

Scottish Enterprise

Annual Audit Plan 2016/17



 **AUDIT SCOTLAND**

Prepared for Scottish Enterprise
December 2016

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Risks and planned work

1. This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice \("the Code"\)](#), and any other relevant guidance. This plan identifies our audit work to provide an opinion on the financial statements and related matters and meet the wider scope requirements of public sector audit. The wider scope of public audit contributes to conclusions on the appropriateness, effectiveness and impact of corporate governance, performance management arrangements and financial sustainability.

Audit risks

2. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for Scottish Enterprise. We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

Exhibit 1: Key Audit Risks

Audit Risk	Management assurance	Planned audit work
Financial statement issues and risks		
<p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work includes consideration of 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 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. • Substantive testing of transactions to confirm expenditure and income have been accounted for in the correct financial year. • Evaluation of significant transactions that are outside the normal course of business.
<p>2 Risk of fraud over income and expenditure</p> <p>ISA 240 requires auditors to presume a risk of fraud where income streams, are significant (excluding Scottish Government funding).</p> <p>Scottish Enterprise receives a significant amount of income (£51m) from third parties.</p>	<ul style="list-style-type: none"> • Effective budget monitoring by management and members. • Internal audit testing of income. • Effective Counter Fraud and Whistleblowing policies and procedures in place. 	<ul style="list-style-type: none"> • Controls testing over income system, with reliance on Internal Audit. • Detailed substantive testing of revenue transactions focusing on the areas of greatest risk.

Audit Risk	Management assurance	Planned audit work
<p>The extent and complexity of income means that there is an inherent risk of fraud.</p> <p>ISA240 and the Code of Audit Practice require auditors to consider the risk of fraud over certain types of public sector expenditure. This includes grants and other claims made by individuals and organisations on the public purse. Examples of grants provided by Scottish Enterprise include Regional Selective Assistance grants, R&D grants and SMART grants.</p>	<ul style="list-style-type: none"> • Effective controls are in place to vet all grant recipients. • Specific controls in place to vet expenditure by recipients of European Structural Fund grants. 	<ul style="list-style-type: none"> • Controls testing over expenditure systems, with reliance on Internal Audit. • Reliance on Internal Audit review of European Funding. • Substantive testing of grant expenditure. • Review action taken in respect of NFI data matches. • Undertake performance audit work on European funding.
<p>3 Estimation and judgements</p> <p>Non current assets (land and buildings), pensions and investments are revalued annually at 31 March by third party expert valuers/actuaries.</p> <p>There is an inherent risk due to the extent of assumptions used in calculations and the impact they can have on the financial statements.</p>	<ul style="list-style-type: none"> • Sound arrangements for providing valuations information have been established. • Actuary and valuers are established and recognised providers in their field. 	<ul style="list-style-type: none"> • Review the work of an expert for the professional valuers (pensions, investments and properties). • Focused substantive testing of year-end balances.
<p>4 Investment Write-Offs</p> <p>Scottish Enterprise's funding for investments and projects can result in the write-off of equity, loans or grants when those companies are in financial difficulty.</p> <p>There is a risk that write-offs are not correctly disclosed in the financial statements, or that they have not been approved appropriately.</p>	<ul style="list-style-type: none"> • Sound arrangements are in place for the approval of write-offs. • Current expectation is that the value of write-offs in 2016/17 will be significantly less than the past two years. 	<ul style="list-style-type: none"> • Substantively test significant write-offs to ensure that <ul style="list-style-type: none"> – they have been approved in line with procedures, and – they have been disclosed correctly in the financial statements.
<p>Wider dimension risks</p>		
<p>5 Governance and Transparency (see also paragraph 29 below)</p> <p>The Board Chair has reviewed the structure and composition of the Board. This has led to a reduction in the number of Board members, number of committees and frequency of meetings.</p> <p>The first phase of Scottish Government's Review of Enterprise & Skills has announced the creation of a new</p>	<ul style="list-style-type: none"> • Board meetings have been extended to full-day sessions to allow members more time to fulfil their functions. • There has been no diminution of knowledge and experience. 	<ul style="list-style-type: none"> • Follow up to our 2010 Role of Boards Report. • Monitor the Scottish Government's Review of Enterprise & Skills (phase 2) and consider the impact on the organisation. • Follow up on any outstanding matters from our review of conflicts of interest report (2015/16).

Audit Risk	Management assurance	Planned audit work
<p>Board to oversee Enterprise Agencies.</p> <p>There is a risk that these changes impact on the Board's ability to fulfil its functions effectively. There may be a lack of scrutiny and challenge.</p>		
<p>6 Financial Sustainability and Financial Management (see also paragraphs 26-28 below)</p> <p>In June 2014, Audit Scotland reported on Scotland's Public Finances and identified that financial planning improvements were required by public bodies.</p> <p>In 2015/16, management agreed to prepare a 5 year financial strategy to test the impact of potential scenarios by March 2017.</p> <p>The outcome of the EU referendum led to uncertainty over future European funding, which is a significant source of income for Scottish Enterprise.</p>	<ul style="list-style-type: none"> • A three year business plan is in place, with a financial budget. Management reviews performance against budget regularly. Scottish Enterprise's budget is rebased in September each year to ensure the efficient use of resources. • We will implement a 5 year financial strategy, as agreed in the 2015/16 Annual Audit Report. • Assurance has been provided that the 2014-20 European Structural Funds expenditure will be underwritten. 	<ul style="list-style-type: none"> • Review progress in developing a 5 year financial strategy. Test the robustness of this strategy. • Place reliance on Internal Audit's review of European Funding and the arrangements to mitigate against future breaches. • Undertake performance audit work on European funding.
<p>7 ICT - Disaster Recovery and Cyber Attack</p> <p>Scottish Enterprise does not have a Disaster Recovery Plan in Place. In 2015/16, management advised that plans were in place to perform a rolling programme of disaster recovery testing with a plan to be developed thereafter.</p> <p>Organisations are increasingly threatened by cyber attacks. There is a risk that a cyber attack could disrupt Scottish Enterprise's systems, including key financial systems.</p>	<ul style="list-style-type: none"> • Internal Audit is reviewing Cyber Security. • Internal Audit is reviewing arrangements for Disaster Recovery 	<ul style="list-style-type: none"> • Review Internal Audit follow-up work on Disaster Recovery. • Place reliance on Internal Audit's review of Cyber Security. • Liaise with management regarding further audit work, including Your Business @ Risk.

National Fraud Initiative

3. The National Fraud Initiative (NFI) is a data-matching exercise led by Audit Scotland to aid the detection of fraudulent payments. NFI allows public bodies to investigate matches and, if fraud or error has taken place, to stop payments and attempt to recover the amounts involved. It also allows auditors to assess the arrangements that bodies have put in place to prevent and detect fraud, including how they approach the NFI exercise itself.

4. The current data matching exercise collected data in October 2016 and match investigation work is due to begin in January 2017. We shall monitor Scottish Enterprise's participation and progress with NFI. We shall report progress in our Annual Audit Report, which will be presented to the Audit Committee in June 2017.

Follow up of prior year findings

5. In 2015/16, we reviewed Scottish Enterprise's conflicts of interests' procedures. We noted that the planned annual requirement for staff to declare conflicts of interests last took place in August 2014. We have since been advised that the annual conflict of interests' declaration process was rolled-out in June 2016 and a completion rate in excess of 80% has been achieved to date. Submissions are currently being reviewed in line with policy. We are aware that Internal Audit intends to review the process and we shall consider the findings of this work and the impact on our financial statements audit.

Reporting arrangements

6. Audit reporting is the visible output for the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

7. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

8. We will provide an independent auditor's report to Scottish Enterprise and the Auditor General for Scotland that the audit of the financial statements has been completed in accordance with applicable statutory requirements. We will provide the Accountable Officer and Auditor General for Scotland with an annual report on the audit containing observations and recommendations on significant matters which have arisen in the course of the audit.

Exhibit 2 : 2016/17 Audit outputs

Audit Output	Target date	Audit Committee (or equivalent) Date
Annual Audit Plan	December 2016	15 December 2016
Interim report	March 2017	23 March 2017
Annual Audit Report including ISA 260 requirements	June 2017	26 June 2017
Signed Independent Auditor's Report	June 2017	Following Board on 30 June 2017

Audit fee

9. The proposed audit fee for the 2016/17 audit of Scottish Enterprise has yet to be confirmed. We shall discuss the proposed fee as soon as possible. In determining the audit fee we will take account of the risk exposure of Scottish Enterprise, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited single entity financial statements and complete working papers package on 15 May 2017. Officers have advised that the draft Performance and

Accountability Reports will be provided by 24 May 2017 and the full unaudited group financial statements, including complete narrative and associated working papers will be provided by 29 May 2017.

10. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Responsibilities

Audit Committee and Accountable Officer (or equivalent)

11. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

12. The audit of the financial statements does not relieve management or the Audit Committee, as those charged with governance, of their responsibilities.

Appointed auditor

13. Our responsibilities as independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice, and guided by the auditing profession's ethical guidance.

14. Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

15. The statutory financial statements audit will be the foundation and source for the majority of the audit work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of Scottish Enterprise and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how Scottish Enterprise will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free of material misstatement.

16. We will give an opinion on the financial statements as to:

- whether they give a true and fair view of the financial position of the audited bodies and their expenditure and income
- whether they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements
- the regularity of the expenditure and income.

Materiality

17. Materiality defines the maximum error that we are prepared to accept and still conclude that that our audit objective has been achieved. It helps assist our planning of the audit and allows us to assess the impact of any audit adjustments on the financial statements. We calculate materiality at different levels as described below. The calculated materiality values for Scottish Enterprise are set out in [Exhibit 3](#).



Exhibit 3: Materiality values

Materiality level	Amount
Planning materiality. This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross expenditure for the year ended 31 March 2017 based on the latest audited accounts for 2015/16.	£2.5 million
Performance materiality. This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 50% of planning materiality.	£1.25 million
Reporting threshold. We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 2% of planning materiality.	£50,000

18. It should be noted that we continue to exercise our professional judgement and in certain areas of the financial statements such as the management commentary, remuneration report and annual governance statement. All unadjusted errors of a factual nature will be reported to the Audit Committee.

Timetable

19. To support the efficient use of resources it is critical that a financial statements timetable is agreed with us for the production of the unaudited accounts. An agreed timetable is included at [Exhibit 4](#) which takes account of submission requirements and planned Audit Committee dates:

Exhibit 4: Financial statements timetable

 Key stage	 Date
Latest submission date of unaudited Scottish Enterprise single-entity financial statements and a complete working papers package	15 May 2017
Latest submission date of unaudited Performance and Accountability Reports	24 May 2017
Latest submission date of complete unaudited Scottish Enterprise group annual report and accounts with complete working papers package	29 May 2017
Latest date for final clearance meeting with Chief Financial Officer	16 June 2017
Agreement of audited unsigned financial statements; Issue of draft Annual Audit Report including ISA 260 report to those charged with governance	23 June 2017
Independent auditor's report signed	Following Board on 30 June 2017
Latest date for signing of Whole of Government Accounts (WGA) return	30 Sept 2017

Internal audit

20. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carry out an assessment of the internal audit function. Internal audit is provided by Scottish Enterprise's in-house Internal Audit team.

Adequacy of Internal Audit

21. From our review of Internal Audit, we have concluded that overall the Internal Audit service operates in accordance with PSIAS and has sound documentation and reporting procedures in place. We are pleased to note that an independent third party review has recently been commissioned and completed. The external quality assessment was undertaken by the Institute of Internal Auditors.

Areas of reliance

22. To support our audit opinion on the financial statements we intend to place formal reliance on the following planned internal audit reviews:

- Key Project Controls
- Investment
- Finance Centre
- Treasury Management
- Salaries and Benefits

23. In respect of our wider dimension audit responsibilities we also plan to consider other areas of internal audit work including:

- Performance Measurement
- Conflicts, Hospitality and Gifts
- European Funding
- Cyber Security
- Disaster Recovery and Business Continuity

Audit dimensions

24. As noted at paragraph 1 above, we are required to meet the wider scope requirements of public sector audit which are outlined in the Code of Audit Practice.

25. Our audit is based on four audit dimensions that frame this wider scope and which are outlined in [Exhibit 5](#) below. As part of our responsibility to report on the four audit dimensions, we have identified specific areas of audit work for 2016/17 and these are outlined in Exhibit 1 above. We shall undertake further work over our five-year audit appointment.

Exhibit 5: Audit dimensions



Financial sustainability

26. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the body's financial sustainability in the medium (two to five years) and longer term (longer than five years). We shall review selected aspects over our five-year audit appointment and conclude on the following:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of arrangements in place to address any identified funding gaps
- whether Scottish Enterprise can demonstrate the affordability and effectiveness of funding and investment decisions it has made.

Financial management

27. Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

28. We will review, conclude and report on the following over our five-year appointment:

- whether Scottish Enterprise has arrangements in place to ensure systems of internal control are operating effectively
- whether Scottish Enterprise can demonstrate the effectiveness of the budgetary control system in communicating accurate and timely financial performance
- how Scottish Enterprise has assured itself that its financial capacity and skills are appropriate
- whether Scottish Enterprise has established appropriate and effective arrangements for the prevention and detection of fraud and corruption. We shall consider Scottish Enterprise's response to the NFI exercise.

Governance and transparency

29. Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information. We will review, conclude and report on the following over our five-year appointment:

- whether Scottish Enterprise can demonstrate that the governance arrangements in place are appropriate and operating effectively.
- whether there is effective scrutiny, challenge and transparency on the decision-making and finance and performance reports.
- the quality and timeliness of financial and performance reporting.

Value for money

30. Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether Scottish Enterprise can provide evidence that it is demonstrating value for money in its achievement of performance targets.

31. We will review, conclude and report on the following over our five-year appointment:

- whether Scottish Enterprise can provide evidence that it is demonstrating value for money in the use of its resources.
- whether Scottish Enterprise can demonstrate that there is a clear link between money spent, output and outcomes delivered.
- whether Scottish Enterprise can demonstrate that outcomes are improving.
- whether there is sufficient focus on improvement and the pace of it.

Independence and objectivity

32. Auditors appointed by Audit Scotland must comply with the Code of Audit Practice. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has in place robust arrangements to ensure compliance with these standards including an annual “fit and proper” declaration for all members of staff. The arrangements are overseen by the Assistant Auditor General, who serves as Audit Scotland’s Ethics Partner.

33. The engagement lead for Scottish Enterprise is Angela Cullen, Assistant Director. Auditing and ethical standards require the appointed auditor, Angela Cullen, to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of Scottish Enterprise.

Quality control

34. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor’s report or opinion is appropriate in the circumstances.

35. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland

conducts peer reviews, internal quality reviews and is currently reviewing the arrangements for external quality reviews.

36. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

Scottish Enterprise

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