The 2020/21 audit of the Scottish Government Consolidated Accounts

AUDITOR GENERAL

Prepared for the Public Audit Committee by the Auditor General for Scotland
Made under section 22 of the Public Finance and Accountability (Scotland) Act 2000
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Contents

Introduction

1. I provide this report on the 2020/21 audit of the Scottish Government Consolidated Accounts under section 22(3) of the Public Finance and Accountability (Scotland) Act 2000. My report is intended to support the Scottish Parliament in its important scrutiny role of the Government's finances. The report contains key information from the 2020/21 Consolidated Accounts and explains what they show about the Scottish Government's management of its budget. It also provides information on governance and financial and performance reporting.

2. Responding to the threat posed by the Covid-19 pandemic was the primary focus of the Scottish Government throughout the 2020/21 financial year. Plans to support and protect public health alongside the development of economic recovery activity using the 'four harms' framework dominated decision-making including committing significant additional amounts of public spending during the year to support its ongoing response. [1]

3. The uncertainty caused by the pandemic and the damage inflicted on individuals, businesses and communities means its effects will be felt across all aspects of the Scottish public sector and the wider economy for years to come. Good use of public money and sound governance remains essential to ensuring that maximum value can be achieved from future spending plans and recovery activity.

4. In February 2020, the Scottish Government published its draft 2020/21 Scottish Budget which set out its spending priorities and plans for the year. This was subsequently revised through three separate budget revisions over the course of the year to reflect additional monies available to support the Covid-19 response, taking the Scottish Government's total budget for the year to £50.7 billion. The Scottish Government's Consolidated Accounts for 2020/21 provide information on how this budget was managed and where money was spent and are a key component of the Scottish Government's accountability to the Scottish Parliament and the public. This was the first full financial year in which funding to support the Covid-19 pandemic response and recovery is reflected in the Scottish Government's financial performance.

[1] Framework for Decision Making – Assessing the Four Harms of the Crisis, Scottish Government, December 2020.

5. The boundary for the Consolidated Accounts is determined by the Scottish Government and reflects the areas for which it has direct responsibility and accountability, including the core portfolios, supporting administration, the executive agencies and NHS bodies. It does not include bodies where the Scottish Government holds significant shareholdings such as Ferguson Marine (Port Glasgow) Holdings Limited, Caledonian Maritime Assets Limited (CMAL), Scottish Futures Trust or Prestwick Airport.

6. The Consolidated Accounts:

- cover around 90 per cent of the budget approved by the Scottish Parliament
- report the amounts the Scottish Government spent against each main budget heading, and the reasons for any significant differences
- show the amounts distributed to other public bodies including local government
- report the assets, liabilities and other financial commitments of the core Scottish Government, and bodies within the consolidated boundary, carried forward to future years
- contain a performance report, in which the government gives an account of its performance during the year.

Key messages

- The 2020/21 financial year is the first in which the Scottish Government's funding to support the Covid-19 pandemic response is reflected in its financial performance. The Scottish Government's Consolidated Accounts for 2020/21 show that total net expenditure was £50,121 million. This was £10,736 million (27 per cent) more than in 2019/20 reflecting the significant additional amounts of public spending committed to responding to the Covid-19 pandemic.
- Overall, total spending was £580 million less than budget. The resource budget was underspent by £373 million (0.8 per cent) against a budget of £48,573 million and capital was underspent by £207 million (9.7 per cent) against a budget of £2,128 million.
- My independent audit opinion is unqualified. This means in my opinion, I am content the Scottish Government Consolidated Accounts show a true and fair view, following accounting standards, and that the income and expenditure for the year is lawful.
- The Scottish Government allocated £8.6 billion of Barnett consequentials to support its Covid-19 response activity through three budget revisions during 2020/21. Over the year, Audit Scotland has published briefing papers to track the Scottish Government's plan for these additional funds to support the Scottish Parliament's understanding of the financial implications of Covid-19. These funds formed a significant part of the Scottish Government's financial response to supporting the health service, businesses, local government, and the wider economy during the year.
- High-level details are provided in the Scottish Government's accounts over how this money was spent during the year. The Scottish Government needs to be proactive in publishing comprehensive Covid-19 financial reporting information which clearly links budgets, funding announcements and spending levels. This will increase transparency in the Government's financial reporting in an area of significant parliamentary and public interest.
- During 2020/21, the Scottish Government operated two large Business Support Schemes: The Business Support Fund Grants (including the Small Business Support Grant and the Retail, Hospitality and Leisure Grant) and the Strategic Framework Business Fund (including Retail, Hospitality and

Leisure Top-up Grant). The schemes were established to respond quickly to the financial impact of Covid-19 on businesses and were essential in supporting jobs and the wider economy at a critical time. The need to make payments quickly meant the Scottish Government had to accept a higher-than-normal level of fraud risk. Over the course of the year, the Scottish Government took action to minimise fraud risk, working closely with local authorities who administered individual payments on behalf of the Government.

- In recent years, the Scottish Government has taken a direct role in providing financial support to private companies. Financial support provided to businesses such as Burntisland Fabrications Limited, Ferguson Marine Engineering Limited, Prestwick Airport and the Lochaber Aluminium Smelter (Liberty Group) has not delivered expected outcomes and is unlikely to achieve value for money. In 2018, my predecessor recommended that the Scottish Government develop a framework to outline its principles and approach for decisions about future investment in private companies. This is now being actioned by the Scottish Government. Such a framework should help the Scottish Government provide assurance to Parliament over its strategic objectives in entering any future agreements and the decision-making process involved.

- The Scottish Government has strengthened aspects of its governance arrangements. During 2020/21, there was a strong focus on the impact of the Covid-19 pandemic on the organisation, including the challenges facing staff capacity and wellbeing. Sponsorship of public bodies remains an area of concern and the Scottish Government has taken steps in the last year to make improvements. Significant changes have taken place, and will continue to take place, across a number of important leadership roles within the Scottish Government, including a new Permanent Secretary, who will take up post in January 2022. Strong leadership and effective governance will remain critical as the Scottish Government seeks to recover from the effects of the pandemic and plan for the future.

Financial management

Scottish Government budget performance 2020/21

7. The Consolidated Accounts show that total net expenditure during 2020/21 was £50,121 million, £580 million less than budget (Exhibit 1). The resource budget was underspent by £373 million (0.8 per cent) against a budget of £48,573 million and capital underspent by £207 million (9.7 per cent) against a budget of £2,128 million.

Exhibit 1
Total expenditure (resource and capital) against the Scottish Budget approved by the Scottish Parliament
The Scottish Government consolidated total was £580 million under budget in 2020/21.

Portfolio	Actual (£m)	Budget (£m)	Over/(under) spend (£m)
Health and Sport	17,798	18,090	(292)
Communities and Local Government	13,096	13,050	46
Finance	228	231	(3)
Education and Skills	4,984	4,950	34
Justice	2,844	2,885	(41)
Transport, Infrastructure and Connectivity	3,814	4,135	(321)
Rural Economy and Tourism	945	998	(53)
Environment, Climate Change and Land Reform	475	502	(27)
Economy, Fair Work and Culture	2,033	1,980	53
Social Security and Older People	3,686	3,660	26
Constitution, Europe and External Affairs	46	50	(4)
Crown Office and Procurator Fiscal Service	172	170	2

Portfolio	Actual (£m)	Budget (£m)	Over/(under) spend (£m)
Scottish Government consolidated total	**50,121**	**50,701**	**(580)**

Source: Scottish Government Consolidated Accounts 2020/21 (page 104). Further information on individual portfolio spending performance can be found in pages 105 to 116 in the Consolidated Accounts.

8. High-level reasons for significant variances between actual and budgeted spend are included in the Consolidated Accounts (pages 105-116). The largest variances relate to underspends in the Transport, Infrastructure and Connectivity portfolio (£321 million) and the Health and Sport portfolio (£292 million). The Scottish Government reported that the variances for the former included lower than budgeted demand for Covid-19-related grants for concessionary travel, lower than expected demand for energy efficient schemes and lower than anticipated depreciation costs. The underspend in the Health and Sport portfolio was attributed to the timing of Barnett consequentials received around the financial year end which have been carried forward to be utilised in 2021/22.

9. My independent auditor's report is set out at pages 100-103 of the Consolidated Accounts. My opinion on the 2020/21 financial statements is unqualified. This means, in my opinion, I am content the Scottish Government Consolidated Accounts show a true and fair view and have been properly prepared to follow accounting standards and that the income and expenditure for the year is lawful.

10. The Scottish Government allocated £8.6 billion of Barnett consequentials to support its Covid-19 response activity through three budget revisions during 2020/21. This formed a significant part of the Scottish Government's financial response to supporting the health service, businesses, local government and the wider economy during the year. Earlier Scottish Government analysis provided to Audit Scotland indicated that around £8.8 billion was spent on Covid-19 during the year.

11. High-level details are provided in the Scottish Government's accounts over how this money was spent during the year. The Scottish Government needs to be proactive in publishing comprehensive Covid-19 financial reporting information which clearly links budgets, funding announcements and spending levels. This will increase transparency in the Government's financial reporting in an area of significant parliamentary and public interest.

12. During 2020/21, the Scottish Government operated two large Business Support Schemes: The Business Support Fund Grants (including the Small Business Support Grant and the Retail, Hospitality and Leisure Grant) and the Strategic Framework Business Fund (including the Retail, Hospitality and Leisure Top-up Grant). Payments from these schemes totalled £1,599 million during the year. The schemes were established to respond quickly to the financial impact of Covid-19 on businesses and were essential in supporting jobs and the wider economy at a critical time. The need to make payments quickly meant the Scottish Government had to accept a higher-than-normal level of fraud risk. Over the course of the year, the Scottish Government took action to minimise fraud risk, working closely with local authorities who administered individual payments on behalf of the Government.

13. It is the Scottish Government's responsibility to ensure it can appropriately assess the levels of error and fraud that may exist within its accounts. In the Governance Statement (page 59), the Scottish Government outlined how it obtained assurance on grants to local authorities for the payment of these large support schemes including its own estimate of fraud and error. The Scottish Government estimates fraud and error in these schemes to be no more than one to two per cent of payments, approximately £16 million to £32 million. This is based on information available about the schemes being targeted, the quality and completeness of fraud controls and the evidence of fraud detected. While this estimate is not unreasonable, the Scottish Government needs to regularly assess and improve its estimates of fraud and error in Covid-19 grant schemes and assure themselves that controls to detect and prevent fraud and error are working in practice. They should also ensure regular public reporting to satisfy high levels of public interest in this area.

Social security and older people portfolio

14. The 2020/21 financial year is the second full year that Social Security Scotland, an executive agency, is consolidated into the Scottish Government's accounts as a separate component audited body. The relevant expenditure is disclosed within the Social Security and Older People portfolio outturn statement (page 114).

15. The 2020/21 accounts of Social Security Scotland include benefit expenditure of £3,260 million administered by the Department for Work and Pensions (DWP) under agency agreements with Scottish Ministers. Due to these delivery arrangements, Social Security Scotland cannot directly assess the levels of fraud and error in these benefits and is instead reliant on the DWP's annually published estimates.

16. The estimated overpayments as a result of fraud and error in relation to each type of benefit that is delivered by the DWP, ranged from 1.5 to 5.2 per cent of expenditure. This means an estimated £65.4 million of overpayments were made in Scotland. As a result, the auditor qualified their regularity opinion as these overpayments were not incurred in accordance with relevant legislation and regulations. Further details can be found in the 2020/21 Annual Audit Report of Social Security Scotland. I will also publish a performance audit in Spring 2022 on Social Security: implementing the devolved powers.

17. As a component audit, the qualified audit opinion on the Social Security Scotland accounts requires me to assess the potential impact of its inclusion within the Scottish Government's Consolidated Accounts. I concluded that, for 2020/21, the likely amount of error and fraud incurred is not significant enough to influence the economic decisions of the users of the accounts and therefore I have not qualified my opinion in respect of this matter.

Crown Office and Procurator Fiscal Service

18. The Scottish Government's Consolidated Accounts include special payments of £40.2 million made by the Crown Office and Procurator Fiscal Service (COPFS) during 2020/21 (page 98) of which £40 million relates to a specific legal case brought against the Lord Advocate by individuals prosecuted in connection with the acquisition and administration of Rangers Football Club (page 99).

19. The auditor of the COPFS noted in their 2020/21 Annual Audit Report that COPFS overspent its annual budget by £14.6 million due to unplanned costs arising from ongoing court proceedings against the COPFS. The Scottish Government authorised the overspend.

20. Some cases have resolved, with sums paid to the pursuers totalling £35.3 million to September 2021 (£27.2 million settlement costs and £8.1 million legal costs). In February 2021, the Lord Advocate made a statement in the Scottish Parliament about this matter and has committed to further public accountability and to a process of inquiry once all litigation has concluded.

Capital and resource borrowing

21. Under the terms of the Scotland Act 2016, Scottish Ministers can borrow up to £3 billion for capital purposes, with an annual borrowing limit of 15 per cent (£450 million) of the overall borrowing cap. In 2020/21, the Scottish Government borrowed £200 million. This was less than the £450 million outlined by Scottish ministers as part of the 2020/21 Scottish budget. The loan will be repaid to the National Loans Fund over 25 years. This is in line with timescales outlined in the Fiscal Framework. The Scottish Government have advised that 2020/21 borrowing was used to support its overall capital programme although no details of how this applied to specific projects is included within the Consolidated Accounts.

22. In 2020/21, the Scottish Government borrowed to fund resource expenditure for the first time. During the year it borrowed £207 million from the National Loans Fund to be repaid over five years. This was within the £300 million limit for Resource Borrowing for the financial year 2020/21. The Scottish Government reported the requirement for resource borrowing arose due to a forecasting issue where the 2017/18 level of Scottish income tax to be received was over-estimated by £204 million.

23. As at 31 March 2021, the total principal level of capital borrowing outstanding was £1,219.7 million, with interest of £164.3 million applying over its remaining life. Revenue borrowing outstanding at 31 March 2021 was £207 million with interest of £1.7 million accruing over the five-year repayment period.

24. Details of the overall loan, repayments and interest payments are outlined on pages 55 and 56 of the Consolidated Accounts. The Scottish Government's borrowing and associated repayments are made via the Scottish Consolidated Fund (SCF). Borrowed amounts and repayments are made between the SCF and HM Treasury with the corresponding adjustments made to funding received by the Scottish Government from the SCF. This means there is no associated liability disclosed in the Statement of Financial Position within the Scottish Government's Consolidated Accounts. Details of the amount of capital borrowing and the associated liability are set out within a separate account prepared for the SCF.

Overall financial position

25. The Consolidated Statement of Financial Position (page 117) is one of the primary financial statements in the Consolidated Accounts. It summarises what is owned and owed by the core Scottish Government and those public bodies within the consolidated boundary. This shows taxpayers' equity – an accounting measurement of the amount of taxpayers' money applied that has continuing public benefit. It shows how much of this has arisen from the application of parliamentary funding (arising from the Scottish Block Grant, borrowing and devolved taxes) and how much resulted from changes in the value of physical assets over time.

26. Taxpayers' equity has increased in each of the last five years from £31.2 billion to £33.6 billion, largely due to an increase in physical assets (such as property and roads) and financial assets (such as loans and investments). Total liabilities (such as payments for private-financed projects) have increased from £7.7 billion to £9.9 billion. It is important to note that the position does not reflect all the assets and liabilities of the Scottish public sector. Key assets and liabilities are excluded such as resource and capital borrowing, local government borrowing, and all public sector pension liabilities funded from the Scottish budget.

Financial support to private companies

27. In recent years, the Scottish Government has taken a direct role in providing financial support to private companies in addition to support provided through its enterprise agencies; Scottish Enterprise, Highlands and Islands Enterprise and South of Scotland Enterprise.

Prestwick Airport

28. In November 2013, the Scottish Government purchased Prestwick Airport for a nominal price of £1 with the stated aim of protecting jobs and safeguarding what it considered to be a strategic infrastructure asset. The total level of loan support provided up to 31 March 2021 is £43.4 million although this was valued at £11.6 million in Transport Scotland’s accounts at the financial year end following an independent valuation. A further £1.2 million interest charges have accrued during the year resulting in total accrued interest of £6.3 million. In keeping with Transport Scotland’s approach in previous years, the interest on these loans has been impaired to nil.

29. In June 2019, the Scottish Government announced that the sale of Prestwick Airport was being progressed, in keeping with its long-term objective that the airport should be returned to the private sector. In October 2020, the Cabinet Secretary for Transport, Infrastructure and Connectivity confirmed to the Scottish Parliament that the preferred bidder, selected earlier in the year, had withdrawn from the process considering the global impact of Covid-19 on the aviation sector. Transport Scotland is still looking to sell Prestwick Airport once a buyer is found.

Ferguson Marine (Port Glasgow) Holdings Limited

30. Over 2017 and 2018, the Scottish Government provided commercial loan facilities totalling £45 million to Ferguson Marine Engineering Limited (FMEL), a shipbuilding and engineering company based in Port Glasgow. The purpose of the loans was to support FMEL's completion of a contract to build two ‘dual-fuel’ ferry vessels (Vessels 801 and 802) for Caledonian Maritime Assets Limited (CMAL). By April 2019, FMEL had drawn down the full loan facility of £45 million and no extended facilities were provided.

31. In August 2019, FMEL entered administration which led to the Scottish Government acquiring the business in December 2019 following a review of bids by the administrator. Following administration, a new company was established, known as Ferguson Marine (Port Glasgow) Holdings Limited (FMPG). FMPG is a company wholly owned by Scottish Ministers established under the Companies Act 2006. It does not fall within the boundary of the Scottish Government’s Consolidated Accounts.

32. As part of the reorganisation of the contractual arrangements, the Scottish Government entered into new contracts with FMPG for the completion of work on Vessels 801 and 802 as at 1 April 2020. The existing voted loans, including all capital and interest sums (£97.7 million) were terminated and ownership of the Vessels 801 and 802 and the associated equipment and design rights transferred from CMAL to the Scottish Government. In advance of the transfer of ownership, the vessels were valued at £74.8 million. The difference between the valuation and the outstanding loans (£22.9 million) was written-off through the Scottish Government 2020/21 Consolidated Accounts.

33. In December 2020, the Scottish Parliament’s Rural Economy and Connectivity Committee published its report into the cost overruns and delays associated with the delivery of Vessels 801 and 802. It concluded there had been serious failures in vessel procurement, project planning, project management and communication.

34. In March 2022, I will publish a performance audit assessing the management of the project to deliver Vessels 801 and 802. The audit will review the initial arrangements that were in place to manage the project and how well the Scottish Government, Transport Scotland and CMAL responded when problems arose. It will consider the learning that has been applied to the new arrangements and make recommendations to help improve the management of similar projects.

Burntisland Fabrications Limited (BiFab)

35. In 2018/19 the Scottish Government converted £37.4 million of commercial loans it had advanced to BiFab into equity in the company representing a total equity stake of 32 per cent. In the 2019/20 Consolidated Accounts, the Scottish Government’s equity stake was valued at nil to reflect expected losses in line with accounting requirements.

36. During 2020/21 the Scottish Government provided further loans of £4.5 million to BiFab to help the completion of outstanding contracts. In December 2020, BiFab went into administration due to its challenging financial position. There was no legal route for either the Scottish Government or the UK Government to provide further financial support to the company in the current situation and the loan of £4.5 million was fully written off in year. The Consolidated Accounts (page 54) refers to the subsequent sale of the business in February 2021 and that the Scottish Government will continue to work with the administrators to maximise the recovery of public money.

Lochaber Aluminium Smelter – Liberty Group

37. In December 2016, the Scottish Government issued a 25-year financial guarantee contract to SIMEC Lochaber Hydropower Limited. This contract guarantees the power purchase obligations of the Liberty Aluminium Lochaber Limited smelter if the business does not fulfil its obligations to pay for contracted power. The Scottish Government receives an annual fee in return for the guarantee.

38. The annual exposure to the Scottish Government is between £14 million and £32 million, over the lifetime of the contract. At the start of the contract in December 2016, the total potential financial exposure to the Scottish Government was £586 million. To reduce the exposure of the contract, the Scottish Government created a security package which includes first line security over the hydro plant, the smelter and land which formed part of the original purchase of the smelter by the GFG Group.

39. In March 2021, Greensill Capital (UK) Limited, a major provider of working capital to GFG Alliance, went into administration. This impacts on the Lochaber smelter as it is a subsidiary of Liberty Industries UK Limited, alongside Liberty Steel Limited, under GFG Alliance. The situation is further complicated as the hydro power station that supplies the smelter is owned by GFG Alliance through its other main group of companies, SIMEC.

40. With the ongoing uncertainty regarding the financial stability of the GFG Alliance group, the Scottish Government reviewed the level of provision required with regards to their guarantee. The provision in the Consolidated Accounts increased from £37 million in 2019/20 to £161 million as at 31 March 2021. I have concluded for 2020/21, the Scottish Government's approach to setting the level of provision against the potential exposure through the guarantee is reasonable.

The strategic approach to financial interventions

41. In my 2019/20 report on the audit of the Scottish Government's Consolidated Accounts, I highlighted the need for the Scottish Government to clearly outline its plans for future investment in private companies to ensure there is greater transparency over financial support provided and the value of public funds committed. The Scottish Government had already recognised that there were a range of risks, for example, EU exit and Covid-19, likely to have a business impact and which could potentially increase the number of distressed and restructured businesses.

42. During the year, the Scottish Government established a new Covid Business Resilience and Support Directorate which includes the Strategic Commercial Investments Division (part of DG Economy). The Division aims to consolidate expertise and knowledge and increase capacity to respond to cases that arise seeking support from the Scottish Government.

43. In 2018, my predecessor recommended that the Scottish Government develops a framework to outline its principles and approach for decisions about future investment in private companies. This is now being actioned by the Scottish Government. Such a framework should help the Scottish Government provide assurance to Parliament over its strategic objectives in entering any future agreements and the decision-making process involved.

44. It remains essential for the Scottish Government to learn lessons from its experience of recent financial interventions in private companies. In adopting a framework for investment, it is important that the Scottish Government clearly outlines its plans for future investment in private companies to ensure there is greater transparency over the value of financial support provided, the risks involved and the expected outcomes for the public.

European Structural and Investment Funds

45. The Scottish Government is responsible for managing two European Structural and Investment Funds for the period 2014 to 2020; the European Social Fund (ESF) and the European Regional Development Fund (ERDF).

46. In November 2019, the EC placed the ESF programme in suspension after the Scottish Government was unable to resolve all outstanding issues by this deadline. In January 2020, the EC also placed the ERDF programme into suspension. The Scottish Government cannot make claims for funding to the EC until the issues identified are resolved. While programmes are suspended, the Scottish Government's claims to the EC for reimbursement of funds will not be paid until all issues identified are resolved. The ERDF suspension was lifted in December 2020 but the ESF suspension continues.

47. In 2020/21, the Scottish Government recognised that implementing the agreed methodology will likely result in greater expenditure over the course of the programme than can be reclaimed from the EC. As a consequence, and in line with accounting standards, the Scottish Government wrote off £16 million in the 2020/21 Consolidated Accounts in respect of grant payments already made and has provided a further £28.7 million relating to the future under-recovery of costs.

48. Following the UK's withdrawal from the European Union, ESF funding will be replaced by UK Government-led funding programmes including the Shared Prosperity Fund, Community Renewal Fund and the Levelling-up Fund. Under the Withdrawal Agreement, the UK will continue to participate in the Multiannual Financial Framework programmes, like ESF, until it ends in 2023.

Non-Domestic Rating Account

49. Non-domestic rates are a tax charged on properties that are used for non-domestic purposes, for example, private businesses, and public and third sector properties. The tax is collected by individual councils and pooled by the Scottish Government. It is then redistributed to councils as part of the overall annual local government funding settlement. The Scottish Government, on behalf of Scottish Ministers, is required to prepare a NDR account at the end of each financial year, in accordance with the Local Government Finance Act 1992. The purpose of the account is to demonstrate that the non-domestic rates receipts collected by councils are redistributed to them by the Scottish Government.

50. The NDR account is made up of two key components:

- receipts from non-domestic rates income collected by councils; and
- payments redistributed to councils from the Scottish Government.

51. The amounts received from and redistributed to councils are subject to timing differences as, in any year, the amount raised by non-domestic rates will only become known once the financial year is over. To help manage variances, each council provides an estimate of what they expect to raise in non-domestic rates, less any retentions from relief schemes, and submits this to the Scottish Government at the start of each financial year.

52. Regulations made under the legislation permit mid-year adjustments to councils' funding only where revised NDR income estimates by councils are below 97 per cent of their initial estimates. During the 2020/21 financial year, to support councils' cashflows during the Covid-19 pandemic, the Scottish Government adjusted NDR receipts and payments based on councils' mid-year estimates. However, the adjustments included £60.3 million where the mid-year estimates were more than 97 per cent of the initial estimates. As a result, the NDR account includes £40.4 million of receipts and £19.9 million of payments which were not in accordance with the regulations. The auditor of the 2020/21 NDR account therefore qualified his opinion on regularity in relation to this matter.

53. The differences between NDR estimates and actual amounts do not impact the level of funding provided to councils during the financial year. The Scottish Government guarantees the combined amount of revenue grant funding and non-domestic rates distributions provided to councils each year and manages the financial risk of variances within its own budget. Where variances in non-domestic rates occur, the Scottish Government adjusts the council's general revenue grant to ensure funding levels to local government align to the levels agreed in the local government finance settlement for that year.

Financial and performance reporting

Financial reporting

54. In January 2021, the Scottish Government published its third Medium Term Financial Strategy alongside the 2021/22 draft Scottish Budget. The introduction of an annual strategy followed a recommendation from the Parliament's Budget Process Review Group in 2017. The strategy aims to provide an assessment of the medium-term outlook for Scotland's public finances as the financial powers from the Scotland Acts 2012 and 2016 come into effect. The 2021 Strategy sets out its assessment of Scotland's economic and fiscal outlook, as well as a broad spending outlook considering the effects of changing funding levels for government spending. The Scottish Government is due to publish its next iteration of the MTFS alongside its draft 2022/23 budget in December 2021.

55. In February 2021, the Scottish Government also published its Capital Spending Review setting out its indicative capital spending allocations in years 2021/22 to 2025/26 that aim to support the implementation of the Government's Infrastructure Investment Plan published at the same time. Looking ahead, in November 2021 the Cabinet Secretary for Finance and the Economy committed to publishing a Scottish Resource Spending Review before the end of May 2022.

56. The Covid-19 pandemic has brought increased uncertainty and potential volatility to public finances over the medium-term. There is uncertainty as to how the economic impact of the pandemic will affect devolved tax and social security powers, as well as the wider pressures on the budget from increased demand for services. It is important that these key fiscal publications clearly reflect the likely impact of the pandemic on public finances including on planned outcomes and options for ensuring financial sustainability. This will help to aid Parliament's understanding of the financial risks and opportunities that emerge from the Covid-19 pandemic including the difficult choices required over public spending.

Public sector consolidated account

57. In 2016, the Scottish Government committed to producing a consolidated account to cover the devolved public sector in Scotland including total assets, investments, and liabilities such as local government borrowing and public sector pension liabilities.

58. Progress in finalising the draft account for audit remains slow with the Scottish Government prioritising responding to the Covid-19 pandemic and the preparation of the 2019/20 and 2020/21 Consolidated Accounts. There have also been delays in finalising the 2019/20 Whole of Government Account which forms the basis for these pan-Scotland accounts largely due to ICT issues at HM Treasury.

59. The Scottish Government has committed to the development of a devolved public sector account on a two-stage basis. In the first stage, the Scottish Government aims to compile the account at the Scottish Administration level and then add the other directly funded bodies. This will include the 2020/21 financial outturn together with prior year comparators. The Scottish Government plans to provide this account for audit in Spring 2022.

60. In the second stage, the Scottish Government plans to explore further the use of the UK Whole of Government Accounts process to obtain the information about NDPBs, other public bodies and local authorities. The Scottish Government does not expect this to be complete until later in 2022 as incorporating that level of expenditure will require more in-depth analysis and review.

61. The consequences of the pandemic and the impact of EU withdrawal continue to pose significant risks to the sustainability of public finances. There remains a need for a public consolidated account to provide a comprehensive and transparent assessment of the state of Scotland's public finances particularly given the financial consequences of the pandemic and the investment required as part of the Government's recovery and renewal plans. This is important for decision-making over the longer term as it will provide information about the impact of past decisions on future budgets, the potential risks to financial sustainability and the scale of assets and liabilities, including those held by publicly owned companies.

62. I note the commitment made by the Scottish Government to the development of this account and I urge the Scottish Government to move as swiftly as possible towards fulfilling this revised timetable.

Performance reporting

63. The 2020/21 Consolidated Accounts include a performance report and an accountability report in line with the requirements of the Government Financial Reporting Manual (FReM). In May 2020, HM Treasury outlined minimum reporting requirements to support public bodies in their preparation of financial statements to reflect the pressures facing them as a result of the pandemic. This included the option to omit certain aspects of performance reporting.

64. The Scottish Government's performance report (pages 4 to 57) summarises financial performance for the year, with emphasis on performance against budget. It also contains some specific performance information which is required by current guidance on supplier payment performance, and signposts where more information is available on sustainability and environmental performance.

65. The performance report provides information around the impact of Covid-19 on performance during the year and the shift of priorities to address the different stages of the pandemic. The impact on national outcomes is well documented in The Impact of Covid-19 published in December 2020 by the Scottish Government. Initial evidence indicates that some outcomes were more adversely affected than others and that some will have a longer-term impact on society with existing inequalities expected to widen further.

66. For 2020/21, the Performance Analysis section of the performance report has been largely redesigned to provide the reader with a range of information on each portfolio's policy aims, impact of Covid-19 on these priorities, the deliverables during the year and the intended contribution to the national outcomes.

67. The additional information is welcome, but it requires to be refined further to ensure greater accessibility and transparency to the reader. It is difficult to form an overall picture of the performance of the Scottish Government from the various strands of information presented. In the absence of defined, measurable targets, it is difficult for the reader to assess whether the national outcomes are being achieved. In addition, it is challenging to link the performance information with the individual portfolio outturn statements which are provided in the financial statements.

68. The Scottish Government acknowledges that there is further room for improvement in the transparency of the reporting and the links between performance analysis and financial performance in the portfolio outturn statements. Further changes will enhance reporting to the Scottish Parliament and the public and help strengthen accountability and scrutiny.

Governance

69. A Governance Statement (pages 59-81) prepared by the Permanent Secretary is a key feature of the Consolidated Accounts. It forms part of a wider accountability report and summarises how the core Scottish Government organisation is controlled and directed. The statement confirms that the Scottish Government complies with relevant guidance on corporate governance. It also highlights the main risks and opportunities for the organisation and any significant internal control issues in 2020/21. I am content that the Governance Statement is consistent with the financial statements and has been prepared in accordance with guidance issued by the Scottish Ministers.

70. The Scottish Government has strengthened aspects of its governance arrangements. During 2020/21, there was a strong focus on the impact of the Covid-19 pandemic on the organisation, including the challenges facing staffing capacity and wellbeing. The scale and pace of demands placed considerable strain on staff across the organisation combined with existing capacity pressures and the challenges of remote working. Improvements to risk management processes continue to evolve and embed across the organisation. This includes greater scrutiny and challenge of risks at both portfolio and corporate level. There remains scope for greater clarity on the impact of planned actions on reducing risk levels and the anticipated time taken to achieve risk targets across the organisation.

71. Over the last year, there were several changes to the Scottish Government's Corporate Board. These included new Directors General for both Education and Justice, and Health and Social Care portfolios. In addition, there were new appointments to the posts of Director of Communications, Ministerial Support and Facilities and, Equality, Inclusion and Human Rights. A new Chief Financial Officer also started in November 2020.

72. This level of change will continue into next year with a new Permanent Secretary starting in January 2022. DG Economy retired in November 2021 with the role being split into DG Economy and DG Net Zero. External recruitment campaigns during 2021 for the posts of DG Economy and DG Net Zero were unsuccessful in identifying appointable candidates. These have been filled on an interim basis and will be re-advertised in early 2022. These are key roles for the Scottish Government and are essential to achieving the objectives set out in the national outcomes.

73. Currently, there are ten Non-Executive Directors (NXDs) whose role is to provide support and challenge to the Scottish Government. Three of the four NXDs currently serving on the Corporate Board will reach the end of their term during 2022. One other NXD left the Scottish Government during 2020/21 and was replaced later in the year.

74. The changes in senior leadership roles presents a good opportunity for the Scottish Government to reflect further on its governance and operational structures, its decision-making processes, and its overall senior capacity to ensure it can fully support the various demands, both internal and external, on the organisation in the years ahead. It will be important that the Scottish Government limits the use of interim appointments to ensure greater stability and certainty within its leadership group. Overall, it remains important for the Scottish Government to keep its governance arrangements under review to ensure they remain fit for purpose, particularly during this continuing period of change and uncertainty.

75. The Scottish Government's arrangements for sponsoring public bodies remains an area of concern. Last year, I reported that the Scottish Government had taken initial steps to improve the effectiveness of its role in sponsoring public bodies but that the establishment of a governance hub module on sponsorship training, accreditation for sponsors and workshops and networking events for Accountable Officers and sponsors had largely paused due to Covid-19.

76. I am pleased to report that the Public Bodies Unit has restarted its support and training role for sponsors. An online support portal has been launched providing guidance and training to sponsorship staff and a programme of training events has restarted. A training package has been developed and delivered to sponsor teams across the Scottish Government, and training has also been provided during the year to board members and practitioners, including Accountable Officers.

77. During 2021, the Scottish Government commissioned an external consultant to conduct a review of the Scottish Government's relationships with public bodies. The review will consider the current delivery of sponsorship arrangements within the Scottish Government including how it should organise and manage its relationships with public bodies. It will also consider how sponsors and public bodies can effectively manage risk and escalation of issues when challenges arise. The report is expected to make a number of recommendations for improvement and is due to be considered by the Scottish Government's Executive Team before the end of 2021. I will review the effectiveness of changes made in forthcoming audit work.

Conclusion

78. The Consolidated Accounts remain a critical component of the Scottish Government's accountability to the Scottish Parliament and the public. They are particularly important during times of significant challenges and uncertainty, none more so than responding to, and recovering from, the Covid-19 pandemic. The unprecedented impact on public finances and the economy means the Scottish Government will need to manage further turbulence over the next few years. Strong financial management and good governance remain essential to ensure the Scottish Government can minimise the effects of any further disruption. Looking ahead, the Scottish Government should:

- be proactive in publishing comprehensive Covid-19 financial reporting information which clearly links budgets, funding announcements and spending levels. This will increase transparency in the Government's financial reporting in an area of significant parliamentary and public interest
- regularly assess and improve its estimates of fraud and error in Covid-19 grant schemes to assure themselves that controls to detect and prevent fraud and error are working in practice. They should also ensure regular public reporting to satisfy high levels of public interest in this area
- commit to its revised timetable over the production of public consolidated accounts. Public sector accounts will be important to help identify the potential risks to financial sustainability including the scale of assets and liabilities held by the devolved public sector in Scotland
- ensure greater accessibility and transparency of its performance reporting within the Consolidated Accounts, including better links between spending in portfolios and performance towards achieving national outcomes. This will help strengthen accountability and scrutiny of the Scottish Government's own performance
- keep its governance arrangements under review to ensure they remain fit for purpose, particularly as changes are made to its leadership and uncertainty remains as a result of the pandemic. In doing so, the Government should limit the use of interim appointments where possible to ensure greater stability and certainty within its leadership group.

The 2020/21 audit of the Scottish Government Consolidated Accounts

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