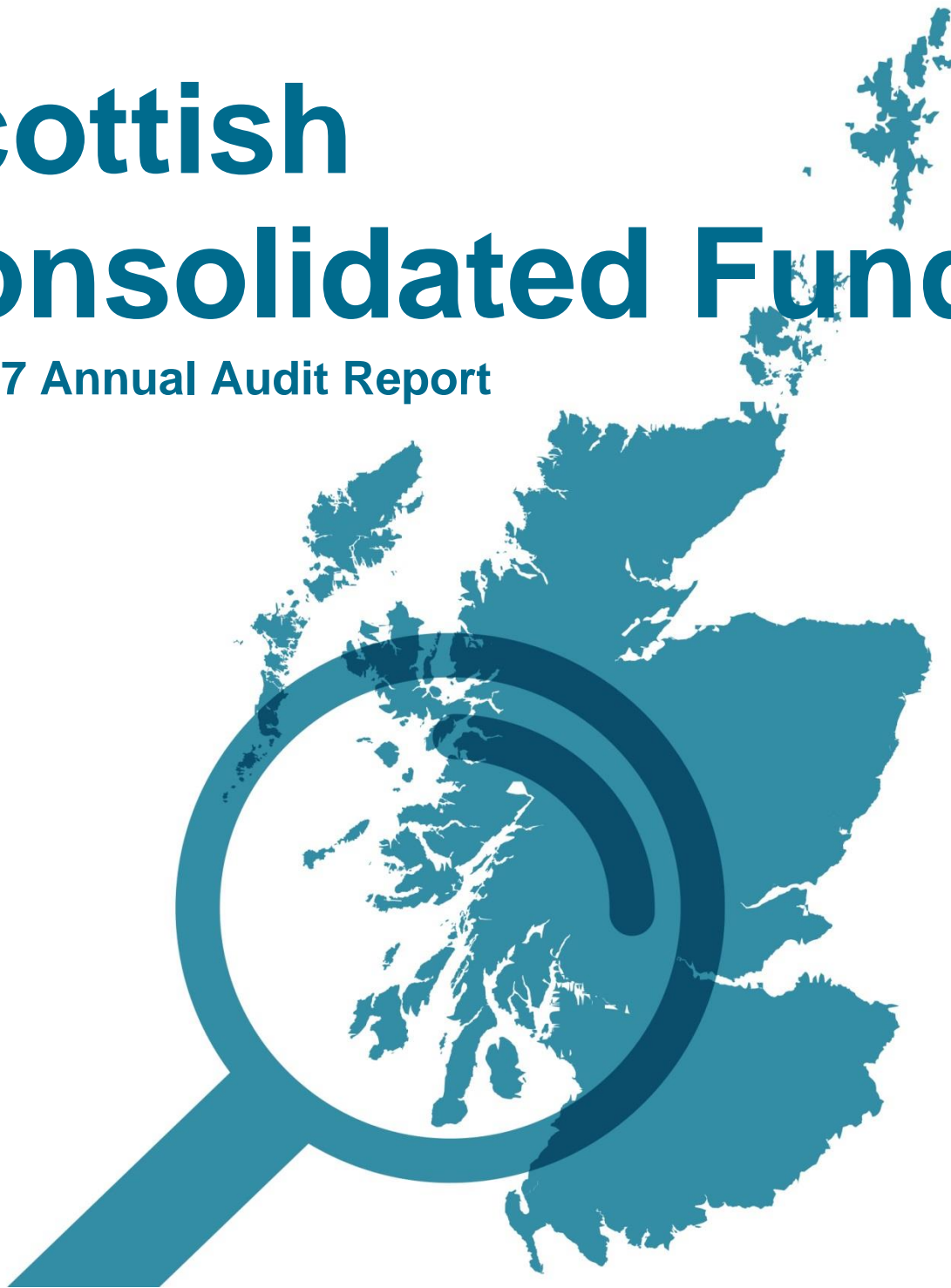


# Scottish Consolidated Fund

2016/17 Annual Audit Report



 AUDIT SCOTLAND

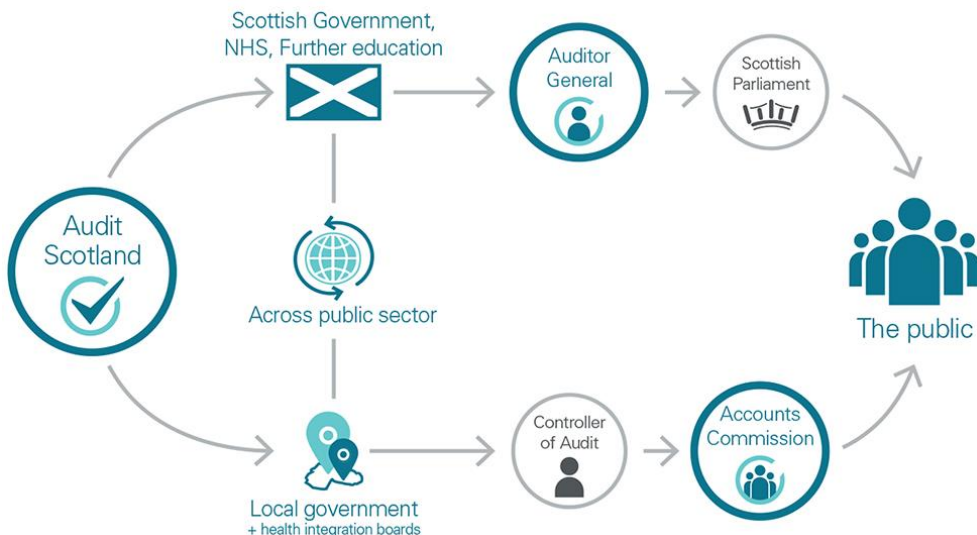
Prepared for the Scottish Government and the Auditor General for Scotland

September 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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# Key messages

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## Audit of the 2016/17 financial statements

- 1** The financial statements of the Scottish Consolidated Fund (SCF) properly present the receipts and payments of the fund for the year ended 31 March 2017 and the balances held at that date.
- 2** The payments and receipts in the financial statements were incurred or applied in accordance with applicable enactments and guidance.
- 3** The other information in the annual report and accounts was consistent with the financial statements and prepared in accordance with legal requirements.
- 4** The independent auditor's report on the 2016/17 Scottish Consolidated Fund account is unqualified.

## Financial management and sustainability

- 5** The Scottish Government had effective overall management of the SCF in 2016/17.
- 6** Systems of internal control operated effectively in 2016/17.

## Governance, transparency and value for money

- 7** We concluded that the Scottish Government has effective governance arrangements in place. The Scottish Government has clarified the role of the Scottish Government Assurance and Audit Committee in relation to its oversight of the Fund.
- 8** Internal audit operates in accordance with the Public Sector Internal Audit Standards.
- 9** The Scottish Consolidated Fund's audited accounts are made available on the Scottish Government's website. In addition, amounts paid to, and received from, other public bodies by the Fund are also reported in individual organisations' accounts, allowing users of the accounts to follow the flow of funds.

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# Introduction

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1. This report is a summary of our findings arising from the 2016/17 audit of the Scottish Consolidated Fund (SCF). The scope of our audit was set out in our 2016/17 Annual Audit Plan. This report comprises:

- an audit of the annual accounts
- consideration of the wider dimensions set out in the [Code of Audit Practice 2016](#) as illustrated in [Exhibit 1](#).

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## Exhibit 1

### Audit dimensions



Source: Code of Audit Practice 2016

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2. The main elements of our audit work in 2016/17 were:

- a review of the key controls in place in relation to the Scottish Consolidated Fund
- an audit of the Scottish Consolidated Fund 2016/17 accounts including the issue of an independent auditor's report setting out our opinions.

3. Scottish Government officials are responsible for:

- preparing the accounts and ensuring they properly present the receipts and payments for the financial year
- ensuring the regularity of transactions, by putting in place systems of internal control.

- 4.** Our responsibilities as independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the [Code of Audit Practice 2016](#), and guided by the auditing profession's ethical guidance.
- 5.** Further details of the respective responsibilities of management and the auditor can be found in the [Code of Audit Practice 2016](#) and supplementary guidance.
- 6.** The weaknesses or risks identified in this report are only those that have come to our attention during our normal audit work, and may not be all that exist. Also, our annual audit report contains an action plan at [Appendix 1 \(page 14\)](#). It sets out specific recommendations, responsible officers and dates for implementation.
- 7.** Communication in this report of matters arising from the audit of the annual report and accounts or of risks or of weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.
- 8.** As part of the requirement to provide fair and full disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2016/17 audit fee for the audit was set out in our Annual Audit Plan and as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.
- 9.** This report is addressed to the Scottish Government's Executive Board and the Auditor General for Scotland and will be made available on Audit Scotland's website [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).
- 10.** We would like to thank all management and staff who have been involved in our work for their cooperation and assistance during the audit.

# Part 1

## Audit of 2016/17 financial statements



### Main judgements

The financial statements of the Scottish Consolidated Fund for 2016/17 properly present the receipts into and payments out of the Fund for the year ended 31 March 2017 and the balances held at that date.

The payments and receipts in the financial statements were incurred or applied in accordance with applicable enactments and guidance.

### Unqualified audit opinions

11. We reported, within our independent auditor's report:

- an unqualified opinion on the financial statements;
- an unqualified opinion on regularity of receipts and payments; and
- an unqualified audit opinion on the Governance Statement.

12. Additionally, we are satisfied that there are no matters which we are required by the Auditor General to report by exception.

### Submission of annual report and accounts for audit

13. We received the unaudited financial statements on 19 June 2017, in line with our agreed audit timetable.

14. The working papers provided with the unaudited financial statements were of a good standard and finance staff provided support to the audit team which helped ensure the final accounts audit process ran smoothly.

### Whole of Government Accounts

15. In accordance with the WGA guidance we completed the required assurance statement and submitted to the National Audit Office (NAO) by the 30 September 2017 deadline.

### Risk of material misstatement

16. [Appendix 2 \(page 15\)](#) provides a description of those assessed risks of material misstatement that were identified during the planning process which had the greatest effect on the overall audit strategy, the allocation of resources to the audit and directing the efforts of the audit team.

The annual report and accounts are the principal means of accounting for the stewardship of its resources and its performance in the use of those resources.

## Materiality

**17.** Materiality defines the maximum error that we are prepared to accept and still conclude that our audit objective has been achieved. The assessment of what is material is a matter of professional judgement. It involves considering both the amount and nature of the misstatement.

**18.** Our initial assessment of materiality for the annual report and accounts was undertaken during the planning phase of the audit and is summarised in [Exhibit 2](#). Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.

**19.** On receipt of the annual report and accounts we reviewed our original materiality calculations and concluded that they remained appropriate.

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## Exhibit 2

### Materiality values

Materiality level	Amount
<b>Overall materiality</b> – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It was set at one per cent of judicial salaries for the year ended 31 March 2017.	£0.3 million
<b>Performance materiality</b> – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality, this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 90 per cent of overall materiality.	£0.27 million
<b>Reporting threshold</b> – We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. For this audit all unadjusted errors are reported.	

Source: Audit Scotland

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## Evaluation of misstatements

**20.** 1 error was found during our audit, breaching performance materiality. The designated receipts amount in the receipts and payments account was originally reported as £25,689k when it should have been £25,405k (a difference of £284k). This was corrected when brought to the attention of the preparer of the accounts and had no impact on our audit approach.

## Significant findings from the audit

**21.** International Standard on Auditing (UK and Ireland) 260 requires us to communicate significant findings from the audit to you. No significant findings were made during the audit of the financial statements.

## Other findings

**22.** Our audit identified a number of presentational and disclosure issues which were discussed with management. These were adjusted and reflected in the audited financial statements.



# Part 2

## Financial management and sustainability



### Main judgements

**The Scottish Government had effective overall management of the SCF in 2016/17.**

**Systems of internal control operated effectively in 2016/17.**

### Financial performance in 2016/17

**23.** The SCF is operated by the Treasury and Banking Branch (TBB) of the Scottish Government. Following the completion of cash flow forecasting exercises, officials make monthly drawdown requests for funding from the UK Consolidated Fund. These amounts are tracked against a maximum limit set by the UK Parliament through the Central Government Supply Estimates.

**24.** In 2016/17 the SCF received funding from this source of £23,058 million, £4 million less than the £23,062 million limit stated in the 2016/17 UK Supplementary Estimate. The limit is set by forecasting the cash requirement for the 2016/17 Scottish budget. Drawing down less than the limit has no effect on the overall spending power of the Scottish Government and the wider Scottish Administration.

**25.** The implementation of the Scotland Act 2012 powers for devolved taxes and enhanced borrowing powers affect the amounts and disclosures in the Scottish Consolidated Fund accounts. The total amount of devolved tax receipts (Land and Buildings Transaction Tax and Scottish Landfill Tax) paid into the SCF in 2016/17 was £636 million. No cash borrowing was undertaken using the enhanced borrowing powers in 2016/17. If the borrowing powers are used in future years, cash generated from borrowing and repayments of principal and interest will be reflected in the SCF.

**26.** Consolidated Fund Extra Receipts (CFERs) of £35.6 million were paid into the SCF in 2016/17. This constitutes income that cannot be applied by Scottish public bodies, in line with applicable legislation. An amount of £25.4 million is classed as designated receipts and was paid over to the UK Consolidated Fund in line with the Designation of Receipts Order 2009.

**27.** The Queen's and Lord Treasurer's Remembrancer collects the unclaimed sums arising from personal estates and sequestrated companies and after a set period pays them over to the SCF. In 2016/17, receipts of £6.3 million are included in the Fund.

**28.** There is no clear guidance or statutory regulations covering the use of non-designated CFERs and QLTR receipts. They cannot be used to fund additional expenditure without the agreement of Her Majesty's Treasury (HMT). The Scottish Government have previously indicated they planned to resolve this issue with HM Treasury in their discussions on the Fiscal Framework, however this has not been included in discussions so far and no guidance has been issued.. See action point 1.

**29.** Payments out of the Fund are made to the Scottish Administration and directly-funded bodies in line with the cash authorisation limits set out in the Scottish Budget. Payments totalling of £33,348 million in 2016/17 were within the overall limit of £33,938 million set by the Budget (Scotland) Act 2016.

**30.** In 2016/17 there was a deficit of receipts over payments of £30.725 million. This decreased the general reserve balance of the Scottish Consolidated Fund to £242.428 million. The balance does not necessarily represent amounts available to spend under budget acts.

## Financial sustainability

**31.** The annual budget setting process sets cash allocation limits for the authorities funded by drawdowns from the SCF and monthly drawdowns are monitored against these limits. Requests for cash allocation increases are processed through budget revisions generating a surplus or deficit for the year.

**32.** A cash reserve is held in the SCF general reserve to manage surpluses or deficits. The reserve currently shows a balance of £242 million, of which £4.8 million is owed to other bodies.

**33.** The main receipts into the Scottish Consolidated Fund come from the Scotland Office, Scottish Rate of Income Tax, Non Domestic Rates and National Insurance Contributions. Payments made are predominantly authorised by the Budget Act to fund spending plans approved by Parliament. The financial statements show that:

- there was a net deficit for the period of £30.725 million.
- the General SCF Reserve balance reduced to £242.428 million. The balance does not necessarily represent amounts available to spend under budget acts.

## Internal controls

**34.** As part of our audit we identify and inspect the key internal controls in those accounting systems which we regard as significant for the production of the financial statements. Our objective is to gain assurance that there are systems of recording and processing transactions in place which provide a sound basis for the preparation of the financial statements.

**35.** The Scottish Consolidated Fund is subject to the same controls that apply to the Scottish Government therefore for this audit we could place reliance on our findings from the interim audit report presented to the Scottish Government Assurance and Audit Committee on 22 June 2017. We concluded that the controls were operating effectively. No significant internal control weaknesses were identified during the audit which could 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 of the SCF.

## Prevention and detection of fraud and irregularity

**36.** We assessed the arrangements for the prevention and detection of fraud in relation to the SCF. Our work as part of the Scottish Government audit covered a number of areas such as whistleblowing and review of the counter fraud strategy.

**37.** We concluded that there are appropriate and adequate arrangements in place for fraud detection and prevention during 2016/17.

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Financial management is about financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

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

**38.** We reviewed the arrangements in place to maintain standards of conduct including the Staff Handbook and Civil Service and Members' Codes of Conduct as part of the wider Scottish Government audit. There are established procedures for preventing and detecting any breaches of these standards including any instances of corruption. The Scottish Consolidated Fund is operated by the Treasury and Banking branch of the Scottish Government and based on our review of the evidence we concluded that the Scottish Government has appropriate arrangements in place for the prevention and detection of bribery corruption. We are not aware of any specific issues that we need to bring to your attention relating to the Scottish Consolidated Fund.

# Part 3

## Governance, transparency and value for money



### Main judgements

**The Scottish Consolidated Fund has effective governance arrangements in place.**

**Internal audit operates in accordance with the Public Sector Internal Audit Standards.**

### Governance arrangements

**39.** The governance arrangements for the Scottish Consolidated Fund operate within the context of the Scottish Government's overall system of corporate governance. Our audit of the 2016/17 Scottish Government's Consolidated Accounts found that the Scottish Government has introduced new governance arrangements during the year. It is too early to comment on their effectiveness.

**40.** The Scottish Government Assurance and Audit Committee (SGAAC) confirmed governance arrangements for the SCF at its meeting on 2 March 2017 that includes oversight of the Fund on an exceptions basis. Any issues relating to reporting or the administration of the Fund will now be escalated to SGAAC.

**41.** Under the UK Government's Financial Reporting Manual (FRoM), the annual report of the Scottish Consolidated Fund must include an annual governance statement within the Annual Report and Accounts. Guidance is set out within the Scottish Public Finance Manual (SPFM) for the content of the statement and provides assurances around the achievement of the organisation's strategic objectives.

**42.** The SPFM does not prescribe a format for the annual governance statement, but sets out minimum requirements for central government bodies. The Governance Statement within the 2016/17 annual report and accounts of the SCF complies with the minimum SPFM requirements.

**43.** We also concluded that the annual governance statement 2016/17 complies with the guidance issued by the Scottish Ministers and, based on our knowledge and work performed, presents an appropriate assessment of governance arrangements and matters.

### Internal audit

**44.** Internal audit provides the Scottish Government and The Principal Accountable Officer with independent assurance on overall risk management, internal control and corporate governance processes.

**45.** The internal audit function is carried out by Scottish Government Internal Audit Directorate. We carried out a review of the adequacy of the internal audit function

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information.

as part of the Scottish Government audit and concluded that it operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place.

**46.** To avoid duplication effort we place reliance on the work of internal audit wherever possible. In 2016/17 we did not place any formal reliance on internal audit reviews for the purpose of obtaining direct assurance for our financial statements work. Also, we considered internal audit report findings as part of our wider dimension work.

## Transparency

**47.** Transparency means that the public have access to understandable, relevant and timely information about how the public bodies are taking decisions and using resources. The Scottish Consolidated Fund audited accounts are made available on the Scottish Government's website. Amounts paid to, and received from, other public bodies by the Fund are also reported in individual organisations' accounts, allowing users of the accounts to follow the flow of funds.

## National performance audit reports

**48.** Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. In March 2017, we published a report [\*Managing new financial powers: an update\*](#), which focused on the new financial powers devolved to the Scottish Parliament as a result of the 2012 and 2016 Scotland Acts. These new powers are of direct relevance to the operation of the SCF and the disclosures within the financial statements. The report made a number of recommendations for the Scottish Government to consider.

**49.** The Scottish Government Executive Board considers our national reports. In addition, we highlight relevant reports to SGAAC in our regular updates to the Committee.

# Appendix 1

## Action plan 2016/17

### Recommendation for improvement



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Issue/risk

Recommendation

Agreed management  
action/timing

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**1. Treatment of QLTR and CFERS**

There remains no clear guidance or statutory regulations in place covering the treatment of QLTR and other miscellaneous receipts within the SCF.

The Scottish Government has indicated they plan to resolve this issue with HM Treasury in their ongoing discussions on the Fiscal Framework.

**Risk**

These balances continue to accumulate with no clear, agreed processes for how they will be applied.

The Scottish Government should develop, in agreement with HMT, clear and comprehensive guidelines covering all relevant receipts within the SCF and how these apply to Scotland.

# Appendix 2

## Significant audit risks identified during planning

The table below sets out the audit risks we identified during our planning of the audit and how we addressed each risk in arriving at our conclusion. The risks are categorised between those where there is a risk of material misstatement in the annual report and accounts and those relating our wider responsibility under the [Code of Audit Practice 2016](#).

Audit Risk	Assurance procedure	Results and conclusions
<b>Risks of material misstatement in the financial statements</b>		
<p><b>1 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>	<p>We performed:</p> <ul style="list-style-type: none"> <li>Detailed testing of journal entries.</li> <li>Testing of all transactions.</li> </ul>	<p>We tested all transactions into and out of the Scottish Consolidated Fund and found no evidence of management override of controls.</p>
<p><b>2 Risk of fraud over income and expenditure</b></p> <p>ISA 240 presumes a risk of fraud in regard to revenue recognition in the financial statements and Practice Note 10 (Audit of financial statements of public sector bodies in the UK) and the Code of Audit Practice expands the ISA assumption to aspects of expenditure.</p>	<p>Testing of all transactions.</p>	<p>We tested all transactions into and out of The Scottish Consolidated Fund and found no evidence of income fraud.</p>
<p><b>3 Financial reporting: Transparency</b></p> <p>The Scottish Government has committed to enhance its financial reporting in the context of new financial powers. This approach should include relevant disclosures in the SCF accounts, given their increased significance in the wider system of financial reporting as the new powers come into effect.</p> <p>This audit risk requires us to assess whether adequate</p>	<p>Draft accounts reviewed to evaluate disclosures.</p>	<p>Disclosures in the draft accounts were judged adequate.</p>

Audit Risk	Assurance procedure	Results and conclusions
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disclosures are made, to enhance understanding of public finances.

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#### Risks identified from the auditor's wider responsibility under the Code of Audit Practice

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#### 4 Governance arrangements

The Scottish Government has implemented revised governance arrangements. As part of the new arrangements, it has determined oversight arrangements for the SCF.

This audit risk requires us to consider the application of the new arrangements as they affect the SCF.

The Scottish Government Audit and Assurance Committee (SGAAC) confirmed governance arrangements for the SCF at its meeting on 2 March 2017.

How the new governance arrangements operated throughout the year was reviewed.

SGAAC's new governance role operates on an exception basis. There were no issues identified during our audit that require formal escalation to SGAAC under the new arrangements.

The SGAAC's Terms of Reference do not currently refer to their role overseeing the Scottish Consolidated Fund. They should be updated as soon as possible to include this detail.

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# Scottish Consolidated Fund

## 2016/17 Annual Audit Report

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