# Scottish National Investment Bank plc

**Report to the Audit Committee**

Consolidated financial statements for the period ended 31 March 2022

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Report date : 22 July 2022

Meeting date: 27 July 2022

# Introduction

**To the Audit Committee of Scottish National Investment Bank plc**

I am pleased to have the opportunity to meet with you on 27 July 2022 to discuss the results of our audit of the consolidated financial statements of Scottish National Investment Bank plc (the 'Company') and its subsidiaries (the 'Group'), as at and for the year ended 31 March 2022.

I am providing this report in advance of our meeting to enable you to consider our findings and hence enhance the quality of our discussions. This report should be read in conjunction with our audit plan and strategy report, presented on 1 December 2021. I shall be pleased to elaborate on the matters covered in this report when we meet.

Our audit is substantially complete other than those matters described at page 6. There have been no significant changes to our audit plan and strategy.

Subject to the Board's approval, I expect to be in a position to sign our audit opinion on the Group's financial statements on 2 August 2022, provided that the outstanding matters noted on page 6 of this report are satisfactorily resolved.

We expect to issue an unmodified Auditor's Report.

I draw your attention to the important notice on pages 3-4 of this report, which explains:

— the purpose of this report;

— limitations on work performed; and

— restrictions on distribution of this report.

Yours sincerely

Phil Merchant

Phil Merchant

22 July 2022

**How we have delivered audit quality**

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.

We consider risks to the quality of our audit in our engagement risk assessment and planning discussions.

We define 'audit quality' as being the outcome when audits are:

— **executed consistently**, in line with the requirements and intent of **applicable professional standards** within a strong **system of quality controls**; and

— All of our related activities are undertaken in an environment of the utmost level of **objectivity**, independence, **ethics** and **integrity**.



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# Important notice

This report is presented under the terms the terms of the Audit Scotland letter of appointment.

— The content of this report is based solely on the procedures necessary for our audit.

— Circulation of this report is restricted.

**Restrictions on distribution**

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries.

**Purpose of this report**

This Report has been prepared in connection with our audit of the consolidated financial statements of Scottish National Investment Bank plc (the 'Company') and its subsidiaries (the 'Group'), prepared in accordance with International Financial Reporting Standards ('IFRSs'), as at and for the period ended 31 March 2022.

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's Code of Audit Practice ('the Code'). The Code sets out SNIB's responsibilities in respect of:

— corporate governance;

— financial statements and related reports;

— standards of conduct for prevention and detection of fraud and error;

— financial position; and

— best value.

This report is for the benefit of Scottish National Investment Bank Plc ('SNIB') and is made available to Audit Scotland, the Auditor General and the Scottish Government, as a body (together 'the Beneficiaries'). This report has not been designed to be of benefit to anyone except the Beneficiaries. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we may have been aware that others might read this report. We have prepared this report for the benefit of the Beneficiaries alone.

This report summarises the key issues identified during our audit but does not repeat matters we have previously communicated to you.

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# Important notice (continued)

**Status of our audit**

Our audit is not yet complete and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status. Page 5 outlines the outstanding matters in relation to the audit. Our conclusions will be discussed with you before our audit report is signed.

**Limitations on work performed**

This Report is separate from our audit report and does not provide an additional opinion on the Group's financial statements, nor does it add to or extend or alter our duties and responsibilities as auditors reporting to the Company's members in accordance with the Companies Act.

We have not designed or performed procedures outside those required of us as auditors for the purpose of identifying or communicating any of the matters covered by this Report.

The matters reported are based on the knowledge gained as a result of being your auditors. We have not verified the accuracy or completeness of any such information other than in connection with and to the extent required for the purposes of our audit.

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# Our audit findings

**Significant audit risks** Pages 9-10

Those marked as key audit matters will be covered in our final audit report.

| Significant audit risks | Risk change | Our findings |
|---|---|---|
| Management override of controls | None | We have not detected evidence of management override of controls from the audit work performed to-date; we will provide an update to the Audit Committee in due course. |
| Valuation of investments (key audit matter) | None | Subject to finalisation of our procedures, we expect to confirm that we found the Company's valuation of unlisted investments to be acceptable. |
| **Key audit matters that are not deemed to be significant audit risks** | | |
| Recoverability of parent's debt due from group entities (key audit matter for the parent) | Yes | Subject to finalisation of our procedures, we expect to conclude that the balance is recoverable. |

**Materiality**

Materiality has been revised since the issue of the Audit Strategy to reflect the year end total asset position.

| Materiality | Actual | Planned |
|---|---|---|
| Materiality (Group) | £4,117k | £2,650k |
| Reporting threshold (Group) | £205k | £130k |
| Materiality (Parent) | £1,876k | £1,855k |
| Reporting threshold (Parent) | £94k | £90k |

**Key accounting judgements** Page 10

| | Judgement | Our findings |
|---|---|---|
| Valuation of unlisted investments | Neutral | We assessed the valuation of unlisted investments as reasonable following our review of the variable inputs to each valuation. We have not identified any indicators of potential management bias. |

**Control deficiencies** Page 10

| | |
|---|---|
| Significant control deficiencies | 0 |
| Other control deficiencies | 1 |
| Prior-year control deficiencies remediated | 0 |

**Audit misstatements**

At the date of this report we have not identified any corrected or uncorrected audit misstatements. We will provide further update on this matter at the meeting to be held on 27 July 2022.

**Directors' Remuneration**

We have assessed that a lower materiality is required to be applied to audited information within the Directors' Remuneration Report. These figures are expected to be immaterial based on the overall materiality set for the Financial Statements as a whole, yet in our professional judgement these balances would be of interest to the shareholders of the Group. We have lowered the overall materiality for the Financial Statements as a whole to £1k (PY: £1k) for Directors' remuneration based on our professional judgement.

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# Our audit findings (continued)

**Scope of consolidation**

We subjected all three components to full scope audits for Group purposes. The work on all components, including the audit of the parent company, was performed by the Group team. The scope of the audit work performed was fully substantive as we did not rely upon the Group's internal control over financial reporting, as we considered substantive testing to be more efficient.

**Outstanding matters**

The following items are outstanding as at the date of this Report:

- finalisation of audit work over the tax balances;
- finalisation of our review of the annual report:
  - review of the updated set of financial statements;
  - internal going concern consultation and review of relevant disclosures;
  - completion of disclosure checklists;
- receipt of the signed Management Representation Letter;
- completion of our post balance sheet events review up to the date of sign-off; and
- completion of internal review procedures including our audit file finalisation.

The matters above are based on the work performed up to the date of this report. We will provide a verbal update to the Audit Committee at the meeting on 27 July 2022.

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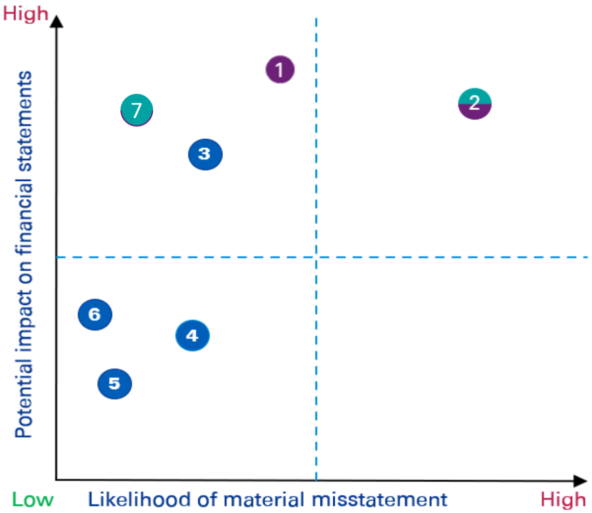
# Impact on the financial statements of the identified significant risks and other audit risks

**We discussed the significant risks which had the greatest impact on our audit with you when we were planning our audit.**

Our risk assessment draws upon our historic knowledge of the business, the industry and the wider economic environment in which Scottish National Investment Bank plc operates.

We also use our regular meetings with senior management to update our understanding and take input from local audit teams and internal audit reports.

There have been no significant changes to our risk assessment since our strategy document. However, we have added risk 7 which is a key audit matter for the parent company.




**Significant risks**

| | |
|---|---|
| 1 | Management override of controls |
| 2 | Valuation of unlisted investments (key audit matter) |

**Other Areas of Audit Focus**

| | |
|---|---|
| 3 | Going concern and the impact of COVID-19 |
| 4 | Expenses |
| 5 | Cash |
| 6 | Financial reporting |
| 7 | Recoverability of parent's debt due from group entities (key audit matter for the parent) |

**KEY**

- 1 Key audit matter
- 1 Key audit matter and significant financial statement audit risk
- 1 Significant financial statement audit risks
- 1 Other audit risks



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# Audit risks

**1** **Management override of controls[(a)]**

Fraud risk related to unpredictable way management override of controls may occur

## Significant audit risk

**The risk**

- Professional standards require us to communicate the fraud risk from management override of controls as significant.
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.
- We have not identified any specific additional risks of management override relating to this audit.

**Our response**

- Our audit methodology incorporates the risk of management override as a default significant risk.
- Assessed accounting estimates for biases by evaluating whether judgements and decisions in making accounting estimates, even if individually reasonable, indicate a possible bias.
- In line with our methodology, evaluated the design and implementation of controls over journal entries and post closing adjustments.
- We set high risk criteria for specific journals to test substantively. Any journals meeting these criteria, we tested each journal individually as part of our year-end audit process.
- Assessed the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates.
- Assessed the business rationale and the appropriateness of the accounting for any significant transactions that are outside the component's normal course of business, or are otherwise unusual.

**Our findings**

- We identified 12 journal entries and other adjustments meeting our high-risk criteria – our examination did not identify any inappropriate entries.
- We evaluated the accounting estimates involved in the valuation of unlisted investments, and did not identify any indicators of management bias. See page 10 for further discussion.
- We did not identify any significant unusual transactions.

*Note: (a) Significant risk that professional standards require us to assess in all cases.*

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# Audit risks (continued)

**2** **Valuation of unlisted investments (key audit matter)**

Risk that the carrying value of unlisted investments is materially misstated

## Significant risk and key audit matter

**The risk**

- The Group's portfolio of unlisted investments makes up 92% of the total assets (based on the draft financial statements as at 31 March 2022).Unlisted investments are measured at fair value, which is established in accordance with the International Private Equity and Venture Capital Valuation Guidelines by using measurements of value such as prices of recent orderly transactions, earnings multiples and net assets. There is a significant risk over the judgement and estimates inherent in the valuation and therefore one of the key areas that our audit focuses on.
- The effect of these matters is that, as part of our risk assessment, we determined that the valuation of unlisted investments has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole.

## Our response

- **Methodology choice**: In the context of observed industry best practice and the provisions of the International Private Equity and Venture Capital Valuation Guidelines, we challenged the appropriateness of the valuation basis selected.
- **Our valuations experience**: We challenged management on key judgements affecting investee company valuations, such as the choice of benchmark for earnings multiples. We compared key underlying financial data inputs to external sources, investee company audited accounts and management information as applicable. We challenged the assumptions around sustainability of revenue or earnings based on the plans of the investee companies and whether these are achievable. Our work included consideration of events which occur subsequent to the period end up until the date of our audit report.
- **Comparing valuations**: Where a recent transaction is used to value a holding, we obtained an understanding of the circumstances surrounding the transaction and whether it is considered to be on an arm's length basis and suitable as an input into a valuation.
- **Our Corporate Finance expertise**: Based on our assessment of the portfolio we concluded that involvement from our corporate finance specialists was not required.
- **Assessing transparency**: We considered the appropriateness, in accordance with relevant accounting standards, of the disclosures in respect of unlisted investments and the effect of changing one or more inputs to reasonably possible alternative valuation assumptions.

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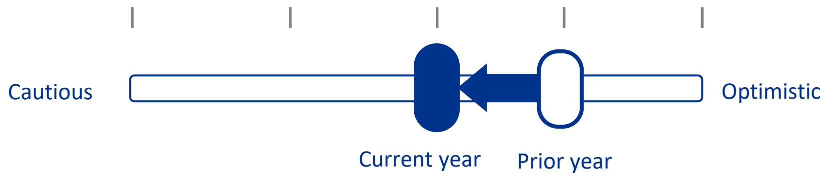
# Audit risks (continued)

**2** **Valuation of unlisted investments (key audit matter)**

Risk that the carrying value of unlisted investments is materially misstated

**Our findings**

- We have concluded based on our work to date and discussion with the Audit Committee, that the valuations on the whole are acceptable. We have not raised any proposed judgemental audit differences, meaning we believe that each individual valuation to be within an acceptable range.
- We consider the valuations, on the whole, to be balanced (2021: towards the higher end of an acceptable range).
- Our views on management judgements with respect to accounting estimates are based solely on the work performed in the context of our audit of the financial statements as a whole. We express no assurance on individual financial statement captions.
- We have considered the controls in place over the unlisted valuation process and substantively tested the year end valuations through a combination of independent verification and challenge over key judgements and assumptions.
- The FRC expects management to disclose sufficient information to enable investors to understand material sources of estimation uncertainty. Disclosures should include the range of outcomes or sensitivities for those that have a significant risk of requiring material adjustment in the next year. Our work on disclosures remains ongoing and we expect to conclude that disclosures made are proportionate.




**Control deficiency**

- We note that the Valuation Committee review the valuation of unlisted investments and provide challenge on the assumptions and judgements which underpin the valuation of those investments. However, given the nature of unlisted investments, the unique characteristics of each, no control can operate to a sufficiently precise degree that would allow us to reduce our level of substantive audit procedures.
- We therefore are required to assess the design and implementation of this review control as being ineffective, as directed by auditing standards and our audit methodology as we are not able to rely on this control to mitigate the associated significant audit risk. This has had no impact on our audit approach.
- This is a common finding, in particular in relation to unlisted investments, where the threshold to meet formal criteria for an effective management review control are too high and implementation of such control may not be efficient, sustainable or practical. Management often choose to rely primarily on competencies of those performing the controls and wider control environment, rather than on a formalised review control over investments valuations.

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# Audit risks (continued)

**3** **Going concern and the impact of COVID-19**

Risk relating to disclosures related to going concern including the judgement of whether there is material uncertainty

## Other areas of audit focus

**The risk**

- Management's assessment of the Group's ability to continue as a going concern involves consideration of all factors affecting the Group, including the impact of COVID-19.
- There is a risk that management's assessment of the Group's ability to continue as a going concern does not appropriately consider the impact of the COVID-19 pandemic, including plausible but severe downside scenarios on the income of the Company and carrying value of assets.
- The risk that disclosures in the financial statement and the annual report are not adequate with regard to the effect of COVID-19 risks on the Company's financial position, performance, business model and strategy.

**Our response and findings**

- We evaluated how management's risk assessment process identified business risks relating to events and conditions that may cast significant doubt on the ability to continue as a going concern.
- We evaluate any models management uses in its assessment and evaluated how the information system captures events and conditions that may cast significant doubt on ability to continue as a going concern.
- We evaluated whether management's assessment had failed to identify events or conditions that may cast significant doubt on going concern and whether the method used by management is appropriate.
- We evaluated management's assessment including the plausible but severe downside scenarios particularly whether those downside scenarios reflect plausible impacts of COVID-19 on the business.
- We evaluated whether sufficient and appropriate audit evidence had been obtained to conclude whether a material uncertainty exists and the appropriateness of management's use of the going concern basis of accounting.
- We evaluated whether there was adequate support for the assumptions underlying management's assessment, including the support provided by Scottish Government, whether they are realistic and achievable and consistent with the external and/or internal environment and other matters identified in the audit.

We consider director's assessment of going concern appropriate and have not identified material uncertainties in relation to going concern. Our work over related disclosures in the annual report, including an internal consultation, remains ongoing. We will provide an update to the Audit Committee on 27 July 2022.



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# Audit risks (continued)

**4** **Expenses**

Expenses may be recorded incorrectly leading to material misstatement

## Other areas of audit focus

**The risk**

— Expenses could be recorded in the incorrect year (cut-off), at the incorrect amount (accuracy) or not recorded at all (completeness).

— We expect that as the Group builds up their investment portfolio expenses will become immaterial and will be removed from other areas of audit focus.

**Our response and findings**

— We traced a sample of administrative expenses and staff costs transactions back to the supporting documentation and to bank statements.

— We recalculated the accounting charge for the long-term incentive plan (‘LTIP’) awarded in the year after verifying the inputs to the calculation against source documentation.

— We reviewed a sample of payments made post year end to identify expenses that may have been omitted in the year.

— We concluded that staff costs and other administrative expenses are free from material misstatement.

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# Audit risks (continued)

**5** **Cash**

Cash balances may be materially misstated

## Other areas of audit focus

**The risk**

Cash balances, as reported by management, may not be complete or accurate, or the company may not have the rights to ownership of the bank accounts.

**Our response and findings**

- All year-end cash balances recorded in the financial statements have been agreed to third-party confirmations received independently.
- We have tested the design and implementation and operating effectiveness of controls over bank reconciliations.
- We concluded that cash balances are free from material misstatement.

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# Audit risks (continued)

**6** **Financial reporting**

Risk related to non compliance with the various regulatory and disclosure requirements

## Other audit risk

**The risk**

The Group must ensure the financial statements have been properly prepared and comply in all material respects with the disclosure requirements of:

- IFRS, where appropriate, as interpreted and adapted by the 2020/21 Government Financial Reporting Manual (the 2020/21 FReM);
- the Companies Act 2006; and
- directions made under the Public Finance and Accountability (Scotland) Act 2000 by the Scottish Ministers.

The directors have decided to prepare voluntarily a Corporate Governance Statement as if the Company were required to comply with the Listing Rules and the Disclosure Guidance and Transparency Rules of the Financial Conduct Authority in relation to those matters.

**Our response and findings**

We are in the process of completing the following procedures over the financial statements:

- Over the course of our audit, we will evaluate the appropriateness of the Group's accounting policies, accounting estimates and financial statement disclosures including those over key estimates and judgements.
- We will also read the Viability Statement, including consideration of the robust assessment of the principal risks threatening the business, how these have been mitigated and the period over which they have been considered that the Group can reasonably expect to continue in operation.
- We will review the s172 statement and assess it for compliance with corporate governance requirements.
- We will consider the disclosures surrounding COVID-19 in the context of the situation at year-end.
- We will consider the appropriateness of any ESG disclosures in the annual report, as well as the wider impact of climate-related matters on any account balances and disclosures.
- We will evaluate the financial statements using our tailored disclosure checklists, covering the requirements of the Companies Act 2006, IFRS, the UK Corporate Governance Code and the FCA Disclosure, Guidance and Transparency Rules.

No significant disclosure omissions or discrepancies have been identified to-date.  We have provided comments on draft financial statements to management.



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# Audit risks (continued)

**7** **Recoverability of parent's debt due from group entities (key audit matter for the parent)**

Risk related to recoverability of intra-Group loan from the parent to subsidiary

## Key audit matter

**The risk**

The carrying amount of the intra-group debtor balance represents 99% (2021: 80%) of the Company's total assets. The recoverability is not at a high risk of significant misstatement or subject to significant judgement. However, due to its materiality in the context of the financial statement, this is considered to be an area that will have the greatest effect on our overall parent company audit.

Note: This risk is applicable to the parent only.

**Our response and findings**

- **Test of detail**: We have assessed 100% of debtors to identify with reference to the subsidiary company's draft balance sheet, whether it has a positive net asset value and therefore coverage of the debt owed, as well as assessing whether the debtor company has historically been profit-making.
- **Assessing the subsidiary company audit**: We will assess the work performed on the subsidiary company audit, and considering the results of that work, on those net assets, including assessing the liquidity of the assets and therefore the ability of the subsidiary to fund the repayment of the receivable.

No significant issues have been identified to date. We expect to find the intra-group debtor balance to be acceptable.

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# Wider scope reporting

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's Code of Audit Practice which required us to report on the company's arrangements in the context of four dimensions:

— financial sustainability;

— financial management;

— governance and transparency, and

— value for money.

Our findings are summarised on pages 16-19. In our assessment we took into account that the Bank is in an early stage of their operations; with certain processes and controls still evolving.

# 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.

**Work performed**

— Interviews with the executive team.

— Review of going concern assessment prepared by the directors (ref to page 11).

— Review of current funding arrangements with the Scottish Government.

**Findings**

— The Bank is at an early stage of its development and remains reliant on the Scottish Government.

— It is intended that the Bank will become financially self-sustaining in the medium term. The Bank will achieve this by generating income from the investments it makes and by closely controlling its costs and expenses.

— The Bank has made some important steps in the period in establishing their financial sustainability, in particular continuing to grow the investment portfolio and initiating the process for obtaining FCA permissions.

— Establishing and maintaining investments pipeline is crucial for achieving sustainability and will continue to be assessed in future periods. The Bank has diversified its investment portfolio, most notably by making debt investments (which generate regular income) as well as equity.

**Conclusion**

— We have not identified a significant risk in relation to Financial sustainability.

— Based on the work performed, we consider the arrangements in place to be effective and appropriate for the current early stage of the Bank's operations.

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# Wider scope reporting - financial management

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

**Work performed**

— Review of relevant policies.

— Interviews with the executive team.

— Walkthroughs of the finance processes relevant to reporting.

— Audit work over annual reporting.

**Findings**

SNIB adopts a 'Financial Management policy' designed to ensure that the Bank operates with robust financial systems, processes, procedures and controls; and that the Bank complies with all relevant requirements for its financial records and reporting and a 'Financial Reporting policy'.

The key processes in place include:

— financial planning, budgeting and forecasting;

— general ledger management and internal controls;

— treasury and cash management; and

— reporting:

- – annual reporting;
- – monthly and quarterly reporting; and
- – financial reporting to Scottish Government.

**Conclusions**

— We have not identified a significant risk in relation to Financial management dimension.

— Based on the work performed, we consider the arrangements in place to be effective and appropriate for the current early stage of the Bank's operations.

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# Wider scope reporting - 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.

**Work performed**

— Reviewing the organisational structure, reporting lines and level of scrutiny within SNIB.

— Review of board and committee minutes.

— Review of relevant policies.

— Interviews with the executive team.

— Reading the annual governance statement.

— Consideration of scrutiny over key risks.

**Findings**

SNIB complies with the UK Corporate Governance Code in so far as it is relevant and applicable.

***Section 172 statement***

SNIB has also considered its duties under Section 172 of the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 as well as the 'Guidance on the Strategic Report' issued by the Financial Reporting Council and the UK Corporate Governance Code 2016.

***Gender pay gap***

Gender pay gap legislation applies for the UK private sector companies and requires pay comparisons be made between the contractual pay of men and women including base salary, paid leave, pay allowances, shift pay and on-call and standby payments. SNIB has adopted the legislation for transparency and therefore disclose a gender pay gap in line with the private sector calculation but using the two-year frequency of Public Sector Equality Duties ('PSED') reporting.

***Risk assessment***

The bank has a risk management framework which summarises key processes and methodologies applied to identify, evaluate, mitigate and monitor and report risks.

**Conclusions**

— We have not identified a significant risk in relation to Governance and Transparency dimension.

— Based on the work performed, we consider the arrangements in place to be effective and appropriate for the current early stage of the Bank's operations.



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# Wider scope reporting - value for money

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

**Work performed**

— Review of relevant policies.

— Interviews with the executive team.

— Walkthroughs of the relevant processes (including appropriate segregation of duties).

— Audit work over expenses.

**Findings**

SNIB are subject to Public Procurement law including; Procurement Reform (Scotland) Act 2014 and Procurement Regulations (Scotland) 2015 and 2016 as well as Requirements of the Scottish Public Finance Manual.

SNIB adopted a 'Procurement and Outsourcing Policy' which summarises relevant processes design to ensure compliance with the VfM principle.

The key controls and processes in place are:

— **Separation of duties**: In accordance with the Scottish Public Finance Manual, the Bank will ensure separation of duties:
  - in procurement and the award of contracts: Between financial / budgetary authority and procurement authority; and
  - in the purchasing cycle: Between staff who place orders, those who receive goods or services, and those who authorise payment.

— **Supplier due diligence and supplier monitoring**: Undertaking an assessment of the risks associated with the proposed supplier, service/goods to be provided and the use of these services by the Bank. Thereafter reviewing and updating supplier due diligence on an annual basis.

— **Effective competition and value for money**: Engaging procurement support early, avoiding distressed purchases, and ensuring a strong link between Procurement and Finance on the management of supplier costs for budgeting purposes.

— **Appropriate contractual arrangements**: Including agreements review by Governance, Legal, Risk and Compliance.

**Conclusions**

— We have not identified a significant risk in relation to Value for money dimension.

— Based on the work performed, we consider the arrangements in place to be effective and appropriate for the current early stage of the Bank's operations.


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# Appendix

**Contents**

# Confirmation of independence

**We confirm that, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and that the objectivity of the engagement partner and audit staff is not impaired.**

To the Audit Committee

**Assessment of our objectivity and independence as auditor of Scottish National Investment Bank Plc and its subsidiaries ('the Group')**

Professional ethical standards require us to provide to you at the conclusion stage of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

— general procedures to safeguard independence and objectivity;

— independence and objectivity considerations relating to the provision of non-audit services; and

— independence and objectivity considerations relating to other matters.

**General procedures to safeguard independence and objectivity**

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

— instilling professional values;

— communications;

— internal accountability;

— risk management;

— independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

**Independence and objectivity considerations relating to the provision of non-audit services**

We have not provided any non-audit services to the Group.

**Application of the FRC Ethical Standard 2019**

That standard became effective for the first year commencing on or after 15 March 2020, except for the restrictions on non-audit and additional services that became effective immediately at that date, subject to grandfathering provisions.

We confirm that as at date of this document we are not providing any non-audit or additional services that required to be grandfathered.

**Confirmation of audit independence**

We confirm that as of the date of this letter, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Partner and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee of the Group and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

Yours faithfully

KPMG LLP

KPMG LLP

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# Required communications with the Audit Committee

| Type | | Response |
|---|---|---|
| **Our draft management representation letter** | OK | We have not requested any specific representations in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2022. |
| **Adjusted audit differences** | OK | There were no adjusted audit differences. |
| **Unadjusted audit differences** | OK | There were no unadjusted audit differences. |
| **Related parties** | | Queries surrounding management's process for identifying and tracking related parties remain outstanding as at the date of this report. |
| **Other matters warranting attention by the Audit Committee** | OK | There were no matters to report arising from the audit that, in our professional judgement, are significant to the oversight of the financial reporting process. |
| **Control deficiencies** | OK | We communicated to management in writing all deficiencies in internal control over financial reporting of a lesser magnitude than significant deficiencies identified during the audit that had not previously been communicated in writing. |
| **Actual or suspected fraud, noncompliance with laws or regulations or illegal acts** | OK | No actual or suspected fraud involving group or component management, employees with significant roles in group-wide internal control, or where fraud results in a material misstatement in the financial statements identified during the audit. |

| Type | | Response |
|---|---|---|
| **Significant difficulties** | OK | No significant difficulties were encountered during the audit. |
| **Modifications to auditor's report** | OK | None. |
| **Disagreements with management or scope limitations** | OK | The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit. |
| **Other information** | OK | No material inconsistencies were identified related to other information in the annual report, Strategic and Directors' reports.<br>The Strategic report is fair, balanced and comprehensive, and complies with the law. |
| **Breaches of independence** | OK | No matters to report. The engagement team and the firm have complied with relevant ethical requirements regarding independence. |
| **Accounting practices** | OK | Over the course of our audit, we have evaluated the appropriateness of the Group's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate. |
| **Significant matters discussed or subject to correspondence with management** | OK | No significant matters arising from the audit required discussion or specific correspondence to correspondence with management. |

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# Compliance with the UK Corporate Governance Code

**We have communicated the information we believe to be relevant to the board and the audit committee, in the context of fulfilling their responsibilities under the Corporate Governance Code provisions.**

**Our auditor's report sets out our responsibilities in relation to reporting on certain provisions of the UK Corporate Governance Code information relevant to understanding the rationale and evidence to support our professional judgement exercised in the course of the audit and in reaching an opinion on the financial statements. Our comments on additional areas are below.**

**Emerging and principal risks**

— We believe that the principal and emerging risks facing the company and identified by management in the Annual Report are a robust assessment of the Company. The disclosure is proportionate to the early stage of the Bank's operations but we expect these to be expanded in future years.

**Significant accounting policies**

— We consider that the accounting policies applied are appropriate in the circumstances of Scottish National Investment Bank plc. We have also reviewed the application of these policies and are not aware of any significant areas where the policies have not been properly applied.

**Corporate Governance Disclosures**

— We are satisfied that the directors' statement of compliance with the provisions of the UK Corporate Governance Code (to the extent that we are required under the ISAs to report on that statement) and the directors' statements regarding going concern and longer-term viability are consistent with knowledge obtained during our audit.

**Significant accounting estimates**

— We are satisfied that management's valuations of unlisted investments are materially appropriate, and there are no indicators of associated management bias. Refer to Page 10 for further details.

**Risk management and internal control**

— We are satisfied that there are no significant deficiencies in internal control based on the audit work performed so far.


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# FRC's areas of focus

The areas of focus from the FRC's Annual Review of Corporate Reporting 2020/21, annual letter to CEOs, CFOs and audit committee chairs along with the five thematic reviews issued in 2021 should be considered for reporting in the current financial period. The reports identify where the FRC believes companies should be improving their reporting. Below is a high level summary of the key topics. We encourage management and those charged with governance to read further on those areas which are significant to the [entity]/[group].

| | |
|---|---|
| **Judgements and Estimates** | In the current climate it is particularly important for Companies to provide as much context as possible for the assumptions and predictions underlying the amounts recognised in the financial statements, including potential sensitivities or ranges of possible outcomes.<br>Companies should disclose the carrying amounts impacted by estimation uncertainty. Disclosures of key assumptions and sensitivities could be improved. Preparers are encouraged to clearly distinguish between sources of estimation uncertainty with a significant risk of a material adjustment in the following year and other, perhaps longer-term, uncertainties.<br>Significant accounting judgements should be clearly explained along with factors considered. |
| **Revenue** | Having raised a considerable number of queries in relation to revenue recognition policies and related disclosure, the FRC strongly encourage preparers to read their thematic report which includes tips and examples of good and inadequate disclosure.<br>Companies should disclose significant judgements made in accounting for revenue. This could include judgements in relation to performance obligations, transaction price and amounts allocated to performance obligations. Disclosures should clearly identify the methods used to estimate any variable consideration, including the application of the constraint. The FRC notes that disclosure of a significant risk of a downward adjustment to revenue suggests that the variable constraint may not have been applied appropriately. |
| **Statement of Cash Flows** | Companies need robust reviews of the cash flow statement to ensure consistency with other parts of the annual report and to ensure preparation in line with the accounting standard.<br>Errors continue to be identified, including inappropriate classification of cash flows and inappropriate netting. The FRC also challenges companies on the composition of cash equivalents and on incomplete or incorrect related disclosures.<br>Companies are reminded that even in the limited cases where borrowings can be included as a component of cash and cash equivalents in the cash flow statement, the IAS 32 'Financial Instruments: Presentation' criteria need to be applied to determine whether they can be presented on a net basis in the balance sheet. |
| **Alternative Performance Measures (APMs)** | APMs should not be given undue-prominence. Preparers should avoid statements appearing to provide APMs with more authority than IFRS measures and are reminded that meaningful commentary on the IFRS figures is required.<br>APMs, including ratios, should be appropriately labelled and reconciled to the most directly reconcilable financial statement line item. It should be clear how reconciling items are determined and companies should explain clearly why amounts are excluded from adjusted measures. Adjusting items should include gains as well as losses, where relevant. |

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# FRC's areas of focus (continued)

| | |
|---|---|
| **Impairment of Assets**<br>- FRC Thematic Review<br>- 2020 Review of Climate Related Considerations | Impairment remains an area of focus in light of continued COVID-19 uncertainty and the risks related to climate change. Companies need to consider the impact of climate change on impairment reviews, especially in industries where investors may reasonably expect climate changes to significantly affect future expected cash flows.<br>When uncertainties indicate possible impairment, disclosures should indicate whether impairment tests have been performed and explain and quantify the key assumptions (including when parent company investments in subsidiaries are assessed, for example when the net assets of the parent company exceed market capitalisation).<br>Preparers are also encouraged to provide clear disclosures the effect of reasonably possible changes to clear assumptions. |
| **Financial Instruments**<br>- FRC's Thematic Review<br>- Case Study | Factoring and reverse factoring arrangements require transparent disclosures, covering the nature of any material arrangements, the liquidity implications and the relevant amounts.<br>If significant judgement is required to determine the appropriate accounting or measurement basis, then it is expected that the basis of this judgement will be explained in the disclosure.<br>Non-banking preparers should ensure that they properly apply the credit risk-related disclosures such as the inputs, assumptions and estimation techniques used to measure impairment, amounts by credit risk rating grades, information about credit risk management practices and the concentration of credit risk, where material.<br>The FRC expect companies to provide information about their banking covenants unless the likelihood of any breach is considered remote. |
| **Strategic Report** | The strategic report should provide a fair, balanced and comprehensive analysis of the development and performance of the business in the financial year and of its position at the end of the year. In particular companies are encouraged to include discussion of relevant significant matters and performance against key strategic objectives e.g. discussion of cash flow performance where cash generation is a key strategic action. |
| **Provisions and contingencies** | Provisions and contingencies should be clearly explained including the nature of the exposure, the timeframe and the basis for determining the amount. Any significant judgements and relevant assumptions should be disclosed clearly.<br>There should be consistency between information provided in the annual report and accounts.<br>If material provisions are dependent on the future performance of a business expected to be heavily impacted by climate change, this should be disclosed and detail provided on how climate change had been taken into account in the estimate. |
| **Leases** | Lessees and lessors are required to disclose information that gives a basis for users to assess the effect of leases on financial position, financial performance and cash flows. This could include information about variable payment features, for example. Judgements should be disclosed.<br>Entity-specific accounting policies should be disclosed for material transactions. |


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# FRC's areas of focus (continued)

| | |
|---|---|
| **Income Taxes** | Where a loss-making entity is recognising deferred tax assets ('DTAs') and utilisation depends on future profits, entities are required to disclose the amount of the DTA, the nature of the evidence considered, any critical judgements used in the recognition of the DTAs and the key sources of estimation uncertainty. |

**2021/22 priorities for FRC review:**

- Impact of COVID-19
- Climate Change (FRC Thematic Review 2020 and 2021)

In addition to the 'top ten' topics summarised above, the FRC have indicated that routine monitoring for the 2021/22 cycle will include a focus on:

— judgement and uncertainty in the face of continuing economic and social impact of Covid-19; and

— climate-related risks and new disclosures.

Disclosure on judgements and assumptions about the future will remain important to users of reports, particularly when considering matters such as going concern and liquidity. Therefore as part of their routine 2021/22 routines, the FRC will continue to consider whether companies:

— explain the significant judgements and estimates made;

— provide meaningful sensitivity analysis or details of a range of possible outcomes;

— describe any significant judgements made in determining whether there is a material uncertainty about their ability to continue as a going concern; and

— ensure that assumptions used in the going concern assessment are compatible with those used elsewhere.

For accounting periods beginning on or after 1 January 2021, premium listed companies will be required to disclose their compliance with the Taskforce for Climate-related Financial Disclosures ('TCFD') recommendations on a comply-or-explain basis. To achieve this they must include a statement in their annual financial report setting out:

— whether they have made disclosures consistent with the recommendations of the TCFD;

— where the disclosures are instead in a document outside of the annual financial report, an explanation of why and a reference to where they can be found; and

— where disclosures are not made, an explanation of why, and a description of any steps taken or planned to be able to make consistent disclosures in the future, including time frames.

Furthermore, proposals for mandatory climate-related financial disclosure requirements for PLCs, large private companies and Limited Liability Partnerships have been consulted on. It is proposed that regulations will come into force for periods starting on or after 6 April 2022, for entities meeting the following requirements:

— all UK companies that are currently required to produce a non-financial information statement;

— UK registered companies admitted to AIM with more than 500 employees; and

— other meeting companies meeting the definition of 'large'.

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# Newly effective standards

| | Expected impact | | | | Effective for years beginning on or after | | |
|---|---|---|---|---|---|---|---|
| **Standards** | **High** | **Moderate** | **Low** | **None** | **1 January 2021** | **1 January 2022** | **1 January 2023** |
| *Interest Rate Benchmark Reform Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)* | | | ● | | ✓ | | |
| *Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37)* | | | | ○ | | ✓ | |
| *Annual Improvements to IFRS Standards 2018-2020* | | | ● | | | ✓ | |
| *Property, Plant and Equipment: Proceeds Before Intended Use (Amendments to IAS 16)* | | | ● | | | ✓ | |
| *Reference to the Conceptual Framework (Amendments to IFRS 3)* | | | | ○ | | ✓ | |
| *Classification of Liabilities as Current or Non-current (Amendments to IAS 1)* | | | ● | | | | ✓ |
| *IFRS 17 Insurance contracts* | | | | ○ | | | ✓ |
| *Accounting Policies, Changes in Accounting Estimates and Errors: definition (Amendments to IAS 8)* | | | ● | | | | ✓ |
| *Amendments to IAS 1 Presentation of Financial Statements and IFRS Practice Statement 2 Making Materiality Judgements* | | | ● | | | | ✓ |
| *Deferred Tax Related to Assets and Liabilities Arising from a Single Transaction – Amendments to IAS 12 Income Taxes* | | | ● | | | | ✓ |

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# KPMG's Audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.

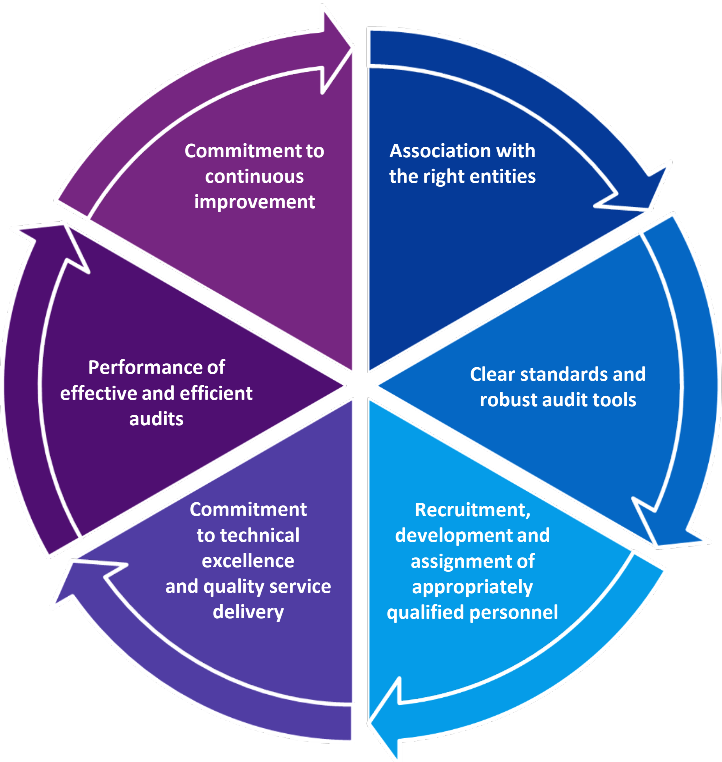
To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework.

Responsibility for quality starts at the top through our governance structures as the UK Board is supported by the Audit Oversight Committee, and accountability is reinforced through the complete chain of command in all our teams.

- Comprehensive effective monitoring processes
- Significant investment in technology to achieve consistency and enhance audits
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching, including the second line of defence model
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Insightful, open and honest two way communications

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights




- Select clients within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- KPMG Clara incorporating monitoring capabilities at engagement level
- Independence policies

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members and specialists

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