

South of Scotland Enterprise

Annual Audit Plan 2021/22



 AUDIT SCOTLAND

Prepared for South of Scotland Enterprise

February 2022

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Introduction

Summary of planned audit work

1. This document summarises the work plan for our 2021/22 external audit of South of Scotland Enterprise (SOSE). The main elements of our work include:

- evaluation of the key controls within the main accounting systems
- an audit of, and provision of an Independent Auditor's Report
- an audit opinion on regularity and other statutory information published within the annual report and accounts including the Performance Report, the Governance Statement and the Remuneration and Staff Report
- consideration of arrangements in relation to the audit dimensions that frame the wider scope of public sector audit: financial management, financial sustainability, governance and transparency and value for money.

Impact of Covid-19

2. The coronavirus disease (Covid-19) pandemic has had a significant impact on public services and public finances, and the effects will be felt well into the future.

3. Audit Scotland continues to assess the risks to public services and finances from Covid-19 across the full range of our audit work, including annual audits and the programme of performance audits. The well-being of audit teams and the delivery of high-quality audits remain paramount. Changes in our approach may be necessary and where this impacts on annual audits, revisions to this annual audit plan may be required.

Adding value

4. We aim to add value to SOSE through our external audit by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. In so doing, we will help SOSE promote improved standards of governance, better management and decision-making and more effective use of resources. Additionally, we attend meetings of the Audit and Risk Committee (ARC) and actively participate in discussions.

Respective responsibilities of the auditor and SOSE

5. The [Code of Audit Practice \(2016\)](#) sets out in detail the respective responsibilities of the auditor and the organisations we audit. Key responsibilities are summarised below.

Auditor responsibilities

6. Our responsibilities as independent auditors are established by the Public Finance and Accountability (Scotland) Act 2000 and the [Code of Audit Practice](#) (including [supplementary guidance](#)) and guided by the Financial Reporting Council's Ethical Standard.

7. Auditors in the public sector give an independent opinion on the financial statements and other information within the annual report and accounts. We also review and report on the arrangements within the body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

SOSE responsibilities

8. SOSE is responsible for maintaining accounting records and preparing financial statements that give a true and fair view.

9. Also, SOSE has the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable SOSE to deliver its objectives.

Managing the transition to 2022/23 audits

10. Audit appointments are usually for five years but were extended to six years due to Covid-19. 2021/22 is the final year of the current appointment and we will work closely with our successors to ensure a well-managed transition.

Financial statements audit planning

Materiality

11. Materiality is an expression of the relative significance of a matter in the context of the financial statements as a whole. We are required to plan our audit to determine with reasonable confidence whether the financial statements are free from material misstatement. The assessment of what is material is a matter of professional judgement over both the amount and the nature of the matter arising.

Materiality levels for the 2021/22 audit

12. We assess materiality at different levels as described in [Exhibit 1](#). The materiality values for SOSE are set out in [Exhibit 1](#).

Exhibit 1 2021/22 Materiality levels for SOSE

Materiality	Amount
Planning materiality – This is the figure we calculate to assess the overall impact of audit adjustments on the financial statements. It has been set at 1 per cent of gross expenditure for the year ended 31 March 2022 based on the latest financial forecasts.	£0.326 million
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality, this would indicate that further audit procedures should be considered. Using our professional judgement, we have assessed performance materiality at 60 per cent of planning materiality.	£0.196 million
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount.	£16,000

Source: Audit Scotland

Significant risks of material misstatement to the financial statements

13. Our risk assessment draws on our cumulative knowledge of SOSE, its major transaction streams, key systems of internal control and risk management

processes. Also, it is informed by our discussions with management, meetings with internal audit, attendance at committees and a review of supporting information.

14. Based on our risk assessment process, we identified the following significant risks of material misstatement to the financial statements. These are risks which have the greatest impact on our planned audit procedures. [Exhibit 2](#) summarises the nature of the risk, the sources of assurance from management arrangements and the further audit procedures we plan to perform to gain assurance over the risk.

Exhibit 2

2021/22 Significant risks of material misstatement to the financial statements

Significant risk of material misstatement	Sources of assurance	Planned audit response
<p>1. Risk of material misstatement due to fraud caused by the management override of controls</p> <p>As stated in International Standard on Auditing (UK) 240, management is in a unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance</p>	<ul style="list-style-type: none"> • Assess the design and implementation of controls over journal entry processing. • Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments. • Test journals at the year-end and post-closing entries and focus on significant risk areas. • Consider the need to test journal entries and other adjustments during the period. • Evaluate significant transactions outside the normal course of business. • Assess the adequacy of controls in place for identifying and disclosing related party relationship and transactions in the financial statements. • We will assess any changes to the methods and underlying assumptions used to prepare accounting estimates compared to the prior year. • Substantive testing of income and expenditure transactions around the year-end to confirm they are accounted for in the correct financial year.

Significant risk of material misstatement	Sources of assurance	Planned audit response
<p>2. Risk of material misstatement due to fraud over expenditure under ISA 240</p> <p>As most public-sector bodies are net spending bodies, the risk of fraud is more likely to occur in expenditure than income. A significant proportion of SOSE's expenditure (currently forecast to be £20.6 million in 2021/22 representing 63 per cent of total spend) is on business support grants, some of which are specifically to address the impact of Covid-19.</p> <p>As SOSE continues to establish itself, it also continues to develop its controls in relation to the payment of grants. While these controls are being fully embedded there remains a risk of fraud which could result in material misstatement.</p>	<ul style="list-style-type: none"> • The Delegation of Authority is in place to control the approval process of invoices and payments • 14 employees including one director attended a live online training course, over 16 hours, on CIPFA Fraud Awareness and Investigations • All new employees complete Counter Fraud, Bribery and Corruption training on the Learning Platform for Government • SOSE's Counter Fraud Policy is available on the hub 	<ul style="list-style-type: none"> • Focussed testing of accounting accruals and prepayments. • Review SOSE's anti-fraud arrangements. • Walkthrough testing of the key controls in the grant approval process. • Substantively test a sample of grant payments. • Substantively test a sample of grant payments to ensure expenditure is recognised in the correct financial year. • Review the internal audit report on operational activities.
<p>3. Estimates and judgements: valuation of land and buildings.</p> <p>SOSE owns a portfolio of property assets. At 31 March 2021 these were valued at £2.261 million. SOSE's policy of triennial valuations complies with the relevant standard (IAS 16).</p> <p>An overriding aspect of IAS 16 is that assets valuations are kept under review.</p>	<ul style="list-style-type: none"> • SOSE's Property Board meet on a monthly basis, on 18 February 2022 the Board discussed Impairment of Assets. Senior Management agreed that assets should be formally valued at 31 March 2022, procurement are working to engage a Valuer for year-end. 	<ul style="list-style-type: none"> • Assess the approach SOSE has adopted for the valuation of land and buildings. • Assess SOSE's assumptions for the valuation of land and buildings and the adequacy of the disclosures in its financial statements. • Completion of 'review of the work of an expert' in respect of the property valuer. • Test the reconciliation between the financial ledger and the property asset register to ensure that any in-

Significant risk of material misstatement	Sources of assurance	Planned audit response
<p>Given the next valuation is not due until 2023, SOSE must assure itself that any in-year changes in the property market do not result in material changes to the asset valuation. Without this review, there is a risk that carrying value of land and buildings may be materially misstated.</p>		<p>year valuation movements are correctly accounted for.</p>
<p>4. Estimates and judgements: valuation of retirement benefit obligations.</p> <p>SOSE is a member of the Scottish Borders Council pension fund (i.e. the local government pension scheme) and accounts for it under the relevant accounting standard (IAS 19). At 31 March 2021 the obligation was £2.281 million.</p> <p>The present value of the retirement (pension) obligations depends on a number of factors that are determined on an actuarial basis underpinned by a series of assumptions.</p> <p>There is a risk that errors in the information provided to the actuary or in the underlying assumptions, or late information, can result in a material misstatement.</p>	<ul style="list-style-type: none"> • The work of Hymans Robertson, SOSE's independent actuary, will provide the basis for the pension liability estimate. 	<ul style="list-style-type: none"> • Review of information provided by SOSE to its actuary. • Completion of 'review of the work of an expert' in respect of the actuary including a review of actuarial assumptions. • Review evidence confirming that SOSE management has assessed the estimate provided by its actuary. • Testing of pension disclosures in the financial statements, including disclosures in the key estimates and judgements note.
<p>5. Business support loans</p> <p>During 2021/22 SOSE began offering business loans, These loans (forecast to be £2.5 million) are funded from the Financial Transactions (FT)</p>	<ul style="list-style-type: none"> • SOSE will provide details on the loan process and accounting transactions before 31st March 2022 to agree process with AS. 	<ul style="list-style-type: none"> • Review arrangements in place to award loans to businesses and compliance with the conditions are met. • Substantively test the loans awarded in year to ensure they comply with policies and procedures.

Significant risk of material misstatement	Sources of assurance	Planned audit response
<p>funding from the Scottish Government.</p> <p>There is a risk that the accounting requirements for FT transactions are not followed and that the financial statements are materially misstated as a result.</p>		<ul style="list-style-type: none"> • Ensure the accounting and disclosures in the financial statements are in accordance with the requirements.

Source: Audit Scotland

15. As set out in International Standard on Auditing (UK) 240: *The auditor's responsibilities relating to fraud in an audit of financial statement*, there is a presumed risk of fraud over the recognition of revenue. There is a risk that revenue may be misstated resulting in a material misstatement in the financial statements. We have rebutted this risk for SOSE because almost all of SOSE's income is through Scottish Government funding which presents a low risk of fraud. SOSE also receives a material amounts from rental properties which is managed by a landlord. Given this arrangement and related controls we have assessed this as a low risk of fraud.

16. We have not, therefore, incorporated specific work into our audit plan in this area over and above our standard audit procedures.

Other areas of audit focus

17. As part of our assessment of audit risks, we have identified other areas where we consider there are also risks of material misstatement to the financial statements. Based on our assessment of the likelihood and magnitude of the risk, we do not consider these to represent significant risks. We will keep these areas under review as our audit progresses. If our assessment of risk changes and we consider these risks to be significant, we will communicate this to management and those charged with governance and revise our planned audit approach accordingly.

18. The areas of specific audit focus are:

- **Accruals:** By their nature, accruals involve a degree of estimation. As such there is a level of uncertainty attached to these balances. At 31 March 2021, SOSE held accrual balances of £0.4 million which is material. These typically involve balances in relation to grants and the employee leave accrual.

Audit risk assessment process

19. Audit risk assessment is an iterative and dynamic process. Our assessment of risks set out in this plan may change as more information and evidence

becomes available during the progress of the audit. Where such changes occur, we will advise management and where relevant, report them to those charged with governance.

Audit dimensions and Best Value

Introduction

20. The [Code of Audit Practice](#) sets out the four dimensions that frame the wider scope of public sector audit. The Code of Audit Practice requires auditors to consider the adequacy of the arrangements in place for the audit dimensions in audited bodies.

Audit dimensions

21. The four dimensions that frame our audit work are shown in [Exhibit 3](#).

Exhibit 3

Audit dimensions



Source: Code of Audit Practice

22. In summary, the four dimensions cover the following:

- **Financial management** – financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.
- **Financial sustainability** – as auditors, we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on financial sustainability in the longer term.

We define this as medium term (two to five years) and longer term (longer than five years).

- **Governance and transparency** – governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership, and decision-making and transparent reporting of financial and performance information.
- **Value for money** – value for money refers to using resources effectively and continually improving services.

Duty of Best Value

23. [Ministerial Guidance to Accountable Officers](#) for public bodies and the [Scottish Public Finance Manual](#) (SPFM) explain that accountable officers have a specific responsibility to ensure that arrangements have been made to secure Best Value. We will be carrying out a high-level review to confirm that such arrangements are in place within SOSE.

24. This work will involve monitoring the progress which SOSE has made to implement a framework for Best Value which we referred to in our annual audit report in 2020/21. Additionally, as part our work in this area, we will be carrying out a review of the Best Value characteristic “fairness and equality” within SOSE.

Audit dimension risks

25. We have not identified audit risks in the areas set out in [Exhibit 3](#). There are though some areas of interest which we shall cover during 2021/22, see below:

- Follow-up on 2020/21 recommendations regarding:
 - The need for SOSE to periodically review its governance arrangements (governance and transparency)
 - The development of a performance management framework to ensure that SOSE can demonstrate its contribution to national priorities (value for money).
- Cyber security – review developments in this area through updates provided to the ARC and relevant internal audit reports.
- Consider whether the arrangements for the prevention and detection of fraud and corruption in the procurement function are effective and appropriate. This is in context of the [‘Red Flags in Procurement’](#) document produced by Audit Scotland in October 2019.

Reporting arrangements, timetable, and audit fee

Reporting arrangements

26. Audit reporting is the visible output for the annual audit. All Annual Audit Plans and the outputs, as detailed in [Exhibit 4](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

27. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

28. We will provide an independent auditor's report to SOSE, the Scottish Parliament and the Auditor General for Scotland setting out our opinions on the annual report and accounts. We will provide the SOSE and the Auditor General for Scotland with an annual report on the audit containing observations and recommendations on significant matters which have arisen during the audit.

29. [Exhibit 4](#) outlines the target dates for our audit outputs. We acknowledge this will be challenging due to the ongoing pressures and uncertainties caused by Covid-19.

Exhibit 4 2020/21 Audit outputs

Audit Output	Target date	Audit and Risk Committee Date
Annual Audit Plan	23 February 2022	2 March 2022
Independent Auditor's Report	TBC	TBC
Annual Audit Report	TBC	TBC

Source: Audit Scotland



Timetable

30. To support an efficient audit, it is critical that the timetable for producing the annual report and accounts for audit is achieved. We have included a proposed timetable for the audit at [Exhibit 5](#) that has been discussed with management.

31. Covid-19 has had a considerable impact on the conduct and timeliness of the audit. We recognise that it is in the best interests of public accountability to get the reporting of audited accounts back to pre-pandemic timelines. To this end, 2021/22 is a transition year with the reporting deadline brought forward by one month relative to the two prior years. We are identifying ways to work more efficiently to expedite the 2021/22 audits whilst maintaining high standards of quality.

32. We will continue to work in close partnership with management with clarity over timescales and the requirement for high quality unaudited accounts and supporting working papers. Progress will be discussed with management and finance officers over the course of the audit.

Exhibit 5 Proposed annual report and accounts timetable

 Key stage	 Provisional Date
Consideration of the unaudited annual report and accounts by those charged with governance	24 May 2022
Latest submission date for the receipt of the unaudited annual report and accounts with complete working papers package.	25 May 2022
Latest date for final clearance meeting with the Director of Finance (or equivalent)	24 June 2022
Issue of Letter of Representation and proposed Independent Auditor's Report	27 July 2022
Agreement of audited and unsigned annual report and accounts	27 July 2022
Issue of Annual Audit Report to those charged with governance.	27 July 2022
Signed Independent Auditor's Report	TBC

Source: Audit Scotland

Audit fee

33. The proposed audit fee for the 2021/22 audit of SOSE is £TBC (2020/21: £95,000). In determining the audit fee, we have taken account of the risk exposure of the body, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit.

34. Where our audit cannot proceed as planned through, for example, late receipt of unaudited annual report and accounts, the absence of adequate supporting working papers or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required

in relation to any work or other significant exercises out with our planned audit activity.

Other matters

Internal audit

35. International standards on Auditing (UK) 610: *Considering the work of internal audit* requires us to:

- consider the activities of internal audit and their effect on external audit procedures;
- obtain an understanding of internal audit activities to inform our planning and develop an effective audit approach that avoids duplication of effort;
- perform a preliminary assessment of the internal audit function when there is scope for relying on internal audit work which is relevant to our financial statements' responsibilities; and
- evaluate and test the work of internal audit, where use is made of that work for our financial statements responsibilities to confirm its adequacy for our purposes.

36. From our initial review of the internal audit plans, we do not plan to place formal reliance on internal audit's work for our financial statements' responsibilities. We do plan to consider the findings of Internal Audit across a range of work including:

- Financial Management
- Operational Activities
- Performance Measurement
- IT Partnership Audit - Cyber Security Follow Up

Independence and objectivity

37. Auditors appointed by the Auditor General for Scotland or Accounts Commission must comply with the [Code of Audit Practice](#) and relevant supporting guidance. When auditing the financial statements, auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual *'fit and proper'* declaration for all members of staff. The arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland's Ethics Partner.

38. The engagement lead (i.e. appointed auditor) for SOSE is currently Gordon Smail, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of SOSE.

Quality control

39. International Standard on Quality Control (UK) 1 (ISQC1) requires a system of quality control to be established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

40. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the [Code of Audit Practice](#) (and supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards, Audit Scotland conducts peer reviews and internal quality reviews. Additionally, the Institute of Chartered Accountants of Scotland (ICAS) have been commissioned to carry out external quality reviews.

41. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time, and this may be directed to the engagement lead.

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Audit Scotland's published material is available for download on the website in a number of formats. For information on our accessibility principles, please visit:

www.audit-scotland.gov.uk/accessibility

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