



# **HIGHLANDS AND ISLANDS ENTERPRISE**

**Annual audit report 2014/15**

**September 2015**

# Contents

Key Messages .....	2
Introduction .....	3
Audit of the 2014/15 financial statements.....	4
Financial management and sustainability.....	10
Governance and transparency .....	13
Best Value .....	17
Appendix I – Significant audit risks.....	19
Appendix II – Summary of local audit reports 2014/15 .....	22
Appendix III – Summary of national reports 2014/15.....	23
Appendix IV – Action plan .....	24

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This report will be published on our website after it has been considered by the risk and assurance committee. The information in this report may be used by Audit Scotland in any reporting to the Scottish Parliament.

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# Key Messages

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 <p>Audit of financial statements</p>	<ul style="list-style-type: none"><li>• Unqualified independent auditor's report on the 2014/15 financial statements.</li></ul>
 <p>Financial management and sustainability</p>	<ul style="list-style-type: none"><li>• Highlands and Islands Enterprise operated within its resource budgets.</li><li>• Total equity decreased by £9.4 million, attributed to an increase in pension fund liabilities. There is a recovery plan in place to address the significant pension liability position.</li><li>• The financial position remains stable. A balanced budget of income and expenditure is projected for a 3 year period to 2018 based on continuing grant in aid provision.</li></ul>
 <p>Governance and transparency</p>	<ul style="list-style-type: none"><li>• Overall we found that Highlands and Islands Enterprise had sound governance arrangements.</li><li>• Systems of internal control operated effectively during 2014/15.</li><li>• Highlands and Islands Enterprise could do more to improve openness by keeping the website up to date with board meetings and minutes.</li></ul>

# Introduction

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1. This report is a summary of our findings arising from the 2014/15 audit of Highlands and Islands Enterprise.
2. The management of Highlands and Islands Enterprise is responsible for:
  - preparing financial statements which give a true and fair view, in accordance with the relevant financial reporting framework
  - ensuring the regularity of transactions, by putting in place systems of internal control
  - maintaining proper accounting records
  - preparing and publishing with their financial statements an annual governance statement and a remuneration report
  - preparing consolidation packs.
3. Our responsibility, as the external auditor of Highlands and Islands Enterprise, is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.
4. An audit of 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; that have been prepared by management with the oversight of those charged with governance. This does not relieve management of their responsibility for the preparation of financial statements.
5. A number of reports, both local and national, have been issued by Audit Scotland during the course of the year. These reports are summarised at [appendix II](#) and [appendix III](#).
6. [Appendix IV](#) is an action plan setting out our recommendations to address the high level risks we have identified from the audit. We recognise that not all risks can be eliminated or even minimised. What is important is that Highlands and Islands Enterprise understands its risks and has arrangements in place to manage these risks. The committee should ensure that they are satisfied with proposed action and have a mechanism in place to assess progress and monitor outcomes.
7. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures; consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.
8. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

# Audit of the 2014/15 financial statements

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## Financial Statements

- The financial statements for 2014/15 give a true and fair view of the state of the body's affairs and of its net expenditure for the year.
- We confirm that the financial statements have been properly prepared in accordance with the 2014/15 FReM and the requirements of the Enterprise and New Towns (Scotland) Act 1990 and directions made by the Scottish Ministers.

## Regularity

- In all material respects, the expenditure and income in the financial statements were incurred or applied in accordance with applicable enactments and guidance.

## Other prescribed matters

- The remuneration report to be audited has been properly prepared in accordance with the requirements of the Enterprise and New Towns (Scotland) Act 1990 and directions made by the Scottish Ministers.
- The information in the management commentary is consistent with the financial statements.

## Submission of financial statements for audit

9. We received the unaudited financial statements on 29 June 2015, in accordance with the agreed timetable. As in previous years the extent of errors identified by the audit process, including areas that still contained prior year information, indicates that further improvements are required to support delivery of a strong set of unaudited financial statements. Next year will present a specific challenge due to the significant changes outlined at paragraph 26.

### Refer Action Plan no. 1

10. The working papers were of a reasonable standard and staff provided support to the audit team which enabled us to complete our on-site fieldwork on 30 July 2015. There were some minor issues with staff availability during this on-site period, however we acknowledge that finance officers worked to increase key officer availability and we will work together to secure further improvements next year.

## Overview of the scope of the audit of the financial statements

11. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual Audit Plan presented to the Risk and Assurance Committee on 10 March 2015.

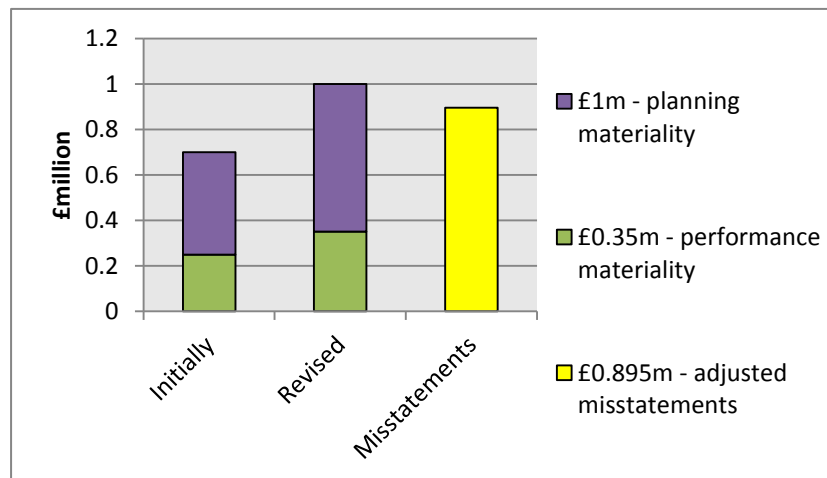
12. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken any non-audit related services. The 2014/15 agreed fee for the audit was set out in the Annual Audit Plan and, as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.
13. The concept of audit risk is of central importance to our audit approach. During the planning stage of our audit we identified a number of key audit risks which had the greatest effect on the audit strategy, resources and effort. We set out in our Annual Audit Plan the audit work we proposed to undertake to secure appropriate levels of assurance. [Appendix I](#) sets out these significant audit risks and how we addressed each risk in arriving at our opinion on the financial statements.
14. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

## Materiality

15. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other qualitative reasons (for example an item contrary to law).

## Audit of the 2014/15 financial statements

16. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
17. We summarised our approach to materiality in our Annual Audit Plan. Based on the unaudited financial statements, we revised our planning materiality for 2014/15 to £1 million (1% of gross expenditure). Performance materiality of £0.35 million is determined to ensure that uncorrected and undetected audit differences do not exceed our planning materiality level. We report all misstatements greater than £20,000.



## Evaluation of misstatements

18. We identified a number of misstatements in the unaudited financial statements, which individually exceeded our reporting threshold of £20,000. These have been adjusted by management in the audited accounts. As a result of these adjustments net expenditure increased by £0.895 million. Further changes in other comprehensive expenditure/ income resulted in total net assets increasing by £0.088 million.
19. The total value of adjustments exceeded our overall performance materiality level of £0.35 million. These were due to infrequent transactions where officers applied the wrong accounting treatment (paragraphs 22 - 25). We conclude that these do not indicate further systematic errors within the accounts. We considered the impact of these misstatements on our audit approach and extended our testing of amortised cost calculations.

## Significant findings from the audit

20. International Standard on Auditing 260 requires us to communicate to you significant findings from the audit including:
  - the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and disclosures
  - significant matters arising from the audit that were discussed, or subject to correspondence with management

## Audit of the 2014/15 financial statements

- significant difficulties encountered during the audit
- written representations requested by the auditor
- other matters which in the auditor's professional judgment, are significant to the oversight of the financial reporting process.

21. The following table details those issues or audit judgements that, in our view, require to be communicated to those charged with governance in accordance with ISA 260.

### Significant findings from the audit in accordance with ISA260

22. **Investee body rental income** - Highlands and Islands Enterprise entered into a lease arrangement with an investee body and deferred rental income until May 2016, when a lump sum payment of £1 million would be made. An appropriate receivable balance is reflected in the unaudited financial statements (£0.767 million), however audit testing established that a bad debt provision had been made against this amount. The valuation of the asset associated with this rental agreement was based on future cash inflows and had increased in value from £0.65 million to £0.9 million (taking into account the income payment due in May 2016). The approach to valuing the collectability of the debt and the related asset were inconsistent and, as there is a guarantee in place from the parent of the investee body, officers have reversed the bad debt provision of £0.767 million in the audited financial statements.

23. **Wave Energy VAT recovery** - Wave Energy Scotland Ltd is a new wholly-owned subsidiary of Highlands and Islands Enterprise. During the group consolidation process, finance officers made an adjustment of £0.152 million to the expenditure figures due to the expected recovery of VAT paid by the subsidiary. Discussions confirmed that the subsidiary's current VAT position was no longer sufficiently clear to allow it to be recognised in the financial statements. The audited financial statements have been adjusted to remove the VAT recovery of £0.152 million.



## Significant findings from the audit in accordance with ISA260

- 24. Financial instrument accounting** - Audit testing identified that the spreadsheet used to calculate the amortised cost of outstanding loans hadn't been accurately updated to reflect the in-year cash flows. Adjustments were required for a number of the significant loans arrangements within the accounts, however the overall impact was minimised due to the majority of the loans being fully provided for (£0.01 million increase in expenditure). Due to the non-receipt of interest payments, discussions with officers confirmed that a provision was required for another loan and this resulted in a £0.866 million adjustment in the accounts. Officers didn't process the adjustment for one of the loans due to the amount involved (£0.02 million) and the fact that there was no overall impact on the core financial statements.
- 25. Discontinued operation** – Highlands and Islands Enterprise disposed of Cairngorm Mountain Ltd during the year. This required the subsidiary to be deconsolidated from the group financial statements. When doing so, officers reclassified £0.565 million to net expenditure. This was the cost of the original investment in Cairngorm Mountain Ltd rather than the fair value. The audited financial statements have been adjusted to remove the reclassification to net expenditure.

## Future accounting and auditing developments

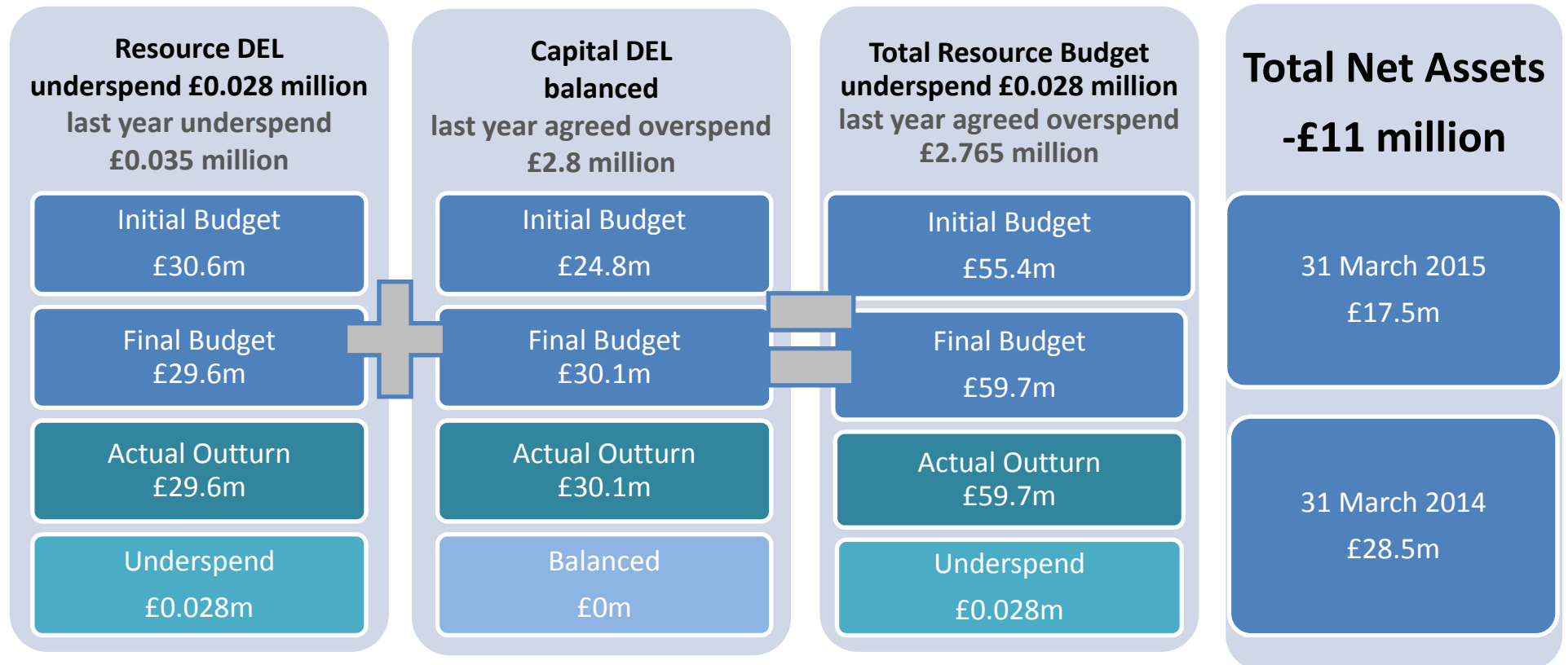
### *Revisions to the Financial Reporting Manual (FReM)*

- 26.** The financial statements are prepared in accordance with the Government Financial Reporting Manual (FReM). Two significant revisions will apply from 2015/16:
- adoption of IFRS 13 *Fair value measurement* for the first time – this also includes IAS 16 and IAS 38 adaptations
  - simplification and streamlining project – changes to the form and content of the annual report and accounts.
- 27. International Financial Reporting Standards – IFRS 13 Fair value measurement:** sets out the requirements for assets to be valued at fair value and is applied in full by the FReM only to assets that are not held for their service potential (i.e. investment properties and assets held for sale). It also applies to operational assets which are surplus to requirements where there are no restrictions on disposal which would prevent access to the market.
- 28.** IFRS 13 does not apply to operational assets which are in use delivering front line services or back office functions, and surplus assets with restrictions on their disposal. These will be valued in accordance with the adaptations to *IAS (International Accounting Standard) 16 property, plant and equipment*.

29. **Restructuring of the annual report:** the 2015/16 FReM has been extensively re-written to require the annual report and accounts to include:
- a performance report which will give a fair, balanced and understandable analysis of performance and will include an overview section and a performance analysis section
  - an accountability report incorporating the following three main sections:
    - corporate governance report consisting of a directors' report, a statement of the Accountable Officer's responsibilities and a governance statement
    - remuneration and staff report which will cover a number of prescribed disclosures including remuneration policy, payments to directors, staff numbers and sickness absence rates
    - parliamentary and accountability report which will include information on the regularity of expenditure and the independent auditor's report.

**Refer Action Plan no. 2**

# Financial management and sustainability



*In addition to its resource budget above, Highlands and Islands Enterprise also had a non-cash DEL budget of £12.7 million and an AME budget of £8 million. The non-cash DEL outturn was an underspend of £10.4 million, however the AME budget had a year end overspend of £1.9 million which was approved by the Scottish Government.*

## 2014/15 financial position

30. The main financial objective for Highlands and Islands Enterprise is to ensure that the financial outturn for the year is within the resource budget allocated by Scottish Ministers. Highlands and Islands Enterprise operated within the resource budgets for 2014/15 as detailed above. The Scottish Government agreed that £5.3 million of revenue funding would be transferred to capital during the year. Highland and Island also received an additional revenue budget of £3.3 million for Community Broadband Scotland and £1 million for other specific initiatives.
31. At 31 March 2015 Highlands and Islands Enterprise's statement of financial position shows a decrease in total equity of £9.4 million which can be primarily attributed to the pension fund net liability which has increased by £8.5 million. The assets and liabilities of a pension scheme are sensitive to a number of external factors e.g. bond rates, inflation, etc ... so that year on year fluctuations are typical. The pension assets and liabilities were subject to an independent valuation at the year end.
32. Highlands and Islands Enterprise, in agreement with the Pension Fund trustees and the Scottish Government, has introduced a recovery plan to address the pension shortfall. The plan includes increasing member contributions and a move from the current final salary to a new career average scheme.
33. The statement of financial position for 2014/15 shows a stronger current asset to current liability ratio due to the additional cash and cash equivalents held for Community Broadband Scotland.
34. The Operating Plan 2015 - 2018 was approved at the February board meeting and includes a balanced budget of £97.7 million, including a non cash allocation of £22.7 million. Indicative budgets for the following 2 years have been prepared based on an assumption of stable grant-in-aid provision.
35. The 2015/16 budget is consistent with prior year levels, at this stage in the year. Built into the budget is Highland and Islands Enterprise's share of the Scottish Government's Strategic Forum Savings Target of £3.2 million (£3.2 million in 2014/15) and a £3.9 million "negative reserve" which represents a funding gap that must be met from slippage in projects during the course of the financial year.
36. The inclusion of a negative reserve is in line with prior years' budget setting processes, however the initial 2015/16 balance of £3.9 million is higher than previous years and may be more challenging for Highlands and Islands Enterprise to achieve.
37. Recent financial reporting to the Board shows expenditure to 31 July 2015 of £34.5 million against a profile position of £30.5 million, however excluding broadband expenditure this reduces to £21.7 million against profile of £26 million. The report shows a forecast outturn within current budget for the year.

## Financial management and sustainability

38. Highlands and Islands Enterprise receives over 80% of its income from the Scottish Government with additional funding also provided for the Broadband project and Wave Energy Scotland. The remaining income sources have remained steady with future projections in line with current levels. Subject to the continuing funding support from the Scottish Government, we conclude that the financial position remains stable.

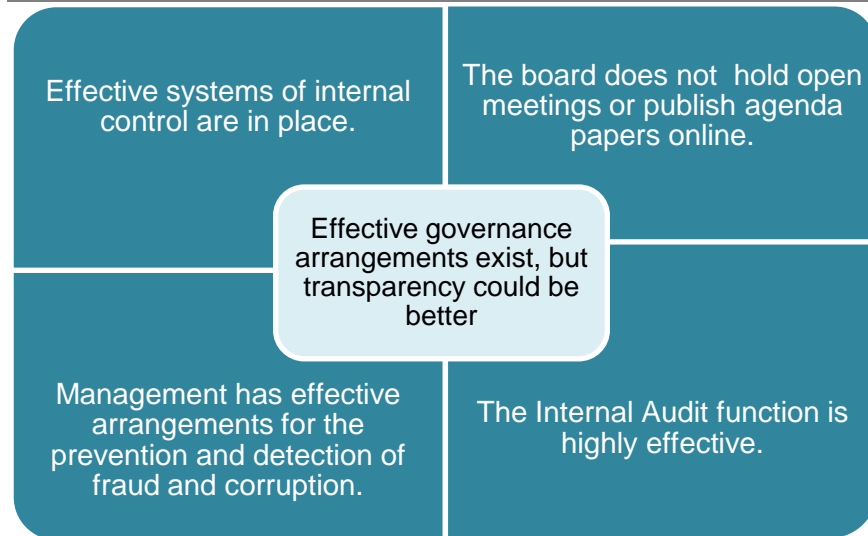
## Financial management

39. As auditors we need to consider whether bodies have established adequate financial management arrangements. We do this by considering a number of factors, including whether:

- the Director of Finance and Corporate Services has sufficient status to be able to deliver good financial management
- standing financial instructions and standing orders are comprehensive, current and promoted within the body
- reports monitoring performance against budgets are accurate and provided regularly to budget holders
- monitoring reports do not just contain financial data but are linked to information about performance
- members provide a good level of challenge and question budget holders on significant variances.

40. Based on our accumulated knowledge, our review of board papers and through our attendance at committees we conclude that Highlands and Islands Enterprise has strong financial management arrangements in place.

# Governance and transparency



## Corporate governance

41. The board and Accountable Officer are responsible for establishing arrangements for ensuring the proper conduct of the affairs of Highlands and Islands Enterprise and for monitoring the adequacy of these arrangements.
42. Highlands and Islands Enterprise is managed by a board including non-executive directors and is accountable through the Scottish Ministers to the Scottish Parliament. The board's Chair and non-executives are appointed by Scottish Ministers.

43. The board is supported in its role by the risk and assurance committee and the remuneration committee. The committees meet on a regular basis to consider relevant matters.
44. We concluded that Highlands and Islands Enterprise has effective overarching and supporting governance arrangements which provide an appropriate framework for organisational decision making.

## Transparency

45. The Scottish Government's On Board guidance (<http://www.gov.scot/Publications/2015/04/9736/0>), for board members of public bodies was updated and reissued in April 2015. On Board states that boards should demonstrate high standards of corporate governance at all times including openness and transparency in decision making. It recommends boards should consider:
  - holding an annual open meeting
  - holding board meetings in public unless there is a good reason not to
  - publishing summary reports and/or minutes of meetings
  - inviting evidence from members of the public in relation to matters of public concern

## Governance and transparency

- consulting stakeholders and users on a range of issues
  - making corporate plans and the annual report widely available.
46. Audit Scotland also believes in transparency of financial reporting within the annual report and accounts including a clear reconciliation between expenditure and the outturn against Scottish Government Resource budgets and identification of, and explanation of, significant movements in budget during the year.
47. While we acknowledge that there are aspects of board meetings that are commercially sensitive in nature, there is scope to include more information on the website and to consider making board meetings open to the public. This has been discussed with the leadership team following recent work by the business improvement and internal audit service. Overall, we conclude that Highlands and Islands Enterprise could do more to improve their openness and transparency.

**Refer Action Plan no. 3**

## Internal control

48. As part of our audit we reviewed the high level controls in a number of systems fundamental to the preparation of the financial statements. Our objective was to obtain sufficient audit evidence to support our opinion on the financial statements.
49. No material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the organisation's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.
50. We reported our findings to the Director of Finance and Corporate Services on 14 April 2015 and the risk and assurance committee on 22 June 2015.

## Internal audit

51. Internal audit provides the risk and assurance committee and accountable officer with independent assurance on the overall risk management, internal control and corporate governance processes. We are required by international auditing standards to make an assessment of internal audit to determine the extent to which we can place reliance on its work. To avoid duplication, we place reliance on internal audit work where possible.
52. Our review of internal audit concluded that the business improvement and internal audit service operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place. The internal audit plan for 2014/15 is materially complete and we were able to place formal reliance on aspects of internal audit work on significant transactions and certificates of assurance.

### ICT audit

53. ICT is a key area of control because it underpins all systems used by Highlands and Islands Enterprise. As part of our planning process we carried a high level review of ICT covering a number of areas. Overall, we conclude that the ICT arrangements are satisfactory and we are not aware of any specific issues that require to be brought to the attention of members.

### Arrangements for the prevention and detection of fraud

54. We assessed the arrangements for the prevention and detection of fraud during the planning phase of our audit. This involved reviewing the Counter Fraud Strategy, Counter Fraud Policy, Fraud Response Plan and Whistleblowing Policy and Procedures. We conclude that there are effective arrangements for the prevention and detection of fraud.

### National Fraud Initiative in Scotland

55. The National Fraud Initiative (NFI) in Scotland is a counter-fraud exercise led by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different financial systems, to identify circumstances (matches) that might suggest the existence of fraud or error.

56. Auditors are required to assess the arrangements that bodies have put in place to prevent and detect fraud, including how they approach the NFI exercise itself.

57. The National Fraud Initiative has a high profile within the Highlands and Islands Enterprise with data matches actively investigated and findings reported to the risk and assurance committee.

58. As part of this year's NFI exercise, Highlands and Islands Enterprise submitted payroll and creditors data and the matching process identified 1,013 records for investigation with 53 of these "recommended" for investigation. All "recommended" matches have been investigated along with a further 23 matches. No issues have been identified from the investigations and there are no issues of concern that we require to include in this report.

### Arrangements for maintaining standards of conduct and the prevention and detection of corruption

59. Highlands and Islands Enterprise has in place a range of activities designed to maintain standards of conduct including Codes of Conduct for officers and members. Also, there are established procedures for preventing and detecting corruption including annual reviews of Standing Financial Instructions and Standing Orders.



## Governance and transparency

60. An area of good practice undertaken by Highlands and Islands Enterprise relates to staff and board members completing Register of Interests forms which highlight where there may be a potential conflict of interest. This process extends to all Highlands and Islands Enterprise staff and is renewed annually. Details for non-executive board members are contained within the financial statements.
61. Based on our review of the evidence we concluded that there are appropriate arrangements in place for the prevention and detection of corruption and we are not aware of any specific issues that we need to record in this report.

# Best Value

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62. Accountable officers have a specific responsibility to ensure that arrangements have been made to secure Best Value in the use of resources.

## Arrangements for securing Best Value

63. Highlands and Islands Enterprise developed their CREATIVE vision following consideration of a range of best practice models and guidance. The CREATIVE characteristics are detailed in the Operating Plan 2015 - 2018 and the aim is to ensure that best value and continuous improvement are embedded in all activities, with the CREATIVE characteristics mapped to best value principles.
64. During the year the business improvement and internal audit team carried out various business improvement activity based on the CREATIVE vision. This included an independent review of customer service and a review to ensure resources were best aligned to achieve organisational outcomes.

## National performance audit reports

65. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2014/15, a number of reports were issued which are of direct interest. These are

outlined in [appendix III](#).

66. Highlands and Islands Enterprise has processes in place to ensure that all relevant national performance reports are considered by the risk and assurance committee.
67. **Superfast broadband for Scotland: a progress report** ([http://www.audit-scotland.gov.uk/docs/central/2015/nr\\_150226\\_broadband.pdf](http://www.audit-scotland.gov.uk/docs/central/2015/nr_150226_broadband.pdf)). This report by Audit Scotland assessed whether the Scottish Government and Highlands and Islands Enterprise have clear plans and arrangements in place to build their superfast broadband network in Scotland.
68. British Telecom is responsible for installing the infrastructure through two contracts. The contracts do not guarantee planned speeds to all users and the Scottish Government and Highlands and Islands Enterprise cannot yet state with certainty what broadband speeds they expect their contracts with British Telecom to ultimately deliver.
69. The total cost of the network is £412 million, with the Scottish public sector contributing £165 million of this. It is difficult to conclude whether the Scottish contracts represent value for money because British Telecom is also the sole contractor for all other UK broadband projects.

## Best value

70. British Telecom has exceeded its contractual targets for providing access to the broadband network by 57,000 premises, although it is about 14,000 premises short of where it expected to be against original implementation plans. The arrangements for scrutinising British Telecom's progress against the contracts are good. However, the Scottish Government and Highlands and Islands Enterprise have still to fully develop plans to measure the wider benefits of their broadband investment.
71. The report recommended the Scottish Government should improve ways of reporting the range of speeds its investment will deliver and report publicly what the contracts are expected to deliver.
72. The report recommended the Scottish Government and Highlands and Islands Enterprise should:
- encourage take-up of superfast broadband to maximise the benefits of their investments and identify what further work is needed to realise these benefits
  - develop clear plans, by June 2015, for the planned investment of a further £42 million in superfast broadband, announced by the UK and Scottish Governments in February 2014
  - review work programmes and payment profiles and make any changes necessary to ensure that payment is closely linked to successfully achieving the agreed targets
- keep staffing levels and workloads under review and alter the skills mix and number of staff when needed, to ensure project teams are able to fulfil their contract management and monitoring roles as well
  - further develop their performance measurement frameworks, including benchmarking with other countries' implementation of superfast broadband, and report publicly on these measures each year.

## Appendix I – Significant audit risks

The table below sets out the audit risks, how we addressed each risk and our judgement in arriving at our opinion on the financial statements.

Audit Risk	Planned assurance procedure	Results and conclusions
<b>Risk of material misstatement</b>		
<p><b>Income</b></p> <p>Highlands and Islands Enterprise receives a significant amount of income in addition to Scottish Government funding.</p> <p><i>The extent and complexity of income means there is an inherent risk of fraud in accordance with ISA240.</i></p>	<ul style="list-style-type: none"> <li>Detailed testing of income during the financial statements audit.</li> </ul>	<p>We undertook detailed testing of income streams and did not identify any evidence of fraudulent activity or significant weaknesses in related controls.</p>
<p><b>Management override of controls</b></p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p>	<ul style="list-style-type: none"> <li>Detailed testing of journal entries.</li> <li>Review of accounting estimates.</li> <li>Focused testing of accruals and prepayments.</li> <li>Evaluation of significant transactions that are outside the normal course of business.</li> </ul>	<p>We undertook detailed testing of journal entries, accruals and prepayments. We also reviewed accounting estimates and transactions for appropriateness.</p> <p>We did not identify any incidence of management override of controls.</p>

## Appendix I – Significant audit risk

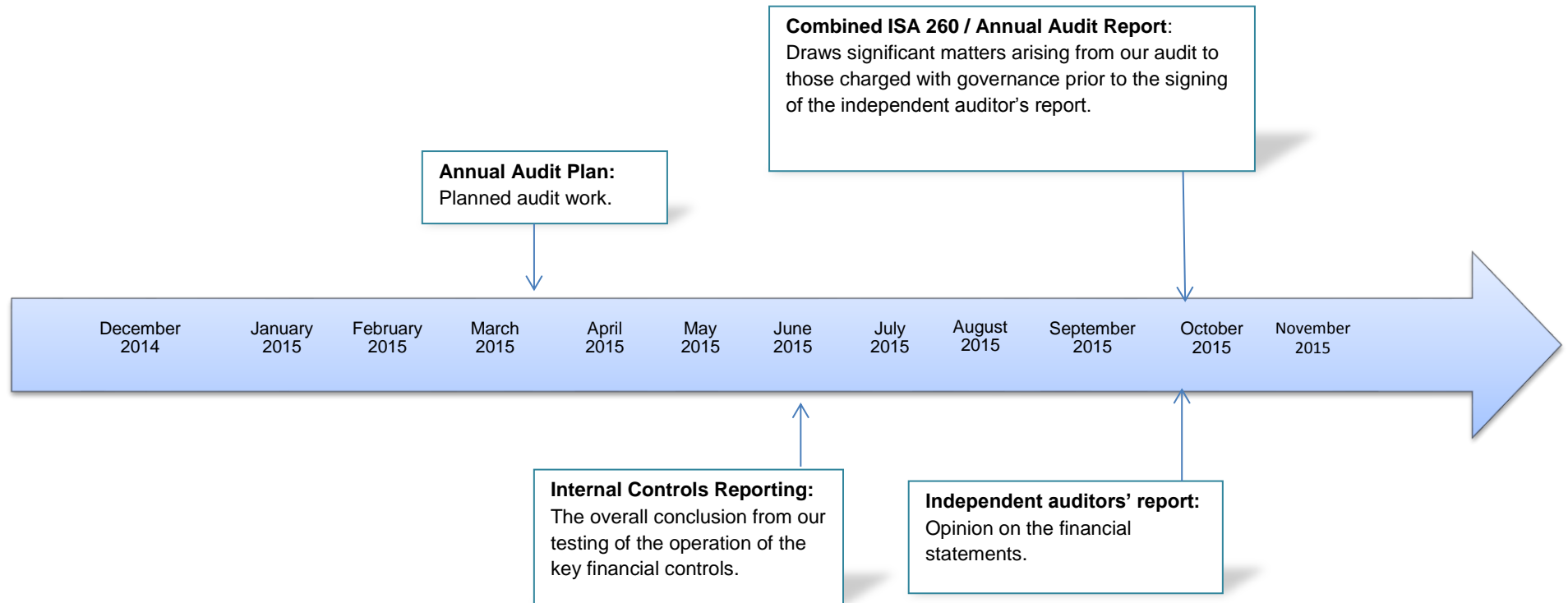
Audit Risk	Planned assurance procedure	Results and conclusions
<p><b>Preparation of the financial statements</b></p> <p>The capacity of the finance team and limited quality control when preparing the 2013/14 financial statements resulted in significant adjustments to the financial statements.</p> <p><i>There is a risk that the financial statements do not comply with accounting requirements.</i></p>	<ul style="list-style-type: none"> <li>• A completed NAO checklist will be subject to audit review.</li> <li>• Early discussion with finance officers on an agreed timetable for the preparation of the financial statements.</li> <li>• Early review of strategic report to identify any areas of non-compliance.</li> </ul>	<p>In the absence of fully completed checklists we completed the NAO disclosure checklists to ensure the financial statements contained the required disclosures.</p> <p>The financial statements were provided in accordance with the agreed timetable, however the extent of errors indicates further improvements are required.</p> <p>The audit process has ensured the financial statements are materially compliant with the FReM disclosure requirements.</p>
<p><b>Non current assets</b></p> <p>The 2013/14 audit identified non current assets grouped within the asset register with inaccurate useful lives. Finance officers are reviewing non current assets for the 2014/15 financial statements.</p> <p><i>There is a risk that non current assets are incorrectly accounted for in the financial statements.</i></p>	<ul style="list-style-type: none"> <li>• Detailed review of non current assets during the financial statements audit including separation of the identified assets and a review of the useful lives.</li> </ul>	<p>We undertook detailed testing of non current asset useful lives and depreciation calculations.</p> <p>We did not identify any issues with the accounting treatment.</p>

## Appendix I – Significant audit risk

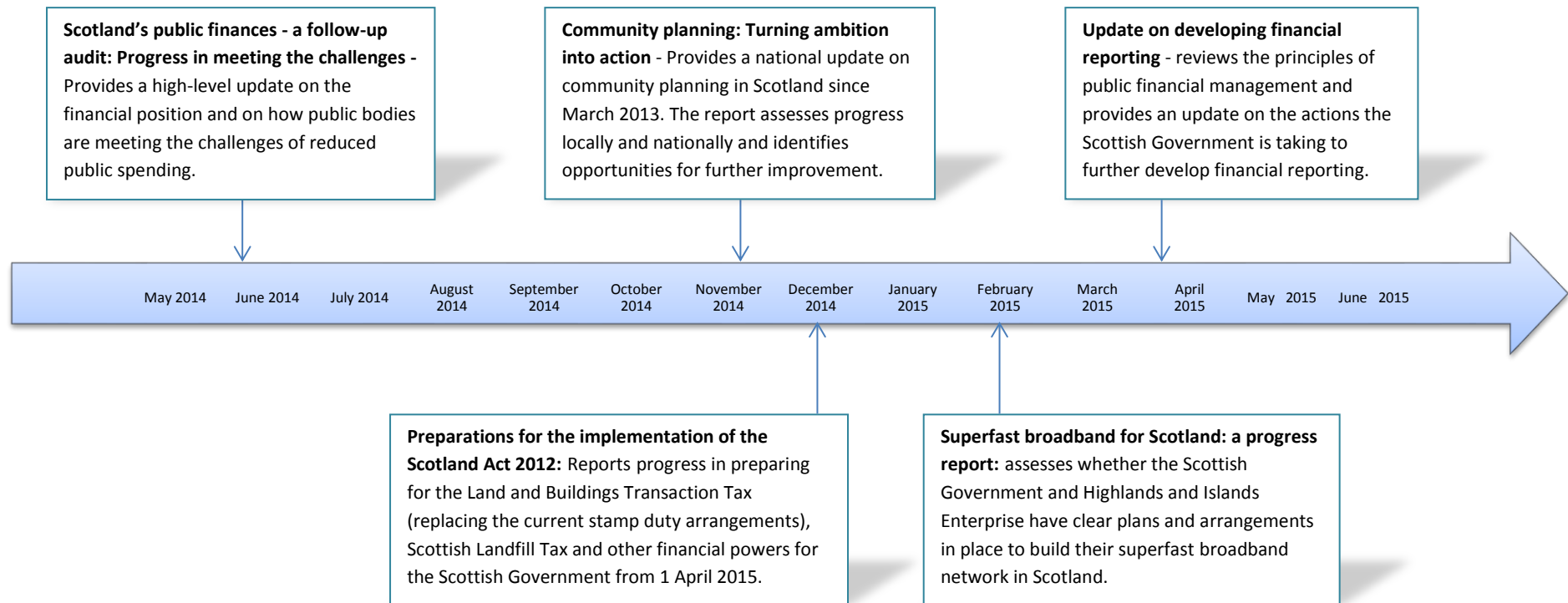
Audit Risk	Planned assurance procedure	Results and conclusions
<p><b>Financial position of investee</b></p> <p>An investee of Highlands and Islands Enterprise has funds available to remain in operation until May 2015, with the process of finding a buyer ongoing.</p> <p><i>There is a risk that Highlands and Islands Enterprise will need to disclose and account for any change in status after the 31 March as an event after the balance sheet date.</i></p>	<ul style="list-style-type: none"> <li>• Detailed review of the investment valuation included in the financial statements.</li> <li>• Review any disclosures to ensure compliance with requirements.</li> <li>• Monitor the status of the organisation up to the signing of the financial statements.</li> </ul>	<p>The investee body is still operating and discussions are ongoing on the continued operation of the business.</p> <p>We reviewed the valuations within the financial statements and, following some audit adjustments, are satisfied that they are consistent with the current status of the investee body.</p>
<p><b>New subsidiary</b></p> <p>Wave Energy Scotland, a wholly owned subsidiary of Highlands and Islands Enterprise, has been identified as the preferred bidder and has now purchased non current assets from Pelamis Wave Power Ltd.</p> <p><i>There is a risk that the subsidiary is not correctly accounted for in Highlands and Islands Enterprise's financial statements.</i></p>	<ul style="list-style-type: none"> <li>• Review of the business case for establishing the company and for its funding.</li> <li>• Detailed review of the consolidation of the new body into the group financial statements, including elimination of inter-organisational transactions.</li> </ul>	<p>We reviewed the letter from the Scottish Government which directed the establishment of Wave Energy Scotland to facilitate research and development activity to accelerate the development of wave technologies.</p> <p>We obtained assurances from the auditors of Wave Energy Scotland and completed detailed testing of the consolidation.</p> <p>Following an audit adjustment we are satisfied that the body is correctly accounted for in the group financial statements.</p>

# Appendix II – Summary of local audit reports 2014/15

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# Appendix III – Summary of national reports 2014/15





# Appendix IV – Action plan

Ref	Para	Issue / Recommendation	Management action / Response	Responsible officer	Target date
<b>Financial audit issues</b>					
1	9	<p><b>Preparation of financial statements</b></p> <p>While we recognise that there were specific IT issues that impacted on finance staff availability the unaudited financial statements required a number of changes as a result of the audit process.</p> <p>We recommend that finance officers prioritise the accounts preparation process, discuss accounting treatment with audit and ensure sufficient time is built in for a comprehensive review process.</p>	<p>The finance team will review the accounts preparation process to identify improvements and ensure a robust review process is in place.</p>	<p>Director of Finance and Corporate Services</p>	<p>31 March 2016</p>

## Appendix IV – Action plan

Ref	Para	Issue / Recommendation	Management action / Response	Responsible officer	Target date
2	29	<p><b>2015/16 FReM changes</b></p> <p>The 2015/16 FReM contains changes that will require action by finance officers to ensure they are fully reflected in the 2015/16 unaudited financial statements.</p> <p>We recommend that finance officers review the changes, discuss key areas with the audit team and put arrangements in place to ensure full compliance.</p>	<p>The finance team will review the FReM changes, discuss with Audit Scotland and put arrangements in place to address them in the unaudited financial statements.</p>	<p>Director of Finance and Corporate Services</p>	<p>31 March 2016</p>
<b>Wider audit issues</b>					
3	47	<p><b>Openness</b></p> <p>Boards should demonstrate high standards of corporate governance at all times including openness and transparency in decision making, in accordance with “On Board”.</p> <p>We recommend Highlands and Islands Enterprise consider including more information on the website and revisit making board meetings open to the public.</p>	<p>Processes are in place to update the website for board meetings.</p>	<p>Director of Finance and Corporate Services</p>	<p>31 March 2016</p>