

# Forest Enterprise Scotland

Annual Audit Plan 2017/18



 AUDIT SCOTLAND

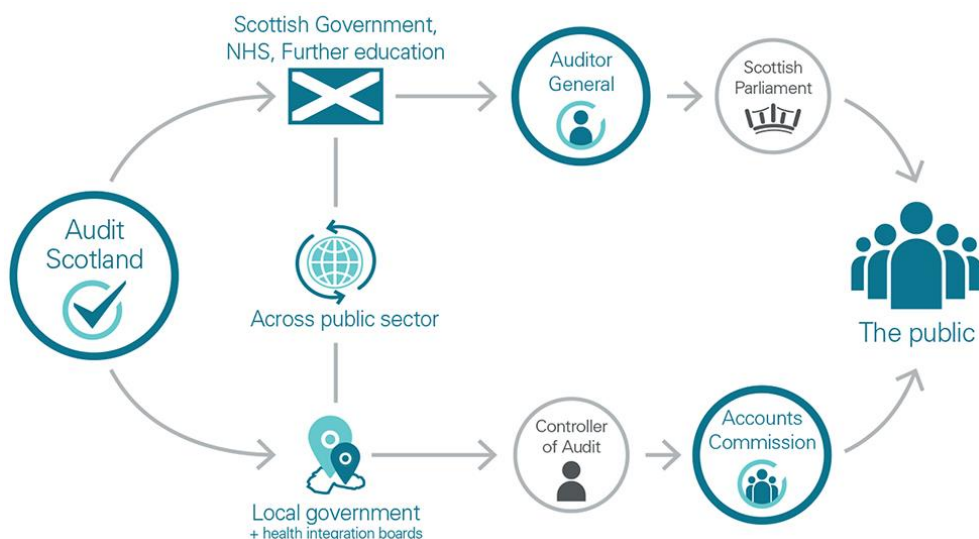
Prepared for Forest Enterprise Scotland

March 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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# 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](#), 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.

2. 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

3. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main audit risk areas for Forest Enterprise Scotland (FES). 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

### 2017/18 Key audit risks

Audit Risk	Source of assurance	Planned audit work
<b>Financial statement issues and risks</b>		
<p><b>1 Risk of management override of controls</b></p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance.</p>	<p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Focused testing of year-end payables and receivables.</p> <p>Substantive cut-off testing of income and expenditure to ensure that these have been recognised in the correct financial year.</p> <p>Evaluation of significant transactions that are outside the normal course of business.</p> <p>Review of internal audit's work on, and subsequent follow up of, procurement, contract management and finance support visits audits. We shall also consider progress against management's action plan.</p>

Audit Risk	Source of assurance	Planned audit work
<p><b>2 Risk of fraud over income</b></p> <p>FES receives a significant amount of income in addition to Scottish Government funding.</p> <p>In 2016/17, FES received income in excess of £87.8m from other sources, including £65m from timber sales. The nature, extent and complexity of income sources mean that, in accordance with ISA 240, there is an inherent risk of fraud.</p>	<p>Effective budget monitoring.</p> <p>Effective Counter Fraud and Whistleblowing policies and procedures in place.</p> <p>Well established systems and control procedures in place.</p>	<p>Analytical procedures on income streams.</p> <p>Detailed testing of revenue transactions focusing on the areas of greatest risk.</p> <p>Substantive cut-off testing of income to ensure it has been recognised in the correct financial year.</p> <p>Controls testing during the forest district visit, including timber income controls and timber security arrangements.</p> <p>Review of the Sales Recording Package (SRP) system and key controls.</p> <p>Review of FES's anti-fraud arrangements.</p> <p>Review of internal audit's work on, and subsequent follow up of, Contract Management. We shall also consider progress against management's action plan.</p>
<p><b>3 Accounting estimation and judgements</b></p> <p>There is a significant degree of subjectivity in the measurement and valuation of the material account areas of non current assets and contingent liabilities.</p> <p>Forest estate/ biological asset values are based on a random sample of assets, with results extrapolated across the whole forest estate. Respective valuations of £914M and £910M in 2016/17. A quinquennial valuation of forest estate/ biological assets, land and buildings will take place in 2017/18. Land and buildings were valued at £220M and £34M respectively in 2016/17.</p> <p>A contingent liability of £17.4m was disclosed in the 2016/17 accounts in relation to the restoration of opencast coal sites.</p> <p>The 2016/17 accounts also disclosed a contingent liability for the HMRC audit, which is ongoing in 2017/18. There is a possibility of future non-compliance liabilities arising from</p>	<p>Sound arrangements for providing valuation information have been established.</p> <p>Established methodology for quinquennial valuation of biological assets, land and buildings.</p> <p>Valuers are established and recognised providers in their field.</p> <p>Management monitor opencast coal site contingent liability.</p> <p>FES appointed an independent tax adviser (Scott Moncrieff) to identify potential VAT liabilities and develop a tax strategy.</p>	<p>Review the work of an expert for the professional valuer (wind farms/ hydro, and forest estate/ biological assets).</p> <p>Review of quinquennial valuation exercise and subsequent accounting adjustments.</p> <p>Review of accounting policies to ensure they are reasonable.</p> <p>Regular discussions with management on the opencast coal sites potential liability. We will also examine the accuracy and valuation of the disclosure in the financial statements.</p> <p>Regular discussions with management on the FES HMRC inspection. Examine the accuracy, completeness and disclosures in the financial statements.</p> <p>Focused substantive testing of year end balances.</p>

Audit Risk	Source of assurance	Planned audit work
<p>the audit.</p> <p>This subjectivity represents an increased risk of misstatement in the financial statements.</p>		
<b>Wider dimension risks</b>		
<p><b>4 Financial sustainability</b></p> <p>Eighty per cent of FES' expenditure is funded by income generating activities (£88M in 2016/17). The remainder is met by a Forestry Commission Scotland (FCS) grant (£22M in 2016/17).</p> <p>Timber income in 2016/17 was £65M. Fluctuations in timber income and cost pressures continue to have an impact on the financial sustainability of Forest Enterprise Scotland. Although exchange rates have been favourable for domestic timber trading, the impact of Brexit on the UK's timber industry is still largely unknown.</p> <p>There is a risk to the financial sustainability of FES, should prevailing economic conditions have an adverse affect on UK timber prices.</p>	<p>Development of long-term financial strategy/ plan.</p>	<p>Monitoring of monthly finance reports.</p> <p>Monitor impact of economic conditions on timber income in the UK.</p> <p>Review progress of long-term financial strategy and plan.</p>
<p><b>5 Governance and transparency</b></p> <p>FES is currently in the process of significant organisational change following the review of Forestry Commission services. Major programmes include:</p> <p><u>Establishing Corporate Services Scotland:</u></p> <p>This programme is reviewing the transition of shared services from Forestry Commission Central Services into FCS/FES. The remaining shared services should be transferred to England and Wales by the end of March 2018 although delays have been identified.</p> <p>There is a risk that any prolonged slippage in the programme could impact on service delivery, knowledge transfer and transition to agency status (Forestry and Land Scotland). There is a further risk that internal controls</p>	<p>Internal Communications Manager to ensure effective communication to staff.</p> <p>Corporate Services Programme Board monitors progress.</p> <p>Implementation plans are under development for Finance &amp; Digital services projects to ensure transfer of knowledge and continuity of services.</p> <p>Change Manager to ensure project co-ordination and effective transition.</p> <p>Progress monitored by Scottish Government Forestry Devolution Programme Board and the Forestry Commission's Scotland Executive Board.</p>	<p>High level review of organisational change programmes.</p> <p>Review procedures for maintaining the register of interests including application of Your Reputation @ Risk survey (to be discussed with management).</p> <p>Monitor progress on testing plans for business continuity and review progress on implementing General Data Protection Regulation.</p> <p>Monitor progress of transition of Finance and Digital services.</p> <p>Review cyber security arrangements.</p>

Audit Risk	Source of assurance	Planned audit work
<p>may not be as effective in a period of change.</p> <p><u>Forestry and Land Management (Scotland) Bill</u>:</p> <p>Forest Enterprise Scotland will become a separate, larger Agency. The following risks are associated with this period of organisational change:</p> <ul style="list-style-type: none"> <li>• loss of key staff and knowledge due to the uncertainty</li> <li>• detrimental impact on the effectiveness of internal controls during a period of change, including maintenance of the register of interests</li> <li>• unable to provide key services alongside managing the change programme.</li> </ul>		

## Reporting arrangements

**4.** 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](http://www.audit-scotland.gov.uk).

**5.** 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 officer(s) to confirm factual accuracy.

**6.** We will provide an independent auditor's report to Forest Enterprise Scotland, Scottish Parliament and the Auditor General for Scotland setting out our opinions on the annual accounts. 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

### 2017/18 Audit outputs

Audit Output	Target date	Audit Committee (or equivalent) Date
Annual Audit Plan	01 February 2018	08 February 2018
Interim Report	31 May 2018	27 July 2018
Annual Audit Report, including ISA260 requirements	23 July 2018	27 July 2018
Signed Independent Auditor's Report	30 July 2018	-

### Audit fee

7. The agreed audit fee for the 2017/18 audit of Forest Enterprise Scotland is £62,500 (2016/17: £62,500). In determining the audit fee we have taken account of the risk exposure of FES, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our fee reflects a planned increase in testing as a result of findings arising from internal audit reports; the impact of significant organisation change and changes in key finance staff. Our audit approach assumes receipt of the unaudited financial statements, with a complete working papers package on 31 May 2018.

8. 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

9. 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.

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

#### Appointed auditor

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

12. Auditors in the public sector give an independent opinion on the financial statements and other specified information accompanying 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

**13.** 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 Forest Enterprise Scotland 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 FES 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.

**14.** We will give an opinion on the financial statements as to whether:

- they give a true and fair view of the financial position of FES and its income and expenditure
- they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements
- the information included in the performance and accountability reports meets requirements for their preparation and is consistent with the financial statements
- income and expenditure is regular.

## Materiality

**15.** We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinion in the auditor's report.

**16.** We calculate materiality at different levels as described below. The calculated materiality values for FES are set out in [Exhibit 3](#).



## Exhibit 3

### Materiality values

Materiality level	Amount
<p><b>Planning materiality</b> – 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. For the remaining items in the Statement of Financial Position and all items in the Statement of Comprehensive Net Expenditure, we have set a separate materiality of 1% of gross expenditure.</p>	£1.4 million
<p><b>Performance materiality</b> – 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 the following performance materiality levels:</p> <ul style="list-style-type: none"> <li>- For items in the Statement of Financial Position (excluding biological assets, forest estate and land), and all items in the Statement of Comprehensive Net Expenditure, we have set a separate performance materiality of 65% of planning materiality.</li> <li>- For biological assets, forest estate and land, the performance materiality level is set at 60% (1% of total assets less total liabilities (£21.3M)).</li> </ul>	<p>£0.9 million</p> <p>£12.8 million</p>
<p><b>Reporting threshold (i.e. clearly trivial)</b> – 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 5% of planning materiality.</p>	£71,000



**17.** We review and report on other information published with the financial statements including the performance and accountability reports which include the annual governance statement and the remuneration and staff report. Any issues identified will be reported to the Audit and Risk Committee as appropriate.

### Timetable

**18.** 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 and Risk Committee dates:

## Exhibit 4

### Financial statements timetable

 Key stage	 Date
Latest submission date of unaudited annual accounts with complete working papers package	By 31 May 2018
Latest date for final clearance meeting with the senior finance manager and head of finance and procurement	11 July 2018
Agreement of audited unsigned annual accounts; Issue of Annual Audit Report including ISA 260 report to those charged with	23 July 2018

governance

Independent auditor's report signed	30 July 2018
Latest date for signing of WGA return	28 September 2018

## Changes in key finance staff

**19.** FES and FCS finance teams are currently undergoing significant change in terms of resourcing and responsibilities. A key member of the finance team, who prepared the annual report and accounts for both FCS and FES in 2016/17, left the organisation in January 2018. In addition, responsibility for the preparation of FES' financial statements has now transferred to FES. These changes could have a potential impact on the financial statements timetable. We will have regular discussions with management to monitor progress against the timetable.

## Shared account areas

**20.** A number of the key financial systems continue to be applied throughout the UK. As in previous years we shall carry out a programme of audit work on these shared account areas and linked common systems on behalf of the NAO. This approach minimises duplication of effort and has proved effective in previous years. We shall provide a separate assurance letter to the NAO.

## Internal audit

**21.** 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 the Scottish Government Internal Audit Directorate.

### Adequacy of Internal Audit

**22.** Audit Scotland's Scottish Government audit team plans to carry out a review of the effectiveness of the internal audit function to ensure it operates in accordance with Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place. We plan to place reliance on that work.

**23.** We are aware that a number of internal audit reports to management have reported insufficient assurance. Internal audit are working with management to address these weaknesses and follow up findings. We will assess this work and resulting impact on the financial statements.

### Areas of Internal Audit reliance

**24.** To support our audit opinion on the financial statements, we plan to place formal reliance on the review, and follow up, of procurement; contract management; and finance support visit audits.

## Audit dimensions

**25.** Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#). In our 2016/17 Annual Audit Report, we reported on arrangements in place within FES to support the four audit dimensions: financial sustainability; financial management; governance and transparency; and value for money.

**26.** As part of our continued responsibility to report on the four audit dimensions, we have identified specific areas of audit work for 2017/18 and these are outlined in [Exhibit 1](#) above.

## Exhibit 5

### Audit dimensions



Source: Code of Audit Practice

### Financial sustainability

**27.** 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 longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. Over our five-year appointment, we shall consider:

- 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 potential funding gaps
- whether FES can demonstrate the affordability and effectiveness of funding and investment decisions it has made.

### Financial management

**28.** Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We shall consider over our five-year appointment:

- whether FES has arrangements in place to ensure systems of internal control are operating effectively
- whether FES can demonstrate the effectiveness of budgetary control system in communicating accurate and timely financial performance
- how FES has assured itself that its financial capacity and skills are appropriate
- Whether FES has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

### 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. Over our five-year appointment, we shall consider:

- whether FES 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 shall consider over our five-year appointment whether:

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

### Independence and objectivity

**31.** Auditors appointed by the Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. 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 Director of Audit Services, who serves as Audit Scotland’s Ethics Partner.

**32.** The engagement lead for Forest Enterprise Scotland is Mark Taylor, Assistant Director. Auditing and ethical standards require the appointed auditor, Mark Taylor, 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 Forest Enterprise Scotland.

### Quality control

**33.** 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.

**34.** 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 (and relevant supporting guidance) 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.

**35.** 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.

## **Adding Value**

**36.** Through our audit work we aim to add value to FES. We will do this by ensuring our Annual Audit Report provides a summary of the audit work done in the year together with clear judgements and conclusions on how well FES has discharged its responsibilities and how well it has demonstrated the effectiveness of its arrangements. Where it is appropriate we will recommend actions that support continuous improvement and summarise areas of good practice identified from our audit work.

# Forest Enterprise Scotland

## Annual Audit Plan 2017/18

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