



Scottish Arts Council

**Annual Report to Creative Scotland and
the Auditor General for Scotland
2009/10**

September 2010



Scottish Arts Council

Annual Report to Creative Scotland and the Auditor General for Scotland 2009/10

Executive Summary	1
Introduction	3
Financial position	4
Use of resources	9
Performance	11
Governance	13
Looking Forward	15
Appendix 1: Action Plan	17
Appendix 2: Audit Adjustments	24

Executive Summary

Financial Statements

Our audit opinion on the truth and fairness of the Scottish Arts Council (the Council) and the Scottish Arts Council National Lottery Distribution Fund (SAC NLDF) annual accounts and on the regularity of transactions is unqualified. The deadline for submitting final accounts will be achieved.

2009/10 was the first year that central government bodies were required to prepare financial statements under International Financial Reporting Standards (IFRS). As the Council has charitable status, it continued to prepare its financial statements under UK Generally Accepted Accounting Practices (UK GAAP). SAC NLDF however prepared its financial statements under IFRS. We are pleased to report that both sets of accounts have been prepared in accordance with the financial reporting frameworks.

Use of Resources

The Council incurred expenditure of £53.054m in 2009/10 (2008/09: £49.912m) and received income of £52.346m (2008/09: £48.871m) including grant-in-aid funding of £50.312m from the Scottish Government. Following adjustments for the disposal of the Council's interest in the Centre for Contemporary Arts and the reversal of notional interest, the overall effect was a decrease in the Council's reserves of £0.023m (2008/09: decrease £1.279m).

The SAC NLDF incurred expenditure of £20.421m in 2009/10 (2008/09: £30.127m) and received income of £19.893m (2008/09: £17.056m) including National Lottery Fund proceeds of 19.206m. The net impact was a decrease in the in the general fund of £0.550m. The SAC NLDF negative balance sheet position is the result of the over commitment of grants to third party organisations.

Governance

Creative Scotland became a Statutory Non Departmental Public Body (NDPB) on 1 July 2010, under the Public Services Reform (Scotland) Act. It replaces the Scottish Arts Council and Scottish Screen and has been established a single body responsible for overseeing Scotland's arts and culture sector. Both lottery funds' (SAC NLDF and SSNLDF) powers as a National Lottery Fund Distributor have been transferred to Creative Scotland under the National Lottery etc. Act 1993 (Amendment of Section 23) (Creative Scotland) Order 2010.

The Scottish Arts Council and Scottish Screen latterly operated under a Joint Board and related Committee structure, to facilitate a smooth transition to Creative Scotland. From January 2009 until the establishment of Creative Scotland, the Scottish Arts Council and Scottish Screen boards held individual and joint meetings to allow management to focus on both individual organisational responsibilities as well as joint working arrangements.

During 2009/10 the Scottish Arts Council worked towards the successful establishment of Creative Scotland whilst operating as business as usual in as many aspects as possible. This has enabled the transition to take place in accordance with ministerial plans.

Looking Forward

Creative Scotland has taken over the functions and resources of the Scottish Arts Council and Scottish Screen, as well as having a wider responsibility for developing the cultural sector as a whole. The transition to Creative Scotland will be accounted for as a Machinery of Government change. Interim accounts will have to be prepared for the intervening period 31 March 2010 and 30 June 2010.

Creative Scotland management, external audit and the Scottish Government are currently involved in agreeing the detailed requirements for this transition.

Conclusion

This report concludes the 2009/10 audit of the Scottish Arts Council and Scottish Arts Council National Lottery Distribution Fund. We have performed our audit in accordance with the Code of Audit Practice published by Audit Scotland, International Standards on Auditing (UK and Ireland) and Ethical Standards.

This report has been discussed and agreed with the Creative Scotland Head of Programme Management. We would like to thank all management and staff for their co-operation and assistance during our audit.

Scott-Moncrieff
September 2010

Introduction

1. This report summarises the findings from our 2009/10 audit of the Scottish Arts Council group (the Council) and Scottish Arts Council National Lottery Distribution Fund (SAC NLDF). The scope of our audit was set out in our External Audit Plan, which was presented to the Audit Committee at the outset of our audit.
2. The Auditor General for Scotland is responsible for reporting to the Scottish Parliament on how public bodies spend public money, manage their finances and achieve value for money in the use of public funds. In discharging this responsibility the Auditor General appoints central government auditors and sets the terms of their appointment. The Auditor General has appointed Scott-Moncrieff as auditors of the Council and the SAC NLDF for the five year period 2006/07 to 2010/11.
3. Audit Scotland is an independent statutory body that provides the Auditor General with the services required to carry out his statutory functions, including preparing a Code of Audit Practice setting out the role and responsibilities of the external auditor. With reference to the Code of Audit Practice, the main elements of our audit work in 2009/10 have been:
 - Audit of the financial statements, including a review of the Statement of Internal Control
 - Review of the 2008/09 SAC NLDF financial statements, restated under International Financial Reporting Standards (IFRS)
 - Review of governance arrangements, internal controls and financial systems
 - Follow-up of relevant national performance audit studies published by Audit Scotland

The key issues from these outputs are summarised in this annual report

4. This report is addressed to Creative Scotland and the Auditor General for Scotland and will be published on Audit Scotland's website, www.audit-scotland.gov.uk.

Financial position

Introduction

5. The financial statements are a key way the Council demonstrate stewardship of the resources made available to them. In this section we summarise the key outcomes from our audit of the 2009/10 financial statements for the Council and SAC NLDF. We also report on the work which we have undertaken on International Financial Reporting Standards (IFRS).

Our responsibilities

6. We audit the financial statements and give an opinion on:
 - whether they give a true and fair view of the financial position of the body and its expenditure and income for the year then ended;
 - whether they were prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements;
 - whether the information which comprises the management commentary in the Annual Report is consistent with the financial statements; and
 - the regularity of the expenditure and receipts.
7. We also review the Statement of 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; and
 - assessing whether disclosures in the statement are consistent with our knowledge of the Council.

Independence

8. International Standard on Auditing 260 – Communication of Audit Matters with those Charged with Governance – requires us to communicate on a timely basis all facts and matters that may have a bearing on our independence.
9. We provided no additional services to either the Council or SAC NLDF during the year and can confirm that we have complied with the Auditing Practices Board Ethical Standard 1 – Integrity, Objectivity and Independence. In our professional judgement the audit process has been independent and our objectivity has not been compromised.

Overall conclusion

10. We are pleased to report that our independent auditors' report expressed an unqualified opinion on the financial statements for the year ended 31 March 2010 (for both the Council and SAC NLDF) and on the regularity of transactions reflected in those financial statements. The annual

accounts will be submitted to the Scottish Government and the Auditor General for Scotland prior to the 31 October 2010 deadline.

11. The quality of the financial statements prepared by the Council is of a satisfactory standard. There is however scope to further improve the quality of the financial statements. During our review we noted a number of adjustments to be made to the disclosure and presentation of the accounts.

Action plan point 1

Accounts Direction

Scottish Arts Council

12. The Council is required, in preparing its financial statements, to comply with the directions given by Scottish Ministers. The Direction by Scottish Ministers requires the Council to comply with the accounting principles and disclosure requirements of the Government Financial Reporting Manual (FReM).
13. The 2009/10 FReM notes that non-departmental public bodies (NDPBs) that have charitable status, should comply with regulations issued under charities legislation and, where applicable, the Statement of Recommended Practice (SORP) Accounting by Charities. They should also follow the principles in the FReM and provide the additional disclosures (for example, on notional costs and salary and pension entitlements) where these go beyond the SORP.
14. We are pleased to report that the 2009/10 financial statements of the Scottish Arts Council comply with the 2009 edition of the FReM which was in force for the year when the statement of accounts were prepared and the Charities Statement of Recommended Practice (Charities SORP).

Scottish Arts Council National Lottery Distribution Fund

15. During 2009/10 Scottish Ministers issued a revised Accounts Direction for the Scottish Arts Council National Lottery Distribution Fund. The Accounts Direction requires the Scottish Arts Council to prepare a statement of accounts in respect of its National Lottery Distribution Activities which comply with the principles and disclosure requirements of the Government Financial Reporting Manual (FReM). The FReM requires bodies to apply international financial reporting standards (adapted and interpreted for the public sector context) for the first time in 2009/10.
16. We are satisfied that the SAC NLDF 2009/10 accounts comply with the requirements of the FReM in all material respects.

International Financial Reporting Standards (IFRS)

17. As noted above, SAC NLDF was required to prepare full IFRS-compliant financial statements for 2009/10. In January 2010 we undertook a review of the 2008/09 SAC NLDF accounts, restated on an IFRS basis, and reported our findings and recommendations to the Audit Committee. The

report confirmed that SAC NLDF had successfully restated the 2008/09 financial statements, as required.

18. We are pleased to report that the 2009/10 financial statements have been prepared in accordance with IFRS.

Audit Adjustments

19. Appendix 2 outlines the adjustments made over the course of the audit review to the Council and SAC NLDF financial statements. All adjustments were agreed with the Creative Scotland Head of Programme Management and both sets of financial statements have been amended to reflect these adjustments. The net effect on the financial statements is as follows:

Table 1: Impact of Audit Adjustments on Financial Position

	Council £'000	SAC NLDF £'000
Net deficit for the year – per draft financial statements	(50,077)	(2,702)
Net effect of adjustments made during the audit	(820)	2,152
Revised deficit per final accounts/decrease on fund	(50,897)	(550)

Issues arising from the audit

20. We are required by international auditing standards to report to the Board the main issues arising from our audit of the financial statements. The most significant issues are noted below.

Scottish Arts Council

Centre for Contemporary Arts

21. In January 2010, the Council disposed of its interest in the Centre for Contemporary Arts (CCA). As part of this transaction, the property at Sauchiehall Street was transferred back to the Scottish Arts Council for a nominal sum. This property is now leased to CCA for a minimum period of five years with a peppercorn rent being paid. We have considered the accounting treatment surrounding this event as part of our audit work. Adjustments have been made to the draft financial statements to ensure compliance with the relevant accounting standards.

Voluntary Redundancy/Severance Payments (VER/VES):

22. As part of the transition to Creative Scotland, employees at the Council have been offered voluntary redundancy. The scheme has been funded through additional grant in aid. A provision (£311,000) has been made in the financial statements in relation to this scheme.

Remuneration Report

23. The term directors is interpreted as (for the purposes of the remuneration report):

- (reporting entities other than departments) the names of the chairman and chief executive; and
- (all reporting entities) the composition of the management board (including advisory and non-executive members) having authority or responsibility for directing or controlling major activities of the entity during the year. This means those who influence the decisions of the entity as a whole rather than the decisions of individual directorates or sections within the reporting entity.

24. The Council and SAC NLDF disclose within the remuneration report details of the chairman and Chief Executive. No information is provided on the corporate/senior management team. We would encourage Creative Scotland to revisit this disclosure in future years to ensure compliance with the definition and disclosure outlined in the FReM.

Action Plan Point 2

Related Parties

25. The Charities SORP requires the following disclosure with regard to related parties:

- The amounts involved
- Outstanding balances with related parties at the balance sheet date and any provisions for doubtful debts from such persons
- Any amounts written off from such balances during the accounting year
- Any other elements of the transactions which are necessary for the understanding of the accounts.

26. We noted during our audit that the Council and SAC NLDF accounts disclose the original grant award under related parties and does not disclose the information noted above. We recommend that Creative Scotland review this disclosure going forward to ensure compliance with the applicable guidance.

Action Plan Point 3

National Lottery Distribution Fund

Kirkintillochs Initiative Ltd

27. During the audit it was brought to our attention that a grant awarded to Kirkintillochs Initiative Ltd had been withdrawn. This resulted in an adjustment of £1.665m. The decision that this grant could be withdrawn was made by the Lottery Committee on 22 March 2010.

Legacy Trust Funding

28. SAC NLDF has entered into a partnership funding arrangement with Legacy Trust UK. This is a five year investment programme. The Legacy Trust has committed to providing total funding of £2.570 million over the five year period. SAC NLDF drawdown this funding based on project milestones. As at 31 March 2010, SAC NLDF had claimed for £661,000 from the Legacy Trust. This is reported as 'other income' in the financial statements.

Final payment of lottery grants

29. SAC NLDF has established a grant payment process whereby the first 90% of a NLDF grant is paid on approval of the application. The final 10% is paid on submission of a final management report by the claimant. During our audit we found a number of grants where the final management report is still outstanding. The outstanding awards go as far back as 2006. As a final management report has not been submitted by the claimant there is a risk that the SAC NLDF has distributed funds which are not being used for their intended purpose.
30. We recommend that the SAC NLDF considers alternative methods to distributing awards, by linking funding with the progress of the project. We also recommend that SAC NLDF review outstanding final grant awards and consider if they should be written off and potential seek full repayment of the grant paid out on the basis of non-compliance.

Action plan point 4

Statement of Internal Control

31. As part of our audit we have considered the statement of internal control, included with the Annual Report and Accounts (for both the Council and SAC NLDF). We are satisfied that the statement is consistent with guidance issued by Scottish Ministers and that the contents are not inconsistent with information gathered during the course of our normal audit work.

Regularity

32. The Public Finance and Accountability (Scotland) Act 2000 imposes a responsibility on auditors 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 issued an unqualified opinion on the regularity of transactions in Council and SAC NLDF accounts.
33. We have also concluded that the financial statements and the part of the Remuneration Report to be audited for both the Council and SAC NLDF have been properly prepared in accordance with guidance issued by Scottish Ministers, and that information in the management commentary which is included within the Annual Report is consistent with the financial statements.

Use of resources

34. This section sets out our main findings from our review of how the Council and the SAC NLDF manages its key resources.

Financial performance

Whilst the Council incurred a deficit in the year, a strong balance sheet position was maintained through grant-in-aid

35. The Council incurred expenditure of £53.054m in 2009/10 (2008/09: £49.912m) and received income of £52.346m (2008/09: £48.871m) including grant-in-aid funding of £50.312m from the Scottish Government. The overall effect, as shown in Table 2, was a decrease in the Council's reserves of £0.023m (2008/09: decrease £1.279m).

Table 2: Summary financial position

	2009/10 (£'000)
Total Income (including interest)	2,034
Grant expenditure	(46,428)
Arts services	(2,993)
Other operating costs	<u>(3,633)</u>
Final deficit position	(51,020)
Grant-in-aid funding	50,312
Reserve movements (including disposal of interest in CCA, revaluation in year and reversal of notional interest)	<u>685</u>
Total decrease in reserve	(23)

Source: Scottish Arts Council's 2009/10 financial statements

SAC NLDF incurred a reduction in funds of £0.550m in 2009/10, this has contributed to a negative general fund balance of £0.517m

36. The SAC NLDF incurred expenditure of £20.421m in 2009/10 (2008/09: £30.127m) and received income of £19.893m (2008/09: £17.056m) including National Lottery Fund proceeds of 19.206m. The net impact was a decrease in the in the general fund of £0.550m.
37. The SAC NLDF negative balance sheet position is the result of over commitment of grants to third party organisations. Table 3 below highlights the level of awards committed against resources available.

Table 3: Analysis of commitments

	(£'000)
Total commitments (hard and soft) as at 31 March 2010	24,822
Grant approved awards (offer not issued) as at 31 March 2010	1,310
Total commitments and grants approved	26,132
Total balance held with NLDF and bank	<u>(24,195)</u>
Over commitment	1,937

Source: Scottish Arts Council NLDF 2009/10 financial statements

38. The table above demonstrates that the SAC NLDF has overcommitted its resources resulting in a negative balance sheet position. As part of the legacy trust funding the SAC NLDF is contractually obliged to receive funding of £1.909m, which is not included in the assessment above however this would still lead to fund being overcommitted by £28,000. We recommend that, as a matter of urgency, the SAC NLDF develop robust financial plans that enable the fund to return to a positive balance sheet position.

Action plan point 5

Financial management

SAC NLDF has over committed its financial resources. Financial plans should be developed to allow the organisation to return to a positive balance sheet position

39. SAC NLDF has a responsibility to conduct its financial affairs in a proper manner. We are required to consider the arrangements for financial planning, budgetary control and financial reporting.
40. Budgets are devised at the start of the year, approved by the Lottery Committee and then reviewed during the year to take account of any new information. Our analysis during the year found that whilst financial performance was regularly monitored by the Lottery Committee the information did not appear robust enough to determine the actual level of commitments made by the fund. As demonstrated in Table 2 above, this has led to the organisation over-committing resources within the year.
41. We recommend that SAC NLDF revise its budget monitoring arrangements to ensure that grant commitments are recognised when the commitment is made rather than when it is confirmed by the claimant.

Action plan point 6

Performance

Quality Framework

42. The Council launched its Quality Framework in March 2007. The Quality Framework is a set of guidelines for arts organisations. Arts organisations in receipt of grant funding from the Council are expected to comply with these guidelines. Foundation organisations are required to report to the Scottish Arts Council on all areas of the Quality Framework and any organisation funded on a flexible basis is required to report primarily against artistic leadership.
43. The Council commissioned external consultants to perform an independent review of the Quality Framework. A revised framework was launched in 2009 and builds on the evaluation and feedback from organisations which use the framework and the independent evaluation. No major changes were introduced in the revised framework.

Best Value

44. We have found no evidence in the course of our audit work to indicate that the entity has operated in a manner which is inconsistent with the principles of Best Value. Previously, the size and context of the Council and SAC NLDF has meant specific and formal Best Value assessments were not undertaken. Rather, management looked to adopt Best Value principles as inherent in the day to day running of the organisation. Whilst this arrangement has until now been considered appropriate, with the move to Creative Scotland, and in recognition of the challenging financial environment, it would seem appropriate to consider whether more formal Best Value work could support optimising the efficiency and effectiveness of the new organisation. Management, external audit and internal audit could all play a role in taking this forward.

National Studies

45. Audit Scotland has prepared National Studies in a variety of areas. There is an expectation that central government bodies review the National Studies published between April 2009 and March 2010 relevant to them and action them accordingly. As external auditors, Audit Scotland, requires Scott-Moncrieff to complete a pro forma template for each National Study which will address the following points:
- Was the national report discussed at any of the body's committees and on what dates?
 - Did the body carry out a self assessment against the national report?
 - Did the board produce an action plan? A copy of which is to be submitted to Audit Scotland.
 - Are there plans to provide the committee(s) with feedback on the actions?
46. During our 2009/10 audit we reviewed the action the Scottish Arts Council has taken in relation to the following reports:

- Improving public sector purchasing
- Scotland's public finances: preparing for the future

47. In February 2010 we submitted the completed pro-formas to Audit Scotland. We are pleased to report that no issues were identified from our review.

48. We will continue to monitor any further National Studies published in the coming year and consider the action taken by the Scottish Arts Council in response to these.

Governance

Successful transition to Creative Scotland

49. Following a review of the arts and creative sector in Scotland by the Cultural Commission, the then Scottish Executive announced that the Scottish Arts Council and Scottish Screen would be replaced by a new body called Creative Scotland. Creative Scotland Ltd was established to facilitate the transition process. During 2009/10, the Council and Scottish Screen played an important role in the transition to Creative Scotland, as part of the wider 12 month transitional plan. Creative Scotland became a Statutory Non Departmental Public Body (NDPB) on 1 July 2010, under the Public Services Reform (Scotland) Act. It replaces the Scottish Arts Council and Scottish Screen and has established a single body responsible for overseeing Scotland's arts and culture sector.
50. A Joint Board for the Scottish Arts Council and Scottish Screen was in operation during 2009/10, with the final meeting held in June 2010. On 11 June 2010 the Scottish Government announced the appointment of the first Chair and Board of Creative Scotland.

Accountable officer

51. Andrew Dixon was appointed Chief Executive Officer of Creative Scotland in May 2010. Given transition and reporting timescales, Andrew Dixon will be the Accountable Officer and will therefore sign the SAC and SAC NLDF 2009/10 accounts as such. Jim Tough, Scottish Arts Council CEO during 2009/10, has provided formal assurances to the new Creative Scotland CEO to support him in signing the accounts.

Statement of Internal Control

52. The framework of internal controls operating within SAC NLDF is reported within the Statement of Internal Control (SIC) included with the annual accounts. No significant areas have been identified which require to be raised within the SIC. We are satisfied that the contents of the SIC are not inconsistent with information gathered during our normal audit work and that the statement is in line with Scottish Ministers' guidance. This is underpinned by a risk management framework sufficient and appropriate in the context of the Scottish Arts Council.

Internal audit

53. Internal audit is a key component of Scottish Arts Council's corporate governance arrangements. The Council's 2009/10 internal audit service was provided by Deloitte. We have considered the internal audit service and concluded that it complies with relevant internal audit standards. In order to maximise the value of the total audit resources available to Scottish Arts Council, we have made use of internal audit where applicable to our external audit work and are grateful to Deloitte for their assistance in this respect.

Fraud, irregularity and corruption

54. We are required to consider the arrangements made by management for the prevention and detection of fraud, irregularity and corruption. Our audit identified no issues in this area.

Standards of conduct, integrity and openness

55. Propriety requires that public business is conducted with fairness and integrity. Guidance on standards of conduct, accountability and openness has been issued by the Scottish Government. Our work in this area included a review of the arrangements against our standards of conduct checklist and review of the register of interests. We are pleased to report that our audit identified no issues of concern in relation to standards of conduct, integrity and openness.

Looking Forward

Creative Scotland

From 1 July 2010, the assets, liabilities and operations of the Scottish Arts Council transferred to Creative Scotland. The powers as a National Lottery Fund Distributor also transferred from Scottish Arts Council to Creative Scotland

56. Creative Scotland has taken over the functions and resources of Scottish Arts Council and Scottish Screen, as well as having a wider responsibility for developing the cultural sector as a whole. The transition to Creative Scotland will be accounted for as a Machinery of Government change, avoiding potentially significant impact on the going concern assessment for the 2009/10 accounts. The Scottish Arts Council will prepare accounts, under the Charities SORP, for the three month period to the 30 June 2010. An exercise will also be carried out to convert these accounts to reflect international financial reporting standards.
57. In June 2010 the National Lottery etc. Act 1993 (Amendment of Section 23) (Creative Scotland) Order 2010, was approved by Scottish Ministers. This transfers Scottish Arts Council's powers as a National Lottery Distributor to Creative Scotland from 1 July 2010.
58. At the time of our audit, senior management were in final stages of discussion with the Scottish Government over the specifics of recognising the transition to Creative Scotland within the financial statements. At the time of writing, Creative Scotland management external audit and the Scottish Government are involved in agreeing the detailed requirements for this transition.

Funding

The London 2012 Olympic Games continues to have an adverse affect on funding

59. Creative Scotland will continue to receive funding from the Scottish Government in the form of Grant in Aid. For the remainder of the 2010/11 financial year from 1 July 2010 the funding awarded to Creative Scotland was the aggregate of that received by the Scottish Arts Council and by Scottish Screen less the amount drawn down before the transition date.
60. National Lottery receipts are projected to decrease because of funding being taking up by the London 2012 Olympic Games, both in terms of direct transfer to the Olympic Distribution Fund and through reduced non-Olympic ticket sales. During 2009/10 SAC NLDF transferred a total of £3,358,000 (2008/09: £840,000) to the Olympic Lottery Distribution Fund. The impact of the reduction in income has been incorporated into financial plans.

Relocation of Creative Scotland Edinburgh Office

61. Following the transition to Creative Scotland in July, the joint board agreed to relocate the Edinburgh base of Creative Scotland from Manor Place to Waverley Gate. This move is due to be completed by the end of the calendar year. We will continue to monitor the position and consider the impact of this for the 2010/11 accounts in next year's audit.

Appendix 1: Action Plan

Our annual report action plan details the control weaknesses and opportunities for improvement that we have identified during 2009/10. These are the issues that we believe need to be brought to the attention of the Council.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist.

Grading

To assist the Council in assessing the significance of the issues raised and prioritising the action required to address them, the recommendations have been rated. The grading structure is summarised as follows:

- Grade 5 Very high risk exposure – major concerns requiring Board attention
- Grade 4 High risk exposure – material observations requiring management attention
- Grade 3 Moderate risk exposure – significant observations requiring management attention
- Grade 2 Limited risk exposure – minor observations requiring management attention
- Grade 1 Efficiency/housekeeping point

The following Management Comments have been provided by the Head of Programme Management as part of legacy responsibilities.

The Creative Scotland Director of Finance and Operations will inherit the recommendations from Scott Moncrieff and action as appropriate.

No	Title	Issue identified	Risk and recommendation	Management comments
1	Preparation of the financial statements (Para 11)	Whilst we noted that the quality of the financial statements prepared is of a satisfactory standard we would encourage the Council to put in place arrangements to demonstrate continuous improvement in this area.	We would encourage the Council to put in place arrangements to demonstrate continuous improvement in this area. Grade 3	The Council is committed to an approach of continuous improvement and Creative Scotland will also embrace that approach. The transition to, and establishment of, Creative Scotland has an impact on capacity in the operations processes and our expectation is for process improvements in a more stable environment. Response by: Head of Programme Management Implementation Date: March 31 st , 2011

No	Title	Issue identified	Risk and recommendation	Management comments
2	Remuneration Report (Para 24)	The Council and SAC NLDF disclose within the remuneration report details of the chairman and Chief Executive. No information is provided on the corporate/senior management team.	We would encourage Creative Scotland to revisit this disclosure in future years to ensure compliance with the definition and disclosure outlined in the FReM. Grade 3	Historically, the approach taken by Council and SAC NLDF regarding remuneration details has been to interpret the guidance of FReM to associate ultimate decision-making authority with the posts of the Chair and the Chief Executive. As discussed in previous years, supporting and delegated decision-making levels are structured through other committees and senior management structures. Creative Scotland will likely revisit this disclosure under an overall review of policies and procedures. Response by: Head of Programme Management Implementation Date: March 31 st , 2011

No	Title	Issue identified	Risk and recommendation	Management comments
3	Related Parties (Para 26)	We noted during our audit that the Council accounts disclose the original grant award under related parties and does not disclose the information as required by the Charities SORP.	We recommend that Creative Scotland review this disclosure going forward to ensure compliance with the applicable guidance. Grade 3	Historically, the approach taken by Council and SAC NLDF regarding Related Parties has been to apply the spirit of disclosing in full any interest of a related party in the financial year under review. Rather than showing awards net of any transactions during the year, where significant withdrawals would understate the disclosure of the original award, the Council has implemented disclosure reporting to show the original award. I know that Creative Scotland plans to review all policies and procedures. Response by: Head of Programme Management Implementation Date: March 31 st , 2011

No	Title	Issue identified	Risk and recommendation	Management comments
4	Final Payment of Lottery Grants (Para 29)	<p>During our audit we found, for a number of grants awarded, that the final management report is still outstanding. As a result the final payment has not been made. The outstanding awards go as far back as 2006. As a final management report has not been submitted by the claimant</p>	<p>There is a risk that the SAC NLDF has distributed funds which are not being used for their intended purpose.</p> <p>We recommend that the SAC NLDF considers alternative methods to distributing awards, by linking funding with the progress of the project.</p> <p>We also recommend that SAC NLDF review outstanding final grant awards and consider if they should be written off and potential seek full repayment of the grant paid out on the basis of non-compliance.</p> <p>Grade 3</p>	<p>To ensure exposure relating to end of project reports is limited, the proportion of award remaining to be paid is relatively small. For significant value project awards, there are compensating controls in the form of interim project monitoring arrangements. Operationally, Investment Administration and Development Officers share responsibilities for monitoring the final management reports and the issue of system limitations for exception reporting is being addressed.</p> <p>While this approach to final project reporting is intended to minimise financial exposure, it may not be sufficient to incentivise funded projects to complete the monitoring requirements. Creative Scotland is reviewing investment strategy which will inform future changes to investment procedures.</p> <p>Response by and Responsible Officer: Head of Programme Management Implementation Date: March 31st, 2011</p>

No	Title	Issue identified	Risk and recommendation	Management comments
5	Financial Performance (Para 38)	SAC NLDF has overcommitted its resources resulting in a negative balance sheet position.	We recommend that, as a matter of urgency, the SAC NLDF develop robust financial plans that enable the fund to return to a positive balance sheet position. Grade 5	<p>Notwithstanding that the analysis in Para 38 includes £1.9m of soft commitments which in accordance with accounting standards are not included in the Annual Account, the apparent over-commitment on the NLDF balance of £24.195million is £28,000.</p> <p>The Scottish Arts Council, or its successor body, is confirmed as a Lottery distributor until 2019. The ability to treat Lottery income as a continuing fund as opposed to an annual grant means that expenditure may anticipate future income.</p> <p>Response by: Head of Programme Management</p> <p>Implementation Date: March 31st, 2011</p>

No	Title	Issue identified	Risk and recommendation	Management comments
6	Financial Management (Para 41)	Our analysis during the year found that whilst financial performance was regularly monitored by the Lottery Committee the information does not appear robust enough to determine the actual level of commitments made by the fund. This has led to the organisation over-committing resources within the year.	We recommend that SAC NLDF revise its budget monitoring arrangements to ensure that grant commitments are recognised when commitment is made rather than when it is confirmed by the claimant. Grade 5	The budgeting process is to allocate budgeted income to initiatives and projects in support of strategic priorities. In terms of the life-cycle of the investment award process, budget is allocated to, and monitored against an activity, in advance of agreeing commitments or ultimately awarding funds. The apparent over-commitment of resources is as a result of timing differences in the recognition of expenditure and associated income. The example of the LTUK is used to illustrate the full recognition of commitments in accordance with accounting standards, in anticipation of contractually agreed income. Commitments do not determine cash-flow, with payments made only on satisfactory achievement of project milestones and deliverables. The Lottery Committee review the content and format of financial information presented. Response by: Head of Programme Management Implementation Date: March 31 st , 2011

Appendix 2: Audit Adjustments

We made a number of audit adjustments during the audit which impacted on the final position as follows:

Scottish Arts Council	£'000
Net deficit for the year – per draft financial statements	(50,077)
Adjustment to include voluntary redundancy severance accrual	(311)
Increase in grants paid and committee	(1,705)
Removal of disposal of asset	1,196
Adjusted deficit	(50,897)

Scottish Arts Council NLDF	£'000
Deficit for the year - per draft financial statements	(2,702)
Adjustment for withdrawal of grant to Kirkintillochs Initiative Ltd	1,655
Adjustment for valuation of NLDF to market value from cost	209
Being recognition of additional legacy trust income in the year	267
Being adjustment for holiday pay accrual during year	21
Adjusted deficit	(550)



Scott-Moncrieff
(www.scott-moncrieff.com), one
of Scotland's leading independent
professional services firms,
provides industry-focused audit,
tax, business advisory and
corporate consulting services
for commercial, public, not-for-profit
and private clients.

© Scott-Moncrieff Chartered Accountants
2010. All rights reserved. "Scott-Moncrieff"
refers to Scott-Moncrieff Chartered
Accountants, a member of Moore Stephens
International Limited, a worldwide network
of independent firms.

Scott-Moncrieff Chartered Accountants is
registered to carry on audit work and
regulated for a range of investment
business activities by the Institute of
Chartered Accountants of Scotland.