



Crown Estate Scotland (Interim Management)

External Audit Annual Report to the Accountable Officer and the Auditor General for Scotland for the 2017/18 Financial Year

Final Report - September 2018

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Our audit at a glance



We have fulfilled our responsibilities per International Standards on Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice throughout our work and this final report to the Accountable Officer and the Auditor General for Scotland concludes our work.



We have performed sufficient audit testing around our identified area of significant risk including: management override of controls; risk of fraud in revenue recognition; the risk of fraud in expenditure recognition; and the valuation of investment property. We have not identified any issues to outline to you.



We have raised two audit recommendations around accounts preparation and performance management arrangements.

An audit underpinned by quality



A wider scope audit for the Crown Estate Scotland (Interim Management) (CES(IM)), as set out in our plan, was considered not appropriate. However we have considered your financial planning arrangements and governance. These arrangements continue to be developed and will then be embedded across the organisation.



2017/18 represented the first year that CES(IM) had to produce financial statements. Management demonstrated clear commitment to prepare the financial statements. However, delays in receipt of the Accounts Direction and subsequent amendments lead to delays in finalising the accounts. Going forward, there are opportunities to enhance the financial statements preparation process to ensure timely completion of the accounts.



2017/18 represented the first year of operation for CES(IM). On 1st April 2017, under the Crown Estates Transfer Scheme (2017), £289.4 million of capital assets were transferred to CES(IM) from the Crown Estate. We have confirmed the appropriateness of the recognition of these and agreed to the Transfer Scheme.

Contents

Section	Page
1. Introduction	4
2. Our financial statements audit	5
3. CES(IM) financial and governance arrangements	11
Appendices:	
1. Audit Adjustments	14
2. Action plan	15
3. Fees, independence and fraud arrangements	16
4. Financial reporting future developments	17
5. Communication of audit matters	18



Adding value through our external audit work

First and foremost our objective is to ensure we deliver a quality external audit which fully complies with International Standards on Auditing (ISAs) UK and the Audit Scotland Code of Practice (2016). By ensuring our audit is efficient and effective, gives you assurance over our opinion.

Through this Annual Report we seek to provide insight and commentary over certain aspects of Crown Estate Scotland (Interim Management) (CES(IM)) arrangements, sharing relevant practices with the Audit and Risk Committee and Management.

In the first year of our audit we have looked to develop our relationship with management and our understanding of Crown Estate Scotland (Interim Management) as an organisation. During the year we have supported management with any technical queries, particularly surrounding the accounts production and basis of preparation.

Lastly we are committed to audit quality. In the first year of operation we have focused on key areas of risk at CES(IM), including reviewing key financial processes and internal controls. As the organisation develops and governance arrangements, including internal controls embed, we will consider the key wider scope areas in the remaining years of our audit appointment.

Introduction

This report is a summary of our findings from our external audit work for the financial year ended 31 March 2018.

Our work has been undertaken in accordance with International Standards of Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice 2016.

Our report is addressed to the Crown Estate Scotland (Interim Management) Accountable Officer. In addition, in accordance with our reporting responsibilities the report is jointly addressed to the Auditor General for Scotland.

Once finalised this report will be made publically available on the Audit Scotland website (www.audit-scotland.gov.uk)

We would like to thank Crown Estate Scotland (Interim Management)' management and the finance team for all their support and assistance in the audit process.

Structure of this report

As set out in our Audit Plan we consider in accordance with the Audit Scotland Code of Practice that CES(IM) is a smaller body. Therefore full wider scope is not appropriate. Our report concludes on our financial statements audit and certain aspects of the Authority's arrangements as follows:

Financial statements – Section 2 and Appendix 1

Financial and governance arrangements – Section 2



Our Opinion

For the financial year ended 31 March 2018 we have issued an **unqualified audit opinion**

- True and fair view of the financial statements
- Regularity – expenditure has been incurred in accordance with the purpose of Crown Estate Scotland (Interim Management)
- Other prescribed matters (which include the audited information in the remuneration report)



First year of financial statements

CES(IM) was established on 16 February 2017 under the Crown Estate Scotland (Interim Management) Order 2017 and began operations on 1 April 2017. Consequently the financial statements represent the accounting period from 16 February 2017 to 31 March 2018. These represent the first financial statements prepared by the entity.

The audit process

2017/18 represented the first year that CES(IM) had to produce financial statements. Management demonstrated clear commitment to prepare the financial statements. However, delays in receipt of the Accounts Direction and subsequent amendments lead to delays in finalising the accounts. Going forward, there are opportunities to enhance the financial statements preparation process to ensure timely completion of the accounts.

There were three adjustments arising during the course of the audit (detailed in appendix 1) and a number of disclosure adjustments required to the draft accounts.



Our financial statements audit



Materiality was set at 1% of gross income based on 2017/18 un-audited information (£0.150 million). We have calculated materiality as set out in our plan, and this remains unchanged.



2017/18 represented the first year that CES(IM) had to produce financial statements. Management demonstrated clear commitment to prepare the financial statements. However, delays in receipt of the Accounts Direction and subsequent amendments lead to delays in finalising the accounts. Going forward, there are opportunities to enhance the financial statements preparation process to ensure timely completion of the accounts.



We have issued a true and fair audit opinion on the financial statements, including the wider information contained in the financial statements, and regularity opinion. The audited parts of the Remuneration and staff Report are free from error.



Testing provided assurance on all identified areas of significant audit risks. There were two adjustments made to the draft financial statements during the audit and there were no unadjusted audit differences arising during the course of our audit.

Basis of preparation

Under the Crown Estate Scotland (Interim Management) Order 2017, CES(IM) is required to manage certain assets on behalf of the Crown. Under this arrangement, the CES(IM) makes an annual contribution to the Scottish Government based on net comprehensive revenue account income for the year. This differs from most public sector bodies who are allocated an annual revenue allocation or grant for the year. During 2017/18, CES(IM) made an annual contribution of £9 million to the Scottish Government, exceeding the budgeted £6 million, primarily through higher than forecast marine revenue.

Capital and revenue accounts

Under the provisions of the Crown Estate Scotland (Interim Management) Order 2017 and the Crown Estate Act 1961, CES(IM) is required to maintain a separate capital account within its statement of comprehensive income. The Capital account reflects all profits or losses arising on the sale of investment properties, the realisation of revaluation gains, the income arising on the grant of operating leases over land in exchange for a premium, the charge from revenue for salary costs, and the transfers between the capital and revenue account as required by Statutory provisions and capital transfer agreements. We are satisfied that these have been appropriately reflected in the accounts.

Audit approach and materiality

Our audit approach was set out in our annual audit plan presented to the Audit and Risk Committee on 8 February 2018.

As set out in our plan, we updated our materiality calculations based on the unaudited 2017/18 financial statements. Overall materiality has been set at £0.150 million (1% of gross income) and performance materiality is set at £97,500 (65% of materiality). We report to management any audit difference identified over £7,500 (Trivial as 5% of materiality).

We received a draft trial balance and supporting schedules to support our audit work. However there were delays in finalising the accounts and areas of the draft accounts that were incomplete. 2017/18 was the first year that CES(IM) financial statements have been required and the draft Accounts Direction, which clarifies the basis of preparation of the accounts, was received late in the accounts preparation process from Scottish Ministers and required amendment. Furthermore, we recognise that CES(IM) accounting recognition of revenue and capital comprehensive income statements is uncommon and therefore there was not a template accounts that could be referred to. Going forward we recommend that arrangements are in place to ensure that a complete set of accounts are prepared for audit inspection.

Action plan 1

Audit opinion

Based on our audit procedures performed we have issued an unqualified audit opinion on the financial statements including:

- they give a true and fair view
- they have been properly prepared in accordance with relevant legislation and standards
- the wider information contained in the financial statements
- regularity of expenditure
- audited parts of the remuneration and staff report have been prepared in accordance with applicable guidance

Internal control environment

During the year we sought to understand CES(IM)'s overall control environment (design) as related to the financial statements. In particular we have:

- Sought to understand procedures and controls around related parties, journal entries and other key entity level controls
- Performed procedures around entity level controls and there are no significant matters that we wish to draw to your attention.

During the year CES(IM) were developing and embedding the system of internal financial controls. As a result we have not sought to place any direct reliance on the operating effectiveness of these controls and instead have adopted a substantive based approach to the audit of the financial statements and therefore our review is limited to the design of controls rather than the operating effectiveness of these. Based on the work performed, no material weaknesses in the accounting and internal control systems were identified based on our work undertaken during the audit which could have an adverse impact on the organisation's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

Internal Audit

CES(IM) did not have an internal audit function in place during 2017/18. From 2018/19, Scott-Moncrieff have been appointed as internal audit providers. The internal audit function plays a critical role in supporting organisations bring together a systematic approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Key audit issues – Our response to significant audit risks

	Identified audit risk	Work completed	Our conclusion
Risk of fraud in revenue	As set out in ISA 240, there is a presumed risk that revenue may be misstated due to improper recognition of revenue. The organisation has multiple revenue streams. Our presumed risk focuses on material revenue streams including rent and royalties. We consider the risk to be prevalent around the year end and therefore focus our audit work on transactions around this period.	<ul style="list-style-type: none"> Developed our understanding of CES(IM)'s material revenue streams including walkthrough of key transactions. Performed targeted review and testing of key revenue streams during the year, including analytical procedures and transaction testing including information from asset managers and underlying transactions Performing revenue cut off procedures and substantive testing year end balances Testing the existence of balances at the year end 	<p>From our audit procedures performed we are satisfied that revenue is free from material misstatement. During the audit an adjustment was raised to revenue but we do not consider this to be indicative of fraud or irregularity and are comfortable that this has been appropriately corrected in the accounts.</p> <p>We are satisfied that revenue has been recognised in the appropriate financial year.</p>
Operating expenditure is not treated correctly	Operating expenditure is understated or not treated in the correct period (risk of fraud in expenditure). As set out in Practice Note 10 (revised) which applies to public sector entities.	<ul style="list-style-type: none"> Developed our understanding of CES(IM)'s material expenditure streams including walkthrough of key transactions. Performing targeted review and testing of key expenditure streams during the year, including analytical review of expenditure and targeted transaction testing, including consideration of the regularity of expenditure incurred. Performing cut-off testing of expenditure transactions around the year end to ensure these had been allocated to the appropriate financial year. Reviewing post year end payments for any potential unrecorded liabilities. 	<p>Reasonable assurance gained that expenditure has been recorded within the appropriate financial year and that payables are free from material misstatement. During the audit an adjustment was raised to revenue but we do not consider this to be indicative of fraud or irregularity and are comfortable that this has been appropriately corrected in the accounts.</p> <p>We are satisfied that expenditure has been incurred in accordance with the type/nature of CES(IM) as an organisation.</p>
Management override of controls	As set out in ISA 240 there is a presumed risk that management override of controls is present in all entities	<ul style="list-style-type: none"> Developed our understanding of the entity level controls in place at CES(IM) that reduce the risk of management override Performed review of journal transactions for unusual transactions or balances. Evaluated key areas of judgement within the Financial statements and the basis for these judgements / application of accounting policies Reviewed unusual and/or significant transactions 	<p>We did not identify any significant areas of bias in key judgements by management. We have not identified any unusual or significant transactions during the course of the year that would indicate management manipulation.</p>
Valuation of investment reports	CES(IM) holds a range of assets, including investment property. In accordance with the FReM, investment property is held on a fair value basis in accordance with IFRS 13. The valuation of these properties can often be complex.	<ul style="list-style-type: none"> Developing our understanding of the arrangements in place to obtain investment property valuations Reviewed and challenged valuations to ensure that assumptions used are reasonable, including agreeing to appropriate data sources, where applicable. Ensuring that investment valuations are correctly accounted. 	<p>We are satisfied that the investment property valuations have been appropriately reflected in the accounts and the basis of the valuations are reasonable and appropriate for the asset type. Appropriately qualified valuers have been used to support the valuation (We have detailed these below under <i>Investment Properties</i>).</p>

Other key areas of the financial statements

As part of our audit there were other particular key areas of focus. While not considered a significant audit risk, these are areas of potential increased risk due to their complexity or magnitude.

Crown Estate Transfer Scheme 2017: CES(IM) took ownership and control of a significant number of assets previously held by the Crown Estate. £289.4 million of capital assets were transferred to CES(IM) under the Crown Estate Transfer Scheme 2017. In our audit plan we had assumed this to be an opening balance sheet adjustment. However, under the Scheme this represented an in-year transaction with the balance of assets transitioning across from Crown Estate to CES(IM). We have agreed the assets transferred to the 2016/17 Crown Estate audited financial statements, the transfer scheme itself as well as CES(IM) accounting records.

Bonus payments: CES(IM) staff who joined before 1st January 2018, are contractually eligible for a discretionary bonus. The bonus payment for 2017/18 was subject to consideration by the Board during the year. Following independent legal advice, CES(IM) as an employer had a legal obligation to continue to honour the terms of employment of staff transferring from The Crown Estate, including a duty to provide bonus arrangements. Given potential reputational and legal risks of having a two tiered remuneration approach to same groups of staff, it was determined that staff joining up to 1 January 2018 were eligible to participate in the scheme. The bonus is based on delivery of key performance targets including:

- the delivery of the overall financial targets for CES(IM), being the level of contribution to the Scottish Government.
- Individual performance targets – being assessment of a maximum six individual objectives in addition to two mandatory objectives relating to behaviours and health and safety.

The structure of the bonus scheme is also based on level of responsibility, aligned to the CES(IM) role level hierarchy, with bonus rates linked to level of responsibility.



Based on the outcome of the annual performance assessment, total amount of £169,115 was accrued at the year end for bonuses for the financial year. This related to 31 employees. We have reviewed the conditions of the bonus and are satisfied that the bonuses accrued at 31 March 2018 reflected the CES (IM) performance assessment of the relevant staff.

During 2017, reflecting the performance of The Crown Estate the financial year ended 31 March 2017, the former Chief Executive received a bonus paid through CES (IM) of £49,860. This related to the performance and contribution to the results of The Crown Estate for the prior financial year and was wholly funded by The Crown Estate.

CES(IM) entered into an agreement with the former Chief Executive the terms of which provided that a payment in compensation for loss of office would be payable, subject to the fulfilment of certain conditions. During 2018, these conditions were satisfied and a payment of £94,425 made. The agreement was subject to independent legal advice, reflecting the former Chief Executive's term of appointment from the Scottish Government and was subject to approval from the Chair of the Board. Remuneration amounts have been appropriately disclosed in the accounts.. As part of our 2018/19 as the staffing arrangements at CES(IM) embed we will review remuneration arrangements in more detail.

Narrative elements of your annual accounts

In accordance with our responsibilities we have reviewed your narrative aspects of the Annual Accounts and Report. We have considered the consistency of this narrative with our understanding and the financial statements and have set out our observations below. We have also audited the required information in the remuneration report (marked audited) and have no matters we wish to bring to your attention.

We have audited the relevant sections of the Remuneration and Staff Report (marked audited) and have reviewed the remaining sections of the draft report to ensure that they are not inconsistent with other information in the financial statements.

Key aspects of your financial statements

As set out in our audit plan we consider particular aspects of your financial statements in relation to management judgements including estimates and where management may have particular options or choices in what accounting standards or disclosure requirements to apply. We have summarised where these apply, and our conclusions below.

CES(IM) accounting policies are in accordance Crown Estate Scotland (Interim Management) Order 2017 and the Crown Estate Act 1961 and the FReM (except where these are inconsistent with the requirements of the 1961 Act) and we consider these to be appropriate to the organisation and consistent with those adopted in prior years.

Accounting estimates and judgements

Crown Estate Scotland (Interim Management)' significant accounting estimates and judgement impacting on the annual accounts are the following:

- *Investment property valuations:* Where we are satisfied these are supported by qualified expert valuations. See *Investment Properties* below for more detailed consideration of these estimates.
- *Bad debt provision calculations:* Allowances for bad and doubtful debts are based on discussions between management agents and Management, including legal representation. We have reviewed the provision recognised in the current year as well as considering the recoverability of outstanding debtors and are satisfied that these are appropriate.

We are satisfied that the estimates and judgements applied by management are reasonable and not subject to management bias.



Fraud and irregularity

There are no provisions or uncertainties related to the accounts.

In relation to the audit risk of fraud in respect of expenditure we tested CES(IM) cut off arrangements in particular (timing) and identified no issues in accruals or prepayments which would indicate potential fraud. There are no post balance sheet events or legal uncertainties at year-end.

Going concern

CES(IM) has an agreed budget for 2018/19 and is satisfied that it continues to represent a going concern.

For 2017/18 CES(IM) generated a profit (comprehensive revenue account) of £9 million and capital account profit of £50.4 million for the financial year. This performance allows CES(IM) to contribute an additional £3.1 million than the planned £5.9 million to the Scottish Government. In addition CES(IM) retains a strong balance sheet with net assets of £339.8 million and cash and cash equivalents of £10.9 million. There are no indications that CES(IM) will not continue to meet its obligations as they fall due and therefore continues to represent a going concern.

Investment properties

In accordance with IAS 40: *Investment properties*, investment properties the property portfolio was valued on 31 March 2018. Given the diverse range of properties held, the work was conducted by independent accredited external valuers with a recognised relevant professional qualification and with recent experience in the locations and categories of the investment property being valued.

Class of property	Fair value 31 March 2018 £m	Audit satisfied of the suitability of the work of the expert	Valuation recognised is reasonable
Rural and Coastal portfolio:			
Agricultural	106.7	✓	✓
Coastal	32.5	✓	✓
Forestry	16.0	✓	✓
Minerals	1.2	✓	✓
Marine portfolio:			
Renewables – Offshore Wind	100.7	✓	✓
Renewables – Wave & Tidal	0.3	✓	✓
Cables & Pipelines	23.5	✓	✓
Aquaculture	27.0	✓	✓
Urban portfolio:			
Offices & retail	16.7	✓	✓
Total all portfolios at valuation	324.6		

For each class of property, we have agreed the valuation recognised to the independent valuation report. We have reviewed the appropriateness of the valuer, including their relevant skills, experience and objectivity as well as the scope of their work. We have considered the reasonableness of the valuation, including the technique applied and, where applicable, the accuracy of the underlying data to support this valuation. We are satisfied that the approach adopted is considered reasonable.

CES(IM)'s financial and governance arrangements

Financial Management

For 2017/18, CES(IM) generated a revenue account profit of £9 million exceeding budget of £5.9 million. CIES generated capital account profit of £50.4 million, predominantly reflecting the £49.7 million of revaluation gains on investment property. The outturn against budget primarily reflected higher revenue across aquaculture, with higher than anticipated finfish production. It is recognised that the in-year increase may reduce future short term production levels.

Financial performance is monitored throughout the year by senior management and reported to the Board and also monitored through the Audit and Risk Committee. CES(IM) demonstrated reasonable financial management arrangements. Arrangements for monitoring and reconciling management agent information were developed during the year and this continues to be an area of continued focus and scrutiny.



Financial Sustainability

CES(IM)'s 2018/19 budget projects a revenue account profit of £7.3 million. This reflects assumed revenue of £16.4 million. The organisation recognises that since separation from The Crown Estate new and increased indirect costs have emerged as they continue to develop the infrastructure to operate the business on a stand alone basis. However, CES(IM)'s financial forecasts continue to demonstrate strong financial performance with approximately 44% of total revenue paid in contributions to the Scottish Government.



Over the medium to longer term CES(IM) strategic objectives include growth of revenue and enhancing the capital value of the estate. Successful delivery of the Investment strategy will be critical in delivering this, balancing not only financial returns and growth but also wider social and economic value and environmental sustainability. The level of revenue and valuation of investments is directly impacted on economic factors including market values and prices. As a result key social and political events such as Brexit remain an area of focus and identified risk to the delivery of the organisations strategic goals.



Governance arrangements

2017/18 represented the first year of the CES(IM) being established with the responsibility for the management of the assets transferred from the Crown Estate. While governance arrangements, including the membership of the Board and supporting committees, policies and frameworks have been established during the year, these will require time to fully embed across the organisation. In particular, the organisations risk management and governance arrangements continue to be developed and transparency over decisions enhanced. Key to this will be an efficient and effective internal audit function to support and assure the organisation on its internal control and risk management arrangements.

The CES(IM) Board consists of the Chair and eight members who are appointed by Scottish Ministers. The role of the Board is set out in the Framework Document including defined delegations to its two committees: Audit and Risk Committee; and Investment Committee, which were established during the year.

New primary legislation, the Scottish Crown Estate Bill, is currently being considered by the Scottish Parliament. It proposes introducing new mechanisms for other bodies ('managers') to potentially manage parts of the Scottish Crown Estate and will establish the permanency of the organisation. Management recognises that the transition from an interim body to a permanent organisation may create significant challenges and pressures on the organisation, particularly around new ways of working and potentially new or enhanced systems. It will be critical that the organisation embrace this change and ensure that there is continuous focus and prioritisation of the organisations strategic goals and objectives. To support this the continued development of key performance measures and the close monitoring of these will be critical in supporting the organisation continue to develop.

Action plan 2

Appendices

Audit adjustments

Action plan

Fees, independence and fraud arrangements

Financial reporting future developments

Communication of audit matters

Audit adjustments

Uncorrected and corrected misstatements

We are pleased to report that there were no uncorrected misstatements to the financial statements arising during our audit.

There were a number of smaller adjustments to the draft accounts received for audit inspection. These were primarily in relation to late allocation adjustments between the draft trial balance received for audit inspection and the final accounts. The adjustments made are detailed below

Item		Dr (£'000)	(Cr) (£'000)	Description
1	Expenditure (operating costs)	78		<i>Being adjustment to recognise unrecorded expenditure</i>
	Accruals		(78)	
2	Investment Properties	4,337		<i>Being adjustment to recognise the fair value of investment properties</i>
	Gain on revaluation of properties (capital fund)		(4,337)	
3	Revenue		(49)	<i>Being adjustment to recognise unrecorded revenue</i>
	Receivables	49		

Disclosure misstatements

In accordance with auditing standards we are required to highlight significant disclosure misstatements to allow the Audit and Risk Committee to evaluate the impact of these matters on the financial statements. There were no material/significant disclosure misstatements identified we wish to bring to your attention. We recognise that 2017/18 represented the first year of accounts production and that the final Accounts Direction, detailing the basis of accounts, was received relatively late in the accounts production process from Scottish Ministers. There is therefore an opportunity for management to re-look at the template accounts to ensure this continues to comply with the FReM and meets all of the organisation's disclosure requirements.

Action plan

We have set out below, based on our audit work undertaken in 2017/18, those risks and recommendations we consider are of a higher risk to Crown Estate Scotland (Interim Management) that Management may wish to consider in the future.

Recommendation

Agreed management response

Financial statements preparation

We received a draft trial balance and supporting schedules to support our audit work. 2017/18 was the first year that CES(IM) financial statements have been required and the draft Accounts Direction, which clarifies the basis of preparation of the accounts, was received late in the accounts preparation process and required amendment. Consequently there were delays in finalising the financial statements.

Going forward we recommend that arrangements are in place to ensure that a complete set of accounts are prepared for audit inspection.

Management response: Agreed – Note the Accounts Direction and accounts template is now established.

Action owner: Head of Finance and Commercial

Timescale for implementation: For Financial year end 31 March 2019

Governance and performance management

Following the establishment of CES(IM) in 2017 and ongoing progress of transitioning to a more permanent arrangement, the organisations key governance and operating systems and process continue to embed and be developed. It will be critical that the organisation embrace this change and ensure that there is continuous focus and prioritisation of the organisations strategic goals and objectives. To support this the continued development of key performance measures and the close monitoring of these will be critical in supporting the organisation continue to develop.

Management response: Agreed

Action owner: Senior Management Team

Timescale for implementation: Ongoing

Fees, independence, fraud arrangements

External Audit Fee

Service	Fees £
External Auditor Remuneration	25,000
Pooled Costs	3,270
Contribution to Audit Scotland costs	820
Contribution to Performance Audit and Best Value	0
2017-18 Fee	29,090

The audit fee was calculated in accordance with guidance issued by Audit Scotland and agreed with Management.

The above fee has not changed and our final fee was £29,090.

Fees for other services

Service	Fees £
We can confirm there are no non-audit fees for the 2017/18 financial year	Nil

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention.

We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

We are required by auditing and ethical standards to communicate any relationships that may affect the independence and objectivity of the audit team.

We can confirm no independence concerns have been identified.

Fraud arrangements

In assessing our audit risks, the audit team was alert to the possibility of fraud at CES(IM)

As part of our audit work we are responsible for:

- identifying and assessing the risks of material misstatement of the financial statements due to fraud in particular in relation to management override of controls.
- Leading a discussion with those charged of governance (for Crown Estate Scotland (Interim Management) this is assumed to be the Audit and Risk Committee) on their view of fraud. We did this when presenting our audit plan.
- designing and implementing appropriate audit testing to gain assurance over our assessed risks of fraud
- responding appropriately to any fraud or suspected fraud identified during the audit. – None were identified in-year

As auditors we obtain reasonable but not absolute assurance the financial statements as a whole are free from material misstatement, whether due to fraud or error.

We will obtain annual representation from management regarding managements assessment of fraud risk, including internal controls, and any known or suspected fraud or misstatement.

It is **Crown Estate Scotland (Interim Management)'s** responsibility to establish arrangements to prevent and detect fraud and other irregularity. This includes:

- developing, promoting and monitoring compliance with standing orders and financial instructions
- developing and implementing strategies to prevent and detect fraud and other irregularity
- receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity.

Throughout the audit we worked with CES(IM)) to review specific areas of fraud risk, including the operation of key financial controls.

We also examined certain policies in place, strategies, standing orders and financial instructions, as relevant to the fraud framework, to ensure that they provide a reasonable framework of internal control.

No suspected frauds or irregularities have been identified by Management and reported in-year.

Financial reporting - future developments

As financial reporting standards continue to develop we highlight to management those areas which are most likely to have an impact on CES(IM)'s financial statements:



International Financial Reporting Standard 16: Leases (IFRS 16) supersedes IAS 17 Leases and its associated interpretations. IFRS 16 introduces a single lessee accounting model whereby assets and liabilities for all leases with a term greater than 12 months are expected to be recognised within the lessee's financial statements. This is expected to result in a number of lease arrangements, currently recognised as operating leases, coming on to the balance sheet. The standard is expected to apply in the public sector from 2019/20 and therefore it is important that organisations consider the impact on the current accounting treatment of their lease agreements.

IFRS 15: Revenue from Contracts with Customers is effective from 1 January 2018. The standard introduces a five-step model to determine when to recognise revenue, and at what amount. Revenue is recognised as a company transfers control of goods or services to a customer at the amount to which the company expects to be entitled. Given the nature of the organisation's revenue streams, it is unlikely that the new standard will materially impact on revenue recognised.

Impact on CES(IM)

Management are in the early stages of considering the impact of the revised accounting standards. IFRS 16 is unlikely to have an accounting impact where CES(IM) acts as lessor and the organisation currently has a relatively low level of operating leases where it acts as lessee. The extent of the impact of IFRS 15 will depend on underlying rental agreements. We will continue to monitor the progress made by the organisation, particularly where these are likely to result in a material change to financial reporting.

Communication of audit matters

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	•	
Overview of the planned scope and timing of the audit, including planning assessment of audit risks and wider scope risks	•	
Confirmation of independence and objectivity		
We are independent of Crown Estate Scotland (Interim Management) and have not identified any conflicts of interest	•	•
A statement that we have complied with relevant ethical requirements regarding independence. Relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged. Details of safeguards applied to threats to independence	•	•
We have not incurred any non-audit fees during the year and no threats to independence identified		
Significant matters in relation to going concern	•	•
No significant going concern matters identified		
Views about the qualitative aspects of Crown Estate Scotland (Interim Management) accounting and financial reporting practices, including accounting policies, accounting estimates and financial statement disclosures		•
Set out in the Financial statements Section		
Significant findings from the audit		•
No significant findings from our audit		
Significant matters and issues arising during the audit and written representations that have been sought		•
Letter of representation has been signed by the Accountable Officer. This is our standard, unmodified letter of representation.		
Significant difficulties encountered during the audit		•
No difficulties encountered		
Significant deficiencies in internal control identified during the audit		•
None identified		
Significant matters arising in connection with related parties		•
None identified		
Identification or suspicion of fraud involving management and/or which results in material misstatement of the financial statements		•
None identified. A nil fraud return was submitted to Audit Scotland in April 2018 in accordance with the planning guidance.		
Non-compliance with laws and regulations		•
None noted		
Unadjusted misstatements and material disclosure omissions		•
None noted. Minor disclosure amendments only and these were not material in nature		
Expected modifications to the auditor's report, or emphasis of matter		•
None, an unqualified opinion		

International Standards on Auditing (UK) (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table above.

We communicate any adverse or unexpected findings affecting the audit on a timely basis, either informally or via a report to Crown Estate Scotland (Interim Management) Management and the Audit and Risk Committee.

