



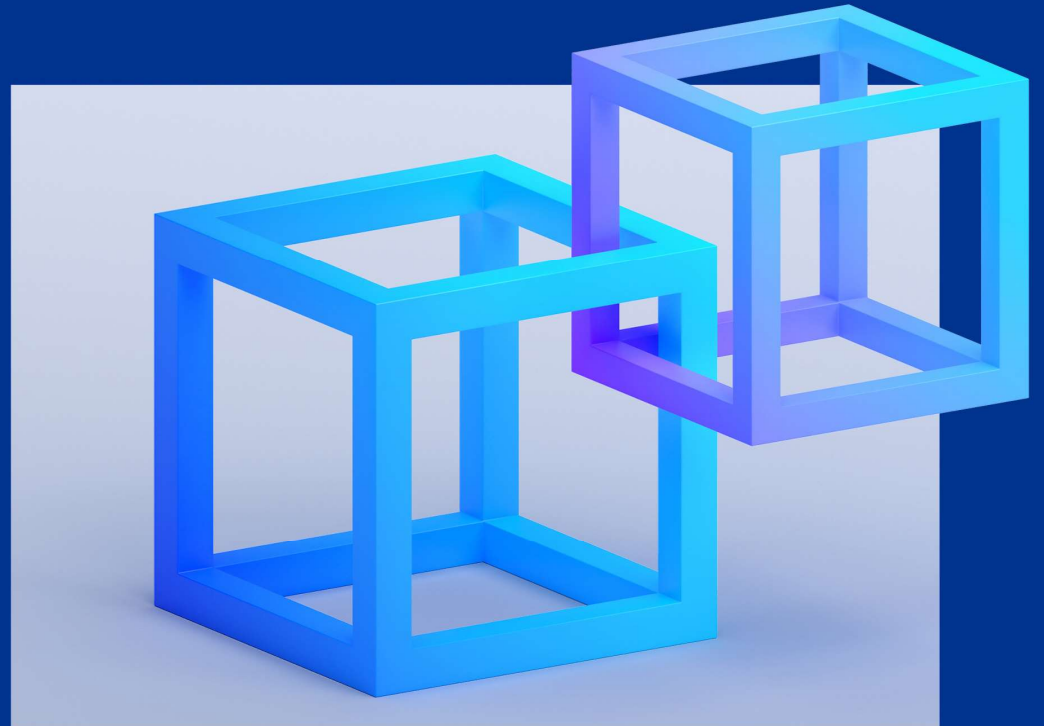
Scottish National Investment Bank plc

Report to the Audit Committee

**Consolidated financial statements for the year ended 31
March 2023**

Report Date: 3 July 2023

Meeting Date: 4 July 2023



Introduction

To the Audit Committee of Scottish National Investment Bank plc

Following the completion of our audit we are pleased to provide you with an updated view of our findings in respect 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 2023.

We are 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 16 November 2022 and our Audit Highlights Memorandum presented to the Audit Committee on 21 June 2023.

The engagement team

Our audit is substantially complete other than those matters described at page 5. There have been no significant changes to our audit plan and strategy.

Subject to the Board's approval, we expect to be in a position to sign our audit opinion on 4 July 2023, subject to the Board's approval of the financial statements and auditor's representation letter, provided that the outstanding matters noted on page 5 of this report are satisfactorily resolved.

We expect to issue an unmodified Auditor's Report.

We draw your attention to the important notice on page 3 of this report, which explains:

- The purpose of this report
- Limitations on work performed
- Restrictions on distribution of this report

Yours sincerely



Philip Merchant

3 July 2023

How we deliver 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 of the Audit Scotland letter of appointment.

Circulation of this report is restricted.

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

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 year ended 31 March 2023.

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

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.

Nothing in this report constitutes an opinion on a valuation or legal advice.

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

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.

Status of our audit

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

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.



Our audit findings



Significant audit risks Page 7

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.
Valuation of unlisted investments (key audit matter)	None	We found the Group's valuation of unquoted investments to be acceptable.

Key audit matters that are not deemed to be significant audit risks	Risk change	Our findings
Recoverability of parent's debt due from group entities (key audit matter for the parent)	None	We found the conclusion that there is no impairment of the intra-group debtor balance to be acceptable.

Key accounting estimates Page 11

Valuation of unlisted investments	Cautious	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.
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Corrected / Uncorrected Audit Misstatements

We have not identified any corrected or uncorrected audit misstatements.

Misstatements in respect of Disclosures

We have not identified any corrected or uncorrected misstatements in respect of disclosures.

Number of Control deficiencies Page 11 12

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

Materiality Financial statements Actual £ 000 Planning £ 000

Total assets		
Materiality (Group)	7,560	5,850
Reporting threshold (Group)	378	292
Materiality (Parent)	3,400	2,633
Reporting threshold (Parent)	170	132

Materiality has been revised because the selected benchmark of total assets as at 31 March 2023 has increased since planning.



Outstanding matters



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

- Completion of internal file review in accordance with internal mandatory review requirements;
- Final assessment of Annual Report and Financial Statements and subsequent finalisation of our disclosure checklists, including any changes following the board's review of annual report;
- Receipt of signed financial statement and management representation letter;
- Completion of post balance sheet events review up to date of sign off.

The matters above are based on the work performed up to the date of this report.

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.

See the following slides for the cross-referenced risks identified on this slide.

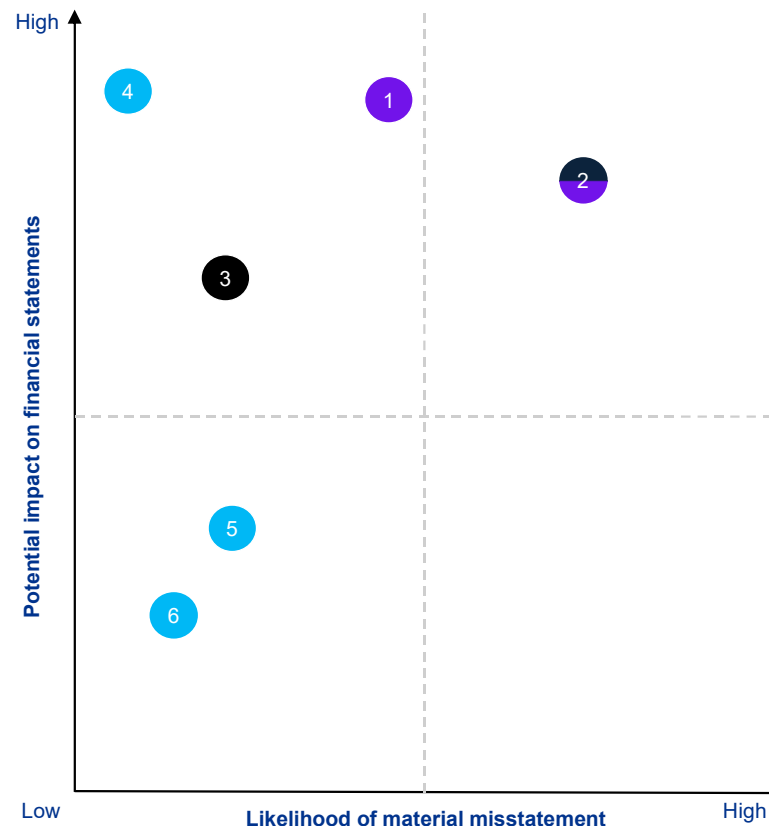
Significant risks

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

Other audit risks

3. Recoverability of parent's debt due from group entities (key audit matter for the parent)
4. Going concern
5. Expenses
6. Cash

- Key:**
- # Key audit matter for parent company and/or group
 - # Other audit risk
 - # Key audit matter and significant financial statement audit risk
 - # Significant financial statement audit risks



Significant risks

Audit risks



1 Management override of controls

Fraud risk related to unpredictable way override of controls may occur



Significant risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant
- Management of any company 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 response

- Our audit methodology incorporates the risk of management override as a default significant risk.
- In line with our methodology, we have 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 to the methods and underlying assumptions used to prepare accounting estimates.
- Assessed the appropriateness of the accounting for significant transactions that are outside the Group's normal course of business, or are otherwise unusual as applicable.

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

Audit risks (cont.)



1 Management override of controls^(a)

Fraud risk related to unpredictable way override of controls may occur



Significant risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant
- Management of any company 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 findings

- Through the high-risk criteria analysis, we identified that there were some journal entries processed in the period where the ledger system recorded the same individual initiating and approving the entry.
- As a result, we identified a mitigating control and tested the design and implementation and operating effectiveness of the control. The control was determined to be effective but some observations were provided to management.
- We identified 14 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 recoverability of deferred tax assets and did not identify any indicators of management bias. See page 11 for further discussion.
- We did not identify any significant unusual transactions.

Audit risks (cont.)



2 Valuation of unlisted investments (key audit matter)

Risk that the carrying value of unlisted investments is materially misstated



Significant audit risk and key audit matter

- As at 31 March 2023, 96% (2022: 92%) of the Group's total assets (by value) are investments where no quoted market price is available. 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, milestone analysis, discounted cash flows, earnings multiples and valuing fund interests by reference to their reported net asset value.
- There is a significant risk over the judgements and estimates inherent in the valuation and therefore this is one of the key areas that our audit has focused on.
- The effect of these matters is that, as part of our risk assessment, we determined that certain unlisted investments have 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 the directors on key judgements affecting investee company valuations, such as the choice of benchmark for earnings multiples, progress against milestones, credit risk assessments and use of appropriate discount rates. 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 forecasts of the investee companies and whether these are achievable and we obtained understanding of milestones completed during the year. Our work included consideration of events which occur subsequent to the period end up until the date our audit report.
- **Comparing valuations:** Where a recent transaction has been used to value a holding, we obtained an understanding of the circumstances surrounding the transaction and vouched the price to supporting documentation. We also assessed whether subsequent changes or events such as market or entity specific factors would imply a change in value.
- **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.

Key:
□ Prior year ■ Current year



Audit risks (cont.)



2 Valuation of unlisted investments (key audit matter)

Risk that the carrying value of unlisted investments is materially misstated



Significant audit risk and key audit matter

- The factors considered in assessing which unlisted investments were subject to significant risk included the quantum of the individual investment, performance of the investment, nature of the asset held as well as the estimation uncertainty of the methodology and inputs used.



Our findings

- Based on our work and challenge of management, we have concluded that the valuations of investments are reasonable. Across the portfolio we see a mix of investments where some are slightly optimistic and some cautious but at a portfolio level are satisfied that the assets are reasonably valued towards the slightly cautious end of an acceptable range (2022: Balanced).
- 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. Please refer to slide 16 for control deficiency identified.
- 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.

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 and the subjective elements involved in determining their fair value, it is unlikely that Committee level control can operate to a sufficiently precise degree that would allow us to reduce our level of substantive audit procedures.

Key:
○ Prior year ● Current year



Audit risks (cont.)



2 Valuation of unlisted investments (key audit matter)

Risk that the carrying value of unlisted investments is materially misstated



**Significant
audit risk
and key
audit matter**

- The factors considered in assessing which unlisted investments were subject to significant risk included the quantum of the individual investment, performance of the investment, nature of the asset held as well as the estimation uncertainty of the methodology and inputs used.



**Our
findings**

Control deficiency (continued)

As the unlisted investments represent a key audit matter and significant risk, we are required to assess the design and implementation of this control, which as it is a Committee level review control is considered to be ineffective, for audit reliance purposes. We reach this conclusion as the control does not operate to a level of precision that could prevent material misstatement, given the judgement involved in the valuation of unlisted investments. 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 is 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.

Key:
□ Prior year ■ Current year



Other audit risks

Audit risks (cont.)



3 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



Other audit risk – key audit matter for the parent

The carrying amount of the intragroup debtor balance represents 99% (2022: 99%) 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 their 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



Our findings

- **Test of detail:** We have assessed 100% of debtors to identify with reference to the subsidiary Company's 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:** We have assessed 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.

We did not identify any significant issues. We found the conclusion that there is no impairment of the intra-group debtor balance to be acceptable.

Audit risks (cont.)



4 Going Concern

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



Other audit 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 uncertainty in the UK economy.
- 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 uncertainty in the UK economy, including plausible but severe downside scenarios on the income of the Company and carrying value of assets. Severe and plausible downside scenarios are a requirement of the FRC going concern guidance for all entities.
- The risk that disclosures in the financial statements and the annual report are not adequate with regard to the effect of uncertainty in the UK economy on the Group's financial position, performance, business model and strategy.



Our response

- 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 evaluated 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 external impacts 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 findings



Audit risks (cont.)



5 Expenses

Expenses may be recorded incorrectly leading to material misstatement

6 Cash

Cash balances may be materially misstated



Other audit 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

- We traced a sample of expenses back to supporting documentation.
- We reviewed a sample of payments made post year end to identify expenses that may have been omitted in the year.
- We recalculated the accounting charge for the long-term incentive plan ('LTIP') awarded in the year after verifying the inputs to the final calculation against source documentation.



Our findings

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



Other audit 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

- 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 with no issues noted.



Our findings

- We concluded that cash balances are free from material misstatement.

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;
- vision, leadership and governance; and
- use of resources to improve outcomes.

Our findings are summarised on pages 17-20. 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:

- Review of relevant policies;
- Inquires with the executive team;
- Review of going concern assessment prepared by the directors (ref to page 12-13);
- 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 operationally 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 stage of the Bank's operations.

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;
- Inquires with the executive team;
- Review of internal audit reports.

- Walkthroughs of the finance processes relevant to reporting; and
- 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;
 - financial reporting to Scottish Government.

Conclusion

- 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 stage of the Bank's operations.

Wider scope reporting – vision, leadership and governance

Vision, Leadership and Governance 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.
- Review of internal audit reports.
- Inquiries with the executive team.
- Reading the annual governance statement.

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 2018.

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.

Conclusion

- We have not identified a significant risk in relation to Vision, Leadership and Governance.
- Based on the work performed, we consider the arrangements in place to be effective and appropriate for the current stage of the Bank's operations.

Wider scope reporting – Use of resources to improve outcomes



Audited bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities. This includes demonstrating economy, efficiency, and effectiveness through the use of financial and other resources and reporting performance against outcomes.

Work performed:

- Review of relevant policies.
- Inquiries with the executive team.
- Review of internal audit reports.
- 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.

Internal audit assessed the procurement and value-for-money process, with some observations related to refreshing the Group's procurement policy and ensuring staff have access to guidance & template forms to enhance the policy and make efficiencies in evidencing compliance.

SNIB adopted a 'Procurement and Outsourcing Policy' which summarises relevant processes designed to ensure compliance with the value for money concept.

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:** Undertaking an assessment of the risks associated with a requirement through collaboration with IT/Legal and Risk teams as appropriate to identify risks associated with contracts and determine what mitigation might be required for each.. Applying a robust process for supplier selection that evaluates the expertise and technical ability of the supplier to deliver the required services/goods to the Bank.
- **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

Conclusion

- We have not identified a significant risk in use of resources to improve outcomes.
- Based on the work performed, we consider the arrangements in place to be effective and appropriate for the current stage of the Bank's operations.

Appendix

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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 members

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 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.



Confirmation of independence (cont.)

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 Company 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



Required communications with the Audit Committee



Type	Response
Our draft management representation letter	<input checked="" type="checkbox"/> 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 2023.
Adjusted audit differences	<input checked="" type="checkbox"/> OK There were no adjusted audit differences at the date of this report.
Unadjusted audit differences	<input checked="" type="checkbox"/> OK There were no unadjusted audit differences at the date of this report.
Related parties	<input checked="" type="checkbox"/> OK There were no significant matters that arose during the audit in connection with the entity's related parties.
Other matters warranting attention by the Audit Committee	<input checked="" type="checkbox"/> OK There were no matters to report arising from the audit that, in our professional judgment, are significant to the oversight of the financial reporting process.
Control deficiencies	<input checked="" type="checkbox"/> 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 to-date that had not previously been communicated in writing.
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts	<input checked="" type="checkbox"/> 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	<input checked="" type="checkbox"/> OK No significant difficulties have been encountered during the audit to-date.
Modifications to auditor's report	<input checked="" type="checkbox"/> OK None.
Disagreements with management or scope limitations	<input checked="" type="checkbox"/> OK The engagement team has had no disagreements with management and no scope limitations have been imposed by management during the audit.
Other information	<input checked="" type="checkbox"/> OK No material inconsistencies were identified related to other information in the annual report, Strategic and Directors' reports. The Strategic report is fair, balanced and comprehensive, and complies with the law.
Breaches of independence	<input checked="" type="checkbox"/> OK No matters to report. The engagement team and the firm have complied with relevant ethical requirements regarding independence.
Accounting practices	<input checked="" type="checkbox"/> 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 following procedures to-date.
Significant matters discussed or subject to correspondence with management	<input checked="" type="checkbox"/> OK No significant matters arising from the audit were discussed, or subject to correspondence, with management.

FRC's areas of focus

The FRC released their [Annual Review of Corporate Reporting 2021/22](#) in October 2022, along with a [summary of key matters for the coming year](#), primarily targeted at CEOs, CFOs and Audit Committee chairs. In addition, they have released six thematic reviews during the year which should be considered when preparing reporting for 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 group.

Reporting in uncertain times

This year's Annual Review of Corporate Reporting from the FRC has been prepared in the context of heightened economic and geopolitical uncertainty. The challenges of the Covid-19 pandemic, Russia's invasion of Ukraine and slowing of global economies has led to inflationary pressure worldwide and rising interest rates.

This makes meaningful disclosure more important than ever, and the FRC has stressed the need for companies to move beyond simply complying with the minimum requirements of the relevant accounting and reporting frameworks. They expect companies to provide high-quality, decision-useful information for investors, with companies continually assessing evolving risks and ensuring these are clearly explained in annual reports.

The potential effects of uncertainty on recognition, measurement and disclosure are numerous, and companies will need to think carefully about the impacts of uncertainty, in particular inflation, on their reporting. The Annual Review gives a number of examples including:

Strategic report: the impact of inflation on the business model, changes to principal risks and uncertainties, and the impact of inflation on stakeholders.

Discount rates: inputs need to follow a consistent approach in incorporating the effects of inflation.

Material assumptions: where inflation assumptions represent a source of significant estimation uncertainty, the FRC expects companies to provide explanation of how these have been calculated and sensitivity disclosures if appropriate.

Climate-related reporting

Climate-related reporting has advanced significantly this year as premium listed entities are required by the Listing Rules to provide disclosures consistent with the Taskforce on Climate-Related Disclosures (TCFD) recommendations. This follows the expansion of the Streamlined Energy and Carbon Reporting (SECR) rules last year, which require quoted companies and large unquoted companies and LLPs to provide emissions reporting.

Climate has therefore been an area of ongoing focus for the FRC, with a thematic reviews in both 2021 and 2022 on aspects of climate reporting. From reviews of TCFD disclosures in the year, the FRC has highlighted five areas of improvement for companies to consider going forwards:

Granularity and specificity: disclosures should be granular and specific both to the Company and the individual disclosure requirement, including a clear link to financial planning.

Balance: discussion of climate-related risks and opportunities should be balanced, and companies should consider any technological dependencies.

Interlinkage with other narrative disclosures: companies should ensure clear links between TCFD disclosures with other narrative disclosures in the annual report.

Materiality: companies should clearly articulate how they have considered materiality in the context of their TCFD disclosures.

Connectivity between TCFD and financial statements disclosures: the FRC may challenge those that disclose significant climate risks or net zero transition plans in narrative reporting, but do not explain how this is taken into account in the financial statements.



FRC's areas of focus (cont.)



Cash flow statements

This continues to be a particular area of concern as it is a recurring source of errors identified by the FRC, with 15 companies restating their cash flow statements in the review period as a result of the FRC's enquiries.

Companies are encouraged to consider the guidance in the 2020 thematic review on this topic, and to ensure that robust pre-issuance reviews of the financial statements have been undertaken.

Cash flows must be classified as operating, investing or reporting in line with the requirements of the standard, and amounts reported should be consistent with disclosures elsewhere in the report and accounts including the elimination of non-cash transactions.

Several errors identified by the FRC related to the parent Company cash flow statement, and it should be ensured that this statement also complies with the requirements of the standard.

Financial Instruments

Companies should ensure that disclosure is sufficient to enable users to evaluate the nature and extent of risks arising from financial instruments and the approach taken to risk management.

These disclosures should include the approach and assumptions used in the measurement of expected credit losses, and details of concentrations of risk. In times of economic uncertainty, disclosure of methods used to measure exposure to risks, and details of hedging arrangements put in place for interest rates or inflation are all the more important.

In addition, accounting policies should be provided for all material financing and hedging arrangements and any changes in these arrangements. Where companies have banking covenants, information about these should be provided (unless the likelihood of a breach is considered remote).

Income taxes

Where material deferred tax assets are recognised by historically loss-making entities, disclosures should explain the nature of the evidence supporting their recognition. In addition, any connected significant accounting judgements or sources of estimation uncertainty will also need to be disclosed.

On tax more generally, the FRC expects companies to ensure that tax-related disclosures are consistent throughout the annual report and accounts, and material reconciling items in the effective tax rate reconciliation are adequately explained.

For groups operating in several jurisdictions, effective tax reconciliations may be more meaningful if they aggregate reconciliations prepared using the domestic rate in each individual jurisdiction, with a weighted average tax rate applied to accounting profit.

Strategic report and other Companies Act 2006 matters

The strategic report needs to articulate the effects of economic and other risks facing companies, including inflation, rising interest rates, supply chain issues and labour relations. Mitigation strategies should be explained, with links, where relevant, to information disclosed elsewhere in the annual report.

Business reviews should discuss significant movements in the balance sheet and cash flow statement, and should not be limited to just an explanation of financial performance in the period.

The FRC has also identified instances of companies not complying with legal requirements around distributions, and companies are reminded of the need to file interim accounts to support distributions in excess of the distributable profits shown in the relevant accounts.

Revenue

Accounting policies should be provided for all significant performance obligations and should address the timing of revenue recognition, the basis for over-time recognition, and the methodology applied.

Inflationary features in contracts with customers and suppliers and the accounting for such clauses are under increased focus this year.

Alternative performance measures ('APMs')

APMs should not be presented with more prominence, emphasis or authority than measures stemming directly from the financial statements, and should be reconciled to the relevant financial statements line item.

FRC's areas of focus (cont.)

Provisions and contingencies

Companies should give clear and specific descriptions of the nature and uncertainties for material provisions or contingent liabilities, the expected timeframe and the basis for estimating the probable or possible outflow.

Inputs used in measuring provisions should be consistent in the approach to incorporating the effects of inflation, and details of related assumptions should be provided if material.

Presentation of financial statements and related disclosures

Material accounting policy information should be clearly disclosed, and additional Company-specific disclosures should be provided when compliance with IFRS requirements is insufficient to adequately explain transactions.

Judgements and estimates

Economic uncertainty increases the likelihood of companies needing to make significant judgements when preparing financial statements. The FRC highlights two specific examples – going concern assessments and accounting for inflationary features in contracts – where disclosure is key.

More generally, the FRC highlights the need for disclosures to clearly distinguish between estimates with a significant risk of a material adjustment to the carrying amounts of assets/liabilities within the next year, and other sources of estimation uncertainty.

Significant estimates, and the associated disclosures should be updated at the balance sheet date. Sensitivity disclosures should be meaningful for readers, for example by sensitising the most relevant assumptions, and explaining any changes in assumption since the previous year.

Impairment of assets

Economic uncertainty may have a significant impact on impairment assessments, and this is an area where queries raised from the FRC could have been avoided by clearer disclosure.

Companies need to explain the sensitivity of recoverable amounts to changes in assumptions, especially where the range of possible outcomes has widened. This should include explanation of the effect of economic assumptions, such as reduction in customer demand and increased cost.

Inflation should be treated consistently in value in use calculations. Nominal cash flows are discounted at a nominal rate, and real cash flows are discounted at a real rate.

Lastly, the FRC stresses the importance of consistency between impairment reviews/disclosures and other disclosures in the annual report.

Thematic reviews

The FRC has released six thematic reviews on corporate reporting in the current year, and companies are encouraged to consider the guidance in those reviews, where relevant, to enhance their financial reporting. The topics covered this year are:

- [TCFD disclosures and climate in the financial statements](#)
- [Judgements and estimates](#)
- [IFRS 3 Business Combinations](#)
- [Discount rates](#)
- [Deferred Tax Assets \(IAS 12\)](#)
- [Earnings per Share \(IAS 33\)](#)

2022/23 review priorities

The FRC has indicated that its 2022/23 reviews will focus on the extent to which companies' disclosures address risks and uncertainty in the challenging economic environment, including those relating to climate change. Companies need to clearly articulate the impact of these risks on their strategy, business model and viability. In particular, the FRC intends to prioritise reviews of companies operating in the following sectors:

 Travel, hospitality and leisure

 Construction materials

 Retail

 Gas, water and multi-utilities



ISA (UK) 315 Revised: Overview

Summary

ISA (UK) 315 Identifying and assessing the risks of material misstatement incorporates significant changes from the previous version of the ISA.

These have been introduced to achieve a more rigorous risk identification and assessment process and thereby promote more specificity in the response to the identified risks. The revised ISA is effective for periods commencing on or after **15 December 2021**.

The revised standard expands on concepts in the existing standards but also introduces new risk assessment process requirements – the changes had a significant impact on our audit methodology and therefore audit approach.

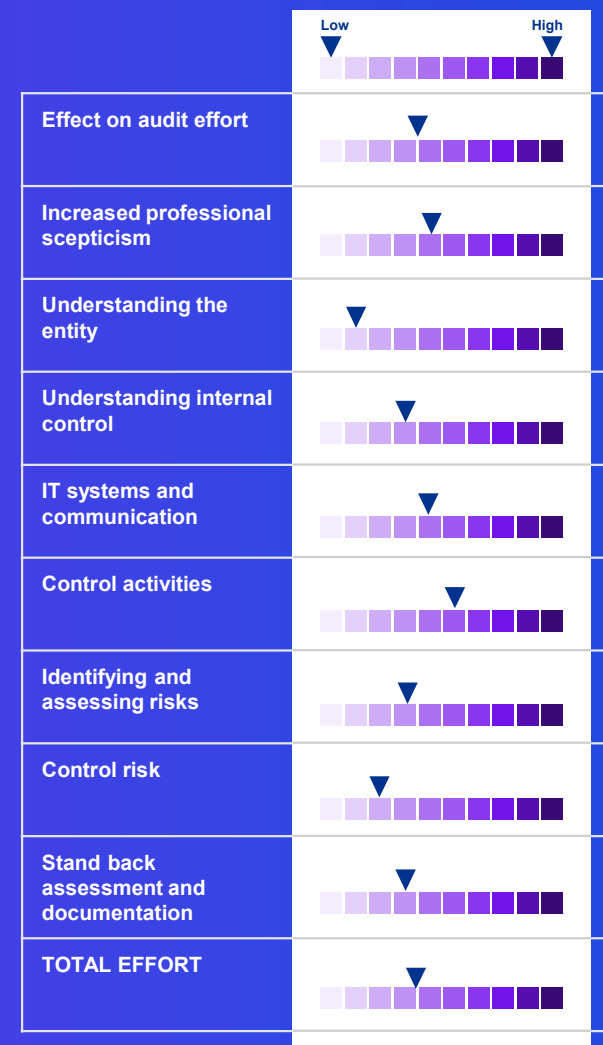
Why have these revisions been made?

With the changes in the environment, including financial reporting frameworks becoming more complex, technology being used to a greater extent and entities (and their governance structures) becoming more complicated, standard setters recognised that audits need to have a more robust and comprehensive risk identification and assessment mechanism.

The changes are aimed at (i) promoting consistency in effective risk identification and assessment, (ii) modernising the standard by increasing the focus on IT, (iii) enhancing the standard's scalability through a principle based approach, and (iv) focusing auditor attention on exercising professional scepticism throughout risk assessment procedures.

What did this mean for our audit?

To meet the requirements of the new standard, auditors have been required to spend an increased amount of time across the risk assessment process, including more detailed consideration of the IT environment. These changes have resulted in significantly increased audit effort levels which in turn, has affected auditor remuneration. This additional effort is a combination of time necessary to perform the enhanced risk assessment procedures and the need to involve more technical specialists (particularly IT Audit professionals) in our audits.



ISA (UK) 240 Revised: Summary of key changes



Summary and background

ISA (UK) 240 The auditor's responsibilities relating to fraud in an audit of financial statements includes revisions introduced to clarify the auditor's obligations with respect to fraud and enhance the quality of audit work performed in this area. The revised ISA (UK) is effective for periods commencing on or after **15 December 2021**. Unlike ISA (UK) 315 which mirrors updates in the international ISA, the updated UK fraud standard is not based on international changes by the IAASB.

The impact of the revisions to ISA (UK) 240 is less extensive compared to ISA (UK) 315, but nevertheless resulted in changes to our audit approach. The table to the right summarises the main changes and our final assessment of their impact.

What did this mean for our audit?

The changes introduced new requirements which increased audit effort and therefore the audit fee. The additional work is largely the result of investing more time identifying and assessing the risk of fraud during risk assessment and involving specialists to aid with both risk identification and the auditor's response to risk.

Area	Effect on audit effort	Summary of changes and impact
Risk assessment procedures and related activities		<ol style="list-style-type: none"> Increased focus on applying professional scepticism – the key areas affected are: <ul style="list-style-type: none"> obtained evidence that is corroborative in nature or our consideration of contradictory evidence. remained alert for indications of inauthenticity in documents and records, and investigated inconsistent or implausible responses to inquiries performed. Our inquiries with individuals at the entity were expanded to include, amongst others, those who deal with allegations of fraud We determined whether to involve technical specialists (including forensics) to aid in identifying and responding to risks of material misstatement due to fraud. As a result of this assessment we concluded no specialist involvement was required in the audit.
Internal discussions and challenge		We complied with enhanced requirements for internal discussions among the audit team to identify and assess the risk of fraud in the audit, including a requirement to determine the need for additional meetings to consider the findings from earlier stages of the audit and their impact on our assessment of the risk of fraud.
Communications with management / TCWG		We have complied with new requirements for communicating matters related to fraud with management and those charged with governance, in addition to the reporting in our audit reports.

Compliance with the UK Corporate Governance Code



We communicate 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 & 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.

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 & internal control

We are satisfied that there are no significant deficiencies in internal control which impact the financial statements.

Newly effective standards



Standards	Expected impact				Effective for years beginning on or after	
	High	Moderate	Low	None	1 Jan 2022	1 Jan 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)				●		✓
IFRS 17 Insurance contracts				●		✓
Amendments to IFRS 17 Insurance Contracts: Initial application of IFRS 17 and IFRS 9 – Comparative Information				●		✓
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			●			✓

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.

■ Commitment to continuous improvement

- 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

■ Performance of effective & efficient audits

- 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

■ Commitment to technical excellence & quality service delivery

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



■ Association with the right entities

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

■ Clear standards & robust audit tools

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

■ Recruitment, development & assignment of appropriately qualified personnel

- 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 employed KPMG specialists and specific team members



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