences for the Scottish Government. We will continue to monitor closure of these programmes and will report as appropriate.
123. During 2015/16, the Scottish Government developed a management control system, which is required to achieve managing authority designation from the EC for the 2014-20 structural fund programmes. It achieved designation in July 2016. To avoid the difficulties experienced during the 2007-13 and the associated financial consequences, the Scottish Government should ensure that its arrangements for managing structural funds, and those of the other bodies receiving funding, comply fully with EC requirements.

Arrangements for the prevention and detection of fraud

124. The Scottish Government is responsible for establishing arrangements to prevent and detect fraud and other irregularity. We reviewed Scottish Government's Fraud Policy, Counter-Fraud Strategy, Whistleblowing Policy and its annual Fraud Report and how these arrangements are communicated across the organisation. We concluded that arrangements for the prevention

and detection of fraud are effective and have been satisfactorily disseminated to staff.

National Fraud Initiative in Scotland

125. The Scottish Government participates in the biennial National Fraud Initiative (NFI) exercise through uploads of payroll and accounts payable data. The NFI uses electronic data analysis techniques to compare information held on individuals by different public sector bodies and different financial systems, to identify data matches that might indicate the existence of fraud or error. The data submitted by the Scottish Government covers of all those bodies which use its payroll and accounts payable shared services in addition to its own operations.
126. We reviewed the Scottish Government's progress during 2015/16 in investigating data matches. We found that the accounts payable matches were investigated promptly with one minor error found and corrected. There were delays in investigating recommended payroll matches due to resourcing pressures. NFI is effective in detecting fraud and error in public sector organisations. In addition, it can help strengthen internal controls to protect against fraud and error. We recommend that Scottish Government improves its planning and resourcing for future NFI exercises in order to maximise the benefits of data matching, for itself and its shared service partners.

Appendix IV – Action Plan Point 4

127. The 2014/15 NFI exercise concluded with the publication of Audit Scotland's national NFI report in June 2016 which reported fraud

and error outcomes of nearly £17 million. Further information about the NFI process and the calculation of outcome figures is included in our report [The National Fraud Initiative in Scotland](#).

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

- 128.** We have reviewed the arrangements in place to maintain standards of conduct including the Staff Handbook and Civil Service and Members' Codes of Conduct. There are established procedures for preventing and detecting any breaches of these standards including any instances of corruption.
- 129.** Based on our review of the evidence we concluded that there are appropriate arrangements in place to help prevent and detect corruption and we are not aware of any specific issues that we need to record in this report.

Correspondence referred to the auditor for enquiry

- 130.** As part of our wider Code of Audit Practice responsibilities we are required to consider issues raised and follow these up as part of our risk based approach to the audit if they fall within our remit.
- 131.** In 2015/16 we received correspondence raising concerns about the process for awarding £0.15 million funding from the major events budget in connection with the 'T in the Park' music festival. We

reviewed the documents and analysis supporting the business decision to award £0.15 million.

- 132.** We concluded that there was a clear rationale for the grant at the point at which the Scottish Government committed to provide the grant to DF Concerts. This is set out in the grant award letter, which states that the grant was '....provided to assist DF Concerts and Events with operational costs related to the transition of the T in the Park event...'. The outcomes and milestones against which progress was to be monitored are also clearly articulated in the award letter.
- 133.** We also concluded that the Scottish Government had the legal authority to make the grant, under Section 23 of the National Heritage Scotland 1985 Act. The decision to award the grant to DF Concerts was a legitimate policy decision for the Cabinet Secretary, and was consistent with advice she received from Scottish Government officials. There was also budget provision for the grant, within the Culture and European Affairs budget, Major Events and Themed Years.
- 134.** There is evidence that the DF Concerts consultants' costs associated with gaining planning consent incurred in 2014 and 2015 for the 2015 event, together with the increase in venue costs, exceeded the grant Scottish Government provided. There is also evidence that Scottish Government has taken steps to confirm that the money was spent in line with the grant conditions through its review of the final report provided by DF Concerts and related invoices.

135. In our opinion, the robustness and internal clarity of the decision factors leading to the award of grant would be enhanced if there was a requirement for:
- Scottish Government staff to record, in one place, consideration of factors such as aims and objectives; options appraisal, value for money, additionality and expected outcomes
 - Organisations applying for funds to formally set out economic, financial, social and other arguments in favour of their request. Where appropriate, this could be facilitated by the completion of an application form or equivalent.
136. We understand that the Scottish Government requires flexibility to react promptly to circumstances as they arise but in our view this needs to be balanced with enhanced internal clarity and evidence to support decision-making. The Scottish Government has work on-going in this area and we plan to review progress as part of our on-going audit work.

Performance and value for money

National performance reports

137. This section summarises key themes drawn from our performance and value for money audits. Since October 2015, we have published eleven performance audit reports, which contained findings or recommendations of relevance to the Scottish Government. These are listed in Table 4 and summarised in [Appendix III](#).
138. The Scottish Parliament's Public Audit Committee (PAC) considers performance audit reports which we publish on behalf of the Auditor General for Scotland (AGS). The PAC can take a range of actions such as noting the report, referring it to another committee for consideration, asking the audited bodies concerned to provide further information, or conducting an inquiry. In many instances the PAC will ask the Scottish Government to detail how it intends to implement any recommendations made.

Table 4: Performance audit reports published in last year

Title	Publication date
Efficiency of prosecuting criminal cases through the sheriff courts	24 September 2015
NHS in Scotland 2015	22 October 2015
Health and social care integration	3 December 2015
Implementing the Scotland Act 2012: an update	10 December 2015
Community planning: an update	3 March 2016
Changing models of health and social care	10 March 2016
Common Agricultural Policy (CAP) Futures programme – an update	19 May 2016
Audit of higher education in Scottish Universities	7 July 2016
Supporting Scotland's economic growth: The role of the Scottish Government and its economic development agencies	14 July 2016
Maintaining Scotland's roads: a follow-up report	4 August 2016
Scotland's colleges 2016	25 August 2016
Superfast broadband for Scotland: a progress update	18 August 2016

Source: Audit Scotland

Key audit themes from our national reports

- 139.** The Scottish Government is leading an ambitious and complex programme of public service reform aimed at:
- improving long-term outcomes, with a focus on addressing long-standing inequalities of outcomes amongst some groups
 - supporting the drive to deliver more preventative and sustainable service models across the public sector
 - promoting better integrated and more seamless public services using collaboration and partnership working a vehicle for achieving this
 - improving overall public service quality
 - giving communities and service users a stronger voice about, and greater control over, local public services.
- 140.** A common theme in our 2015/16 performance audit reports is the potential for greater alignment of resources and actions, including those of public organisations, to the National Performance Framework (NPF). For example, audit reports identified the need to establish a clearer line of sight between NPF measures and the specific contribution of policies and initiatives, or the performance of different public bodies, to delivering these outcomes. We also found that while some major government policies, such as the Government's 2020 Vision for Health and Social Care, are clear about their long-term objectives, implementation plans are often lacking or do not contain indicators or measures which can be used to monitor progress.

- 141.** A key element of the Scottish Government's programme is public service reform often involving long-term transformation of services, in vital areas including new models for health and social care and including moves to more preventative care. Many of these programmes of reform require the Scottish Government to deliver change collaboratively with and through a range of public bodies, such as councils, universities and enterprise agencies. Several audit reports have highlighted challenges that the Scottish Government is experiencing in translating its ambitions into changes in service delivery and outcomes.

Leading and managing change

- 142.** Increasingly, the Scottish Government is trying to manage change and deliver its policy ambitions through complex sets of networks, often with multiple partners. This approach to managing change, while necessary when dealing with complex issues that span different parts of the public sector, such as ensuring outcomes focussed, preventative approaches to delivering public services and addressing inequalities, can also create issues around measuring success and the attribution of impact, due to the numbers of partners involved. This was evident in our most recent audit work on [Community Planning: an update](#) and our work on [Supporting Scotland's economic growth: The role of the Scottish Government and its economic development agencies](#).
- 143.** Working with the general public and local communities is an increasingly important focus of the Scottish Government as part of leading and managing change, to both draw on the expertise and

assets that exist within communities, and to ensure that their views are taken account of when difficult choices are made about reshaping services for the future. This provides a number of challenges both in terms of effective engagement to inform policies and successfully communicating information about changing services. We highlight areas where improved communication with the public is necessary across a number of our reports. For example, our work on [Changing models of health and social care](#) highlighted the need for a significant cultural shift to alter the way in which people access, use and receive health and social care services.

Planning for change

144. One of the areas where we identified improvements could be made across a number of audits was in planning for the changes needed to operational delivery. Clear plans and timely guidance to bridge the gap between the national policy objectives and operational delivery of public services are necessary to help partners make changes. Without clear plans it is difficult to assess progress and measure success.
145. We identified situations where the Scottish Government issued guidance later than was helpful for its partners. For example, our [Health and social care integration](#) audit found guidance on localities and performance reporting were issued too late for some partnerships which had already started to develop their own processes.

146. We found similar issues in our work on [Supporting Scotland's economic growth: the role of the Scottish Government and its economic development agencies](#). The Scottish Government's economic strategy outlined priorities and the high-level policy approach to support economic growth. However, it had not clearly set out how this would be implemented with clear targets or timescales. Individual public bodies responsible for economic growth received annual ministerial guidance letters, but the Scottish Government did not detail how public bodies contributed to the delivery of the strategy.
147. We have repeatedly reported that the Scottish Government needs to clarify what community planning is trying to achieve and how success will be measured. Without this clarity, it is difficult to assess progress. Our [Community Planning: an update](#) report recommends that the Scottish Government works with COSLA to set out the short, medium and longer term steps needed to implement their Statement of Ambition and the Community Empowerment (Scotland) Act 2015.
148. We also identified a need to improve planning for change both in terms of planning over the longer-term and financial planning for change. For example our [Changing models of health and social care](#) report recommended that the Scottish Government should:
- provide a clear framework by the end of 2016 of how it expects NHS boards, councils and integration authorities to achieve the 2020 Vision, outlining priorities and plans to reach its longer-term strategy up to 2030. This should include the longer-term

changes required to skills, job roles and responsibilities within the health and social care workforce

- estimate the investment required to implement the 2020 Vision and the National Clinical Strategy
 - ensure that long-term planning identifies and addresses the risks to implementing the 2020 Vision and the National Clinical Strategy.
149. Additional examples of recommended actions to improve longer term and financial planning were highlighted in our reports on [Implementing the Scotland Act 2012: an update](#) and [NHS in Scotland 2015](#). The Scotland Act gives, for example, new borrowing powers to Scotland. Our audit highlighted that the Scottish Government was developing a strategy for borrowing which should be progressed as a priority to help support future decisions on capital borrowing. Our work on the NHS in Scotland recommended that the Scottish Government allows NHS boards greater flexibility in managing their finances. Although some flexibility is currently possible this does not allow NHS boards to plan over the long-term with great certainty.

Measuring performance and use of data

150. Much of our performance audit work in 2015/16 highlighted issues over data to assess performance and evaluate costs. Relevant, comparative data is necessary to evaluate and improve performance and make decisions. However, a common theme identified across our performance audits related to the absence of or poor use of existing performance data to measure performance.

151. Our report [on Efficiency of Prosecuting Criminal Cases through the Sheriff Courts](#) highlighted issues around the reported measures of efficiency. Only one measure of efficiency was used to evaluate performance and this had a number of limitations. Other data was held, but was not evaluated.
152. Our audit of [Health and social care integration](#) identified that although there had been some good progress in supporting local partnerships to access data, the core integration performance indicators did not take account of the full expected benefits of the reform programme. For example, integration is anticipated to help shift the balance towards more community based or preventative settings. However, it is not clear how the indicators would measure any shift.

Alignment of performance measures with outcomes

153. Another recurring theme from our national work was a lack of alignment between performance measures and outcomes. This is important to direct focus and help evaluate progress towards delivering anticipated outcomes.
154. For example, our [Community Planning: an update](#) audit highlighted that in public sector bodies the overall balance of performance measures do not reinforce the principles of outcomes, prevention and reducing inequalities set out in the Statement of Ambition. The audit found that it is not clear that the Scottish Government has reviewed the full range of existing planning and performance reporting frameworks to assure itself that:

- They all align with the Scottish Government's 16 national outcomes
 - There is clarity about the contribution that the bodies working within these planning and performance reporting frameworks are making to the Scottish Government's five objectives and 16 national outcomes.
- 155.** Other examples around the lack of alignment between performance measures and the desired outcomes were identified in our [Audit of higher education in Scottish universities](#) and [Supporting Scotland's economic growth: The role of the Scottish Government and its economic development agencies](#). Our work on higher education recommended improvements to outcome agreements between the Scottish Funding Council (SFC) and universities. These included aligning measures used in outcome agreements with the Scottish Funding Council's strategic outcomes, using indicators which appropriately assess how activities contribute to key aims, more consistency and clarity in how outcome agreements are written and represented, and reporting against all national measures.
- 156.** Our work on economic growth highlighted another example of issues around alignment between performance measures and desired outcomes. This work found the National Performance Framework measured progress towards economic targets and outcomes, but it did not measure the contributions of policies and outcomes to delivering these outcomes.
- 157.** We highlighted some good practice where local areas were making effective use of the data they hold. For example our [Changing](#)

[models of health and social care](#) audit highlighted partnerships making good use of local data. In these examples, partnerships identified a small number of priorities to focus on, which is much more manageable than trying to change everything at once. We have made recommendations in a number of our reports about the need for the Scottish Government to assist partners in learning from each other by helping to identify and spread good practice examples. Our [Community Planning: an update](#) report highlighted that the Scottish Government was still to develop a well coordinated national programme of support for community planning partnerships (CPPs) to reflect good practice and meet individual CPPs improvement and development needs.

Local performance audit reports

- 158.** In addition to our national reports, we also undertake local work in on Scottish Government performance in key areas. As part of our 2015/16 audit, we reviewed the Scottish Government's workforce planning arrangements – the findings from this are set out later in this section.
- 159.** As indicated earlier in this report, we also reviewed how the Scottish Government manages budgets. We are completing the audit work and the report on this topic will be issued to management in due course.

Workforce planning

- 160.** During 2015/16, auditors of all public bodies reviewed workforce planning arrangements with reference to the recommendations

included in our November 2013 report *Scotland's public sector workforce*.

161. We found that the Scottish Government has workforce planning processes in place based on workforce capability and capacity requirements. The Scottish Government's capability plan is rolled forward on an annual basis and progress is monitored by the People Board.
162. The Scottish Government uses a number of approaches to manage workforce numbers and costs including:
 - a tightly controlled recruitment and retention allowance
 - redeployment
 - voluntary early severance schemes
 - pay restrictions.
163. The Scottish Government manages a number of development programmes, including modern apprenticeships, which are designed to build long-term capacity across the organisation. There is also evidence of scenario planning to inform workforce approaches. New workforce controls were agreed during 2015/16 to provide better quality management information, to make better workforce decisions and highlight pressure areas. A further development is the preparation of more detailed workforce plans at directorate and specialist level.
164. The Scottish Government's 2020 programme was set up to implement organisational change by the year 2020. The programme recognises the challenges in meeting Ministerial

priorities and delivering additional responsibilities, while working with reduced resources and delivering continuing activities during this period of change. The overall programme includes work on investing in effectiveness and matching resources to priorities. These two projects in particular will have an impact on future workforce planning arrangements with an increased emphasis on capability planning and flexible resourcing.

165. There is limited guidance on joint working and sharing of workforce planning information for central government bodies. The Scottish Government's Remuneration Group considers and provides advice on pay and reward across public bodies, to ensure alignment with Scottish public sector pay policy. The Scottish Government Delivery Bodies Group brings together chief executives from key agencies to exchange practice and engage with the Scottish Government corporate initiatives. The Scottish Government's HR Forum, which meets approximately three times each year, provides an informal information sharing function for HR practitioners. Across these formal and informal settings there is scope for a more proactive and systematic approach to be taken to the sharing of workforce planning information between central government bodies.

Appendix IV – Action Plan Point 5

166. Our current programme of performance audit work includes examining how well the Scottish Government and others are implementing or preparing to introduce the new financial powers in the 2012 and 2016 Scotland Acts. This will include reviewing the

Scottish Government's progress in securing appropriate capacity for managing the implementation of the new powers and the associated costs alongside other priorities, including its consideration of the implications of the EU referendum result. We are aiming to publish a national report on the findings from this work in spring 2017.

Appendix I: Significant audit risks

The table below sets out the audit risks we identified during the course of the audit and how we addressed each risk in arriving at our opinion on the financial statements.

Audit Risk	Assurance procedure	Results and conclusions
Risk of material misstatement in the financial statements		
<p>European Structural Funds (ESF)</p> <p>As at February 2016, the four European Structural Funds programmes remained in interruption or suspension. These procedures aim to avoid EU funds being paid over to member states where there is a risk that European rules on how the Funds are spent may not have been followed.</p> <p>The Scottish Government is working to provide assurances to the European Commission about how the Scottish Government and the bodies in receipt of funds are addressing identified control weaknesses. While this matter is unresolved, there is a risk that the Scottish Government may face penalties and may not be able to recover the full amount accounted for as income in its financial statements.</p>	<ul style="list-style-type: none"> • We will review the disclosures in the Statement of Financial Position relating to EU income and advances to satisfy ourselves that they are fairly reflected. • We will undertake detailed transaction testing of payments of claims made during 2015/16 to satisfy ourselves that expenditure declared in the IIC outturn statement is fairly reflected. • We will review internal audit annual controls report to monitor the position regarding suspension, and the Scottish Government's management of the control environment. • We will review ESF papers submitted to the EE ARC, to monitor the position regarding suspension and the on-going work on the management action plan. 	<p>Detailed transaction testing of payment of claims confirmed expenditure declared in the IIC Outturn statement is fairly reflected.</p> <p>We also considered Statement of Financial Position disclosures, including the calculation of the self-correction which formed the basis of the provision recognised in the accounts.</p> <p>We reviewed internal audit's annual controls report and other reports relevant to ESF.</p> <p>Two suspensions were lifted in relation to the European Social Fund during 2016/17 and we reviewed correspondence from the EC and confirmed receipts of funds. The EC has signalled its intention to lift the remaining suspension and the interruption.</p> <p>Our work confirmed the accounting is appropriate in relation to the European Structural Funds.</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>New European Agricultural Guarantee Fund (EAGF) Schemes</p> <p>The Scottish Government has experienced problems in developing a new computer system to support payments under the schemes.</p> <p>Problems with the payment schedule give rise to a risk that the expenditure is not accounted for in the correct period. There is also a risk that control procedures required in advance of payments are not fully carried out, increasing the risk of irregular payments.</p>	<ul style="list-style-type: none"> Reliance will be placed on both controls and substantive testing completed by the schemes' external auditors (dependent on timing). We will complete testing of accrued expenditure balances at the year end. 	<p>Our audit of the European Agricultural Fund Accounts is underway.</p> <p>The problems developing the system continued throughout 2015/16 and as a result the scheme auditors were unable to carry out testing fully.</p> <p>During 2015/16 provisions increased by £1 million in relation to disallowance incurred during the previous CAP period. The accounting treatment was reviewed as part of our audit.</p> <p>The Scottish Government established schemes to loan funds from the Scottish budget to farmers while claims are being processed. The accounting treatment of these loans was reviewed as part of the financial statements audit. Substantive testing of the loans was also performed.</p>
<p>New financial powers</p> <p>From April 2015, additional financial powers under the Scotland Act 2012 came into force;</p> <ul style="list-style-type: none"> The Scottish Government has budgeted to use its enhanced borrowing powers in 2015/16 but it is unclear how these will be applied in practice and 	<ul style="list-style-type: none"> We will review the accounting treatment and disclosures as part of our 2015/16 financial statement audit. 	<p>The initial budget for 2015/16 anticipated that new capital borrowing powers would be used, and £306 million forecasted of the capital budget was established on this basis. However, HM Treasury agreed exceptional arrangements for 2015/16 so that the £283 million budget charge created by the NPD classification was</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>accounted for</p> <ul style="list-style-type: none"> The 2015/16 budget is partly funded by devolved tax receipts. If these receipts vary from forecasts, the Scottish Government may choose to use revenue borrowing powers or deposit excess receipts in its cash reserve. <p>Overall, there is a risk that the use of the additional financial powers will not be correctly accounted for or disclosed transparently in the 2015/16 consolidated accounts.</p>		<p>set against capital borrowing limits.</p> <p>We reviewed financial reporting across the Scottish Government consolidated accounts, the devolved taxes account produced by Revenue Scotland and new financial powers related disclosures in the Scottish Consolidated Fund.</p> <p>We are content with the disclosures in the consolidated accounts, the overall direction of travel and the commitment to further enhance reporting. The annual report of the Scottish Government consolidated accounts explains the linkages between these accounts.</p>
<p>Minutes of management boards</p> <p>We continue to experience delays in receiving minutes of the Scottish Government management boards. We reported this issue in our 2014/15 Annual Audit Report and the matter has not yet been resolved.</p> <p>There is a risk that the audit team is not sighted on important information which may be relevant to amounts and disclosures included in the accounts.</p>	<ul style="list-style-type: none"> As part of our 2015/16 audit activity we will continue to pursue to ensure we obtain regular and timely access to all management board minutes. 	<p>We have now received minutes of boards covering the 2015/16 year. Some minutes of relevant board meetings required for the 2015/16 audit were not received until June 2016 onwards. We noted that the Strategic Board minutes provided to us, were as published and redacted.</p> <p>No process was established during 2015/16 for minutes to be provided to audit on a timely and regular basis. We understand that the Scottish Government will review and address this as part of the revised governance arrangements</p>

Audit Risk	Assurance procedure	Results and conclusions
		<p>recently approved by the Scottish Government. Access to minutes is a key aspect in discharging our audit responsibility to 'understand the business' and we will continue to report on this until it is fully resolved.</p>
<p>Risk of management override of control 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"> • Detailed testing of journal entries. • Review of accounting estimates. • Focused testing of accruals and prepayments. • Evaluation of significant transactions that are outside the normal course of business. • Monitor internal audit reports. • Consider the results of controls testing. 	<p>We carried out testing of internal controls and journal entries and reviewed accounting estimates and unusual transactions. We reviewed internal audit reports. The results of this audit work were satisfactory.</p>
<p>Revenue and expenditure recognition ISA 240 presumes a risk of fraud in regard to revenue recognition in the financial statements and this can be extended to include expenditure recognition. This requires us to do routine audit testing. The Scottish Government receives most of its funding from the UK Government and is responsible for budget allocation, adjustment and monitoring across portfolios and numerous</p>	<ul style="list-style-type: none"> • Obtain an understanding of key controls around the recognition and accounting for revenue and expenditure to ensure compliance with the FReM. • Perform detailed testing of significant transactions, particularly around the financial year-end. • Carry out analytical procedures • Monitor budgetary process and 	<p>We tested controls in this area and tested transactions around the year-end. We examined budget control, monitoring and reporting processes and considered internal control findings. The results of this audit work were satisfactory.</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>public entities. The complexities in this process mean there is an inherent risk that revenue/expenditure could be materially misstated.</p>	<p>reporting.</p> <ul style="list-style-type: none"> Consider internal audit findings. 	
<p>Risks identified from the auditor's wider responsibility under the Code of Audit Practice</p>		
<p>Transparency of budget reporting</p> <p>The powers in the Scotland Act and the proposals in the Scotland Bill 2015 (now the Scotland Act 2016) have significant implications for the Scottish budget, heightening the need for transparent reporting on budgets, including in-year changes.</p> <p>In view of the increasing focus on budgets and the drive for greater transparency in public finances generally, we will build on our 2014/15 work and review the Scottish Government's arrangements for reporting in-year changes in budgets.</p>	<ul style="list-style-type: none"> We will review internal audit's cross-cutting review of budgetary control to inform our review. We will review the Scottish Government's arrangements for reporting in-year changes in budget. 	<p>We have concluded our review and have identified areas which may further enhance transparency. We will include these in a report to management.</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>Developing financial reporting</p> <p>It is becoming increasingly important to understand the overall position of the devolved Scottish public sector as a whole, but there is currently no single set of accounts that shows the position.</p> <p>While there is a commitment from the Scottish Government to develop this reporting, firm plans to take this forward have yet to be established.</p> <p>There is a risk that without this level of reporting, taxpayers and others are unable to get a full picture and understanding about public spending and the longer-term implications for public finances.</p>	<ul style="list-style-type: none"> We will continue to report on the progress of this as part of the 2015/16 audit. 	<p>A paper was presented to SGARC in June 2016 which sets out the Scottish Government’s proposals for a programme of work to develop financial reporting.</p> <p>We will continue to monitor progress and report as appropriate.</p>
<p>Performance reporting</p> <p>The Financial Reporting Manual (FReM) 2015/16 has been re-written and includes changes to the form and content of the annual report.</p> <p>The Scottish Government will take account of the guidance in developing its reporting, drawing on relevant performance data including the National Performance Framework (NPF) and key financial information from the</p>	<ul style="list-style-type: none"> We will review the changes made to the annual report in response to changes to the FReM. We will review the Government’s approach to developing the NPF and related reporting. 	<p>The 2015/16 consolidated accounts comply with the principles of the FReM as they contain a performance report. For information on the Scottish Government’s progress towards its overall aims and objectives, users of the accounts are directed to the National Performance Framework.</p> <p>While the performance report provides analysis of some key aspects of financial performance, the consolidated accounts provide limited</p>

Audit Risk	Assurance procedure	Results and conclusions
financial statements.		<p>insight into the performance of the Scottish Government as a whole.</p> <p>The Scottish Government continues to refine the NPF and in March 2016 published an updated NPF indicator set.</p>
<p>National accounts classification</p> <p>In 2014/15 the Office for National Statistics (ONS) reviewed a number of Scottish Non Profit Distributing (NPD) projects and concluded that they should be classified as public sector projects.</p> <p>Although the accounting treatment of the NPD project does not change upon classification, it does mean the Scottish Government will have less capital DEL (CDEL) budget to spend elsewhere.</p> <p>While CDEL budget has been used for these in 2016/17, the position for 2014/15 and 2015/16 is unclear.</p> <p>There is a risk that these pressures could impact on longer- term financial sustainability.</p>	<p>We will monitor the position as part of our audit and consider the implications of developments for financial management and sustainability.</p>	<p>HM Treasury agreed exceptional arrangements for 2015/16 so that the £283 million budget impact of the NPD classification was set against capital borrowing limits.</p> <p>We will review future spending plans to assess any on-going impact of ONS classification on capital budgets and plans.</p>

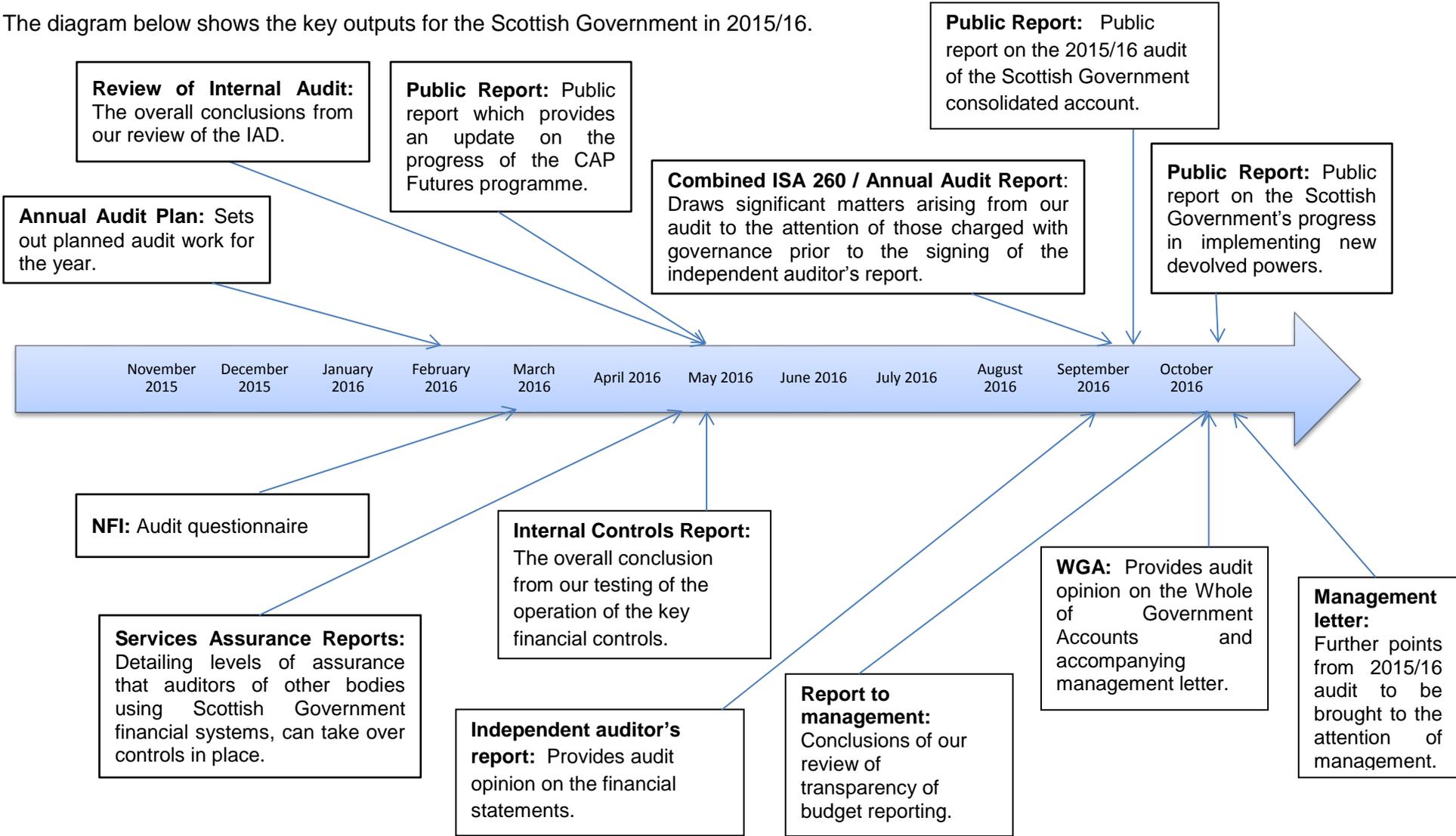
Audit Risk	Assurance procedure	Results and conclusions
<p>CAP Futures</p> <p>The CAP Futures programme has proved significantly more complex and challenging than the Scottish Government anticipated. There is still significant risk to the successful delivery of the programme arising from the potential late delivery of critical milestones and from increased costs.</p> <p>The timescales for implementing the final elements of the IT system for direct support payments to farmers are now very tight. Any further delays could have a serious impact on the Scottish Government's ability to process payments by the EC deadline of June 2016.</p>	<ul style="list-style-type: none"> • We will perform controls and substantive testing of payment to contractors. New payment controls were put in place during 2015. • Review of Programme and Delivery Board minutes and supporting documents. • Analysis of cost information and SEAS transactions. • Review of any Internal Audit work. • Interviews with key personnel • An update on the Scottish Government's progress in implementing the CAP programme will be published in May. 	<p>We reported in May 2016 that there is a risk that the programme budget will run out before a CAP compliant system is in place. As at 31 July 2016 the programme had spent £140.8 million, therefore a budget of £37.7 million remains. We do not expect the programme to achieve value for money.</p> <p>We will continue to monitor and report as appropriate.</p>
<p>Cyber security</p> <p>The Scottish Government's Information Services and Information Systems has reported an increase in the number of cyber attacks on the Scottish Government's IT systems and data, with increasingly sophisticated methods being employed. The risk to the Scottish Government's IT systems needs to be managed with effective mechanisms in place to protect them. There is</p>	<p>We will conduct a joint review of the Scottish Government's security arrangements with internal audit.</p>	<p>The joint review has been conducted and a report to management is currently being finalised.</p> <p>Overall, the Scottish Government is aware of the risks associated with cyber security and is taking appropriate action to mitigate those risks. Some areas for improvement have been identified including staff training, technical monitoring, incident response and assessment of cost implications.</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>a risk that business continuity could be compromised by a cyber attack on the Scottish Government's systems.</p>		
<p>Workforce capacity</p> <p>Increasing financial devolution is leading to increased responsibility for financial management at a time of growing resource pressures. The Scottish Government may not have sufficient capacity or resources to effectively manage its increased financial responsibilities and implement the new financial powers alongside business as usual. There is a risk that overall workforce planning arrangements are not effective. This could impact on the Scottish Government's ability to implement additional powers.</p>	<p>We will undertake local follow up work on our report Scotland's public sector workforce.</p>	<p>The Scottish Government has planning processes in place. These processes are focussed around capacity and capability. There is also evidence of succession planning, scenario planning and developments which are intended to improve management information. Our follow-up work did not cover the impact on the Scottish Government's ability to implement new financial powers in detail. Our 2016/17 performance audit on new financial powers will consider the workforce implications for the Scottish Government. A national report on the findings from this work will be published in Spring 2017.</p>
<p>Internal Audit</p> <p>Internal Audit is currently undergoing a period of transition. The findings of the Strategic Review of Internal Audit were presented to SGARC in December. The recruitment process for a new Director Level Head of Internal Audit is now underway. There is a risk that if the recommendations are</p>	<ul style="list-style-type: none"> • Overview of internal audit work • Regular meetings with Internal Audit management. • Review of Scottish Government ARC/PARC IA progress reports. 	<p>We reported the findings of our annual review of internal audit to SGARC in June 2016. IAD continued to face resource pressures in 2015/16 with further demands and competing priorities, particularly in relation to its European funding audit work.</p> <p>The new Director of Internal Audit took up post in April 2016 and is working to ensure that the</p>

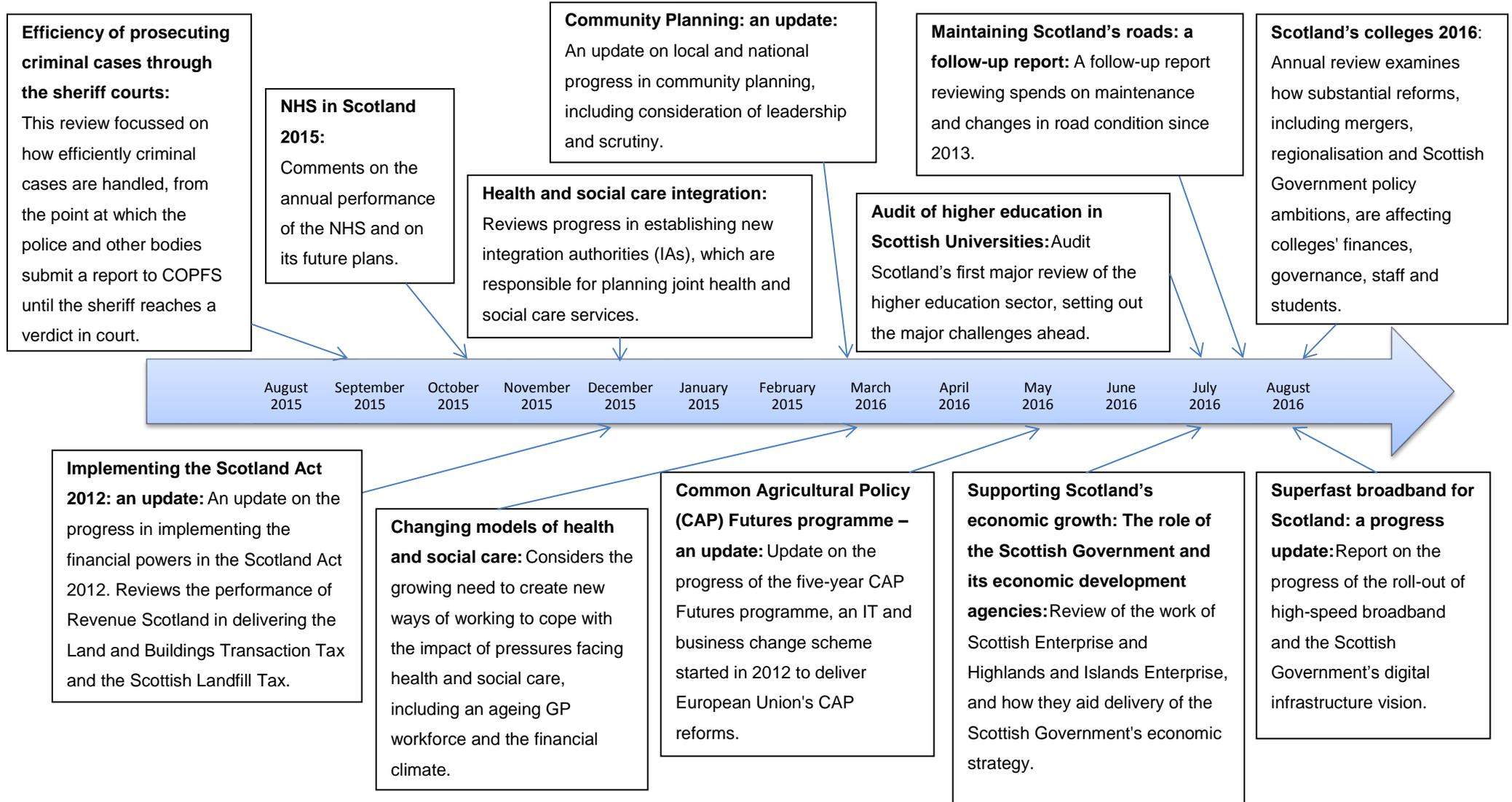
Audit Risk	Assurance procedure	Results and conclusions
not implemented to timescales then the section will continue to face challenges in service delivery.		strategic review recommendations are implemented.

Appendix II: Summary of audit reports 2015/16

The diagram below shows the key outputs for the Scottish Government in 2015/16.



Appendix III: Summary of national reports 2015/16



Appendix IV: Action plan

No.	Paragraph ref.	Issue/risk/recommendation	Management action/response	Responsible officer/target date
1.	15	<p>Presentational changes and completion of key components of the annual report (financial statements risk)</p> <p>Significant presentational changes were made to the accounts presented for audit. There were also delays in completing the annual report and the remuneration report.</p> <p>Risk</p> <p>There is a risk that changes are not compliant with accounting and reporting standards.</p> <p>Recommendation</p> <p>We recommend that the Scottish Government considers future changes to the accounts earlier in the process and would encourage early discussion with audit on its proposals.</p>	<p>The decision to adopt the new FReM model was proposed and considered by SGARC in June 2016. The likely impact of this was discussed with auditors in July; we also took a prudent decision to collect information and prepare draft accounts on the basis of the former model, so that we would not have any information gaps. It was also in the nature of some of the improvements that they had to go through internal processes for approval before being shared with audit.</p> <p>A review of the 2016-17 process confirms that we will follow the same model for the accounts this year, and may also consider further presentational changes. Where possible, these will be discussed early in the audit process; we cannot rule out the identification of improvements in the later stages of the process and we appreciate that this has an impact on audit.</p>	<p>Aileen Wright, Deputy Director, Finance</p>

No.	Paragraph ref.	Issue/risk/recommendation	Management action/response	Responsible officer/target date
2	76	<p>Developing financial and performance reporting (wider dimension risk)</p> <p>The Scottish Government has commenced a programme of work to review and broaden its financial reporting in the context of the new financial powers and has committed to continue to enhance financial transparency.</p> <p>There is much still to do as further powers are introduced, and this programme of work is continuing.</p> <p>The consolidated accounts do not report on the performance of the Scottish Government as a whole. A more rounded account of the Scottish Government's overall performance would enhance reporting to the Scottish Parliament and the public, and help strengthen accountability and scrutiny.</p> <p>Risk</p> <p>There is a risk that without this level of reporting, taxpayers and others are unable to get a full picture and understanding about public spending and its impact.</p> <p>Recommendation</p> <p>The Scottish Government should set out its overall plans for developing financial and performance reporting.</p>	<p>The approach here is necessarily progressive, as further powers are implemented and at the respective stages of the financial cycle. It is not exclusively about accounts. Specific commitments had already been made for reporting as part of Budget processes, and as part of the recent Public Audit and Post Legislative Scrutiny Committee of the Parliament, the Permanent Secretary made public specific commitments to financial reporting – and this further work is now in progress in accordance with the timetable set out.</p> <p>The Performance Board is overseeing ongoing work to refresh the National Performance Framework.</p>	<p>DG Finance December 2016</p>

No.	Paragraph ref.	Issue/risk/recommendation	Management action/response	Responsible officer/target date
3	92	<p>Minutes of board meetings (financial statements risk)</p> <p>There are as yet no systematic arrangements for our access to board minutes on a regular and timely basis. We understand this is being taken forward as part of the discussions on the implementation of the Scottish Government's governance review.</p> <p>Risk</p> <p>Restrictions are placed on the conduct of the audit.</p> <p>Recommendation</p> <p>The Scottish Government should review its processes to ensure that approved minutes of all relevant boards are provided to its external auditor in a timely manner.</p>	<p>The review and implementation of the new governance arrangements has included consideration of this and a systematic quarterly process has been put in place for access to minutes of the corporate boards. Auditors may also request information from the workings of other boards and these will be progressed on a case by case basis via the relevant secretariat.</p>	<p>Brian Taylor</p> <p>Head of Financial Capability Team</p>
4	126	<p>National Fraud Initiative (financial statements risk)</p> <p>The Scottish Government's payroll recommended matches resulting from the 2014/15 NFI exercise were not timeously investigated.</p> <p>Risk</p> <p>There is a risk that undetected fraud or error may be present in payroll records; this risk affects the Scottish Government and the bodies which use its shared payroll services.</p> <p>Recommendation</p> <p>We recommend that the Scottish Government improves its</p>	<p>The Scottish Government understands the importance of the NFI exercise to support the detection of fraud and error in public sector organisations.</p> <p>Following up recommendations for investigation is resource intensive and it is acknowledged that the 2014/15 payroll work took longer than anticipated to undertake.</p> <p>Planning for the NFI is incorporated within the audit strand of HR Service Centre business</p>	<p>Head of HR Shared Service Centre</p> <p>2015/16 exercise expected to be completed by October 2017</p>

No.	Paragraph ref.	Issue/risk/recommendation	Management action/response	Responsible officer/target date
		planning and resourcing for future NFI exercises in order to maximise the benefits of data matching for itself and its shared service partners.	planning and resource is allocated to ensure the exercise is completed each year. Ownership of and resource for the 2015/16 exercise were identified in September 2016.	
5	165	<p>Workforce planning arrangements (wider dimension risk)</p> <p>There is limited guidance on joint working and sharing of workforce planning information for central government bodies. There are a small number of formal and informal settings which provide scope for a more joined-up approach to workforce planning however this is not a key purpose of these groups at the present time.</p> <p>Risk</p> <p>The lack of a co-ordinated approach to workforce planning across central government bodies could impact on the efficiency and effectiveness of these arrangements.</p> <p>Recommendation</p> <p>The Scottish Government should review the opportunities for a more co-ordinated approach to workforce planning across central government bodies, and consider the appropriate structure to support this.</p>	<p>The Scottish Government has a number of relevant actions planned or in progress:</p> <ul style="list-style-type: none"> • Research effective approaches to workforce planning and test practice against Civil Service Workforce Planning Maturity Model (by Summer 2017). • Test and share the principles and approach with wider public bodies, using existing structures for engaging with sponsor teams, Chief Executives and HR leads (by Autumn 2017). • Evaluate value and determine if different structural arrangements would assist (by Autumn/Winter 2017). 	<p>Director, People or People Board</p> <p>Dates as specified</p>