

South of Scotland Enterprise

2022/23 Annual Audit Report



 AUDIT SCOTLAND

Prepared for the South of Scotland Enterprise and the Auditor General for Scotland

August 2023

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Key messages

2022/23 annual report and accounts

- 1 Audit opinions on the annual report and accounts are unmodified, i.e. the financial statements and related reports are free from material misstatement.
- 2 Improvements are required to the processes in place around evidencing the approval of grants and monitoring of grant conditions.
- 3 Two reclassification adjustments totalling £1.8 million were made to the annual report and accounts. These adjustments had no impact on the net position reported in the Statement of Comprehensive Net Expenditure or Statement of Financial Position.

Financial management and sustainability

- 4 South of Scotland Enterprise operated within its revised fiscal resources, reporting an underspend of £2.41 million, which was mainly due to low demand for financial transactions.
- 5 Budget processes were appropriate, with regular updates to the Board on in-year budget revisions.
- 6 There is scope for enhancing some financial systems of internal control.

Vision, leadership and governance

- 7 South of Scotland Enterprise has clear plans in place to implement its vision, strategy, and priorities.
- 8 Governance arrangements are appropriate, and South of Scotland Enterprise has finalised and published its framework document with the Scottish Government.
- 9 South of Scotland Enterprise has made progress with climate change arrangements but more has to be done to establish and monitor targets.
- 10 Cyber security arrangements appear appropriate.

Use of resources to improve outcomes

- 11 South of Scotland Enterprise should further develop its approach to demonstrating Best Value.

- 12** South of Scotland Enterprise has developed a new performance measurement framework, but specific targets should be set for 2023/24 onwards to assess progress.

Introduction

1. This report summarises the findings from the 2022/23 annual audit of the South of Scotland Enterprise (SOSE). The scope of the audit was set out in our Annual Audit Plan shared with members of the Audit and Risk Committee in March 2023. This Annual Audit Report comprises:

- significant matters arising from an audit of SOSE’s annual report and accounts
- conclusions on the following wider scope areas that frame public audit as set out in the [Code of Audit Practice 2021](#):
 - Financial Management
 - Financial Sustainability
 - Vision, Leadership, and Governance
 - Use of Resources to Improve Outcomes.

2. This report is addressed to the Audit and Risk Committee of South of Scotland Enterprise and the Auditor General for Scotland and will be published on Audit Scotland's website www.audit-scotland.gov.uk in due course.

Audit appointment from 2022/23

3. I, Pauline Gillen, have been appointed by the Auditor General as auditor of SOSE for the period from 2022/23 until 2026/27. The 2022/23 financial year was the first of this five-year appointment. My appointment coincides with the new [Code of Audit Practice](#) which was introduced for financial years commencing on or after 1 April 2022.

4. My team and I would like to thank Audit and Risk Committee members, executive directors, and other staff, particularly those in finance, for their cooperation and assistance in this year and we look forward to working together constructively over the course of the five-year appointment.

Responsibilities and reporting

5. SOSE has primary responsibility for ensuring the proper financial stewardship of public funds. This includes preparing an annual report and accounts that are in accordance with the account's direction from the Scottish Ministers. SOSE is also responsible for establishing appropriate and effective arrangements for governance, propriety, and regularity.

6. The responsibilities of the independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the [Code of Audit Practice](#)

[2021](#), and supplementary guidance and International Standards on Auditing in the UK.

7. Weaknesses or risks identified are only those which have come to our attention during our normal audit work and may not be all that exist. Communicating these does not absolve management of SOSE from its responsibility to address the issues we raise and to maintain adequate systems of control.

8. This report contains an agreed action plan at [Appendix 1](#). It sets out specific recommendations, the responsible officers, and dates for implementation.

Auditor Independence

9. We can confirm that we comply with the Financial Reporting Council's Ethical Standard. We can also confirm that we have not undertaken any non-audit related services. We are not aware of any relationships that could compromise our objectivity and independence.

10. The Annual Audit Plan set out an audit free of £110,720 for the 2022/23 audit. However, a rebate of £8,523 was issued, relating to previous years' audit fees, resulting in a final audit fee of £102,197.

11. We add value to SOSE by:

- identifying and providing insight on significant risks, and making clear and relevant recommendations,
- providing clear and focused conclusions on the appropriateness, effectiveness and impact of corporate governance, arrangements to ensure the best use of resources and financial sustainability, and
- sharing intelligence and good practice identified.

1. Audit of 2022/23 annual report and accounts

Public bodies are required to prepare annual reports and accounts comprising financial statements and other related reports. These are principal means of accounting for the stewardship public funds.

Main judgements

Audit opinions on the annual report and accounts are unmodified.

Improvements are required to the processes in place around evidencing the approval of grants and monitoring of grant conditions.

Two reclassification adjustments totalling £1.8 million were made to the annual report and accounts. These adjustments had no impact on the net position reported in the Statement of Comprehensive Net Expenditure or Statement of Financial Position.

Audit opinions on the annual report and accounts are unmodified

12. The Board approved the annual report and accounts for SOSE for the year ended 31 March 2023 on 17th August 2023. As reported in the independent auditor's report, in my opinion as the appointed auditor:

- the financial statements give a true and fair view and were properly prepared in accordance with the financial reporting framework,
- expenditure and income were in accordance with applicable enactments and guidance,
- the audited part of the Remuneration and Staff Report was prepared in accordance with the financial reporting framework, and
- the Performance Report and Governance Statement were consistent with the financial statements and properly prepared in accordance with the relevant legislation and directions made by Scottish Ministers.

Overall materiality was assessed as £0.57 million

13. Broadly, the concept of materiality is applied by auditors to determine whether misstatements identified during the audit could reasonably be expected to influence the economic decisions of users of the financial statements, and hence impact their opinion set out in the independent auditor's report. Auditors

set a monetary threshold when considering materiality, although some issues may be considered material by their nature. It is ultimately a matter of the auditor's professional judgement.

14. Our initial assessment of materiality was carried out during the risk assessment and planning phase of the audit. This was reviewed and revised on receipt of the unaudited annual report and accounts and is summarised in [Exhibit 1](#).

Exhibit 1

Materiality values

Materiality level	Amount
Overall materiality	£0.57 million
Performance materiality	£0.34 million
Reporting threshold	£30,000

15. The overall materiality threshold was set with reference to gross expenditure, which we judged as the figure most relevant to the users of the financial statements.

16. Performance materiality is used by auditors when undertaking work on individual areas of the financial statements. It is a lower materiality threshold, set to reduce the probability of aggregated misstatements exceeding overall materiality. Performance materiality was set at 60% of overall materiality, reflecting a small number of errors identified in the previous year's audit and the level of estimation and judgement in the valuation of key accounts areas (land and buildings within non-current assets and the retirement benefit obligation).

17. It is our responsibility to request that all misstatements, other than those below our reporting threshold, are corrected, although the final decision on making the correction lies with those charged with governance.

Significant findings and key audit matters

18. Under International Standard on Auditing (UK) 260, we communicate significant findings from the audit to those charged with governance, including our view about the qualitative aspects of SOSE's accounting practices.

19. The Code of Audit Practice also requires all audits to communicate key audit matters within the Annual Audit Report under International Standard on Auditing (UK) 701. These are matters that we judged to be of most significance in our audit of the financial statements.

20. The significant findings and key audit matters from the audit are summarised in [Exhibit 2](#).

Exhibit 2

Significant findings and key audit matters from the audit of the annual report and accounts

Issue	Resolution
<p>1. Grant award process and monitoring</p> <p>Grant awards to businesses are a key element of SOSE's operations. While our substantive testing of grants did not identify any misstatements (see Exhibit 3, risk 2), improvements can be made to the processes in place around evidencing the approval of grants and subsequent monitoring of grant conditions and whether these are being met by recipients.</p> <p>Our audit testing in 2022/23 did not identify any instances of grants being inappropriately awarded. However, gaps in these processes could result in SOSE being unable to demonstrate that all conditions were met before a grant was awarded and grants not being reclaimed in instances where recipients do not meet any grant conditions after their initial approval.</p>	<p>Management have advised that guidance and templates are being created to ensure all grant awards can be evidenced in a consistent manner, and this will be issued to all staff involved in the grant award process.</p> <p>Recommendation 1</p> <p>(Refer Appendix 1, action plan)</p>

Our audit work responded to the risks of material misstatement we identified in the annual report and accounts

21. We have obtained audit assurances over the identified significant risks of material misstatement in the annual report and accounts. [Exhibit 3](#) sets out the significant risks of material misstatement to the financial statements we identified in our 2022/23 Annual Audit Plan. It also summarises the further audit procedures we performed during the year to obtain assurances over these risks and the conclusions from the work completed.

Exhibit 3

Significant risks of material misstatement in the annual report and accounts

Audit risk	Assurance procedure	Results and conclusions
<p>1. Risk of material misstatement due to fraud caused by management override of controls</p> <p>As stated in International Standard on Auditing (UK) 240, management is in a</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 	<p>Results: Work undertaken included detailed testing of journal entries, accruals, prepayments and invoices; as well as review of accounting estimates and transactions for appropriateness. Specific enquiries were made of</p>

Audit risk	Assurance procedure	Results and conclusions
<p>unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively.</p>	<p>about inappropriate or unusual activity.</p> <ul style="list-style-type: none"> • Test journals at the year-end and post-closing entries and focus on significant risk areas. • Evaluate significant transactions outside the normal course of business. • Assess the adequacy of controls in place for identifying and disclosing related party relationships 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. • Focussed testing of accounting accruals and prepayments. 	<p>individual staff as to whether they had knowledge or awareness of manipulation of financial recording or processing of fraudulent journals.</p> <p>Conclusion: No incidents of management override of controls were identified.</p>
<p>2. Risk of material misstatement caused by fraud and error in capital grants expenditure.</p> <p>Practice Note 10 extends the requirements of ISA 240 to include consideration of fraud in expenditure for public bodies. A significant proportion of South of Scotland Enterprise's expenditure is on project expenditure (£16.7 million in 2021/22) which includes capital grant payments.</p> <p>Audit testing in 2021/22 identified two grant payments</p>	<ul style="list-style-type: none"> • Walkthrough testing of the key controls in the grant approval process. • Substantively test a sample of grant payments to ensure expenditure is recognised in the correct financial year. 	<p>Results: Substantive testing of grant payments found expenditure was recognised in the correct year and payments were supported by appropriate supporting documentation.</p> <p>However, our substantive testing identified deficiencies in processes in place around evidencing the approval of grants and subsequent monitoring of grant conditions and whether these are being met by recipients. This is outlined in more detail in Exhibit 2.</p>

Audit risk	Assurance procedure	Results and conclusions
<p>which were made without appropriate supporting evidence. While improved controls are being fully embedded there remains a risk of fraud which could result in a material misstatement.</p>		

22. In addition, we identified “areas of audit focus” in our 2022/23 Annual Audit Plan where we considered there to be risks of material misstatement to the financial statements. These areas of specific audit focus were:

- Estimations in valuation of land and buildings:** we identified that land and buildings were not revalued in year. SOSE values land and buildings on a triennial basis, with the last valuation carried out in 2021/22. We assessed if there was a possibility that the carrying value of land and buildings could be materially different to their current value and concluded there was unlikely to be a material difference.
- Estimations in valuation of pension assets and liabilities:** we assessed the design and implementation of controls over the valuation of pensions. We carried out ‘reliance on a management expert’ work on the actuary. Based on the findings of the audit procedures performed we concluded that we could place reliance on the actuary’s valuation of the pension liability. We reviewed the pension adjustments throughout the financial statements and identified an issue with how service costs had been processed. Service costs had been split over two lines in the SOCNE but have now been adjusted to sit within one line. After this was corrected, we confirmed that pension adjustments had been accurately processed.
- IFRS 16:** we obtained an understanding of the process in place to implement the requirements of IFRS 16 and we reviewed the transactions processed through the annual report and accounts to account for the requirements. This included reviewing existing leases that were brought into IFRS 16 and any new leases. No issues were identified with the implementation and application of IFRS 16. However, we did identify one instance of a potential sub-lease arrangement that SOSE should look to clarify and reflect in the 2023/24 annual report and accounts if required.
- Implementation of a new payroll system:** we obtained an understanding of the of the implementation process, including data migration between the old and new systems and testing undertaken by the Skills Development Scotland audit team. Further audit procedures were also carried out to obtain assurance over the completeness and

accuracy of the payroll data. No issues were identified from the testing of the new payroll system.

23. Based on the findings of the audit procedures performed, there are no matters which we need to bring to your attention other than those already outlined in [Exhibit 2](#).

Two reclassification adjustments totalling £1.8 million were made to the annual report and accounts

24. It is our responsibility to request that all misstatements, other than those below our reporting threshold are corrected. However, the final decision on making corrections lies with those charged with governance. There are no unadjusted misstatements to report.

25. Adjustments to the annual report and accounts totalled £1.8 million for 2022/23 and £1.48 million for 2021/22 comparatives reported in the annual report and accounts. This includes the classification adjustment set out in paragraph 22 relating to pension service costs. Both adjustments were reclassifications therefore these had no impact on the net position reported in the SOCNE or Statement of Financial Position (SOFP).

26. We reviewed the nature and cause of these adjustments and have concluded that they were isolated in nature and have been identified in their entirety and do not indicate further systemic error.

The unaudited annual report and accounts were received in line with the agreed audit timetable

27. Working papers were received on 5th June 2023, with the unaudited annual report and accounts received slightly later than the agreed timetable on 8th June 2023. This did not impact on our ability to progress the audit. We received good support from management and the wider finance team which enabled us to complete the audit in accordance with the agreed timetable.

Progress was made on prior year recommendations

28. SOSE has made progress in implementing the audit recommendations identified in the prior year Annual Audit Report. For actions not yet implemented, revised responses and timescales have been agreed with management, and are set out in [Appendix 1](#).

2. Financial management

Financial management means having sound budgetary processes, and the ability to understand the financial environment and whether internal controls are operating effectively.

Conclusion

SOSE operated within its revised fiscal resources, reporting an underspend of £2.41 million which was mainly due to low demand for Financial Transactions.

Budget processes were appropriate, with regular updates to the Board on in-year budget revisions.

There is scope for enhancing some financial systems of internal control.

SOSE operated within its revised budget in 2022/23, with an overall underspend of £2.41 million against its fiscal budget

29. The main financial objective for SOSE is to ensure that the financial outturn for the year is within the budget allocated by Scottish Ministers.

30. SOSE has reported an outturn of £27.97 million against its fiscal budget for 2022/23 (the fiscal budget includes resource and capital Departmental Expenditure Limits (DEL) budgets and the financial transactions budget). This outturn resulted in an underspend of £2.41 million. The financial performance against all budgets is shown in [Exhibit 4](#).

Exhibit 4

Performance against fiscal resource in 2022/23

Performance	Initial budget £m	Final budget £m	Outturn £m	Over/(under) spend £m
Resource DEL	14.80	14.97	14.74	(0.23)
Capital DEL	15.20	13.50	13.17	(0.33)
Financial Transactions	6.00	1.91	0.06	(1.85)
Total	36.00	30.38	27.97	(2.41)

Source: South of Scotland Enterprise 2022/23 Annual Report and Accounts

31. The underspends reported in [Exhibit 4](#) were mainly due to:

- Resource DEL – half of the underspend relates to additional funding provided at the Spring Budget Revision for expected credit losses (ECL) that was ultimately not required. The remainder of the underspend relates to a small number of projects that have been delayed until 2023/24.
- Capital DEL – the underspend relates to a land purchase that was not concluded before the year-end.
- Financial Transactions – the underspend arises as the appetite for loans was low in year and a large loan that was expected to be processed not going ahead.

Budget processes were appropriate

32. SOSE's budget was adjusted as part of the Scottish Government's in-year budget revision process. Details on budget revisions are reported to the Board throughout the year. The most significant revisions over the course of the year for SOSE included:

- a reduction of £1.7 million in the capital DEL budget to reflect unspent elements being returned to the Scottish Government, and
- a reduction of £4 million in the financial transactions budget to reflect unspent elements being returned to the Scottish Government.

Net assets increased by £3.91 million

33. SOSE's net assets at the year-end increased by £3.91 million from £1.4 million in 2021/22 to £5.31 million in 2022/23. While the overall movement is an increase in net assets, there have been significant upward and downward movements in assets and liability on the SOFP. The most significant movements are:

- a £1.69 million increase in property, plant, and equipment, mainly due to expenditure incurred on developing the Mountain Bike Innovation Centre,
- a £0.97 million increase in intangible assets under construction, mainly due to expenditure incurred on developing MySOSE,
- a £2.09 million decrease in cash and cash equivalents, mainly due to movements in working capital management, and
- a £2.69 million decrease in the retirement benefit obligation, mainly due to changes in actuarial assumptions as a result of changes in market conditions affecting yield and inflation rates.

There is scope for enhancing some financial systems of internal control

34. From our review of the design, implementation and operating effectiveness of systems of internal control (including those relating to IT) relevant to our audit approach, we noted the following areas where there is scope for improvement to the operation of certain internal controls:

- Local controls – Skills Development Scotland (SDS) provide financial systems on behalf of SOSE. SOSE then have number of controls and checks in place around the information provided to them from SDS. Our evaluation of the design and implementation of these local controls found that the month-end reconciliations which have been prepared and reviewed by SDS are checked by SOSE, but this is not evidenced by a signature.
- Grants process – refer to [Exhibit 2](#).

Recommendation 2

Management should review its processes around the local controls in place to gain assurance over the information provided by Skills Development Scotland.

Standards of conduct and arrangements for the prevention and detection of fraud and error are appropriate

35. Public sector bodies are responsible for implementing effective systems of internal control, including internal audit, which safeguard public assets and prevent and detect fraud, error and irregularities, bribery, and corruption.

36. We concluded that SOSE has appropriate arrangements for the prevention and detection of fraud, error and irregularities. We also reviewed arrangements to maintain standards of conduct, including the Board and staff code of conduct and register of interests. We concluded that SOSE has established procedures for preventing and detecting any breaches of these standards.

National Fraud Initiative

37. The National Fraud Initiative (NFI) is a counter-fraud exercise across the UK public sector which aims to prevent and detect fraud.

38. SOSE participated in the NFI for payroll, supplier standing data, and supplier payments. The NFI data matches were issued to SOSE in January 2023 as part of the NFI exercise for 2022/23. A total of 81 data matches were identified for SOSE. Of these, 10 matches were selected for investigation due to their value. Work is currently underway to investigate these matches by the deadline of 30 September 2023.

3. Financial sustainability

Financial Sustainability means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs.

Conclusion

SOSE has effective and appropriate arrangements in place to continue to deliver services. This includes the development of a five-year financial plan.

SOSE approved a balanced budget for 2023/24 which includes identified pressures of £0.59 million.

SOSE has a five-year financial plan in place

39. The final 2023/24 budget was approved by the Board in March 2023. An updated five-year financial plan was presented alongside the 2023/24 budget. SOSE forecasts a break-even position in each year of the financial plan. It forecasts that resource grant-in-aid will decrease over the five-year period and therefore to achieve this break-even position each year, client and project resource expenditure will decrease while other expenditure (such as staff costs and estates) will increase due to inflationary pressures.

40. The five-year plan is based on a number of assumptions, including a five percent payroll uplift and incremental increases. The plan also identifies risks which could impact on the assumptions and delivery of the plan, such the pay uplift being higher than five percent. SOSE should ensure that these assumptions are kept under review over the duration of the plan and are updated to reflect any changes in circumstances.

41. The approved budget position for 2023/24 is £34.8 million. SOSE have identified £0.59 million of 'pressures' on the resource budget in 2023/24, these include:

- Business Gateway Funding – £0.078 million
- Staffing – £0.27 million
- Mountain Bike Innovation Centre – £0.106 million
- Reduction in loan interest – £0.09 million
- Additional Civtech resource value – £0.048 million.

42. Per the finance update to the Board in June 2023, management were developing an action plan to deliver savings to address the pressure in the resource budget. Pressures reduced to £0.45 million since the original

budget, but management advised this would be very challenging to deliver and difficult decisions would be required.

4. Vision, leadership and governance

Public sector bodies must have a clear vision and strategy and set priorities for improvement within this vision and strategy. They work together with partners and communities to improve outcomes and foster a culture of innovation.

Conclusion

SOSE has clear plans in place to implement its vision, strategy, and priorities.

Governance arrangements are appropriate and SOSE has finalised and published its framework document with the Scottish Government.

SOSE has made progress with climate change arrangements but more has to be done to establish and monitor targets.

Cyber security arrangements appear appropriate.

SOSE has plans in place to implement its vision, strategy and priorities

43. SOSE launched a new corporate plan in April 2023 outlining their role in delivering the Scottish Government's National Strategy for Economic Transformation (NSET). 'Our Five Year Plan' covers the period 2023-28 and was presented to the Board in March 2023. The plan sets SOSE's vision and long-term priorities and is structured around six areas of strategic focus.

44. SOSE's vision is to "create success, increase opportunity, lead a sustainable and just transition to Net Zero and advance equality."

45. The corporate plan is then supported by an Operating Plan for the 2023/24 year which sets out the priority activities for SOSE in order to deliver against the six areas of strategic focus:

- Accelerating net-zero and nature positive solutions
- Advocating for fair work and equality
- Activating and empowering enterprising communities
- Attracting ambitious investment
- Awakening entrepreneurial talent

- Advancing innovation and improving productivity.

46. To deliver on these six areas, each one has several key objectives, which will be monitored through a new performance measurement framework. Per 'Our Five Year Plan', SOSE's focus over the next five years is to start collecting data in line with the performance measurement framework and establish a baseline to measure their impact in the coming years.

Governance arrangements are appropriate

47. SOSE's governance arrangements have been set out in the Governance Statement in the annual report and accounts. We have reviewed these arrangements and concluded that they are appropriate and effective.

48. There continues to be an increasing focus on demonstrating the best use of public money. Openness and transparency in how a body operates and makes decisions is key to supporting understanding and scrutiny. Transparency means that the public have access to understandable, relevant and timely information about how the board is taking decisions and how it is using resources.

49. SOSE's website is clear and well structured. Board minutes are available to the public along with key publications including the latest annual report and accounts. We concluded that the Board conducts its business in an open and transparent manner.

SOSE has finalised its framework agreement with the Scottish Government

50. The 2021/22 Annual Audit Report highlighted that SOSE was operating with an interim framework agreement with the Scottish Government. The purpose of this document is to set SOSE's overall aims and the key roles and responsibilities which underpin its relationship with the Scottish Government.

51. The delay in finalising the document was due to the intention to align it with the equivalent documents for the other enterprise agencies. SOSE's framework document was completed in March 2023 and was published on its website in May 2023.

Climate change arrangements are in place, but clear targets should be set and monitored

52. The Scottish Parliament has set a legally binding target of becoming net zero by 2045 and has interim targets including a 75 percent reduction in greenhouse gas emissions by 2030. The public sector in Scotland has a key role to play in ensuring these targets are met and in adapting to the impacts of climate change.

53. SOSE has introduced a 'Net Zero, Nature and Entrepreneurship' directorate, with the aim of embedding the transition to Net Zero in the organisation. There is currently no separate climate change strategy or action plan as the aim is for this to sit within organisation-wide planning.

54. SOSE have made progress in year with the development of a South of Scotland Route Map to Net Zero with Dumfries and Galloway and Scottish Borders Councils, the establishment of the Energy Transition Group, and becoming a silver-accredited 'Carbon Literate Organisation'.

55. The annual report and accounts include the Sustainability and Environment Report which reports SOSE's carbon emission data for 2022/23. No specific targets outwith this have been set in relation to achieving net zero. 'Accelerating net zero and nature-positive solutions' is one of the six areas of strategic focus per the corporate plan, and, per paragraph 45, a performance measurement framework has been developed to collect data and set a baseline to measure progress against. We have been advised that the pandemic had an impact on the development of such targets over the first two years of SOSE coming into operation.

56. The Auditor General and Accounts Commission are developing a programme of work on climate change. This involves a blend of climate change-specific outputs that focus on key issues and challenges as well as moving towards integrating climate change considerations into all aspects of audit work.

Recommendation 3

SOSE should set clear and specific targets for the achievement of net zero.

Cyber security arrangements are appropriate

57. There continues to be a significant risk of cyber-attacks to public bodies, and it is important that they have appropriate cyber security arrangements in place. A number of recent incidents have demonstrated the significant impact that a cyber-attack can have on both the finances and operation of an organisation. In 2022/23, we considered SOSE's arrangements for managing and mitigating cyber security risks.

58. The Audit and Risk Committee receives regular updates on cyber security, due to its inclusion as a risk within the corporate risk register. The risk register sets out the mitigations in place to manage the risk around cyber security.

59. Information technology services for SOSE are managed by its internal IT service and by the Enterprise Information Services (EIS). The EIS partnership board provides the strategic oversight of the EIS partnership (also involving Scottish Enterprise, Highland and Islands Enterprise, and Skills Development Scotland).

60. Cyber Essentials Plus was accredited to SOSE and all EIS partner bodies in September 2022. IT security tools and measures are in place to mitigate any cyber security risks, including anti-virus and virus scanning software, intrusion prevention and detection systems, firewalls, and security information and event management systems.

61. We reviewed other documentation relating to SOSE's IT arrangements. There is currently a high-level IT road map in place which outlines the IT objectives that SOSE hopes to achieve. However, it does not outline the

resources required or the timescales involved for this. SOSE, alongside the other three bodies involved in the EIS partnership, are currently working with EIS to develop a more robust IT strategy. The aim is for this to include each partner bodies IT aims and clear and budgeted actions to achieve these. We will review the EIS strategy once it has been finalised.

5. Use of resources to improve outcomes

Public sector bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities.

Conclusions

SOSE should further develop its approach to demonstrating Best Value.

South of Scotland Enterprise has developed a new performance measurement framework, but specific targets should be set for 2023/24 onwards to assess progress.

SOSE should further develop its approach to demonstrating Best Value

62. [Ministerial guidance to Accountable Officers](#) for public bodies and the [Scottish Public Finance Manual](#) (SPFM) sets out the accountable officer's duty to ensure that arrangements are in place to secure best value. The guidance sets out the key characteristics of best value and states that compliance with the duty of best value requires public bodies to take a systematic approach to self-evaluation and continuous improvement.

63. We consider whether Accountable Officers have put in place appropriate arrangements to satisfy their corresponding duty of Best Value. We may also, in conjunction with SOSE, agree to undertake local work in this area. We did not undertake any specific work in 2022/23 but concluded that appropriate arrangements were in place for securing Best Value based on the outcome of our other audit work. However, we found that SOSE does not have a formally agreed document that details the arrangements in place to support the Best Value characteristics.

64. The Best Value process could be further enhanced by producing a document that is updated annually detailing the arrangements that support the characteristics. The annual update should be presented and approved by the Board or appropriate committee.

Recommendation 4

SOSE should produce an annual formally agreed document which details how it meets the Best Value characteristics as set out in the SPFM.

SOSE has developed a new Performance Measurement Framework, but 2022-23 indicators do not have any targets

65. Within the 2022/23 annual report and accounts, SOSE reported on its performance in relation to the 2022/23 Operating Plan which set out three priorities:

- Supporting Economic Recovery and Resilience
- Driving Change and Influencing Others in Action
- Developing our Offer.

66. While SOSE reported on developments and activity for each of the three priorities in the year, there had been no targets set for 2022/23 to assess this performance against.

67. As documented at paragraph 45, SOSE has developed a new performance measurement framework to monitor the progress of the Operating Plan 2023-24 and the six areas of strategic focus. An update was presented to the Audit and Risk Committee in March 2023 which set out the timeline for the development of the new measures and the approach to data collection. SOSE has also put a team in place to develop and implement the framework. This will take time to embed within the organisation, but it is important that SOSE sets targets to assess progress against for 2023/24 and beyond.

Recommendation 5

SOSE should ensure it sets measurable targets for performance to be assessed against for 2023/24 and beyond.

Appendix 1. Action plan 2022/23

2022/23 recommendations

Issue/risk	Recommendation	Agreed management action/timing
<p>1. Grant award process and monitoring</p> <p>Our audit testing identified improvements are required to the processes in place for evidencing the approval of grants and the subsequent monitoring of grant conditions and whether these are being met by recipients. For example, SOSE was unable to provide evidence of checks carried out prior to the award of a grant that we selected for substantive testing.</p> <p>Risk - SOSE makes grant payments to bodies who do not meet the terms and conditions of the grant award.</p>	<p>SOSE should review the controls and processes in place around the award of grants and subsequent monitoring of recipients and ensure these are applied consistently across the organisation.</p> <p>Exhibit 2</p>	<p>Agreed action: SOSE issued a Finance Guidance Note on the grant claims process on the 28/6/23 to all staff, reminding everyone of the correct claim process and their responsibilities. This document was shared with Audit Scotland on 11/07/23.</p> <p>Effective 1/7/23 SOSE added an extra step for all grant invoice approvals so finance verify a spreadsheet has been completed and attached in Agresso. This spreadsheet will detail the evidence checked against the Grant Offer Letter criteria and intervention rate. Finance will approve an invoice in Agresso once they confirm existence of this documentation.</p> <p>Responsible officer: Anthony Daye and Bryan McGrath</p> <p>Agreed date: Immediate effect</p>
<p>2. Local controls</p> <p>Skills Development Scotland (SDS) provide financial systems on behalf of SOSE. SOSE then have number of controls and checks in place around the information</p>	<p>SOSE should consider implementing evidenced checks on the financial information provided to them by the service provider (SDS).</p> <p>Paragraph 34</p>	<p>Agreed action: During 2022/23 SOSE reviewed the details of aged creditor listing in their signed month-end pack but acknowledge on a monthly basis two reconciliation documents are</p>

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<p>provided to them from SDS. Our evaluation of the design and implementation of these local controls found that the month-end reconciliations which have been prepared and reviewed by SDS are checked by SOSE, but this is not evidenced by a signature.</p> <p>Risk – Financial information provided by the service organisation is not accurate.</p>		<p>received from SDS 3 days after the general ledger has been locked for the period. The reconciliations include details of the preparer and reviewer with formal sign off, SOSE at present are reviewing but not signing so with effect from July 2023 month-end SOSE will sign these documents to evidence our check.</p> <p>Responsible officer: Anthony Daye</p> <p>Agreed date: 31/08/2023 (July month-end)</p>
<p>3. Climate change targets</p> <p>The Sustainability and Environment Report shows SOSE's carbon emission data for 2022/23. We have been advised no targets have been set around the achievement of net zero.</p> <p>Risk – SOSE cannot monitor its progress towards the achievement of net zero.</p>	<p>SOSE should develop clear and measurable targets to monitor progress in the achievement of net zero.</p> <p>Paragraph 55</p>	<p>Agreed action: SOSE has completed multiple actions to further our ambitions in this space we recognise that more work needs to be done to identify specific targets that can be measured to evidence our achievements towards Net Zero.</p> <p>Responsible officer: Martin Valenti</p> <p>Agreed date: 31/3/2024</p>
<p>4. Best Value Framework</p> <p>SOSE does not have a formally agreed document that details the arrangements in place to support the Best Value characteristics.</p> <p>Risk – SOSE is unable to demonstrate compliance with the duty of Best Value per the characteristics set out in the SPFM.</p>	<p>SOSE should produce an annually agreed document which details how it meets the Best Value characteristics as set out in the SPFM.</p> <p>Paragraph 65</p>	<p>Agreed action: SOSE agree to the recommendation and will produce the document proposed on annual basis going forward.</p> <p>Responsible officer: Anthony Daye</p> <p>Agreed date: 31/3/2024</p>

Follow-up of 2021/22 Annual Audit Report recommendations

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<p>5. Performance Measurement 2020/21 AAR</p> <p>SOSE has started developing a performance measurement framework, but progress was delayed as SOSE focused on responding to the impact of Covid-19.</p> <p>Risk – There is a risk that SOSE cannot demonstrate its contribution to Scottish Government priorities.</p>	<p>SOSE should develop a suite of measurable performance indicators. These should have a clear link to the Scottish Government's National Performance Framework, clearly demonstrating SOSE's contribution to the national priorities.</p>	<p>Ongoing – SOSE has introduced a new Performance Measurement Framework aligned to its new corporate plan and operating plan.</p> <p>Revised recommendation – SOSE should ensure it sets measurable targets for performance to be assessed against for 2023/24 and beyond.</p> <p>Paragraph 68</p> <p>Propose targets will be measured for 6 months of 2023/24.</p> <p>Responsible officer: Bryan McGrath</p> <p>Revised date: March 2024</p>
<p>6. Significant accounting estimates and judgements 2021/22 AAR</p> <p>The accounts include a note on critical accounting estimates and judgements. The note refers to significant estimates such as property valuations and retirement benefit obligations. However, testing found that the disclosures are not in line with good practice.</p> <p>Risk – the reader of the accounts is unclear about the main areas of judgement and estimation in the accounts.</p>	<p>SOSE should consider implementing some elements of the Audit Scotland best practice guide. This should include clearly differentiating between judgements and estimates, confirming the carrying value of any estimates and providing a sensitivity analysis.</p>	<p>Ongoing – our review of this disclosure in the 2022/23 annual report and accounts identified that improvements could still be made with this disclosure.</p> <p>Revised recommendation – SOSE should consider separating out the note to ensure that judgements are distinguished from estimates.</p> <p>Responsible officer: Anthony Daye</p> <p>Revised date: March 2024</p>
<p>7. Documentation of loans agreements 2021/22 AAR</p> <p>During our walkthrough of one business support loan, we found that a due diligence</p>	<p>SOSE should ensure that minutes which document meetings where decisions are taken in respect of prospective loans are comprehensive and provide</p>	<p>Complete – there were limited loans issued during 2022-23 so our audit work in this area was limited to a small sample.</p>

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<p>report had been prepared which highlighted areas of risk. The minutes of the meeting where the loan was approved did not however fully document the decision taken in light of this report.</p> <p>Risk – SOSE approves a high-risk loan without making its decision-making process fully transparent.</p>	<p>clarity regarding due diligence reports.</p>	<p>We will review the documentation of loan agreements and conclude on arrangements as part of our standard audit procedures in 2023/24.</p>
<p>8. Equalities arrangements 2021/22 AAR</p> <p>While SOSE has enshrined standards regarding equalities in the code of conduct and carried out an equality impact assessment, further work is required. Particular areas for action include finalisation of the equalities' strategy and preparation of the mainstreaming and outcomes report.</p> <p>Risk – without enhancing its arrangements SOSE may not comply with the Companies Act 2010.</p>	<p>SOSE should finalise its equality strategy and look to develop its first mainstreaming and outcomes report.</p>	<p>Complete – SOSE published its first Equalities Mainstreaming Report in April 2023. An Equalities Strategy has been published that covers a three-year period. The document outlines SOSE's objectives around equalities and outlines the three themes that have been developed to achieve the objectives.</p>
<p>9. Governance Arrangements 2020/21 AAR</p> <p>SOSE has established governance arrangements including an interim framework document between the Scottish Government and a committee structure. Internal audit concluded that SOSE's arrangements were appropriate in the context of a new organisation facing the challenges from Covid-19.</p> <p>Risk – As SOSE develops the governance arrangements may require to</p>	<p>SOSE should review its governance arrangements periodically during its first years of operation to confirm that governance is working as intended and is effective.</p>	<p>Complete – SOSE and the Scottish Government agreed a framework document in March 2023 and this was published on SOSE's website in May 2023.</p> <p>Our work on the Governance Statement in the annual report and accounts concluded that governance arrangements were appropriate and effective. We will continue to review this as part of our audit work each year.</p>

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be amended to ensure that that they are still effective.		
<p>10. Capital grants 2021/22 AAR</p> <p>Capital grants should be supported by evidence of underlying activity by the grant recipient. This can take the form of valuation certificates for work performed or invoices for items purchased.</p> <p>Sample testing of capital grants found two examples where the signed grant claim was not fully supported.</p> <p>Risk – SOSE funding could be used inappropriately.</p>	<p>SOSE should implement a process to ensure that all capital grant claims are suitably evidenced prior to payment.</p>	<p>Complete – substantive testing of grant payments found expenditure was recognised in the correct year and payments were supported by appropriate supporting documentation.</p>

South of Scotland Enterprise

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