

Scottish Natural Heritage

Report on the 2008/09 Audit

October 2009

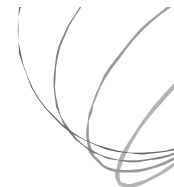


 AUDIT SCOTLAND



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Key messages

In 2008/09 we looked at the key strategic and financial risks being faced by Scottish Natural Heritage (SNH). We audited the financial statements and we also reviewed the use of resources and aspects of performance management and governance. This report sets out our key findings.

Financial statements

We have qualified our opinion on the financial statements of SNH for 2008/09, in relation to the limitation in scope of the audit work arising from uncertainty over the regularity of payments under management agreements entered into prior to 1 January 2000. During the year, SNH made payments of £1.3 million under these agreements, which in the absence of European sanction, may be deemed irregular.

With the exception of the pre 2000 management agreements, we have concluded that in all material respects, the expenditure and receipts shown in the financial statements were incurred or applied in accordance with applicable enactments and relevant guidance, issued by Scottish Ministers.

Financial position and use of resources

SNH had total resource budget of £70.657 million for 2008/09. The outturn for the year was an overspend of £2.7 million, or 3.8% of the overall resource budget. The overspend was caused by the revaluation of land and buildings during the year, which resulted in an impairment charge of £3.589 million. Approval for this overspend was secured from the Scottish Government during the financial year.

Scottish Ministers have agreed a resource budget for SNH of £65.850 million for 2009/10. This comprises operating expenditure of £63.770 million and capital expenditure of £2.080 million.

SNH achieved its 2% efficiency plan target for 2008/09 as defined in the grant in aid letter. These savings were achieved mainly through recurring savings arising from staffing efficiencies. In addition, a property disposal during the year generated a further £6 million saving. Future efficiency savings are set at 2% per annum, as part of the budget settlement from the Scottish Government for the next two years. The delivery of these efficiency savings together with other budget pressures in the medium term are a significant challenge for SNH.

Governance and accountability

Corporate Governance is concerned with the structures and process for decision making, accountability, control and behaviour at the upper levels of an organisation. Overall the corporate governance and control arrangements for SNH operated satisfactorily during the year, as reflected in the Statement on Internal Control.



We examined the key financial systems which underpin the organisation's control environment. We concluded that financial systems and procedures operated sufficiently well to enable us to place reliance on them.

Performance

SNH performed well during 2008/09 achieving 8 of the 9 targets agreed with Scottish Government. These targets are drawn from the Corporate Plan and are used to demonstrate SNH's contribution towards achievement of the Scottish Government's strategic objectives.

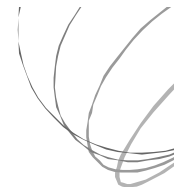
SNH does not anticipate achieving the missed target relating to bringing 95% of the special features on Scotland's nationally important nature sites into favourable condition by March 2010. At 31 March 2009, 78.4% of features were assessed as being in a favourable condition. This is an improvement on the prior year, however achieving the target of 95% by March 2010 seems unlikely for a variety of reasons, including the number of nature sites with no on-site remedy. We will continue to monitor SNH's performance arrangements and delivery against objectives.

Looking forward

The final part of our report notes some key risk areas and issues for SNH going forward. We highlight a number of national issues which affect other public sector bodies as well as SNH, including the impact of international financial reporting standards, efficiencies and future funding. In the current economic climate, public bodies face significant financial pressure over the next three years to achieve financial balance. We will continue to monitor financial planning arrangements and SNH's financial position.

The assistance and co-operation given to us by Board members and staff during our audit is gratefully acknowledged.

Audit Scotland
October 2009

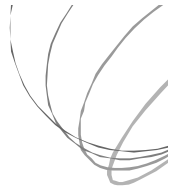


Introduction

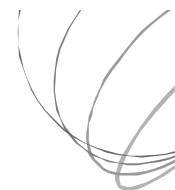
1. This report summarises the findings from our 2008/09 audit of SNH. The scope of the audit was set out in our Audit Plan, which was presented to the Audit and Risk Management Committee on 4 February 2009. This plan set out our views on the key business risks facing the organisation and described the work we planned to carry out on financial statements, performance and governance.
2. We have issued a range of reports this year, and we briefly touch on the key issues we raised in this report. Each report set out our detailed findings and recommendations and the Board's agreed response.
3. Best value duties apply across the public sector and, in central government, best value is a formal duty on all accountable officers. Audit Scotland has adopted a generic framework for the audit of best value across the public sector and throughout this report we comment on aspects of SNH's arrangements.

Exhibit 1: Framework for a best value audit of a public body





4. Our comments are made on the basis of information made available in the course of the annual audit. We do not make an overall best value judgement because we do not have enough evidence to conclude on all relevant areas. Our intention is to build up the corporate assessment over time. This report is the first step towards that goal.
5. Another building block for our assessment of best value is the national study programme carried out by Audit Scotland on behalf of both the Auditor General for Scotland and the Accounts Commission. We mention the key findings from all relevant reports, and the implications for SNH, throughout this report. Full copies of the study reports can be obtained from Audit Scotland's website, www.audit-scotland.gov.uk.
6. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by staff and board members of SNH during the course of our audit. This report will be submitted to the Auditor General for Scotland and will be published on our website.



Financial Statements

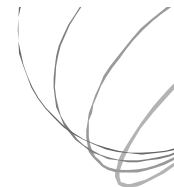
7. In this section we summarise key outcomes from our audit of SNH financial statements for 2008/09 and comment on the key financial management and accounting issues faced. The financial statements are an essential means by which the organisation accounts for its stewardship of the resources available to it and its financial performance in the use of those resources.

Our responsibilities

8. We audit the financial statements and give an opinion on:
- whether they give a true and fair view of the financial position of SNH and its expenditure and income for the period in question;
 - whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements;
 - the consistency of the information which comprises the Basis of Accounts, Statutory Background, Principal Activities, SNH Board and Management Team, Key Performance Targets, Results For the Year, Valuation of Land and Buildings, Transfer of Assets to the Isle of Rum Community Trust, Activities in the Field of Research and Development, Events After the Balance Sheet Date, Future Developments, State Aids, Supplier Payment Policy, Sustainable Development, Best Value, Corporate Diversity, Communication and Employee Involvement, Sickness Absence, Personal Data Related Incidents, Auditors, and Disclosure of Audit Information to the Auditors within the financial statements;
 - the regularity of the expenditure and receipts.
9. We also review the statement on internal control by:
- considering the adequacy of the process put in place by the Chief Executive as Accountable Officer to obtain assurances on systems of internal control;
 - assessing whether disclosures in the statement are consistent with our knowledge of SNH.

Overall conclusion

10. With the exception of the pre 2000 management agreements detailed in paragraph 14 below, we have concluded that in all material respects, the expenditure and receipts shown in the financial statements were incurred or applied in accordance with applicable enactments and relevant guidance, issued by Scottish Ministers.



11. As agreed the unaudited accounts were provided to us on 29 May 2009, supported by a comprehensive working paper package. The continued good standard of the supporting papers and timely responses from SNH staff allowed us to conclude our audit within the agreed timetable and provide our opinion to the Audit and Risk Management Committee on 30 July 2009 as timetabled.

Issues arising from the audit

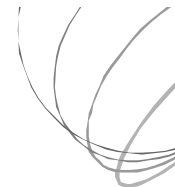
12. Auditing standards require us to report the main issues arising from our audit of the financial statements to those charged with governance. On 30 July we reported to the Audit and Risk Management Committee that other than the regularity qualification noted in paragraph 14, there were no significant issues identified.

Regularity

13. The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors that requires us to certify that, in all material respects, the expenditure and receipts shown in the accounts were incurred or applied in accordance with applicable enactments and guidance issued by the Scottish Ministers. We have been able to address the requirements of the regularity assertion through a range of procedures, including written assurances from the Accountable Officer as to his view on adherence to enactments and guidance.
14. We have given a qualified opinion on the financial statements of SNH for 2008/09, in relation to the limitation in scope of the audit work arising from uncertainty over the regularity of payments under management agreements entered into prior to 1 January 2000. In 2001, the European Commission confirmed that UK nature conservation management agreements entered into after 1 January 2000 were allowable as state aid. However no ruling has yet been made regarding retrospective approval of management agreements entered into prior to 1 January 2000. During 2008/09 Scottish Natural Heritage spent approximately £1.3 million under pre-January 2000 agreements which, in the absence of European sanction, may be deemed irregular, as in previous years.

International financial reporting standards (IFRS)

15. As announced by the Chancellor in the 2008 Budget report on 12 March 2008 (Budget report paragraph C103), Government departments and other public sector bodies will report using International Financial Reporting Standards (IFRS) from 2009/10. The Scottish Government announced on 25 April 2008 that all Scottish Government Departments, Executive Agencies, Health Bodies and Non-Departmental Public Bodies would be required to produce shadow IFRS based accounts for financial year 2008/09. This was to include a restated balance sheet as at 1 April 2008.



16. In terms of the audit of the IFRS opening balance sheet at 1 April 2008, there were two key dates to achieve as outlined below, both of which were achieved:
- **28 November 2008** – opening 2008 IFRS-based balance sheet were to be presented to auditors for dry-run audit
 - **28 February 2009** – dry-run audit of opening balances was to be completed, resulting in a letter to management highlighting the work done, auditors' findings and areas for further work.
17. We made some recommendations for the delivery of the next stage of IFRS reporting – the production of the shadow accounts for 2008/09, and will consider progress on these when we review the shadow accounts later in 2009. These included:
- **Partners** - SNH enter into several types of funding arrangements with other bodies to achieve shared objectives. These arrangements are currently accounted for as grant funding under UK GAAP. Under IFRS, some of these arrangements could potentially be accounted for as subsidiaries, associates or joint ventures, depending on the framework agreement in place. SNH are currently reviewing these arrangements to determine whether the current accounting treatment is appropriate
 - **Intangible assets** – the opening balance sheet should be adjusted to reflect the transfer of £278,000 componentised software costs from tangible to intangible assets. This amendment will be reflected in the 2008/09 shadow accounts.
 - **Non-current assets** – the split of current and non-current assets in the opening balance sheet is to be adjusted for the £60,146 long term debtor error identified.
 - **Liabilities** - the analysis of provisions into current and non-current liabilities should be completed and reflected in the opening balance sheet.
 - **Segmental reporting** – IFRS 8 requires that financial information is reported on the same basis as that used internally for allocating resources and evaluating performance. Scottish Natural Heritage is considering the implications of recording and reporting segmental information as part of the shadow accounts.



Use of Resources

18. Sound management and use of resources (people, money and assets) to deliver strategic objectives is a key feature of best value. This section sets out our main findings from our review of SNH.

Financial Position

Outturn 2008/09

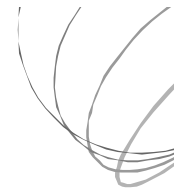
19. SNH is required to work within its resource budget set by the Scottish Government. SNH is expected to ensure that, taking one year with another, income from Grant in Aid and charging schemes, equals expenditure. For 2008/09 SNH had a deficit of £2.7 million. This is the difference between the operating cost for the year of £73.357 million and the funding received from the Scottish Government of £70.657 million.
20. SNH's balance sheet at 31 March 2009 shows net assets of £27.872 million (2007/08 net assets of £27.904 million).
21. SNH operated within the resource budget limits set by the Scottish Government – see exhibit 2 below. The deficit was caused by the impairment charges on revalued land and buildings. Approval for this deficit was secured from the Scottish Government during the financial year.

Exhibit 2 – Performance against resource budget 2008/09 (£ million)

Limits	Budget	Actual Outturn	Difference
Non Cash Expenditure	3.564	7.051	(3.488)
Cash	67.093	66.305	0.788
Total	70.657	73.357	(2.700)

Financial sustainability and the 2009/10 budget

22. Scottish Ministers have agreed a resource budget for SNH of £65.850 million for 2009/10. This comprises an operating budget of £59.991 million, capital allocation of £2.080 million and non-cash resources of £3.779 million to cover depreciation charges and notional interest costs.
23. In previous years, the profile of expenditure in SNH has been skewed towards the end of the financial year. This puts pressure on the management of spend, and increases the risk of error or control failure. To address this, SNH has profiled the 2009/10 budget to include earlier spend, and set



commitment targets for each quarter of the financial year. Current estimates show an over-commitment of expenditure, which will be managed back through the financial year.

24. SNH is expected to achieve a minimum 2% recurring efficiency savings in 2009/10 and 2010/11. SNH has currently set targets of £2.786 million and £3.820 million respectively and this is reflected in the budget agreed with Scottish Ministers.

National Studies

25. Audit Scotland published two national studies relevant to SNH's use of resources. These were use of consultancy services and improving energy efficiency.

Use of consultancy services

26. The overall aim of the study was to review central government's use of consultancy services and to make recommendations to improve the public sector's use of consultants' knowledge, skills and resources to help deliver new services and initiatives quickly and expertly. The key findings were as follows:
 - The public sector is strengthening the way it buys goods and services
 - Central government does not have a clear strategy for its use of consultants or for linking use to its priorities or financial and workforce plans
 - In most cases, central government buys consultancy services well but some improvements can be made
 - Central government could improve how it manages consultancy projects through more consistent and formal evaluation of consultants' work and learning more from them
 - Central government could make savings of up to £13 million a year through better planning and buying of consultancy services.
27. The report made specific recommendations for public bodies:
 - confirm they have clear processes for approving and recording the use of consultants and monitoring progress, and reinforce these as required
 - plan their use of consultancy services when developing their forward work programme to ensure that consultants are used where their knowledge and skills bring greatest value for money
 - always evaluate the option to use consultants against the option to use their own staff



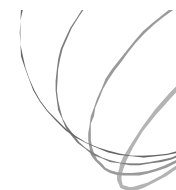
- gather and share consistent information on the consultancy skills bought and why consultants are used
- improve the quality of their invitations to tender through better and earlier discussion with consultants about their consultancy needs
- increase the use of framework agreements where possible by ensuring that existing agreements are used and new ones developed as appropriate
- select and use the most economical competition routes by using framework agreements, restricted competitions and closed tendering approaches when appropriate
- evaluate the work of consultants more systematically and share findings from these reviews
- work closely with consultants to increase assurance on quality and make use of opportunities to learn from consultants and ensure knowledge transfer, where appropriate.

28. In 2008/09, SNH incurred consultancy costs of £0.603 million, less than 1% of gross expenditure. The current procurement arrangements are considered to be appropriate and sufficient for buying-in consultancy services and no specific action is considered necessary by SNH in response to the findings of the study.

Improving energy efficiency

29. Audit Scotland assessed how councils, NHS bodies and central government bodies were improving energy efficiency in relation to buildings and transport use. This included examination of a range of issues including whether public bodies demonstrate commitment to improving energy efficiency; how public bodies are performing against their objectives and targets for improving energy efficiency; and if public bodies are delivering continuous improvement in this area.

- Funding has been made available by the Scottish Government and public bodies to improve energy efficiency. While energy consumption in buildings has fallen, spending on energy increased in the three years to 2006/07
- There is a need for stronger leadership by the Scottish Government and within public bodies to improve energy efficiency and ensure that the necessary cultural and behavioural changes are made
- A robust strategy is central to the coordination of activities to improve energy efficiency, however, there are inconsistencies in the quality of strategies being implemented
- There is a lack of formal monitoring and reporting of progress in improving energy efficiency by public bodies and the Scottish Government.



30. SNH currently operates an environmental management system that monitors progress in reducing environmental impact against a range of targets. An annual greening report has been produced for 2008/09, setting out key environmental achievements for the year and targets going forward. The national study reinforced existing policies and procedures within SNH, and no specific action is considered necessary in response to the study findings.

Delivery of efficiencies

31. In June 2004, the Scottish Executive launched the Efficient Government Initiative. The initiative aspired to achieve £1.5 billion of efficiency savings by 2007/08 and reported efficiency savings of £1.7 billion. In November 2007 the Scottish Government announced the Efficient Government Programme 2008/09 – 2010/11, setting out its target to deliver cash-releasing efficiency savings amounting to £1.6 billion in 2010/11.
32. To achieve this level of savings the Scottish Government set portfolios a target of two percent cash-releasing savings – producing the same outputs with fewer inputs – for each of the three financial years. Public bodies will therefore need to be able to deliver year on year efficiency savings and contribute to the achievement of these portfolio savings targets.
33. As part of Audit Scotland's performance audit programme a national study on the delivery of efficiencies within the Scottish public sector is being undertaken. The study will provide an overview of the Scottish Government's Efficient Government Initiative 2005/06 – 2007/08 and consider the extent to which public bodies are set up to deliver year on year efficiency savings.
34. To assess the readiness and ability of public sector bodies to deliver year on year efficiency savings Audit Scotland undertook fieldwork across central government, the NHS and councils, with five bodies selected from each.
35. The fieldwork was carried out during March and April, including interviews with senior officers and analysis of supporting documentation. The fieldwork used Audit Scotland's Best Value Efficiency Toolkit. The toolkit is a document specifically created to enable auditors and public sector bodies to assess the efficiency arrangements in place within an organisation. The fieldwork assessed the arrangements for monitoring and measuring efficiencies and how public bodies seek to ensure that reported savings have been delivered without affecting service delivery.
36. Audit Scotland's national report will be published in late 2009.



Governance and Accountability

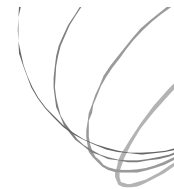
37. High standards of governance and accountability, with effective structures and processes to govern decision-making and balanced reporting of performance to the public, are fundamental features of best value. This section sets out our findings arising from a review of SNH's arrangements.
38. Increasingly services are being delivered across the public sector through partnership working, sometimes involving complex governance and accountability arrangements. Best value characteristics also include effective partnership working to deliver sustained improvements in outcomes.

Overview of arrangements

39. This year we reviewed:
- partnership working
 - key systems of internal control
 - internal audit
 - arrangements for the prevention and detection of fraud and irregularity, including standards of conduct.
40. Our overall conclusion is that arrangements within SNH are sound and have operated effectively through 2008/09.

Partnership working

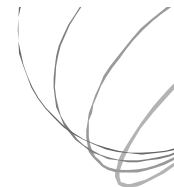
41. In June 2007 Ministers challenged the organisations delivering the rural affairs and environment portfolio to create a single environment and rural delivery service (SEARS). SEARS brings together nine delivery-focused bodies within the Environment and Rural Affairs sector to provide more joined-up services, initially to rural land managers.
42. The three principles of public service delivery are at the heart of the SEARS approach:
- user focus – putting the person and not the institution first
 - effectiveness – focusing on real improvements in public value through services delivered for the people of Scotland
 - value for money – making sure that each and every public pound is spent wisely.



43. SEARS is a partnership approach and it is therefore vital that the SEARS partners have a clear understanding of their responsibilities, with clear lines of accountability. To ensure this a memorandum of agreement, setting out the framework for the partnership, was agreed by the SEARS Programme Board in March 2008.
44. SEARS is a commitment to working in a joined-up way. The Annual Review 2008/09 notes that during the first year since the partnership was launched it has:
- carried out 2,000 fewer inspections or visits to land managers ahead of the October 2009 target
 - saved the sheep farming industry around £150,000 in groundwater license charges through SEPA waiving the second instalment of the annual charge for 2008/09
 - introduced a 24/7 contact centre and established the SEARS web portal
 - given land managers the opportunity to change their personal information with the nine bodies within the Environment and Rural Affairs sector through single contact, thereby reducing duplication
 - improved the co-ordination of communication between the SEARS partners
 - co-located SNH, SGRPID and FCS, along with staff from Highlands & Islands Enterprise and Community Energy Scotland in a new office in Golspie.
45. SEARS is currently exploring the following areas for further development including reducing bureaucracy, further co-locations, sharing services and linking the natural and built environment. SNH continues to be an active partner in the group, particularly in terms of co-location and sharing services, with Cairngorms National Park Authority utilising SNH information technology infrastructure. Discussions are also ongoing with Loch Lomond and the Trossachs National Park Authority with a view to providing them access to SNH health and safety expertise.

Systems of internal control

46. Key controls within systems should operate effectively and efficiently to accurately record financial transactions and prevent and detect fraud or error. This supports a robust internal control environment and the effective production of financial statements. In his annual report for 2008/09 the head of audit and consultancy services provided his opinion based on the internal audit work undertaken during the year, and concluded that the programme of internal audits in 2008/09 has offered reasonable assurance that SNH continues to have a broadly sound framework of internal controls.



47. As part of our audit we reviewed the high level controls in a number of SNH's systems that impact on the financial statements. Our overall conclusion was that key controls were operating effectively and that SNH has adequate systems of internal control in place.

Statement on Internal Control

48. The Statement on Internal Control provided by SNH's Accountable Officer reflected the main findings from both external and internal audit work. This recorded management's responsibility for maintaining a sound system of internal control and set out SNH's approach to this. Attention was drawn to some specific issues which are being addressed during 2009/10:
- **Security policy framework** – areas of non-compliance will be assessed for relevancy and significance of risk to SNH. Where applicable, improvement actions will be identified.
 - **Risk management** – although current arrangements are considered satisfactory, further training is planned to assist units in better identifying and communicating risks to operational delivery.

Internal Audit

49. The establishment and operation of an effective internal audit function forms a key element of effective governance and stewardship. We therefore seek to rely on the work of internal audit wherever possible and as part of our risk assessment and planning process for the 2008/09 audit we assessed whether we could place reliance on SNH's internal audit function. We concluded that the internal audit service operates in accordance with the Government Internal Audit Manual and therefore placed reliance on their work in number of areas during 2008/09, as we anticipated in our annual audit plan. This included reliance on aspects of internal audit's systems work to avoid duplication of effort.

Prevention and detection of fraud and irregularities

50. SNH has appropriate arrangements in place to prevent and detect fraud, inappropriate conduct and corruption, including policies and codes of conduct for staff and Board members. During the year, a procedural breach in the use of a Government Procurement Card was identified. Following investigation it was established that no fraud had occurred and appropriate action was taken to prevent further breaches.

National Studies

51. Audit Scotland published one national study relevant to SNH's use of resources. This was a review of major capital projects.



Major capital projects

52. This report was the first systematic review of major capital projects in Scotland. It considered the progress of all 43 projects completed in the five years between April 2002 and March 2007, and a sample of current major projects. It looked at progress against cost and time estimates, quality specifications and project management in general. The main findings from the report were as follows:
- In general, the achievement of cost and time targets improved significantly as projects progressed
 - Early cost and time estimates at project approval stage were too optimistic for many major projects
 - Performance against cost and time estimates is better after contracts are awarded, as plans are more certain and risks clearer
 - Most completed projects have successfully delivered the required roads, hospitals and other assets, and all current projects are forecast to do so. However, few projects have been evaluated to demonstrate that they have delivered the expected wider benefits which originally justified the investment
 - Nine current projects examined had awarded the main construction contract, which should increase cost certainty. However, four projects had significant increases in estimated cost before reaching this stage
 - Project management and governance arrangements within individual projects are broadly effective, although room for improvement remains. A more strategic approach to managing the programme of capital projects could improve value for money.
53. SNH has in place a framework based on established project management methodologies. In recent years it has used this to deliver a number of significant projects on time and to budget, including the construction of Great Glen House and the new Golspie office. SNH should continue to review established arrangements against any emerging good practice.

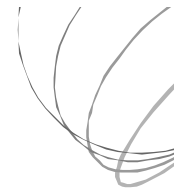


Performance

54. Public audit is more wide-ranging than in the private sector and covers the examination of, and reporting on, performance and value for money issues. Key features of best value include:
- setting a clear vision of what the organisation wants to achieve, backed up by plans and strategies to secure improvement, with resources aligned to support their delivery
 - a performance management culture which is embedded throughout the organisation and a performance management framework which is comprehensive and supports the delivery of improved outcomes.
55. In this section we comment on:
- SNH's corporate plan
 - performance against targets
 - performance management arrangements
 - SNH's efficiency programme

Vision and strategic direction

56. SNH's Corporate Strategy 2008 established the strategic framework for its 3 year corporate plan. The plan focuses on five key strategic priorities:
- Caring for nature
 - Responding to climate change
 - Delivering health and wellbeing
 - Supporting the Scottish economy
 - Delivering a high quality public service.
57. SNH has identified a set of actions which indicate how the body intends to take forward each strategic priority. These actions are set out in nine separate business planning programmes, which contribute to the achievement of the corporate strategy. Each programme sets out objectives, allocates funding and specifies measurable targets.



Performance overview

58. SNH has aligned its 5 strategic priorities with the Scottish Government's strategic objectives. Performance is measured regularly against 9 key targets that have been drawn from the Corporate Plan and agreed with Scottish Government, with quarterly reporting to the board.
59. SNH performed well during 2008/09, achieving 8 of the 9 agreed targets. The missed target relates to bringing 95% of the special features on Scotland's nationally important nature sites into favourable condition by March 2010. Quarterly milestones were set and monitored during the year, with steady progress resulting in 108 natural features benefitting from a change in management regime or activity. This raised the overall percentage of natural features in favourable condition to 78.4%, however further progress continues to be challenging. There are a number of features, including seabirds and some high mountain habitats, where factors such as the change in climate appear to be having an adverse effect. In this situation there is a limit to what can be achieved through any applied management regime. At the present time, there are 271 unfavourable features which have been categorised as having no on-site remedy. If these features were discounted, the proportion of sites in favourable condition would be 84%. We will continue to monitor SNH's performance arrangements and delivery against objectives.

Risk management

60. There are a number of key challenges and risks for SNH in delivering its strategic priorities. SNH has put in place robust systems for the identification and management of risk. Identified risks are monitored through its business planning database, with units undertaking monthly review of changes to risks. Key risks are reported regularly to Management Team, Audit and Risk Management Committee and the Board. Key risks identified include:
- **Government funding** – there is a risk of significant reduction in future grant in aid allocation. Management is reviewing organisational priorities and expenditure associated with future work, to evaluate the consequence of different levels of budget reduction.
 - **Staff workload** – a number of areas of the business have identified the workload pressures on staff as a high risk. Senior management in SNH are working with unit managers to establish the best approach to managing this risk.
 - **Pathway development** – the proposed establishment of new pathways will require additional resources and may displace other planned activity. SNH will liaise with other key partners around the proposals to develop a workable project plan.



Efficiency

61. SNH is required to deliver 2% cash-releasing efficiency savings within the three year spending review period of 2008/09 to 2010/11. This target has been met in the 2008/09 financial year through recurring savings of £1.9 million resulting from staffing efficiencies. In addition, a one-off property disposal during the financial year generated savings of £6 million.

62. The recurring savings identified in 2008/09 will contribute towards efficiencies over the coming years; however SNH is required to identify a further 2% cash savings in 2009/10 in addition to these. SNH expects to meet the 2009/10 efficiency target. Proposed measures to achieve this include co-location and sharing services with other SEARS and public sector partners. An Efficient Government Programme Board has been set up to monitor progress in this area. We will continue to monitor the financial position and the actions taken by SNH to manage these risks.

Looking Forward

63. SNH faces a number of challenges in 2009/10, which include:

- **Efficiencies and future funding** – In the current economic climate, budgets for 2009/10 and the immediate future will need to be managed within a tighter funding regime. This includes no scope for the application of end of year flexibility for the Government with HM Treasury until the next Spending Review; no option to transfer funds from capital to revenue; and the impact of the introduction of International Financial Reporting Standards (IFRS), particularly on leases and infrastructure accounting. The challenge for SNH is to review future commitments and prioritise spending to ensure delivery of key targets and objectives.
- **IFRS**- The timetable for IFRS implementation require central government accounts in Scotland to become IFRS compliant with effect from the 2009/10 financial year. As part of the timetable for the implementation of IFRS, shadow accounts will require to be produced for 2008/09 for audit review by the end of November 2009. These processes require significant resource to complete and SNH has developed a project plan to ensure successful delivery of both shadow accounts and IFRS compliant 2009/10 accounts.
- **Deer Commission Scotland** – The Public Sector Reform (Scotland) Bill, published in May 2009, includes provisions to transfer the functions of the Deer Commission for Scotland to SNH. This merger is intended to bring significant benefits to the deer sector in Scotland by bringing it alongside the range of wildlife management issues handled by SNH. The merger is scheduled for completion in July 2010 and a number of issues need to be progressed to meet this target. A DCS Merger Board has been established to oversee and manage this process, with three separate project strands covering legislation and sponsorship, organisational merger, and strategic integration. We will continue to monitor progress in this area, including the financial management and reporting arrangements covering the transfer period.
- **Isle of Rum** – The first phase of asset transfers to the Isle of Rum Community Trust was concluded in 2008/09, and a second phase involving housing stock is planned for early 2010. This second transfer will divest SNH from management responsibility for these non-service delivery assets, however they retain responsibility for Kinloch Castle until an independent charitable trust can be established, and the necessary capital funds become available. We will continue to monitor developments in this area.