

Skills Development Scotland

Interim Audit Report 2016/17



 AUDIT SCOTLAND

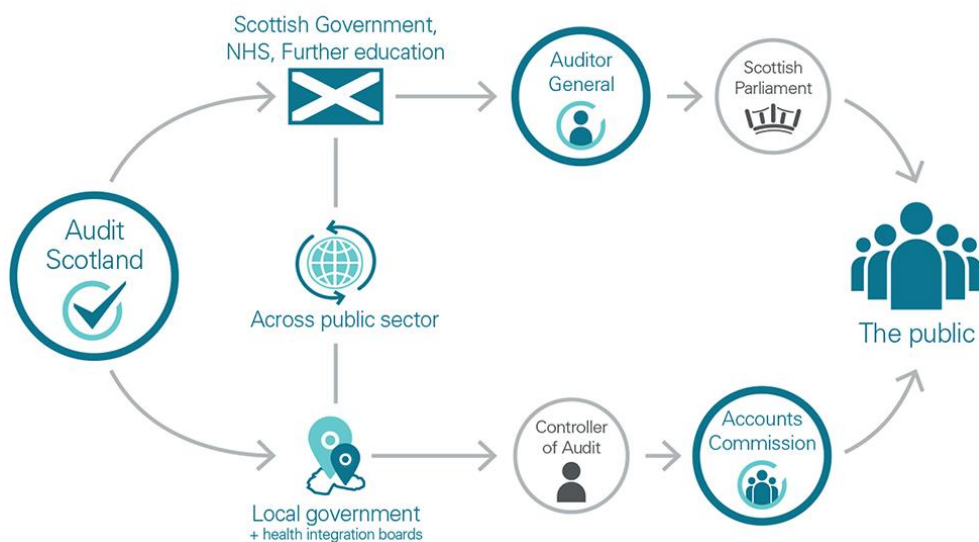
Prepared for Skills Development Scotland

March 2017

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Audit findings

Introduction

1. This report summarises the key issues identified during our interim audit work at Skills Development Scotland (SDS).
2. Our responsibilities under the Code of Audit Practice require us to assess the system of internal control put in place by management. We seek to gain assurance that SDS:
 - has systems of recording and processing transactions which provide a sound basis for the preparation of the financial statements
 - has systems of internal control which provide an adequate means of preventing and detecting error, fraud or corruption
 - complies with established policies, procedures, laws and regulations.
3. We carried out early substantive testing on material accounts areas including income, expenditure and staff costs.
4. Under the Code of Audit Practice (2016), we are also required to carry out wider dimension audit work. This focussed on financial management, financial sustainability and governance and transparency.

Conclusion

5. We identified the need to do further work to gain further assurances in key areas involving the national training programme expenditure and income from the Enterprise IS recharges (IT service desk providers) as set out at paragraph 9 and summarised in Exhibit 1.
6. In terms of our wider dimension audit work we concluded that appropriate arrangements are in place for financial sustainability, financial management and governance and transparency, with some areas for improvement as set out at paragraphs 10 to 13 and Exhibit 1.

Work summary

7. During our interim visit we carried out the following audit work:
 - Initial systems reviews and walkthroughs of the key controls identified for each financial system.
 - Initial substantive testing of income, expenditure and some elements of staff costs.
 - Follow-up of our 2010 'Role of Boards' report, in the knowledge of the ongoing Scottish Government review of enterprise & skills.
 - Detailed review of the adequacy and reasonableness of medium to long-term financial plans, including focused review of how scenario planning feeds into financial plans.

8. The contents of this report have been discussed with relevant officers to confirm factual accuracy. The co-operation and assistance we received during the course of our audit is gratefully acknowledged.

Findings

Initial Substantive Work

9. We carried out substantive testing on transactions for the first ten accounting periods of the 2016/17 financial year. Testing focused on income, expenditure and staff costs. We identified the following points :
- **Non-pay expenditure** - for national training programme (NTP) expenditure we completed an initial systems review to document the work undertaken by the compliance team. This informed our audit testing. We tested a sample of 20 NTP payments covering modern apprenticeship and employability fund payments. This did not identify any significant issues. As this is a key area of expenditure, we plan to carry out further audit procedures as part of our on-going work.
 - **Income** - we were unable to agree two out of ten items of income we sampled to the supporting documentation. Both were journals for the accrued income and reversals relating to 2015/16 EIS recharges. (SDS incur the EIS expenditure and recharge Scottish Enterprise and Highlands and Islands Enterprise share of the cost). For these items, it was unclear how the amounts have been calculated. Management advised they will check the accounting entries at year-end and make appropriate corrections. We were advised there will be an exercise at the financial year-end to ensure the recharges over the EIS IT provider are accurate and correct. As this is a key area of income, we plan to carry out further audit procedures as part of our on-going work.

Financial Sustainability

10. We completed a detailed review of the five-year rolling financial model maintained by SDS. In particular, we considered:
- the assumptions and forecasts built into the model
 - how the model is used for financial monitoring and reporting
 - sensitivity analysis carried out by SDS.
11. We found that:
- SDS is well advanced in financial planning. Its financial model is detailed and comprehensive and is based on reasonable assumptions. Key finance officers regularly update and develop the model for any changes in circumstances.
 - The work carried out by SDS in developing the financial model identifies a significant increase in apprenticeship family expenditure as they work towards achieving the targets set by the Scottish Government. Without a commitment from the Scottish Government for additional funding, there is a risk SDS will have a significant funding gap going forward.
 - SDS used scenario planning to prepare the financial model. They have since used sensitivity analysis to consider options for service delivery under different funding levels. We have been advised that SDS is now at a stage where further scenario planning is required to identify required action over financial planning.
 - The financial model is used to inform the Executive Leadership Group's budget review. While elements of the model are shared with the Board and

the Scottish Government's sponsor department, presenting the full picture would help promote a shared understanding of SDS' financial position.

Financial Management

12. We have reviewed budget monitoring reports, presented to the Board, and attended a Board meeting to observe the scrutiny of these reports and the 2017/18 annual budget. We also considered internal audit's review of budget monitoring. From this we found:

- Finance reports for the Board are prepared on a cash rather than accruals basis and do not include forecasted figures to the year-end. While they show committed expenditure which can indicate potential accruals, they do not make it clear how this may impact on the year-end outturn. More detailed information is presented to the Finance and Operational Performance (FOP) Committee. This includes the approved budget, autumn and spring budget revisions, and possible areas of over or underspends but does not include the forecasted year-end outturn. There is a risk that the Board is not aware of the total outturn forecast for the financial year and this could impact on the level of scrutiny.
- Internal Audit did not identify any significant weaknesses in SDS budget monitoring. They identified two areas for improvement in relation to identifying and reporting variances and actions taken to address variances.
- From attendance at a Board meeting, we observed Board members providing effective scrutiny of finance reports and the draft annual budget. Members showed a good level of understanding and provided challenge as appropriate.

'Role of Boards' follow-up

13. As part of the wider review of governance arrangements across the public sector, we completed a follow-up of the 'Role of Boards' national report, published in September 2010. This involved review of documentation, discussions with key officers and attendance at a Board meeting. From this work we found:

- The SDS Board is well established. Members demonstrate a strong level of commitment to their roles and responsibilities. The Corporate Office is well established in its role of supporting and developing the Board. The arrangements in place support effective working relationships between the Board and the SDS Executive Leadership Group.
- The Board, with the support of the Corporate Office, demonstrates a commitment to continuous improvement and personal development. There is clear evidence that the Board effectively scrutinises policy decisions and performance.
- Detailed Board minutes are published on the SDS website but Board papers are not available to the public. SDS acknowledges that making the papers publicly available would increase transparency but considers the cost and resource required to facilitate this would be too high. Management informed us that, while there has been little public interest in accessing the papers, the Corporate Office recognises the need to keep this policy under review.
- As at March 2017, the Board is made up of nine Scottish Government appointees and three co-opted members. The terms of two Board members expire at the end of February 2017 and a further four expire at the end of September 2017. Discussion is on-going for re-appointment of the two members whose terms end in February. Further succession planning will be required in 2017/18 as other Board members' terms come to an end. There is a risk that going forward the Board may have gaps in skills and expertise and there may be lack of scrutiny as a result.

Exhibit 1

Key findings and action plan 2016/17

Issue identified	Management response	Responsible officer and target date
Audit findings		
Income testing <p>We were unable to agree two out of ten items of income we sampled to the supporting documentation provided. We were advised there will be an exercise at the financial year-end to ensure the recharges over the EIS IT provider are accurate and correct. As this is a key area of income, we plan to carry out further audit procedures as part of our ongoing work.</p>	Missing support documentation is now available. We will undertake the year-end calculation post 31 March.	Director - Finance & Audit; 30 April 2017
Financial Sustainability <p>The work carried out by SDS in developing the financial model identifies a significant increase in apprenticeship family expenditure as they work towards achieving the targets set by the Scottish Government. Without a commitment from the Scottish Government for additional funding, there is a risk SDS will have a significant funding gap going forward.</p>	Following the completion of FA and GLA contracting cycles for 2017-19, SDS now has more information on likely costs and timelines. This will be collated for discussion with ELG, then FOP and possibly the SDS Board, prior to discussion at the SDS SG Liaison Group scheduled for 24 April. Thereafter, we will work with SG officials to determine future GIA requirements and those for ESF/successor initiatives.	Director - Finance & Audit; 30 November 2017
Financial Sustainability - Reporting the financial model <p>Elements of the financial model are shared with the Board and the Scottish Government's sponsor department. Presenting the full picture would help promote a shared understanding of SDS's financial position.</p>	We plan to share summary and detailed reports more effectively with ELG and FOP, in the first instance. FOP will guide efficacy re the frequency of Board reporting. We would aspire to discuss the 5-year model with SG colleagues, including the Business Partner, at the monthly Finance Liaison meetings.	Director - Finance & Audit; from May 2017
Financial Management - Finance Reports <p>Finance reports for the Board are prepared on a cash rather than accruals basis and do not include forecasted figures to the year-end. More detailed information is presented to the Finance and Operational Performance Committee but this does not include the forecasted year-end outturn. There is a risk that the Board is not aware of the total outturn forecast for the financial year and this could impact on the level of scrutiny. SDS may wish to consider including the forecasted year-end outturn in the finance reports and providing a high-level summary of FOP presentations to the Board.</p>	The purpose of reporting management accounting information on a cash basis was to drive focus on areas of the business where activities did not appear to be being managed to completion within the budget timeline. This has been discussed with FOP and the full Board, and we included a Commitment column for clarification. The SDS ABR and SBR revisions are the working outturn at any point in time, so any risk would only arise where a variance from those plans arose which was not identified via the cash basis. There is a high level of financial literacy on the Board, and there has never been a challenge on this point, but we will consider re-designing the management accounts from April reporting, in May.	Director - Finance & Audit; from May 2017

Issue identified	Management response	Responsible officer and target date
<p>Role of Boards - Board papers</p> <p>Detailed Board minutes are published on the SDS website but Board papers are not available to the public. The Corporate Office recognises the need to keep this policy under review.</p>	<p>We will continue to monitor SG guidance and good practice.</p>	<p>Director - Corporate Services; ongoing</p>
<p>Role of Boards - Board succession planning</p> <p>SDS need to ensure appropriate succession planning is in place to ensure there are sufficient skills and experience on the Board to enable appropriate scrutiny.</p>	<p>Currently, this is outwith the control of the SDS Board or Executive as SG are undertaking the Enterprise and Skills Agency Review. Recommendations from this review may impact the role, power and format of any SDS Board going forward, so we will keep this matter under review.</p>	<p>Director - Corporate Services; ongoing</p>

14. Any weaknesses identified represent those that have come to our attention during the course of normal audit work and therefore are not necessarily all the weaknesses that may exist. It is the responsibility of management to decide on the extent of the internal control system appropriate to SDS.

15. All our outputs and any matters of public interest will be published on our website: www.audit-scotland.gov.uk.

Skills Development Scotland

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