

Revenue Scotland

Management Report 2017/18



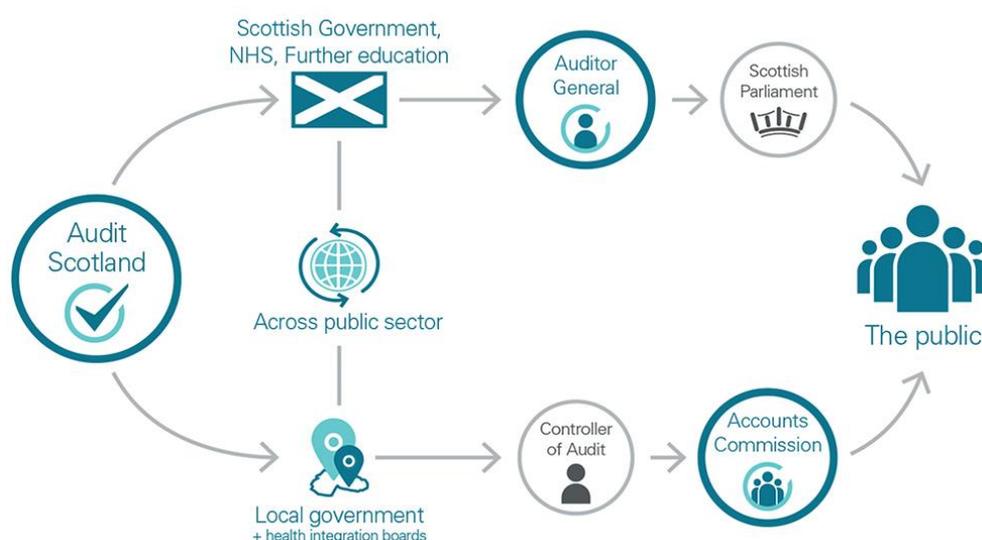
 AUDIT SCOTLAND

Prepared for Revenue Scotland
July 2018

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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Audit findings

Introduction

1. This report contains a summary of the key issues identified during the interim audit work carried out at Revenue Scotland. This work included testing of key controls within financial systems to gain assurance over the processes and systems used in preparing the financial statements. We will use the results of this testing to determine our approach during the 2017/18 financial statements audit.
2. Our responsibilities under the [Code of Audit Practice](#) require us to assess the system of internal control put in place by management. We seek to gain assurance that Revenue Scotland:
 - has systems of recording and processing transactions which provide a sound basis for the preparation of the financial statements
 - has systems of internal control which provide an adequate means of preventing and detecting error, fraud or corruption
 - complies with established policies, procedures, laws and regulations.
3. We have also under the [Code of Audit Practice](#), carried out work on the wider dimension audit. This focussed on financial management, financial sustainability and governance and transparency.

Conclusion

4. In respect of our testing of the systems operated on behalf of Revenue Scotland by the Scottish Government, our interim work identified no significant control weaknesses. Our review of controls was therefore satisfactory and this will enable us to take planned assurance on these systems for our audit of the 2017/18 Resource Accounts.
5. Our testing of the tax collection system (Scottish Electronic Tax System {SETS}) found there has been some good progress during the year in Revenue Scotland's compliance activity. This is important in terms of preventing and detecting fraud and error in tax returns. In particular we noted the development of the Tax Governance Policy and Compliance Strategy documents which assist in bringing rationale and clarity to compliance work. Some compliance activity is still at an early stage as tax staff build up knowledge and expertise but we acknowledge the progress made. We have also noted that concerns over vacancy levels in the organisation which we reported last year have been addressed with a significant increase in the staffing complement.
6. We have made a number of recommendations arising from our interim audit work on the SETS system and these are outlined in Exhibit 1.
7. On the basis of the work undertaken to date on the wider dimension audit, we have not identified any areas of concern which require reporting at this stage in respect of financial management, financial sustainability and governance and transparency. We shall report our findings from our wider dimension work in our Annual Audit Report, which we will present to the September 2018 Audit and Risk Committee.

Work summary

8. Our 2017/18 testing of the systems supporting the Resource Accounts covered key controls in a number of areas including bank reconciliations, payroll validation and exception reporting, authorisation of journals, change of supplier bank details and IT access controls. Additionally, our testing covered budget monitoring and control, feeder system reconciliations and controls for preventing and detecting fraud in areas such as taxation receipts.

9. Our 2017/18 testing of SETS included a follow-up to the matters raised in our 2016/17 interim report, and more generally updating our knowledge of tax compliance activity and the operation of the system.

10. In accordance with *ISA 330: the auditor's response to assessed risk*, our audit judgements are based on current year testing of controls and where appropriate prior year results. Our risk based audit approach allows us to take a three-year cyclical approach to controls testing. This approach enables us to place reliance on previous years' audit work where controls remain unchanged and no significant weaknesses had been identified. Also, where possible we will consider placing reliance on the work of internal audit to avoid duplication of effort.

11. The contents of this report have been discussed with relevant officers to confirm factual accuracy. The co-operation and assistance we received during the course of our audit is gratefully acknowledged.

Risks identified

12. The key control and wider dimension risks identified during the interim audit are detailed in [Exhibit 1](#). These findings will inform our approach to the financial statements audit where relevant.

13. Any weaknesses identified represent those that have come to our attention during the course of normal audit work and therefore are not necessarily all the weaknesses that may exist. It is the responsibility of management to decide on the extent of the internal control system appropriate to Revenue Scotland.

Additional follow-up work

14. As we noted above, there have been improvements this year in the framework of control in place to prevent and/or detect fraud in tax receipts and we are pleased to note that Revenue Scotland is enhancing its intelligence over the devolved taxes. As this is still an early stage in Revenue Scotland's compliance activity, controls are not yet sufficiently developed or embedded for us to be able to place reliance on them for our audit opinion. We will therefore use substantive testing of tax returns, directed at known risk areas, to seek appropriate assurance over tax revenues.

Exhibit 1

Key findings and action plan 2017/18

Issue identified	Management response	Responsible officer and target date
Audit findings		
SETS to SEAS reconciliations	Agreed	Chief Accountant
Monthly reconciliations between the tax system SETS and the general ledger SEAS are a key control which ensures that information in the	It is accepted that best practice is for this reconciliation to be carried out monthly and this is our normal practice. The reconciliations are however based on year to	June 2018

Issue identified	Management response	Responsible officer and target date
<p>Devolved Taxes Account matches the tax returns and tax paid as recorded in SETS. We noted from our interim testing that the reconciliation for January 2018 had not been prepared.</p> <p>We acknowledge that the February reconciliation was undertaken timeously.</p> <p>There is a risk that if differences arising between the two systems are not timeously investigated, this could lead to incomplete or inaccurate data in either or both systems.</p>	<p>date data so that if one month is missed due to pressure of work, then data is picked up and reconciled in the following month ensuring nothing is missed. The January reconciliation was not completed prior to the February data becoming available and therefore the reconciliation was carried out on the latest available data.</p>	
<p>SETS access control</p> <p>The Revenue Scotland IT Change Management Procedure document does not specify approval levels for access to SETS. There is a need to formalise SETS access controls. For standard change requests approval comes from the appropriate line manager but for staff with advanced system privileges approval should come from a member of the Senior Leadership Team.</p> <p>There is a risk of unauthorised system access where control processes are not formally documented.</p>	<p>Agreed.</p> <p>This relates solely to System Administrator accounts held by Revenue Scotland IT staff. The procedure will be amended so that formal SLT approval is given and documented.</p>	<p>Head of Strategy & Change June 2018</p>
<p>LBTT Sample checks of tax returns</p> <p>Last year we commented on a sampling exercise undertaken by compliance staff who examined 132 tax returns from 2015/16 across 4 high-level categories. Management agreed to undertake a review of the random enquiry programme and base any decision on whether to increase the sample size or frequency on the outcome of that.</p> <p>This exercise acts as a deterrent to fraud and error by taxpayers and also helps Revenue Scotland staff identify any new risk areas</p> <p>This year we have examined the 2016/17 sampling work (the 2017/18 results were not yet available at the time of our interim work) and found no change to the approach taken to sample testing.</p> <p>No major issues were identified from the sampling undertaken to date. We</p>	<p>Partially agreed</p> <p>Following a recent recruitment exercise, resource is now in place to increase the compliance activity that we undertake. The additional resource will allow us to undertake more targeted compliance activity in 2018-19. We will also provide updates to the Board on a regular basis.</p> <p>Key areas of risk are usually identified from our knowledge of tax reliefs, opinions and other types of technical work; we consider it unlikely that increasing the sample size of the random enquiry programme will identify new areas of risk. On that basis, we are content to keep the sample size for the random enquiry programme relatively small.</p>	<p>Head of Tax September 2018</p>

Issue identified	Management response	Responsible officer and target date
<p>recommend that Revenue Scotland considers:</p> <ul style="list-style-type: none"> increasing the sample sizes to give a greater degree of assurance over accuracy based on the results of the compliance testing, adopting a more targeted approach to include known high-risk areas (for instance, non-residential property transactions by incorporated taxpayers) carrying out checks on a more regular basis and within the relevant time period reporting the results from the compliance exercise in the Tax Update report to the Board. <p>There is a risk that the current approach provides limited assurance over the accuracy of tax returns.</p>		
<p>Compliance strategy and use of tax data</p> <p>In 2016/17, we recommended that Revenue Scotland develop compliance strategies for both devolved taxes.</p> <p>This year we note that compliance strategies have recently been introduced for LBTT and SLfT and there has been progress made in internal reporting to assist staff with identifying variances and risks. This is still at an early stage. There is still much work to do to enhance the use of tax data, both internally-held data and data held by partner bodies such as Registers of Scotland and HMRC, so that compliance activity becomes more intelligence-led and therefore more effective.</p> <p>Revenue Scotland should continue to develop its compliance activity together with making better use of the potential from shared data with its partner bodies.</p> <p>There is a risk to the collection of tax revenues where supporting data and evidence is not being used to enhance compliance activity.</p>	<p>Agreed</p> <p>As part of our commitment to build on existing work to maximise tax compliance and protect revenue against tax evasion and avoidance, our intention in 2018-19 is to further develop our approach to compliance activity by developing a revised compliance strategy, supported by compliance plans for each tax. In this context, we will continue to enhance the use of internal data and work with partner bodies to make better use of the data that can be made available to us.</p>	<p>Head of Tax</p> <p>September 2018</p>

Issue identified	Management response	Responsible officer and target date
<p>Retention of SLfT enquiry documentation</p> <p>All LBTT documentation is held on SETS which was designed to hold all case management information. We noted that some SLfT enquiry details are held on Huddle, a shared information system which Revenue Scotland's partner body the Scottish Environment Protection Agency (SEPA) can access. Whilst this facilitates efficient collaboration, we recommend that all relevant documentation in support of enquiry work is retained on the SETS system which is the designated tax administration and collection system.</p> <p>There is a risk that the audit trail in support of enquiry work is incomplete. There is a further risk that using 2 locations to store taxpayer data could increase the risk of a data protection breach.</p>	<p>Agreed</p> <p>We recognise and accept the need to provide an audit trail of our enquiry work. Huddle currently offers a more accessible way of storing these whilst the enquiry is in progress. It enables all documents to be kept in one place where they can be accessed by both SEPA and Revenue Scotland staff.</p> <p>Whilst Huddle meets our security standards and has been agreed to enable collaborative working, our policy is for final documents to be stored on SETS or ERDM.</p> <p>We have therefore taken steps to ensure that enquiry records are transferred to SETS once an enquiry has been completed.</p> <p>We have specified the need for a more comprehensive case management system as part of SETS2 to enable us to better manage the records that we hold in respect of landfill operators.</p>	<p>Head of Tax</p> <p>December 2018</p>
<p>Procurement of SETS2</p> <p>The current contract for the operation of the SETS system will expire in August 2019. A re-procurement process is well underway with the intention that a new system will be in place to ensure a smooth transition for the collection and administration of the devolved taxes.</p> <p>It is important that the new system builds on prior experience of collecting and administering devolved taxes; can support the desired enhancements to compliance activity as set out in the new compliance strategies; and is set up to reflect a robust framework of controls which incorporate clear levels of authorisation and evidence of review.</p> <p>There is a risk that the new tax system does not facilitate improvements to the overall control and compliance environment.</p>	<p>Agreed</p> <p>We have gained significant experience in administering and collecting taxes over the last three years. The programme is drawing expertise from the business to ensure that this is fed into the development and implementation of the new system but also benefits from external representation from tax and other similar delivery fields. Key areas within the LEAP programme are around process design and development to ensure learning is built into the design. In addition the programme is considering the design of a sustainable delivery model to support continuous improvement beyond day 1.</p> <p>The contract for tender seeks the provision of a system which is easily adaptable so that changes resulting from internal or external feedback as well as the introduction of new taxes can be implemented quickly and efficiently.</p>	<p>Head of Strategy & Change</p> <p>April 2019</p>

Source: Audit Scotland

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