



# Technical bulletin 2017/1 January to March 2017

 AUDIT SCOTLAND

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Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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# Foreword

Technical bulletins are prepared by Audit Scotland's Technical Services Unit (TSU), and approved by the Assistant Auditor General, to provide external auditors appointed by the Accounts Commission and Auditor General for Scotland with

- information on the main public sector technical developments in the quarter that are relevant to their audit appointment
- guidance from the TSU on any emerging risks identified in the quarter.

Technical bulletins are available to external auditors from Audit Scotland's *Technical reference library*, and published on the [Audit Scotland website](#) so that audited bodies and other stakeholders can access them.

It is important that auditors read this technical bulletin promptly so they are familiar with the information and guidance provided. The auditor action checklist section at the end of each chapter should be completed by a senior member of the audit team.

The articles on technical developments are intended to highlight the key points that the TSU considers external auditors require to be aware of. It may still be necessary for auditors to read the source material where greater detail is required. The documents referred to in the articles can be obtained by using the hyperlinks, where available. They are also available to external auditors from Audit Scotland's *Technical reference library*.

While auditors act independently, and are responsible for their own conclusions and opinions, the TSU has a role in ensuring that those conclusions and opinions are reached on the basis of informed judgement. Consistency in similar circumstances is important and paragraph 108 of **Audit Scotland's Code of audit practice therefore states that auditors should normally follow TSU guidance**. This means that auditors are expected to follow the guidance or provide a reasonable explanation as to why not. Auditors should advise the TSU promptly if they intend not to follow guidance provided in this technical bulletin on an emerging risk.

The TSU encourages feedback on this technical bulletin. Comments should be sent to [pobrien@audit-scotland.gov.uk](mailto:pobrien@audit-scotland.gov.uk).

More in-depth and extensive guidance is provided in separate technical guidance notes published by the TSU. Technical guidance notes published in the quarter are referred to in this technical bulletin, and can be obtained by using the hyperlinks to the [Audit Scotland website](#).

Audit Scotland makes no representation as to the completeness or accuracy of the contents of technical bulletins or that legal or technical guidance is correct. Points of law, in particular, can ultimately be decided only by the Courts. Audit Scotland accepts no responsibility for any loss or damage caused as a result of any person relying upon anything contained in this technical bulletin.

# Headlines

This chapter provides brief headlines for the articles on technical developments and guidance in this technical bulletin, classified by the audit year to which it relates, and referenced to the paragraphs containing the main article.

Cross sector chapter		Paragraphs
<b>2016/17 audit year</b>		
<b><i>Technical developments</i></b>		
The FRC has issued a report on quality control policies and procedures		1-7
The FRC has issued a report on the use of audit data analytics		8-13
The Financial Reporting Lab has issued a report on good practice in business model reporting		18-21
<b>2018/19 audit year</b>		
<b><i>Technical developments</i></b>		
The FRC has issued a consultation paper on proposed revisions to <i>ISA (UK) 250</i>		14-17
CIPFA has issued a consultation paper on the treasury management code		22-24

Local authority chapter		Paragraphs
<b>2016/17 audit year</b>		
<b><i>Technical developments</i></b>		
CIPFA has issued guidance notes to the 2016/17 accounting code		26-29
CIPFA has issued a revised version of its capital accounting reference manual		30-31
CIPFA has issued a statement on the highways network asset		32-35
CIPFA has issued 2016/17 LGPS example accounts and disclosure checklist		36-40
The DWP has issued guidance on the 2016/17 HB subsidy claim		41-42
PSAA has issued 2016/17 HB COUNT modules		43-46

Local authority chapter	Paragraphs
The DWP has issued various HB circulars	47-50
CIPFA has issued a consultation on the prudential code	51-52

Central government chapter	Paragraphs
<b>2016/17 audit year</b>	
<b><i>Technical developments</i></b>	
The TSU has published a technical guidance note on planning and performing the audit of the 2016/17 central government annual report and accounts	54-58
The TSU has issued a technical guidance note containing the 2016/17 model independent auditor's reports for central government bodies	59-64
Treasury has issued a revised 2016/17 FReM	67-73
The NAO has issued the 2016/17 FReM disclosure guide for the financial statements	74-76
The TSU has issued an annual report disclosure guide for Scottish bodies	77
Treasury has issued the 2017/18 FReM	78-79
The Cabinet Office has issued guidance on the remuneration and staff report for 2016/17	80-87
Treasury has issued the discount rate for post-employment benefits liabilities and general provisions as at 31 March 2017	88-91
The Scottish Government has issued a revised version of the guidance on the role of board members	92-93

Health chapter	Paragraphs
<b>2016/17 audit year</b>	
<b><i>Technical developments</i></b>	
The TSU has published a technical guidance note on planning and performing the audit of the 2016/17 health board annual accounts	95-99

Health chapter	Paragraphs
The TSU has issued a technical guidance note containing the 2016/17 model independent auditor's reports for health boards	100-105
The SGHSCD has issued the 2016/17 accounts manual for health boards	109-117
The SGHSCD has issued the 2016/17 CAM	118-120

Further education chapter
There are no items in this technical bulletin specific to further education colleges

Fraud and irregularity chapter	Paragraphs
The TSU has provided a summary of reported fraud cases	122

# Cross-sectoral chapter

## Introduction

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This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to all sectors.

It should be read by all external auditors. Information on developments and guidance from the TSU in the quarter that are relevant to only one sector are covered in the relevant sector-specific chapter.

## Auditing developments

### Report on audit quality control procedures

1. The [Financial Reporting Council](#) (FRC) has issued a [report](#) setting out the findings from a thematic review of quality control policies and procedures in the six largest UK audit firms. The report highlights areas of good practice as well as areas where improvements can be made.
2. Some firms have set out their audit quality procedures using the following 'three lines of defence' model
  - The first line of defence includes the selection of an appropriate audit team, reviews of work by more senior team members, access to technical support, and technical reviews of financial statements.
  - The second line of defence is the functions that oversee audit quality management, e.g. leadership responsibilities for audit quality, the audit methodology, resource management, as well as the recruitment, training and appraisal of staff.
  - The third line of defence is the functions that provide independent assurance, e.g. internal quality monitoring.
3. The report highlights the importance of auditors consulting with technical support on accounting and auditing matters. It explains that consultation
  - improves the application of professional judgement
  - aids consistency of approach
  - assists the appropriate application of professional standards
  - facilitates meaningful discussion and challenge which should result in more robust, defensible and better documented audit evidence.
4. The review found that audit teams were using the firms' consultation processes appropriately, and clearly documenting the conclusions of these consultations.



5. All firms' audit methodologies require a number of audit procedures to evaluate the overall presentation of the annual report and accounts. These procedures include
  - completing disclosure checklists
  - reviews by members of the audit team
  - obtaining a technical review from an independent reviewer with specific accounting technical expertise.
6. The responsibilities of the individuals involved in these procedures varied between firms and, in some cases, it was not clear whether these responsibilities were appropriate. Lines of responsibilities may therefore become confused and errors may not be identified.
7. The report notes differences in the structure of the firms' functions in respect of the independent technical review. Differences that may affect the quality and effectiveness of the reviews included
  - the types of audits where the financial statements are required to be subject to technical review
  - the information received by the technical reviewer
  - the responsibilities for dealing with the points raised by the reviewer.

## Report on data analytics

8. The FRC has also issued a [report](#) on the findings from an audit quality thematic review on the use of audit data analytics (ADAs) which focusses on good practice in the development of ADAs at the six largest UK audit firms.
9. ADA is defined in the review as the science and art of discovering and analysing patterns, deviations and inconsistencies, and extracting other useful information in the data underlying or related to the subject matter of an audit through analysis, modelling and visualisation for the purpose of planning and performing the audit.
10. The review identified ADA that has been implemented to
  - analyse all transactions in a population, stratify that population and identify outliers for further examination
  - re-perform calculations relevant to the financial statements
  - match transactions as they pass through a processing cycle
  - assist in segregation of duties testing
  - compare entity data to externally obtained data
  - manipulate data to assess the impact of different assumptions.
11. Many of these standard ADA tools employ data visualisation techniques. Graphs, plots and information graphics may be used to enable patterns, trends, correlations and outliers to be identified more easily. In addition they may also be useful in communicating insights arising from the ADA work to the audit committee.

12. Some firms are at an early stage in considering further ADA techniques, including continuous control monitoring, benchmarking of data between audit clients at a transactional level, and unstructured data analysis (e.g. the content of emails).
13. Section 1.4 of the report summarises the findings from review, with further details set out in section 2. For example findings include
  - The use of data analytics in the audit is not as prevalent as the market might expect. Pressure on firms to promote the use of ADA techniques may result in the pace of development and usage being overemphasised.
  - Audit quality can be enhanced through the use of data analytics. ADA techniques can provide audit evidence that is more focused to the audit risks and provide useful insights to an entity's management and the audit committee.
  - Audit teams need to have a clear understanding of the purpose of the ADA technique within the audit methodology.

### Proposed revisions to ISA (UK) 250

14. The FRC has issued a consultation paper on proposed revisions to [ISA \(UK\) 250 Section A Consideration of laws and regulations in an audit of financial statements](#) to reflect recent revisions to the international ISA 250.
15. The revisions to ISA 250 were in response to changes to the international ethics code which addressed the professional accountant's responsibility in relation to non-compliance with laws and regulations (NOCLAR). The limited amendments are intended to address inconsistencies of approach between the NOCLAR provisions in the revised ethics code and the ISAs.
16. The proposed consequential amendments to ISA (UK) 250
  - clarify the requirement regarding the auditor's determination of whether to report identified or suspected NOCLAR to an appropriate authority outside the entity
  - highlight that the auditor may have additional responsibilities under law, regulation or relevant ethical requirements
  - enhance the consideration of the implications of NOCLAR on the audit, e.g. the reliability of management's representations.
17. Comments should be sent to [AAT@frc.org.uk](mailto:AAT@frc.org.uk) by 26 May 2017.

## Accounting developments

### Management commentary

#### New report on business model reporting

18. The [Financial Reporting Lab](#) has issued [Business model reporting](#) which summarises good practice in reporting information on an entity's business model.

19. As no commonly agreed definition currently exists, this report defines the term business model as being what the organisation does, how it does it, and how it currently creates economic value. The report contrasts a business model with a business strategy which is concerned with where the organisation is going and how it intends getting there.
20. The report recommends that business model disclosures in the annual accounts (including a local authority' management commentary) should describe
  - how the body generates or preserves value over the longer term
  - what the body does and why
  - how the body is structured
  - the nature of the relationships, resources and other inputs that are necessary for the success of the business.
21. Good practice in the presentation of business model disclosures includes the following
  - The appropriate location is towards the front of the strategic report (or equivalent report) as it provides context and understanding for the other narrative and financial information.
  - Disclosures should be written in plain, clear, concise and factual language.
  - Information is best communicated through a combination of narrative and infographics, tables and charts.

## Other developments

### Treasury management

#### Consultation on treasury management code

22. The [Chartered Institute of Public Finance and Accountancy](#) (CIPFA) has issued a [consultation paper](#) to seek views on whether the current edition of the *Treasury management in the public services code of practice* should be amended.
23. The consultation paper includes questions on whether
  - each public body has adopted the treasury management code and if any practical implementation issues have been experienced
  - the principles in the code are relevant to each body
  - there are areas not fully covered by the principles.
24. Comments are required to be sent to [mandy.bretherton@cipfa.org](mailto:mandy.bretherton@cipfa.org) by 21 April 2017. CIPFA will then hold a further consultation on proposed changes to the code which are expected to apply from 2018/19.

## TSU contact for cross-sector chapter

25. The contact in the TSU for this chapter is Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or [pobrien@audit-scotland.gov.uk](mailto:pobrien@audit-scotland.gov.uk).

# Local authority sector

## Introduction

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This chapter contains information on the main technical developments, and guidance from the TSU on any emerging risks, in the quarter that are relevant to the local authority sector.

It should be read by external auditors with appointments in the local authority sector. Auditors should also read the cross-sectoral chapter.

## Accounting developments

### General accounting

#### 2016/17 code guidance notes

26. CIPFA has issued guidance notes to assist in understanding the accounting requirements of the 2016/17 *Code of practice on local authority accounting in the UK* (the accounting code). The guidance notes provide background to the 2016/17 accounting code's requirements and include detailed illustrations, but are not prescriptive.
27. The main changes in the guidance notes are to Module 3 (sections C to I) to reflect the
  - new formats and reporting requirements for the comprehensive income and expenditure statement and the movement in reserves statement
  - introduction of the new expenditure and funding analysis required by Code paragraphs 3.4.2.96 to 3.4.2.98.
28. Page 351 of the guidance notes provides an illustration of the expenditure and funding analysis. Code paragraph 3.4.2.95 requires that due prominence be given to the expenditure and funding analysis in accordance with the needs of users. This means each authority can decide where it is best positioned. The guidance notes have positioned the expenditure and funding analysis before the main statements. However, a footnote clarifies that the status of the analysis is that of a note to the financial statements.
29. Module 3 also includes the accounting code's amendments to reflect the changes to *IAS 1 Presentation of financial statements* under the International Accounting Standards Board's (IASB) *Disclosure initiative*, including
  - guidance on ordering the notes covered by Code paragraph 3.4.2.84
  - the presentation of sub-totals referred to at Code paragraph 3.4.2.61.

## Property, plant and equipment

### Revised reference manual

30. CIPFA has issued a revised version of its *Local authority capital accounting - a reference manual for practitioners* provides guidance on local authority capital accounting. The manual focuses on the practical application of the accounting theory set out in the accounting code.
31. This is the second edition of the manual. The previous edition has been updated to reflect the requirements of *IFRS 13 Fair value measurement*. The manual is in the following three parts
  - The first part of the manual is a reference section organised by topic which is based on the most frequently asked questions on capital accounting received by CIPFA.
  - Part 2 contains fictional stories about two assets. The first shows events happening to a building over an authority's eight year ownership, while the second sets out the treatment of leased vehicles.
  - Part 3 provides a glossary of accounting terms used in the manual.

## Highways network asset

### Update on move to current value

32. Technical bulletin 2016/4 (paragraph 47) referred to the decision of the [CIPFA/LASAAC Local Authority Code Board](#) to postpone the change to measuring the highways network asset at current value planned for 2016/17.
33. CIPFA/LASAAC has subsequently issued a [statement](#) to advise that it has decided not to proceed with the change in measurement basis. The board will give further consideration to this matter if there is clear evidence that the benefits outweigh the costs. An [Update to 2016/17 accounting code](#) had previously been issued to remove references to the change in measurement basis from the 2016/17 code.
34. In addition, CIPFA has issued [Highways network asset briefing number 4](#) which clarifies that the infrastructure class of assets will continue to be accounted for as in previous years and it will include the components of the highways network asset. There are therefore no reporting provisions relating to the highways network asset for the 2016/17 financial year.
35. As a result of the above, module 2 of technical guidance note 2016/10(LA), and references in the 2016/17 audit planning guidance, on auditors' responsibilities in respect of the highways network asset no longer apply.

## Pension funds

### Illustrative 2016/17 financial statements

36. CIPFA has issued the *2016/17 LGPS fund accounts – example accounts and disclosure checklist* to illustrate the financial statements of local government pension scheme (LGPS) pension funds.

37. The publication provides an example set of accounts that meet the minimum requirements of the accounting code in respect of LGPS accounts. It sets out a fund account and a net assets statement as well as information to be disclosed in the notes.
38. The main change for the 2016/17 example pension fund accounts is the extension of the fair value disclosures required under section 2.10 of the accounting code to pension funds. The additional disclosures required are included in note 16 which deals solely with items at fair value and which now includes property investments.
39. Other changes made to the example pension fund accounts include the following
  - Note 11 now includes an analysis of investment management expenses in line with CIPFA's *Accounting for local government pension scheme management expenses* (2016).
  - The net assets statement along with relevant notes have been amended to align with new investment classifications required by the accounting code.
  - An additional disclosure note (note 25a) covering remuneration of key management personnel has been included in related party transactions.
40. The publication also includes a disclosure checklist that identifies the accounting code's requirements in relation to pension funds.

## Other developments

### Housing benefit

#### Guidance on 2016/17 subsidy claims

41. The [Department for Work and Pensions](#) (DWP) has issued a letter and notes on completing the 2016/17 subsidy claim to provide guidance on the housing benefit (HB) subsidy claim for 2016/17.
42. The letter contains details of the amounts paid for 2016/17 in respect of administration subsidy and interim benefit subsidy received. The deadlines for receipt of the
  - pre-certified claim to the DWP and external auditors is 30 April 2017
  - the certified claim by the DWP is 30 November 2017.

#### 2016/17 HB COUNT modules

43. Public Sector Audit Appointments has issued the following modules of the 2016/17 HB COUNT approach
  - Module 2 contains a checklist to help auditors ensure that the authority's system is using the correct benefit parameters to calculate benefit entitlement and for the authority to claim the correct amount of subsidy.
  - Module 3 comprises workbooks to be completed for detailed testing, incorporating step-by-step guidance and a test result summary.

44. Module 1 has also been issued and provides an overview of the approach, but this is superseded in Scotland by guidance from the TSU.
45. For 2016/17, the key changes are to reflect DWP changes to the regulations and subsidy order, including reductions to both the benefit cap and the maximum period a claim can be backdated.
46. An e-learning package setting out the principles of the HB COUNT approach to the certification of HB subsidy claims for 2016/17 has also been issued.

### **2016/17 funding**

47. The DWP has issued HB circular [S2-2017 Final new burdens payment 2016/17 for the Real Time Information Bulk Data Matching initiative](#) to provide details of funding to help meet the costs incurred in implementing the *Real time information bulk data matching initiative* in 2016/17.

### **2017/18 uprating**

48. The DWP has issued HB circulars [A12/2016 Housing benefit: Uprating 2017/18](#) and [A1/2017 War pensions: uprating 2017/18](#) to advise of the benefits rates from April 2017.
49. A12/2016 contains specific advice for local authorities that apply percentage increases to uprate income from other social security benefits. As some of the rates have been uprated by different indices, authorities are required to consider whether applying standard percentages will result in correct determinations.

### **2017/18 administration subsidy**

50. The DWP has issued [HB circular S10/2016: 2017/18 Housing benefit administration subsidy arrangements for English, Scottish and Welsh local authorities](#) to provide details of the HB administration subsidy for Scottish local authorities for 2017/18.

## **Prudential framework**

### **Consultation on revising prudential code**

51. CIPFA has issued a [consultation paper](#) to seek views on whether the prudential code should be amended. The consultation paper includes questions on whether
  - the objectives of the prudential code are still relevant, and whether it achieves its objectives
  - the code's scope should be extended to cover arms-length external organisations and group entities
  - the code can be strengthened to encompass the risks related to increasing commercial activities and in respect of strategic planning elements
  - the indicators can be improved to enhance the assurance they provide.

52. Comments are required to be sent to [mandy.bretherton@cipfa.org](mailto:mandy.bretherton@cipfa.org) by 21 April 2017. CIPFA will then hold a further consultation on proposed changes to the code which are expected to apply from 2018/19.

## TSU contacts for local authority chapter

53. The contacts in the TSU for this chapter are
- Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or [pobrien@audit-scotland.gov.uk](mailto:pobrien@audit-scotland.gov.uk).
  - Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or [acairns@audit-scotland.gov.uk](mailto:acairns@audit-scotland.gov.uk) (for housing benefit).



# Central government chapter

## Introduction

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This chapter contains technical developments and guidance from the TSU on emerging risks that are relevant to the central government sector.

It should be read by external auditors with appointments in the central government sector. It should also be read by auditors with appointments in the health sector and further education sector as most of the articles also apply to those sectors. Auditors should also read the cross-sectoral chapter.

## Auditing developments

### Technical guidance notes

#### Auditing 2016/17 annual report and accounts

54. The TSU has published [Audit of 2016/17 annual report and accounts \(central government\) - technical guidance note 2017/1\(CG\)](#) to provide guidance to support auditors in planning and performing the audit of the 2016/17 central government annual report and accounts.
55. The technical guidance note comprises
  - an overview module including the financial reporting framework, key auditing standards, and presentation of financial statements
  - modules 1 to 5 on financial statement areas, e.g. property, plant and equipment, financial instruments, group financial statements
  - module 6 on the regularity of expenditure and income
  - module 7 on the performance report, governance statement, and remuneration and staff report. This module has been updated to provide guidance on
    - the new opinions referred to later at paragraph 62
    - applying the requirements of the FReM to Scottish bodies as a result of the FReM amendment referred to later at paragraph 68.
  - module 8 on charitable NDPBs.
56. The modules highlight the main risks of misstatement in each area, explain the correct treatment, and set out actions for auditors to assess whether the body has followed the required treatment. Following extensive consultation with all auditors, the technical guidance note represents an agreed position on a range of complex technical issues and is a key document as auditors plan and perform the audit of 2016/17 central government annual report and accounts.

57. For the purposes of the Audit Scotland website, all the modules have been combined into one document. The individual modules are also available from the relevant subject pages on the central government site of the *Technical reference library*. There is also a module containing a summary of the risks of misstatement available as a word document which auditors may use to satisfy themselves that their audit programmes adequately address the highlighted risks.
58. While auditors are responsible for their own conclusions and opinions, consistency in similar circumstances is important. Auditors should read the technical guidance note so they are familiar with the guidance provided. It is important that auditors follow the actions set out, subject to local judgements on materiality, to ensure that all auditors adopt a consistent approach to common risks.

### 2016/17 model independent auditor's reports

59. The TSU has issued [2016/17 Independent auditor's report \(central government\) - technical guidance note 2017/4\(CG\)](#) to provide auditors with the model independent auditor's reports which should be used for the 2016/17 annual report and accounts of central government bodies. The technical guidance note also provides application guidance on their use.
60. In the interests of consistency, auditors are required to use the relevant model report in appendices 1 to 5 of the technical guidance note as a condition of their audit appointment. The only exceptions to using the wording in each model are cases where there are group accounts or any amendments required to tailor the terminology to reflect local circumstances.
61. The models for 2016/17 are required to comply with *ISA (UK&I) 700 The independent auditor's report on financial statements*. This standard will be replaced from 2017/18 by the new *ISA (UK) 700 Forming and opinion and reporting on financial statements*, which contains a revised structure for the independent auditor's report. Although ISA (UK) 700 does not yet formally apply, the model reports for 2016/17 have been revised to follow the structure set out in that new standard, while also complying with the minimum requirements of ISA (UK&I) 700.
62. The models have also been revised to reflect the new reporting requirements for 2016/17 for auditors to express opinions on whether
  - the performance report has been properly prepared in accordance with the accounts direction
  - the governance statement is consistent with the financial statements and has been properly prepared in accordance with the accounts direction.
63. Any proposed modifications to any audit opinion or conclusion in the model reports, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with the TSU in advance of finalising the report.
64. Auditors should use this technical guidance note when reporting on 2016/17 audits. They should complete for each report the checklist at Appendix 6 which provides a list of the key auditor actions.

## 2016/17 GBS account information

65. The TSU will obtain information on account balances at 31 March 2017 for central government bodies from the Government Banking Service (GBS) and distribute them to relevant auditors.
66. The GBS has confirmed that the arrangements for obtaining 2016/17 account balances are unchanged.

## Accounting developments

### General accounting

#### Amendments to the 2016/17 FReM

67. [HM Treasury](#) has issued a revised version of the [2016/17 Government financial reporting manual](#) (the FReM).
68. The most significant change from the previous version is to paragraph 5.1.4 which has been expanded to clarify the application of FReM requirements to Scottish bodies. The format of accounts of Scottish bodies requires to be based on the principles, but not the detail, set out in chapter 5 of FReM. The clarification explains that the accounts of these bodies should meet disclosure requirements which originate in
  - accounting standards
  - Companies Act application as set out in the FReM
  - Scottish legislation
  - the *Scottish public finance manual* (SPFM).
69. Guidance on the impact of the clarification added to FReM paragraph 5.1.4 is provided in [technical guidance note 2017/1\(CG\)](#) (module 7) and is summarised as follows
  - The requirements in the FReM for disclosures in the remuneration and staff report on expenditure on consultancy and data on off-payroll arrangements do not apply to Scottish bodies.
  - There are a number of FReM disclosure requirements for the parliamentary accountability report that do not directly apply in Scotland, but are replaced by equivalent requirements in the SPFM, e.g. losses and special payments.
70. The requirement at FReM paragraph 5.3.25 for bodies to disclose information comparing the remuneration of the highest paid director with the median remuneration of the body's staff is not a Companies Act requirement, and there is no equivalent requirement in Scottish legislation or, currently, the SPFM. However, the Scottish Government has confirmed to Audit Scotland that they consider this disclosure should apply to Scottish bodies and has indicated that the SPFM will be amended or other guidance issued to reflect this requirement.
71. This is also the case for information on sickness absence.
72. Other amendments to the FReM are the following

- Paragraph 5.4.23 contains a new requirement for the notes on expenditure to include a brief summary of staff costs with a reference to the more detailed disclosures in the remuneration and staff report.
- Paragraph 5.4.22 has been added to emphasise that the notes to the accounts should include disclosures required under *IFRS 8 Operating segments*. This is in response to evidence of some bodies not complying with IFRS 8's requirements.

73. Auditors should ensure they refer to this revised version of the FReM, as interpreted by technical guidance note 2017/1(CG), when auditing the 2016/17 annual report and accounts.

### 2016/17 disclosure checklists

74. The [National Audit Office](#) (NAO) has issued the [2016/17 FReM disclosure guide for financial statements](#) which is designed to ensure that bodies covered by the FReM have prepared their 2016/17 annual report and accounts in the appropriate form and have complied with FReM disclosure requirements.
75. The guides are cross-referenced to the 2016/17 FReM, individual financial reporting standards, and the *Companies Act 2006*. Auditors will need to generate a tailored checklist by selecting the criteria that are material to their audited body.
76. While the guide is designed primarily for the NAO's internal use, auditors in Scotland may also find it helpful.
77. The NAO has also issued the *2016/17 FReM disclosure guide for annual reports*. The TSU has amended this guide for application to Scottish bodies in line with technical guidance note 2017/1(CG), and it is available from the *Technical reference library*. Auditors should ensure they use the amended guide rather than the NAO original which does not reflect Scottish requirements.

### 2017/18 FReM

78. Treasury has issued the [2017/18 FReM](#). It applies EU adopted IFRS and Interpretations in effect for accounting periods commencing on or after 1 January 2017.
79. There are no changes from the 2016/17 FReM.

## Remuneration and staff report

### Preparation guidance for 2016/17

80. The [Cabinet Office](#) has issued [EPN 492 2016/17 Disclosure of salary, pension and compensation information](#) to provide guidance on the preparation of the pay pension and compensation disclosures in remuneration and staff report for 2016/17. Example disclosures are provided at Annex 13C.
81. There are no significant changes to the remuneration disclosures set out for 2015/16. However, this guidance does not reflect the application of the FReM's requirements to Scottish bodies in line with FReM paragraph 5.1.4.

82. Page 1 of the annex provides a table setting out the single total figure of remuneration for each senior officer. Remuneration disclosures include
- information on the pay and pension packages of the senior management team
  - the median remuneration of all staff and the ratio between this and the mid-point of the banded remuneration of the highest paid director
  - the number of exit packages for all staff by cost band, broken down by the number of compulsory redundancies and the number of other departures agreed
  - compensation payments made to senior management.
83. The disclosure of the median remuneration of all staff and the ratio between this and the mid-point of the banded remuneration of the highest paid director is illustrated on page 3 of the annex.
84. The following disclosures required in respect of pensions are shown on page 5 of the annex
- Accrued pension and lump sum as at 31 March 2017 disclosed on £5,000 bands, which should be the pension that the individual would receive if that was their last day in service.
  - The real increase in pension and lump sum, i.e. the increase after considering inflation, in bands of £2500.
  - The cash equivalent transfer value (CETV) to the nearest £1,000, and the real increase in CETV that is funded by the employer.
85. Paragraph 13.1.11 provides guidance in cases where an officer is not in post for the whole year. Bodies should disclose the date of appointment for individuals appointed during the reporting year and the last day of service for those who left. Disclosures should only relate to the period during which they were in a post, but the full year equivalent of the salary should also be disclosed. An illustration is provided at paragraph 13.1.12.
86. Illustrative disclosure are also provided
- on page 8 of the annex for the number of exit packages for all staff by cost band, broken down by the number of compulsory redundancies and the number of other departures agreed. For staff who left under the voluntary terms, the cost to be used must include any top-up to compensation provided by the employer to buy out the actuarial reduction on an individual's pension
  - on page 7 in respect of compensation payments made to senior management.
87. Auditors should refer to this guidance when auditing the remuneration and staff report in the 2016/17 annual report and accounts.

## Provisions

### 2016/17 discount rates

88. HM Treasury has issued PES(2016)10 to announce the discount rate for post-employment benefits liabilities and general provisions as at 31 March 2017.

89. The discount rate for post employment benefits, including early departure provisions, will change from 1.37 % real to 0.24% real from 31 March 2017. The appropriate interest rate to be used in assessing interest costs of scheme liabilities for 2016/17 is 2.80%. The financial assumptions, based on market conditions, related to post employment benefit discount rates are set out in an annex. Funded schemes within central government should use a discount rate based on financial assumptions at 31 March each year, rather than these assumptions which are as at 30 November.
90. The real discount rates to be applied to provisions recognised in accordance with IAS 37 as at 31 March 2017 are as follows
- The short term rate (for cash-flows up to 5 years from the statement of financial position date) is minus 2.70%.
  - The medium term rate (between 5 and 10 years) is minus 1.95%.
  - The long term rate (more than 10 years) is minus 0.80%.
91. Auditors should refer to this paper when reviewing the discount rates applied to provisions in 2016/17 financial statements.

### Governance statement

92. The Scottish Government has issued a revised version of [On board - a guide to members of statutory boards](#) which provides information on the role of board members of public bodies in Scotland. The guidance applies to those appointed under statute to be members of the boards of public bodies.
93. The main changes are to extend the scope of the guide to cover most non-ministerial offices and public corporations as well as non departmental public bodies, and to reflect changes since the previous edition was published in 2015 such as the *Community Empowerment (Scotland) Act 2015*.

### Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action required by paragraph 58 in respect of technical guidance note 2017/1(CG)?			
2 Have you carried out the action required by paragraph 64 in respect of 2016/17 model independent auditor's reports?			
3 Have you carried out the action recommended at paragraph 73 in respect of the 2016/17 FReM?			

	Yes/No/N/A	Initials/date	W/P ref
4 Have you carried out the action recommended at paragraph 87 in respect of the remuneration and staff report?			
5 Have you carried out the action recommended at paragraph 91 in respect of 2016/17 discount rates?			

## TSU contacts for central government chapter

94. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or [ncameron@audit-scotland.gov.uk](mailto:ncameron@audit-scotland.gov.uk).
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or [hcobb@audit-scotland.gov.uk](mailto:hcobb@audit-scotland.gov.uk).

# Health chapter

## Introduction

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This chapter contains technical developments that are relevant to the health sector.

It should be read by external auditors with appointments in the health sector. Auditors should also read the central government sector and cross-sectoral chapter.

## Auditing developments

### Technical guidance notes

#### Auditing 2016/17 annual report and accounts

95. The TSU has published [Audit of 2016/17 annual report and accounts \(health\) - technical guidance note 2017/2\(H\)](#) to provide guidance to support guidance in planning and performing the audit of the 2016/17 health annual report and accounts.
96. The technical guidance note comprises
  - an overview module including the financial reporting framework, key auditing standards, and presentation of financial statements
  - modules 1 to 3 on financial statement areas, e.g. property, plant and equipment
  - module 4 on the regularity of expenditure and income
  - module 5 on the performance report, governance statement, and remuneration and staff report. This module has been updated to provide guidance on
    - the new opinions referred to later at paragraph 102
    - applying the requirements of the FReM to Scottish health boards as a result of the FReM amendment referred to at paragraph 68.
97. The modules highlight the main risks of misstatement in each area, explain the correct treatment, and set out actions for auditors to assess whether the board has followed the required treatment. Following extensive consultation with all auditors, the technical guidance note represents an agreed position on a range of complex technical issues and is a key document as auditors plan and perform the audit of 2016/17 health annual report and accounts.
98. For the purposes of the Audit Scotland website, all the modules have been combined into one document. The individual modules are also available from the relevant subject pages on the health site of the *Technical reference library*. There is also a module containing a summary of the risks of misstatement available as a word document which may be used as a checklist.
99. While auditors are responsible for their own conclusions and opinions, consistency in similar circumstances is important. Auditors should read the technical guidance note so they are



familiar with the guidance provided. It is important that auditors follow the actions set out, subject to local judgements on materiality, to ensure that all auditors adopt a consistent approach to common risks.

### 2016/17 model independent auditor's reports

100. The TSU has issued [2016/17 Independent auditor's report \(health\) - technical guidance note 2017/3\(H\)](#) to provide auditors with the model independent auditor's reports which should be used for the 2016/17 annual report and accounts of health boards. The technical guidance note also provides application guidance on their use.
101. In the interests of consistency, auditors are required to use the relevant model report in appendices 1 to 2 of the technical guidance note as a condition of their audit appointment. The only exception to using the wording in each model is to tailor the terminology to reflect local circumstances.
102. As for central government bodies, the model reports have been revised to
  - follow the structure set out in ISA (UK) 700
  - reflect the new opinions on the performance report and governance statement.
103. Any proposed modifications to any audit opinion or conclusion in the model reports, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with the TSU in advance of finalising the report.
104. Auditors should use this technical guidance note when reporting on 2016/17 audits. They should complete for each report the checklist at Appendix 3 which provides a list of the key auditor actions.
105. The technical guidance note also provides an assurance statement for the consolidation schedules at Appendix 4. Auditors should complete the auditor action checklist at Appendix 4.

### Review of central work on CNORIS

106. The TSU is currently undertaking a review of the work carried out by the NHS Central Legal Office (CLO) relating to the *Clinical negligence and other risks indemnity scheme* (CNORIS). The objective of the review is to establish the extent to which the information prepared using the work of the CLO, as a management expert under *ISA (UK&I) 500 Audit evidence*, can be used as audit evidence.
107. The TSU will also evaluate the appropriateness of the methodology adopted by the Scottish Government to establish the total national liability for CNORIS. The review will focus on the estimation of the liability as at 31 March 2017.
108. The TSU will then provide auditors with the outcome of the reviews to
  - inform auditors' evaluation of the relevance and reliability of the information prepared by the CLO as audit evidence

- provide assurance on the methodology used in the preparation of the CNORIS figures as at 31 March 2017 which are provided by the Scottish Government to NHS boards.

## Accounting developments

### General accounting

#### 2016/17 accounts manual

109. The Scottish Government Health and Social Care Directorates (SGHSCD) has issued the *2016/17 NHS board manual for annual report and accounts* to complement the guidance contained in the 2016/17 FReM. An initial version issued in December 2016 has been replaced by an updated version which reflects the changes in the revised version of the FReM.
110. The main changes included in the updated version of the accounts manual compared with 2015/16 are summarised in the following paragraphs. Auditors should refer to this manual when auditing health boards' 2016/17 annual report and accounts.

#### Foreword

111. Paragraph 1 has been amended to clarify that the accounts manual does not supersede the FReM, and that boards are responsible for ensuring that their accounts are compliant with the requirements of the FReM.

#### Financial statements

112. The covering letter that accompanies the revised accounts manual
- clarifies that the title of the statement of comprehensive net expenditure should not include reference to the summary of resource outturn (SoRO), and the SoRO should not be described as a statement
  - advises the term net expenditure, rather than net operating costs, should be used in the annual accounts.
113. The covering letter also provides a form of words to be used in the note on pension cost disclosures.

#### Performance report

114. Pages 10 and 11 have been amended as a result of disclosures being moved from the accountability report to the performance analysis section of the performance report. The disclosures are
- performance against the Scottish Government payment policy target
  - pension liabilities
  - details of events after the reporting period.

### Remuneration and staff report

115. The table on page 26 covering the fair pay disclosure has been amended to include the range of staff remuneration required by FReM paragraph 5.3.25.
116. The staff report on pages 27 to 33 has been amended to
- include the higher paid employees and staff costs disclosure previously included at note 2
  - remove the requirements to disclose information on off payroll arrangements and expenditure on consultancy.

### Parliamentary accountability report

117. Pages 31 and 32 have been amended to reflect the requirement for a parliamentary accountability report to be included in the accountability report. The parliamentary accountability report should include the disclosures required by the SPFM.

## Property, plant and equipment

### 2016/17 capital accounting manual

118. The SGHSCD has issued the *2016/17 NHS capital accounting manual (CAM)* to interpret the accounting guidance contained in the 2016/17 FReM on capital accounting issues in the NHS.
119. There are no significant changes from the 2015/16 CAM.
120. Auditors should refer to the CAM when auditing property, plant and equipment in 2016/17 annual report and accounts.

## Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 99 in respect of technical guidance note 2017/2(H)?			
2 Have you carried out the action required by paragraph 104 in respect of 2016/17 model independent auditor's reports?			
3 Have you carried out the action recommended at paragraph 110 in respect of the 2016/17 NHS board manual for annual report and accounts?			
4 Have you carried out the action recommended at paragraph 120 in respect of the 2016/17 capital accounting manual?			

## TSU contact for health chapter

121. The contact in the TSU for this chapter is Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or [ncameron@audit-scotland.gov.uk](mailto:ncameron@audit-scotland.gov.uk).

# Fraud and irregularities

## Introduction

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This chapter contains a summary of fraud cases and other irregularities arising at audited bodies that have recently been reported by auditors to the TSU.

Auditors should consider whether the weaknesses in internal control that facilitated each fraud may apply at their audited bodies and take the appropriate action.

## Expenditure and income

122. An administrative assistant employed in a council criminal justice service embezzled £5,000 over a seven year period.

### Key features

The perpetrator

- submitted false expense claims for the valeting of council vehicles
- failed to bank cash income
- requested cash advances in addition to the petty cash float.

The fraud was possible as

- the employee had sole control of the petty cash
- team managers did not have access to the ledger to allow them to identify discrepancies in their budgets
- the employee intimidated other employees to sign blank expense claims which she then authorised without supporting receipts.

The fraud was identified when internal audit followed up concerns raised by a whistle-blower.

The employee was prosecuted and received a community payback order. All criminal justice staff have since received financial training, and team managers now have access to the ledger to allow them to monitor their budgets.

## TSU contact for fraud and irregularities chapter

123. The contact in the TSU for this chapter is Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or [acairns@audit-scotland.gov.uk](mailto:acairns@audit-scotland.gov.uk).

# Technical Services Unit

Audit Scotland's Technical Services Unit (TSU) informs the professional judgement of appointed external auditors on technical matters and encourages the proper exercise of professional scepticism to improve the quality of the audit delivered to the Accounts Commission and Auditor General for Scotland. The TSU provides authoritative guidance and practical assistance to support appointed auditors in carrying out their responsibilities under the *Code of audit practice* to

- provide an opinion on audited bodies' financial statements and, where required, the regularity of transactions
- review and report on other information published with the financial statements, including governance statements and remuneration reports
- examine and report on approved grant claims and other returns submitted by local authorities
- review and report on whole of government accounts returns.

Contact details for relevant TSU staff are included at the end of each chapter.

**Feedback on technical bulletins is encouraged and should be sent to**

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**16 March 2017**