

Scottish Rail Holdings Limited

2023/24 Annual Audit Report



 AUDIT SCOTLAND

Prepared for Scottish Rail Holdings Limited and the Auditor General for Scotland

12 December 2024

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Key messages

2023/24 annual report and accounts

- 1 Audit opinions on the annual report and accounts are unmodified.
- 2 Our audit resulted in amendments to the annual report and accounts to ensure they reflected the requirements of the 2023/24 FReM.
- 3 Management should work with the SRT and CSL finance teams to agree a timetable that ensures the component bodies 2024/25 accounts are available in time for consolidation in the SRH 2024/25 annual report and accounts presented for audit. SRH should also ensure that FReM accounting requirements are adopted by the component bodies wherever possible to reduce the volume of consolidation adjustments required.

Financial management and sustainability

- 4 SRH had appropriate budget monitoring and reporting arrangements in place during 2023/24, but there is scope to improve these. Management should establish what budget monitoring information they require from SRT and CSL for each period to better support its monitoring of the financial performance of the train operators, and to streamline the group budget monitoring and reporting processes.
- 5 £718 million of the £746 million grant-in-aid funding drawn down by SRH during 2023/24 was paid across to SRT to fund the delivery of ScotRail train services. The SRH group reported an underspend of £15.1 million against its resource budget allocation for 2023/24, due to strong passenger revenue growth during the year.
- 6 SRH is working with SRT to manage down a projected RDEL budget pressure of £24.5 million for 2024/25 but this is likely to prove challenging due to the limited levers available to SRT in the short-term to reduce costs or increase passenger revenue.

Vision, leadership, and governance

- 7** SRH needs to work with Transport Scotland to increase the pace of progress in establishing effective arrangements to oversee train operations in Scotland. This includes expediting the recruitment and appointment of staff to the vacant roles within SRH's approved organisational structure, to ensure the organisation has sufficient capacity and skills to effectively perform its duties.
- 8** SRH prepared a five-year Strategic Plan 2024-2029 and 2024/25 Business Plan. Management is now working to further develop these plans, including the oversight arrangements of rail services in Scotland from 2025/26.
- 9** SRH is working with Transport Scotland, and in close cooperation with Network Rail Scotland, to design, develop and implement a Scottish Rail Fleet Strategy and Fleet Procurement Strategy.
- 10** Management needs to strengthen SRH's governance arrangements, which includes holding regular meetings of the Audit and Risk Committee. SRH operated without an internal audit function during 2023/24 but appointed an interim Audit and Risk Manager in October 2024.

Use of resources to improve outcomes

- 11** SRH has still to develop a Best Value framework. It also needs to review the suite of key performance indicators reported to the board to ensure these support it in effectively monitoring the performance of SRT and CSL, and assist it in driving improvements and efficiencies in the delivery of rail services in Scotland in the future.

Introduction

1. This report summarises the findings from the 2023/24 annual audit of Scottish Rail Holdings Limited (SRH) and will be published on Audit Scotland's website: www.audit-scotland.gov.uk.
2. This annual audit report comprises significant matters arising from the audit of the Scottish Rail Holdings Limited annual report and accounts and conclusions on the wider scope areas, as set out in the [Code of Audit Practice](#).
3. We would like to thank Board members and officers, particularly those in finance, for their cooperation and assistance during the course of the audit.

Responsibilities and reporting

4. SRH has responsibility for ensuring the proper financial stewardship of public funds. This includes preparing an annual report and accounts that are in accordance with the accounts direction from Scottish Ministers. SRH is also responsible for establishing appropriate and effective arrangements for governance, propriety, and regularity.
5. The responsibilities as the independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000, the [Code of Audit Practice](#), supplementary guidance and International Standards on Auditing in the UK (ISAs).
6. This report contains an agreed action plan at [Appendix 1](#) setting out specific recommendations, responsible officers and dates for implementation. Weaknesses or risks identified in this report are only those which have come to our attention during our audit work and may not be all that exist. Communicating these does not absolve management of its responsibility to address the issues we raise and from maintaining adequate systems of control.

Auditor Independence

7. 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 and therefore the 2023/24 audit fee of £42,111, as set out in our 2023/24 Annual Audit Plan, remains unchanged. We are not aware of any relationships that could compromise our objectivity or our independence.

1. 2023/24 annual report and accounts

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

Audit opinions on the annual report and accounts are unmodified.

Our audit resulted in amendments to the annual report and accounts to ensure they reflected the requirements of the 2023/24 FReM.

Management should work with the SRT and CSL finance teams to agree a timetable that ensures the component bodies 2024/25 accounts are available in time for consolidation in the SRH 2024/25 annual report and accounts presented for audit. SRH should also ensure that FReM accounting requirements are adopted by the component bodies wherever possible to reduce the volume of consolidation adjustments required.

Audit opinions on the annual report and accounts are unmodified

8. The Board approved the annual report and accounts for SRH and its group for the year ended 31 March 2024 on 12 December 2024. The independent auditor's report included the following audit opinions on the annual report and accounts:

- 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
- 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.

The 2023/24 annual report and accounts were certified on 12 December 2024

9. We received the unaudited annual report and accounts and working papers on 4 October 2024, in line with the agreed audit timetable. However,

management advised that some sections were still being worked on at this point and these would be provided when available. This included the group statements consolidating the financial results of ScotRail Trains Limited (SRT) and Caledonian Sleeper Limited (CSL). A substantially complete set of accounts was provided on 28 October 2024.

10. The accounts and working papers presented for audit were of a reasonable standard and management and finance staff provided good support to the team during the audit process. However, revisions were required to the layout and contents of the annual report and accounts presented for audit to ensure they complied with 2023/24 FReM requirements, and adequately explained SRH's operations to readers of the accounts. The extent of these changes was in part due to the complexities of the first time consolidation of the financial results of CSL into the SRH group statements, and the delays in finance staff receiving this information. A further complication was the adoption of the FRS101 Reduced Disclosure Framework reporting standard by SRT and CSL which resulted in consolidation adjustments to align the accounting treatment with the requirements of the FReM for the SRH group statements. Alongside this, SRH's limited finance team resources, and lack of continuity of finance staff from 2022/23, meant that it was not until early September that it had dedicated resources to work on the preparation of the 2023/24 accounts. This reflects the wider staffing capacity challenges that the organisation has faced during 2024 (discussed at paragraphs [48.](#) and [53.](#)).

Recommendation 1

Management should work with the SRT and CSL finance teams to agree a timetable that ensures the component bodies 2024/25 accounts are available in time for consolidation in the SRH 2024/25 annual report and accounts presented for audit. SRH should also ensure that FReM accounting requirements are adopted by the component bodies wherever possible to reduce the volume of consolidation adjustments required.

11. Despite the issues encountered with the accounts presented for audit, our audit was completed in time for the 2023/24 annual report and accounts to be certified on 12 December 2024 and laid at the Scottish Parliament prior to the 31 December deadline.

Our audit approach and testing were informed by the overall materiality level of £23 million

12. 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 impact the 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 and it is ultimately a matter of the auditor's professional judgement.

13. Our initial assessment of materiality was carried out during the planning phase of the audit and was based on the projected group and single entity expenditure for the year ended 31 March 2024. These materiality levels were reported in our annual audit plan to the June 2024 meeting of the Audit and Risk Committee.

14. On receipt of the unaudited 2023/24 annual report and accounts we revised our materiality levels based on the actual financial results for the year ended 31 March 2024, to reflect the higher than projected group and single entity expenditure. The revised materiality levels are detailed in [Exhibit 1](#).

Exhibit 1

Materiality values for the 2023/24 audit

Materiality level	Single Entity	Group
Overall materiality: This is the figure we calculate to assess the overall impact of audit adjustments on the financial statements. It has been set based on our assessment of the needs of the users of the financial statements and the nature of SRH's operations. For the year ended 31 March 2024, we set our materiality at 2 per cent of gross expenditure.	£14.5 million	£23.0 million
Performance materiality: This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality, this could indicate that further audit procedures are required. Using our professional judgement, we set performance materiality at 75 per cent of overall materiality for the single entity and 65 per cent for the group.	£10.75 million	£15.0 million
Reporting threshold: We are required to report to those charged with governance on all unadjusted misstatements above the 'reporting threshold' amount.	£0.5 million	£0.5 million

Source: Audit Scotland

Our audit identified and addressed the risks of material misstatement

15. [Exhibit 2](#) sets out the significant and non-significant risks of material misstatement to the financial statements. It also summarises the audit procedures we performed during the year to obtain assurances over these risks and the conclusions from the work completed.

Exhibit 2

Significant and other risks of material misstatement

Audit risk	Assurance procedure	Results and conclusions
Significant risks of material misstatement		
<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 unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively. As a result, we are required to design audit procedures to specifically address this risk for all of our financial statements audits.</p>	<ul style="list-style-type: none"> • Detailed testing of SRH consolidation adjustments, transactions and journals. • Reviewed significant accounting estimates. • Focussed testing of accruals and prepayments. • Evaluated significant transactions outside the normal course of business. • Group auditor assurances obtained from PwC, based on the outcome of the audit procedures designed to address the risk of management override of controls for the ScotRail Trains Limited external audit – see risk 2 below. 	<ul style="list-style-type: none"> • Our testing of consolidation adjustments identified an issue in relation to grant funding owed to the subsidiaries, where a creditor balance and corresponding expense was omitted (see issue 1 in Exhibit 3). Our testing of the adjustments to remove intercompany transactions between SRH and the subsidiaries did not identify any issues. • We reviewed accounting estimates and concluded these were appropriate. • Focused testing of accruals and prepayments identified one issue (see issue 1 in Exhibit 3). We concluded that this was an isolated error that had been identified in its entirety and did not indicate further systematic error. • No significant transactions outside the normal course of business were identified during the audit. • Group auditor assurances received from PwC confirmed that they were satisfied that there was no material misstatement arising from this risk for the SRT audit. <p>Satisfactory: Our audit procedures did not identify any evidence of management override of controls to manipulate the financial position reported in the annual report and accounts. We are satisfied that there is no material</p>

Audit risk	Assurance procedure	Results and conclusions
<p>2. Significant risks of material misstatement in ScotRail Trains Limited (SRT)</p> <p>PwC, as the appointed external auditors of SRT, has identified the following significant risks of material misstatement for SRT's 2023/24 financial statements:</p> <ul style="list-style-type: none"> • Management override of controls • Fraud in revenue recognition • Service agreement length assumptions • Pensions assumptions and service agreement adjustment methodology. <p>As SRT is a significant component of the SRH group, representing over 90 per cent of annual group expenditure, these also represent significant risks of material misstatement for the SRH 2023/24 group financial statements.</p>	<ul style="list-style-type: none"> • As the SRH Group auditor we will obtain group auditor assurance over the audit of SRT from PwC as the component auditor, in accordance with the requirements of International Standard on Auditing (UK) 600 – Special considerations: audit of group financial statements (including the work of component auditors). 	<p>misstatement arising from this risk.</p> <p>Satisfactory: PwC provided component auditor assurances in respect of the significant risks of material misstatement for SRT's 2023/24 financial statements.</p>
<p>Other non-significant risks of material misstatement</p>		
<p>3. First time consolidation of the Caledonian Sleeper Limited (CSL) financial results within the SRH group statements</p> <p>Sleeper train services were brought into public ownership on 25 June 2023 and CSL was established to oversee the operation of the sleeper</p>	<ul style="list-style-type: none"> • It is expected that CSL's Accounts Direction will require it to comply with the FReM which will reduce the number of consolidation adjustments required to the financial results of CSL to align its accounting policies 	<ul style="list-style-type: none"> • The 2023/24 accounts directions for CSL and SRT both stated they should: "...comply with the accounting principles and disclosure requirements of the edition of the FReM which is in force for the year for which the statement of accounts are prepared, and with the Companies Act 2006." As a result, CSL adopted the FRS101 Reduced Disclosure Framework reporting

Audit risk	Assurance procedure	Results and conclusions
<p>service. CSL is a subsidiary of SRH and its financial results will therefore require to be consolidated within SRH's group financial statements in the SRH 2023/24 Annual Report and Accounts.</p> <p>The classification of CSL has not yet been confirmed by the Office of National Statistics (ONS) but we expect ONS to confirm CSL's status as a Non-Departmental Public Body (NDPB). We also expect the Accounts Direction will reflect this classification and require CSL to produce accounts in accordance with the Government Financial Reporting Manual (FReM). This should reduce the number of consolidation adjustments required to the financial results of CSL to align its accounting policies with SRH for the preparation of the SRH group statements. However, there remains a risk that the information required to consolidate CSL and prepare FReM compliant group accounts may be incomplete or unavailable.</p>	<p>with SRH for the preparation of the SRH group statements.</p> <ul style="list-style-type: none"> • Discussions between SRH and CSL will identify any areas of significant divergence in accounting policies that will require adjustments to be made to the CSL financial results as part of the consolidation process. • Processing consolidation adjustments is an expected part of the group statements preparation process and officers already have experience of consolidating the SRH financial results in the prior year. • Intercompany transactions between SRH and CSL relate primarily to train operator funding payments which are easy to identify and eliminate upon consolidation. 	<p>standard which resulted in consolidation adjustments to align the accounting treatment with the requirements of the FReM for the SRH group statements (see issue 2 in Exhibit 3).</p> <ul style="list-style-type: none"> • The SRH finance team discussed areas of divergence with the CSL finance team to identify the consolidation adjustments required to align with the SRH accounting policies, including a number of audit adjustments (see issue 2 in Exhibit 3). • Our testing of the adjustments to remove intercompany transactions between SRH and the subsidiaries did not identify any issues. <p>Satisfactory: All material issues identified with first time consolidation of CSL financial results within the SRH group statements were corrected within the audited SRH 2023/24 Annual Report and Accounts.</p>
Other opinion risks		
<p>4. Remuneration and Staff Report</p> <p>The Auditor General for Scotland prescribes that the appointed auditor should</p>	<ul style="list-style-type: none"> • We reviewed the completeness of the pension disclosures in the Remuneration and Staff Report in 	<p>Satisfactory: The Remuneration and Staff Report included the required pension information for all officers.</p>

Audit risk	Assurance procedure	Results and conclusions
<p>provide an opinion as to whether the audited part of the Remuneration and Staff Report has been compiled in accordance with the appropriate regulations and frameworks, and is consistent with the financial statements.</p> <p>The Remuneration and Staff Report is required to disclose pension information for members of the SRH Board and the Senior Management Team. However, these disclosures were not complete in 2022/23 as pension information had not been obtained for all officers on the SMT. There is a risk that similar issues are encountered for the 2023/24 Annual Report.</p>	<p>the accounts presented for audit.</p>	
<p>5. Performance Report</p> <p>The Auditor General for Scotland prescribes that the appointed auditor should provide an opinion as to whether the Performance Report has been compiled in accordance with the appropriate regulations and frameworks, and is consistent with the financial statements.</p> <p>The Performance Report is required to provide a clear and transparent summary of the performance of the organisation during 2023/24. For SRH this should also cover the performance of the group and include high level performance data for SRT and CSL. There is a risk that this information is not available.</p>	<ul style="list-style-type: none"> • We reviewed the contents of the Performance Report in the accounts presented for audit to ensure it provided an adequate summary of the performance of the organisation during 2023/24. 	<ul style="list-style-type: none"> • The performance summary and key risks section of the performance report required a small number of amendments to be made to present a more balanced group position. We discussed these with management and the relevant disclosures were updated and amended for the audited accounts. <p>Satisfactory: Issues identified were all adjusted in the audited SRH 2023/24 Annual Report and Accounts.</p>

Source: Audit Scotland

We reported the significant findings from the audit to those charged with governance prior to the annual report and accounts being approved and certified

16. International Standard on Auditing (UK) 260 requires us to communicate significant findings from the audit to those charged with governance, including our view about the qualitative aspects of SRH's accounting practices. The Code of Audit Practice also requires auditors to communicate key audit matters within the annual audit report under the International Standard on Auditing (UK) 701. These are matters that we judged to be of most significance in our audit of the financial statements.

17. The significant findings from our audit of the Scottish Rail Holdings Limited 2023/24 Annual Report and Accounts are summarised in [Exhibit 3](#). Our audit also identified some other presentational and disclosure issues which were discussed with management. These were all adjusted in the audited annual report and accounts and were not considered significant enough to be separately reported under ISA260.

Exhibit 3

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

Issue	Resolution
<p>1. Accounting treatment of SRT and CSL accrued income grant funding</p> <p>Our testing of the group consolidation adjustments identified that the SRT accounts included accrued income and a receivables balance of £60.996 million for grant funding due to it from SRH at 31 March 2024, and the CSL accounts included accrued income and a receivables balance due from SRH of £7.891 million. These amounts were in relation to grant funding owed to the subsidiaries from SRH for rail services delivered during 2023/24 to ensure the rail operators achieves financial balance for the financial year, in line with the conditions of the grant agreements and the Scottish Government's commitment to fund rail services in Scotland.</p> <p>The SRH single entity accounts presented for audit did not recognise the corresponding expenditure or payables balance for the grant funding due to the subsidiaries at 31 March 2024.</p>	<p>Management made the necessary adjustment in the audited 2023/24 financial statements. This increased the SRH single entity 'Net Operating Expenditure' in the <i>Statement of Comprehensive Net Expenditure</i> by £68.887 million, and increased the SRH single entity 'Current Liabilities' in the <i>Statement of Financial Position</i> by the same value. This did not affect the group position as these intragroup transactions were reversed in the group consolidation process.</p> <p>As the additional grant funding due to SRT and CSL for 2023/24 was not drawn down by SRH before 31 March 2024 it is not included in the 'Grant in Aid from the Scottish Government for the period' figure in the <i>Statement of Changes in Taxpayers' Equity</i>.</p> <p>A similar year-end adjustment will be required in the SRH single entity</p>

Issue	Resolution
	<p>accounts every year, management should establish a process that aligns with the SRH accounts preparation and closedown timetable, to identify the value of the outstanding grant funding due to the subsidiaries at 31 March for rail services delivered during the year.</p> <p>Recommendation 2</p> <p>This was judged to be a key audit matter.</p>
<p>2. Post-audit adjustments / classification issues</p> <p>A significant number of post-audit adjustments and classification issues were identified as part of our audit of the group consolidation working papers.</p> <p>The extent of the changes required was in large part due to the late receipt of fully complete accounts from the subsidiary bodies which resulted in revisions being made throughout the audit process. CSL produced accounts for the first time in 2023/24 and numerous revisions were made to their accounts during the audit process. SRT also made some changes to their accounts during our audit of the group statements but the volume of these was far lower.</p> <p>The late changes to the CSL and SRT accounts resulted in amendments being made to the SRH group statements to reflect these changes during our audit of the group statements. This created challenges in tracking through all the changes made, and also placed pressure on both the SRH finance team and the audit team in finalising the SRH 2023/24 Annual Report and Accounts.</p>	<p>The errors and late adjustments we identified in the group statements were all corrected in the audited SRH 2023/24 Annual Report and Accounts.</p> <p>Management should work with the SRT and CSL finance teams to agree a timetable that ensures the component bodies 2024/25 accounts are available in time for consolidation in the SRH 2024/25 annual report and accounts presented for audit. SRH should also ensure that FReM accounting requirements are adopted by the component bodies wherever possible to reduce the volume of consolidation adjustments required.</p> <p>Recommendation 1</p>
<p>3. Segmental Reporting</p> <p>The FReM specifies segmental reporting requirements for public sector bodies in the UK which reflect the requirements of <i>IFRS8 – Operating Segments</i>. These include a requirement for public sector bodies accounts to report on segments in line with internal budget monitoring reports and to disclose for each reportable segment: segment income and expenditure for the year, and the resulting profit or loss for the period; as well as the prior year comparative figures. Public sector bodies</p>	<p>These disclosures were discussed with management and we accepted a segmental analysis table being included in the financial performance section of the Performance Report in the audited SRH 2023/24 Annual Report and Accounts.</p> <p>Management should ensure they have all the information needed for the segmental reporting disclosures</p>

Issue	Resolution
<p>accounts should also include a reconciliation of the total income and expenditure reported for the operating segments to the consolidated position reported for the year.</p> <p>These disclosure requirements are designed to ensure that the financial statements provide a clear and comprehensive view of the financial performance and position of each segment within the public sector body.</p> <p>Given SRH's role in monitoring the financial performance of SRT and CSL we expected the annual accounts to include segmental analysis of the financial performance of each company, along with a reconciliation to the outturn position reported for the SRH group. However, these disclosures were not included in the SRH accounts presented for audit.</p>	<p>required for the SRH 2024/25 Annual Report and Accounts.</p> <p>Recommendation 3</p>
<p>4. Unallocated dilapidations provision balance</p> <p>When assets are leased by a public body the lease agreement generally includes a clause that the lessee will need to restore the leased asset to its original condition at the end of the lease agreement. Therefore, the lessee has to create a dilapidation provision to reflect the costs that will be incurred by the organisation at the end of the lease.</p> <p>Under <i>IFRS16 Leases</i> the value of any dilapidation provision requires to be reflected included in the lease liability and the value of the corresponding right of use leased asset, to reflect the additional costs and economic benefits to the organisation of leasing those assets.</p> <p>As part of the arrangements to bring the Caledonian Sleeper service into public ownership, CSL took on £0.869 million of dilapidations provisions relating to rolling stock and property right of use leased assets transferred across to it from the previous rail franchise operator. However, these dilapidations provisions were not charged to the Statement of Comprehensive Net Expenditure or allocated against the corresponding right of use assets in CSL's 2023/24 accounts.</p>	<p>We agreed with management that the amount is not material and does not require to be adjusted in the audited SRH 2023/24. Had an adjustment been made for this error it would have increased both the SRH group expenditure in the <i>Statement of Comprehensive Net Expenditure</i> by £0.869 million and the 'right of use assets' in the <i>Statement of Financial Position</i> by the same amount.</p> <p>Management has agreed to review this to ensure it is correctly reflected in the 2024/25 annual accounts.</p>

Issue	Resolution
<p>5. Revisions to annual report disclosures</p> <p>Our review of the SRH 2023/24 Annual Report and Accounts presented for audit identified a number of revisions that were required to the Performance Report, Governance Statement, and Remuneration and Staff Report to ensure the information reported was in accordance with the appropriate regulations and frameworks.</p> <p>(See paragraphs 20. and 21. for details)</p>	<p>We worked with management to agree the additional and revised disclosures that were required for the annual report. These are all reflected in the audited SRH 2023/24 Annual Report and Accounts.</p>
<p>Source: Audit Scotland</p>	

We only have one unadjusted error to report as management corrected all other errors we identified for the audited accounts

18. We are required to report to those charged with governance, all misstatements above our reporting threshold, and request that these are corrected. As detailed in [Exhibit 3](#), we identified a number of misstatements in above our reporting threshold during the course of audit. The only misstatement not corrected in the audited accounts was the unallocated dilapidations provision balance (issue 4 in [Exhibit 3](#)) which is reported as an unadjusted error of £0.869 million. As this value is well below our materiality level it does not impact upon our audit opinions on the annual accounts.

19. Due to the nature of the misstatements identified during the audit we are satisfied that these have been identified in their entirety and there is no material misstatement in the untested population.

Our audit work on the annual report identified the requirement for a number of revisions

20. In addition to the appointed auditor's opinion on the financial statements, the Auditor General for Scotland prescribes that the appointed auditor should provide opinions as to whether the Performance Report, Governance Statement, and the audited part of the Remuneration and Staff Report, have been compiled in accordance with the appropriate regulations and frameworks, and are consistent with the financial statements.

21. Our review of the annual report within the SRH 2023/24 Annual Report and Accounts identified revisions required to the annual report presented for audit:

- **Performance Report:** The performance summary and key risks section of the performance report required a small number of amendments to

present a more balanced group position. Management updated relevant disclosures in the audited SRH 2023/24 Annual Report and Accounts.

- **Remuneration and Staff Report:** Our review identified corrections and improvements required and management made the relevant amendments in the audited SRH 2023/24 Annual Report and Accounts. These included correcting the pay banding disclosure for two members, updating the narrative and adding more detail to the fair pay disclosures, as well as including an exit package nil disclosure.
- **Governance Statement:** We identified this did not accurately reflect SRH's governance arrangements or adequately disclose the weaknesses in the operation of these arrangements during 2023/24 (discussed at paragraphs [62.](#) to [66.](#)). We discussed these issues with management, including the newly appointed interim Internal Audit and Risk Manager, who accepted our recommendations and updated the Governance Statement to accurately reflect these in the audited SRH 2023/24 Annual Report and Accounts.

Limited progress has been made in implementing our prior year recommendations

22. Our 2022/23 Annual Audit Report was issued in December 2023 and contained 6 recommendations for improvement. These included actions to address some of the barriers to SRH operating effectively (discussed at paragraphs [43.](#) to [47.](#)), to establish effective governance arrangements (discussed at paragraphs [62.](#) to [66.](#)), and to develop a Best Value framework for SRH's operations (discussed at paragraphs [76.](#) and [77.](#)). Limited progress was made in implementing these recommendations during 2024, although we have seen some progress in moving these forward over the last few months of the year. An update on each recommendation is provided in [Appendix 1](#).

2. Financial management and sustainability

Financial management means having sound budgetary processes, and the ability to understand the financial environment and whether internal controls are operating effectively. Financial Sustainability is being able to meet the needs of the present without compromising the ability of future generations to meet their own needs.

SRH had appropriate budget monitoring and reporting arrangements in place during 2023/24, but there is scope to improve these. Management should establish what budget monitoring information they require from SRT and CSL for each period to better support its monitoring of the financial performance of the train operators, and to streamline the group budget monitoring and reporting processes.

£718 million of the £746 million grant-in-aid funding drawn down by SRH during 2023/24 was paid across to SRT to fund the delivery of ScotRail train services. The SRH group reported an underspend of £15.1 million against its resource budget allocation for 2023/24, due to strong passenger revenue growth during the year.

SRH is working with SRT to manage down a projected RDEL budget pressure of £24.5 million for 2024/25 but this is likely to prove challenging due to the limited levers available to SRT in the short-term to reduce costs or increase passenger revenue.

Significant capital investment from the Scottish Government will be required in future years to support the modernisation of the ScotRail Trains fleet.

SRH had appropriate budget monitoring and reporting arrangements in place during 2023/24, but there is scope to improve these

23. During 2023/24 SRT and CSL submitted management accounts packs to SRH every 4 weeks to align with the grant payment periods and inform discussion with SRH management of the cash funding requirements of the subsidiaries for the next period. The management accounts packs included details of the financial position to date and projections for the full year, a “colour of money” summary (i.e. analysis of expenditure against Scottish Government budget categories), as well as information on risk sensitivities, budget variances and emerging pressures.

24. SRH's finance team used the management accounts packs from SRT and CSL, and its own management accounting information, to produce regular budget monitoring packs for the SRH group during 2023/24. These detailed the single entity and group position for the year to date, and the projected year-end outturn. These reports were considered by the Executive Management Team to enable them to respond to any emerging issues and take corrective action. A summary of this information was also included within the Finance Update papers to each meeting of the SRH Board. This also included an update on any budget discussions or financial management and governance issues.

25. We noted that the format and contents of the management accounts packs submitted to SRH during 2023/24 differed between SRT and CSL, and the single entity management accounting information. This presented some challenges to the SRH finance team in consolidating this to produce a group position, and also in drilling down on the financial performance of the subsidiaries during the year. We acknowledge that the constraints on finance staff resources to date have hindered progress in this area.

26. There is an opportunity for SRH to prescribe the format and contents of the management accounting information it requires from SRT and CSL to better support its role in monitoring the financial performance of the subsidiaries, and to streamline the group budget monitoring and reporting processes.

Recommendation 4

Management should establish what budget monitoring information they require from SRT and CSL for each period to better support its monitoring of the financial performance of the train operators, and to streamline the group budget monitoring and reporting processes.

£718 million of the £746 million grant-in-aid funding drawn down by SRH during 2023/24 was paid across to SRT to fund the delivery of ScotRail train services

27. SRH is the vehicle through which the Scottish Government, via Transport Scotland, provides funding for Scottish rail passenger operations. During 2023/24 this covered the funding of ScotRail train services provided by SRT, and, from 25 June 2023, the funding of the Caledonian Sleeper train services provided by CSL.

28. During 2023/24, SRH drew down grant-in-aid funding from the Scottish Government of £745.7 million, with £718.9 million (96 per cent) paid across to SRT to fund the costs of delivering ScotRail train services during the year and £23.0 million (3 per cent) paid across to CSL to fund the costs of delivering Caledonian Sleeper train services from June 2023. It should be noted that the funding provided to CSL during 2023/24 was lower than would usually be required to fund these services for 9 months due to the cash balance held by CSL at the time that the services were brought into public ownership.

29. In addition to the funding paid across to SRT and CSL during 2023/24, SRH also owed £61.0 million to SRT and £7.9 million to CSL for grant funding due for services provided up to 31 March 2024, but where the operators did not require the cash funding during 2023/24. As explained at issue 1 in [Exhibit 3](#), this is in line with the conditions of the grant agreements and the Scottish Government's commitment to fund rail services in Scotland and therefore these outstanding amounts have been recognised as expenditure, and with a corresponding payables balance, in the SRH 2023/24 Annual Report and Accounts.

30. SRH single entity expenditure for 2023/24 totalled £2.4 million with £1.9 million used for staff costs. This is an increase from SRH's staff costs of £1.4 million in 2022/23 which reflects the fact that majority of staff did not take up their posts until part way through the prior year. We would expect SRH staff costs to increase again in 2024/25 as new staff are appointed to the vacant roles within its approved organisational structure, to ensure the organisation has sufficient capacity to effectively perform its duties in overseeing train operations in Scotland (discussed at paragraphs [48.](#) to [52.](#)).

The SRH group reported an underspend of £15.1 million against its resource budget allocation for 2023/24, due to strong passenger revenue growth during the year

31. As explained at paragraphs [27.](#) to [30.](#), almost all of SRH's 2023/24 expenditure consisted of payments to SRT and CSL for the delivery of ScotRail and Caledonian Sleeper train services. [Exhibit 4](#) shows how this expenditure was split across the body's Scottish Government budget allocations, and the final outturn against the non-cash and annually managed expenditure budget allocations for the year.

32. As can be seen from [Exhibit 4](#), SRH reported an underspend for the year of £28.9 million against its Scottish Government budget allocation, which included a £15.1 million underspend against its RDEL budget and an underspend of £1.8 million against its CDEL budget. The positive resource outturn position reported for 2023/24 was mainly due to strong passenger revenue growth during the year which offset the in-year cost pressures created by increased Network Rail charges and decreased compensation receipts, higher energy prices and increased train maintenance costs resulting from SRT's ageing fleet.

33. As shown in [Exhibit 4](#), the SRH group reported an underspend of £1.8 million against its CDEL budget of £383.7 million for 2023/24. This budget was used to cover fixed track access charges paid by SRT and CSL to Network Rail, and expenditure on a range of low value capital projects during the year.

Exhibit 4**Performance against Scottish Government budget allocations in 2023/24**

Scottish Government budget allocation category	Budget allocation £m	Outturn £m	Over/(under) spend £m
Resource departmental expenditure limit (RDEL)	440.7	427.4	13.3
Capital departmental expenditure limit (CDEL)	383.7	381.9	1.8
Operating subtotal	824.4	809.3	15.1
Non-cash limit (RfDEL)	2.5	5.2	(2.7)
Annually managed expenditure (AME)	4.5	2.9	1.7
Capital AME (CAME)	-	1.0	(1.0)
Lease accounting adjustments	91.1	75.3	15.8
Total	922.5	893.6	28.9

Source: Scottish Rail Holdings Limited 2023/24 Annual Report and Accounts

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

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

35. SRH's [Code of Governance \(December 2021\)](#) includes the body's code of conduct. This is based around the requirements of the Ethical Standards in Public Life (Scotland) Act 2000 and sets out guidance on expected conduct at meetings and principles to be followed. It also details requirements for registering interests and avoiding conflicts of interest.

36. SRH also has a separate fraud strategy which is based around the requirements set out within the Scottish Public Finance Manual and is aligned with the Transport Scotland fraud strategy. The document also sets out that Transport Scotland's Audit and Risk Committee (ARC) has a general responsibility for monitoring the operation and effectiveness of anti-fraud arrangements and the committee require regular reports on fraud activity from SRH. Management advised that any fraud risks identified would be reported to the Transport Scotland ARC and would also be included in the SRH ARC Chair's report to the quarterly meetings of the Strategic Rail Board. These arrangements would ensure that any fraud risks identified are discussed with SRH's sponsor body.

37. We noted in the prior year that the fraud strategy has a section on whistleblowing which referred to a SRH Whistleblowing Policy but this was not yet in place. We are pleased to note that the Board recently approved the whistleblowing policy, as well as a staff code of conduct.

SRH is working with SRT to manage down a projected RDEL budget pressure of £24.5 million for 2024/25 but this is likely to prove challenging due to the limited levers available to SRT in the short-term to reduce costs or increase passenger revenue

38. The financial monitoring information presented to the October meeting of the SRH Board showed a £24.5 million RDEL budget pressure for 2023/24 relating to the projected outturn for SRT for the year. This is largely attributable to reduced passenger revenue during the period when a temporary timetable was in operation between July and September 2024, as well as the impact on passenger fare income of the [ScotRail Peak Fares Removal Pilot](#) which ran from October 2023 to March 2024.

39. SRH is working with SRT to try and manage down this projected budget pressure. However, as the majority of SRT's expenditure relates to staff and other operational costs which are linked to the delivery of the regulated rail services, and its income generating potential is also linked to the level of regulated fares for these services; then the main lever available to SRT to address this is through increased fare income through higher passenger numbers which is hard to achieve in the short-term and unlikely to bridge the 2023/24 budget gap.

SRH has still to develop medium-term and long-term financial plans

40. As reported in our [2022/23 Annual Audit Report](#), a medium or long-term financial strategy has not yet been developed by SRH for the funding of its two train services operated by its subsidiaries, or for its corporate role. The focus during 2024 has been on the development of the 5-year strategic plan and supporting annual business plans, discussed at paragraphs [54.](#) to [57.](#) We note that there are also other core strategies that need to be developed which will underpin any longer-term financial strategy, including the Scottish Rail Fleet Strategy and Fleet Procurement Strategy, discussed at paragraphs [58.](#) to [61.](#)

Significant capital investment from the Scottish Government will be required in future years to support the modernisation of the ScotRail Trains fleet

41. As highlighted in the Fleet Renewal and Decarbonisation section of SRH's [Strategic Plan 2024-2029](#): *"From approximately 2030 onwards, 65 per cent of the ScotRail fleet will either need to be life extended or replaced"*.

42. As discussed at paragraphs [58.](#) to [61.](#), SRH is working with Transport Scotland, and in close cooperation with Network Rail Scotland, to design, develop and implement a Scottish Rail Fleet Strategy and Fleet Procurement

Strategy. This is expected to be published by autumn 2025 but it is clear that significant capital investment from the Scottish Government will be required in future years to support the modernisation of the ScotRail Trains fleet, and to life extend the existing fleet until replacement fleets are procured.

3. 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.

SRH need to work with Transport Scotland to increase the pace of progress in establishing effective arrangements to oversee train operations in Scotland. This includes expediting the recruitment and appointment of staff to the vacant roles within SRH's approved organisational structure, to ensure the organisation has sufficient capacity and skills to effectively perform its duties.

SRH prepared a five-year Strategic Plan 2024-2029 and 2024/25 Business Plan. Management is now working to further develop these plans, including the oversight arrangements of rail services in Scotland from 2025/26.

SRH is working with Transport Scotland, and in close cooperation with Network Rail Scotland, to design, develop and implement a Scottish Rail Fleet Strategy and Fleet Procurement Strategy.

Management needs to strengthen SRH's governance arrangements, which includes holding regular meetings of the Audit and Risk Committee. SRH operated without an internal audit function during 2023/24 but appointed an interim Audit and Risk Manager in October 2024.

SRH need to work with Transport Scotland to increase the pace of progress in establishing effective arrangements to oversee train operations in Scotland

43. Scottish Rail Holdings Limited is an organisation controlled by Scottish Ministers that was set up with the express purpose of overseeing the governance of train operating companies under Section 30 of the Railways Act 1993.

44. We reported in our [2022/23 Annual Audit Report](#) that greater clarity was needed over the role of SRH in setting strategic policy for Scotland's rail services, and highlighted that this required all parties to work together to progress this as a matter of priority. We also reported that SRH was still to fully develop its oversight arrangements of SRT and CSL and it continued to develop its governance arrangements.

45. Our report noted that a government gateway review had been undertaken on behalf of Transport Scotland during 2023 to review the framework agreement to ensure it was fit for purpose and was delivering everything it was designed to. The resulting report was issued to Transport Scotland in July 2023 but this had not been shared with SRH. We therefore recommended that management should seek to obtain a copy of the gateway review and assess whether this includes any additional context or findings which could help inform the development of SRH.

46. SRH obtained a copy of the government gateway review report during 2024. This report included a range of “essential” recommendations to be taken forward by Transport Scotland and SRH. These recommendations largely reflect issues that we have also identified during SRH’s first two years of operation, and which have presented barriers to the organisation establishing effective arrangements to oversee train operations in Scotland.

47. While some progress has been made in addressing the recommendations in our 2022/23 report, and those arising from the government gateway review, a number of challenges remain, including staff capacity issues (discussed at paragraphs [48.](#) to [52.](#)), a need to strengthen SRH’s governance arrangements (discussed at paragraphs [64.](#) to [66.](#)), and action required to develop a framework to monitor and report on the performance of SRT and CSL (discussed at paragraphs [78.](#) and [79.](#)). It is essential that SRH work with Transport Scotland to increase the pace of progress in establishing effective arrangements to oversee train operations in Scotland.

SRH has recently appointed a permanent Chief Executive and filled other posts in its executive management team, but still face significant staff capacity issues across the organisation

48. We highlighted in our [2023/24 Annual Audit Plan](#) that staff capacity issues were impacting on SRH’s ability to review performance arrangements and provide effective financial and performance oversight of the delivery of rail services provided by SRT and CSL. Our plan also identified a further risk relating specially to the strategic leadership and management capacity of the organisation due to departure of the former interim Chief Executive and the former General Counsel and Company Secretary during 2024.

49. Following the departure of the former interim Chief Executive in June 2024, SRH operated with a new interim Chief Executive, who was seconded in from the Scottish Government. This arrangement continued until a permanent Chief Executive was appointed in September 2024. The interim Chief Executive has remained on secondment from the Scottish Government to SRH, and is now undertaking the role of Chief Operating Officer to help support the handover period and provide additional resource at senior management level.

50. SRH has also recently appointed a new permanent General Counsel, following the departure of the previous incumbent, and as well as appointing a new Finance Director. These appointments mean that SRH has now filled all of

the posts on its executive management team with permanent appointments other than the newly created Head of People post.

51. The SRH Board recently approved a new organisational structure which reflects its assessment of the staff numbers and skills required to enable it to effectively perform its duties in overseeing train operations in Scotland. This structure comprises 29 posts (including the Chief Executive, 3 Executive Directors and Head of People) split across the Rail Business Director (20 posts), the Finance Director (5 posts) and the General Counsel (2 posts). This includes 10 new posts that were not in the SRH organisational structure at the time of mobilisation.

52. We noted that of the 29 posts in the new organisational structure, only 20 are filled with a permanent member of staff, and 6 are currently vacant. We are also aware that in order for SRH to make permanent appointments to these posts it will require approval from Transport Scotland, and in some circumstances the Accountable Officer within the Scottish Government's Transport Division.

53. There is an urgent need to address staffing levels and capability within SRH to ensure it can provide adequate oversight of the rail operators.

Recommendation 5

SRH should work with Transport Scotland and the Scottish Government to expedite the recruitment and appointment of staff to the vacant roles within its approved organisational structure, to ensure the organisation has sufficient capacity and skills to effectively perform its duties in overseeing rail services in Scotland.

SRH prepared a five year Strategic Plan 2024-2029 and 2024/25 Business Plan. Management is now working to further develop these plans, including the oversight arrangements of rail services in Scotland from 2025/26.

54. SRH's framework agreement with Scottish Ministers, acting through Transport Scotland, requires it to prepare a five year strategic plan setting out strategic objectives, expenditure plans, performance indicators, and other key information to support it in exercising its role in overseeing the delivery of rail services in Scotland.

55. In October 2024 SRH published its first five year [Strategic Plan](#) covering the period 2024-2029. This set out SRH's vision and objectives that will enable it contribute to the priorities of the [National Transport Strategy](#) to reduce inequalities, take climate action, help deliver inclusive growth and improve health and wellbeing.

56. The strategic plan is supported by an annual Business Plan with the first version developed for 2024/25. The business plan set out SRH's focus on

making sure it has the capability to provide effective oversight of both SRT and CSL to ensure that the rail service provided meets the needs of passengers and the expectations of Scottish Ministers.

57. Management acknowledge that these plans are the first step towards establishing effective oversight arrangements of rail services in Scotland. The preparation of the next business plan, and annual refresh of the five year strategic plan, is underway which will further develop the oversight arrangements of rail services in Scotland from 2025/26.

SRH is working with Transport Scotland, and in close cooperation with Network Rail Scotland, to design, develop and implement a Scottish Rail Fleet Strategy and Fleet Procurement Strategy

58. An important aspect of SRH's Strategic Plan 2024-2029 is its approach to Fleet Renewal and Decarbonisation. This highlights that: *"From approximately 2030 onwards, 65 per cent of the ScotRail fleet will either need to be life extended or replaced. As well as supporting the crucial decarbonisation policy objective, this opportunity will be used as a business transformation - driving efficiencies and reductions in operational costs and developing the new fleet specifications to support passenger growth initiatives."*

59. The plan identifies that a key element of this will be SRH working with Transport Scotland, and in close cooperation with Network Rail Scotland, to design, develop and implement a Scottish Rail Fleet Strategy and Fleet Procurement Strategy, to support the replacement of life-expired fleets. This will also need to be coordinated with other Scottish Government infrastructure programmes.

60. An essential element of the new Scottish Rail Fleet Strategy will be that it supports the Scottish Government's decarbonisation plans for transport services in Scotland. The Scottish Government's updated Climate Change Plan is due to be laid before parliament early in 2025 and is expected to pass in to legislation by March 2025. Following this, Transport Scotland will publish a Rail Service Decarbonisation Action Plan. The fleet strategy is being developed in parallel with these plans and SRH therefore anticipate being able to publish the strategy by autumn 2025.

61. The fleet strategy will include the procurement of the replacement for the High Speed Train fleet which operates on intercity routes between Glasgow, Edinburgh, Aberdeen, and Inverness; which was [announced by the Cabinet Secretary for Transport in September 2024](#).

Management needs to strengthen SRH's governance arrangements, which includes holding regular meetings of the Audit and Risk Committee

62. We reported on the importance of SRH establishing effective governance arrangements in our [2022/23 Annual Audit Report](#) and this remained an issue during 2023/24.

63. During 2022/23 SRH established an Audit and Risk Committee to monitor issues of risk, control, and governance and associated assurance through a process of constructive challenge. The ARC remit includes monitoring and reporting to the Board on the planned activity and results of both internal and external audit, including the adequacy of management response to issues identified by audit activity. The ARC is also responsible for reviewing the accounting policies, the accounts and annual report of the organisation.

64. Despite the ARC's important role in the effective operation of SRH's governance arrangements, we noted that it only met twice during 2023/24, in May and December 2023, with the December meeting focussed entirely on the approval of the 2022/23 Annual Report and Accounts.

Recommendation 6

Management should agree a timetable of Audit and Risk Committee meetings, and a procedural timetable for the issue of committee papers, that supports non-executive members in undertaking their role and fulfilling the committee's remit.

65. Management acknowledged that SRH's governance arrangements required to be strengthened and had committed to reviewing these during 2024 but this review was deferred due to the departure of the General Counsel in June 2024. The review has now commenced and is being led by the Chair of the Audit and Risk Committee with support from officers including the interim Audit and Risk Manager. Amongst the wider governance areas where SRH has already identified improvement will be required are:

- Progressing improvements to ensure a more consistent and systemic approach across the group to risk identification, assessment, mitigation and reporting.
- Reviewing existing arrangements to ensure SRH's approach to information security, data protection and records management is consistent with best practice.
- Progressing a range of organisational improvements to ensure SRH has the right organisational structures and sufficient staff with appropriate skills and capacity to deliver against its objectives.

- Continuing to develop and further embed arrangements in place for monitoring and reporting on progress implementing the Strategic Plan and Annual Business Plan.

66. We will review the outcome of the review of governance arrangements as part of our 2024/25 audit.

SRH operated without an internal audit function during 2023/24 but appointed an interim Audit and Risk Manager in October 2024

67. SRH operated without an internal audit function during 2022/23 and we recommended in our [2022/23 Annual Audit Report](#) that management should determine what internal audit coverage and assurance is required for SRH single-entity functions, based on the review and development of SRH responsibilities.

68. During 2024 SRH obtained approval to appoint an Audit and Risk Manager but this post remained vacant until an interim Audit and Risk Manager was appointed in October 2024. As a result, SRH operated without any internal audit function for the duration of 2023/24. However, following the appointment of the interim Audit and Risk Manager, the ARC approved a proposal for him to undertake some limited substantive testing of a sample of transactions across key financial processes to provide some limited additional and independent assurance on these activities. No significant issues were identified through this work. He also established certificates of assurance to enable executive directors within SRH, and relevant officers from SRT and CSL, to provide the Chief Executive, as Accountable Officer, with assurances over the operation of the single entity and group governance arrangements and systems of internal control during 2023/24.

69. From 2024/25, SRH's review of effectiveness of its governance arrangements will be informed by the work and annual opinion of the Audit and Risk Manager.

70. In addition to the Audit and Risk Manager's work to support the review of governance arrangements for the Governance Statement in the SRH 2023/24 Annual Report and Accounts, he has also been implementing procedures and steps to establish an Internal Audit function and provide the SRH Group with assurance over its operations. Alongside this he is helping to progress a range of other activity across the organisation including improvements to risk management arrangements. The impact of this appointment in a relatively short period of time illustrates the importance of SRH appointing staff to the vacant posts within its approved organisational structure as soon as possible (discussed at paragraphs [48.](#) to [52.](#)).

Management is taking action to develop and review key policies and procedures to support the effective operation of the organisation

71. We highlighted in our [2023/24 Annual Audit Plan](#) that SRH required to develop or review a range of key policies and procedures to support the effective operation of the organisation. There were delays in developing these during 2024 due to resourcing and capacity issues, but we noted that the Board recently approved a whistleblowing policy and staff code of conduct. Management has also advised that work to develop a risk management framework is underway, along with plans to refresh the organisation's people policies during 2025.

SRH should review its cyber security arrangements and training to ensure the organisation is as prepared as possible for any potential cyber-attacks

72. Given the increased prevalence of cyber-attacks on public sector bodies, including successful attacks on [Comhairle nan Eilean Siar \(Western Isles Council\)](#) and [NHS Dumfries and Galloway](#) over the last 18 months, it is vital that public sector employees can recognise and mitigate cyber risks and that organisations have suitable plans in place to respond to cyber-attacks. Cyber security training for all staff is a key aspect of how organisations can support employees to do this and to foster a culture of vigilance and resilience that will help minimise human error, reduce breaches, and safeguard sensitive data and assets. Robust business continuity and disaster recovery plans, including a well tested Cyber Incident Response plan, are essential for an organisation to be able to respond to any cyber-attack and minimise its impact.

Recommendation 7

SRH should review its cyber security arrangements and training to ensure the organisation is as prepared as possible for any potential cyber-attacks.

A steering group has been established to oversee the development of CSL's back-office systems which require to come in to operation by June 2025

73. As part of the transition arrangements following the Caledonian Sleeper train services being brought into public ownership in June 2023, CSL have been utilising back-office systems and support services provided by Serco (the previous franchisee). However, this arrangement is due to expire in June 2025 and CSL are required to put in place alternative arrangements from this date.

74. A Steering Group has been established to oversee the work carried out by the programme team as CSL develop their own systems and establish processes to deliver back-office services. This is essential to ensure there is no disruption to CSL services when the current agreement with Serco ends.

75. Management has advised that this work is on schedule to be completed in advance of the June 2025 transfer date. We will monitor and report on the delivery of this as part of our 2024/25 audit.

4. 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.

SRH has still to develop a Best Value framework. It also needs to review the suite of key performance indicators reported to the board to ensure these support it in effectively monitoring the performance of SRT and CSL, and assist it in driving improvements and efficiencies in the delivery of rail services in Scotland in the future.

SRH has still to develop a Best Value framework

76. [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.

77. We highlighted in our [2022/23 Annual Audit Report](#) that due to SRH's unique role in overseeing the delivery of rail services in Scotland, the Chief Executive, as Accountable Officer, should establish how it can demonstrate that it is securing best value in the delivery of these services. Action has still to be taken in this area but we would expect that the development of a full suite of KPIS for monitoring and reporting on the performance of SRT and CSL, discussed at paragraphs [78.](#) and [79.](#), would go a long way to addressing this recommendation.

SRH should review the suite of key performance indicators reported to the board to ensure these support it in effectively monitoring the performance of SRT and CSL, and assist it in driving improvements and efficiencies in the delivery of rail services in Scotland in the future

78. The tripartite ScotRail grant agreement between Scottish Ministers, SRH and SRT and the Caledonian Sleeper service tripartite grant agreement between Scottish Ministers, SRH and CSL, sets out the conditions of the train operator arrangements. These agreements were largely based on the previous franchise agreements but make it clear that SRH is expected to provide oversight of SRT and CSL's delivery of rail services and to monitor and report on performance, including financial performance.

79. While a number of KPIs for monitoring the performance of SRT and CSL are included within the Framework and Grant Agreements specified by Transport Scotland, SRH need to review the KPIs beyond those specified by these agreements to ensure they have an effective framework to monitor key aspects of performance and policy delivery, and drive improvements. Management has advised that they are in the process of developing their oversight arrangement of the subsidiaries. As SRH review their Strategic Plan and Business Plan in 2025, they should review the suite of key performance indicators reported to the board. This will support SRH to fulfil its oversight role to monitor and report on SRT and CSL's performance, and assist it in driving improvements and efficiencies in the delivery of rail services in Scotland in the future.

Recommendation 8

SRH should review the suite of key performance indicators reported to the board to ensure these support it in effectively monitoring the performance of SRT and CSL, and assist it in driving improvements and efficiencies in the delivery of rail services in Scotland in the future.

Appendix 1. Action plan

2023/24 recommendations

Issue/risk	Recommendation	Agreed management action/timing
<p>1. Group consolidation</p> <p>A significant number of audit adjustments and classification issues were identified as part of our audit of the group consolidation working papers. The extent of the changes required was in large part due to the late receipt of fully complete accounts from the subsidiary bodies and the need for a large volume of consolidation adjustments to align the accounting treatment of SRT and CSL with those of SRH.</p> <p>Risk: There are errors in the SRH group statements.</p>	<p>Management should work with SRT and CSL finance teams to agree a timetable that ensures the component bodies 2024/25 accounts are available in time for consolidation in the SRH 2024/25 annual report and accounts presented for audit. Management should also ensure that FReM accounting requirements are adopted by the component bodies wherever possible to reduce the volume of consolidation adjustments required.</p> <p>Paragraphs 9. and 10. / Issue 2 in Exhibit 3</p>	<p>SRH will agree a group reporting timetable to ensure subsidiary deliverables are received in sufficient time to present the consolidated SRH 2024/25 annual report and accounts for audit.</p> <p>SRH Audit & Risk Committee to consider and agree approach to FReM accounting requirements for the subsidiaries for 2024/25.</p> <p>Responsible officer: Finance Director</p> <p>Agreed date: 31 March 2025</p>
<p>2. Accounting treatment of SRT and CSL accrued income grant funding</p> <p>SRT and CSL will require to recognise receivables balances due from SRH at 31 March each year in respect of services delivered during 2023/24 that funding has not been provided for during the year.</p> <p>Risk: The exact amounts due to SRT and CSL from SRH is not known in time for the production of the unaudited SRH accounts.</p>	<p>Management should establish a process that aligns with the SRH accounts preparation and closedown timetable, to identify the value of the outstanding grant funding due to the subsidiaries at 31 March for rail services delivered during the year.</p> <p>Issue 1 in Exhibit 3</p>	<p>Agreed timetable for Issue 1 above to include process and deadline for SRT and CSL to confirm accrued grant funding balances at 31st March each year.</p> <p>Responsible officer: Finance Director</p> <p>Agreed date: 31 March 2025</p>

Issue/risk	Recommendation	Agreed management action/timing
<p>3. Segmental reporting</p> <p>The FReM includes specific segmental reporting requirements for public sector bodies in the UK which reflect the requirements of IFRS8 – Operating Segments. These were not included in the SRH accounts presented for audit but we accepted a segmental analysis table being included in the financial performance section of the Performance Report in the audited SRH 2023/24 Annual Report and Accounts.</p> <p>Risk: SRH’s annual report and accounts do not include the required segmental analysis information.</p>	<p>Management should ensure they have all the information needed for the segmental reporting disclosures required for the SRH 2024/25 Annual Report and Accounts.</p> <p>Issue 3 in Exhibit 3</p>	<p>Lessons learned sessions to be held with key stakeholders to further develop segmental reporting and agree deliverables.</p> <p>Responsible officer: Finance Director</p> <p>Agreed date: 31 March 2025</p>
<p>4. Group budget monitoring and reporting arrangements</p> <p>There is an opportunity for SRH to prescribe the format and contents of the management accounting information it requires from SRT and CSL to better support its role in monitoring the financial performance of the subsidiaries, and to streamline the group budget monitoring and reporting processes.</p> <p>Risk: The SRH finance team is not able to accurately or quickly assess the consolidated group position during the course of the year.</p>	<p>Management should establish what budget monitoring information they require from SRT and CSL for each period to better support its monitoring of the financial performance of the train operators, and to streamline the group budget monitoring and reporting processes.</p> <p>Paragraphs 23. to 26.</p>	<p>SRH to further develop subsidiary reporting packs to ensure all required budget monitoring information is provided on a periodic basis and refine the group’s consolidation model.</p> <p>Responsible officer: Finance Director</p> <p>Agreed date: 30 June 2025</p>

Issue/risk	Recommendation	Agreed management action/timing
<p>5. Staff capacity issues</p> <p>Of the 29 posts in the new SRH organisational structure, only 20 are filled with a permanent member of staff, and 6 are currently vacant.</p> <p>Risk: SRH lack sufficient capacity and skills to effectively perform its duties in overseeing train operations in Scotland.</p>	<p>SRH should work with Transport Scotland and the Scottish Government to expedite the recruitment and appointment of staff to the vacant roles within its approved organisational structure, to ensure the organisation has sufficient capacity and skills to effectively perform its duties in overseeing rail services in Scotland.</p> <p>Paragraphs 48. to 52.</p>	<p>The business case for the additional posts in the first tranche of the organisational structure (6 out of 10) has been submitted to the Sponsor for approval. Of these, SRH have been advised that two finance posts are being actively considered by Transport Scotland with the remaining four to be reviewed. The action and associated timescale for these posts is:</p> <ul style="list-style-type: none"> • Continue to support Transport Scotland in respect of their consideration of the business case for all six posts (timing: ongoing). • Advertise posts for recruitment (timing: immediate on receiving Transport Scotland approval). • Complete recruitment of two finance posts (timing: 31 May 2025). • Complete recruitment of remaining approved four posts and confirm Job Descriptions in light of the 2025-30 Strategy and 2025/26 Business Plan (timing: 31 July 2025). <p>The business case for the remaining posts (4 out of 10) in the organisational structure is to be submitted to Transport Scotland. The actions and timescales for these posts is:</p> <ul style="list-style-type: none"> • Confirm posts requirement on completion of capacity

Issue/risk	Recommendation	Agreed management action/timing
		<p>and capability review in context of the 2025-30 Strategy and 2025/26 Business Plan (timing: 31 January 2025).</p> <ul style="list-style-type: none"> • Confirm requirement for business case, and if required submit to Transport Scotland for review (timing: 28 February 2025). • Advertise posts for recruitment (timing: immediate on receiving Transport Scotland approval). • Complete recruitment (timing: 30 November 2025) <p>Responsible officer: Chief Executive</p> <p>Agreed date: See dates for each action above.</p>
<p>6. Audit and risk committee</p> <p>The ARC only met twice during 2023/24.</p> <p>Risk: The committee is not performing its important role in the effective operation of SRH's governance arrangements.</p>	<p>Management should agree a timetable of Audit and Risk Committee meetings, and a procedural timetable for the issue of committee papers, that supports non-executive members in undertaking their role and fulfilling the committee's remit.</p> <p>Paragraphs 62. to 66.</p>	<p>SRH management will agree with the SRH ARC Chair the timetable of meetings and a procedural timetable for the issues of committee papers.</p> <p>Responsible officer: Finance Director</p> <p>Agreed date: 31 March 2025</p>
<p>7. Cyber security</p> <p>There has been an increased prevalence of cyber-attacks on public sector bodies, including successful attacks on Comhairle nan Eilean Siar</p>	<p>SRH should review its cyber security arrangements and training to ensure the organisation is as prepared as possible for any potential cyber-attacks.</p>	<p>SRH will complete a self-assessment of existing cyber security arrangements for both the SRH single-entity function and the wider Group by 28 February 2025.</p>

Issue/risk	Recommendation	Agreed management action/timing
<p>(Western Isles Council) and NHS Dumfries and Galloway over the last 18 months. It is vital that public sector employees can recognise and mitigate cyber risks and that organisations have suitable plans in place to respond to cyber-attacks.</p> <p>Risk: SRH may not have adequate arrangements in place to prevent or respond to a cyber-attack.</p>	<p>Paragraph 72.</p>	<p>Actions determined from the review will be prioritised, and priority policy/training requirements will be put in place and delivered by 31 May 2025.</p> <p>SRH will develop and embed continual improvement policies to ensure SRH and the wider Group's commitment to improving its cyber security arrangements and alignment with best practice (timing: 30 September 2025)</p> <p>Responsible officer: General Counsel</p> <p>Agreed date: See dates per actions above.</p>
<p>8. Performance monitoring of rail operators</p> <p>While a number of KPIs for monitoring the performance of SRT and CSL are included within the Framework and Grant Agreements specified by Transport Scotland, SRH need to review the KPIs beyond those specified by these agreements to ensure they have an effective framework to monitor key aspects of performance and policy delivery, and drive improvements.</p> <p>Risk: SRH is not able to effectively monitor the performance of the rail operators.</p>	<p>SRH should review the suite of key performance indicators reported to the board to ensure these support it in effectively monitoring the performance of SRT and CSL, and assist it in driving improvements and efficiencies in the delivery of rail services in Scotland in the future.</p> <p>Paragraphs 78 and 79.</p>	<p>SRH will develop a suite of Key Performance Indicators to monitor the performance of SRT and CSL, and also suggest amendments to Transport Scotland on those contained in the Framework and Grant Agreements to ensure that the KPIs specified allow performance monitoring and reporting to be progressed in a meaningful and efficient manner.</p> <p>Responsible officer: Rail Business Director</p> <p>Agreed date: 30 April 2025</p>

Follow-up of prior year recommendations

Issue / recommendation	Agreed Action	Progress
<p>PY1. Internal audit provision</p> <p>Management is still to determine what internal audit coverage is required for the SRH single entity functions.</p> <p>Recommendation: Management should determine what internal audit coverage and assurance is required for SRH single-entity functions, based on the review and development of SRH responsibilities.</p>	<p>As part of refining its structure and people plans, SRH will be determining how to resource its internal audit requirements.</p> <p>Responsible officer: General Counsel</p> <p>Agreed date: 30 June 2024</p>	<p>Ongoing</p> <p>An interim Internal Audit and Risk Manager was appointed in October 2024 and has been implementing procedures and steps to establish an Internal Audit function and provide the SRH Group with assurance over its operations. Further work is required to embed the internal audit provision within the organisation.</p> <p>Paragraphs 67. to 70.</p> <p>Revised action:</p> <p>Management have determined the internal audit scope and resource requirements for the SRH single-entity functions and the wider group. The required resources will be secured to deliver and embed the internal audit provision within the organisation.</p> <p>Responsible officer: Finance Director</p> <p>Revised date: 31 March 2025</p>
<p>PY2. Gateway review</p> <p>A government gateway review was undertaken on behalf of Transport Scotland in response to the requirement to review the framework agreement within 12 months of its commencement to ensure it is fit for purpose and is delivering everything it is designed to. However, SRH</p>	<p>SRH will request the gateway review to assess whether this has any important recommendations or findings which could inform the development of SRH.</p> <p>Responsible officer: General Counsel</p> <p>Agreed date: 31 March 2024</p>	<p>Completed</p> <p>SRH obtained a copy of the government gateway review report during 2024.</p> <p>Paragraphs 43. to 47.</p>

Issue / recommendation	Agreed Action	Progress
<p>has not yet seen the full results of this process.</p> <p>Recommendation: SRH should seek to obtain a copy of the gateway review and assess whether this has any additional context or findings which could help inform the development of SRH.</p>		
<p>PY3. Strategic Plan</p> <p>SRH's 5-year strategic plan has still to be finalised.</p> <p>Recommendation: Management should work with Transport Scotland to finalise SRH's 5-year strategic plan for overseeing the delivery of rail services in Scotland.</p>	<p>SRH is working with a variety of stakeholders, including Transport Scotland, to agree the SRH group strategy following the mobilisation of CSL and SRT.</p> <p>This strategy will be presented to Transport Scotland for approval in 2024.</p> <p>Responsible officer: Rail Business Director</p> <p>Agreed date: 30 September 2024</p>	<p>Completed</p> <p>SRH developed a five year Strategic Plan 2024-2029 and 2024/25 Business Plan. Management is now working to further develop these plans, including the oversight arrangements of rail services in Scotland from 2025/26.</p> <p>Paragraphs 54. to 57.</p>
<p>PY4. Staff capacity</p> <p>Since June 2023 SRH has been required to provide oversight of CSL's delivery of the sleeper service, while still providing similar oversight of the SRT rail services.</p> <p>Recommendation: Management should engage with Transport Scotland to agree what additional resource SRH requires to expand its capacity to enable it to review performance arrangements and to provide effective financial and performance oversight of the delivery of rail services provided by SRT and CSL.</p>	<p>SRH is in the process of refining its structure and people plan. It anticipates commencing the recruitment of additional permanent resources in 2024 once approval is obtained from Transport Scotland.</p> <p>As an interim measure, the SRH Board has authorised the recruitment of interim resources to improve its short term capacity.</p> <p>Responsible officer: Chief Executive Officer</p> <p>Agreed date: 31 March 2025</p>	<p>Ongoing</p> <p>SRH has recently appointed a permanent Chief Executive and filled other posts in its executive management team, but still face significant staff capacity issues across the organisation.</p> <p>Paragraphs 48. to 53. and Recommendation 5 above</p>

Issue / recommendation	Agreed Action	Progress
<p>PY5. Governance Arrangements</p> <p>Arrangements to support good governance have still to be fully established.</p> <p>Recommendation: The Audit and Risk Committee should continue to develop governance arrangements.</p>	<p>The SRH Audit and Risk Committee (ARC) will determine appropriate developments for the governance arrangements.</p> <p>Resourcing these arrangements will form part of the refinement of SRH's structure and people plans.</p> <p>Responsible officer: General Counsel</p> <p>Agreed date: 30 June 2024</p>	<p>Ongoing</p> <p>Management needs to take action to strengthen SRH's governance arrangements, which includes holding regular meetings of the audit and risk committee.</p> <p>Paragraphs 62. to 66. and Recommendation 6 above.</p>
<p>PY6. Best Value framework</p> <p>SRH has still to develop a Best Value framework.</p> <p>Recommendation: The Chief Executive should develop an appropriate Best Value framework for SRH, that reflects its developing role.</p>	<p>The SRH strategic plan that is being developed will include measures to demonstrate the value being delivered by the group and its constituent parts.</p> <p>Responsible officer: Chief Executive</p> <p>Agreed date: 30 September 2024</p>	<p>Not Implemented</p> <p>SRH has still to develop a Best Value framework.</p> <p>Revised action: SRH will develop a Best Value Framework.</p> <p>Responsible officer: Chief Executive</p> <p>Revised date: 30 June 2025</p>

Scottish Rail Holdings Limited

Annual Audit Report

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