

# Scottish Natural Heritage

## Annual Report on the 2012/13 Audit



Prepared for Scottish Natural Heritage and the Auditor General for Scotland  
September 2013

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. It provides services to the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Government and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

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# Key Messages

## 2012/13

We have given an unqualified opinion that the financial statements of Scottish Natural Heritage (SNH) for 2012/13 give a true and fair view of the state of the body's affairs and of its net expenditure for the year.

There were two issues identified during the final accounts process that will require to be revisited in 2013/14. The first issue is regarding the Chief Executive's taxable payments and how this is presented within the Remuneration Report. The second issue surrounds the accounting treatment and exclusion of flexitime balances in the annual accounts. These issues have been discussed with senior officers.

Overall SNH's arrangements for the prevention and detection of fraud were satisfactory during 2012/13. From our review of the key controls within the main financial systems, we concluded that the systems of internal control are operating effectively.

## Outlook

We confirm the financial sustainability of SNH on the basis of its financial position and projected three-year financial summary. The financial position going forward is becoming more challenging than previous years with limited increases in funding coupled with increasing cost pressures. This represents a major challenge for Scottish Natural Heritage and expenditure during the year will be closely monitored to identify and address any emerging budget pressures or projected overspends at an early stage.

# Introduction

1. This report is the summary of our findings arising from the 2012/13 audit of SNH. The purpose of the report is to set out concisely the scope, nature and extent of the audit. It summarises our opinions on the financial statements and conclusions on any significant issues arising.
2. The report also reflects our overall responsibility to carry out an audit in accordance with the public sector audit model which is based on the Code of Audit Practice prepared by Audit Scotland (May 2011). This sets out the wider dimensions of the public sector audit which involves not only the audit of the financial statements but also consideration of areas such as financial performance and corporate governance. An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements prepared by management; however this does not relieve management of their responsibilities in this respect. This report has been prepared for the use of SNH and no responsibility to any third party is accepted.
3. [Appendix A](#) is an action plan setting out the high level risks we have identified from the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "planned management action". We do not expect all risks to be eliminated or even minimised. What we expect is that SNH understands its risks and has arrangements in place to manage these risks. Members should ensure that they are satisfied with the proposed management action and have a mechanism in place to assess progress.
4. This report is also addressed to the Auditor General for Scotland and will be published on our website after consideration by the Audit and Risk Management Committee.

# Financial statements

## Conduct and scope of the audit

5. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in the Annual Audit Plan presented to the Audit and Risk Management Committee on 7 February, and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in May 2011.
6. As part of the requirement to provide full and fair disclosure of matters relating to our independence we can confirm that we have not undertaken non-audit related services. The 2012/13 agreed fee for the audit was disclosed in the Annual Audit Plan and as we did not require to carry out any additional work outwith our planned audit activity this fee remains unchanged.

## Audit opinion & accounting issues

7. We have given an unqualified opinion that the financial statements of SNH for 2012/13 give a true and fair view of the state of the body's affairs and of its net expenditure for the year. The audit opinion was formally issued and signed on 25 July.
8. We received the unaudited financial statements on 31 May in accordance with the agreed timetable. The working papers were of a high standard and the staff provided good support to the audit team and we completed our on-site fieldwork on 21 June. SNH is required to follow the 2012/13 Financial Reporting Manual (FReM) and we can confirm that the financial statements have been properly prepared in accordance with these accounting requirements.

## Significant findings (ISA260)

9. During the course of the audit we identified the following:
10. **Chief Executive's Taxable Payments** - The Chief Executive is in receipt of taxable payments in addition to his basic salary. The payments received are under contract and are the reimbursement of those costs directly incurred by the Chief Executive due to the relocation of SNH to Inverness (accommodation and travel costs). SNH feel that these payments do not constitute part of the Chief Executive's remuneration package and as a result have not included this within the table as part of the Remuneration Report. There is however a narrative disclosure of the payments in the Remuneration Report. It is our view that these payments should form part of the Chief Executive's remuneration and be disclosed in the tables in the Remuneration Report.
11. **Flexitime Accrual** - There was no accrual in the accounts representing employees' flexitime accrued and owed at 31 March 2013. SNH policy states that staff are allowed to carry up to two days flexitime credit and 1.5 days flexitime debit per month. IAS 19, Employee Benefits states that, *employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for the termination of employment*. It is our view that there

should be an accrual in the accounts for this. We were provided with the average daily rate for each staff member and have estimated that the maximum understatement of expenditure is not material. SNH do not regard the flexitime accrual as a contractual liability and it is for this reason that they have not included it in the accounts. SNH are considering the inclusion of the flexitime accrual for future years.

## Whole of Government Accounts

12. The whole of government accounts (WGA) are the consolidated financial statements for all branches of government in the UK. We were advised by the National Audit Office in August 2013 that the certification threshold is now more than £300 million (£100 million in 2011/12). As a result, there is no audit certification required for SNH's 2012/13 WGA return.

## Financial position

### 2012/13 Outturn

13. The main financial objective for SNH is to ensure that the financial outturn for the year is within the resource budget allocated by Scottish Ministers.
14. SNH operated within the resource budgets for 2012/13 as detailed in Table 1 below which also shows the budget changes that occurred during the financial year.

**Table 1: 2012/13 Budget v Outturn**

	Initial Budget (£'000)	Final Budget (£'000)	Actual Outturn (£'000)	Under / (Over) spend
Resource DEL	53,194	51,420	51,317	103
Non Cash DEL	3,080	2,280	2,211	69
Capital DEL	1,500	1,850	1,863	(13)
AME	0	0	0	0
<b>Total</b>	<b>57,774</b>	<b>55,550</b>	<b>55,391</b>	<b>159</b>

Source: 2012/13 SNH Grant in Aid Letters

15. Although capital expenditure nominally exceeded the allocation the overall expenditure of £55.391 million was within the total allocation of £55.550 million. This performance was in the context of a 6.8% reduction in the total grant in aid allocation from the previous year.

### 2012/13 financial position

16. The Statement of Financial Position reports a net asset position of £26.230 million, which is a reduction of £0.179 million from the previous year. This small, downward movement is largely due to asset revaluations in the year coupled with a significant reduction in staff costs. Overall

this presents a healthy financial position whilst continuing to meet increasing and challenging grant in aid targets.

## Financial planning

17. The 2013/14 budget for SNH is £55.3m. SNH align their budget to their Business Plan within the agreed resource allocation for the coming year. SNH also have detailed planning and delivery against the Ministerial priorities and this is captured within their annual Business Plan covering the same period.
18. SNH incorporates a small provision in its operating budget to allow for late year slippage as much of their expenditure is project led (involving grant payments to other bodies) therefore outwith their direct control. This was previously discussed at the Audit and Risk Committee and members felt this to be acceptable given the nature of spend.
19. We found that SNH provides good financial information to the Board. Financial information is presented quarterly to the Board as part of SNH's performance reporting. This includes an operating cost statement position statement which can be compared to the budget in the original Business Plan and also provides year-end forecast out-turn figures.

## Corporate governance and systems of internal control

### Overall governance arrangements

20. The Code of Audit Practice gives auditors a responsibility to review and report on audited bodies' corporate governance arrangements and overall we found SNH had sound governance arrangements in place which included a number of standing committees overseeing key aspects of governance.

### Accounting and internal control systems

21. While auditors concentrate on significant systems and key controls in support of the opinion on the financial statements, their wider responsibilities require them to consider the financial systems and controls of audited bodies as a whole. However, the extent of this work should also be informed by their assessment of risk and the activities of internal audit.
22. No material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.
23. Internal audit is an important element of SNH's governance structure. Our review established that the work of both the in-house internal audit team and that of Scott-Moncrieff (who are providing additional internal audit services to SNH in 2012/13, primarily for payroll) was of a good quality allowing us to place reliance on a number of key areas. This not only avoided duplication of effort but also enabled us to focus on other key risk areas. The areas we placed formal reliance on include:



- New Payroll system (Scott-Moncrieff)
- Corporate Governance for period 2012/13 (in-house)
- Risk Management for period 2012/13 (in-house)

## Prevention and detection of fraud and irregularity

24. In our Annual Audit Plan we highlighted the responsibility audited bodies have for establishing arrangements to prevent and detect fraud and other irregularities. SNH's Fraud Policy was reviewed and updated in November 2012 (to reflect changes to the Scottish Government's own Fraud Policy) and then reissued to staff.
25. There were no instances of fraud reported in 2012/13 that we are aware of. In our opinion SNH's overall arrangements for the prevention of fraud are satisfactory, although it should be noted that no system can eliminate the risk of fraud entirely.

## NFI in Scotland

26. Audit Scotland has coordinated another major counter-fraud exercise working together with a range of Scottish public bodies, external auditors and the Audit Commission to identify fraud and error. These exercises, known as the National Fraud Initiative in Scotland (NFI), are undertaken every two years as part of the statutory audits of the participating bodies. The latest exercise started in October 2012 but is not due to report until May 2014.
27. The NFI works by using data matching to compare a range of information held on bodies' systems to identify potential inconsistencies or circumstances that could indicate fraud or error which are called 'matches'. Where matches are identified these are made available to bodies to investigate. SNH has been committed to and engaged well with the NFI process. In particular, we noted that senior members of the organisation have been involved in the process and the Audit & Risk Management Committee has been advised of progress.
28. SNH submitted their trade creditor data for NFI during 2012/13. SNH did not submit payroll data as part of the 2012/13 NFI process due to the implementation of a new payroll system. This approach was agreed by Audit Scotland and SNH intend to submit payroll and creditor NFI data for the 2014/15 NFI exercise.
29. SNH is making good progress with the NFI. All recommended matches have been actioned and resolved and some work is still on-going to follow-up a sample of categorised matches. In 2013/13, SNH plans to update its Fraud Policy, to make reference to its involvement in NFI. No frauds or errors have been found as a result of the NFI process to date.

## Standards of conduct and arrangements for the prevention and detection of corruption

30. Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and have proper arrangements in place for implementing and monitoring compliance with standards and codes of conduct, standing orders and financial

instructions. Auditors consider whether bodies have adequate arrangements in place. No issues have been identified by us for inclusion in this report.

## Best value

31. Accountable officers are required to put in place appropriate arrangements to satisfy their corresponding duty of best value.
32. SNH is currently implementing a Change Improvement Programme, which will include the implementation of a workforce planning process during 2013/14, for which development is currently underway.
33. SNH is also demonstrating their commitment to best value including planning to be smaller, smarter and more influential over the period 2012-2015:
  - Smaller is about responding successfully to the challenge of working with fewer resources.
  - Smarter involves both using information and knowledge effectively and working smartly to achieve efficiencies.
  - More influential is about having good evidence, about good people skills, about helping to find solutions, about building relationships and allies, about providing information to the right people at the right time.

## National Performance Audits

### Scotland's Public Finances: Addressing the Challenges (targeted follow-up)

34. *Scotland's Public Finances: Addressing the Challenges* was published by the Auditor General and the Accounts Commission in August 2011. The report provided an overview of the scale of budget cuts expected to be faced by the Scottish public sector in the period 2010/11 to 2014/15, and how public bodies were beginning to respond to the challenges of reducing expenditure. In particular, the report highlighted some of the main pressures facing public bodies and emphasised the importance of them achieving long-term financial sustainability.
35. During the 2012/13 audit we undertook follow-up work to assess the progress made by SNH against key recommendations in the report. The aim of the follow-up work was to assess how SNH is responding to the challenges of public sector budget constraints and the efforts to achieve financial sustainability, specifically:
  - Does SNH have sustainable financial plans which reflect a strategic approach to cost reduction?
  - Do senior officials, elected members and non-executive directors demonstrate ownership of financial plans and are they subject to sufficient scrutiny before approval? Our findings are listed below.
36. We are currently in the process of following up this national report and our findings will be reported to SNH shortly by way of a management letter.

## Acknowledgements

37. We would like to express our thanks to the staff of SNH for their help and assistance during the audit of this year's financial statements which has enabled us to provide an audit report within the agreed timetable.

# Appendix A: Action Plan

## Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer/ Target Date
1	<a href="#">10</a>	<p><b>Remuneration Report</b></p> <p>The Chief Executive's taxable payment, in addition to his basic salary, should be disclosed within the table in the Remuneration Report.</p> <p>The table and disclosures within the Remuneration Report are not in line with the required reporting guidelines (e.g. the FReM).</p>	SNH will consider the Risk identified by Audit Scotland and respond accordingly in preparing the 2013/14 Annual Accounts.	<p>Director of Corporate Services</p> <p>October 2013</p>