Historic Environment Scotland

Report to the Audit, Risk and Assurance Committee (ARAC), the Board and the Auditor General for Scotland on the 2019/20 audit

Issued on 5 August for the meeting on 14 August 2020

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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.

I have pleasure in presenting our final report to the Audit, Risk and Assurance Committee (ARAC) of Historic Environment Scotland (HES) and Historic Environment Scotland Enterprises Limited (HESe) for the 2019/20 audit. The scope of our audit was set out within our planning report presented to the ARAC in February 2020.

This audit was carried out under unusual circumstances, being a remote audit conducted during the national lockdown in response to COVID-19. We recognise the extra pressure faced by HES staff through this challenging time in making a rapid move to working from home, preparing the annual report and preparing for a remote audit. We engaged early with management on the potential implications of COVID-19 for the preparation of the annual report as well as the audit, and management confirmed their desire to work to the original timetable. While the shift to remote working placed pressure on the original timetable for preparation of the annual report and completion of the audit, we have worked closely with management to mitigate this whilst maintaining audit quality as our number one focus.

This report summarises our findings and conclusions in relation to:

- The audit of the **financial statements**; and
- Consideration of the **four audit dimensions** that frame the wider scope of public sector audit requirements as illustrated in the following diagram. This includes our consideration of the Accountable Officers' duty to secure best value.

Introduction (continued)

The key messages in this report (continued)

I would like to draw your attention to the key messages of this paper:

Conclusions from our testing

Based on our audit work completed to date we expect to issue a modified audit opinion for both HES and HESe.

The impact of COVID-19 has led to a number of changes to our audit report during the audit process, in particular:

- a material uncertainty being identified by HES's property valuers in relation to the valuation of its property assets. As a result, we expect to include an 'Emphasis of Matter' paragraph within our audit report.
- the restrictions on movement in the UK in March meant that HES staff were unable to perform all of its planned year-end stock count and we have been unable to attend any counts. As set out in auditing standards, there is an acceptance that stock counts cannot be conducted where there is a threat to the safety of the auditor. In line with this, given the current situation, government guidance and our firm policy, we were unable to perform stock counts. In addition, we were unable to perform alternative procedures to satisfy ourselves as to the existence and condition of stock as at the year-end. As a result, our opinion is expected to be qualified as a result of the limitation of scope on stock existence and condition for both HES and HESe.

Whilst HES has estimated a reduction in commercial income of £53m for the financial year 2020/21, we have concluded that this does not represent a material uncertainty in relation to going concern given ongoing support from the Scottish Government.

Given the significant impact of COVID-19 on HES, we reviewed our risk assessment and performed significant additional work, including ongoing discussion with management, on the above areas. As a result of the increased risk associated with the audit and the concurrent increase in audit work required, we will be proposing an increase in audit fee for 2019/20. This will be discussed with management as part of the close down of the audit. The fee set out on page 50 has not been updated to reflect this additional work.

The Performance Report and Accountability Report comply with the statutory guidance and proper practice and are consistent with the financial statements and our knowledge of the HES. We note that the linkage of performance to national outcomes is strong and represents best practice.

The Charities Statement of Recommended Practice (Charities SORP) does not require a separate Remuneration and Staff Report, however, HES has chosen to publish one in accordance with the requirements of the Government Financial Reporting Manual (FReM) to aid transparency.

We have included specific disclosure deficiencies in the Remuneration and Staff Report on page 46. These included correcting the calculation of the median pay ratio, trade union facility time disclosures in the prescribed format and restating the staff composition table to match the restated headcount disclosure.

Following correction of the deficiencies by management, we are satisfied that the auditable parts of the Remuneration and Staff Report have been prepared in accordance with the relevant regulation.

A summary of our work on the significant risks is provided in the dashboard on page 11. HES met its financial targets for 2019/20 with a small overall surplus at the end of the year.

Four misstatements in excess of our reporting threshold of £103k (HES: £91k; HESe: £15k) and four disclosure deficiencies identified up to the date of this report have been reported on page 44 which were corrected by management. The most significant adjustments relate to the dilapidations provision (£826k), legal provision (£960k) and reimbursement asset – insurance monies which cover legal claims (£944k) as discussed on page 14. We identified one uncorrected misstatement relating to the deferral of membership income which is detailed on page 43.

Introduction (continued)

The key messages in this report (continued)

Conclusions on audit dimensions

As set out on page 3, our audit work covered the four audit dimensions. Our audit work was risk based and proportionate, covering each of the four dimensions.

The outbreak of COVID-19 has brought unprecedented challenges to organisations around the country. It is not yet known what long-term impacts these will have on populations and on the delivery of public services, but they will be significant and could continue for some time. While this report makes reference to COVID-19 where relevant in each of the dimensions, as well as our considerations on the impact of the financial statements, we have not considered the full impact of COVID-19 on HES at this stage.

Financial management **-** HES continues to have strong financial management arrangements which are sufficiently robust to manage financial activity and capture and address any challenges to the achievement of financial targets. Financial performance is transparently reported to the Senior Management Team (SMT) and Board throughout the year. The Financial Strategy action plan includes a commitment to undertake a targeted efficiency review which we welcome.

Financial sustainability - HES has achieved short-term financial balance in 2019/20, ending the year with a small surplus. Some positive progress had been made in the year, with the update of the Financial Strategy and associated actions and the implementation of the Programme for Success. There also continues to be a robust budget setting process in place. However, given the significant financial impact that COVID-19 has had, and is expected to have on HES, there remains a significant risk of achieving financial sustainability in both the short and medium-to-long term.

Governance and transparency – HES's governance framework and arrangements continue to support good governance and accountability. It continues to have a strong executive leadership and effective scrutiny in place through the ARAC. There has been a positive response to the challenges faced by the COVID-19 pandemic, with appropriate arrangements in place to ensure sufficient support and oversight.

The Board continues to be open and transparent in its decision making and has demonstrated a commitment to continuous improvement through the action plan developed following the 2018 staff survey.

Value for money – HES has a clear and effective performance monitoring framework in place to ensure that its performance is monitored and reported in line with Key Performance Inidicators (KPIs) set out in the 3 year Corporate Plan and Annual Operating Plan. These address both HES priorities and wider national outcomes. HES continues to perform well against its performance targets and have a clear understanding of areas requiring further development. The impact of COVID-19 will have an impact on performance during 2020/21, as set out within its Action Plan for the first six months of 2020/21.

Our detailed findings and conclusions are included on pages 23 to 36 of this report.

Introduction (continued)

The key messages in this report (continued)

Conclusions on audit dimensions (continued)

Best value

We are satisfied that HES has sufficient arrangements in place to secure best value with a strong focus on continuous improvement. It has a clear understanding of areas which require further development**.**

Emerging issues

Deloitte's wider public sector team prepare a number of publications to share research, informed perspective and best practice across different sectors. Most recently, a number of articles have been published focusing on the impact of COVID-19. We have provided a summary of those most relevant to HES in the sector developments section on pages 39 to 41 of this report.

The Office of the Charity Regular (OSCR) has also published some guidance in response to COVID-19 response. A summary and links are also provided within the sector developments section of this report.

Next steps

We have followed up on actions identified in previous years on pages 47 to 48 of this report.

Added value

Our aim is to add value to HES by providing insight into, and offering foresight on, financial sustainability, risk and performance by identifying areas for improvement and recommending and encouraging good practice. In so doing, we aim to help HES promote improved standards of governance, better management and decision making, and more effective use of resources.

We have also included conclusions on HES' Best Value arrangements, which are discussed on page 36.

This is provided throughout the report. In addition, as information emerges as a result of the COVID-19 pandemic, we have shared guidance with management on areas to consider in relation to internal controls, going concern assessment, fraud risks and annual reporting. In addition, invites have been issued to our weekly webinar "Responding to COVID-19: Updates and practical steps" which are open to anyone to join.

Pat Kenny
Audit Director

Financial statements audit

Quality indicators

Impact on the execution of our audit

Management and those charged with governance are in a position to influence the effectiveness of our audit, through timely formulation of judgements, provision of accurate information, and responsiveness to issues identified in the course of the audit. These slides summarise some key metrics related to your control environment which can significantly impact the execution of the audit. We consider these metrics important in assessing the reliability of your financial reporting and provide context for other messages in this report.

Area	Grading	Reason
Timing of key accounting judgements	🟡 !	Accounting standards require management to perform a review of provisions at each year-end. Management's initial judgement was to maintain dilapidations at consistent level in the absence of new information. Following a request during the audit and challenge on the original judgements, a more detailed review was undertaken, we were satisfied with the detailed review subsequently performed by management. Based on our audit work, an adjustment of £826k has been made to the dilapidations provisions, as set out on page 43. Documentation of judgements made and sufficient evidence supporting those judgements for the legal provision was unavailable until a late stage in the audit, with substantial time liaising with management on the information which needed to be obtained. As a result of our audit, an adjustment to the legal provision and the reimbursement asset as disclosed on page 43.
Adherence to deliverables timetable	🟢	Deliverables were provided in line with the revised timeline as requested by HES. The finance team have been responsive to queries. Some deliverables (samples requested during audit fieldwork) were delayed due to the office closure which meant that significant risk testing was not finalised until 1 month after the scheduled end of the audit fieldwork.
Access to finance team and other key personnel	🟢	Deloitte and HES have worked together to facilitate remote communication during the audit which has been successful utilising video-conferencing tools available.
Quality and accuracy of management accounting papers	🟢	On the whole documentation provided has been of a good standard and once management papers were produced for the key estimates and judgements noted above they were of a high standard.

🔴 ! Lagging 🟡 ! Developing 🟢 Mature

Quality indicators (continued)

Impact on the execution of our audit (continued)

Area	Grading	Reason
Quality of draft financial statements	🟡	The initial draft accounts provided were non-compliant with reporting requirements in a number of areas including: the trade union facility time disclosure, key estimates and judgements, restatement disclosures and going concern disclosure as highlighted on page 46. In addition, there was a lack of comparatives throughout the narrative sections of the Performance Report. There were a number of changes to the initial accounts provided to audit which resulted in re-work of our audit testing in those areas. We have highlighted that in future no changes to the accounts should be undertaken once they are passed to audit without first discussing these with audit.
Response to control deficiencies identified	🟢	We noted a small number of instances where segregation of duties was not in place in the posting of journals, and have communicated that to management, who have confirmed that they will address the issue in 2020/21 and through the use of the new Corporate Management Information System (CMIS) system.
Volume and magnitude of identified errors	🟡	We have identified misstatements in relation to the HES dilapidations provision, legal provision, reimbursement asset, membership income and HESe cost of sales. We have identified five adjustments and four disclosure deficiencies, as set out on pages 43 – 47.

🔴 Lagging 🟡 Developing 🟢 Mature

Our audit explained

We tailor our audit to your business and your strategy

Identify changes in your business and environment

In our planning report we identified the key changes in your business and articulated how these impacted our audit approach.

Scoping

Our planning report set out the scoping of our audit in line with the Code of Audit Practice. We have completed our audit in line with our audit plan.

Other findings

As well as our conclusions on the significant risks we are required to report to you our observations on the internal control environment as well as any other findings from the audit.

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

When planning our audit we set our group materiality at £2,111k (HES only £1,878k; HESe £332k) based on forecast gross expenditure. We have updated this to reflect final figures and completed our audit to group materiality of £2,064k (HES only £1,836k; HESe £319k), group performance materiality of £1,548k (HES only £1,377k; HESe £287k) and report to you in this paper all misstatements above £103k (HES only £91k; HESe £15k).

Significant risk assessment

In our planning report we explained our risk assessment process and detailed the significant risks we have identified on this engagement. We report our findings and conclusions on these risks in this report.

Conclude on significant risk areas

We draw to the ARAC's attention our conclusions on the significant audit risks. In particular the ARAC must satisfy themselves that management's judgements in relation to going concern are appropriate.

Our audit report

Based on the current status of our audit work, we envisage issuing a modified audit report.

As discussed further on page 19, our opinion is expected to be qualified as a result of the limitation of scope on stock existence and condition for both HES and HESe arising from the impact of COVID-19.

We also expect to include an 'Emphasis of Matter' in relation to the material uncertainty of property valuations, as discussed further on page 16.

Significant risks

Dashboard

Risk	Material	Fraud risk	Planned approach to controls testing	Controls testing conclusion	Consistency of judgements with Deloitte's expectations	Comments	Page no.
Completeness of commercial income	✓	✓	D+I	Satisfactory	●	Satisfactory	12
Management override of controls	✓	✓	D+I	Satisfactory	●	Satisfactory	13

Note: Both risks cover HES and HESe

Overly prudent, likely to lead to future credit ⊖ ⊖ ● ⊕ ⊕ Overly optimistic, likely to lead to future debit.

D+I: Testing of the design and implementation of key controls

Significant risks (continued)

Risk 1 – Completeness of Commercial Income

Risk identified

ISA 240 states that when identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such Risks.

The main components of income are government grant in aid (HES) and commercial income (HESe). Grant in aid is directed by the Scottish Government and not considered a significant risk as the process for receipt of this income is not complex and can be verified 100%. The significant risk is pinpointed to completeness of commercial income, being income from admissions (HES) and retail income from properties in care (HESe). As commercial income comprises low value, high volume cash transactions across multiple locations there is an inherent risk of fraud in respect of these balances. As regular reconciliations are performed between the bank accounts and the amounts recognised via the Galaxy till receipting system, the risk is focused on how any reconciling items are investigated and addressed. This has been our key area of audit focus.

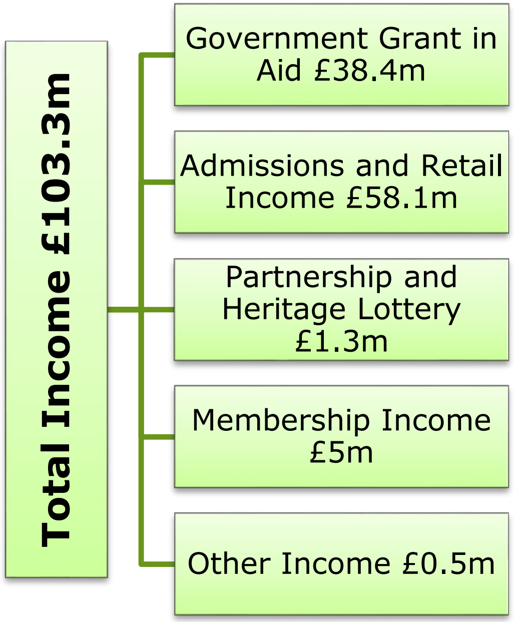
Key judgements

As commercial income comprises low value, high volume cash transactions across multiple locations there is an inherent risk of fraud in respect of these balances. As regular reconciliations are performed between the bank accounts and the amounts recognised via the Galaxy till receipting system, the risk is focused on how any reconciling items are investigated and addressed. This has been our key area of audit focus.

Deloitte response

We have performed the following:

- obtained an understanding of the design and implementation of the key controls in place in relation to recording of commercial income;
- performed analytical procedures over commercial income reported for the year, based on visitor numbers and price changes, to confirm accuracy; and
- Performed detailed testing of the year end reconciling difference as identified in the monthly control account reconciliation for account code 9111 being the difference between the amounts uploaded from the Galaxy system, and the amounts uploaded from the bank statements, to gain assurance over completeness of amounts recognised as income in the financial statements.



Total Income £103.3m

Government Grant in Aid £38.4m

Admissions and Retail Income £58.1m

Partnership and Heritage Lottery £1.3m

Membership Income £5m

Other Income £0.5m

Deloitte view

We have concluded that commercial income has been recognised in accordance with the Charities SORP and FRS 102.

Significant risks (continued)

Risk 2 - Management override of controls

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 HES's controls for specific transactions.

Deloitte response

We have considered the overall sensitivity of judgements made in preparation of the financial statements, and note that:

- HES and HESe results throughout the year were projecting overspends in operational areas in line with budget (discussed further on page 24). This was closely monitored throughout the year; and
- Senior management's remuneration is not tied to particular financial results.

We have considered these factors and other potential sensitivities in evaluating the judgements made in the preparation of the financial statements.

Significant and unusual transactions

We did not identify any significant transactions outside the normal course of business or any transactions where the business rationale was not clear.

Journals

We have performed design and implementation testing of the controls in place for journal approval.

We have used Spotlight data analytics to risk assess journals and select items for detailed follow up testing. The journal entries were selected using computer-assisted profiling based on areas which we consider to be of increased interest.

We have tested the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting. We noted a small number of instances where segregation of duties was not in place in the posting of journals, and have communicated that to management, who have confirmed that they will address the issue in 2020/21 and through the use of the new CMIS system.

Accounting estimates and judgements

We have performed design and implementation testing of the controls over key accounting estimates and judgements.

We reviewed accounting estimates for biases that could result in material misstatements. (see summary on the following page).

We note that overall the changes to estimates in the period were balanced and the adjustments identified did not indicate a bias to achieve a particular result. We tested accounting estimates and judgements focusing on the areas of greatest judgement and value, including:

- Dilapidations;
- Legal Claims;
- Property Valuations; and
- Grant Commitments.

Our procedures included comparing amounts recorded or inputs to estimates to relevant supporting information from third party sources.

Other than the adjustments detailed on page 43-44 for the dilapidations, legal provisions and deferred income no further issues were identified.

Significant risks (continued)

Risk 2 - Management override of controls (continued)

Key judgements	The key judgements in the financial statements include those which we have selected to be significant audit risks around completeness of commercial income (page 12). This is inherently the area in which management has the potential to use their judgement to influence the financial statements. We have also specifically considered the judgements in property valuations given the material uncertainty as a result of COVID-19 (see page 16). As part of our work on this risk, we have also reviewed and challenge other key estimates and judgements, specifically including:

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Dilapidations Provision	HES provide for legal or constructive obligations that are of uncertain timing or amount at the balance sheet date on the basis of the best estimate of the expenditure required to settle the obligation. A dilapidations provision of £521k was made in respect of a leased properties at John Sinclair House and Longmore House.	The provision is not quantitatively material for the financial statements however it was unusual that the provision had not moved given the new Longmore House lease in the year. Management had initially provided £521k for John Sinclair House however no provision was made for Longmore House. We reviewed the lease schedules, dilapidations schedules, management's expert valuation reports and considered amounts not included in management's assessment such as professional fees. We considered management's revised estimate and based on this and our audit work, raised an adjustment of £826k as set out on page 44.
Legal Provision	HES provides for any legal claims which HES has probable liability for and can be measured reliably. Management had originally offset anticipated reimbursement against the legal provision and included a provision of just £124k to cover outstanding legal claims.	We have assessed the legal claims outstanding at 31 March 2020 alongside the legal team to determine the probability of HES having liability. In line with FRS 102 the recognition criteria for provisions and reimbursement assets are separate and as such should be recognised separately. Provision: Management initially provided £124k for legal claims (see left). We reviewed and requested further information from the HES legal team and HES insurance regarding ongoing cases including those covered by insurance which management had not considered. We considered management's revised estimate and based on this and our audit work, raised an adjustment of £960k as set out on page 44. Reimbursement Asset: As a result of our audit work in relation to the legal provision we reviewed evidence provided by insurers to consider whether the reimbursement was virtually certain in line with FRS 102. We considered management's revised estimate and based on this and our audit work, raised an adjustment of £944k as set out on page 44. The net impact of both adjustments was £16k.

Significant risks (continued)

Risk 2 - Management override of controls (continued)

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Grant Commitments	Under the Charities SORP the award of a grant is recognised as a liability when the criteria for a constructive obligation are met, payment is probable, it can be measured reliably, and there are no conditions attached to its payment that limit its recognition. HES has recognised £11.2m of grant commitments as at 31 March 2020.	We have tested a sample of grant accruals, commitments and retentions at the year-end to assess whether they have been accounted for in accordance with the SORP. No issues have been identified.

Deloitte view

From our review of the dilapidations provision and the legal provision, we concluded that HES had understated the provisions by £826k and £960k respectively, as set out further on page 44. The increase in the legal provision is offset by the recognition of a reimbursement asset of £944k following our audit work, which is separately disclosed. These have been corrected by management.

We have not identified any instances of management override of controls in relation to the specific transactions tested, although note as set out on page 13 that there were a number of cases where there was insufficient segregation of duties in place with regards to the posting of journals.

Other areas of audit focus

Property valuations

Risk identified

HES is required to hold property assets at a modern equivalent use valuation. The valuations are, by nature, significant estimates based on specialist and management assumptions and which can be subject to material changes in value. We did not identify this as a significant risk in our Audit Plan as our property specialists, Deloitte Real Estate, reviewed the methodology applied by HES's valuer in previous years and concluded it was robust.

HES has had an independent valuation carried out at 31 March 2020 for the purposes of the 2019/20 financial statements as part of its 5 year rolling programme. The impact of COVID-19 has led to a material uncertainty being identified by the property valuer regarding the valuation of properties. Although our overall assessment of the risk level regarding the property valuation has not increased to 'significant', we expect to include an 'Emphasis of Matter' in our audit report.

Key judgements

The valuation method has not changed from the prior year and is in line with FRS 102, with a revaluation being carried out in line with the five year rolling programme. The revaluation has resulted in an upward valuation to property values of £1.2m.

The District Valuer identified a material uncertainty due to the impact of Covid-19 on individual markets, this is in line with RICS guidance published on 18 March 2020, as follows:

"*The outbreak of the Novel Coronavirus (COVID-19), declared by the World Health Organisation as a "Global Pandemic" on 11 March 2020, has impacted global financial markets. Travel restrictions have been implemented by many countries.*

Market activity is being impacted in many sectors. As at the valuation date, we consider that we can attach less weight to previous market evidence for comparison purposes, to inform opinions of value. Indeed, the current response to COVID-19 means that we are faced with an unprecedented set of circumstances on which to base a judgement.

Our valuation(s) is / are therefore reported on the basis of 'material valuation uncertainty' as per VPS 3 and VPGA 10 of the RICS Red Book Global. Consequently, less certainty – and a higher degree of caution – should be attached to our valuation than would normally be the case. Given the unknown future impact that COVID-19 might have on the real estate market, we recommend that you keep the valuation of this property / these properties under frequent review.".

Deloitte response

- We have engaged our property specialists in relation to the impact of COVID-19;
- We have assessed the presentation of revaluation movements and impairments, taking into account revaluation reserves for individual assets, and the disclosures included in the financial statements.
- We have reviewed the District Valuer's report and assessed managements disclosure of the key source of estimation uncertainty.

Deloitte view

Based on the audit evidence obtained, we are satisfied that the valuation of the property assets is appropriate. However, we expect to include an 'Emphasis of Matter' in our Independent Audit Report due to the material uncertainty identified by the valuers concerning valuations at 31 March 2020 due to the impact of COVID-19 on the property market. We have raised a disclosure deficiency in relation to the disclosure of this material uncertainty in the notes to the financial statements, which has been corrected by management, as set out on page 46.

Other significant findings

Financial reporting findings

Below are the findings from our audit surrounding your financial reporting process.

Qualitative aspects of your accounting practices:

The HES Annual Report and Accounts have been prepared in accordance with the Charities SORP. In 2019/20 management have made changes to accounting policies which we assessed during our audit work. Following our audit work, we are satisfied that the changes to accounting policies in the year are appropriate and that appropriate disclosure of the changes have been made. We consider that the membership income should be accounted for under the accruals basis rather than the cash basis at present and have raised an adjustment for this on page 43.

Significant matters discussed with management:

Significant matters discussed with management related primarily to the impact of COVID-19 on the organization, the basis of assessment relation to the going concern assumption and the assessment of significant judgements and estimates.

Other matters relevant to financial reporting:

We have not identified other matters arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process.

We will obtain written representations from the Board on matters material to the financial statements when other sufficient appropriate audit evidence cannot reasonably be expected to exist. A copy of the draft representations letter has been circulated separately.

Coronavirus (COVID-19) outbreak

Impact on the Annual Report and audit

The current crisis is unprecedented in recent times. HES is directly exposed to the practical challenges and is undergoing major, rapid operational changes in response.

The uncertainties and changes to ways of working also impact upon reporting and audit processes, and present new issues and judgements that management and the Audit, Assurance and Risk Committee needs to consider. OSCR has issued guidance relating to the impacts on charities including reporting requirements (see page 41 for further details). We summarise below the key impacts on reporting and audit:

Impact on the Annual Report and Accounts	Impact on our audit
HES needs to consider the impact of the outbreak on the Annual Report and Accounts, including: • Principal risk disclosures; • Change in the funding regime for 2020/21; • Property valuation material uncertainty; • Impairment of non-current assets; • Allowance for expected credit losses; • Fair value measurements based on unobservable inputs; • Going concern; and • Events after the end of the reporting period.	COVID-19 has fundamentally changed the way we have conducted our audit this year including: • Teams are working remotely with some challenges in efficiency due to communication and deliverables. • The teams have had regular status updates to discuss progress and facilitate the flow of information. • Consideration of impacts on the areas of the financial statements and Annual Report listed has been included as part of our audit work in the current year and comments have been included where appropriate within this report. • As set out in auditing standards, there is an acceptance that stock counts cannot be conducted where there is a threat to the safety of the auditor. In line with this, given the current situation, government guidance and our firm policy, we were unable to perform stock counts. In addition, we were unable to perform alternative procedures to satisfy ourselves as to the existence and condition of stock as at the year-end. • The team has undertaken additional work as a result of the higher risk relating to going concern. • In conjunction with management, we will continue to consider any developments for potential impact up to the finalisation of our work in August 2020.

Our audit report

Other matters relating to the form and content of our report

Here we discuss how the results of the audit impact on other significant sections of our audit report.

Our opinion on the financial statements

Our opinion on the financial statements is modified.

The restrictions on movement in the UK in March meant that HES staff were unable to perform all of its planned year-end stock count and we have been unable to attend any counts. As set out in auditing standards, there is an acceptance that stock counts cannot be conducted where there is a threat to the safety of the auditor. In line with this, given the current situation, government guidance and our firm policy, we were unable to perform stock counts. In addition, we were unable to perform alternative procedures to satisfy ourselves as to the existence and condition of stock as at the year-end. As a result, our opinion is expected to be qualified as a result of the limitation of scope on stock existence and condition for both HES and HESe.

Material uncertainty related to going concern

We have not identified a material uncertainty related to going concern and will report by exception regarding the appropriateness of the use of the going concern basis of accounting.

See our detailed considerations on page 21.

Emphasis of matter and other matter paragraphs

As discussed on page 16 we expect to include an ‘Emphasis of Matter’ paragraph within our audit report in relation to the material uncertainty associated with the property valuations.

There are no matters relevant to users’ understanding of the audit that we consider necessary to communicate in an other matter paragraph.

Other reporting responsibilities

The Annual Report is reviewed in its entirety for material consistency with the financial statements and the audit work performance and to ensure that they are fair, balanced and reasonable.

Opinion on regularity
In our opinion in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

Our opinion on matters prescribed by the Auditor General for Scotland are discussed further on page 20.

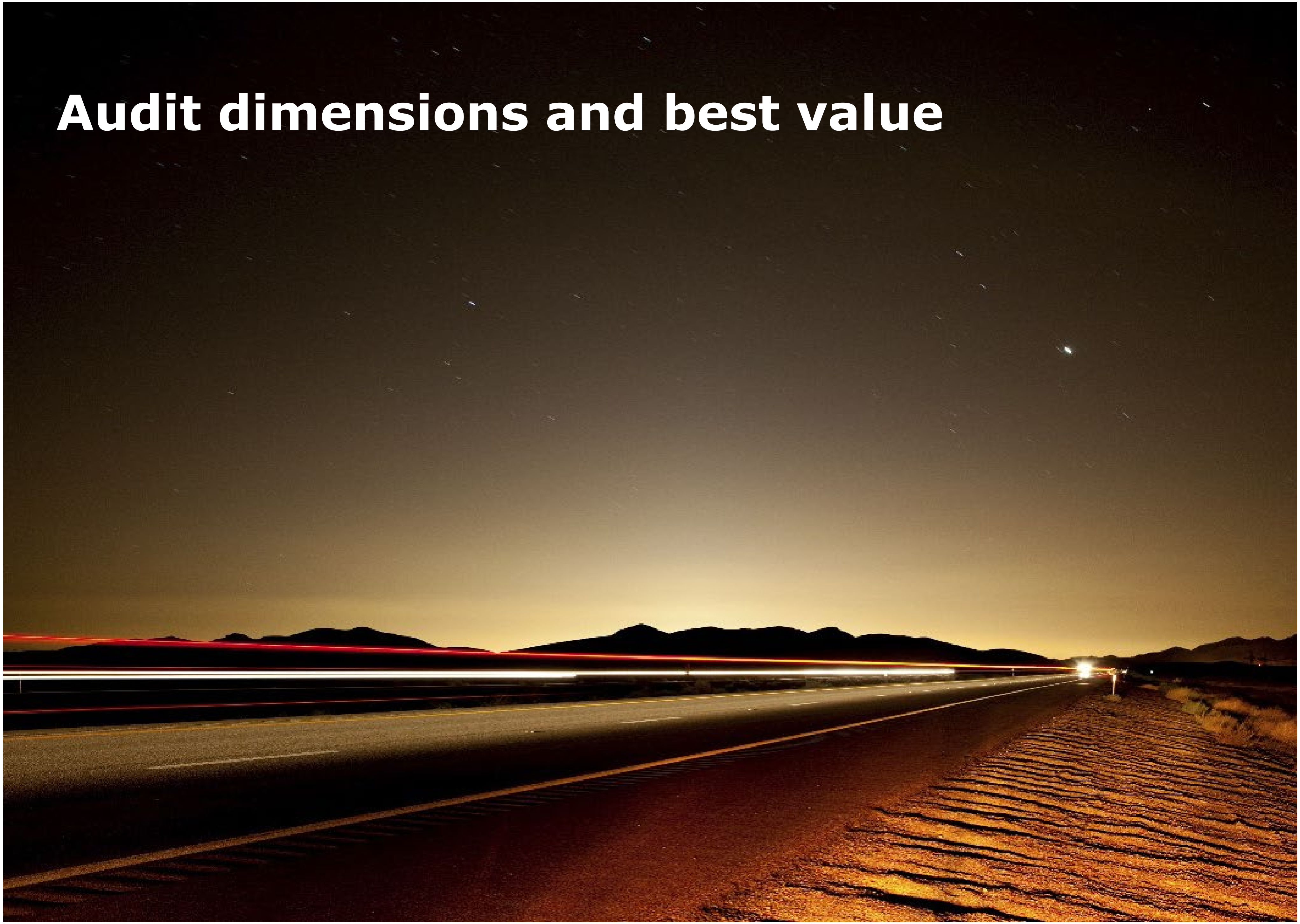
Your annual report

We are required to provide an opinion on the auditable parts of the Remuneration and Staff Report, the annual governance statement and whether the management commentaries are consistent with the disclosures in the accounts.

	Requirement	Deloitte response
Annual Report	Charitable Non Departmental Public Bodies (NDPBs) are not required to comply with the FReM requirements in relation to a Performance Report and Accountability Report. Instead, the Charities SORP sets out the requirements for a Trustees' Annual Report. HES has, however, chosen to follow the format set out within the FReM whilst still ensuring the full requirements of the Charities SORP are met as part of its Annual Report.	We have assessed whether the Annual Report has been prepared in accordance with the Charities SORP. We are satisfied that following the disclosure of methods to recruit and appoint trustees, the Charities SORP requirements have all been met, albeit following the format and heading structure of the FReM. We have also read the Annual Report and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading. We noted that there is good linkage of performance to national outcomes and would like to highlight this as good practice.
The Governance Statement	The FReM requires a governance statement to be published with the financial statements and guidance on content is provided in the Scottish Public Finance Manual (SPFM).	We have assessed whether the information given in the Governance Statement is consistent with the financial statements and has been prepared in accordance with the accounts direction. We have not identified any issues through our work.
Remuneration and Staff Report	Charitable NDPBs are not required to comply with the requirements of chapter 5 of the FReM, therefore the remuneration disclosures in the notes, as required by the Charities SORP is all that is required These disclosures replace the need for a separate Remuneration and Staff Report. HES has, however, chosen to publish a separate Remuneration and Staff report in accordance with the requirements of the FReM to aid transparency.	We have audited the auditable parts of the Remuneration and Staff report. We have identified four issues, as set out on page 46, which management have corrected. Based on this, we are satisfied that the auditable parts of the Remuneration and Staff Report have been prepared in accordance with the FReM.

Your annual report (continued)

	Requirement	Deloitte response
Going Concern	Management has made appropriate disclosure relating to Going Concern matters.	As noted on pages 28 to 31 we have be unable to conclude that HES is financially sustainable over the short or medium term due to uncertainties surrounding the impact of COVID-19. HESe is reliant on HES due to the lack of commercial income as a result of COVID-19 restrictions. In addition, the initial disclosure in the Annual Report and Accounts (for both HES and HESe) for going concern required updating to include the impact of COVID-19 and the factors considered in the assessment of the going concern basis. The closing Balance Sheet reports a negative unrestricted reserve of £10.4m, a decrease of £0.8m in comparison with the prior year. This has arisen due to the need for HES to commit to grants on a longer-term basis, which under the Charities SORP are recognised when that commitment is made. This is out of line with the government grant funding, which is received on an annual basis and accounted for on the basis of need. The increase in the negative unrestricted reserve in the year is due to new three year grant funding agreements. We are satisfied from a review of the 2020/21 budget, the medium to long-term financial strategy, correspondence with the Scottish Government and consideration of the actual position to date in 2020/21 that it is appropriate to prepare the accounts on a going concern basis, and that no material uncertainty on going concern exists. We have requested that management include this as a critical judgement in the notes to the accounts.



Audit dimensions and best value

Audit dimensions

Overview

As set out in our Audit Plan, public audit in Scotland is wider in scope than financial audits. This section of our report sets out our conclusions on our audit work covering the following areas. Our report is structured in accordance with the four **audit dimensions**, but also covers relevant risks identified by Audit Scotland.

Financial management

Financial sustainability

Value for money

Governance and transparency

Financial management

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

Is financial management effective?

Are budget setting and monitoring processes operating effectively?

Is there sufficient financial capacity?

Financial Management

Areas considered

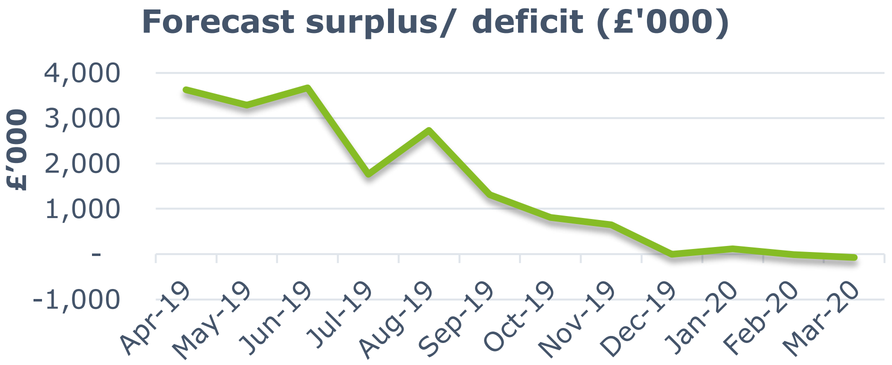
Our approach to the audit dimensions is risk focused. While we did not identify any specific risks in this area in our audit plan, we have continued to review the financial management arrangements including the extent to which there is effective scrutiny over both operational spend as well as delivery of savings plans. Our work considered the extent to which the performance impact of in year savings is monitored.

Budget monitoring

2018/19 Conclusion: HES achieved a year-end balanced budget for 2018/19. While forecast over commitments were reported throughout the year, this was carefully managed throughout and flexed to accommodate the available budget. In particular, overspends in salary costs as a result of unachieved savings were offset against slippage in capital projects.

2019/20 Update and Conclusion: The Board approved a budget at the start of the year incorporating a £3m over-commitment within the Investment Plan to allow flexibility throughout the year. This allows the Board to have projects ready to bring forward if additional income allows given the requirement to achieve a breakeven position each year.

HES achieved a small surplus of £74,000 at the year end. Forecast deficits were reported throughout the year as illustrated opposite, and similar to 2018/19, over commitments were carefully managed.



The key variances throughout the year included:

- Despite closures of some sites due to bad weather in January and February, and all sites closed from mid-March as a result of COVID-19, commercial income was still £1.6m greater than budgeted for the full year.
- A further £0.8m additional income was received compared to budget through recovery of grant and Heritage Lottery Funding.
- Cost of sales were £0.8m greater than budget reflecting a higher level of travel trade and retail income.
- The Investment Plan came in £1.9m under budget which reflects the over-commitment at the start of the year, which was revised down to £1.7m as part of the mid-year review.

Financial management (continued)

Savings Plans

2018/19 Conclusion: We reported that the final outturn included an adverse variance of £2.2m on the budgeted salary costs of £44.5m. The main reason for this was that the 2018/19 approved budget incorporated a challenging vacancy target which fell short of the target of £3.9m by £1.7m.

2019/20 Update and Conclusion: Similar to 2018/19, the Board approved a vacancy factor of 7.5% in the 2019/20 budget. This has been largely achieved with some departments performing better than others. Commercial and tourism and corporate services both reported underspends due to difficulties in recruitment and retention of staff. This was offset by overspends in other areas. This has been achieved through close control of vacant positions as well as non-salary costs such as overtime and agency.

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The vacancy target relates to an approach taken to reduce staff costs in the year by setting a mandatory three month vacancy target following a post being vacated. As reported in our 2018/19 report, while this is a blunt instrument, HES has adopted this approach as it is bound by the Scottish Government pay policies of no compulsory redundancies and yearly pay increases. This makes it difficult to identify staff cost savings, therefore departments are encouraged to identify means other than permanent staff to fill any resource gaps fills created by vacancies. This could be using fixed term contracts or redeployment from other areas of the organisation.

As part of the Financial Strategy (discussed further on page 29), HES plans to review its operational expenditure and develop a targeted efficiency programme for future years to ensure maximum value for money is being achieved. This is a positive step forward and should be progressed to help ensure that realistic and achievable savings targets are set at the start of the budget process.

Investment programme

2018/19 Conclusion: We reported that the investment plan outturn for 2018/19 was £10.4m against a budget of £12.6m. The underspend was largely due to slippages in capital projects, including Edinburgh Castle toilet upgrades, CMIS and NCAP relation. The underspend was used to offset the overspends in salary costs, resulting in an overall breakeven position.

2019/20 Update and Conclusion: A budgeted investment plan of £12m was set at the start of the year, which included an over-commitment of £3m to accommodate the uncertainties present when rolling out a number of simultaneous projects.

The key areas of capital expenditure included in the Investment Plan in 2019/20 were:

- £5.6m investment in site conditions;
- £1m investment in visitors experience; and
- £2.9m in other corporate priorities, including the CMIS project discussed on page 31.

The final outturn for 2019/20 was £9.5m against a budget of £12m, which is consistent with the previous year. The reason for this is again as a result of managed slippage and the need to manage the overall annual budget to achieve a breakeven position. HES have therefore effectively managed its investment programme in line with plan.

Financial management (continued)

Financial reporting

2018/19 Conclusion: HES has effective financial planning and management arrangements in place. We reported that we were satisfied that the underlying financial performance was transparently presented, including disclosure of reasons for variances.

2019/20 Update and Conclusion: Senior management and Board members regularly review progress against budget. The Senior Management Team (SMT) and the Board review financial performance monthly and quarterly respectively. In year financial reporting therefore continues to be robust with explanations for variances transparently reported throughout the year.

Financial capacity

2018/19 Conclusion: We reported that there are suitably qualified and experienced staff leading the finance team.

2019/20 Update and Conclusion: The finance team continues to be led by the Director of Finance, with two distinct teams below her:

- A finance team led by the Head of Finance; and
- A financial business support team led by the Head of Financial Business Support.

The team have remained consistent with previous year. We are therefore satisfied that the finance team capacity continues to be sufficient to support HES's financial management arrangements.

Internal audit

The Internal Audit function has independent responsibility for examining, evaluating and reporting on the adequacy of internal controls. During the year, we have completed an assessment of the independence and competence of the internal audit team and reviewed their work and findings. The conclusions have helped inform our audit work, although no specific reliance has been placed on the work of internal audit.

From our review of the internal audit reports issued during 2019/20, we have noted two "High Risk" graded recommendations in relation to project management and strategy. We are satisfied that these have been considered as part of the Annual Governance Statement disclosures.

No frauds have been identified as a result of these issues, and management has either addressed or made plans to address the risks highlighted.

Standards of conduct for prevention and detection of fraud and error

We have reviewed HES's arrangements for the prevention and detection of fraud and irregularities. Overall we found the HES's arrangements to be designed and implemented appropriately.

National Fraud Initiative (NFI)

All relevant public bodies are participating in the most recent NFI exercise which commenced in 2018/19. We have continued to monitor HES's participation and progress in the NFI during 2019/20 and submitted an assessment of HES's participation to Audit Scotland in February 2020. The information submitted will be used by Audit Scotland in its next national NFI report which is due to be published in the summer of 2020.

We concluded that HES was fully engaged in the exercise.

Financial management (continued)

Fraud and corruption in respect of the procurement function

As noted in our audit plan, and in accordance with Audit Scotland planning guidance, fraud and corruption in the procurement function (such as illicit rebates, kickbacks and false invoicing) is a risk across the public sector. We have therefore considered HES's controls and processes as a matter of particular focus, and concluded:

- While procurement fraud is not specifically included in the strategic risk register, there is a more general fraud risk considered.
- There are controls in place around the procurement process, including segregation of duties.
- A gift and hospitality policy in place as part of the staff code of conduct. A register is maintained for all declarations from staff. Similarly, a register of interest is in place for Board members and declarations provided at each meeting.
- All staff involved in procurement related decisions are trained on how to identify procurement fraud 'red flags' (e.g. excessive entertaining of procurement staff by suppliers).
- Internal Audit coverage of procurement systems is adequate and proportionate to the risks faced by HES. There is a specific review planned in relation to electronic payment cards as part of the regular review by internal audit.
- A whistleblowing policy is in place.

Based on the above, we are satisfied that the arrangements for the prevention and detection of fraud and corruption in the procurement function are effective and appropriate.

Deloitte view – financial management

HES continues to have strong financial management arrangements which are sufficiently robust to manage financial activity and capture and address any challenges to the achievement of financial targets. Financial performance is transparently reported to the SMT and Board throughout the year. We welcome the commitment to undertake a targeted efficiency review as part of the financial strategy action plan.

The capacity of the finance team has remained consistent during the year and is sufficient to support HES's financial management arrangements.

Financial sustainability

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.

Can short-term (current and next year) financial balance be achieved?

Is there a long-term (5-10 years) financial strategy?

Is investment effective?

Financial Sustainability

Areas considered

Our approach to the audit dimensions is risk focused. We identified the following risk in our audit plan:

"There is a risk that the plans for efficiency and financial sustainability are not sufficiently robust to allow the benefits to be realised".

Budget setting

2018/19 Conclusion: The Board approved a budget for 2019/20 of £99.5m together with an over commitment of £3m, bringing the total planned expenditure to £102.5m. The over-commitment was approved to provide flexibility to bring forward projects should income exceed expectations.

We concluded that there was evidence of efforts being made to work towards outcome based budgeting which will provide greater linkages between the budget and national outcomes This should be aided by the new CMIS system (discussed further on page 31).

2019/20 Update and Conclusion: In the context of the COVID-19 pandemic, the Board made the decision in March 2020 that it was no longer able to continue operating as business-as-usual and its planning and budgeting had to be adjusted to reflect this.

An Action Plan for the first six months of the 2020/21 financial year was therefore published in lieu of the Annual Operating Plan. This set out the workplan for the immediate future to address the direct impact of the outbreak on the organisation and to ensure that HES is able to maximise the resources still available. On the assumption of fixed costs and non-fixed costs funding business critical activity, total planned spend for the period is £45.5m. This projected a surplus of £2.4m after taking into account Government's reliefs and slippage on the grant programme.

HES is in a fairly unique position compared to other public bodies in that it has a volatile income stream with uncertainty of funding cover and a large fixed cost base which exceeds the annual grant in aid available. The COVID-19 pandemic has resulted in a projected loss of £53.3m income, being 85% of the budgeted self-generated income and 50% of the total budgeted income for 2020/21. The full estate has been closed since March 2020 and at the time of preparing the six month action plan, estimated a worst-case scenario of a loss of six months visitor income.

This significantly increases the risk of HES being financially unsustainable in the short term. The implications of the going concern considerations are set out on page 21.

Financial sustainability (continued)

Budget setting (continued)

In response to these significant challenges, HES has submitted a request to the Scottish Government for supplementary resource grant in aid to ensure HES has sufficient funds to carry out its statutory and lead body function for the remainder of 2020/21. Based on a number of assumptions, HES has estimated a realistic scenario which would require additional funding of £29.3m for 2020/21. Meeting the estimated grant commitments would require an additional £11.9m, bringing the total funding requirement to £41.2m.

Discussions have been ongoing with the Scottish Government Sponsor Division and Scottish Government Finance, with supplementary information provided in addition to the business case submitted on 8 June 2020. At the time of issuing this report, a formal agreement has been received on the funding required awarding £37.1m for the reminder of 2020/21 which based on updated projections will cover the funding required.

Despite the challenging position, we are satisfied HES continue to have a robust budget setting process in place. A significant risk of not achieving short term financial balance remains.

Medium to long-term financial planning

2018/19 Conclusion: A medium to long-term Financial Strategy covering the period to 2030 was endorsed by the Board in November 2018. The most likely scenario was a cumulative total £126m funding gap over the 12 year period to 2029/30. While it was positive to note that a robust Financial Strategy had been agreed, this only sets the basis for considering how best to achieve long-term financial sustainability. We highlighted that achieving sustainability would require detailed action plans to be put in place and the impact of these closely monitoring by HES.

2019/20 update and Conclusions: The Financial Strategy was refreshed in November 2019. This incorporates a baseline, worst, and best case net outturn scenario for the 10 year period to 2029/30 the most likely scenario is an annual funding gap of £26.9m by 2029/30. This is an increase of £5.4m compared to the funding gap estimated in the November 2018 Financial Strategy so is showing an increasingly challenging position.

The updated strategy is based on the following key assumptions as the most likely scenario:

- Grant in Aid Reduction of 3% in 2020/21 to 2022/23 with a 2% reduction thereafter;
- Commercial income expected to increase by 1.4%-3.6% in 2020/21 to 2022/23 and 3% per annum thereafter;
- Staff costs expected to increase by 5% per annum; and
- Inflationary increase in operational expenditure of 2% per annum.

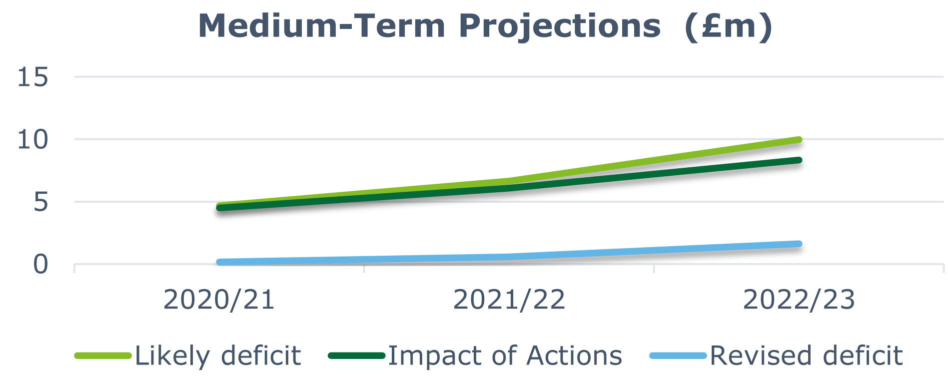
In view of the challenges faced, the Financial Strategy incorporated a number of key actions with set timescales, including:

- Development of a commercial strategy;
- Income diversification;
- Staffing review, including the development of a comprehensive workforce plan;
- Cost management;
- Planning and Investment;
- Review of grant strategy;
- Review of operating model; and
- Implementation of CMIS.

Financial sustainability (continued)

Medium to long-term financial planning (continued)

The action set out in the plan anticipates to reduce the projected deficit over the next three years, although not completely eliminate, as illustrated below:

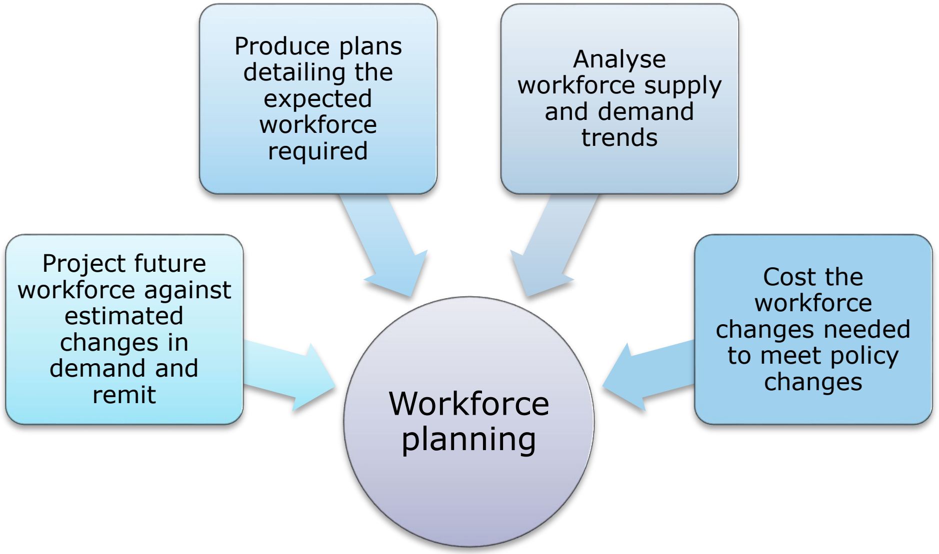


Given the impact of COVID-19 on both the financial position and operational activity of HES, as discussed on page 29, there is a need for a refresh of the Financial Strategy to re-assess the likely position and actions required.

Workforce - As noted in the Financial Strategy, HES plan to carry out a staffing review incorporating the development of a workforce plan. A Director of People was appointed September 2019 and will be driving this forward. This is a positive step given the significance of the workforce to both the financial and operational aspects of HES.

It is important that this plan considers the needs of the organisation and those of its workforce, ensuring it is sufficient to meet its legal obligations and objectives. Workforce planning provides a basis for understanding workforce behaviours, considering areas such as recruitment, promotion and turnover, as well as looking at causes of absenteeism and changes in productivity. Understanding these issues can allow the organisation to plan appropriately.

Audit Scotland has produced reports on workforce planning in the NHS in Scotland, identifying key areas which need to be considered for effective workforce planning. Although not directly applicable, the overarching principles here could be used to guide HES's workforce planning.



While there has been some progress with the key actions identified within the Financial Strategy, in particular the implementation of CMIS (discussed on page 31), little progress has been made in reducing the estimated funding gap over the next 10 years. The action plan contained within the latest Financial Strategy is a positive step, however, given the impact of COVID-19 on the organisation, this will need to be revisited once HES has clarity on its short-term funding position. HES therefore continues to be faced with an extremely challenging financial position.

Financial sustainability (continued)

Programme for Success

2018/19 conclusion: We reported that the CMIS project was a significant part of the transformation work as a key enabler to a number of areas.

2019/20 update and Conclusion: During 2019/20, HES has been developing its Programme for Success and in April 2020 has appointed a Programme Manager to oversee the implementation of the ambitious plans. The Programme is overseen by a Corporate Projects Programme Board. The programme includes the following:

- A Corporate Management Information System (CMIS) – this has seen some delay, with changes in implementation partner, but Phase 1 is due to go live in October 2020. HES have recently received a delivery gateway assurance report providing a Green-Amber Delivery Confidence Assessment which means "Successful delivery appears probable however constant attention will be needed to ensure risks do not materialise into major issues threatening delivery‟;
- An Electronic Document Record Management System;
- IT investment including the development of Intranet; and
- Properties in Care Asset Management Plan.

In view of the impact of COVID-19, planned projects to review the Headquarter facilities and Archives and Collections accommodation have been put on hold and are being fully re-considered through an options appraisal.

The development of the programme is a positive step, as is the appointment of a Programme Manager to drive these forward. It is important that clear benefits tracker is in place to monitor the success of these projects against plan. The impact on COVID-19 increases the risk of successful delivery of these projects.

Deloitte view – Financial sustainability

As discussed on page 28, HES has achieved short-term financial balance in 2019/20, ending the year with a small surplus.

Some positive progress had been made in the year, with the update of the Financial Strategy and associated actions and the implementation of the Programme for Success. There also continues to be a robust budget setting process in place. However, given the significant financial impact that COVID-19 has had, and is expected to have on HES, there remains a significant risk of achieving financial sustainability in both the short and medium-to-long term.

Governance and transparency

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

Is governance effective?
Is there effective leadership?
Is decision making transparent?
Is there transparent reporting of financial and performance information?
Governance and transparency

Areas considered

Our approach to the audit dimensions is risk focused. While we did not identify any specific risks in this area in our audit plan, we have continued to review the work of the Board and the ARAC.

Leadership, governance and scrutiny arrangements

2018/19 Conclusion: HES's governance framework and arrangements were appropriate and supported good governance and accountability. HES had strong executive leadership, the relationship between board members and officers was good, and there was evidence of effective challenge from committee meetings. We also concluded that the Board was open and transparent in its decision making with all key strategy documents and Board minutes available on its website.

2019/20 update and conclusions: HES continues to have strong leadership and has a clear vision for what it wants to achieve for the future as demonstrated in various strategy documents, such as the Finance Strategy, Annual Operating Plan, and three year Corporate Plan The Board and staff support the vision, as demonstrated by Board approval of various key documents, and from the 2018 Staff Survey.

A number of changes have been made to the Non-Executive Board membership during the year with two members stepping down in December 2019 and four new members appointed by Scottish Ministers in April 2020. All new members have undergone a formal induction process.

As noted in our 2018/19 report, HES had developed an action plan to address the findings from the staff survey, specifically focusing on openness and transparency. It is positive to note that the following actions have taken place in the year:

- The Chief Executive is now completing video blogs;
- There is increased site visits by SMT including Q&A sessions at Longmore House and the Engine Shed; and
- All Directors hold regular open door sessions.

The impact of these actions will be assessed as part of the next Staff Survey which is expected in 2021.

Governance and transparency (continued)

Leadership, governance and scrutiny arrangements (continued)

We reviewed HES's governance and accountability arrangements which included:

- Confirming that the governance framework and governance arrangements, including decision making and scrutiny, are regularly reviewed and updated to ensure they remain effective;
- Assessing the effectiveness of decision making to ensure it is balanced by effective scrutiny and challenge by those independent of the body;
- Confirming that there is effective scrutiny and challenge in place over policy decisions, service performance and programme management;
- Confirming that decision makers have the information they need to scrutinise, challenge and make best value and transparent decisions; and
- Assessing that it is clear what decisions have been made, who make them and the rationale supporting the decisions.

We have concluded that overall HES's arrangements are appropriate and adequate in supporting effective governance and accountability.

The ARAC continues to play a key role in the governance and scrutiny arrangements of the Board. In line with good practice, ARAC completed its annual self-assessment exercise in May 2019 identifying 4 areas for further progress. It considers reports from internal audit throughout the year and has also considered the risk management framework and associated risk reports bi-annually.

In response to the challenges arising as a result of COVID-19, the Board has provided a heightened level of support and oversight, in particular through weekly conference calls of the Board and the Chief Executive. Board and ARAC meetings have continued to operate virtually during this period.

Deloitte view

HES's governance framework and arrangements continue to support good governance and accountability. It continues to have a strong executive leadership, with positive relations between Board members and staff. There is evidence of strong and effective scrutiny, particularly through the ARAC. There has been a positive response to the challenges faced by the COVID-19 pandemic, with appropriate arrangements in place to ensure sufficient support and oversight.

The Board continues to be open and transparent in its decision making and has demonstrated a commitment to continuous improvement through the action plan developed following the 2018 staff survey. The impact of these actions need to be assessed when the next staff survey is carried out.

Value for money

Value for money is concerned with using resources effectively and continually improving services.

Are resources being used effectively?

Are services improving?

Is Best Value demonstrated?

Value for money

Areas considered

Our approach to the audit dimensions is risk focused. While we did not identify any specific risks in this area in our audit plan, we have continued to review HES' performance against its Corporate Plan, the Board's reporting and monitoring of these and the actions taken to improve performance.

Performance management framework

2018/19 Conclusion: We reported that HES performance in 2018/19 was measured against the targets laid out in the 2016-2019 Corporate Plan and the 2018-2019 Annual Operating Plan. These measured internal key performance indicators, as well as the wider HES contribution to the national performance framework, and identify direct and indirect contributions to national performance outcomes.

2019/20 Update and Conclusions: 2019/20 is the first year of the new Corporate Plan "Heritage for All" which covers the period 2019-2022. Similar to the arrangements under the previous plan, HES measures its performance against targets laid out in the Corporate Plan and the 2019/20 Annual Operating Plan. These measure internal key performance indicators, as well as the wider HES contribution to the national performance framework, and identify direct and indirect contributions to national performance outcomes. This is in line with good practice.

An effective monitoring framework is in place. Performance is reported monthly to SMT and quarterly to the Board. This is reported in a transparent way using a Red, Amber, Green (RAG) system with focus on those which are at risk.

The Key Priorities from **2019-22 Corporate Plan "Heritage for All":**

1. The historic environment makes a real difference to people's lives.

2. The historic environment is looked after, protected and managed for the generations to come.

3. The historic environment makes a broader contribution to the economy of Scotland and its people.

4. The historic environment inspires a creative and vibrant Scotland.

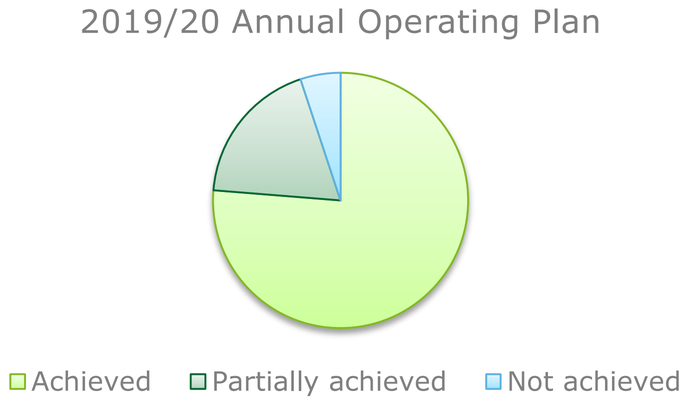
5. The historic environment is cared for and championed by a high-performing organisation.

Value for money (continued)

Performance data

2018/19 Conclusion: Overall, in 2018/19 performance was very positive with 96% delivery of Year 3 KPI's. Only one KPI was not achieved in relation to sickness absence, which was not achieved for the second year. We reported that HR continue to work closely with managers and business areas to support the management of sickness absence across HES.

2019/20 Update and Conclusions: HES has reported 95% of 2019/20 KPIs have either been achieved or partially achieved in the first year of its new Corporate Plan.



The three KPIs that have not been achieved relate to:

1. No significant progress has been made with the Edinburgh Castle Masterplan at year end as it was agreed over the course of the year to delay this and reconsider timings.

2. Built Heritage Management plan was not published by the end of March 2020. In light of the COVID-19 impact, focus is being redirected on reviewing opportunities and delivery models, guided by future needs.

3. The development of a national framework for procurement of indigenous stone has not progressed as a result of the Scottish Government's request to ensure framework can be used as a case study for sustainable procurement nationally. Timescales are currently being revised.

HES therefore continues to perform well against its performance targets and have a clear understanding of areas requiring further development.

Deloitte view – Value for money

HES has a clear and effective performance monitoring framework in place to ensure that its performance is monitored and reported in line with KPIs set out in the 3 year Corporate Plan and Annual Operating Plan. These address both HES priorities and wider national outcomes.

HES therefore continues to perform well against its performance targets and have a clear understanding of areas requiring further development.

The impact of COVID-19 will have an impact on performance during 2020/21, as set out within the Action Plan for the first six months of 2020/21.

Best Value

The Scottish Public Finance Manual (SPFM) explains that accountable officers have a specific responsibility to ensure that arrangements have been made to secure ***Best Value (BV)***

The duty of Best Value, as set out in the SPFM

- To make arrangements to secure continuous improvement in performance whilst maintaining an appropriate balance between quality and cost; and in making those arrangements and securing that balance
- To have regard to economy, efficiency, effectiveness, the equal opportunities requirement and to contribute to the achievement of sustainable development.

The SPFM sets out nine characteristics of Best Value which public bodies are expected to demonstrate. The refreshed guidance issued by the Scottish Government in 2011 focused on 5 generic themes and 2 cross-cutting themes, which now define the expectations placed on Accountable Officers by the duty of Best Value.

Five themes:
1. Vision and Leadership
2. Effective Partnerships
3. Governance and Accountability
4. Use of Resources
5. Performance Management

Cross-cutting themes:
1. Equality
2. Sustainability

BV arrangements

HES has a number of arrangements in place to secure best value. This is evidenced through the Annual Plan and the Performance Monitoring Framework.

As noted elsewhere within this report, HES has an established governance framework and strong leadership. There is a culture of continuous improvement, as evidenced from the work being done through the Financial Strategy and Programme for Success

HES recognises that it must deliver services within the financial resources available and, as noted elsewhere in this report, further work is required to achieve medium to longer term financial sustainability.

Deloitte view – best value

HES has sufficient arrangements in place to secure best value with a strong focus on continuous improvement. It has a clear understanding of areas which require further development.

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 help the ARAC and the Board discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA (UK) 260 to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements and our observations on the quality of your Annual Report;
- Our internal control observations; and
- Other insights we have identified from our audit.

The scope of our work

Our observations are developed in the context of our audit of the financial statements.

We described the scope of our work in our audit plan.

Use of this report

This report has been prepared for the Board, 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.

What we don’t report

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

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, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in fulfilling our audit plan.

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

P. Kenny

Pat Kenny, CPFA

For and on behalf of Deloitte LLP

Glasgow | 5 August 2020

Sector developments

Sector developments

Responding to COVID-19

As part of our "added value" to the audit process, we are sharing our research, informed perspectives and best practice from our work across the wider public sector.

An emerging legacy

How COVID-19 could change the public sector

While governments and public services continue to respond at scale and pace to the COVID-19 pandemic, its leaders have begun to consider how the crisis might permanently change their agencies – and seven legacies are emerging.

The COVID-19 pandemic has been unchartered territory for governments. Elected representatives, officials and public service leaders around the world are making profound decisions with no precedent to draw upon and little certainty around when the crisis will end. As French President Emmanuel Macron observed, this is a kinetic crisis – in constant motion with little time to make far-reaching decisions.

In the UK and across much of Europe, government responses have been radical and exhaustive. Health services have mobilised at scale, finance ministries have acted fast to support businesses, and the full spectrum of departments have made rapid adjustments to ensure public needs continue to be met.

While leaders across the public sector remain focused on the immediate COVID-19 threat, they are increasingly mindful of its longer-term implications – and for some, the crisis could be an inflection point for their agency. This paper explores the pandemic's likely legacy on governments, public services and the debates that shape them.

Seven emerging legacies:

1. Our view of resilience has been recast.
2. Governments could be left with higher debt after a shock to the public finances
3. Debates around inequality and globalisation are renewed
4. Lines have blurred between organisations and sectors
5. The lockdown has accelerated collaborative technologies
6. Civil society has been rebooted and citizen behaviour may change
7. The legacy that still needs to be captured

Read the full article at:

https://www2.deloitte.com/uk/en/pages/public-sector/articles/an-emerging-legacy-how-corona-virus-could-change-the-public-sector.html

Sector developments (continued)

Responding to COVID-19 (continued)

COVID-19: Preparing for the 'next normal'

As the COVID-19 pandemic continues to unfold there is unlikely to be a rapid or decisive transition from crisis to recovery. Organisations are more likely to face a sequence of operational environments that oscillate between restriction and relaxation, before a final end-state of relative normality.

The first phase of COVID-19 response has been characterised by significant and rapid changes in the way people live their lives and how organisations operate. Many of these changes have been government-mandated. The next phase will be an opportunity for organisations to reflect and plan for a period of uncertainty and disruption. During this period businesses will need to maintain their responsibilities to their customers and staff while modifying operations to meet changes in demand and supply as government restrictions change. They will need to ensure that their recovery is sustainable in terms of resource use and flexible enough to meet change.

Copies of this report can be accessed through the following link:
https://www2.deloitte.com/uk/en/pages/risk/articles/preparing-for-the-next-normal.html

COVID-19: Impact on the workforce

It's likely that the way we work will be forever changed as a result of COVID-19. All of us are seeking answers to guide the way forward. That's why Deloitte's Global and UK Human Capital practice have produced a series of articles to inform business leaders on their path to respond, recover, and thrive in these uncertain times. These articles explore the impact of COVID-19 on the workforce and are aimed at supporting HR teams as they navigate their organisation's response to the pandemic.

HR leaders, in particular, have been at the centre of their organisation's rapid response to COVID-19, and have been playing a central role in keeping the workforce engaged, productive and resilient. Understandably, recent priorities have been focused almost exclusively on the respond phase. As progress is made against respond efforts, another reality is forming quickly. Now is the time for HR leaders to turn their attention toward recover to ensure their organisations are prepared to thrive.

The latest thinking from our UK Human Capital practice is "**COVID-19 CHRO Lens: Work, Workforce and Workplace Considerations**". This workbook provides a framework to enable leaders to plan for recovery. It sets out a series of key questions across the dimensions of work, workforce and workplace, enabling organisations to plan for multiple scenarios and time horizons, as they shift from crisis response to recovery.

The workbook can be found at the following link, along with links to other articles which we would encourage you to explore.

https://www2.deloitte.com/uk/en/pages/human-capital/articles/COVID-19-impact-on-the-workforce-insight-for-hr-teams.html

Sector developments (continued)

OSCR developments

OSCR published **COVID-19 guidance for charities** on 30 March 2020.

The guidance brought together information that charities need to know during this time and highlighted other organisations that may be able to offer support.

The guidance included information in relation to:
1. Contacting OSCR;
2. Funding and finance;
3. Charity meetings and governance;
4. Reporting to OSCR: charity accounts and notifiable events;
5. Registering a charity and making changes to your charity;
6. Information for cross-border charities;
7. Fraud;
8. Safer giving and fundraising;
9. Volunteering; and
10. Sources of help and advice.

The full guidance is available through the following link:
https://www.oscr.org.uk/news/oscr-publishes-covid-19-guidance-for-charities/

A survey on the impact of COVID-19 on Scottish charities has been carried out with the results published on 10 July 2020, where almost 5,000 charities responded.

https://www.oscr.org.uk/news/impact-of-covid-19-on-scottish-charities/

SORP engagement process begins as convenors are appointed to take forward the discussion on the next SORP.

The Charities Statement of Recommended Practice (SORP) sets out the framework for how larger charities prepare their annual report and accounts.

Following a governance review of the SORP development process in 2018-19, a new approach has been initiated which has greater engagement at its heart. To support the SORP-making body and the advisory SORP Committee in this work, volunteer engagement partners have been recruited through an open recruitment process. These partners each have a particular interest in one or more specific areas (known as engagement strands) which cover the key users of charity annual reports and accounts and the SORP itself.

To support the engagement work, each engagement strand has a convenor. These convenors have been drawn from SORP engagement partners following expressions of interest in the role.

The Scottish Charity Regulator (OSCR) Board Chair Lindsay Montgomery CBE said,
"Charity annual reports and accounts are a key mechanism for charities to be accountable and transparent. As regulator, we want to make sure that they are as useful, helpful and understandable as possible. Consequently OSCR takes its role as part of the SORP-making body very seriously.

We would like to thank everyone who has volunteered as an engagement partner. To those who will act as convenors, you have a great opportunity to create a thoughtful debate around the development of a critical contributor to public trust in charities."

Appendices

Audit adjustments

Unadjusted misstatements

The following uncorrected misstatements have been identified up to the date of this report which we request that you ask management to correct as required by ISAs (UK). Uncorrected misstatements decrease surplus by £1.023 million and decrease net assets by £1.023 million.

		Debit/ (credit) SOFA £k	Debit/ (credit) in net assets £k	Debit/ (credit) prior year Funds £k	Debit/ (credit) OCI/Equity £k
Misstatements identified in current year					
Deferral of Membership Income	[1]	1,023	(1,023)	-	-
Misstatements identified in prior years					
None					
Aggregation of misstatements individually		1,023	(1,023)		
Total		**1,023**	**(1,023)**		

[1] As noted on page 17, we identified a misstatement due to HES's accounting policy for deferral of membership income. This is currently accounted for under a cash basis rather than the accruals basis. While the adjustment is not material the total value of membership income is material and therefore should be adjusted. Management have accepted the basis for the adjustment and will put in place arrangement to adjust this next year.

Audit adjustments

HES Corrected misstatements

The following misstatements have been identified up to the date of this report which have been corrected by management. We nonetheless communicate them to you to assist you in fulfilling your governance responsibilities, including reviewing the effectiveness of the system of internal control.

		Debit/ (credit) SOFA £k	Debit/ (credit) in net assets £k
Legal Provision	[1]	960	(960)
Reimbursement Asset	[2]	(944)	944
Dilapidations Provision	[3]	826	(826)
Total		**842**	**(842)**

[1] As set out on page 14, we identified a misstatement in relation to the legal provision which management have corrected. Management had originally offset anticipated reimbursement against the legal provision, which is non-compliant with FRS 102. Adjusting for this increases the provision in the Statement of Financial Position and the associated expenditure in the Statement of Financial Activities, thereby reducing HES' reported surplus by £960k.

[2] As set out on page 14, we identified a misstatement in relation to recognition of a reimbursement asset (insurance claim monies receivable), which management have corrected. This reimbursement asset had initially been offset against the legal provision. This recognises an asset in the Statement of Financial Position and decreases the associated expenditure in the Statement of Financial Activities, thereby increasing HES' reported surplus by £944k.

[3] As set out on page 14, we identified a misstatement in relation to the dilapidations provision which management have corrected. Management had not sufficiently considered the available evidence to determine the best estimate of the provision at the reporting date. In addition, a review had not been undertaken of the new lease during the year including the dilapidations schedule which had been served in May 2019. This adjustment increases the provision in the Statement of Financial Position and the associated expenditure in the Statement of Financial Activities, thereby reducing HES' reported surplus by £842k. However, we are aware that the Scottish Government will increase HES' 'annually managed expenditure' allocation so that there is no ultimate impact on the surplus recorded.

Audit adjustments (continued)

HESe Corrected misstatements

		Debit/ (credit) Profit and Loss £k	Debit/ (credit) in net assets £k
Reallocation of HESe recharge costs from Administration to Cost of Sales	[1]	-	-
Total		**-**	**-**

[1] During our audit testing it was identified that management had reallocated a number of general ledger codes from administration expenses to cost of sales, increasing cost of sales by £484k and reducing administration expenses by the same amount. These costs related to utilities and cleaning and therefore do not in our judgement represent cost of sales. Following discussion, management agreed with our judgement and reversed the reallocation to remain in line with the prior year allocation, ensuring comparability between the prior year and current year annual report and accounts, as required by FRS 102.

Audit adjustments (continued)

Disclosures

Disclosure misstatements

The following disclosure misstatements have been identified up to the date of this report which management have corrected as required by ISAs (UK).

Disclosure	Summary of disclosure requirement	Quantitative or qualitative consideration
Remuneration Report: - Disclosure of a seconded director within the Remuneration Report should be on a consistent basis with other directors. - Fair pay: the median ratio should be calculated on the mid-point of the highest paid band, not the actual remuneration. - Exit Packages: This should be disclosed in the required format. - Staff Composition: There was a need to restate the prior year composition to match the restated headcount. - Trade Union Facility Time (TUFT): This must be disclosed in the prescribed format.	Disclosure of the required elements as per sections 5.3.20 to 5.3.28 of the FReM. TUFT - The Trade Union (Facility Time Publication Requirements) Regulations 2017.	Qualitatively material - Important for the users' understanding of the organisations remuneration and for ensuring compliance with laws and regulations.
Key Estimates and Judgements We identified a number of items which significant estimation uncertainty which were not included in this note, including: • Valuation of Property; • Dilapidations provision; and • Legal Provision. We have also asked management to include the determination that there is no material uncertainty regarding going concern as a critical judgement.	Key judgements made by management in the preparation of the accounts and the sources of estimation uncertainty which could have a material effect on the amounts disclosed in the accounts.	Qualitatively material – This is an accounting standard requirement and is a key focus area for regulatory bodies.

Audit adjustments (continued)

Disclosures (continued)

Disclosure	Summary of disclosure requirement	Quantitative or qualitative consideration
Going Concern Increased disclosure was required to include the following: • Principal events and conditions arising from the impact of COVID-19; • Evaluation of the significance of those events in relation to the ability of HES to meet its obligations as they fall due; • Management's plans to mitigate the effect of these events; and • Significant judgements made by management in respect of the impact of COVID-19 as part of this assessment	Key factors and considerations in assessing the judgement to adopt the going concern basis for preparation of the accounts.	Qualitatively material - This is an accounting standard requirement and is a key focus area for regulatory bodies.
Restatement – A Prior Period Adjustment and Change in Accounting Policy note is required for each material relevant item. No disclosure was initially presented. The following material areas have been restated in the 2019/20 accounts: • Classification of Membership Income • Recalculation of headcount; and • Recategorisation of Trading income categories.	IAS 8 sets out the required disclosures, including: • Change in Accounting Policy - the nature of and reasons for the change and the amount of the adjustment for each line item in the accounts affected for the current period and each prior period presented. • Prior Period Adjustment - the nature of the prior period error; for each prior period presented in the accounts, to the extent practicable, the amount of the correction for each account line item affected.	Qualitatively material - This is an accounting standard requirement and is important for the users of the accounts to understand the comparability between the prior year signed accounts and the 2019/20 accounts.

Action plan

Follow-up previous year action plans

In our 2017/18 audit we made two recommendations which were partially implemented in 2018/19. These remain partially implemented in the current year. We will continue to monitor these as part of our 2020/21 audit work. In 2018/19 we made one recommendation which has not been implemented but is no longer relevant.

Area	2017/18 Recommendation	2018/19 Management Response	Responsible person	Target Date	Priority	2019/20 Update
IT – Information Leakage	HES should implement controls to address the risk of information leakage including • Ensuring formal data leakage risk assessment is performed • Implementing controls over portable media, e.g. USB drives and laptops; and • Implementing specific Data Loss Prevention Tools	• Ensuring formal data leakage risk assessment is performed - no formal risk assessment has been performed on data leakage to date However, the risk of data leakage is included in the risk register which is proactively maintained by the Information Security team and therefore this is a managed risk and the recommendation has been addressed. • Implementing controls over portable media, e g USB drives and laptops a recommendation had been made to the Chief Technology Officer (to move to Bitlocker encryption for USB devices at minimum or implement Sophos USB encryption if budget allows this will be revisited in the next financial year 2020/21. • Implementing specific Data Loss Prevention tools HES have implemented the next generation fire walls that perform data packet scanning both into and out of the network This improves data loss prevention capabilities Furthermore, Information Governance are exploring options to implement tools to assist in the classification of sensitive information in an effort to reduce the risk of data loss as part of the EDRMS Intranet project.	Head of Information Governance	March 2021	Medium	***Partially implemented:*** **Updated management response**: HES is in the process of implementing controls to protect HES from threats through portable media. CTO and IG are working together to develop a policy and process for restricting the standard of portable media that is able to effectively access the HES network. It is anticipated that these proposals will be implemented in late summer 2020. **Updated target date:** Remains March 2021

Action plan (continued)

Follow-up previous year action plans (continued)

Area	2017/18 Recommendation	2018/19 Management Response	Responsible person	Target Date	Priority	2019/20 Update
Fixed Asset Register	To ensure the accuracy and completeness of fixed asset records, we recommend that a full data cleansing exercise is carried out on Britannia ahead of transitioning to the new integrated ERP system, CMIS, and that the importance of staff communicating any changes in fixed assets to the Finance team in the annual return is re-emphasised.	In addition to the annual fixed asset verification exercise, we undertook further work in 2018/19 to verify fixed asset register records for land, buildings and vehicles to other sources. Further work on other asset groups will be undertaken in 2019/20 in advance of the migration to the new System.	Head of Finance	March 2020	Medium	***Implemented:*** Action completed ready for migration once CMIS is ready. **Updated management response**: We undertook a fixed asset verification exercise earlier in the year than unusual to allow more time for detailed review. The 2019/20 review had a greater focus on older assets on the register and we managed to cleanse a lot of these older records. The records are now ready for migration.

Our other responsibilities explained

Fraud responsibilities and representations

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. 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.

Required representations:

We have asked the Board to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the entity or group.

We have also asked the Board to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

Audit work performed:

In our planning we identified the risk of fraud in relation to completeness and accuracy of commercial income and management override of controls as a key audit risk for your organisation.

During the course of our audit, we have had discussions with management and those charged with governance.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the financial statements.

We have reviewed the paper prepared by management for the audit committee on the process for identifying, evaluating and managing the system of internal financial control.

Concerns:

No concerns have been identified regarding fraud.

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 HES and and our objectivity is not compromised.
Fees	The audit fee for 2019/20, in line with the expected fee range provided by Audit Scotland, is £78,160, as analysed below: As discussed on page 4, as a result of the increased risk associated with the audit and the concurrent increase in audit work required, we will be proposing an increase in audit fee for 2019/20. This will be discussed with management as part of the close down of the audit. The fee set out above has not been updated to reflect this additional work. No non-audit services fees have been charged for the period.
Non-audit services	In our opinion there are no inconsistencies between the FRC's Ethical Standard and the company'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 are required to provide written details of all relationships (including the provision of non-audit services) between us and the organisation, its board and senior management and its affiliates, including all services provided by us and the DTTL network to the audited entity, its board and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence. We are not aware of any relationships which are required to be disclosed.

Fee analysis (Fees row):

	£
Auditor remuneration	60,690
Audit Scotland fixed charges:	
Pooled costs	14,110
Audit support costs	3,360
Total fee	**78,160**
HESe (Net of VAT)	13,250
Total Fee	**91,410**

Quality of public audit in Scotland

Annual report 2018/19

Audit Scotland published its annual assessment of audit quality carried out on the audit work delivered by Audit Scotland and appointed firms. A copy of the full report is available: https://www.audit-scotland.gov.uk/report/quality-of-public-audit-in-scotland-annual-report-201819

Public audit in Scotland

Recent high-profile corporate collapses in the private sector have led to considerable scrutiny of the audit profession. The Brydon review is looking into the quality and effectiveness of the UK audit market. The Kingman review, the Competition and Markets Authority market study of the audit services market and the Business, Energy and Industrial Strategy Committee's report on the Future of Audit have all reported on structural weaknesses in the private sector audit regime. The reviews are placing a strong focus on the need for independence of auditors from the bodies they audit.

The public audit model in Scotland is fundamentally different to the private sector audit regime and is well placed to meet the challenges arising from the reviews of the auditing profession. Public audit in Scotland already operates many of the proposed features to reduce threats to auditor independence including:

- independent appointment of auditors by the Auditor General for Scotland and Accounts Commission
- rotation of auditors every five years
- independent fee-setting arrangements and limits on non-audit services
- a comprehensive Audit Quality Framework.

The Audit Scotland Audit Quality and Appointments (AQA) team will continue to develop its activities to provide the Auditor General for Scotland and Accounts Commission with assurance about audit quality. The Audit Quality Framework will be refreshed to take account of the findings from the first two years of its application and to reflect on the developments in the wider audit environment. Further development is planned over the following year to include:

- enhancing stakeholder feedback
- reviewing the structure and transparency of audit quality reporting.

Key messages

The programme of work carried out under the Audit Quality Framework provides evidence of compliance with auditing standards and the Code of audit practice (the Code), together with good levels of qualitative performance and some scope for improvements in audit work delivered in the period 1 April 2018 to 31 March 2019.

Independent external reviews of audit quality carried out by The Institute of Chartered Accountants of Scotland (ICAS) show evidence of compliance with expected standards:

- ICAS did not identify any concerns with audit opinions
- 55 per cent of financial audit files reviewed by ICAS over the last two years were graded as limited improvement required, the remaining reviews were graded as improvement required *(100% of Deloitte files – limited improvement)*
- ICAS noted considerable improvements in the documentation of performance audits and Best Value assurance reports.

Other performance measures showing good performance include:

- 78 per cent of internal reviews of financial audits in the last two years required only limited improvements *(100% of Deloitte internal reviews graded as no improvement required)*
- all audit providers have a strong culture of support for performing high-quality audit
- stakeholder feedback shows audit work has had impact
- non-audit services (NAS) are declining in number and value and requests made complied with the Auditor General for Scotland and Accounts Commission's NAS policy.

AQA monitors progress against areas for improvement. A common area for improvement in the last two years has been the need for better documentation of audit evidence. In 2018/19 further areas for improvement were identified in:

- the use of analytical procedures
- the application of sampling.