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BÒRD NA GÀIDHLIG

Bòrd na Gàidhlig

Planning report to Audit and Risk Management Committee on the audit for the year ending 31 March 2019

Issued 25 February 2019 for the meeting on 5 March 2019

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Introduction

The key messages in this report:

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

We have pleasure in presenting our draft planning report to the Audit and Risk Management Committee ('the Committee') for the year ending 31 March 2019 audit. We would like to draw your attention to the key messages of this draft audit plan:

Audit Plan

We have updated our understanding of Bòrd na Gàidhlig ('Bòrd') including discussion with management and review of relevant documentation.

Based on these procedures, we have developed this plan in collaboration with the Bòrd to ensure that we provide an effective audit service that meets your expectations and focuses on the most significant areas of importance and risk to the Bòrd.

Key Risks

We have taken an initial view as to the significant audit risks the Bòrd faces. These are presented as a summary dashboard on page 15.

- As with other public sector bodies, the Bòrd continues to face significant financial challenges, due to uncertainty around future funding and the difficulties of staying within the running costs cap of £1,609k, as highlighted in the 2017/18 audit report. An underspend of £479k against budget (£151k against running costs) has been reported for the period to 31 December 2018 and the Bòrd is on track to meet its Departmental Expenditure Limit (DEL) allocated by the Scottish Government for 2018/19.
- Given the pressures across the whole of the public sector, there is an inherent risk associated with the recording of expenditure within this limit, therefore this will be a key focus of our audit.
- Our significant risk is pinpointed to invoices processed around the year-end (including associated accruals and prepayments).
- In accordance with auditing standards, management override of controls has also been identified as a significant audit risk.
- In line with our prior year audit, having considered the risk factors set out in Auditing Standards and the nature of the revenue streams at the Bòrd, we have determined that the risk of fraud arising from revenue recognition can be rebutted. This is based on the fact that there is little incentive to manipulate revenue recognition with the primary source of revenue being from the Scottish Government which can be agreed to third party confirmations.

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Introduction (continued)

The key messages in this report (continued):

Audit Dimensions

The Code of Audit Practice sets our four audit dimensions which set a common framework for all public sector audits in Scotland. These are financial sustainability, financial management, governance and transparency and value for money.

In previous years we have applied the small bodies exemption which restricted our work in this area to reviewing the appropriateness of the disclosures in the governance statement and the financial sustainability of the Bòrd. The Code requires that we judge whether to apply the full wider scope requirements based on risk, nature and size of the body. As part of our planning work we have identified a number of risks in the areas covered by the audit dimensions (as discussed further on pages 18-20), therefore, in agreement with Audit Scotland, have applied the full wider scope for 2018/19.

Our audit work will consider how the Bòrd is addressing these areas and we will report our conclusions in our interim report to the Committee in April 2019 and our annual report to the Committee in August 2019. In particular, our work will focus on:

Financial sustainability – Bòrd na Gàidhlig continues to face significant financial challenges. The overall 2018/19 forecast position as at December 2018 is projecting that the full DEL will be utilised, despite an underspend as at December 2018. This will be achieved primarily by not filling vacancies which have arisen at the Bòrd. The Bòrd anticipates that there will be no significant cash movements – increases or decreases – in the Grant in Aid received from the Scottish Government over the forthcoming years. At the same time, the Bòrd will have to manage an increasing demand for services due to an increased remit under the Education (Scotland) Act 2016 and the increasing number of Gaelic Language Plans in Scotland, whilst also managing cost pressures (primarily as a result of the lifting of the public sector pay cap).

In 2017/18, the Bòrd forecasted a funding gap of £58k in cash terms in running costs for the period to 2020/21, with it potentially not being possible to stay within the running costs limit thereafter. This funding gap is 2% (7% excluding payroll) of the running cost limit to that period. We will consider whether the Bòrd's savings plans are sufficiently robust to deliver the necessary savings to stay within the running costs allocation, and assess any other action (or inaction) of the Bòrd to address the identified funding gap.

Financial management – we will review the budget and monitoring reports to the Bòrd during the year and liaise with internal audit in relation to their work on the financial control environment to assess whether financial management and budget setting is effective. In 2017/18, we noted a number of improvements which could be made to the budget setting process and will follow up on progress in that regard in 2018/19.

We will assess the capacity and resourcing of the finance function given changes in the Head of Finance position and several changes in financial management and monitoring support providers in the year.

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Introduction (continued)

The key messages in this report (continued):

Governance and transparency – in 2017/18, our work in this area was limited to assessing the appropriateness of the disclosures in the governance statement. A number of changes were suggested and implemented, and this area will be considered again as part of our 2018/19 audit.

In addition, our work in 2018/19 will address specific risks which were identified as part of the planning procedures performed for the audit, as follows:

- The vision and objectives of the Bòrd;
- the capacity, skills and resources within the Bòrd;
- the effectiveness of governance, decision making and scrutiny;
- the Board and the Senior Management Team's ('SMT') understanding of their roles and responsibilities, and their adherence to them;
- the behaviour of Board Members and the SMT; and
- the Bòrd's management of risks.

Value for money – in 2016/17 and 2017/18, we noted concerns around the level of grants awarded in the final period of the year. We will review whether decision making appropriately considers value for money in the awarding of grants, and whether the Bòrd sufficiently reviews the outcomes delivered by the bodies which it funds when considering future grant awards.

Our audit work on the audit dimensions will incorporate the specific risks highlighted by Audit Scotland, in particular: the impact of EU withdrawal; the changing landscape for public financial management; dependency on key suppliers, and increased focus on openness and transparency.

Regulatory Change

New accounting standards on revenue and financial instruments will apply for 2018/19, and for leases from 2020/21, following a decision by HM Treasury to defer implementation. While we do not expect these standards to have a significant impact on the Bòrd, we recommend that the Audit and Risk Management Committee review the impact of IFRS 9 and 15 in the year, including calculating any adjustments that will be required as at 31 March 2018 for transition. We would suggest that the Audit and Finance Committee receive reporting in year from management on the implementation of the new standard, and we will report specifically on the findings from our audit work in this area.

We have reported on other regulatory changes and sector developments on pages 28-31.

Our Commitment to Quality

We are committed to providing the highest quality audit, with input from our market leading specialists, sophisticated data analytics and our wealth of experience.

Adding value

Our aim is to add value to the Bòrd through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Bòrd promote improved standards of governance, better management and decision making and more effective use of resources.

Pat Kenny
Audit director

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Responsibilities of the Audit and Risk Management Committee

Helping you fulfil your responsibilities

The primary purpose of the Auditor's interaction with the Audit and Risk Management Committee:

- Clearly communicate the planned scope of the financial statements audit.
- Provide timely observations arising from the audit that are significant and relevant to the Committee's responsibility to oversee the financial reporting process.
- In addition, we seek to provide the Committee with additional information to help fulfil your broader responsibilities.

We use this symbol throughout this document to highlight areas of our audit where the Committee need to focus their attentions.

As a result of regulatory change in recent years, the role of the Audit and Risk Management Committee has significantly expanded. We set out here a summary of the core areas of Committee responsibility to provide a reference in respect of these broader responsibilities and highlight throughout the document where there is key information which helps the Committee in fulfilling its remit.

Oversight of external audit

- At the start of each annual audit cycle, ensure that the scope of the external audit is appropriate.

- Implement a policy on use of the external auditor for non-audit services and approve these services if they arise.

Integrity of reporting

- Make an impact assessment of key judgements and the level of management challenge.

- Review the external audit findings, key judgements and level of misstatements.

- Assess the quality and capacity of the internal team.

- Assess the completeness of disclosures, including consistency with disclosures on business model and strategy and, where requested by management, provide advice in respect of the fair, balanced and understandable statement.

- Assess and advise on the appropriateness of the Annual Governance Statement.

Internal controls and risks

- Review the internal control and risk management systems.

- Explain what actions have been, or are being taken to remedy any significant failings or weaknesses.

- Oversee the work of the Bòrd's local counter fraud service.

Oversight of internal audit

- Consider annually whether the scope of the internal audit programme is adequate.

- Monitor and review the effectiveness of the internal audit activities.

Whistleblowing and fraud

- Ensure that appropriate arrangements are in place for the proportionate and independent investigation of any concerns that are raised by staff in connection with improprieties.

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Our audit explained

We tailor our audit to your Bòrd and your strategy

Identify changes in the Bòrd and its environment

The Bòrd continues to face significant financial pressures, with it being increasingly difficult to stay within the running costs cap, managed at present by not filling vacancies. There have been various changes in the finance function in the year and a number of concerns raised about management and governance at the Bòrd.

This is discussed on pages 9-10.

Scoping

Our scope is in line with the Code of Audit Practice issued by the Audit Scotland.

More detail is given on pages 12-13.

In our final report

In our final report to you we will conclude on the significant risks identified in this paper, report to you our other findings, and detail those items we will be including in our audit report.

Identify Changes in your business and environment → Determine materiality → Scoping → Significant risk assessment → Conclude on significant risk areas → Other findings → Our audit report

Determine materiality

We have determined a materiality of £105k (2017/18: £106k). This is based on forecasted gross expenditure, consistent with the basis used in the prior year. We have determined a performance materiality of £78k (2017/18: £79k).

We will report to you any misstatements above £5.25k (2017/18: £5.3k). More detail given on page 11.

Significant risk assessment

We have identified significant audit risks in relation to the Bòrd, pinpointed to the achievement of expenditure resource limits and management override of controls. More detail is given on pages 14-17. These significant risks are consistent with those identified in our prior year audit.

Quality and Independence

We confirm all Deloitte network firms are independent of the Bòrd. We take our independence and the quality of the audit work we perform very seriously. Audit quality is our number one priority.

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Continuous communication and reporting

Planned timing of the audit

Planning	Interim	Year end fieldwork	Reporting
• Planning meetings to inform risk assessment and identify judgemental accounting issues. • Update understanding of key business cycles and changes to financial reporting. • Document design and implementation of key controls for significant risks. • Review of key Bòrd documents including Board and Committee minutes. • Planning work for wider scope responsibilities.	• Update risk assessments for any developments since the planning phase before fieldwork begins. • Initiate wider scope procedures. • Report to the Audit and Risk Management Committee on the findings from our wider scope work on vision, leadership, governance and accountability.	• Review of draft accounts. • Substantive testing of all material areas. • Follow up on interim report and finalisation of work in support of wider scope responsibilities. • Detailed review of annual accounts, including Annual Governance Statement. • Review of final internal audit reports and opinion. • Completion of testing on significant audit risks.	• Final Audit and Risk Management Committee. • Issue final Annual Report to the Bòrd and the Auditor General. • Issue audit report and submission of audited financial statements to Audit Scotland. • Audit feedback meeting.
2018/19 Audit Plan	Interim report to the Committee	Final report to the Committee	
November-February	**January-March**	**July-August**	**September**

Ongoing communication and feedback

Audit Team

Pat Kenny, Audit Director

Karlyn Watt, Senior Manager

Conor Healy, Field Manager

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An audit tailored to you
Focusing on your business and strategy

	Impact on our audit
Future financial strategy and sustainability	The prior year audit report noted that the Bòrd's financial monitoring arrangements were sound. The Bòrd has historically met its expenditure resource limit and is anticipated to do so in 2018/19. However, the Bòrd continues to face significant financial challenges, particularly in light of the ongoing cap on running costs (which has dropped in real terms by over 5% since 2014/15). This reduction, combined with increasing staff costs due to the lifting of the public sector pay cap, will place additional pressure on the ability of the Bòrd to deliver its services. It is important to note that the Bòrd has identified a need for £58k (2% overall; 7% of non-payroll costs) of savings in running costs to 2020/21, and noted that without a lifting of the running costs cap, the Bòrd will struggle to deliver services within its expenditure resource limit from 2020/21 onwards. The anticipated financial position reinforces the need for the Bòrd to review the services it provides – linked with the outcomes they deliver, aligned to the Scottish Government's national outcomes, the National Gaelic Language Plan and the Bòrd's corporate plan – to enable the Bòrd to identify areas where service provision can be made more efficient, streamlined, or stopped if this is necessary in order to achieve financial balance and sustainability over the medium to longer term. Linked with the above is the need for the Bòrd to consider the size and skills of its workforce – ensuring it is sufficient to deliver the services which the Bòrd is required to deliver – and the impact of this on the Bòrd's ability to meet resource limits, given that staff costs account for the vast majority of Bòrd running costs. Vacancies in key posts and difficulties in recruiting in the year highlight the need for sufficient workforce planning to be carried out by the Bòrd to deal with changes in the staffing structure, particularly in key roles (such as senior management). This should include appropriate arrangements for succession planning and career progression. It is vital that the Bòrd identifies the workforce it requires – in terms of size, skillset and cost – both for the present environment and the future and develops plans to deliver that workforce.

New significant risk

Continuing significant risk

Considered as part of wider scope audit requirements

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An audit tailored to you

Focusing on your business and strategy

	Impact on our audit
Governance and transparency	As part of our planning work, we identified a number of risk areas, in particular concerning the vision and leadership of the Bòrd and the governance and accountability arrangements in place. As a result of these risks and in agreement with Audit Scotland, we concluded that a full wider scope audit is required to consider these risks. Over the last year there have been a number of changes within the Bòrd, in particular changes in the Senior Management Team, changes in the finance function and a change in the Chair to the Board. Our work in this area will specifically focus on the following key areas: • ***The vision and objectives of the Bòrd.*** We will assess the commitment of the Board and Senior Management Team ('SMT') to this and the direction they provide on it. We will consider whether the vision and objectives of the Bòrd are reflected on and progressed by partner organisations, the communication of the vision and progress against it to staff, and the engagement of staff in the Bòrd. • The ***capacity, skills and resources*** within the Bòrd to deliver the strategic objectives. This will include considering the development of leadership skills and capacity, the awareness of and actions taken to address gaps in skills and resources, and the ability of the management team to work effectively as a corporate unit • The ***effectiveness of the governance, decision-making and scrutiny arrangements***. This will include reviewing the documentation of key discussions and decisions, systems of financial governance, procedures in place for complaints handling and general governance arrangements. • Board members and senior management's ***roles and responsibilities***. This will include considering compliance with the Bòrd Code of Conduct, adherence to the distinction between operational and strategic responsibilities, compliance with policies and procedures. We will review the impact of each of these areas on the effectiveness of decision making and the scrutiny at the Bòrd. • ***Management of risk,*** assessing the monitoring of key risks and actions to mitigate them taken by the Bòrd. • ***Board members and management behaviour***. This will include reviewing standards of conduct, procedures in place and guidance available to Board Members. We will also consider the training and support available to the Board, the SMT and staff in general. Our findings from this part of our audit work will be reported to the Audit and Risk Management Committee in April 2019.

New significant risk

Continuing significant risk

Considered as part of wider scope audit requirements

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Materiality

Our approach to materiality

Basis of our materiality benchmark

- The Audit Director has determined materiality as £105k (2017/18: £106k) and a performance materiality of £78k (2017/18: £79k), based on professional judgement and risk factors specific to the Bòrd, the requirement of auditing standards and the financial measures most relevant to users of the financial statements.
- We have used 2% (2017/18: 2%) of forecasted gross expenditure of the Bòrd as the benchmark for determining materiality and applied 75% (2017/18: 75%) as performance materiality.
- This approach to determining materiality is consistent with our prior year materiality calculation.

Reporting to those charged with governance

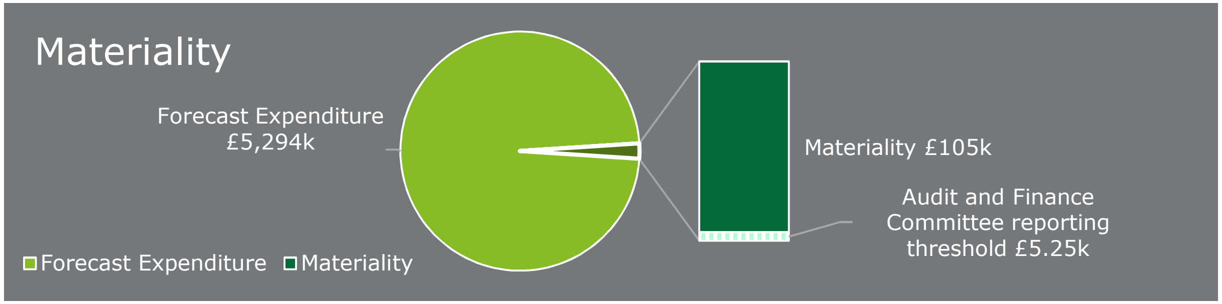
- We will report to you all misstatements found in excess of our clearly trivial threshold which is £5.25k (2017/18: £5.3k).
- We will report to you misstatements below this threshold if we consider them to be material by nature.

- Our approach to determining the materiality benchmark is consistent with Audit Scotland guidance which states that the threshold for clearly trivial above which we should accumulate misstatements for reporting and correction to audit committees must not exceed £250k.

Our annual audit report

We will:

- Report the materiality benchmark applied in the audit of the Bòrd;
- provide comparative data and explain any changes in materiality, compared to prior year, if appropriate; and
- explain any normalised or adjusted benchmarks we use, if appropriate.



Although materiality is the judgement of the Audit Director, the Audit and Risk Management Committee must satisfy themselves that the level of materiality chosen is appropriate for the scope of the audit.

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Scope of work and approach

Our key areas of responsibility under the Code of Audit Practice

Core audit work	Planned output	Timeline
Perform an ISA (UK) compliant audit of the annual accounts	• Annual audit plan • Independent auditor's report	• March 2019 • September 2019
Audit and report on the audit dimensions	• Annual audit plan • Interim audit report • Annual audit report	• March 2019 • April 2019 • August 2019
Share audit intelligence with Audit Scotland including highlighting potential statutory reports	• Current issues returns	• January 2019 • July 2019
Carry out preliminary enquiries into referred correspondence	• None	• N/A
Provide information on cases of fraud	• Fraud returns	• November 2018 • February 2019 • May 2019 • August 2019
Provide information on cases of money laundering	• Audit Scotland to advise	• As required
Contribute to technical guidance notes	• Consultation comments on draft technical guidance notes	• As required

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Scope of work and approach (continued)

Our approach

Liaison with internal audit

The Auditing Standards Board's version of ISA (UK) 610 "Using the work of internal auditors" prohibits use of internal audit to provide "direct assistance" to the audit. Our approach to the use of the work of Internal Audit has been designed to be compatible with these requirements.

We will review their reports and liaise with them to discuss their work. We will discuss the work plan for internal audit, and where they have identified specific material deficiencies in the control environment we consider adjusting our testing so that the audit risk is covered by our work.

Using these discussions to inform our risk assessment, we can work together with internal audit to develop an approach that avoids inefficiencies and overlaps, therefore avoiding any unnecessary duplication of audit requirements on the Bòrd's staff.

Approach to controls testing

Our risk assessment procedures include obtaining an understanding of controls considered to be 'relevant to the audit'. This involves evaluating the design of the controls and determining whether they have been implemented ("D&I").

The results of our work in obtaining an understanding of controls and any subsequent testing of the operational effectiveness of controls will be collated and the impact on the extent of substantive audit testing required will be considered.

Obtain an understanding of the Bòrd and its environment including the identification of relevant controls.

Identify risks and controls that address those risks.

Carry out D&I work on relevant controls.

If considered necessary, test the operating effectiveness of selected controls.

Design and perform a combination of substantive analytical procedures and tests of details that are most responsive to the assessed risks.

Promoting high quality reporting to stakeholders

We view the audit role as going beyond reactively checking compliance with requirements: we seek to provide advice on evolving good practice to promote high quality reporting.

The National Audit Office prepare a checklist each year designed to ensure that entities covered by the Government financial reporting manual (FReM) have prepared their annual accounts in the appropriate form and have complied with all disclosure requirements. We would recommend the Bòrd consider this during drafting the Annual Report & Accounts.

Audit Scotland has published good practice guides in relation the annual report and the Governance Statement to support the Bòrd in preparing high quality drafts of the Annual Report & Accounts, which we would recommend the Bòrd consider during drafting.

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Significant risks

Our risk assessment process

We consider a number of factors when deciding on the significant audit risks. These factors include:

- The significant risks and uncertainties previously reported in the annual report and financial statements;
- the IAS 1 critical accounting estimates previously reported in the annual report and financial statements;
- our assessment of materiality;
- the changes that have occurred in the business and the environment it operates in since the last annual report and financial statements; and
- the Bòrd's actual and planned performance on financial and other governance metrics compared to its peers.

Principal risk and uncertainties

- Reduction in Grant-in-Aid.
- ICT and cyber-security.
- Political support for Gaelic.
- Staff workload.

Changes in your business and environment

- Changes in senior management personnel.
- Changes in the finance function.
- Change in Chair of the Board.

IAS 1 Critical accounting estimates

- Pension liability.

The next page summarises the significant risks that we will focus on during our audit. All the risks mentioned in the prior year Audit and Risk Management Committee report are included as significant risks in this year's audit plan.

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Significant risks
Dashboard

Risk	Material?	Fraud risk identified?	Planned approach to controls testing	Level of management judgement	Page no.
Achievement of expenditure resource limits	✓	✓	Design and implementation	⚠	16
Management override of controls	✓	✓	Design and implementation	⚠	17

⚠ Some degree of management judgement

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Significant risks (continued)
Risk 1 – Achievement of expenditure resource limits

Risk identified	The key financial duty for the Bòrd is to comply with the DEL allocated by the Scottish Government to cover cash expenditure and non-cash costs such as depreciation and amortisation. Given the pressures across the whole of the public sector, there is an inherent risk associated with the occurrence and completeness of recording of expenditure as there is an incentive for management to either over or under accrue expenditure at the year-end, depending on the forecast position, in order to meet the allocation.
Our response	We will evaluate the results of our audit testing in the context of the achievement of the targets set by the Scottish Government. Our work in this area will include the following: • Evaluate the design and implementation of the controls around the monthly monitoring of financial performance and journal entry postings. • Obtain independent confirmation of the resource limits allocated to the Bòrd by the Scottish Government. • Perform focussed testing of accruals and prepayments made at the year-end. • Perform focussed testing of invoices received and paid around the year-end.

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Significant risks (continued)
Risk 2 – Management override of controls

We will use computer assisted audit techniques, including Spotlight, to support our work on the risk of management override

Risk identified	In accordance with ISA 240 (UK) management override is a significant risk. This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Bòrd's controls for specific transactions. The key judgments in the financial statements are those which we have selected to be the significant audit risks around completeness and accuracy of expenditure. This is inherently the areas in which management has the potential to use their judgment to influence the financial statements.
Our response	In considering the risk of management override, we plan to perform the following audit procedures that directly address this risk: **Journal testing** • We will test the design and implementation of controls over journal entry processing. • Using our Spotlight data analytics tool, we will risk assess journals and select items for detailed follow up testing. The journal entries will be selected using computer-assisted profiling based on areas which we consider to be of increased interest. • We will test the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting. **Accounting estimates** • We will test the design and implementation of controls over key accounting estimates and judgements. • We will review accounting estimates for biases that could result in material misstatements due to fraud. This will include both a retrospective review of 31 March 2018 estimates and a review of the corresponding estimates as at 31 March 2019. **Significant and unusual transactions** • We will obtain an understanding of the business rationale of significant transactions that we become aware of that are outside of the normal course of business for the Bòrd, or that otherwise appear to be unusual, given our understanding of the entity and its environment.

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Wider scope requirements
Audit dimensions

The Code of Audit Practice sets our four audit dimensions which set a common framework for all public sector audits in Scotland. We will consider how the Bòrd is addressing these areas, including any risks to their achievement, as part of our audit work as follows:

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.	• The financial planning systems in place across the shorter and longer terms. • The arrangements to address any identified funding gaps. • The affordability and effectiveness of funding and investment decisions made. • Workforce planning.	The Bòrd provides a range of services which it is not statutorily obliged to provide. The cost of providing these services is not immediately clear. We will consider the Bòrd's approach to prioritisation of services within the funding available to ensure it meets its statutory obligations. We will also assess the robustness of the plans put in place by the Bòrd to remain within the running costs cap. The Bòrd has identified a £58k funding gap in running costs to 2020/21 (2% overall; 7% excluding payroll costs), noting it may not be possible to stay within the running costs cap thereafter. **Audit Risk:** The Bòrd may be unable to achieve the necessary savings to stay within the running costs limit whilst meeting its statutory commitments, particularly due to funding restrictions and the use of resources on non-statutory services. In view of the Scottish Government's Medium Term Financial Strategy (MTFS) (discussed further on page 22) we will consider the extent to which the Bòrd has reviewed the potential implications of the MTFS for its own financial planning and whether it is taking these into account in its arrangement for financial management and financial sustainability. **Audit Risk:** The Bòrd's long-term financial planning is inconsistent with the Scottish Governments five-year plan. The Bòrd has a number of vacancies in key posts and has had difficulty recruiting given that it operates in a niche field. Workforce planning needs to be robust to ensure that the Bòrd has the right level of staff with the correct skillset to enable the Bòrd to deliver services. We will consider the robustness of workforce and succession planning at the Bòrd. **Audit Risk:** The Bòrd may not have sufficient and appropriate staffing in place to deliver on its statutory obligations.

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Wider scope requirements

Audit dimensions (continued)

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.	• Systems of internal control. • Budgetary control system. • Financial capacity and skills, including changes in the finance function. • Arrangements for the prevention and detection of fraud.	We will monitor financial performance and outturn reports prepared by the Bòrd in 2018/19. We will specifically consider the changes in the finance team and the arrangements in place for the provision of financial advice which occurred in the year, monitoring the impact this has on ongoing financial management, including the year-end annual accounts process. **Audit Risk:** Finance team capacity is insufficient to deal with the scale of work required. In 2017/18, we noted that there were a number of improvements which could be made to the budget setting process. In view of the Scottish Government's new budget process (discussed further on page 22) we will confirm that underlying financial performance is transparently presented and that budget setting is robust. **Audit Risk:** Budget setting is inappropriate and the underlying financial performance of the Bòrd is not transparently reported. Our fraud responsibilities and representations are detailed on pages 33 and 34.
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.	• Governance arrangements. • Scrutiny, challenge and transparency on decision making and financial and performance reports. • Accountable officers' duty to secure Best Value.	Effective Board and managerial leadership is central to delivering best value, through setting clear priorities and working effectively in partnership to achieve improved outcomes. Leaders should demonstrate behaviours and working relationships which foster a culture of co-operation and a commitment to continuous improvement and innovation. As discussed on page 10, we will consider the vision and objectives of the Bòrd and the capacity, skills and resources to deliver the strategic objectives. **Audit Risk:** Lack of effective Board and managerial leadership could impact on the ability of the Bòrd to deliver best value.

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Wider scope requirements

Audit dimensions (continued)

Audit dimension	Areas to be considered	Impact on the 2018/19 Audit
Governance and transparency (continued)		Governance arrangements should be in place to support the Board in taking informed decisions, effective scrutiny of performance and stewardship of resources. Openness and transparency in decision-making, schemes of delegation and reporting performance is essential. As discussed on page 10, we will consider the effectiveness of governance, decision-making and scrutiny; Board member and senior management's roles and responsibilities; the management of risk; and Board members and management behaviour. **Audit Risk:** Inadequate or ineffective governance arrangements could impact on the Board's ability to take informed decisions and perform its scrutiny and stewardship role. In view of the increased focus on how public money is used and what is achieved (as discussed further on page 22), we will consider how the Bòrd has reviewed its approach to openness and transparency. **Audit Risk:** The Council's approach is not keeping pace with public expectation and good practice.
Value for money is concerned with using resources effectively and continually improving services.	• Link between money spent and outputs and the outcomes delivered. • Improvement of outcomes. • Focus on and pace of improvement.	During 2018/19, we will review how the Bòrd is addressing areas where targets are not being met, areas of strategic importance to the Bòrd and areas of focus for the Bòrd. **Audit Risk:** There is a risk that insufficient resources are targeted to areas of under performance. In 2016/17 and 2017/18, we noted concerns around the level of grants awarded in the final period of the year. We will review whether decision making appropriately considers value for money in the awarding of grants, and whether the Bòrd sufficiently reviews the outcomes delivered by the bodies which it funds when considering future grant awards. **Audit Risk:** The Bòrd may not sufficiently address value for money considerations in the awarding of grants to funded bodies, potentially resulting in insufficient focus on improving and delivering outcomes.

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Wider scope requirements (continued)
Specific risks

As part of the 2018/19 planning guidance, Audit Scotland have identified the following areas as significant risks faced by the public sector. Any specific risks in relation to these areas for the Bòrd have been included in our audit risk under the audit dimensions, discussed on the previous pages. We will continue to monitor these areas as part of our audit work.

Risk	
EU withdrawal	There are uncertainties surrounding the terms of the UK's withdrawal from the European Union in March 2019. Some arrangements have been provisionally agreed, such as a transition period to the end of 2020, although they are dependent on a final deal being reached between the UK Government and the remaining EU countries. The outcome of negotiations should become clearer as we approach 29 March 2019. Whatever the outcome, EU withdrawal will inevitably have implications for devolved government in Scotland and for audited bodies. Audit Scotland has identified three areas where EU withdrawal may have the most significant impact as summarised below: • **Workforce** – Many public services are dependent on workers from EU countries, including health, social care and education. A decline in migration from the EU could potentially result in vacancies and skills gaps in some areas of the public sector. There is a risk that this could impact on some public bodies' ability to deliver 'business as usual' particularly given existing workforce and service pressures. • **Funding –** Funding from the EU makes an important contribution to the Scottish public sector. The main sources of funding provide support to farmers and rural businesses, projects to encourage economic growth and support for research and education. The UK Government has made guarantees to meet some funding commitments to the end of existing programmes, but there are uncertainties about what any replacement funding may look like. • **Regulation –** The EU Withdrawal Bill will transpose existing EU law into UK law immediately after the UK leaves the EU. Legislation in many devolved areas will transfer to the Scottish Parliament. The UK government has identified 24 devolved policy areas where it seeks to retain temporary control until UK-wide common legislative frameworks are developed. In addition, some public bodies may be affected directly by changes to trade and customs rules, which could impact on supply chains and the procurement of goods or services from EU countries. This could influence the availability and cost of supplies and services (e.g. specialist medical equipment or drugs) with potential implications for public bodies' finances and their ability to deliver specific services. While there are considerable uncertainties about the detailed implications of EU withdrawal, at a minimum by the end of 2018/19, we would expect public bodies to have assessed the potential impact of EU withdrawal on their operations and identified any specific risks and how they will respond to them. We will assess how the Bòrd has prepared for EU withdrawal and how it continues to respond to any emerging risk after March 2019. Some suggested key questions for the Audit and Risk Management Committee are included in our technical update on page 29.

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Wider scope requirements (continued)

Specific risks (continued)

Risk	
Changing landscape for public financial management	Scottish public finances are fundamentally changing, with significant tax-raising powers, new powers over borrowing and reserves, and responsibility for 11 social security benefits worth over £3 billion a year transferring to the Scottish Government. This provides the Scottish Parliament with more policy choices but also means that the Scottish budget is subject to greater volatility, uncertainty and complexity. Parliamentary scrutiny of the public finances is increasingly important in this changing landscape. A new Scottish budget process has been introduced, which is based on a year-round continuous cycle of budget setting, scrutiny and evaluation. This involves parliamentary committees looking back to explore what public spending has achieved, looking forward to longer-term objectives and challenges, and considering what this should mean for future budgets. As part of the new budget process, the Scottish Government published an initial five-year Medium Term Financial Strategy (MTFS) in May 2018. This five-year outlook for the Scottish budget provides useful context for audited bodies' financial planning. As part of our wider scope audit work on financial sustainability (discussed further on page 18), we will consider how the Bòrd has reviewed the potential implications of the MTFS for its own finances, including longer-term financial planning. The new budget process places greater emphasis on assessing outcomes and the impact of spending. There is an expectation that the Scottish Government and public bodies will report on their contributions towards the national outcomes in their published plans and performance reports, including their annual reports. Increased complexity and volatility is also likely to mean that the Scottish Government will be increasingly active in managing its overall budget position in-year, engaging with public bodies closely on their anticipated funding requirements. As part of our wider scope audit work on financial sustainability (page 18) and value for money (page 20), we will consider the extent to which the Bòrd's performance report provides an accessible account of the body's overall performance and impact of its public spending. We will also confirm that underlying financial performance, including any in-year changes to funding agreed with the Scottish Government, is transparently presented.

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Wider scope requirements (continued)

Specific risks (continued)

Risk	
Dependency on key suppliers	It has become clear that the collapse of Carillion has had a significant impact across the public sector. This has brought into focus the risk of key supplier failure and the risk of underperformance in suppliers that are experiencing difficult trading conditions. The risk exists on two levels: • Individual public sector bodies are dependent on key suppliers; and • The Scottish public sector as a whole is subject to significant systematic risk. We will determine as part of our detailed risk assessment the extent to which the Bòrd is dependent on key supplier relationships. Where dependency is significant, we will consider this as part of our audit work and report back to the Audit and Risk Management Committee. We will also be requested to complete a short questionnaire to establish the extent, value and nature of key supplier dependencies that can inform the national position. Given that the main areas of expenditure for the Bòrd are staff costs and grant awards, we do not anticipate this to be a material concern for the Bòrd.
Openness and transparency	There is an increasing focus on how public money is used and what is achieved. In that regard, openness and transparency supports understanding and scrutiny. In 2017/18, we proactively engaged with the Bòrd on improving the Annual Report & Accounts to aid improve transparency and will continue to do so in 2018/19. We would expect to see the Bòrd reviewing its approach to openness and transparency to ensure it is keeping pace with public expectations and good practice. Evidence of progress might include: • Increased public availability of Bòrd papers; • more insight into why some business is conducted in private; and • development of the form and content of annual reports.

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Wider scope requirements (continued)

Other responsibilities

Performance Audits

In accordance with Audit Scotland planning guidance, we will be requested to provide information to support performance audits that Audit Scotland intends to publish during 2018/19 and 2019/20, as summarised below:

Title and planned publication date	Local auditor input
Digital progress in central government – Spring/ Summer 2019	We will be asked to inform the performance audit team of any significant ICT and digital developments within their audited body.

Impact reports

We will also be requested to provide information to support assessing the impact of previously published performance audit reports. There are no specific impact reports which directly relate to the Bòrd. We will provide an update to the Audit and Risk Management Committee if there are any changes to this plan.

Anti-money laundering

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 came into force on 26 June 2017 and replace the Money Laundering Regulations 2007. The regulations impose an obligation of the Auditor General to inform the National Crime Agency if she knows or suspects that any person has engaged in money laundering or terrorist financing. As part of our audit work, we will ensure we are informed of any instances of money laundering at the Bòrd so that we can advise the Auditor General.

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Audit Quality

Our commitment to audit quality

Our objective is to deliver a distinctive, quality audit to you. Every member of the engagement team will contribute, to achieve the highest standard of professional excellence.

In particular, for your audit, we consider that the following steps will contribute to the overall quality:

- We will apply professional scepticism on material issues and significant judgements identified, by using our expertise in the central government sector and elsewhere to provide robust challenge to management.
- We have obtained a deep understanding of your business, its environment and of your processes (specifically grant income and expenditure recognition, payroll processing and financial reporting), enabling us to develop a risk-focused approach tailored to the Bòrd.
- Our engagement team is selected to ensure that we have the right subject matter expertise and industry knowledge. We will involve specialists to support the audit team in our work as appropriate.

In order to deliver a quality audit to you, each member of the core audit team will receive tailored learning to develop their expertise in audit skills, delivered by Pat Kenny and other sector experts. This includes sector specific matters, and audit methodology updates.

Engagement Quality Control Review

We have developed a tailored Engagement Quality Control approach. Our dedicated Professional Standards Review (PSR) function will provide a 'hot' review before any audit or other opinion is signed. PSR is operationally independent of the audit team, and supports our high standards of professional scepticism and audit quality by providing a rigorous independent challenge.

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Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to establish our respective responsibilities in relation to the financial statements audit, to agree our audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes:

- Our audit plan, including key audit judgements and the planned scope;
- Key regulatory and corporate governance updates, relevant to you.

What we don’t report

As you will be aware, our audit is not designed to identify all matters that may be relevant to the Bòrd.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, the views on internal controls and business risk assessment in our final report should not be taken as comprehensive or as an opinion on effectiveness since they will be based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

Other relevant communications

We will update you if there are any significant changes to the audit plan.

This report has been prepared for the Audit and Risk Management Committee, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

We welcome the opportunity to discuss our report with you and receive your feedback.

Pat Kenny, CPFA

for and on behalf of Deloitte LLP

Glasgow

25 February 2019

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Sector developments

The State of the State
Government beyond Brexit

Overview

Now in its seventh year, **The State of the State** has once again brought together Deloitte LLP and Reform to reflect on the most pressing public sector issues along with new, exclusive research. Central to the report is our citizen survey, which provides a platform for the most important voices of all in the public sector: that of the public. Also exclusive to the report is our research with the people who know the public sector's challenges best: the people who run it.

This year, we interviewed fifty senior figures including civil servants, police leaders, NHS directors and Council Chief Executives, producing the most extensive qualitative research of its kind in the sector.

This year's The State of the State finds the UK government amid the complex and politically-charged challenge of leaving the EU. But while Brexit may dominate daily headlines, our report finds a wider set of challenges – and opportunities – for government and the public services as they gear up for a Spending Review.

Key findings	
Scotland's government has now been led by the Scottish National Party for three consecutive terms in office	In those eleven years, the administration has taken forward the possibilities of devolution to shape a Scottish public sector landscape that now differs substantially from the rest of the UK – in its public finances, its policy priorities and its ethos.
Austerity has flipped public attitudes to tax and spending -	As austerity began in 2010, more than half of the public backed spending cuts to restore the public finances. In 2018, as the Prime Minister calls a formal end to the austerity years, our exclusive citizen survey finds that support has dwindled to less than one fifth of the public.
People are increasingly concerned about public services and their future provision	Our survey finds that the public is increasingly concerned about public services. It suggests that the past four years have seen a decline in the number of people who think that public bodies understand their needs, listen to their preferences and involve them in decisions – perhaps driven by perceptions of austerity. Looking to the future, the number of people who are worried that the state will provide too little support for them in the years ahead has risen from fifty per cent in 2010 to seventy per cent this year.
Citizen views differ significantly across the UK's four countries	Recent years have seen an acceleration in the public policy differences between the devolved administrations, and our survey finds that citizen attitudes also differ. For example, people in Scotland are more likely to believe that taxes should be higher to pay for more public services, people in Northern Ireland are less likely to say they have felt the effects of austerity, and people in Wales are the most likely to say that public services listen to their needs. These differing views underscore the diverging political and policy landscapes across the UK.
The public back penalty fines for wasting public sector time	Our citizen survey explored the circumstances in which the public would find charges reasonable, and found that the most acceptable would be penalty fines for wasting public sector time, like missing NHS appointments or wrongly calling out the emergency services.

Next steps

The report is available at https://www2.deloitte.com/content/campaigns/uk/the-state-of-the-state/the-state-of-the-state/the-state-of-the-state.html

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UK exit from the EU

Navigating uncertainty – key questions for the Audit & Risk Management Committee

Whilst nobody can predict the outcome of negotiations, we can be sure that Brexit will require all organisations to take some big decisions. As we have seen, some will require lengthy and complicated preparations, and we advise keeping track of the negotiations and thinking what this means for the Bòrd sooner rather than later.

Is the Bòrd set up to navigate the change?

Have you assessed the impact of potential changes and identified key decision points?

Does your assessment include how Brexit could impact on your customers, supply chain and people?

Have you defined the options there are to respond? E.g. scenario or contingency planning?

Are you monitoring developments and are you ready to act proportionately at the right time?

Are all the right people involved? Does this include discussion with key stakeholders?

Are channels of communication clear, both internally and externally, and have company spokespeople been fully briefed?

Impact on internal planning, forecasting and strategy

Is management using forward-looking indicators such as forward bookings, contact conversion rates and supplier forward pricing?

Have cash reserves, financing requirements and longer term viability all been assessed?

Have opportunities as well as risks been considered?

Impact on internal and external audit

Should the scope and plan for internal audit be amended to include contingency planning, or testing key risk indicators?

Should internal audit be asked to perform work on longer term viability?

Is there an impact on critical accounting judgments and areas of estimation uncertainty that need to be discussed with the external auditor?

Impact on external reporting

Will disclosures on principal risks and uncertainties need to be revisited in light of the departure of the UK from the EU on 29 March 2019?

Have you developed a plan for appropriately detailed disclosure in management commentary?

"We encourage companies to provide disclosure which distinguishes between the specific and direct challenges to their business model and operations from the broader economic uncertainties which may still attach to the UK's position when they report. Where there are particular threats, for example the possible effect of changes in import/export taxes or delays to their supply chain, we expect these to be clearly identified and for management to describe any actions they are taking, or have taken, to manage the potential impact. In some circumstances this may mean recognising or remeasuring certain items in the balance sheet.

The broad uncertainties that may still attach to Brexit when companies report will require disclosure of sufficient information to help users understand the degree of sensitivity of assets and liabilities to changes in management's assumptions."

(FRC Letter to CFOs and Audit Committee Chairs, October 2018)

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Appendix: New Accounting Standards

IFRS 9 *Financial Instruments*

In a nutshell

- In July 2014, the IASB published a final version of IFRS 9. This version supersedes all previous versions.
- IFRS 9 *Financial Instruments* will replace IAS 39 *Financial Instruments: Recognition and Measurement*, and has three main impacts
  - *Classification and measurement* - introduces new approach for the classification of financial assets driven by cash flow characteristics and the business model in which an asset is held. This classification determines how financial assets are accounted for in financial statements and, in particular, how they are measured on an ongoing basis.
  - *Amortised cost and impairment of financial assets* – introduces an "expected losses" impairment model where entities are required to account for expected credit losses from when financial instruments are first recognised.
  - *Hedge accounting* - introduces new general hedge accounting model that aligns the accounting treatment with risk management activities and allows for better reflection of the hedging activities in the financial statements.
- HM Treasury has adopted IFRS 9 from 2018/19 onward, with a number of interpretations and adaptations for the public sector, generally simplifying the requirements.
- The key practical change in IFRS 9 for most central government bodies is the introduction of a new approach to recognising impairments of debtors and other financial instruments.
  - The key change to IFRS 9 affecting the Bòrd will be the movement from an incurred losses model for receivables to an expected credit losses (ECL) model. The move is intended to reflect that there is always a risk of late/ non-payment when granting credit and that this should be reflected in the value of receivables upon recognition.
  - If the debt is later repaid in full, the ECL creditor can be reversed. ECL creditors should be set up on a portfolio rather than arrangement-by-arrangement basis, i.e all ECL's for overseas visitors will be scored to one creditor.
  - A further change from IAS 39 to IFRS 9 will be that all financial assets are recognised as Fair Value through Profit or Loss, unless where there are specific business cases to designate alternative treatment.

Effective date

The Standard has a mandatory effective date for annual periods beginning on or after 1 January 2018, with earlier application permitted.

HM Treasury have decided that on transition there will be no restatement of comparatives, and any impact of transition will be recognised as a reserves movement in 2018/19.

Find out more on our UK Accounting Plus website www.iasplus.com/en-gb by following the links to Standards -> IFRS 9

Potential impact on the Bòrd

Given the historically low levels of debtors and other financial instruments held by the Bòrd, IFRS 9 is expected to have relatively limited impact. However, it will nevertheless affect the process of assessing impairment of debtors and other financial assets as noted above.

As part of the process of adoption, the Bòrd will need to consider the impact on policies, processes, systems and people. This may include reviewing how entries are posted for impairment of assets, given the requirement to provide on initial recognition for lifetime expected credit losses. We would recommend that the Bòrd review the impact of IFRS 9 in the year, including calculating any adjustments that will be required as at 31 March 2018 for transition. We would suggest that the Audit and Risk Management Committee receive reporting from management on the implementation of the new standard, and we will report specifically on the findings from our audit work in this area.

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Appendix: New Accounting Standards

IFRS 16 *Leases*

In a nutshell

- The new Standard supersedes IAS 17 *Leases* and its associated interpretative guidance.
- For lessees the distinction between operating and finance leases disappears.
- A lease conveys the right to control an identified asset for a period of time in exchange for consideration.
- The accounting for all leases is similar to finance lease accounting in IAS 17, which means all leases are recognised on the balance sheet (with some exceptions).
- The lease liability is measured at the present value of the future lease payments, using a lease term that includes periods covered by extension options if exercise is reasonably certain. Variable lease payments are only included in the liability if based on an index or rate.
- That right-of-use asset is initially measured at the amount of the lease liability, plus initial direct costs and adjustments for lease incentives, payments at or prior to commencement and dilapidations provisions.
- The right-of-use asset is subsequently accounted for by applying IAS 16 *Property, Plant and Equipment*, at cost less depreciation and impairment (unless it is an investment property that is fair valued or it belongs to a class of property, plant and equipment that is revalued).
- A lessee can elect to keep the following leases off-balance sheet and typically straight line the expense:
  - leases with a lease term of 12 months or less and containing no purchase option – this election is made by class of underlying asset; and
  - leases where the underlying asset has a low value when new, such as personal computers or small office furniture – this election is made on a lease-by-lease basis.
- Operating lease expenses, typically straight line, will be replaced with interest on the liability and depreciation of the asset, producing a front-loaded expense profile.
- Although any individual lease will have a front-loaded expense, portfolios of leases containing both new and mature leases may produce an overall expense profile similar to straight line expensing.
- HM Treasury has consulted across government and is considering specific interpretations and adaptions for consistency across the public sector, but which will follow the overall principles of IFRS 16.

Effective date

Periods commencing on or after 1 January 2019. HMT is planning to adopt for 2020/21 in the public sector.

Find out more on our UK Accounting Plus website www.iasplus.com/en-gb by following the links to Standards -> IFRS 16

Potential impact on the Bòrd

HM Treasury announced in 2018/19 that the implementation of IFRS 16 would be delayed until 2020/21. We would recommend that the Bòrd review the impact of IFRS 16 during 2019/20, so that the impact can be understood and reflected in budgeting for 2020/21. We do not anticipate any material impact on the Bòrd given that its potential lease portfolio consists purely of premises and that this has a term of 12 months or less and will therefore apply for the exemption, allowing the Bòrd to maintain the lease off-balance sheet and straight line the expense as at present.

We would suggest that the Audit and Risk Management Committee receive reporting in year from management on expected impact of the new standard, to support the disclosure in the financial statement on accounting standards not yet effective. We will report to the Audit and Risk Management Committee on any observations on the Bòrd's approach in 2018/19, and on findings from our audit work in 2019/20 onwards.

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Appendices

Fraud responsibilities and representations

Responsibilities explained

Your responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Our responsibilities:

- We are required to obtain representations from your management regarding internal controls, assessment of risk and any known or suspected fraud or misstatement.
- As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risks section of this document, we have identified the risk of fraud in the achievement of expenditure resource limits and management override of controls as a key audit risk for your organisation.

Fraud characteristics:

- Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.
- Two types of intentional misstatements are relevant to us as auditors – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

We will request the following to be stated in the representation letter signed on behalf of the Bòrd:

- We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- We are not aware of any fraud or suspected fraud that affects the entity and involves:
  - (i) management;
  - (ii) employees who have significant roles in internal control; or
  - (iii) others where the fraud could have a material effect on the financial statements.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

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Fraud responsibilities and representations
Inquiries

We will make the following inquiries regarding fraud:

Management

- Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether management has knowledge of any actual, suspected or alleged fraud affecting the entity.

Internal audit and local counter fraud specialist

- Whether internal audit and the Bòrd's local counter fraud specialist has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain their views about the risks of fraud.

Those charged with governance

- How those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks.
- Whether those charged with governance have knowledge of any actual, suspected or alleged fraud affecting the entity.
- The views of those charged with governance on the most significant fraud risk factors affecting the entity.

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Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Bòrd and will reconfirm our independence and objectivity to the Bòrd for the year ending 31 March 2019 in our final report to the Audit and Risk Management Committee.
Fees	The audit fee for 2018/19 is £26,764 as analysed below. This incorporates a provisional amount of £14,344 due in relation to the application of the full wider scope audit work, as agreed with Audit Scotland: £ Auditor remuneration 23,894 Audit Scotland fixed charges: Pooled costs 2,300 Audit support costs 570 **Total proposed fee** **26,764** There are no non-audit services fees proposed for the period.
Non-audit services	In our opinion there are no inconsistencies between the FRC's Ethical Standard and the Bòrd's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.
Relationships	We have no other relationships with the Bòrd, its Board, senior managers and affiliates, and have not supplied any services to other known connected parties.

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Our approach to quality
AQR team report and findings

We maintain a relentless focus on quality and our quality control procedures and continue to invest in and enhance our overall firm Audit Quality Monitoring and Measuring programme.

In June 2018 the Financial Reporting Council ("FRC") issued individual reports on each of the eight largest firms, including Deloitte, on Audit Quality Inspections which provides a summary of the findings of its Audit Quality Review ("AQR") team for the 2017/18 cycle of reviews.

We take the findings of the AQR seriously and we listen carefully to the views of the AQR and other external audit inspectors. We remediate every finding regardless of its significance and seek to take immediate and effective actions, not just on the individual audits selected but across our entire audit portfolio. We are committed to continuously improving all aspects of audit quality in order to provide consistently high quality audits that underpin the stability of our capital markets.

We have improved the speed by which we communicate potential audit findings, arising from the AQR inspections and our own internal reviews to a wider population, however, we need to do more to ensure these actions are embedded. In order to achieve this we have launched a more detailed risk identification process and our InFlight review programme. This programme is aimed at having a greater impact on the quality of the audit before the audit report is signed. Consistent achievement of quality improvements is our aim as we move towards the AQR's 90% benchmark.

All the AQR public reports are available on its website. https://www.frc.org.uk/auditors/audit-quality-review/audit-firm-specific-reports

The AQR's 2017/18 Audit Quality Inspection Report on Deloitte LLP

"The overall results of our reviews of the firm's audits show that 76% were assessed as requiring no more than limited improvements, compared with 78% in 2016/17. Of the FTSE 350 audits we reviewed this year, we assessed 79% as achieving this standard compared with 82% in 2016/17. We are concerned at the lack of improvement in inspection results. The FRC's target is that at least 90% of these audits should meet this standard by 2018/19."

"Where we identified concerns in our inspections, they related principally to aspects of group audit work, audit work on estimates and financial models, and audit work on provisions and contingencies. During the year, the firm has continued to develop the use of "centres of excellence", increasing the involvement of the firm's specialists in key areas of the audit. We have no significant issues to report this year in most of the areas we reported on last year."

"The firm has revised its policies and procedures in response to the revised Ethical and Auditing Standards. We have identified some examples of good practice, as well as certain areas for improvement."

The firm has enhanced its policies and procedures in the following areas:

- Increased use of centres of excellence ("CoE") involving the firm's specialists, including new CoEs focusing on goodwill impairment (established in response to previous inspection findings) and corporate reporting, to address increasing complexity of financial reporting.
- Further methodology updates and additional guidance issued to the audit practice including the audit approach to pension balances, internal controls, data analytics, group audits and taxation.
- A new staff performance and development system was implemented with additional focus on regular timely feedback on performance, including audit quality.
- Further improvements to the depth and timeliness of root cause analysis on internal and external inspection findings.

Our key findings in the current year requiring action by the firm:

- Improve the group audit team's oversight and challenge of component auditors.
- Improve the extent of challenge of management's forecasts and the testing of the integrity of financial models supporting key valuations and estimates.
- Strengthen the firm's audit of provisions and contingencies.

Review of firm-wide procedures. The firm should:

- Enhance certain aspects of its independence systems and procedures.

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