

Scottish Funding Council

Annual Audit Plan 2018/19



 AUDIT SCOTLAND

Prepared for the Scottish Funding Council

December 2018

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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Risks and planned work

1. This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice](#), and other relevant guidance. This plan sets out the work necessary to allow us to provide an independent auditor's report on the financial statements and meet the wider scope requirements of public-sector audit.

2. The wider scope of public audit contributes to assessments and conclusions on financial management, financial sustainability, governance and transparency and value for money.


Adding value


3. We aim to add value to the Scottish Funding Council (SFC) through our external audit work by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. In so doing, we intend to help SFC promote improved standards of governance, better management and decision-making and more effective use of resources. Where appropriate, we will recommend actions that support continuous improvement and summarise areas of good practice identified from our audit work. We will also ensure there are clear links between the annual audit work and relevant national performance audits. This will include, for example, work to follow-up the recommendations in our 'Scotland's colleges 2018' report.


Audit risks


4. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main audit risk areas for SFC. We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

Exhibit 1 2018/19 Key audit risks

 Audit Risk	Source of assurance	Planned audit work
Financial statements issues and risks		
<p>1 Risk of management override of controls</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 to change the position disclosed in the financial statements.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance.</p>	<ul style="list-style-type: none"> • Detailed testing of journal entries. • Review of accounting estimates. • Focused testing of accruals and prepayments. • Evaluation of significant transactions that are outside the normal course of business.

 Audit Risk	Source of assurance	Planned audit work
<p>2 Risk of fraud over expenditure</p> <p>Most public-sector bodies are net expenditure bodies and therefore the risk of fraud is more likely to occur in expenditure.</p> <p>The risk of fraud over expenditure also exists in SFC due to the complexity and extent of expenditure incurred in carrying out its functions.</p>	<p>Key controls working effectively.</p> <p>Sound budgetary control and monitoring arrangements in place.</p> <p>Counter-fraud arrangements well established and working effectively.</p>	<ul style="list-style-type: none"> Analytical procedures on expenditure streams. Detailed testing of expenditure transactions focusing on the areas of greatest risk. Substantive cut-off testing of expenditure to ensure it is recognised in the correct financial year.
<p>3 Grants paid to colleges and universities</p> <p>The main activity of SFC is the award and payment of grants to colleges and universities. Due to the complexities around different year end dates and re-profiling of budgets, there is a risk that grants paid to institutions are incorrectly recorded in the financial statements.</p>	<p>Sound budgetary control and monitoring arrangements in place.</p> <p>Outcome agreements with colleges and universities.</p> <p>SFC receive monthly cash flow projections from the colleges which detail payments made to date and future projections.</p>	<ul style="list-style-type: none"> Detailed testing of grant funding controls. Focused substantive testing of formula-based grant awards to individual bodies. Sample testing of grant commitments at the year end. Substantive cut-off testing of grant payments to ensure they are recognised in the correct financial year.
<p>4 Financial transactions</p> <p>SFC receives financial transactions funding from the Scottish Government which sets conditions on how they are used. The level of this funding has increased significantly from £16.2m in 2017/18 to £40.0m in 2018/19. SFC has used the funding to issue loans to universities.</p> <p>There is a risk that loans issued to universities are incorrectly recorded in SFC's financial statements and that use of financial transactions funding does not meet conditions set by the Scottish Government.</p>	<p>Officers keep up to date with any changes to the accounting framework and seek support where necessary.</p> <p>Guidance to universities indicating the eligibility requirements for projects.</p> <p>Evaluation of bids to ensure compliance.</p>	<ul style="list-style-type: none"> Review appropriateness of accounting treatment to ensure it is correct, in particular compliance with the new requirements of IFRS 9 <i>Financial instruments</i>. Consider the control arrangements in place for evaluating applications to ensure they meet the required conditions. Review how SFC ensures money is used for the purpose agreed. Review loan agreements to ensure the regularity and validity of the use of financial transactions funding.
<p>5 European social fund</p> <p>SFC is the lead partner for the Developing Scotland's Workforce European Social Fund (ESF) programme. It provides funding to colleges and claims European funding through the Scottish Government. It was also the lead partner for the Youth Employment Initiative ESF programme which ended in 2017/18 but for which claims are still outstanding.</p> <p>In prior years SFC accounted for ESF income on a cash basis due to</p>	<p>Officers reassess the accounting treatment of ESF income in preparing SFC's accounts.</p>	<ul style="list-style-type: none"> Review evidence of amount and timing of receipt of ESF income and whether the accounting treatment adopted is appropriate.

 Audit Risk	Source of assurance	Planned audit work
<p>uncertainty about the amount and timing of its receipt.</p> <p>The degree of uncertainty has reduced and there is the risk that the previous accounting approach is no longer appropriate and results in incorrect treatment in the accounts.</p>		
Wider dimension issues and risks		
<p>6 Financial sustainability</p> <p>SFC's strategic plan for 2015 to 2018 contains high level objectives on the use of resources. Financial plans for higher education and further education cover a one-year period.</p> <p>There is a risk that SFC does not have the information available to support a longer-term view of its financial position including, for example, the potential financial impact of significant events, such as EU withdrawal.</p>	<p>The outcome agreement process and related guidance.</p> <p>Regular monitoring of institutions through the engagement framework.</p> <p>Colleges' five-year financial forecasts.</p> <p>Universities' four-year strategic plan forecasts.</p> <p>Briefing material to include deeper analysis of the direct and indirect impact of the UK leaving the EU.</p>	<ul style="list-style-type: none"> • Review SFC's progress on drafting medium to long-term financial plans. • Consider SFC's arrangements for monitoring and reporting on the financial health of institutions. • Review updates to briefing material.
<p>7 Workforce plan</p> <p>There are increasing demands on SFC's resources. This includes work to support the Enterprise and Skills strategic board (see below), preparing for the implications of EU withdrawal and administering ESF funding to colleges. SFC does not have a workforce plan setting out how it will manage its resources in response to these pressures.</p> <p>There is a risk that workforce decisions are not coordinated leading to decisions in one area having unintended consequences in another.</p>	<p>Risk recognised in risk register and discussed at board meetings.</p> <p>SFC is developing a workforce plan.</p> <p>Temporary staff are in place to assist with the ESF checks.</p> <p>Funding from the Scottish Government for temporary posts to provide support in relation to EU withdrawal related work.</p>	<ul style="list-style-type: none"> • Monitor SFC's progress in developing its workforce plan and review once finalised.
<p>8 Enterprise and skills review – strategic plan</p> <p>In October 2018, the enterprise and skills strategic board published its first strategic plan. The plan aims to provide clarity around strategic direction to SFC and other enterprise and skills agencies with the overall aim to increase productivity and drive inclusive and sustainable economic growth in Scotland. The agencies are expected to progress actions set out in the strategic plan through</p>	<p>Regular reports to the board.</p> <p>On-going engagement between SFC, the strategic board and the Scottish Government.</p> <p>Active involvement in the strategic board's four 'mission' groups.</p> <p>New three-year corporate plan which aligns with the planning cycle of the other enterprise and skills agencies and is informed by</p>	<ul style="list-style-type: none"> • Review the new framework document between SFC and the Scottish Government for clarity over new roles, responsibilities and accountabilities. • Review performance management arrangements in place to determine and report on the impact of new arrangements. • Monitor progress with SFC's new corporate plan and strategic plan and review once published.

	Audit Risk	Source of assurance	Planned audit work
	<p>enhanced collaboration and alignment.</p> <p>There is a risk that the transition to the new arrangements affects SFC's effectiveness in the short-term.</p>	<p>the priorities of the strategic board.</p> <p>SFC has extended its 2015-18 strategic plan by one year with the agreement of the Scottish Government.</p>	
9	<p>Openness and transparency</p> <p>There is increasing focus on how public bodies spend their money and the level of transparency in reporting. Openness and transparency supports understanding and scrutiny of the use of public money.</p> <p>There is a risk that SFC does not provide a full and transparent account of its budget, how it has applied its budget and its overall performance.</p>	<p>SFC has agreed to consider the content of its 2018/19 performance report to ensure it provides users of the annual report and accounts with a more understandable analysis of its performance.</p>	<ul style="list-style-type: none"> Review disclosures in the 2018/19 performance report.

Source: Audit Scotland

Reporting arrangements

5. Audit reporting is the visible output for the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

6. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

7. We will provide an independent auditor's report to SFC, the Scottish Parliament and the Auditor General for Scotland setting out our opinions on the annual accounts. We will provide the Accountable Officer and Auditor General for Scotland with an annual report on the audit containing observations and recommendations on significant matters which have arisen during the audit.

Exhibit 2 2018/19 Audit outputs

Audit Output	Target date	Committee Date
Annual Audit Plan	4 December 2018	11 December 2018
Management Report	27 February 2019	6 March 2019
Annual Audit Report	6 June 2019	13 June 2019
Independent Auditor's Report	25 June 2019	25 June 2019

Source: Audit Scotland

Audit fee

8. The proposed audit fee for the 2018/19 audit of SFC is £72,980 [2017/18: £71,500]. In determining the audit fee we have taken account of the risk exposure of SFC Scottish Funding Council, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited annual accounts with complete working papers on 3 May 2019.

9. Where our audit cannot proceed as planned through, for example, late receipt of unaudited annual accounts or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises out with our planned audit activity.

Responsibilities

Audit and Compliance Committee and Accountable Officer

10. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

11. The audit of the annual accounts does not relieve management or the Audit and Compliance Committee as those charged with governance, of their responsibilities.

Appointed auditor

12. Our responsibilities as independent auditors are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice (including supplementary guidance) and guided by the Financial Reporting Council's Ethical Standard.

13. Auditors in the public sector give an independent opinion on the financial statements and other information within the annual accounts. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

14. The annual accounts, which include the financial statements, will be the foundation and source for most of the audit work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of SFC and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how SFC will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free of material misstatement.

15. We will give an opinion on whether the financial statements:

- give a true and fair view in accordance with the Further and Higher Education (Scotland) Act 2005 and directions made thereunder by the Scottish Ministers of the state of affairs of SFC as at 31 March 2019 and of its net expenditure for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2018/19 FReM;
- have been prepared in accordance with the requirements of the Further and Higher Education (Scotland) Act 2005 and directions made thereunder by the Scottish Ministers.



characteristics



responsibilities



principal activities



risks



governance arrangements

Other information in the annual accounts/financial statements

16. We also review and report on other information published within the annual accounts including the performance report, annual governance statement and the remuneration report. We give an opinion on whether these have been compiled in accordance with the appropriate regulations and frameworks in our independent auditor's report.

17. We also read and consider any information in the annual accounts other than the financial statements and audited part of the remuneration report and report any uncorrected material misstatements.

Materiality

18. We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinions in the independent auditor's report.

19. We calculate materiality at different levels as described below. The calculated materiality values for SFC Scottish Funding Council are set out in [Exhibit 3](#).

Exhibit 3 Materiality values



Materiality	Amount
Planning materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross expenditure for the year ended 31 March 2019 based on the audited accounts for 2017/18.	£17.8 million
Performance materiality – 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 75% of planning materiality.	£13.4 million
Reporting threshold (i.e., clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount. This has been calculated at 1% of planning materiality.	£180,000

Source: Audit Scotland

Timetable

20. To support the efficient use of resources it is critical that the annual accounts timetable is agreed with us to produce the unaudited accounts. We have included an agreed timetable at [Exhibit 4](#).

Exhibit 4 Annual accounts timetable

 Key stage	 Date
Latest submission date of unaudited annual accounts with complete working papers	3 May 2019
Latest date for final clearance meeting with Director of Finance	30 May 2019
Issue of Letter of Representation and proposed independent auditor's report	6 June 2019
Agreement of audited unsigned annual accounts	25 June 2019
Issue of Annual Audit Report to those charged with governance	25 June 2019
Independent auditor's report signed	26 June 2019
Latest date for signing of WGA return	28 September 2019

Internal audit

21. Internal audit is provided by Scott-Moncrieff. As part of our planning process we carry out an annual assessment of the internal audit function to ensure that it operates in accordance with Public Sector Internal Audit Standards (PSIAS).

Subject to completion of this review, we plan to consider internal audit's work as outlined below.

Using the work of internal audit

22. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible to avoid duplication. We plan to consider the findings of the work of internal audit as part of our planning process to minimise duplication of effort and to ensure the total resource is used efficiently or effectively.

23. From our initial review of internal audit plans we plan to consider internal audit work in the following areas:

- Financial controls
- Budget setting
- Grant funding distribution
- Institutional review
- Data security and information governance
- GDPR health-check.

Audit dimensions

24. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#).

Exhibit 5

Audit dimensions



Source: Code of Audit Practice

Financial sustainability

25. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the body's financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. We will carry out work and conclude on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of arrangements in place to address any identified funding gaps
- whether SFC can demonstrate the affordability and effectiveness of funding and investment decisions it has made.

Financial management

26. Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We will review, conclude and report on:

- whether SFC has arrangements in place to ensure systems of internal control are operating effectively
- whether SFC can demonstrate the effectiveness of the budgetary control system in communicating accurate and timely financial performance
- how SFC has assured itself that its financial capacity and skills are appropriate
- whether SFC has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

Governance and transparency

27. 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. We will review, conclude and report on:

- whether SFC can demonstrate that the governance arrangements in place are appropriate and operating effectively.
- whether there is effective scrutiny, challenge and transparency on the decision-making and finance and performance reports.
- the quality and timeliness of financial and performance reporting.

Value for money

28. Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether:

- SFC can provide evidence that it is demonstrating value for money in the use of its resources.
- SFC can demonstrate that there is a clear link between money spent, output and outcomes delivered.
- SFC can demonstrate that outcomes are improving.
- There is sufficient focus on improvement and the pace of it.
- SFC assesses its compliance with the principles of Best Value by carrying out periodic self-assessment exercises.
- SFC has addressed the recommendations agreed in the 'Scotland's colleges 2018' performance audit report.

Independence and objectivity

29. Auditors appointed by the Accounts Commission or Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual “fit and proper” declaration for all members of staff. The arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland’s Ethics Partner.

30. The engagement lead (i.e. appointed auditor) for SFC is Gordon Smail, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of SFC.

Quality control

31. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor’s report or opinion is appropriate in the circumstances.

32. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice (and supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews and internal quality reviews. Additionally, the Institute of Chartered Accountants of Scotland (ICAS) have been commissioned to carry out external quality reviews.

33. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

Scottish Funding Council

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If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or info@audit-scotland.gov.uk

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Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk