

# Highlands and Islands Enterprise

Annual Audit Plan 2017/18



 AUDIT SCOTLAND

Prepared for Highlands and Islands Enterprise

February 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.

---

# Contents

---

<b>Risks and planned work</b>	<b>4</b>
Audit risks	4
Reporting arrangements	7
Audit fee	8
Responsibilities	8
<b>Audit scope and timing</b>	<b>9</b>
Financial statements	9
Materiality	9
Internal audit	11
Audit dimensions	11
Independence and objectivity	13
Quality control	13
Adding value	14

# 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 risk areas for Highlands and Islands 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

### 2017/18 Key audit risks

Audit Risk	Source of assurance	Planned audit work
<b>Financial statement issues and risks</b>		
<p><b>1 Accelerated timetable for accounts preparation and audit completion</b></p> <p>The timetable for the preparation of the financial statements has been brought forward by a week and the date for signing the audited accounts by 3 weeks at the request of the Scottish Government. There is a risk that the finance team will not have the capacity to deliver the accounts and working papers to the required quality by the agreed date. In addition, there is a risk that information provided by external parties (eg pensions information, taxation calculations, subsidiaries audited accounts) will not be available prior to the target date for the completion of the audit of the accounts.</p>	<p>HIE Finance team will prepare a detailed plan. We will engage additional (closely supervised) resource from an outside accountancy firm. We will also work closely with colleagues out-with the Finance team to ensure the non-financial deliverables are available in good time. We will engage with third parties in good time for them to provide the information required for the accounts. We will review resources at the Data Centre to ensure source information is progressed in good time. We will work very closely with Audit Scotland's team to minimise the potential for late adjustments.</p>	<p>Agreement of a detailed timetable for the preparation of the unaudited accounts and associated working papers with the Director of Finance &amp; Corporate Services.</p> <p>Regular meetings with the Director of Finance &amp; Corporate Services to identify any issues in respect of the finance team's capacity and the impact these may have on the preparation of the financial statements.</p> <p>Regular meetings with the Director of Finance &amp; Corporate Services to discuss emerging issues from the audit process.</p>

Audit Risk	Source of assurance	Planned audit work
<p><b>2 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 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><b>3 Risk of fraud over income and expenditure</b></p> <p>Highlands and Islands Enterprise receives a significant amount of income (£7.1 million) in addition to Scottish Government funding. The extent and complexity of income means that, in accordance with ISA240, there is an inherent risk of fraud.</p> <p>In public sector audit there is also a risk of fraud over aspects of expenditure for public sector bodies which have an overall net expenditure. Highlands and Islands Enterprise and its group recorded net expenditure of £69m in 2016/17.</p> <p>The Code of Audit Practice requires 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. Highlands and Islands Enterprise provided grants of £29m to third parties in 2016/17.</p>	<p>Effective budget monitoring by management and members.</p> <p>Effective fraud and whistleblowing arrangements.</p> <p>Internal Audit's work on significant transactions testing which includes large grant payments.</p> <p>Fraud Response and Security review team in place to consider any suspected fraud and security issues.</p> <p>Remit of this team subsumed in the updated Information Security and Fraud Governance Group.</p> <p>Vigilance at the Data Centre with attempted credit card frauds regularly averted and reviewed.</p> <p>BIIA undertake a review of attempted frauds as and when appropriate.</p> <p>Awareness raising activity around fraud and cyber security across HIE including all staff communication and webinars.</p> <p>HIE participates fully in the National Fraud Initiative and actively follow up relevant matches with reports being presented to the Risk and Assurance Committee.</p> <p>The Risk and Assurance Committee receive regular updates on any suspected fraud issues.</p>	<p>Analytical procedures on income streams.</p> <p>Substantive testing of income transactions focusing on the areas of greatest risk.</p> <p>Review of property income which is managed by a third party.</p> <p>Controls testing of key expenditure systems including reliance on internal audit's work on travel and subsistence claims.</p> <p>Substantive testing of expenditure transactions with reliance on internal audit's work on significant transactions.</p> <p>Assessment of the results from Highlands and Islands Enterprise's participation in the National Fraud Initiative (NFI), which will contribute to Audit Scotland's National Report on NFI.</p>

Audit Risk	Source of assurance	Planned audit work
	<p>Our Information Systems provider Enterprise Information Systems (EIS) has also established a Security Council to consider and address the information and cyber security environment.</p>	
<p><b>4 Accounting estimates and judgements</b></p> <p>There is a significant degree of subjectivity in the measurement and valuation of the material account areas of land and buildings (£38m), pension liability (£56m) and investments (£3m) which are revalued at the year end.</p> <p>There is an inherent risk that the financial statements are materially misstated due to the degree of subjectivity in the measurement and valuation of these significant areas.</p>	<p>Pension liability and non-current asset valuations are supported by external professional advisers who are recognised in their field.</p> <p>Investments are valued in-house in line with IAS39. This process has been used for a number of years and has been previously agreed with Audit Scotland. HIE will engage early on in the process to agree the appropriate treatment for soft loans.</p>	<p>Review the work of an expert for the professional valuers (pensions liabilities and non-current assets).</p> <p>Focused substantive testing of year end balances.</p>
<b>Wider dimension risks</b>		
<p><b>5 Financial sustainability</b></p> <p>In our 2016/17 Annual Audit Report we recommended that the rolling five year financial plan should include scenario planning (best, worst and more likely positions) and should include a clear assessment of budget assumptions on activity and any residual risks.</p> <p>Without scenario planning, there is a risk that Highlands and Islands Enterprise is not fully prepared for potential changes in its funding levels and that opportunities and risks may not be fully realised/mitigated.</p>	<p>We have formally defined our risk appetite across our major risk categories and this has been approved by the Board. This will provide vital context and ‘boundaries’ for our scenario planning. We are progressing alignment with the planning requirements of the new Strategic Board to align with partners on a five year strategic plan with annual updates from 2019/20. We have had discussions at Leadership Team regarding the concept of scenario planning specifically for financial plans. We have also liaised with Audit Scotland to obtain examples of good practice. We intend to present a financial scenario planning paper to the Board to sit alongside the usual one-year financial plan.</p>	<p>Review Highland and Islands Enterprise’s developments in long term financial planning, including scenario planning.</p>

Audit Risk	Source of assurance	Planned audit work
<p><b>6 Governance and transparency</b></p> <p>The Scottish Government's Enterprise &amp; Skills review led to the creation of a Strategic Board to provide strategic direction to the work of the four enterprise agencies, including Highlands and Islands Enterprise. A new South of Scotland agency is also to be established.</p> <p>There is a risk of lack of clarity about roles, responsibilities and accountabilities as the new arrangements develop and a risk that this impacts on Highlands and Islands Enterprise's effectiveness.</p>	<p>On-going engagement with the Scottish Government.</p> <p>HIE are actively contributing to the new Strategic Board with the HIE Chairman being a member and the Chief Executive participating. HIE participate fully in the various collaborative work strands which arose following the Enterprise and Skills review. This activity is a standing item at HIE Board meetings and is a standing item at quarterly update meetings with the Scottish Government's sponsor team.</p>	<p>Review the impact of the changes on Highlands and Islands Enterprise, including impact on the operation of the Board.</p>

## 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 Highlands and Islands Enterprise, 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	Risk and Audit Committee date
Management Report	28 May 2018	5 June 2018
Annual Audit Report including ISA 260 requirements	7 August 2018	14 August 2018
Signed Independent Auditor's Report	14 August 2018	N/A

## Audit fee

**7.** The proposed audit fee for the 2017/18 audit of Highlands and Islands Enterprise is £133,490 (2016/17: £131,510). In determining the audit fee we have taken account of the risk exposure of Highlands and Islands 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 financial statements, with a complete working papers package, on 18 June 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

### Risk and Assurance 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 Risk and Assurance 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 Highlands and Islands Enterprise 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 Highlands and Islands 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 Highlands and Islands 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.

**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 Highlands and Islands Enterprise and its group and their expenditure and income
- whether they have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements
- whether the information included in the performance and accountability reports meets requirements for their preparation and is consistent with the financial statements
- the regularity of the expenditure and income

## 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 Highlands and Islands Enterprise and its group are set out in [Exhibit 3](#).



## Exhibit 3

### Materiality values

Materiality level	Amount
<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 the group’s gross expenditure based on the latest audited accounts for 2016/17.	£950,000
<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 performance materiality at 40% of planning materiality.	£380,000
<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 2% of planning materiality.	£20,000

Source: Materiality calculation by Audit Scotland based on the audited HIE Group Accounts 2016/17

**17.** We review and report on other information published with the financial statements including the Performance Report and Accountability Report, which include the Governance Statement and Remuneration and Staff Report. Any issues identified will be reported to the Risk and Assurance Committee.



#### 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 Risk and Assurance Committee dates.

**19.** The timetable for the financial statements preparation and audit is challenging this year (refer to Exhibit 1, Risk 1 above). An external auditor for Highlands and Islands Enterprise’s subsidiaries has not yet been appointed although management have advised that this is currently out to tender. We will meet with the subsidiaries’ auditor once s/he is appointed.

## Exhibit 4

### Financial statements timetable

 Key stage	 Date
Latest submission date of unaudited annual accounts with complete working papers package	18 June 2018
Latest date for final clearance meeting with Director of Finance and Corporate Services	31 July 2018
Agreement of unsigned audited accounts, and issue of Annual Audit Report including ISA 260 report to those charged with governance	7 August 2018
Independent auditor’s report signed	14 August 2018
Latest date for signing of Whole of Government Accounts (WGA) return	28 September 2018

## 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 the Highlands and Islands Enterprise in-house Internal Audit team supported by a contract with Scott-Moncrieff to provide specialist and additional resources as required. In addition, Highlands and Islands Enterprise has developed a joint plan with the internal auditors of Scottish Enterprise (SE) and Skills Development Scotland (SDS) to obtain assurances over the operation of Enterprise Information Systems which deliver ICT services to all three bodies.

### Adequacy of Internal Audit

**21.** We reviewed Highlands and Islands Enterprise's in-house internal audit function and concluded that, overall, the service operates in accordance with Public Sector Internal Audit Standards (PSIAS) and has sound documentation and reporting procedures in place. We have been advised that the requirement to comply with PSIAS is built in to all outsourced internal audit services including those jointly tendered with SDS and SE.

**22.** PSIAS requires that an independent third party review of the internal audit service be undertaken at least every five years. Highlands and Islands Enterprise's in-house internal audit service has not been externally assessed since 2010. We have been advised that an external review of the in-house internal audit service is scheduled to take place in summer 2018.

### Areas of Internal Audit reliance

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

- significant transactions
- travel and subsistence.

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

- certificates of assurance/governance statements
- state aid compliance
- review of the Risk and Assurance Committee's effectiveness.

**25.** In order to ensure a joined-up approach, we are also planning to liaise with the external auditors of SE and SDS regarding the internal audit arrangements for Enterprise Information Systems. We will consider placing reliance on internal audit work in this area where possible.

## Audit dimensions

**26.** As noted in 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.

**27.** Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#). As part of our 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. We shall undertake further work over our five year audit appointment.

## Exhibit 5

### Audit dimensions



Source: Code of Audit Practice

### Financial sustainability

**28.** 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 Highlands and Islands Enterprise'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. We will carry out work and conclude on:

- 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 Highlands and Islands Enterprise can demonstrate the affordability and effectiveness of funding and investment decisions it has made.

### Financial management

**29.** Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We will review, conclude and report on:

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

### Governance and transparency

**30.** 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 Highlands and Islands 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

**31.** Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on the following over our five year appointment:

- whether Highlands and Islands Enterprise can provide evidence that it is demonstrating value for money in the use of its resources
- whether Highlands and Islands Enterprise can demonstrate that there is a clear link between money spent, output and outcomes delivered
- whether Highlands and Islands 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 the Accounts Commission or 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 Assistant Auditor General, who serves as Audit Scotland’s Ethics Partner.

**33.** The engagement lead for Highlands and Islands Enterprise is Gordon Smal, Associate Director. Auditing and ethical standards require the appointed auditor 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 Highlands and Islands 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 (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.

**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.

## **Adding value**

**37.** Through our audit work we aim to add value to Highlands and Islands Enterprise. 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 Highlands and Islands Enterprise 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.

# Highlands and Islands Enterprise

## Annual Audit Plan 2017/18

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or [info@audit-scotland.gov.uk](mailto:info@audit-scotland.gov.uk)

For the latest news, reports and updates, follow us on:



Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN  
T: 0131 625 1500 E: [info@audit-scotland.gov.uk](mailto:info@audit-scotland.gov.uk)  
[www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk)