Technical Bulletin 2022/1

Technical developments and emerging risks from January to March 2022

Prepared by Audit Scotland for appointed auditors and audited bodies in all sectors

23 March 2022

Contents

1: Introduction

Purpose

The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General for Scotland and Accounts Commission for Scotland with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- summaries of responses to any requests from auditors for technical consultations with Professional Support.

Appointed auditors are required by the Code of Audit Practice to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require generally to be aware of. It may still be necessary for auditors to read the source material if greater detail is required in the circumstances of a specific audited body. Source material can be accessed by using the hyperlinks.

Any specific actions that Professional Support recommends that auditors take are highlighted in green.

Technical Bulletins are also published on the Audit Scotland website and therefore are available for audited bodies and other stakeholders to access. However, hyperlinks to source material indicated with an asterisk (*) link to files on Audit Scotland's SharePoint* and are only accessible by auditors.

Highlighted items

Professional Support highlights in the following table a selection of the items in this Technical Bulletin that are of particular importance:

Highlighted items		
Professional Support has published model forms of Independent Auditor's Reports for 2021/22 [**paragraph 1**]	Professional Support has published a Good Practice Note on related party disclosures [**paragraph 6**]	RICS has withdrawn its COVID-19 practice alert [**paragraph 10**]
Professional Support has published audit assurance protocols for 2021/22 [**paragraph 11**]	CIPFA/LASAAC has issued proposals to update the 2021/22 and 2022/23 local authority accounting code [**paragraph 14**]	CIPFA has issued a disclosure checklist for the 2021/22 local authority financial statements [**paragraph 16**]
Amendment regulations have been approved on the loans fund and accounts deadlines [**paragraph 20**]	The Scottish Government has issued guidance on the cost of living award [**paragraph 23**]	CIPFA has issued a revised edition of the prudential code [**paragraph 24**]
CIPFA has issued a revised edition of the treasury management code [**paragraph 36**]	The Accounts Commission has issued the 2020/21 financial overview of local authorities [**paragraph 39**]	Professional Support has issued a briefing on section 106 charities [**paragraph 40**]
Professional Support has published guidance on risks of misstatement in 2021/22 annual report and accounts [**paragraphs 44 and 69**]	Treasury has issued a revised edition of the 2021/22 FReM [**paragraph 48**]	Treasury has issued updated guidance on the fair pay disclosure [**paragraph 51**]
Treasury has issued a paper on discount rates for 2021/22 [**paragraph 52**]	Treasury has issued the 2022/23 FReM [**paragraphs 58**]	The SG has issued the NHS accounts manual and the capital accounting manual [**paragraphs 72 and 80**]

Contact point

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2: All sectors

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Independent auditor's reports for 2021/22

1. Professional Support has published the following technical guidance notes (TGN) to provide auditors with model forms of Independent Auditor's Reports (IAR) which should be used for the 2021/22 annual accounts of public bodies in Scotland:

- TGN 2022/2(H) for health boards
- TGN 2022/4(CG) for central government bodies
- TGN 2022/5(LG) for local government bodies.

2. Auditors are required by the Code of Audit Practice to prepare their IARs in accordance with these TGNs. The TGNs are available with supporting material to auditors on SharePoint* and are also freely available from the Audit Scotland website.

3. The model form of IARs set out in the appendices of the TGNs have been tailored to reflect relevant public sector legislation and augmented by the reporting requirements of the Auditor General and Accounts Commission.

4. There are a number of changes to the model forms of IAR and to the application guidance in 2021/22. These are summarised in the following table:

Area	Change
Model IARs	The references to the financial reporting framework have been updated, as a result of the UK's departure from the EU, to reflect that international accounting standards are now those adopted by the UK.
	Changes have been made in the 'Conclusions relating to going concern' and the 'Responsibilities of the Accountable Officer' sections of the model IARs to better explain the application of going concern in the public sector.
	There are also some minor wording clarifications.
Application guidance	Changes in the guidance include: • permitting auditors to amend the specified wording that explains the extent to which the audit is capable of detecting irregularities • advice for auditors to encourage bodies to use the titles for statements that are consistent with the applicable financial reporting framework for the sector • advice on how to deal with the inclusion of any voluntary reports.

5. Auditors should for 2021/22 audits:

- use the relevant model form of IAR for each audited body
- follow the specified wording other than where tailoring adjustments are set out in the application guidance in the TGN
- consult with Professional Support on any modified opinion or conclusion
- complete an auditor action checklist for each IAR prepared.

Good practice in disclosing related parties

6. Professional Support has published a Good Practice Note (GPN) following a review of the disclosures for related parties within the financial statements of a sample of public bodies in Scotland.

7. The related parties note was chosen for a good practice review because of the potential impact of the relationships in understanding the financial statements, along with indications that the quality of the disclosures was variable. Good practice is illustrated, where possible, using examples taken from the 2020/21 financial statements of the bodies in the sample.

8. The review was carried out by a team in Professional Support with knowledge of the relevant financial reporting framework. However, the team does not have a detailed understanding of each body's particular circumstances or the specific underlying transactions.

9. Auditors are requested to encourage their audited bodies to use the GPN to assess and enhance their own disclosures in 2021/22.

Withdrawal of valuation practice alert

10. The Royal Institute of Chartered Surveyors has issued a notice to formally withdraw its Global COVID-19 Valuation Practice Alert. The withdrawal of the alert includes withdrawal of:

- the COVID-19 market conditions explanatory note
- general valuation practice and process recommendations related to COVID-19
- the suggested material uncertainty wording related to COVID-19. In the limited circumstances where material uncertainty is still being declared, it should be reported to reflect the individual circumstances. The decision as to whether material uncertainty exists remains with the valuer, who should include a sound rationale to explain the decision-making process.

3: Local government sector

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Audit assurance protocols for 2021/22

11. Professional Support has published two protocols to provide agreed frameworks for auditors to seek and provide certain assurances from auditors of other public bodies. The assurance protocols are summarised in the following table:

Protocol subject	Nature of audit assurances
Local Government Pension Scheme (LGPS)	LGPS pension fund auditors request assurances from employer body auditors in respect of pension contributions payable by the employer body to the pension fund. Employer body auditors request assurances from pension fund auditors in respect of information provided by the pension fund to the actuary in relation to their reports on employer bodies.
Integration joint boards (IJBs)	IJB auditors request assurances from the auditors of the constituent authorities regarding information not held by the IJB.

12. The protocols set out the potential range of assurances but do not compel any specific assurances to be sought. It is not expected that any assurances outwith the specified range will generally be requested but that will be a matter for local agreement in 2021/22.

13. Auditors should:

- judge whether it is necessary to request any assurances from other auditors in 2021/22
- follow the agreed frameworks in each protocol when requesting or providing assurances.

Proposals to update 2021/22 and 2022/23 accounting code

14. The CIPFA/LASAAC Code Board has issued an Invitation to Comment (ITC) on proposed changes to the Code of Practice on Local Authority Accounting in the UK (accounting code). The proposals are in response to a request from the Department for Levelling Up, Housing and Communities (DLUHC) for CIPFA/LASAAC to consider steps that could help alleviate significant audit delays of local authorities in England. Consequently, the measures were proposed, exceptionally, as an expedient rather than with the aim of improving financial reporting.

15. The consultation ended on 3 March, and CIPFA/LASAAC subsequently issued a Feedback Statement setting out their decisions in light of the consultation results. The proposals and related decisions are summarised in the following table:

Area	Proposal	Decision
Pause requirement to value property, plant and equipment	An amendment to the 2021/22 accounting code in respect of the valuation requirements for property, plant and equipment. In summary, it proposed that local authorities should have the option, as a temporary expedient, to pause the requirement for the valuation of property, plant and equipment for at least two years commencing in 2021/22. There was a related option to apply an approved index during the period.	CIPFA/LASAAC decided not to progress this proposal.
Deferral of IFRS 16	Defer further the implementation of IFRS 16 Leases to later than 2022/23.	CIPFA/LASAAC preliminarily decided to progress deferral for a period of two years, subject to approval of the Financial Reporting Advisory Board.

2021/22 disclosure checklist

16. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued a disclosure checklist* for the 2021/22 financial statements. It is intended for use as an aide-memoire to assist in meeting the requirements of the accounting code.

17. The checklist is in the form of a series of questions and the implications of the answers are set out in the following table:

Answer	Implication
Yes	The accounting code is being complied with.
No	A justification for departing from the accounting code should be given. For example, a legitimate justification may be that the information resulting from a particular disclosure is not material.

18. When evaluating whether the accounting code's disclosure requirements have been met, auditors should:

- request that the body completes the 2021/22 disclosure checklist
- investigate the reasons for any non-compliance that the checklist highlights

- evaluate whether the body's responses in the checklist are consistent with auditor's knowledge.

19. Where the body declines to complete the checklist, auditors should:

- establish the alternative arrangements by which it satisfies itself regarding the completeness of disclosures
- evaluate the adequacy of the arrangements
- consider completing the checklist as part of their audit procedures, where the body’s arrangements are judged not to be adequate.

Amendment regulations on loans fund and accounts deadlines

20. The Local Authority (Capital Finance and Accounting) (Scotland) (Coronavirus) Amendment Regulations 2022 have been approved by the Scottish Parliament, and will shortly be made as a Scottish Statutory Instrument. The regulations amend:

- The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 (the 2016 regulations) in respect of loans fund repayments
- The Local Authority Accounts (Scotland) Regulations 2014 (2014 regulations) in respect of approval and publication dates for the annual accounts.

21. The amendments to the above regulations are summarised in the following table:

Amending regulation	Regulation amended	Nature of amendment
Regulation 2	Regulation 10 of the 2014 regulations	The date by which local authorities must approve the audited 2021/22 annual accounts is deferred until 30 November 2022.
	Regulation 11 of the 2014 regulations	The date by which local authorities must publish the audited 2021/22 annual accounts is deferred until 15 December 2022.
Regulation 3	Regulation 14A of the 2016 regulations	Local authorities are allowed to defer loans fund repayments in 2022/23. This is in addition to the existing ability to defer repayments in either 2020/21 or 2021/22. The option to defer can be used in only one of the three financial years.
Regulation 4	Regulation 14 of the 2016 regulations	The date for replacing the existing repayment provisions with statutory guidance has been deferred from 1 April 2022 to 1 April 2023.

22. The target date for completing the audit of local government bodies remains 31 October 2022 as set out in the guidance on planning 2021/22 audits, which is a month earlier than the amended statutory deadline in the 2014 regulations.

Guidance on cost-of-living award

23. The Scottish Government has issued Finance Circular 2/2022 to assist local authorities in supporting low income households tackle the cost of living crisis, under a scheme announced as part of the 2022/23 Scottish Budget. Some key aspects of the scheme are summarised in the following table:

Area	Para ref	Guidance
Amount	1	The amount of the award is £150.
Eligibility	10 to 16	An eligible person is an individual liable for council tax on 14 February 2022 who is either: • in receipt of Council Tax Reduction; or • liable for council tax for a Band A to D dwelling; or • in certain categories of person living in a property exempt from Council Tax (explained at paragraph 16 of the circular).
Payment and delivery	19 to 21	Eligible persons do not need to apply for the award. Local authorities can make the payment either as a credit to council tax accounts or by direct payment. The payment should be made by 30 April 2022.
Fraud and error	31 to 33	In cases where a direct payment of the award is made, reasonable additional steps should be taken to tackle potential fraud. Authorities are expected to recover any payments made in error if the costs of doing so are proportionate. Authorities are required to robustly pursue the recovery of any payments made where eligibility is based on false or fraudulent information.
Reporting	37 and 38	Authorities are required to report the total value of council tax account credits and any direct payments using the template at Annex A, initially by 29 April and then at the scheme closure.

Revised prudential code

24. CIPFA has issued a revised edition of The Prudential Code for Capital Finance in Local Authorities*. This revised edition applies with immediate effect, except that local authorities may defer introducing the revised reporting requirements until the 2023/24 financial year.

25. The main changes are in respect of:

- borrowing in advance of need
- commercial investments

- prudential indicators.

Borrowing in advance of need

26. The previous edition of the prudential code stated (at paragraph 45) that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

27. However, this has been replaced with new paragraphs 49 to 52. This includes:

- paragraph 50 setting out examples of legitimate prudent borrowing, e.g. financing capital expenditure primarily related to the delivery of a local authority's functions
- paragraph 51 stating that an authority must not borrow to invest primarily for financial return.

Commercial investments

28. Paragraph 95 of the revised prudential code sets out the three categories of investments summarised in the following table:

Category	Definition
Treasury management	Investments that arise from cash flows or treasury risk management activity, and ultimately represent balances which need to be invested until the cash is required for use in the course of business. It may also include: • an allowance for a reasonable level of short-term treasury investments for liquidity purposes • the investment of borrowed cash where it has been prudent to borrow in advance of needing the cash, e.g. in order to reduce financing and interest rate risks.
Service	Investments held primarily and directly for the delivery of public services. There may be financial returns, but they are not the primary purpose of the investment.
Commercial	Investments held primarily for financial return and not linked to treasury management activity or directly part of delivering services. This includes commercial property which is defined at paragraph 91 as any property which the local authority purchases or holds primarily for financial return.

29. The objectives of the prudential code at paragraph 1 have been amended to reflect that the risks associated with investments for commercial purposes should be proportionate to the local authority's financial capacity, i.e. that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services.

30. Paragraph 53 clarifies that authorities with existing commercial investments (including property) are not required to immediately sell these investments, and that they may invest in the repair, renewal and updating of their existing commercial properties. However, it advises that authorities:

- should review options for exiting their financial investments for commercial purposes in their annual treasury management or investment strategies

- should not take new borrowing if financial investments for commercial purposes can reasonably be realised instead.

31. Additional commentary on the assessment of affordability and the details of risks of undertaking commercial activity within the commercial activities section on determining the capital strategy has been added to paragraph 24.

Prudential indicators

32. Paragraphs 81 to 85 set out new indicators for (estimated and actual) net income from commercial and service investments to net revenue stream to assess proportionality.

33. There is also the option to include a local indicator for net income from commercial and service investments as a proportion of useable revenue reserves.

34. The following changes have been made to definitions:

- Interest and investment income has been removed from the list of items at paragraph 94 that are netted off finance costs.

- Clarification has been added to paragraph 96 that net revenue stream should exclude capital grants, contributions and donated assets.

35. Paragraph 43 has been amended to require prudential indicators to be reported at least quarterly rather than the current annual basis.

Revised treasury management code

36. CIPFA has also issued a revised edition of the Treasury Management in the Public Services Code of Practice* and related guidance notes. The revisions to the treasury management code introduce strengthened requirements for investments that are not specifically for treasury management purposes.

37. There is a new requirement for any service and commercial investments to be categorised into appropriate portfolios reflecting the different purposes, objectives and management arrangements of the investments. For each portfolio, a schedule is required to set out the investment objectives, and risk management and reporting arrangements.

38. Other changes include the following:

- Treasury Management Practice (TMP) 1 has been amended to require that the formal counterparty policy should set out the body's policy and practices relating to Environmental, Social and Governance investment considerations.

- A requirement has been added to TMP 10 for a knowledge and skills schedule. Page 55 of the guidance notes set out suggestions for the schedule.

2020/21 financial overview

39. The Accounts Commission has published its annual financial overview of Scottish local authorities. The report provides a high-level independent analysis of the financial performance of local authorities during 2020/21 and their financial position at 31 March 2021. Some key messages include the following:

- Local authority funding increased by £1.5 billion to support dealing with the impact of the COVID-19 pandemic. When COVID-19 funding is excluded, there has been a ‘real terms’ underlying reduction in funding of 4.2% since 2013/14.
- All local authorities increased their usable revenue reserves, mainly due to late COVID-19 funding which was unspent at 31 March 2021.
- Authorities administered a further £1.4 billion of COVID-19 grants on behalf of the Scottish Government.
- Capital expenditure reduced by more than 20%.
- Many management commentaries are still not complying with recommendations on transparency made in previous reports.
- COVID-19 pressures on finance staff contributed to greater and more frequent errors in unaudited accounts. Auditors also reported wider issues, including the slowing of progress in some transformation plans, the impact of reduced income on arm’s-length external organisations, weaknesses in internal control systems, and adverse impacts on long-term planning and capacity.

Section 106 charities accounts

40. Professional Support has issued a briefing to encourage a reduction in the number of sets of accounts of registered charities that fall within the scope of section 106 of the Local Government (Scotland) Act 1973 (section 106 charities). The briefing provides information on:

- the number of section 106 charities administered by each local authority in 2020/21
- the number of related sets of accounts.

41. Local authorities continued to administer a total of 172 section 106 charities; twelve authorities administer more than five each. In order to reduce the number of section 106 charities in 2021/22, auditors should strongly encourage authorities with multiple charities to:

- reorganise their charities through merging or winding them up, particularly when they appear to be failing to meet their charitable aims (e.g. by not disbursing funds)
- consider appointing an external trustee as this would remove the charity from the scope of section 106.

42. In the meantime, there is scope under the charity regulations for connected charities to prepare a single set of accounts. In Professional Support’s view, the definition of connected charities is met for section 106 charities administered by the same local authority even where trustees differ as they meet the condition for ‘unity of administration’. However, in 2020/21

- five authorities made only partial use of the connected charities provisions and produced 19 sets of accounts between them
- eight authorities made no use of the provisions and produced 32 sets of accounts.

43. Auditors should strongly encourage local authorities to make full use of the connected charities provisions in 2021/22.

4: Central government sector

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TGN on risks of misstatement in 2021/22

44. Professional Support has published TGN 2022/1 to provide auditors with guidance on risks of misstatement in the 2021/22 annual report and accounts of central government bodies. The TGN and supporting material is accessible by auditors on SharePoint* and is also freely available to download from the Audit Scotland website.

45. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2021/22 audits. Auditors should advise Professional Support of any intended departures from the guidance.

46. The TGN comprises a number of modules as summarised in the following table:

Module	Risks of misstatement area	Purpose
Overview	Areas that are pervasive to the financial statements as a whole	Explains the appropriate related accounting treatment and sets out the action auditors should undertake to evaluate whether the body has followed the required treatment
1 - 8	Specific classes of transactions, balances and disclosures in the financial statements	
9	Irregularities in expenditure and income	Explains the requirements and sets out the action auditors should undertake
10	Audited part of the Remuneration and Staff Report	
11	Statutory Other Information (e.g. Performance Report and Governance Statement)	Sets out the procedures for considering the Statutory Other Information
12	Charitable NDPBs	Provides guidance on the application of the above modules to charitable NDPBs
13	Health boards	See chapter 5

47. The risks of misstatement for 2021/22 have been updated to reflect new requirements and risks which emerged during the 2020/21 audits that remain applicable. A separate note* summarises the main changes from 2020/21.

Revised 2021/22 FReM

48. HM Treasury has issued a revised version of the 2021/22 Government Financial Reporting Manual (the FReM). This includes in-year changes from the initial version published in December 2020 referred to in Technical Bulletin 2021/1 (paragraph 55).

49. Some in-year changes amend and clarify aspects of the new fair pay disclosure requirements. These changes are summarised in the following table:

FReM para	Area	Change
6.5.19	Percentage changes in non-cash benefits	The new requirement added to the initial version of the 2021/22 FReM to disclose percentage changes in non-cash benefits has been removed.
6.5.20 to 6.5.22	New guidance on calculating percentage change disclosures	New guidance has been added advising that: • the calculation of the percentage change from last year in the salary and allowances of the highest paid director should be based on the mid-point of the band • the calculation in respect of the percentage change for all employees should be the total for all employees divided by the full time equivalent number of employees (both numbers excluding the highest paid director).
6.5.28	Range of remuneration	Clarification has been added that the range of staff remuneration should include all directors (including the highest paid director) but exclude pension benefits.

50. Other changes in the revised version of the FReM are summarised in the following table:

FReM ref	Area	Change
Section 8.2	IFRS 9 adaptation 1	Government Banking Service (GBS) balances have been added to the exclusions from recognising stage 1 or stage 2 expected credit losses.
Section 8.2	IFRS 9 adaptation 4	New adaptation for cases where financial guarantees are issued at below fair value and no active market or observable equivalent exists. Bodies should measure the guarantee at an amount equal to lifetime expected credit losses.

FReM ref	Area	Change
Section 8.2	IAS 19 interpretation 2	The interpretation clarifies that valuation results for pensions may not necessarily be reflected in the financial statements due to timing differences.
Paragraph 10.1.31	Asset transfers	Guidance has been added clarifying that when assets are transferred between bodies, they should be revalued prior to the transfer.

Revised guidance on fair pay disclosure

51. Treasury has issued updated guidance on disclosing fair pay information to reflect the new 2021/22 FReM requirements. Selected aspects of the guidance are summarised in the following table:

Para ref	Disclosure	Guidance
2.1	Pay and benefits of highest paid director	The pay and benefits of the highest paid director should be consistent with those disclosed in the single total figure of the remuneration table (excluding pension benefits).
3.6	Lower, median and upper pay and benefits of employees	The guidance explains that: • the median is the total pay and benefits of the employee in the middle of the linear distribution of all employees (i.e. 50th percentile). • the lower quartile is the total pay and benefits of the employee on the 25th percentile of the linear distribution and the upper quartile relates to the employee on the 75th percentile. • these are based on annualised, full-time equivalent remuneration of all staff as at 31 March.
3.14		The amounts should be disclosed to the nearest pound.
3.19		The calculation should include agency and other temporary employees, but exclude consultancy services.
3.12 and 3.13	Total remuneration	Remuneration should comprise salary, non-consolidated performance-related pay, benefits-in-kind allowances and any other components of remuneration as at 31 March. It should not include severance payments, employer pension contributions and cash equivalent transfer values. This exclusion should be explained in the narrative disclosure.

Para ref	Disclosure	Guidance
3.20	Narrative	Narrative disclosure should assist users to understand the calculations and the body's scope for controlling pay policy arrangements.
3.5		If a body believes that any pay arrangements will give rise to distorted results, such as the use of agency staff or shared executives, the supporting narrative should provide clarification.
3.11	Non-director employees	Bodies are encouraged to disclose information on any (non-director) employees who received remuneration in excess of the highest paid director.

2021/22 discount rates

52. Treasury has issued PES(2021)10* which announces the change in the discount rate for general provisions, post-employment benefits liabilities, and financial instruments as at 31 March 2022.

53. The nominal discount rates to be applied as at 31 March 2022 for discounting general provisions recognised under IAS 37 are set out in the following table:

Category	Period	Percentage
Short term	Within 5 years	0.47%
Medium term	Between 5 and 10 years	0.7%
Long term	Between 10 and 40 years	0.95%
Very long term	More than 40 years	0.66%

54. As nominal rates do not take inflation into account, cash flows require to be inflated separately. There is a rebuttable assumption that the inflation rates specified in the paper will be used (unless other rates are clearly more applicable). The specified rates are:

- 4% for up to one year from the year end
- 2.6% between one and two years
- 2% for after two years.

55. The discount rates for post-employment benefits are set out in the following table:

Use	Rate from 31 March 2022
Real rate used for valuing unfunded pension scheme liabilities and early departure provisions	1.3%
Nominal rate for unwinding discount on liabilities (interest)	1.55%
Rate used for funded pension schemes	Based on returns from AA corporate bonds at 31 March

56. The financial instrument discount rates to be applied at 31 March 2022 are set out in the following table:

Type	Rate
Real rate when financial instrument indexed to RPI	0.7%
Nominal rate when financial instrument is not linked to an inflationary index	1.1%

2021/22 GBS account information

57. Professional Support will obtain information on account balances at 31 March 2022 for central government bodies from the GBS and distribute them to relevant auditors. The GBS has confirmed that the arrangements for obtaining 2021/22 account balances are unchanged.

2022/23 FReM

58. Treasury has issued the 2022/23 FReM. The main change is the adoption of IFRS 16 Leases, as adapted and interpreted for central government.

59. Under IFRS 16, a lease is a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration. The FReM adaptations expand the normal definition of ‘contract’ to include:

- intra-government agreements where non-performance may not be enforceable by law
- peppercorn leases (i.e. leases for which the consideration paid is nil or significantly below market value) if they meet the definition of a lease other than the requirement for consideration. The FReM sets out the accounting treatment for such leases.

60. The FReM also sets out a number of interpretations of IFRS 16 which are summarised in the following table:

IFRS 16	FReM interpretation
Under paragraph 5a, a lessee has the option not to apply the recognition and measurement requirements of IFRS 16 to short-term leases.	Bodies are required to apply this option.
Paragraph 26 requires the lease liability to be measured at the present value of the outstanding lease payments discounted using the interest rate implicit in the lease or, if that rate can be readily determined, the lessee's incremental borrowing rate.	Where bodies cannot readily determine the interest rate implicit in the lease, they are required to use the Treasury discount rates promulgated in PES papers as their incremental borrowing rate, unless another discount rate would be more accurate.
Paragraph C3 allows lessees the option not to reassess whether a contract is, or contains, a lease at the date of initial application. Instead, the lessee is permitted to apply IFRS 16 only to contracts that were previously identified as leases under the previous standards.	Bodies are required to apply this option. However, this presumes that bodies have correctly applied the previous standards in prior years. Any known misapplication should be corrected as a prior period error.
Paragraph C5 gives lessees the option to apply IFRS 16 either: • to each prior reporting period: or • to recognise the cumulative effect of initially applying IFRS 16 by adjusting opening balances of taxpayers' equity at the date of initial application.	Bodies are required to apply the second option, i.e. recognise the cumulative effect as an adjustment to opening balances.
For leases previously classified as an operating lease, paragraph C8b gives lessees the option to initially measure a 'right-of-use asset' at either: • its discounted carrying amount as if IFRS 16 had been applied since the commencement date; or • an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments.	Bodies are required to apply the second option, i.e. based on the lease liability.
Paragraph C9a allows lessees the option to not make any adjustments on transition for leases previously classified as operating leases where the underlying asset is of low value.	Bodies are required to apply this option.

IFRS 16	FReM interpretation
Paragraph C10c allows lessees the option not to adjust on transition for any leases where the lease term ends within 12 months of the date of initial application. The cost associated with those leases should be included within the disclosure of short-term lease expense.	Bodies are required to apply this option, and make the necessary disclosure.
Paragraph C10e gives lessees the option to use hindsight in determining the lease term if the contract contains options to extend or terminate the lease.	Bodies are required to apply this option.

61. In addition, the FReM requires the subsequent measurement basis for all right-of-use assets to be consistent with the principles for subsequent measurement of property, plant and equipment.

62. Chapter 10.2 sets out how to apply these principles. It advises that, in most cases, the cost model set out at paragraphs 30 to 33 of IFRS 16 is an appropriate proxy for current value in existing use or fair value. Where the cost model is used, this fact should be disclosed, including the classes of right-of-use assets within which it has been used and the reasons why.

63. However, the cost model will not be an appropriate proxy for peppercorn leases or other cases where:

- a longer-term lease has no terms that require lease payments to be updated for market conditions (such as rent reviews), or if there is a significant period of time between those updates
- the value of the underlying asset is likely to fluctuate significantly due to changes in market prices, such as for property assets.

64. To measure the current value in existing use of a right-of-use asset, the FReM requires a valuer to calculate the full replacement cost of the right-of-use asset. This valuation should:

- be done by identifying the current market rental value that could be achieved for existing use of the right-of-use asset and capitalising it for the full remaining lease term from the valuation date
- reflect the terms and conditions of the lease giving rise to the right-of-use asset
- assume that the body requires to use the entire right-of-use asset.

65. In addition to leases, the reference to IAS 17 at FReM paragraph 10.1.57 in respect of measuring service concession assets has been replaced with a reference to IFRS 16.

66. Auditors should evaluate whether audited bodies' preparations for complying with IFRS 16 from 2022/23 are satisfactory.

Amendments to SPFM

67. The Scottish Government has issued Finance Guidance Note 2022/1 which announces amendments to the Certificates of Assurance section of Scottish Public Finance Manual (SPFM) in respect of the internal control checklist.

68. The questions in a number of sections of the checklist have been amended or reworded. The main changes are summarised in the following table:

Section	Summary of changes
Business Planning	Substantial revisions to questions relating to: • business objectives • how progress is measured.
Financial Management	the majority of questions have been amended with specific amendments to those on: • delegated authority • skills and training • safeguarding assets • monitoring income.
Sponsored Bodies	Questions on a number of areas have been amended including: • framework documents • effective boards • financial monitoring and forecasting • major investments. A new question added regarding changes to the body's estate.

5: Health sector

Contact: Neil Cameron, Ncameron@audit-scotland.gov.uk

TGN on risks of misstatement in 2021/22

69. Professional Support has published Module 13 of TGN 2022/1 to provide:

- guidance on applying the other modules to the audit of the 2021/22 annual report and accounts of health boards
- supplementary guidance on the risks of misstatements in areas specific to health boards.

70. The module is available with the rest of the TGN and supporting material to auditors on SharePoint* and is also freely available to download from the Audit Scotland website.

71. Auditors are expected to pay due regard to Module 13 and use it as a primary reference source when performing 2021/22 audits of health boards. Auditors should advise Professional Support of any intended departures from the guidance.

2021/22 accounts manual

72. The Scottish Government has issued the 2021/22 Manual for the Annual Report and Accounts of NHS Boards* (accounts manual). The accounts manual complements the guidance contained in the 2021/22 FReM but contains some additional or specific requirements.

73. Page 5 of the accounts manual states that the deadline for submitting the audited annual accounts is 30 June 2022. However, the target date for audit completion continues to be 31 August as set out on the guidance on planning 2021/22 audits. Where an auditor is planning to complete the audit after 30 June, they should request the relevant health board to notify the Scottish Government that the deadline will not be met.

74. The main changes included in the accounts manual for 2021/22 relate to the Performance Report and Remuneration and Staff Report.

Performance Report

75. The accounts manual sets out requirements for the Performance Report on pages 6 to 11. These include:

- A new requirement for 2021/22 to disclose non-financial information including social matters, respect for human rights, anti-corruption and anti-bribery matters and diversity.

- Information on sustainability reporting using new wording set out on page 11 of the accounts manual.

76. The accounts manual also requires disclosures on reporting performance against financial targets. Page 10 of the accounts manual provides wording to be used to explain that, due to the impact of the COVID-19 pandemic, the Scottish Government paused the three-year monitoring for 2020/21 and 2021/22. Additional funding was provided to support in-year financial balance, and there is a new requirement to disclose the amount.

Remuneration and Staff Report

77. Pages 16 to 37 of the accounts manual set out the requirements for the Remuneration and Staff Report. There is revised guidance principally on page 21 to reflect the changed requirements in the 2021/22 FReM in respect of the single figure of remuneration disclosures.

78. Pages 30 and 31 of the accounts manual have been amended to reflect the FReM's revised requirements for fair pay disclosures. This includes a:

- proforma fair pay disclosure to be included in the financial statements
- suggested method for establishing the total pay for the calculations.

79. The accounts manual states that agency staff should be excluded from the fair pay calculations. This contrasts with the fair pay guidance from the Treasury referred to in chapter 4 of this Technical Bulletin which requires agency staff to be included. In the interests of consistency, and because it is more specific guidance, Professional Support recommends that boards follow the accounts manual and exclude agency staff. In either case, auditors should evaluate whether boards have clearly disclosed the approach adopted.

2021/22 CAM

80. The Scottish Government has issued the NHS Scotland Capital Accounting Manual 2021/22* (CAM) to interpret the accounting guidance contained in the 2021/22 FReM on capital accounting issues in the health sector.

81. The main changes to the CAM for 2021/22 are as follows:

- The addition of chapter 14 to reflect the guidance referred to in Technical Bulletin 2021/2 (paragraph 81) on the GP Sustainability Loan Scheme.
- Clarification that assets transferred between health boards should be disclosed as asset transfers between other bodies in the Scottish Government Consolidated Accounts.

2020/21 NHS overview

82. The Auditor General has published an overview of the NHS in Scotland. The report examines the continued impact of the COVID-19 pandemic, and provides an overview of financial performance in 2020/21 and the financial challenges that lie ahead. Some key messages include the following:

- The pandemic resulted in significant additional expenditure across the NHS in 2020/21. External auditors found that financial management associated with COVID-19 expenditure was appropriate across all boards, with a clear distinction between reporting of COVID-19 and non- COVID-19 expenditure.

- The pandemic had a considerable impact on boards’ ability to achieve efficiency savings. The Scottish Government fully funded boards to achieve financial balance for 2020/21

- Boards face an uncertain and challenging financial position in 2021/22 and beyond, as responding to the pandemic has increased pressures on financial sustainability. The Scottish Government has committed additional funding for health and social care but there is uncertainty about future funding levels and the longer-term financial position.

6. Fraud and irregularities

Contact: Anne Cairns, acairns@audit-scotland.gov.uk

This chapter contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their bodies and take the appropriate action.

Corporate procurement card

83. A council employee misused a corporate procurement card to fund personal purchases valued at over £7,300.

Key features
The employee used an emergency authorisation process to bypass the requirement to obtain authorisation at a local level. It was therefore not identified that the purchases were not legitimate. The employee also dishonestly accessed emails and misused a computer system to fraudulently authorise their own purchases. The fraud was identified through budgetary control processes. The employee has been dismissed and reported to the Procurator Fiscal. Two managers are also subject to the council's disciplinary procedures. Detailed instructions and training have since been provided to staff outlining the proper process for the use and authorisation of corporate procurement cards.

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Technical Bulletin 2022/1

Technical developments and emerging risks from January to March 2022

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Technical Bulletin 2022/2

Technical developments and emerging risks from April to June 2022

Prepared by Audit Scotland for appointed auditors and audited bodies in all sectors

22 June 2022

Contents

1: Introduction

Purpose

The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General for Scotland and Accounts Commission for Scotland with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- summaries of responses to any requests from auditors for technical consultations with Professional Support.

Appointed auditors are required by the Code of Audit Practice to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require generally to be aware of. It may still be necessary for auditors to read the source material if greater detail is required in the circumstances of a specific audited body. Source material can be accessed by using the hyperlinks.

Any specific actions that Professional Support recommends that auditors take are highlighted in green.

Technical Bulletins are also published on the Audit Scotland website and therefore are available for audited bodies and other stakeholders to access. However, hyperlinks to source material indicated with an asterisk (*) link to files on Audit Scotland's SharePoint* and are only accessible by auditors.

Highlighted items

Professional Support highlights in the following table a selection of the items in this Technical Bulletin that are of particular importance:

Highlighted items		
Treasury has issued guidance on preparing the 2020/21 WGA [**paragraph 1**]	Professional Support has provided guidance on the audited part of the Remuneration Report [**paragraph 9**]	CIPFA/LASAAC has issued proposed revisions to the accounting code in respect of infrastructure assets [**paragraph 17**]
CIPFA has issued a draft bulletin on accounting for infrastructure assets in local government [**paragraph 24**]	Professional Support has issued a briefing on preparing IARs for 2021/22 [**paragraph 31**]	The Scottish Government has issued statutory guidance on disclosures where a local authority defers loans fund repayments [**paragraph 35**]
LASAAC has issued guidance on COVID-19 related grants in 2021/22. [**paragraph 39**]	CIPFA has issued guidance on 2021/22 financial statements [**paragraph 47**]	PWC has issued a report for auditors on IAS 19 reporting [**paragraph 60**]
Professional Support has published guidance on inspections and objections to 2021/22 local government annual accounts [**paragraph 66**]	The Scottish Government has guidance on the approval and publication dates for the 2021/22 annual accounts of local government bodies [**paragraph 69**]	The NAO has published a disclosure guide on the 2021/22 financial Statements [**paragraph 77**]
Professional Support has provided auditors with advice on issues arising from 2021/22 audits [**paragraph 81**]	The Scottish Government has issued health boards with revised accounts directions from 2021/22 [**paragraph 82**]	The Scottish Government has issued a letter on year-end arrangements for health boards in 2021/22 [**paragraph 86**]
Professional Support has issued an assurance report CNORIS for 2021/22 [**paragraph 92**]	The PAF has issued proposed revisions to PN 10 [**paragraph 94**]	BEIS has issued a response to its consultation on restoring trust in audit and corporate governance [**paragraph 98**]
The FRC has issued reports on its 2020/21 audit quality inspections [**paragraph 116**]	The FRC has issued proposed revisions to ISA (UK) 600 [**paragraph 119**]	The ISSB has issued draft standards on sustainability [**paragraphs 122 and 128**]

Contact point

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2: All sectors

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Guidance on 2020/21 WGA

1. HM Treasury has issued guidance on preparing the 2020/21 Whole of Government Accounts (WGA) for local government and for central government bodies. WGA is prepared by Treasury and consolidates bodies in the UK that exercise functions of a public nature or are funded from public money.

2. Data is collected for the 2020/21 WGA by bodies inputting information directly to the Online System for Central Accounting and Reporting (OSCAR II). Bodies are exempt from the WGA process if their gross expenditure, gross income, gross assets, and gross liabilities are below £30 million for both 2019/20 and 2020/21.

3. Paragraph 1.7.1 sets out the key dates for 2020/21 WGA as summarised in the following table:

Cycle	Return	Submission date
1	Unaudited	31 July
2	Audited	31 August

4. A diagram at paragraph 4.2.2 of the guidance sets out the steps involved in the WGA submission process. The steps depend on whether the body is above the audit threshold. Paragraph 1.7.2 advises that the threshold for audit is breached if any of total assets (excluding property, plant and equipment), total liabilities (less pension liabilities), total income or total expenditure is above £2 billion.

5. Although the guidance states that the deadlines and thresholds may be different in Scotland, the Scottish Government subsequently confirmed that they apply unchanged.

6. Annex A provides a summary of the proforma tabs used to input data. Chapter 7 provides more detailed guidance on inputting data into the tabs. Paragraph 7.2.7 explains that the Audit Report is a view of all data submitted which can be shared with auditors. It may be appropriate, as a new facility for 2020/21, to download the individual tabs instead, and also run the new primary financial statements report.

7. A key part of the WGA process is the elimination of transactions and balances between WGA bodies. Recording complete and accurate counter-party identifier (CPID) information is the only way in which transactions and balances between WGA bodies can be identified and eliminated. Paragraph

6.3.4 explains how bodies can run a Matches Analysis Tool which allows them to see ‘live’ published data from other bodies. Central government bodies are required to formally agree transaction streams and balances that are above £5 million with central government counterparties.

8. A TGN on the evaluation by auditors of the 2020/21 WGA submissions will be provided by Professional Support in due course.

Identification of audited part of Remuneration Report

9. Professional Support has identified that some audited bodies may not be clearly and accurately identifying the part of the Remuneration (and Staff) Report that is subject to audit. The following guidance is intended to assist in that regard.

10. For local government bodies, the Schedule to The Local Authority Accounts (Scotland) Regulations 2014 (accounts regulations) is the main reference source for the Remuneration Report. In summary:

- the items set out at paragraphs 4 to 12 of the Schedule are subject to audit
- the narrative information on remuneration arrangements required by paragraphs 2 and 3 are not audited.

11. In addition, The Trade Union (Facility Time Publication Requirements) Regulations 2017 require employers to publish information in relation to trade union facility time. Guidance from the Cabinet Office indicates that disclosure should be in the Remuneration Report. This information is not subject to audit.

12. The Code of Practice for Local Authority Accounting in the UK (accounting code) requires local authorities to disclose members' salaries, allowances and expenses. Some authorities choose to make the disclosure in the Remuneration Report while others include it as a note to the financial statements. Regardless of where it is disclosed, the information requires to be audited.

13. Finance Circular 8/2011 (paragraph 5) requires local authorities to clearly identify those parts of the Remuneration Report that are subject to audit, and provides illustrative wording. It should be noted that the wording:

- used in the unaudited financial statements should state that the information ‘will be audited’ but the tense should be updated to ‘has been audited’ in the audited financial statements
- needs to reflect that any disclosure of members' salaries, allowances and expenses requires to be audited.

14. For central government bodies and health boards, the requirements for a Remuneration and Staff Report are set out at section 6.5 of the FReM. Information subject to audit is set out at paragraphs 6.5.8 to 6.5.30, and 6.5.31 b) and l). The FReM requires bodies to clearly identify the information as audited. The part of the Remuneration Report that is audited is covered by the opinion on the Remuneration Report.

15. The items required by FReM paragraph 6.5.7 and the other elements of paragraph 6.5.31 are not audited. The unaudited part is statutory other information and should be treated and reported on accordingly.

16. Auditors should check that bodies have correctly and clearly identified the part of the Remuneration Report that is subject to audit, and request amendments where necessary.

3: Local government sector

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Proposed revisions to accounting code

17. The CIPFA/LASAAC Code Board has issued an Invitation to Comment (ITC) that sets out proposed revisions to the accounting code in respect of infrastructure assets.

18. The proposed revisions would apply on a temporary basis up to and including 2022/23, pending a longer-term solution. Responses were required by 14 June 2022.

19. The proposed temporary revisions are in response to issues relating to the derecognition of replaced parts of infrastructure assets. The specific issue is whether local authorities are assessing any undepreciated cost remaining in the replaced parts at the point the replacement parts are added. There are concerns that assessment may not be happening for infrastructure assets due to significant practical difficulties such as:

- it not generally being possible to identify parts of infrastructure assets as the engineering records were not designed to map against identifiable parts
- information on previous historical repairs not being available in a meaningful or identifiable way
- information deficits in relation to historical expenditure on assets created before 1994/95, which were measured on recognition at 'capital undischarged' rather than at historical cost
- issues where assets have been transferred to local authorities on reorganisation.

20. The ITC proposes a temporary adaptation to IAS 16 Property, Plant and Equipment to the effect that it is reasonable to assume that the net book value of replaced parts of infrastructure assets is zero. This is on the basis that parts are rarely replaced before they are fully consumed.

21. The adaptation, however, does not address the overstatement of gross book value and accumulated depreciation of infrastructure assets caused by the failure to derecognise the cost and accumulated depreciation of replaced parts. A second temporary adaptation to IAS 16 is proposed therefore to remove the requirement for those amounts to be disclosed in the financial statements. This is considered to be justified on the basis that this information is not useful to users of the financial statements.

22. In light of the challenges of developing an effective depreciation policy for infrastructure assets, the ITC also proposes that the accounting code should provide guidance to assist in this area. There is a proposed interpretation indicating that it may be appropriate for the pattern of consumption of economic benefits to be reflected by means of weighted average useful lives of the different parts of the asset.

23. CIPFA/LASAAC is considering longer-term solutions to these issues and will consult on proposals in due course.

Draft bulletin on infrastructure assets

24. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued a draft bulletin which is intended to accompany the proposed changes to the accounting code in relation to infrastructure assets. Responses were also required by 14 June 2022.

25. Section 2 of the draft bulletin is on materiality and is intended to help local authorities in making estimations. It advises authorities to consider the information which will be useful to the users of the financial statements for taking economic decisions. Paragraph 31 states that, although the cost of infrastructure assets will be material, for most authorities the incomplete data held on infrastructure assets will limit the usefulness of the figures.

26. Paragraph 34 expands on the proposed adaptation that the net book value of replaced parts of infrastructure assets may be zero. Local authorities have generally applied the accounting code in such a way that, where expenditure has taken place to replace a part of the infrastructure assets, the carrying amount of the replaced part of the asset derecognised is in effect derecognised at a zero amount. This is consistent with the approach that authorities only replace parts of infrastructure assets when they have been fully consumed.

27. If applied by a local authority, the proposed adaptation will need to be carefully reported in the accounting policies. This will need to:

- set out the measurement base for infrastructure assets and the changes in place as a result of the temporary changes to the accounting code
- note the adaptation for derecognition when replacement/renewals expenditure has taken place, except where there has been a disposal of a part of the infrastructure
- reflect accounting policies which effectively measure the consumption pattern of the economic benefits of the parts of the infrastructure asset
- note that gross historical cost or accumulated depreciation has not been reported (where the authority uses that option).

28. An illustrative accounting policy is included in Annex A to the draft bulletin.

29. Section 5 provides guidance on the depreciation of infrastructure assets to support the proposal for a weighted average useful life approach. Determining the depreciation charge for infrastructure assets is difficult as these take the form of a network of assets where there are many different components working as a part of a continuous network maintained in a relatively steady state.

30. The bulletin states that it would be reasonable to use the parts of the network which were defined in the Code of Practice on the Highways Network Asset, i.e., carriageways, footways and cycle tracks, structures, street lighting, street furniture and traffic management systems. The methodology set out in sections 5.2 to 5.8 of the draft bulletin illustrates how weighted averages might be calculated for each. They provide examples where the local authority has information on gross historical cost for different parts of the highways network, or may be able to estimate it on a reasonable basis.

Learning points for 2021/22 IARs

31. Professional Support has issued a briefing* to set out learning points for auditors when preparing Independent Auditors' Report (IARs) for 2021/22. The points arose from a review of the 2020/21 IARs of local authorities which evaluated compliance with the model forms of IAR and auditor actions set out in TGN 2021/5(LG).

32. A summary of findings is provided at section 1 of the briefing with specific areas for improvement highlighted at section 2. The review found a very good level of compliance with the auditor actions set out in the TGN. However, two significant areas for improvement were identified by the review:

- At one local authority, the auditor did not use the wording specified to explain the extent to which the audit is considered capable of detecting irregularities including fraud.
- At another authority, the auditor failed to report that a significant trading operation had failed to meet the prescribed financial objective.

33. The review also identified other issues where it may not have been clear to users what statements had been audited. For example, in half of IARs auditors did not:

- use the precise titles of the financial statements used by the local authority
- ensure that the local authority had properly described the parts of the Remuneration Report that had been audited.

34. Auditors should ensure the areas for improvement are addressed for their IARs in 2021/22.

New statutory Guidance on deferring loans fund repayments

35. The Scottish Government has issued Finance Circular 5/2022 which provides statutory guidance that sets out disclosure requirements where a local authority defers loans fund repayments.

36. Technical Bulletin 2022/1 (paragraph 20) highlighted that The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 had been amended to permit a local authority to reduce the statutory repayments of loans fund advances in any one of the financial years 2020/21, 2021/22 or 2022/23. If an authority adopts that option, repayment of the reduced amount requires to be repaid within the shorter of:

- the remaining period of the loans fund advance
- twenty years.

37. The statutory guidance requires a local authority to disclose in a note to the financial statements:

- the amount of the repayment that has been deferred. This should be disclosed in the year of deferral, but any deferral in 2020/21 should be disclosed in 2021/22.
- the term over which the deferred repayments will be repaid.

38. Where a local authority deferred loans fund repayment in either 2020/21 or 2021/22, auditors should evaluate whether the disclosures required by the statutory guidance have been properly made in the 2021/22 financial statements.

2021/22 guidance on accounting for COVID-19 grants

39. The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) has issued guidance on the classification between agency and principal for COVID-19 related grants in 2021/22.

40. Appendix 1 of the guidance includes an assessment of the appropriate classification to inform the judgements of local authorities and integration joint boards (IJBs). The guidance advises that local authorities should apply Appendix 1 on a ‘comply or explain’ basis.

41. In Professional Support’s view, a ‘comply or explain’ basis means that any local authority that does not follow the classification in Appendix 1 should disclose that fact and the reason why in a note to the financial statements. Professional Support also considers that the same basis should apply to IJBs for consistency.

42. Appendix 1 advises that local authorities are the principal for most funding stream elements of General Revenue Grant (GRG) in Finance Circulars 5/2021 and 1/2022. However, the following two elements of GRG should be classified as agency transactions because the Scottish Government set the amounts and criteria for payment:

- Low Income Pandemic Payments
- Scottish Child Payment Bridging Payments.

43. Local authorities act as agents for the Scottish Government for most specific COVID-related grants. The details for these are set out in various letters from the Scottish Government.

44. As with the guidance for 2020/21, local authorities are considered to be acting as agents when making the £500 payments to health and social care staff, including to their own staff.

45. Appendix 1 advises that IJBs, with the exception of hospice funding, are usually the principal for COVID funding. This classification includes supplier sustainability payments to social care providers as IJBs have a significant degree of discretion.

46. Auditors should evaluate whether:

- local authorities have appropriately classified COVID-19 related grants in 2021/22 between those where the authority is acting as the agent of the Scottish Government and those where the authority is the principal in the transaction
- and explanation has been disclosed where the authority's classification differs from that set out at Appendix 1 of the guidance.

Guidance on 2021/22 financial statements

47. CIPFA has issued Bulletin 10 which provides guidance on the 2021/22 financial statements. The guidance is intended to be best practice, but it does not have the formal status of the accounting code.

48. The following items in the guidance are relevant to Scottish local government:

- Adoption of IFRS 16 Leases before 2024/25
- Valuation of operational property assets
- Critical judgements and estimation uncertainty
- Financial reporting deadlines for 2021/22
- Working papers
- Accounting standards issued but not yet adopted
- Accruals for pay awards in 2021/22
- Infrastructure assets.

Adoption of IFRS 16 before 2024/25

49. Section 1 of the bulletin refers to the latest statement from CIPFA/LASAAC on its decision to defer the mandatory implementation of IFRS 16 until 1 April 2024 (and therefore in the 2024/25 accounting code).

50. However, the accounting code will allow for adoption before 2024/25. The bulletin provides guidance for authorities intending to adopt the standard in 2022/23. Those authorities should:

- advise CIPFA of their intention to adopt (paragraph 1.4)
- disclose IFRS 16 in 2021/22 as a standard issued but not yet adopted (paragraph 1.5)
- follow the provisions for adoption before 2024/25 that will shortly be set out in the 2022/23 accounting code (paragraph 1.7).

Valuation of operational property assets

51. Section 2 of the bulletin reminds local authorities of the key requirements of the accounting code in respect of the valuation of operational property. These include the following:

- The accounting code requires revaluations to be made with sufficient regularity to ensure that the carrying amount of an asset does not differ materially from current value (paragraph 2.2).
- Local authorities need to determine a valuation frequency for operational property based on the expected significance and volatility of changes in current value The accounting code sets five years as the maximum interval between formal valuations. However, where a property experiences significant and volatile changes in current value, an annual revaluation is required (paragraphs 2.3 to 2.5).
- Where a local authority uses 1 April 2021 as the valuation date for 2021/22, the authority needs to consider any movements in value during the year that should be reflected in the 31 March 2022 carrying amount. Where a valuation has been carried out as at 1 April 2022, local authorities should consider this an adjusting event in 2021/22 on the basis that it provides evidence of conditions that existed at 31 March 2022 (paragraph 2.6).

Critical judgements and estimation uncertainty

52. Section 3 provides good practice guidance on meeting the requirements of the accounting code for disclosing critical judgements and sources of estimation uncertainty.

53. Key aspects of the guidance include the following:

- The following two separate notes are required:
  - one that details the decisions taken (i.e. judgements) in applying accounting policies
  - a second note that sets out the assumptions made in calculating estimates that have the greatest risk of being materially incorrect in the next 12 months.

- Only the most significant judgements require to be disclosed (paragraph 3.8), e.g:
  - where the matter was complicated
  - a different conclusion would have resulted in a material difference in the financial statements; and
  - the final assessment finely balanced.
- Judgements not to take action also need to be covered, e.g. a decision that group accounts are not required where they could reasonably be expected (paragraph 3.9).
- Disclosure is only required in relation to assumptions that have a significant risk of resulting in material adjustments to the estimate in the next financial year, not to all assumptions that involve material balances of assets or liabilities (paragraph 3.14).
- The estimates note does not cover those that are not based on attempting to see into the future. For example, estimates that are made for reasons of efficiency (e.g. property valuations using beacon principles) are excluded (paragraph 3.15).

Working papers

54. Section 13 highlights that some local authorities have diverted staff resources away from completing working papers and preparing the financial statements, while the quality of processes within the finance functions has affected their preparedness for audit.

55. The bulletin reminds authorities of the recent CIPFA guidance on streamlining the annual accounts, which includes advice on preparing good quality working papers. Paragraph 13.4 of the bulletin provides a summary of the advice, which includes the following points:

- Spreadsheets, ledger reports and journal postings are unlikely to be sufficient without additional explanations of where the information has come from and what the preparer was trying to achieve.
- All working papers should be internally consistent and agree with the amounts in the financial statements submitted for audit.
- Reconciling items, mis-postings and suspense account items should all be resolved pre-audit.

Accounting standards issued but not yet adopted

56. Paragraph 15.3 lists the following standards introduced by the 2022/23 accounting code which may require to be disclosed in 2021/22 as standards issued but not yet adopted:

- IFRS 16 (for those authorities planning on a 2022/23 adoption).

- Annual Improvements to IFRS Standards 2018-2020, but it is not expected that any of the improvements will have a significant effect on a local authority’s financial statements.
- An amendment to IAS 16 which prohibits an entity from deducting from the cost of property, plant and equipment amounts received from selling items produced while the asset is under construction.

Accruals for pay awards in 2021/22

57. Paragraph 16.1 confirms that any amounts unpaid at 31 March 2022 in relation to agreed pay awards for the 2021/22 year will need to be accrued in the 2021/22 financial statements.

58. Paragraph 16.2 clarifies that the accrual should include employers’ on-cost (i.e. employers’ national insurance contributions and employers’ pension contributions).

Infrastructure assets

59. Section 17 of the bulletin refers to the derecognition of parts of infrastructure assets described earlier in this section. Paragraph 17.8 of the bulletin encourages local authorities to:

- consider in detail the financial information they hold on their infrastructure assets
- ensure they have an effective depreciation policy for those assets.

2021/22 report on actuarial information

60. Professional Support has arranged for PWC to provide a report* to support auditors when assessing the competence and objectivity of, and assumptions and approach adopted by, actuaries producing information required by IAS 19 figures in respect of the Local Government Pension scheme (LGPS) as at 31 March 2022. Auditors should refer to paragraphs 15 to 27 in Module 4 of TGN 2021/8(LG) for guidance on using the report and further information.

61. PWC have confirmed the competence and objectivity of the actuaries involved in valuations for the LGPS in Scotland. They are also comfortable that in aggregate the assumptions adopted by all actuaries will lead to liabilities falling within their expected ranges for a typical employer at 31 March 2022.

62. However, the report advises auditors to consider whether:

- local issues have been adequately covered in instructions issued by employers to actuaries (page 3)
- to subject the source data provided to the actuaries by employers to further audit procedures as discussed in section 4 of the report

- to establish actual asset returns and compare them with expected returns arrived at using market indices (see page 22).

63. Page 17 of the report addresses accounting for plan amendments, curtailments, and settlements (special events) under IAS 19. Auditors need to understand whether any significant special events have occurred, and whether profit and loss items have been remeasured from the date of the event for the remainder of the accounting period. This entails remeasuring both the assets and liabilities using assumptions set at this date. The report confirms that all actuaries are aware of the IAS 19 requirement.

64. Page 18 of the report provides an update on Guaranteed Minimum Pension (GMP) indexation and equalisation, the McCloud judgement and other legal cases. In summary:

- There have been no relevant developments related to GMP and all actuaries are following an approach in 2021/22 consistent with 2020/21
- The only relevant development in respect of McCloud was confirmation that the remedy set out in the consultation paper would be adopted. The actuaries had followed the consultation in making adjustments in 2020/21, and therefore no further change is required.
- Actuaries do not intend making any specific allowance for the Goodwin, O'Brien or similar cases, unless requested to do so.

65. Page 19 highlights the issue of pay awards that have been backdated to 1 January 2021. If the backdated pay award has been paid before 31 March 2022, it may affect the following three areas:

- Auditors need to consider any actions where contribution figures for February and March are based on estimated figures, as the overall contribution figure could be understated if they do not include the backdated pay award.
- Similarly, auditors need to consider whether pensionable pay figures are based on estimated figures
- Although there may be an impact on past service final salary benefits and the McCloud allowance, actuaries do not ordinarily allow for salary experience differences between triennial valuations. Any impact will therefore come through when the IAS 19 figures are based on a new triennial valuation as at 31 March 2024.

Guidance on objections to 2020/21 annual accounts

66. Professional Support has published TGN 2022/3(LG) to provide auditors with guidance on the right of an interested person under section 101 of the Local Government (Scotland) Act 1973 to:

- inspect the unaudited 2021/22 annual accounts of a local government body

- object to those accounts.

67. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

68. Auditors should:

- evaluate whether the public inspection notice for 2021/22 is in accordance with applicable legislation
- carry out the actions set out in the TGN for any objections received.

Guidance on 2021/22 accounts approval and publication dates

69. The Scottish Government has issued Finance Circular 6/2022 to provide guidance on the extension to the approval and publication dates for the 2021/22 annual accounts of local government bodies due to the amendments to the accounts regulations (explained at paragraph 20 of Technical Bulletin 2022/1).

70. In summary, the dates have been amended as follows:

- Regulation 10(1) requires a local authority to aim to approve the audited annual accounts no later than 30 November 2022 (deferred from 30 September)
- Regulation 11(3) requires the approved audited annual accounts to be published no later than 15 December 2022 (deferred from 31 October)

71. The circular confirms that there is no date set in the regulations for audit completion but reiterates that Audit Scotland has set a completion date of 31 October 2022 for 2021/22 audits. This is earlier than the extended statutory deadline to commence the transition back to regular timescales.

2021/22 NDR return and guidance

72. The Scottish Government has issued the 2021/22 Non-domestic rates notified return and guidance*. The most significant changes for 2021/22 are summarised in the following table:

Line	Relief	Change
N/A	General relief	The general relief that was introduced in 2020/21 has been removed.
	Subsidy control	State Aid is now Subsidy Control and the cap on the aggregate amount that can be awarded in specified non-domestic rates relief is 325,000 Special Drawing Rights (which are units of account maintained by the International Monetary Fund).
8	Fresh start relief	The threshold has increased to £95,000 (from £65,000).

Line	Relief	Change
16	District heating relief	A new relief of 90% has been introduced for premises used for a district heating network installed on or after 1 April 2021 powered by renewables
21 to 22	Business growth accelerator relief	The relief is now available where there is an increase in rateable value due to a change in the way the property is being used.
27	Retail, hospitality, leisure and airport relief	An application is required for 2021/22
30 to 31a	Sports club discretionary relief	A new requirement that the relief supports affordable community-based facilities, rather than members' clubs with significant assets.

73. Professional Support has published TGN/NDR/22 on certifying the 2021/22 non-domestic rates return. The TGN is provided with supporting material to auditors on SharePoint* and also on the Audit Scotland website.

74. Auditors should certify 2021/22 NDR returns using TGN/NDR/22.

Housing benefit subsidy

75. The Department for Work and Pensions (DWP) has issued the following modules of the Housing Benefit Assurance Process (HBAP):

- Module 2* uprating checklist to help auditors ensure that the authority's system is using the correct benefit parameters to calculate benefit entitlement and for the authority to claim the correct amount of subsidy.
- Module 3* comprising workbooks to be completed for detailed testing.

76. Professional Support has been discussing with the DWP changes to the testing required for the certification of the subsidy claim. This has delayed the production of the TGN. The DWP submission deadline for the HB subsidy certification is 31 January 2023.

4: Central government sector

Contact: Neil Cameron, Ncameron@audit-scotland.gov.uk

Disclosure guide for 201/22 financial statements

77. The National Audit Office has published a disclosure guide on the 2021/22 financial Statements for bodies covered by the Government Financial Reporting Manual (FReM).

78. The guide is designed to ensure that bodies covered by the FReM have prepared their 2021/22 financial statements in the appropriate form and have complied with all disclosure requirements. The guide is cross-referenced to the 2021/22 FReM, individual financial reporting standards, and the Companies Act 2006. A tailored checklist can be generated by selecting the criteria that are material to the body.

79. When checking that the FReM's disclosure requirements have been met, auditors should in accordance with the Overview Module of TGN 2022/1:

- consider requesting that the body completes the disclosure checklist
- investigate the reasons for any non-compliance that the guide highlights
- evaluate whether the body's responses in the checklist are consistent with auditor's knowledge.

Amendments to SPFM

80. The Scottish Government has issued Finance Guidance Note 2022/02 to announce amendments to the borrowing, lending and investment chapter in the Scottish Public Finance Manual (SPFM). The guidance in respect of investment in private businesses by Scottish Ministers contained in Annex A has been strengthened based on recent experience of interventions in private companies. The amendments include:

- outlining the overarching principles which any investment proposal should take into account. Any proposal must be contingent upon the completion of satisfactory due diligence and demonstrate a clear policy rationale
- additional guidance on commercial risk and the importance of considering individual transaction risk
- more prescriptive language where appropriate, balanced against the aspects of the framework that are principles-based.

Technical consultations with auditors

Professional Support responds to requests from auditors for technical consultations

81. The following tables summarise requests from auditors for technical consultations with Professional Support in respect of issues arising from the audit of the 2021/22 annual accounts of central government bodies, along with the advice offered:

How should a negative pension benefit be treated in a director's total remuneration figure? How should any negative components in the pension benefit calculation be treated?

The increase in value of pension benefit is a component of the total remuneration figure. The FReM requires bodies to use the methodology for calculating remuneration set out in the relevant Employer Pension Notice (EPN). EPN 647 provides an explanation of where an increase could be negative and states that the scheme administrator will explain the reasons where that is the case. The EPN is silent on whether the negative pension element should be included in remuneration in the relevant column in the remuneration table or be replaced with a zero. However, the FReM's requirements are based on The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 which explicitly require that, where calculations (other than in respect of a recovery or withholding) result in a negative value, the result should be expressed as zero in the relevant column in the remuneration table. Professional Support would therefore expect central government bodies to adopt the same treatment but there does not appear to be an explicit requirement to do so.

This approach would be consistent with health boards because, as advised in Module 13 of TGN 2022/1, the accounts manual explicitly requires health boards to express a negative pension benefit as a zero.

The replacement of a negative value with a zero applies only to the calculated result and not to individual components of the calculation. For example, if the real increase in lump sum is negative, that amount should be netted off the real increase in pension in the calculation.

In the fair pay disclosures, what is the difference in principle between (1) the average percentage change in employee salary and allowances and (2) the change in median pay ratio?

The median pay relates to the individual in the middle of the pay range for the body. The median pay ratio is the remuneration of the highest paid director relative to the median pay. Bodies are required by the FReM to make various disclosures, including the change in the median pay ratio since the previous year.

The average percentage change in employee salary and allowances is the total for all employees on an annualised basis (excluding the highest paid director) divided by the FTE number of employees (excluding the highest paid director). This is a new disclosure for 2021/22.

Should payments made in lieu of notice be included in the disclosure of exit packages?

Exit packages for the purposes of disclosure in the annual accounts relate to an individual ceasing to be an employee of a public body in exchange for compensation which requires the agreement of the body. This includes:

- settlement agreements (used to settle an employment dispute)
- voluntary severance (used where the post or skills no longer exist following a restructuring and redeployment is problematic).

The costs associated with an exit package relate to payments that are contractual (those which would be received in the normal course of employment) and non-contractual (those offered on a discretionary basis). It is expected that payment in lieu of notice would be a contractual payment. However, the SPFM expects that notice should be worked by the individual rather than a payment being made in lieu of notice. Where, exceptionally, payment in lieu of notice is made in respect of an agreed exit package, it should be included in the disclosure.

There is no requirement to disclose exit packages which do not require the agreement of the public body (such as where a person exercises a contractual right to leave employment on the grounds of ill health). Any payment in lieu of notice associated with such exit packages does not therefore require to be disclosed.

5: Health sector

Contact: Neil Cameron, Ncameron@audit-scotland.gov.uk

Revised accounts direction from 2021/22

82. The Scottish Government has issued health boards with a revised account directions which applies with effect from the 2021/22 annual report and accounts.

83. The revised direction includes specific reference to the Manual for the Annual Report and Accounts of NHS Boards, Capital Accounting Manual and the SPFM. This replaces the more general reference (to the accounts format, disclosure and accounting requirements issued by the Scottish Ministers) included in previous directions. There is, however, no change to the financial reporting framework.

84. The direction also states that boards are required to use the accounts template when preparing their accounts. However, a subsequent letter from the Scottish Government (see following item) clarifies that the requirement applies only to the Scottish Government Consolidated Accounts. Boards are still able to produce their published accounts in a different format, but they must submit the completed accounts template to the Scottish Government for consolidation purposes. Auditors are still required to complete an assurance statement stating whether the completed templates are consistent with the audited accounts.

85. The direction is required to be included in the published annual accounts. Auditors should confirm that boards include the revised version of the direction in 2021/22.

Guidance on 2021/22 arrangements

86. The Scottish Government has issued a letter* on the year-end arrangements for the 2021/22 annual report and accounts. The letter is intended to clarify certain aspects of the process.

87. The letter advises that it is too early to determine the potential implications of the legal ruling on discharging untested COVID-19 patients into care homes. Therefore, the Scottish Government do not believe that boards should be making any specific disclosures in relation to this matter in 2021/22.

88. The letter clarifies that:

- the threshold for the agreement of balances with other NHS Scotland bodies is £200,000 rather than the £100,000 specified in the accounts manual

- income from donated assets is no longer disclosed in note 7d and is instead disclosed in note 2a Summary of Revenue Outturn. The template also includes this change in the prior year comparators. This will impact on the 2020/21 capital outturn for boards that received donated assets in 2020/21. The letter provides a suggested explanatory footnote for boards affected.

89. As stated in the previous item, the letter also explains that the reference in the revised accounts direction to boards being required to use the accounts templates applies only to the Scottish Government Consolidated Accounts.

Accounting for PPE and testing kits

90. NHS National Services Scotland (NSS) has provided health boards with estimates of the notional costs of personal protective equipment (PPE) and testing kits provided free of charge in 2021/22. This includes equipment supplied by the Scottish Government but also includes equipment from the UK Government, which should be recognised as a donation. The accounting entails recognising a non-cash grant at fair value and an equivalent amount of notional expenditure.

91. The auditor of NSS has reviewed the methodology used to arrive at the estimates provided to boards and concluded that the allocations are reasonable.

Assurance report on 2021/22 clinical negligence claims

92. Professional Support has issued a report to auditors following an examination of the Clinical Negligence and Other Risks Indemnity Scheme (CNORIS). The purpose of the report is to:

- provide assurance on the methodology used by the Scottish Government in the calculation of the CNORIS national obligation at 31 March 2022
- inform auditors' evaluation of the role of the NHS Central Legal Office as a management expert.

93. Auditors should refer to this report when auditing the 2021/22 provisions for CNORIS.

6. Professional developments

Proposed revisions to PN 10

94. The Public Audit Forum has issued an exposure draft of proposed revisions to Practice Note 10 Audit of Financial Statements and Regularity of Public Sector Bodies in the UK (PN 10).

95. Part 1 of PN 10 sets out how auditors of public sector bodies apply auditing standards to their work on financial statements. The aim is to support consistency in the application of auditing standards while also recognising the specific legislative and regulatory frameworks that apply to the audits of public sector bodies. Part 2 provides guidance on the approach to the audit of regularity.

96. PN 10 was last revised in 2020 and there is a need to ensure it is updated to take account of changes to standards and other developments in the auditing profession. Comments on the consultation should be sent to PracticeNote10@public-audit-forum.org.uk by 16 September.

97. The main proposed changes are summarised in the following table:

Section	Pages	Summary of proposed revisions
ISQM (UK) 1	14 - 20	There are revisions to existing material on ISQC 1 to reflect its replacement by ISQM 1 in respect of systems of quality management. Most of the proposed changes apply to contracted out audits and therefore do not apply in Scotland (which uses an appointments basis). Revisions that apply in Scotland are the following: • Paragraph 1-23 has been added to advise that public sector auditors may determine that an engagement quality review is appropriate for bodies judged to have a high public profile. • Paragraph 1-27 has been added to explain that the individual assigned operational responsibility for the system of quality management in the national audit agencies may not be eligible for appointment as a statutory auditor under the Companies Act 2006. However, the national audit agencies comply with ISQM (UK) 1 by ensuring that the individuals have levels of experience, knowledge, influence and authority such that they are capable of fulfilling the role of engagement partner as defined in auditing standards. This is considered to be equivalent to the levels required to achieve eligibility for appointment as a statutory auditor.

Section	Pages	Summary of proposed revisions
ISA (UK) 240	22 - 25	Paragraphs 1-40 to 1-44 have been added to provide guidance on the interaction between fraud and regularity responsibilities. This includes the following points: • The public sector auditor's responsibilities relating to fraud under ISA (UK) 240 are interrelated with the work that underpins the regularity opinion. However, the audit of regularity is not in itself sufficient to provide reasonable assurance about whether the financial statements as a whole are free from material misstatement due to fraud. • The term 'irregularities' refers to instances of non-compliance with laws and regulations, including fraud. In the context of the regularity opinion, the term 'irregular transactions' refers to transactions not in accordance with the framework of authorities. • An irregular transaction may not be an irregularity (e.g. a breach of spending controls may not be unlawful). However, it is likely that transactions relating to an 'irregularity' would also be irregular transactions for the purpose of the regularity opinion. • Even where fraud does not result in misstatement of the financial statements, it may result in transactions that are not in accordance with the framework of authorities. The public sector auditor's responsibilities under ISA (UK) 240 in respect of reporting fraud or suspected fraud extend to such cases.
ISA (UK) 315	29 - 33	There are various proposed revisions to reflect the July 2020 revision of ISA (UK) 315. Key changes include the following: • Paragraph 1-73 explains that ownership of a public body may not have the same relevance as in the private sector because decisions related to the body may be made outside of the body as a result of political processes. Relevant matters include understanding the ability of the body to make unilateral decisions and the ability of other public sector bodies to control or influence it. • Paragraph 1-79 has been added to provide examples of inherent risk factors that may be particularly relevant to public bodies under the categories of inherent risk factors of complexity, subjectivity, change, uncertainty and management bias. • The guidance in paragraph 1-80 on the situation where public bodies are required to work to annual limits on resources has been extended. It explains that the risk of transactions being recorded in the wrong accounting period is increased due to an incentive for an entity to bring forward or delay expenditure or capital additions depending on its expected outturn against these limits. The risk of misclassification is also increased as there is an incentive to recognise items in a manner that increases outturn against limits that are underspent and reduces outturn against limits that are overspent.

Section	Pages	Summary of proposed revisions
ISA (UK) 320	34 - 35	Existing guidance at paragraphs 1-87 and 1-88 has been expanded including providing further examples for determining materiality in the public sector. Key points include: • Attention has been drawn to paragraph A20 of ISA (UK) 450 which highlights circumstances where misclassifications between balance sheet items that do not affect the performance statement may not be considered material. • In some public sector bodies, the value of gross assets and/or liabilities is much higher than the value of total expenditure and income. Where the audited body has custody of significant public assets, their service potential is an important contributor to the body's ability to deliver its services, which may make them an appropriate benchmark for setting materiality for the financial statements as a whole. • Example 5 has been added on setting materiality where the audited body's accounts include high-value property, plant and equipment, but its day-to-day decision making focuses on much lower-value expenditure and income transaction streams. Auditors may determine materiality for the financial statements as a whole using gross assets as a benchmark and also determine a lower materiality level to be applied to transaction streams.
ISA (UK) 570	46 - 56	The following additional clarification has been added for bodies where the financial reporting framework provides for the adoption of the going concern basis due to the anticipated continuation of the provision of a service in the future: • Paragraph 1-156 explains that the factor relevant to the auditor's work on going concern is whether the services will continue rather than the continued existence of the audited body itself. • Paragraph 1-162 clarifies that uncertainty regarding the future existence of the audited body does not create a material uncertainty, provided that this uncertainty does not also extend to the future delivery of the services.
ISA (UK) 600	57 - 59	Paragraph 1-195 has been added to provide guidance on cases where those charged with governance is unclear. It advises that those charged with governance are the persons or organisations with responsibility for overseeing the financial reporting process relating to the combined financial statements. This group may have responsibility for overseeing the strategic direction and obligations related to the accountability of the sector to which the financial information included in the combined financial statements relates.

Section	Pages	Summary of proposed revisions
Revised Ethical Standard	66 - 68	A new section has been added (paragraphs 1-227 to 1-233) on applying the revise ethical standard to the public sector. For example, paragraph 1-232 explains that in the public sector it may not be possible to comply strictly with the engagement partner rotation requirements envisaged for listed entities. Nonetheless it may be in the public interest for public sector organisations to establish policies and procedures to promote compliance with the spirit of rotation of engagement partner responsibility
Materiality for the audit of regularity	77 - 78	Paragraph 2.34A has been added to provide examples of situations when auditors may determine a materiality threshold for the audit of regularity that is different to that determined for the financial statements as a whole. These include where: • the audited body makes payments to individuals or other bodies that are of significantly greater public interest than the administrative functions of the body itself • the benchmark used to determine materiality for the financial statements as a whole has increased significantly but there remains user interest in the regularity of transactions at a more granular level • aspects of the audited body's framework of authorities and/or regulatory oversight regime indicate that quantitatively small non-compliance with the framework of authorities would be perceived more seriously than from assessing the amounts against materiality for the financial statements as a whole • the benchmark used to determine materiality for the financial statements as a whole is based on assets or liabilities and these amounts are out of proportion to the expenditure and income transactions that are subject to the regularity opinion.

BEIS response on restoring trust in audit consultation

98. The Department for Business Energy and Industrial Strategy (BEIS) has issued a response to its consultation on restoring trust in audit and corporate governance (explained in Technical Bulletin 2021/1 – paragraph 75).

99. The response does not set out a timetable for implementing the proposals, but rather outlines the actions to be taken, including what the UK Government intends to ask of the regulator and other stakeholders.

New regulator

100. Section 10 confirms the proposals to establish the Audit, Reporting and Governance Authority (ARGA) as a new regulator with the overarching objective to protect and promote the interests of investors, other users of corporate reporting and the wider public interest. ARGA's operational objectives will focus on quality, competition and acting as an effective 'system leader' for local public audit in England.

101. The reforms will give ARGA a range of statutory responsibilities and powers that the Financial Reporting Local authority does not have. These include:

- formalised responsibility for overseeing the accounting and actuarial professions
- a stronger role in auditor registration
- new powers to tackle breaches of company directors' duties relating to corporate reporting and audit.

102. Section 4 explains that ARGA will exercise oversight of corporate reporting to raise standards and improve the informativeness of company reports. For example, ARGA will be able to:

- direct changes to company reports and accounts
- publish summary findings following a review
- require or commission an expert review to support its corporate reporting review work
- review the entire contents of the annual report and accounts, including corporate governance statements and any voluntary reports.

Extension of PIE definition

103. Section 1.6 advises that the definition of public interest entities (PIEs) is to be extended to include large private companies which have both more than 750 employees and an annual turnover of more than £750 million. These size-based PIEs will not be required to meet all of the audit requirements as existing PIEs.

104. Public bodies such as local authorities will not become PIEs by virtue of this new size-based tests. However, those public bodies that are PIEs under existing legislation will continue to be so.

Internal controls and fraud prevention

105. The consultation proposed requiring directors to report on a company's internal controls and fraud-prevention measures, with auditors providing assurance on the latter.

106. However, section 2.1 of the response advises that the Government believes a more incremental approach to strengthening the internal control framework would be appropriate. It will therefore invite ARGA to strengthen the UK Corporate Governance Code to provide for an explicit directors' statement about the effectiveness of the company's internal controls and the basis for that assessment, and to develop appropriate guidance.

107. Section 6.2 explains that legislation will require directors of size-based PIEs to report on actions they have taken to prevent and detect fraud. Auditors will be required to fulfil the existing requirements of ISA (UK) 720 with respect to the directors' statements on fraud, and the Government considers that will be sufficient. Before considering further action, the Government intends to wait to see if the revisions to ISA (UK) 240 have the anticipated effect in clarifying what is expected of auditors in explaining the work they have done to detect fraud.

Improving the informativeness and quality of audit

108. Section 6.1 covers the proposals in respect of improving the informativeness and quality of audits. Consultation responses suggested that improvements to current auditing standards and practice are likely to be more effective and targeted than legislative changes. The Government will therefore look to ARGA to drive improvements in audit quality, including ARGA taking on responsibility for the registration of PIE auditors.

109. The Government supports the Brydon Review's long-term vision of expanding the future scope and purpose of audit. However, it believes that the first stage should be the development of a market for assuring financial and non-financial information beyond that in the financial statements. The Government does not propose to create a legislative framework for this market at such an early stage in its development.

110. The Government will not seek to establish a new professional body or regulatory oversight of a new 'corporate auditing' framework at this stage. Instead, the Government will create the conditions for the market to develop wider external assurance services. It will also ask professional bodies to improve auditor qualifications, skills, and training in order to help create a more effective and distinctive audit profession.

111. There are no plans for any legislative changes regarding the assurance of Alternative Performance Measures and Key Performance Indicators. It will be left to directors to decide whether specific assurance is necessary.

112. The current 'true and fair' view is to be retained as the standard for financial reporting. It is considered to be functionally identical to the alternative of 'presents fairly in all material respects'.

Resilience, competition, and choice in the audit market

113. To support ARGA's objectives to promote high-quality audit and effective competition in the audit market, the Government has decided to proceed with the proposed package of measures to improve resilience in the audit market for the largest companies. This includes the introduction of a 'managed shared audit' regime which will give challenger audit firms the opportunity to audit a meaningful proportion of subsidiary audits conducted for FTSE 350 companies. There will also be powers for ARGA to:

- operate a 'market share cap' once managed shared audit is in place
- require 'operational separation' of the largest firms
- monitor the health of audit firms and to address any concerns around an audit firm's resilience.

Monitoring audit quality

114. The consultation proposed to legislate for the publication of Audit Quality Review (AQR) reports. The aim was to allow the regulator to publish its AQR reports on individual audits without the need for consent from both the audit firm and the audited entity, as is the case at present.

115. Many respondents to the consultation highlighted problems with the publication of AQR reports without prior discussion. Rather than legislating specifically for the publication of AQR responses by the regulator, the Government is asking the regulator to look at non-legislative ways of improving the AQR process and continuing to seek consent from audit firms and audited entities where possible before publication. In addition, the Government is asking the regulator to engage with investors and other users to improve the usefulness to them of the information published on AQR.

Findings from quality inspections

116. The Financial Reporting Council (FRC) has issued a report on the key findings reported in the 2020/21 audit quality inspections of private sector audits. The inspections focus on:

- the quality of the audit work performed in the areas selected for review
- the sufficiency and appropriateness of the audit evidence obtained
- the appropriateness of the key audit judgments made by the audit partner and their team.

117. Some key findings that may have relevance to public sector audits are summarised in the following table:

Area	Finding
Compliance with laws and regulations	Where issues were identified, insufficient evidence was obtained to conclude on issues identified and whether they were isolated or representative of broader concerns
Bank reconciliation testing	The audit team did not investigate a net reconciling item in the period end bank reconciliation and therefore did not consider whether it was made up of significant offsetting items.
Pension scheme assets	The audit team performed insufficient procedures over the valuation and existence of pension scheme assets. In particular, the audit team did not: • obtain service organisation control reports for investment managers, to assess whether there were appropriate controls, before placing reliance upon their confirmations • in the absence of control reports, test the valuation of harder-to-value pension scheme assets • consider additional pricing information to assess and challenge the valuation of directly held publicly traded assets.

Area	Finding
Understanding and responding to inherent risks	The audit team did not demonstrate a sufficient understanding of the entity and the underlying controls in place to minimise the inherent business risks it faced.
Impairment of non-current assets	The audit team did not obtain sufficient evidence to assess whether an impairment of assets, or additional sensitivity disclosures, were required.
Fair value of financial instruments	Deficiencies were identified in the audit team's testing of financial instrument valuation, primarily the work performed over model risk management

118. The FRC also issued a separate report on good practices reported in the audit quality inspections. Some good practices that may have relevance to public sector audits are summarised in the following tables:

Risk assessment and planning

Area	Finding
First year audit procedures	The audit team's audit procedures supported a risk-based audit. There was comprehensive evidence of review of the predecessor auditor's working papers and of the audit of opening balances.
Fraud	The group instructions included a comprehensive section on entity-specific fraud risks, to be used as part of the component team's discussions. The group audit team tailored its scoping to respond to fraud risks, making good use of the business insights gained from management and the Audit Committee. It also incorporated elements of unpredictability into the audit procedures performed.
Journal entry testing	The journal entry testing across the group was thorough and well-controlled, with the detailed selection criteria communicated as required procedures to the component audit teams.
IT general controls	The audit team planned and scoped their testing of IT general controls from both a bottom-up and top-down perspective, to ensure that all relevant applications were covered. Their plan also reconciled the scope for the current year to the prior year to confirm completeness.

Execution

Area	Finding
Other information	The audit team evidenced a clear and thorough review of the other information included in the annual report, particularly whether it was fair, balanced and understandable.

Area	Finding
Areas requiring a high level of judgement	The audit team's approach to areas requiring a high level of judgement and industry knowledge involved robust challenge of key management assumptions, including effectively utilising the firm's technical team and internal specialists.
Extent of scepticism and challenge of management	The audit team presented its audit approach and findings in a way which clearly demonstrated the effective exercise of professional scepticism and consequent challenge of management in respect of key audit areas.
Valuation of assets	The audit team prepared a comprehensive memorandum evidencing its challenge of management's key assumptions used in their impairment model.
Impact of climate change	The audit team prepared a detailed memorandum evidencing consideration of the potential impacts of climate change. This enabled the team to ensure that all relevant disclosures were included in the financial statements, and informed specific aspects of the audit testing (for example, the testing of the valuation of assets).

Completion and reporting

Area	Finding
Communications with the Audit Committee	The use of graphics in the reports to the Audit Committee, notably in relation to the valuation of assets, aided the communication of complex issues which required the exercise of significant judgement.
Correction of identified errors	The audit team identified a significant number of material errors in the financial statements, and asked management to re-perform certain key assessments.
Review of the financial statements	Documentation clearly demonstrated the extent of the audit team's review of the financial statements and how points were resolved.
Other information	The audit team prepared a comprehensive work paper for narrative disclosures, annotated with testing performed and referenced to supporting evidence.
Delaying the signing of the auditor's report	The audit partner delayed signing their report until certain audit evidence was obtained. Furthermore, there was robust reporting to the Audit Committee in relation to difficulties during the audit.

Proposed revisions to ISA on group financial statements

119. The FRC has issued proposed revisions to ISA (UK) 600 on the audit of group financial statements. The proposals reflect recent changes to the corresponding international standard made by the International Auditing and Assurance Standards Board, as well as proposed additional material to address specific UK requirements. Comments require to be sent to AAT@frc.org.uk by 8 July 2022.

120. The revisions arising from changes in the international standard include:

- clarifying the scope and applicability of the standard
- reinforcing that all ISAs are to be applied in group audits
- focusing the group audit team's attention on the identification and assessment of risk at the group financial statement level and emphasising the importance of designing and performing appropriate procedures to respond to those risks
- reinforcing the need for robust communication and interactions between the group audit team, group audit partner and component auditors.

121. The proposed additional UK material clarifies:

- the relationship between the audit team, group auditor and component auditor (diagram at paragraph 14(h))
- the group audit partner has overall responsibility for compliance with ISAs and for ensuring that the auditor's report is appropriate, and for the design, implementation, and operation of a system of quality management (paragraph 16-1)
- the group audit partner is required to obtain confirmation from the component auditors that:
  – they are able to comply with the FRC Ethical Standard requirements (paragraph 25(b))
  – the ethical requirements have been fulfilled (paragraph 25-1).

Draft standard on disclosing sustainability-related financial information

122. The International Sustainability Standards Board (ISSB) has issued an exposure draft of a standard intended to set out general requirements for the disclosure of sustainability-related financial information.

123. The proposals in the exposure draft set out overall requirements for disclosing a complete set of sustainability-related financial information. Comments require to be sent to commentletters@ifrs.org by 29 July 2022.

124. The exposure draft sets out the objective of disclosing sustainability-related financial information that is useful to the assessment by the primary users of the financial statements of the entity's enterprise value and their decision whether to provide resources to it. The proposals would require an entity to disclose material information about all of the significant sustainability-related risks and opportunities to which it is exposed, even if such risks and opportunities are not addressed by a specific IFRS Sustainability Disclosure Standard.

125. The proposed definition of sustainability-related financial information is information that gives insight into sustainability-related risks and opportunities that affect enterprise value, and which provides a basis to assess the resources and relationships on which an entity's business model and strategy for sustaining and developing that model depend.

126. Sustainability-related financial information should therefore:

- include information about the entity's governance of, and strategy for, addressing sustainability-related risks and opportunities
- depict the reputation, performance and prospects of the entity as a consequence of actions it has undertaken.

127. The exposure draft also proposes that:

- disclosures should provide a fair presentation of an entity's sustainability-related risks and opportunities. Applying IFRS Sustainability Disclosure Standards, with additional disclosure when necessary, is presumed to result in sustainability-related financial disclosures that achieve a fair presentation.
- the definition of material information should be aligned with the definition in IAS 1
- comparative information should be restated if better information becomes available (rather than being reported as part of current year disclosures).

Draft standard on climate-related disclosures

128. The ISSB has issued an exposure draft of a standard intended to set out requirements for the disclosure of climate-related matters. The proposals set out requirements for identifying, measuring, and disclosing climate-related risks and opportunities.

129. Comments require to be sent to commentletters@ifrs.org by 29 July 2022.

130. The exposure draft would require an entity to provide information that enables users of the financial information to understand the matters summarised in the following table:

Area	Explanation
Governance	The governance processes, controls, and procedures an entity uses to monitor and manage climate-related risks and opportunities.

Area	Explanation
Strategy	The climate-related risks and opportunities that could enhance, threaten or change an entity's business model and strategy over the short, medium and long term, including: • whether and how information about climate-related risks and opportunities inform management's strategy and decision-making • the current and the anticipated effects of climate-related risks and opportunities on its business model • the effects of climate-related risks and opportunities that could reasonably be expected to affect the entity's business model, strategy and cash flows, its access to finance and its cost of capital, over the short, medium or long term • the resilience of its strategy (including its business model) to climate-related risks.
Risk management	How climate-related risks and opportunities are identified, assessed, managed and mitigated by an entity.
Metrics and targets	The metrics and targets used to manage and monitor an entity's performance in relation to climate-related risks and opportunities, including: • performance and outcome measures that support the qualitative disclosures across governance, risk management and strategy disclosure requirements • targets that an entity uses to measure its performance goals related to significant climate-related risks and opportunities.

Technical Bulletin 2022/2

Technical developments and emerging risks from April to June 2022

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Technical Bulletin 2022/3

Technical developments and emerging risks from July to September 2022

AUDIT SCOTLAND

Prepared by Audit Scotland for appointed auditors and audited bodies in all sectors

20 September 2022

Contents

1: Introduction

Contact: Paul O’Brien, Pobrien@audit-scotland.gov.uk

Purpose

The purpose of Technical Bulletins from Audit Scotland’s Professional Support is to provide auditors appointed by the Auditor General for Scotland and Accounts Commission for Scotland with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- summaries of selected responses to requests from auditors for technical consultations with Professional Support.

Appointed auditors are required by the Code of Audit Practice to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require generally to be aware of. It may still be necessary for auditors to read the source material if greater detail is required in the circumstances of a specific audited body. Source material can be accessed by using the hyperlinks, where provided.

Any specific actions that Professional Support recommends that auditors take are highlighted in green.

Technical Bulletins are also published on the Audit Scotland website and therefore are available for audited bodies and other stakeholders to access. However, hyperlinks to source material indicated with an asterisk (*) link to files on Audit Scotland’s SharePoint* and are only accessible by auditors.

Highlighted items

The following table highlights a selection of items in this Technical Bulletin:

Highlighted items		
Professional Support has published guidance for auditors on examining and reporting on the 2020/21 WGA returns [paragraph 1].	CIPFA/LASAAC has issued a statement on its consultation on infrastructure assets [paragraph 8].	The Scottish Government has issued statutory overrides in respect of accounting for infrastructure assets in local government [paragraph 11].
The Scottish Government has issued revised statutory guidance on accounting for service concession arrangements and leases in local government [paragraph 14].	CIPFA/LASAAC has issued the local government accounting code for 2022/23 [paragraph 18].	CIPFA/LASAAC has issued an exposure draft of the accounting code for 2023/24 [paragraph 25].
Professional Support has published guidance on certifying the 2021/22 HB subsidy claim [paragraph 34].	Professional Support has provided responses to requests for technical consultations from auditors [paragraph 38].	Professional Support has published guidance on risks of misstatement in the 2021/22 annual report and accounts of colleges [paragraph 39].
Professional Support has published model forms of Independent Auditor's Reports for colleges for 2021/22 [paragraph 42].	The SFC has issued the 2021/22 accounts direction for colleges [paragraph 47].	The SFC has issued guidance on the 2021/22 accounts direction [paragraph 49].
The FRC has issued a new framework to assist auditors in making professional judgements [paragraph 51].	The FRC has issued a report on current practice in auditor reporting [paragraph 60].	The FRC has issued an updated thematic review on the disclosure of judgements and estimates [paragraph 61].
The FRC has issued a thematic review on information on climate change in the annual accounts [paragraph 64].	The FRC has issued a report on the disclosure of digital security risks in the annual accounts [paragraph 67].	The FRC has issued a report on producing ESG data [paragraph 70].

2: All sectors

Contact: Paul O'Brien, Pobrien@audit-scotland.gov.uk

TGN on 2020/21 WGA returns

1. Professional Support has published a Technical Guidance Note (TGN) to provide appointed auditors with guidance on examining and reporting on the 2020/21 Whole of Government Accounts (WGA) returns of public bodies in Scotland. The TGN is provided with supporting material to auditors on SharePoint* and also on the Audit Scotland website

2. HM Treasury prepare WGA for the UK and are responsible for managing the production process. The National Audit Office (NAO) are the group auditor for WGA. The process has been running progressively later over the last few years and, as a result of delays in the preparation of the 2019/20 WGA, the NAO were not able to issue their Group Audit Instructions until July 2022.

3. In order to ameliorate the impact of the delay, Treasury increased the threshold for auditor assurance in England to £2 billion for 2020/21. Professional Support has agreed with the Scottish Government that threshold should also apply for all public bodies in Scotland. This increase from £500 million in previous years greatly reduces the number of bodies above the threshold.

4. Testing and reporting procedures that auditors are required to undertake in respect of providing assurance to the NAO on 2020/21 WGA returns above the threshold is included in the TGN. The procedures are consistent with the NAO's Group Audit Instructions but tailored to Scottish bodies. Reporting procedures include the submission of an Assurance Statement in a form prescribed by NAO.

5. No examination is required for bodies below the threshold, although auditors are required to complete the first eight sections of the Assurance Statement (except for minor bodies) and submit it to the NAO.

6. Treasury and the NAO originally set a date of 31 August 2022 for the submission of the audited WGA returns and Assurance Statements for 2020/21. Subsequent to the publication of the TGN, they revised the submission date to 30 September. Auditors are not expected by Professional Support to meet that date if doing so would compromise the completion of 2021/22 audits of the annual accounts, which should take priority.

7. Auditors should examine and report on the 2020/21 WGA returns of public bodies in Scotland in accordance with the TGN, and make the required submissions as soon as reasonably practicable.

3: Local government sector

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Update on accounting for infrastructure assets

8. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAAC) has issued a statement on the outcome of its consultation on proposed temporary adaptations to be included in the Code of Practice on Local Authority Accounting in the UK (accounting code) in respect of infrastructure assets (explained in Technical Bulletin 2022/2 – paragraph 17).

9. Although there was general support from consultees, concerns were raised by key stakeholders about the proposal that the accounting code should assume that the net book value of replaced parts of infrastructure assets is zero. For example:

- Many respondents were looking for a more positive framing of the assumption about the nil value of derecognised parts.
- Other respondents were of the view that the value of derecognised parts should be based on the best available information.

10. CIPFA/LASAAC was not able to agree an approach that addressed the concerns of all stakeholders while also supporting high quality financial reporting. CIPFA/LASAAC therefore requested the Scottish Government (and governments in England and Wales) for a temporary statutory override while a permanent solution is developed.

11. The Scottish Government has therefore issued Finance Circular 9/2022 which contains temporary statutory overrides of some of the accounting code’s requirements in so far as they relate to infrastructure assets. The statutory overrides are summarised in the following table:

Number	Accounting code para and requirement	Statutory overrides
1	Paragraph 4.1.4.3 1) d) requires disclosure of the gross carrying amount and accumulated depreciation at the beginning and end of the year for each class of property, plant and equipment.	For accounting periods commencing from 1 April 2021 until 31 March 2024, a local authority is not required to report the gross carrying amount and accumulated depreciation for infrastructure assets.
2	Paragraph 4.1.2.51 requires the carrying amount of a replaced part of an item of property, plant and equipment to be derecognised.	For the accounting periods from 1 April 2010 to 31 March 2024, a replaced part of an infrastructure asset is to be derecognised at a nil carrying amount, and no subsequent adjustment can be made to the carrying amount of the asset with respect to that part.

12. A local government body may choose not to apply the overrides. Where the body chooses to apply either or both, paragraph 33 of the circular requires that choice to be disclosed in a note.

13. Auditors should:

- establish whether each local government body is intending to apply one or both overrides
- where the body is not applying both overrides, evaluate whether the relevant accounting code requirements have been complied with
- where the body is applying one or both overrides, evaluate whether the body has made the required disclosures.

Revised statutory guidance on service concession arrangements and leases from 2022/23

14. The Scottish Government has issued Finance Circular 10/2022* to provide revised statutory guidance on accounting for service concession arrangements, leases and similar arrangements. The circular replaces Finance Circular 4/2010 from 2022/23, and provides three options for accounting for these arrangements.

15. The options include no change to the calculation of the statutory charge for the repayment of debt originally set out in Finance Circular 4/2010, which would continue to be charged over the life of the arrangement in equal instalments of principal. The provisions are included at section 2.1 of the new circular.

16. The new circular at section 2.2 sets out a temporary optional flexibility for calculating the statutory charge for the repayment of debt for service concession arrangements entered into prior to 1 April 2022. Key aspects of the flexibility related to this option are explained in the following table:

Aspect	Aspects of flexibility
Nature	The annual charge for the repayment of debt may be calculated: • in accordance with the useful life of the asset • using either equal instalments of principal or the annuity method.
Applicable years	The flexibility may be applied in either 2022/23 or 2023/24. It may have either prospective or retrospective application.
Cumulative statutory adjustment	The cumulative statutory adjustment is from the Capital Adjustment Account to the General Fund and is made as at 1 April in (depending on the year applied) either 2022 or 2023. There is no prior year restatement of statutory adjustments. The service concession arrangement liability will continue to be written down by the contractual principal repayments.

Aspect	Aspects of flexibility
Applicable arrangements	The flexibility must be applied consistently to all service concession arrangements entered into prior to 1 April 2022 with the exception of agreements with less than 5 years until completion provided the annual charge is not materially different. A body should separately identify the value of each service concession arrangement. If not, the asset and liability must be restated at market values. The flexibility does not apply to leases or any similar arrangement.
Governance	The decision to apply the flexibility must be approved by the full Council.
Prepayments	Where a prepayment was originally funded from a revenue or capital source, the body may revisit that decision and choose to fund the prepayment from borrowing. Borrowing should be recognised by a loans fund advance.
Disclosures	The reason for the change should be disclosed, along with an explanation of the movement in both the Balance Sheet and the General Fund. Where the annuity method has been applied, narrative should explain how this method links to the flow of benefits from the asset. Where an arrangement is excluded as it has fewer than five years until expiry, an explanation should be disclosed that the statutory repayment continues to be based on the contract life. Disclosure is required of the: • cumulative value charged to the General Fund prior to applying the flexibility • revised cumulative value charged to the General Fund in adopting the flexibility • funds released as a result of the flexibility.

17. The third option is set out at section 1 of the new circular and involves local government bodies adopting the accounting code requirements in full for service concession arrangements, leases and similar arrangements without any statutory adjustments. Key aspects of this option are explained in the following table:

Aspect	Summary of guidance
Cumulative statutory adjustment	All statutory charges would be reversed, such that only the accounting entries required by the accounting code remain. The cumulative financial effect of all the reversals will be a statutory adjustment from the Capital Adjustment Account to the General Fund. There is no prior year restatement of statutory adjustments.

Aspect	Summary of guidance
Applicable years	The option can be exercised in any financial year from 1 April 2022 and has retrospective application. The statutory adjustment is made as at 1 April in the year the revised arrangements are applied.
Applicable arrangements	The option applies to all service concession arrangements, leases and similar arrangements with the exception of agreements with fewer than 5 years until completion. Once this approach is taken, it should not be reversed in subsequent years.
Disclosures	An explanation should be disclosed of the basis for the accounting policy change and the impact on the balances reported within the annual accounts.

2022/23 accounting code

18. CIPFA/LASAAC has issued the accounting code* to set out local government accounting requirements for 2022/23. The financial reporting framework is based on International Financial Reporting Standards (IFRS) as adopted by the UK, adapted for the local government context where necessary.

19. The most significant change is Appendix F which sets out the requirements for accounting for leases based on IFRS 16 Leases. Although adoption of IFRS 16 is not mandatory until 2024/25, adoption before then is strongly encouraged in which case Appendix F applies.

20. Under IFRS 16, a local government body is required to assess whether a contract meets the definition of a lease. The definition is met where the contract conveys the right to control the use of an identified asset for a period of time. It should be noted that:

- Controlling the use of an identified asset involves having the right to obtain substantially all of the economic benefits and service potential from use of the asset throughout the period of use. Paragraphs B9 to B31 of IFRS 16 provide guidance in this assessment.
- The accounting code adapts the definition of a lease in IFRS 16 to remove the phrase ‘in exchange for consideration’. This means that leases include those agreements that do not include the provision of consideration (nil consideration leases).
- The assessment should take place at inception of a contract, which is usually the date of the lease agreement.
- A body should not make a reassessment on the date of implementation except in relation to leases for nil consideration. Instead, the body is required to apply IFRS 16 only to contracts that were previously identified as leases under the previous standards.

- Reassessment is required only where the terms and conditions of the contract are changed.

21. For lessees, there is no longer a distinction between finance leases and operating leases. A lessee is required to recognise a right-of-use asset and a lease liability. The following table provides a summary of the requirements:

	Right of use asset	Lease liability
Definition	An asset that represents a lessee's right to use the asset that is the subject of the lease (the underlying asset) for the lease term.	The obligation to make lease payments over the lease term.
Initial measurement – commercial terms	At cost, i.e. the amount of the initial measurement of the lease liability.	The discounted present value of outstanding lease payments.
Initial measurement – peppercorn or for nominal lease payments, or for nil consideration	At fair value.	The difference between the fair value and the lease liability is recognised in the surplus or deficit on the provision of services.
Recognition date	The date on which a lessor makes an underlying asset available for use by a lessee (commencement date).	
Subsequent measurement	Current value in accordance with section 4.1 of the accounting code. The cost model can be used as a proxy for current value unless inappropriate (such as for property assets).	The carrying amount of the lease liability is: • increased to reflect interest • reduced to reflect the lease payments made.
Exemptions	A lease that, at the commencement date, has a lease term of 12 months or less (a short-term lease) is exempt, unless it contains a purchase option. A lessee may elect to exempt leases where the underlying asset is of low value.	

22. On transition at 1 April 2022, a local government body as lessee is required to apply IFRS 16 to its leases retrospectively with the cumulative effect of initially applying IFRS 16 recognised at that date. The body should:

- not restate comparative information
- recognise the cumulative effect of initial application as an adjustment to the opening balance of reserves.

23. Appendix C of the accounting code requires a local government body that chooses to adopt IFRS 16 in 2022/23 to disclose information relating to the impact of that accounting change in 2021/22. A body should disclose:

- a statement that IFRS 16 will be adopted on a voluntary basis
- the nature of the impending changes
- a discussion of the impact that initial application of IFRS 16 is expected to have on the body's financial statements (or a statement that the impact is not known or reasonably estimable).

24. Auditors should:

- establish whether the local government body is intending to adopt IFRS 16 in 2022/23
- where adoption is planned for 2022/23, evaluate whether the required disclosures have been made in 2021/22.

Consultation on 2023/24 accounting code

25. CIPFA/LASAAC has issued an exposure draft of the accounting code for 2023/24. There are proposals related to:

- new accounting standards
- sustainability reporting
- changes to the structure or format of the accounting code.

26. Responses to the consultation should be sent to cipfalasaac@cipfa.org by 14 October 2022.

New accounting standards

27. Section A4 of the Invitation to Comment (ITC) sets out two proposed changes to the accounting code as a result of changes to accounting standards. These changes are summarised in the following table:

Accounting standard	Change to standard	Proposed change to code
Definition of Accounting Estimates, Amendments to IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors	The 'change in accounting estimates' definition has been replaced with a definition of accounting estimates which describes them as "monetary amounts in financial statements that are subject to measurement uncertainty"	The revised definition of accounting estimates is included at paragraph 3.3.2.2 of the exposure draft.

Accounting standard	Change to standard	Proposed change to code
	Accounting estimates are developed if accounting policies require items to be measured in a way which involves measurement uncertainty. The effects of a change in input or a measurement technique are changes in estimates provided they do not result from the correction of a prior period error.	It is proposed that paragraphs 3.3.2.14 and 15 of the accounting code are amended to explain that: • an accounting policy may require items to be measured at monetary amounts that cannot be observed directly and must instead be estimated • a local government body is therefore required to develop an accounting estimate to achieve the objective set out by the accounting policy • a body uses measurement techniques and inputs to develop an accounting estimate. In addition, paragraph 3.3.2.18 covers the treatment of a change in an input or measurement technique.
Disclosure of Accounting Policies Amendments to IAS 1 Presentation of Financial Statements	A requirement to disclose an entity's material (rather than significant) accounting policy information. Clarification that accounting policy information may be material because of its nature, even if the related amounts are immaterial. Confirmation that if an entity discloses immaterial accounting policy information, such information must not obscure material accounting policy information.	Paragraphs 3.4.2.88 to 3.4.2.93 have been added to the exposure draft to reflect these changes. This includes at paragraph 3.4.2.90 examples of when accounting policy information is likely to be material.

28. Section B6 proposes to implement IFRS 17 Insurance Contracts from 2025/26, but expects that the standard will apply to local government bodies only in limited circumstances.

Sustainability reporting

29. Section C 7.4 advises that, although there is currently no explicit requirement for local government bodies to produce a sustainability report, sustainability matters should feature in the Management Commentary.

30. In addition to narrative reporting requirements, sustainability reporting will increasingly have a wider impact on the financial statements. A table at paragraph 52 in the ITC provides a list of areas that may be impacted. Examples include:

- asset values
- significant risks that key assumptions may change within the next financial year (e.g. due to potential changes in the regulatory environment)
- any estimation assumptions and uncertainty created by environmental issues
- new additions capitalised to meet climate or other environmental needs
- impairment impacts because of:
  - flooding, coastal defence erosion etc
  - regulatory requirements imposing different building standards
  - assets not meeting environmental standards.
- policy commitments to meet climate change needs that create an obligating event.

31. As the impacts of environmental and sustainability reporting are already covered by the standard provisions of the accounting code, no changes are explicitly required. However, stakeholders' views are sought on the proposal to add this area to CIPFA/LASAAC's strategic plan.

Changes to the structure or format of the accounting code

32. CIPFA/LASAAC considers that it would be timely to consider the structure and format of the accounting code. Preliminary objectives for the review are listed at paragraph 61 of the ITC and include ensuring that the code:

- promotes high-quality financial reporting
- ensures that users are able to understand how a local government body reports its financial position, performance and cash flows
- supports communication of the key messages
- is structured so that its provisions are readily accessible
- clearly sets out where reporting differs from the private sector and the rest of the public sector.

33. CIPFA LASAAC is still considering the objectives for the review and is seeking views.

TGN on certifying 2021/22 HB subsidy claims

34. Professional Support has published TGN/HBS/22 on certifying the 2021/22 housing benefit (HB) subsidy claim. The TGN is provided with supporting material to auditors on SharePoint* and is also available from the Audit Scotland website. The TGN:

- provides guidance for auditors on the examination of the HB subsidy claim, including highlighting the main risk areas
- sets out and explains an overview of the certification approach, the preliminary procedures (at section 1), testing procedures (at section 2), procedures for evaluating results and agreeing amendments (section 3) completion procedures (at section 4) and post-certification procedures (at section 5) that auditors should carry out (all summarised in the checklist at Appendix 1)
- provides examples of reporting errors and observations in a letter to the Department for Work and Pensions (DWP) at Appendix 3
- provides examples of reporting the results of any post-certification procedures at Appendix 4.

35. The approach set out in the TGN is based on the Housing Benefits Assurance Procedures (HBAP) produced by the DWP and used by auditors throughout the UK. However, Professional Support has negotiated with the DWP changes to certification testing for Scottish local authorities for 2021/22. The changes are intended to rationalise the level of auditor testing required by HBAP, and are summarised as follows:

- For local authorities, where auditors have assessed the risks of inaccuracy as low, and with an HB caseload of under 5,000 cases, a smaller initial sample of 10 rent allowances and 10 rent rebates should be selected. A sample size of 20 remains for authorities above that caseload.
- There is no longer a requirement to test a separate sample of 20 modified scheme claims (although any modified scheme claims selected within the initial sample should be tested).

36. The submission deadline for the HB subsidy certification is 31 January 2023.

37. Auditors should certify 2021/22 HB subsidy claims in accordance with TGN/HBS/22.

Technical consultations with auditors

Professional Support responds to requests from auditors for technical consultations

38. The following tables summarise requests from auditors for technical consultations with Professional Support in respect of issues arising from the audit of the 2021/22 annual accounts of local government bodies, along with the advice offered:

Can indexation be used to value land and buildings in local government?

The accounting code contains an interpretation of IAS 16 which requires valuations of land and buildings to be in accordance with RICS valuation standards. The valuation of land and buildings is normally undertaken by professionally qualified valuers. Under RICS standards, a qualified valuer may carry out a:

- valuation inspection, which involves a site visit; or
- desktop investigation where digital mapping is used instead of a site visit.

In Professional Support's view, the use of indices by an accountant to approximate a change in the value of land and buildings does not constitute a valuation in accordance with RICS standards. Professional Support has discussed the matter with CIPFA who has confirmed that indexation is not supported by the accounting code.

However, indices may be used to identify cases where a valuation by a professional valuer under RICS standards is necessary. For example, the accounting code requires assets to be revalued at least every five years, but more regularly if that frequency is insufficient to keep pace with changes in current value. A five-year interval between valuations is dependent on the carrying amount of the asset not being materially different from its current value. Indices may be a useful tool to either demonstrate that is the case or, if a material change is indicated, flag that a valuation by a valuer is necessary.

How should accumulated depreciation be treated at the date of revaluation of property, plant and equipment?

When an item of property, plant and equipment is revalued, the carrying amount of that asset is adjusted to the revalued amount. At the date of the revaluation, paragraph 35 of IAS 16 sets out the following two options for how the asset should be treated:

(a) The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated depreciation at the date of the revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset.

(b) The accumulated depreciation is eliminated against the gross carrying amount of the asset.

For local government bodies, the accounting code has since 2016/17 contained an adaptation to IAS 16 at paragraph 4.1.1.6 which withdraws option (a). Accumulated depreciation should therefore be eliminated against the gross carrying amount of the asset.

Should a local authority be recognising a provision or disclosing a contingent liability for cases of historical child abuse in care?

The Redress for Survivors (Historical Child Abuse in Care) (Scotland) Act 2021established a scheme for financial redress for survivors of historical child abuse in relevant care settings in Scotland.

Should a local authority be recognising a provision or disclosing a contingent liability for cases of historical child abuse in care?

The scheme includes the establishment of Redress Scotland as an arm's-length, independent body to make determinations in connection with applications by individuals under the scheme. Redress Scotland advises the Scottish Government on the amount of redress payments and to whom they should be paid.

A number of public and charitable bodies contribute towards the funding of redress payments. The local government sector makes a contribution to recognise the collective responsibility of all local authorities. The contribution is to be top-spliced from the local government settlement for ten years from 2022/23; it is not allocated to individual local authorities but rather it is made at a sector level. The Act specially provides that making a contribution is not evidence of liability in connection with an allegation of abuse.

Professional Support has considered the legal form under which the scheme has been set up and has concluded that individual local authorities do not have a legal or constructive obligation to provide redress. Rather local government as a sector is simply making a financial contribution through top slicing of total revenue grant. There does not therefore appear to be any obligation that would require a local authority to recognise a provision or disclose a contingent liability. The substance of the scheme reflects that legal form so there does not appear to be any substance over form argument.

Can the statutory method for repaying Loans Fund advances be used for repayments after 31 March 2021?

Finance circular 7/2016 provides statutory guidance on the prudent repayment of Loans Fund advances. The statutory guidance allows the method required by the Local Government (Scotland) Act 1975 (the statutory method) to continue to be used for advances made up to 31 March 2021. Repayments for those advances can continue to us the statutory method until the end of the repayment period.

The statutory method is not available for new loans fund advances made after 31 March 2021. A prudent repayment method for these advances is required as set out in the statutory guidance.

It should be noted that this advice supersedes paragraph 35 in Module 3 of TGN 2021/8(LG) which incorrectly states that the statutory method is not permitted for repaying advances made after 1 April 2016 (the date referred to should have been 1 April 2021).

4: College sector

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TGN on risks of material misstatement in 2021/22

39. Professional Support has published Module 14 of TGN 2022/1. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement in the 2021/22 annual report and accounts of central government bodies generally. Module 14 provides:

- guidance on applying the other modules to the audit of the 2021/22 annual report and accounts of colleges
- supplementary guidance on the risks of misstatements in areas specific to colleges

40. Module 14 is available with the rest of the TGN and supporting material to auditors on SharePoint* and is also freely available to download from the Audit Scotland website.

41. Auditors are expected to pay due regard to Module 14 and use it as a primary reference source when performing 2021/22 audits of colleges. Auditors should advise Professional Support of any intended departures from the guidance.

TGN on 2021/22 model IARs

42. Professional Support has published TGN 2022/6(C) to provide auditors with model forms of Independent Auditor's Reports (IAR) which should be used for the 2021/22 annual report and accounts of colleges.

43. Auditors are required by the Code of Audit Practice to prepare their IARs in accordance with the TGN. The TGN is available with supporting material to auditors on SharePoint* and are also freely available from the Audit Scotland website.

44. The model form of IARs set out in Appendices 1 and 2 of the TGN have been tailored to reflect relevant public sector legislation and augmented by the reporting requirements of the Auditor General.

45. There are a number of changes to the model forms of IAR and to the application guidance in 2021/22. These are summarised in the following table:

Area	Change
Model IARs	Changes have been made in the ‘Conclusions relating to going concern’ and the ’Responsibilities of the Board of Management’ sections of the model IARs to better explain the application of going concern in the public sector.
	There are also some minor wording clarifications.
Application guidance	Changes in the guidance include: • permitting auditors to amend the specified wording that explains the extent to which the audit is capable of detecting irregularities • advice for auditors to encourage bodies to use the titles specified by the Statement of Recommended Practice – Accounting for Further and Higher Education 2019 (the SORP) or Government Financial Reporting Manual (FReM) • advice on how to deal with the inclusion of any voluntary reports.

46. Auditors should for 2021/22 audits:

- use the relevant model form of IAR for each college
- follow the specified wording other than where tailoring adjustments are set out in the application guidance in the TGN
- consult with Professional Support on any modified opinion or conclusion
- complete an auditor action checklist provided at Appendix 4 for each IAR prepared.

2021/22 accounts direction

47. The Scottish Funding Council (SFC) has issued their Accounts Direction for Scotland’s Colleges 2021/22. The direction requires colleges to:

- comply with the SORP in preparing their financial statements
- include a Performance Report and Accountability Report in their annual report and accounts in accordance with the FReM.

48. Specific mandatory disclosure requirements for colleges are set out in Appendix 2 to the direction. The main changes are as follows:

- Paragraph 8 has been added to require the performance analysis section of the Performance Report to include:
  - a description of the way in which the college has promoted equality of delivery of service to different groups and had due regard to public sector equality duty under the Equality Act 2010

  - brief commentary outlining the Fair Work practices that have been developed in agreement with the college's workforce and the progress the college has made in their implementation.

- A suggested table for the amended fair pay disclosure has been added to the example Remuneration Report at Appendix 8.

Guidance on 2021/22 financial statements

49. The SFC has issued guidance notes on completion of the 2021/22 financial statements which are designed to supplement the accounts direction. The guidance covers key disclosures in the financial statements, including model disclosure notes set out at Annexes A to F.

50. There are no significant changes from 2020/21.

5. Professional developments

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New framework for making professional judgements

51. The Financial Reporting Council (FRC) has issued a new framework to assist auditors in making professional judgements. Professional judgement involves applying training, knowledge and experience in making informed decisions about appropriate courses of action. The effective exercise of professional judgement is a critical feature of any audit.

52. The framework is intended to enhance the quality and consistency of professional judgements by helping auditors take account of all relevant considerations and improve their more intuitive judgement-making.

53. Although written for auditors, the framework may be useful for others in the financial reporting chain, or for specialists providing expert input into an audit. It could also be useful for audit committees in enhancing their understanding of an auditor's judgement process.

54. The framework consists of the following four components:

- An appropriate mindset for exercising professional judgement.
- A suggested professional judgement process.
- Effective consultation with a range of relevant parties.
- Factors that can impact on how challenging it is to exercise professional judgement in an appropriate manner.

Mindset

55. The guidance highlights five aspects of mindset that are especially relevant to exercising professional judgement in an effective manner. They are summarised in the following table:

Aspect	Summary of guidance
Appreciation of the purpose of audit and its public interest benefits	Understanding that the purpose of an audit is to enhance the confidence and understanding of users of the financial statements helps emphasise that the interests of the users should be paramount when making judgements. Awareness of the public interest benefits of an audit may motivate the auditor to be objective, professionally sceptical, and committed to quality.

Aspect	Summary of guidance
Professional scepticism	Professional scepticism may be especially relevant when gathering and analysing information, and when effectively challenging management.
Understanding biases and other relevant psychological factors	There are a range of biases that can subconsciously hinder objective reasoning (e.g. availability, confirmation, groupthink, and overconfidence). Certain personality traits may be detrimental to good judgement, e.g. an undue fear of conflict, unwillingness to challenge figures of authority, impatience or stubbornness. Some traits support an effective judgement process, e.g. perceptiveness and a willingness to consult and listen. An auditor's feelings and beliefs affect how susceptible they are to judgement traps such as allowing motivation to unduly influence how information is evaluated. Understanding the above factors assists the auditor in developing strategies to mitigate or cultivate such factors.
Sensitivity to uncertainty	An awareness of the presence of uncertainty can assist the auditor in identifying when they need to exercise professional judgement. An appreciation that some information sources may be more or less reliable than others allows auditors to direct their work efforts in a more effective way. An awareness that not all uncertainty can be eliminated allows the auditor to build mitigating actions into their judgement process.
Commitment to quality	it is important that the auditor is committed to making quality judgements, e.g. by being willing to delay signing the audit opinion to provide the team with enough time to perform a robust professional judgement process.

Professional judgement trigger and process

56. This portion of the framework comprises a series of steps to structure the way in which a judgement is carried out. The steps are summarised in the following table:

Step	Summary of guidance
Remain alert to situations which require the exercise of professional judgement	In deciding whether to use a formal judgement process, auditors should consider the complexity and importance of the judgement being made, their experience and any precedents.

Step	Summary of guidance
Consider who is the right person to make the judgement	Auditors consider the relevant knowledge, skills and experience required; the complexity and importance of the judgement; and the available time and resources. Where an auditor engages an expert to provide a view, the auditor remains responsible for the judgement.
Appropriately frame the issue	Taking the time to fully define and understand the problem, including relevant risks, is a key part of an effective judgement process. The main components of this step are: • articulating objectives to clarify the intended outcomes • identifying the alternatives that will be judged.
Marshal your information	This is a key step as it provides the evidence base. Page 16 of the guidance provides examples of the various enquiries, knowledge and experience from which relevant information may be drawn. Auditors should employ a questioning mindset in seeking information that may contradict as well as corroborate management assertions, while remaining alert to conditions that may indicate information may not be authentic, and to any inconsistencies between different information.
Stand back, and conclude	This includes considering whether: • a judgement step has been inappropriately skipped • all relevant alternatives have been identified and assessed • the judgement has been unduly affected by bias • the course of action decided upon might undermine some of the auditor's other objectives.
Document, communicate and reflect	Effective documentation allows others to understand how judgements were made and the rationale and quality of evidence for the decision reached. Documentation is unlikely to take place at a single point in the audit, but will iterate over time. Key audit matters reported may include significant professional judgments. Auditors should reflect on the process and assess what went well and what could be improved in future.

Consultation

57. It is important that audit teams encourage a healthy culture of debate and challenge to facilitate the input of those with relevant experience and expertise, and provide the opportunity to coach less experienced members of the team.

58. Consultation outside the team, such as with an external expert or an engagement quality reviewer, can further widen the available pool of expertise.

Environmental factors

59. There are a number of factors which may impact on how challenging it may be to exercise professional judgement in a quality manner. The factors are summarised in the following table:

Factor	Summary of guidance
Audit firm: culture, resources, training and processes	An audit firm can facilitate professional judgements by setting an appropriate culture, providing appropriate resources and training, and aligning reward structures to behaviours that demonstrate a commitment to audit quality.
Quantity and quality of relevant information available	If it is especially challenging to obtain relevant and reliable information, this could cause the auditor to place undue reliance on the few sources of information that are easily accessible. The quality of judgement reached should not suffer when information is scarce, though that judgement may have greater uncertainty attached to it which may lead to further work needing to be performed elsewhere.
Time and resources available	Auditors should push back if they feel under pressure to meet a timeline for making the judgement. Resources that can significantly improve the quality and range of information and insight available include: • the capacity and capability of the audit team • access to experts • technological resources such as automated tools and techniques.
Audited entity: management and those charged with governance	The audit committee can support or potentially undermine the auditor's attempts to promote a culture of healthy challenge of management and professional scepticism. The provision of clear and timely supporting information by management can reduce the risk of unnecessary delays, which could in turn lead to a rushed judgement process.

Review of auditor reporting practice

60. The FRC has issued a report which sets out the findings from research it commissioned into the current state of auditor reporting within the UK. A sample of nearly 400 auditor's reports for companies was selected, and the findings have been set out under six themes. The findings that are relevant to public audit are summarised in the following table:

Themes	Areas considered	Findings summary
Understandability and useability of auditor's reports	This explores how the length of reports varies between firms, industrial sectors, and market segments. Objective measures such as readability scores and measurement of standardised language have been used as a proxy for understanding how useability and understandability varies.	Most auditor's reports are located before the financial statements. The surveyed auditor's reports did not include any modified opinions, and nothing was reported by exception. 'Boilerplate' text is most prevalent in shorter auditor reports, and in reports issued by firms outside the Big 4. Proxy measures of readability suggest that longer reports with less boilerplate can be harder to read.
Communicating judgements on materiality and the scope of group audits	This reviews how auditors set out the basis of judgements for the selection of materiality and performance materiality, as well as decisions on the scoping and coverage achieved by group audits.	Profit measures remain the most common benchmark used for the determination of materiality, but are becoming less common. The use of equity as a benchmark, as well as multiple benchmarks, have become more common. A high proportion of auditor reports described the professional judgements made by the auditor for the selection of materiality and performance materiality.
Key audit matters (KAMs)	This includes a review of the number of KAMs and the most common types of risks of material misstatement.	Most reports included three KAMs but there were significant variations. There has been a reduction in the average number of KAMs since the requirement was introduced. The most common type of KAM was revenue recognition. Other common KAMs related to investments, asset impairments, and financial instruments. Very few KAMs dealt with risks arising from non-compliance with laws and regulations.
Specific risks	This reviews how auditors have communicated risks arising from climate change, the COVID-19 pandemic, and alternative performance measures (APMs), and their findings from the audit procedures addressing those risks.	Risks associated with climate change were rarely reported as KAMs. The most common response to the risks associated with the pandemic was to integrate the risk within a consideration of the underlying financial statement item. KAMs on APMs are very rare.

Themes	Areas considered	Findings summary
	It also included the use of graduated findings (the auditor describes the position of estimates and judgements by their position on a range of potential outcomes) and binary findings (the auditor compares management's point estimate with a plausible range of values). when reporting on KAMs.	The use of graduated findings is rare. Binary findings are more common, and both approaches use simple, formulaic approaches to express conclusions.
Going concern	This explores how auditors have reported on the appropriateness of the going concern basis of accounting.	KAMs were the main channel for reporting where the auditor had identified heightened risks on going concern. Paragraphs on material uncertainty relating to going concern were rarely used.
Fraud and other irregularities	This explores how auditors have responded to the new requirement to explain the extent to which their audit has been designed to detect fraud and other irregularities.	Identified fraud risks tended to be those presupposed by the auditing standards. The responses to fraud risks tend to be generic and describe procedures that the auditor is required to do for any audit, rather than being specifically tailored to the circumstances of the entity.

Updated thematic review on judgements and estimates

61. The FRC has issued an update to their thematic review on the disclosure of judgements and estimates (see Technical Bulletin 2017/4 – paragraph 20). The review relates to the requirements in IAS 1 to disclose:

- judgements made by management in applying an entity's accounting policies
- sources of estimation uncertainty.

62. The review identified good examples of detailed, granular disclosure explaining management's judgements and the nature of the uncertainties relating to significant estimates. Estimates were supported by quantification, such as information about assumptions made and the specific amount at risk of material adjustment.

63. However, the review also identified the following areas for improvement which are also relevant to public bodies:

- Disclosures should explicitly state whether estimates have a significant risk of a material adjustment to the carrying amounts of assets and liabilities within the next financial year.
- Entities should reassess whether disclosures on sources of estimation uncertainty should be revised each year.
- Where additional estimate disclosures are provided (e.g. those carrying lower risk or crystallising over a longer timeframe), they should be clearly distinguished from those with a significant short-term effect.

Thematic review of climate disclosures

64. The FRC has issued a thematic review on information on climate change in the annual accounts of a sample of premium listed companies. The report:

- assesses the quality of the Task Force on Climate-related Financial Disclosures (TCFD) in response to a new Listing Rule
- considers the extent to which the financial statements reflect the impact of climate change.

65. The review highlights five main areas in which entities could significantly improve their TCFD disclosures and reporting of climate change in the financial statements. Although TCFD does not yet apply in the public sector, it is anticipated that they will form the basis of future requirements.

66. The areas of improvement, along with a summary of the FRC's expectations for each, are set out in the following table:

Area of improvement	FRC expectations
Granularity and specificity	The granularity and specificity of climate-related disclosures should improve as processes to manage risks and opportunities become more embedded. The link with financial planning should be clearer and more quantified.
Balance	Discussion of climate-related risks and opportunities should be balanced and link the opportunities to any technological dependencies.
Interlinkage with other narrative disclosures	The interlinkages of TCFD with other narrative disclosures in the annual report should be considered.
Materiality	Entities should explain how they applied materiality to their TCFD disclosures. Where elements are excluded, it should be clear whether the entity has decided the elements were not relevant or material, or whether they had been omitted for other reasons such as a lack of robust data.

Area of improvement	FRC expectations
Connectivity between TCFD and financial statements disclosures	Entities should consider the connectivity between TCFD disclosures and the financial statements, and provide explanations to address whether: • the degree of emphasis placed on climate change uncertainties in the narrative reporting is consistent with the way they have been reflected in judgements and estimates applied in the financial statements • emissions reduction commitments and strategies described in the narrative have been appropriately reflected in the financial statements • the extent of progress against climate-related opportunities referred to in the narrative reporting is appropriately reflected in segmental disclosures • discussion of matters which may have an adverse effect on asset values or useful lives in the narrative reporting is consistent with positions taken in the financial statements.

Report on digital security risk disclosure

67. The FRC has issued a report on the disclosure of digital security risks in the annual accounts of a sample of companies. Digital security risks are defined for the purposes of the report as the operational, financial, reputational and stakeholder risks caused by cyber security threats, including the risk of major data breaches arising from internal lapses.

68. Digital security risk is fundamental to business continuity and resilience. Reporting on digital systems, processes and data should provide relevant information to assist stakeholders in assessing an entity's ability to remain viable and resilient.

69. The review identified that, while a significant proportion of the companies in the sample reported at least one digital-related principal risk, the disclosures are often 'boilerplate'. The report recommends a number of enhancements; those relevant to public bodies are summarised in the following table:

Area	Disclosure
Strategy	Explain how digital security and strategy are important to the entity's current and future business model, strategy and environment.
Governance	Detail the governance structures, culture and processes in place to support digital security and strategy.
Risk	Identify digital security and strategy risks and opportunities faced both now and in the future.
Events	Highlight the impact of internal and external events, and the actions and activities that respond to these.

Report on producing ESG data

70. The FRC has issued a report on the production of data on environmental, social and governance (ESG) matters. The report focusses particularly on climate issues.

71. The report identifies three elements of ESG data production which it uses to explore the current landscape, as well as the challenges faced and positive actions to address them. The three elements, along with recommended steps for each, are summarised in the following table:

Motivation	Method	Meaning
What motivates the entity to collect ESG data and how does it identify what it needs?	How is ESG data collected?	How is the data used within the entity and how does it impact decision-making?
Perform a materiality assessment to understand the relevant ESG topics and data points. Collaborate with peers to identify sector-relevant metrics, methods and sources. Identify and encourage internal champions to raise awareness.	Identify the data producers and owners across the entity. Identify the sources for the data and set out the methodology and frequency for gathering it. Apply controls over the data, including evidence trails, reviews and sign-offs. Assess which data should be subject to internal and external assurance.	Consider training and education on why ESG data is needed and how it can be used for effective strategic decision-making. Integrate ESG data in regular processes and embed in the culture. Review whether existing data and data quality is supporting strategic decision-making and whether investment in systems and resource is needed.

6. Fraud and irregularities

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This chapter contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their audited bodies and take the appropriate action.

Payroll (1)

72. A council employee failed to report a £25,000 payroll overpayment over a three-year period.

Key features
An error in processing a reduction in working hours resulted in an increase to the employee's salary. The error was not identified by the authorising officer, and the employee did not report the overpayment. The fraud was identified during a data check carried out by the council. The fraud was not detected for three years as the normal annual data checks were suspended during the pandemic. The council has issued instructions so staff processing and authorising payroll amendments are aware of the importance of ensuring the details are correct. A new checking process has been introduced that requires staff to verify any change of working hours requests to amendment forms, contracts, and payroll details. Disciplinary action has been taken and recovery action is in process.

Payroll (2)

73. An ex-council employee failed to report a £10,500 payroll overpayment over a seven month period.

Key features
The employee left the council's employment and moved to a health board following a secondment period. However, the council salary continued to be paid for seven months after the employee left the council. The fraud was identified when the health board queried an invoice for recovery of the employee's costs. The fraud was possible as the employee's manager in the council failed to complete a termination form.

Key features
The manager has been reminded of the requirement to complete termination forms. The council has re-introduced a previously suspended monthly report requiring managers to confirm the employment status of employees in their service. The case has been referred to Police Scotland and recovery action has commenced.

Theft

74. An unidentified perpetrator stole random access memories (RAMs) valued at £12,000 from laptops stored in the office of a public body.

Key features
It was discovered during a stock check that some laptops had been opened and RAMs removed. The theft was possible due to poor security arrangements. The perpetrator has not been identified due to the absence of CCTV. Security procedures have been strengthened and a process for controlling the distribution of laptops has been developed.

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Technical Bulletin 2022/3

Technical developments and emerging risks from July to September 2022

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Technical Bulletin 2022/4

Technical developments and emerging risks from October to December 2022

Prepared by Audit Scotland for appointed auditors and audited bodies in all sectors

14 December 2022

Contents

1: Introduction

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Purpose

The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- summaries of responses to requests from auditors for technical consultations with Professional Support.

Appointed auditors are required by the Code of Audit Practice to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require generally to be aware of. It may still be necessary for auditors to read the source material if greater detail is required in the circumstances of a specific audited body. Source material can be accessed by using the hyperlinks, where provided.

Any specific actions that Professional Support recommends that auditors take are highlighted in green.

Technical Bulletins are also published on the Audit Scotland website and therefore are available for audited bodies and other stakeholders to access. However, hyperlinks to source material indicated with an asterisk (*) link to files on Audit Scotland's SharePoint* and are only accessible by auditors.

Highlighted items

The following table highlights a selection of items in this Technical Bulletin:

Highlighted items		
Professional Support has published guidance on planning 2022/23 annual audits [see paragraph 1]	Audit Scotland has issued guidance to supplement specific areas in the Code of Audit Practice [see paragraph 6]	The Auditor General has issued a briefing on the challenges and risks faced by Scotland's public finances [see paragraph 7]
Professional Support has published guidance on risks of misstatement in the 2022/23 annual accounts of local government bodies [see paragraph 9]	The Scottish Government has permitted flexibilities to help fund the local government pay award for 2022/23 [see paragraph 13]	The Scottish Government has issued a consultation draft of revised statutory guidance on accounting for capital grant [see paragraph 16]
CIPFA/LASAAC has issued an update to the accounting code for England and Wales [see paragraph 18]	CIPFA has issued revised guidance on audit committees for local authorities [see paragraph 21]	Professional Support has issued a report on a review of the 2021/22 IARs of health boards [see paragraph 32]
The FRC has issued a report on creating an audit environment that enables professional scepticism and challenge [see paragraph 37]	The FRC has issued a report on drivers and barriers to auditors exercising professional scepticism [see paragraph 40]	The FRC has issued a revised ISA (UK) 600 on group audits [see paragraph 44]
The IAASB has issued an exposure draft of proposed revisions to ISA 500 on audit evidence [see paragraph 56]	The FRC has issued a report on audit quality inspections of local audits in England [see paragraph 59]	The IAASB has issued guidance on the impact on ISAs of an amendment to IAS 1 [see paragraph 62]
The FRC has issued a report on disclosures related to net zero targets [see paragraph 66]	The FRC has issued a report that sets out the attributes of a good annual report and accounts [see paragraph 69]	The FRC has issued a report on a review of the corporate reporting of companies [see paragraph 78]

2: All sectors

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Guidance on planning 2022/23 annual audits

1. Professional Support has issued guidance to assist all appointed auditors in planning their 2022/23 annual audits of public bodies. The guidance supplements the Code of Audit Practice (2021) and sets out the range of core annual audit activity and related outputs required for 2022/23, and the timescales for completing the audit in each sector.

2. Auditors should comply with the guidance when planning, performing and reporting their 2022/23 audits. The guidance is accessible by auditors with other supporting materials on SharePoint* but it is also freely available from the Audit Scotland website.

3. The largest component of core annual audit activity is the audit of a public body's annual accounts. However, the audit of the annual accounts has a wider scope than the private sector, and requires conclusions on aspects of public bodies' arrangements and performance. In local government, public audit includes considering arrangements to secure Best Value and community planning and publishing performance information. Auditors also provide important intelligence to the Auditor General, Accounts Commission and Audit Scotland in areas where they are best placed to do so.

4. 2022/23 year is the first year of the new five-year audit appointments. Audit Scotland's policy is not to compromise on audit quality or the wellbeing of audit teams, but that timescales are negotiable. The guidance is intended to strike the right balance in 2022/23 between ambitions for public audit and the capacity for auditors to carry out the work to the appropriate high quality. Target audit completion dates are considered to be stretching but achievable for the majority of audits.

5. The following table provides a summary of the key changes from last year, along with the paragraphs of the guidance in which further information is provided:

Nature of change	Paragraph
The level of expected fees below which auditors may negotiate an increase to auditor remuneration by up to 20% has increased to £35,000.	13
The target date for submitting Annual Audit Plans to Audit Scotland for central government and health has moved back one month to 31 March.	20
Guidance has been provided on the new requirement of the Code of Audit Practice to report key audit matters in the Annual Audit Report.	55 to 57

Nature of change	Paragraph
The target submission dates for the audited annual accounts have been brought forward for local government (30 September) and health (30 June).	61
Guidance has been added on specific wider-scope audit work required on climate change.	76 to 81
Guidance has been added on considering risks related to cyber security.	82 to 85
Guidance has been updated to reflect the new approach to auditing Best Value.	94 to 118
Guidance on grant claims and returns has been updated to reflect that any returns not on the approved list should be treated as non-audit services.	123 to 124
The target submission dates for the Annual Audit Reports have been brought forward for local government (30 September) and health (30 June).	211

Supplementary guidance on areas of the Code of Audit Practice

6. Audit Scotland has issued guidance to supplement specific areas in the Code of Audit Practice. The three areas, and a brief summary of the supplementary guidance related to each, are set out in the following table:

Area	Summary of supplementary guidance
Wider scope of public audit	The guidance sets out example questions at Appendix 1 to assist auditors when carrying out their risk assessment and planning their wider scope audit work.
Criteria to be used when identifying a less complex body	The wider scope audit in a less complex body may be limited to concluding on its financial sustainability. A body with gross revenue, gross assets and gross liabilities less than £10.2m is likely to be less complex. A body should not be treated as less complex where the: • auditor identifies any wider scope risks beyond financial sustainability • body has been subject to a statutory report in the previous year that related to wider scope issues • body is of strategic importance to the Auditor General or Accounts Commission. The guidance requires auditors to: • assess whether a body is less complex as part of planning each year, and document their assessment • explain in the Annual Audit Plan that the body is judged to have met the criteria to be treated as less complex • confirm in the Annual Audit Report that the audit was completed under the less complex body arrangements.

Area	Summary of supplementary guidance
Best Value	The guidance assists auditors to integrate Best Value with the wider scope annual audit work.

Briefing on public finances

7. The Auditor General has issued a briefing on the challenges and risks faced by Scotland's public finances. The briefing:

- focuses on the pressures facing the Scottish budget in 2022/23 and in the medium term, and the implications for public services
- informs and supports scrutiny of proposed spending and tax plans
- emphasises the need for reform to public services.

8. Some key messages from the briefing are summarised in the following table:

Key message	Considerations
Rising costs and increasing demands mean that the Scottish Government has to manage its position to avoid the risk that it overspends on the 2022/23 budget.	The current high level of inflation means that the Scottish Government faces higher public-sector pay and other costs, at the same time as it faces increasing demand for support from people impacted by the cost-of-living crisis. Any overspend by the Scottish Government in 2022/23 could be clawed back from the 2023/24 budget.
The Scottish Government has limited ability to make changes to balance the 2022/23 budget, and will face difficult choices setting the 2023/24 budget.	Within the year, much of the Scottish budget is committed, which means that there is limited flexibility available to the Scottish Government in the short term. In setting the 2023/24 budget, the Scottish Government needs to balance short-term necessities with longer-term priorities.
The pace and scale of reform required across the public sector needs to increase.	Immediate events and financial pressures must not distract from the immediate need for broader reform. In the past, the Auditor General has highlighted an implementation gap between the Scottish Government's ambitions for reform and delivery on the ground.

3: Local government sector

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TGN on risks of misstatement in 2022/23

9. Professional Support has published Technical Guidance Note (TGN) 2022/8(LG) to provide auditors with guidance on risks of misstatement in the 2022/23 annual accounts of local government bodies. The TGN is accessible by auditors on SharePoint*, along with supporting material, and is also available from the Audit Scotland website.

10. The TGN is intended to inform auditors’ judgement when identifying and assessing the risks of material misstatement. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2022/23 audits. Auditors should advise Professional Support of any intended departures from the guidance.

11. The TGN comprises a number of modules as summarised in the following table:

Module	Risks of misstatement area	Purpose
Overview	Areas that are pervasive to the financial statements as a whole	Explains the appropriate related accounting treatment and sets out the action auditors should undertake to evaluate whether the body has followed the required treatment
1 - 9	Specific classes of transactions, balances and disclosures in the financial statements.	
10	Audited part of the Remuneration Report	Explains the requirements and sets out the action auditors should undertake
11	Statutory Other Information (e.g. Management Commentary and Annual Governance Statement)	Sets out the procedures for considering the Statutory Other Information
12	Integration joint boards	Provides guidance on the application of the above modules to these specific bodies
13	Pension fund accounts	
14	Section 106 charities	

12. The risks of misstatement reflect areas of complexity, subjectivity and uncertainty. They have been updated to reflect new requirements and risks which emerged during the 2021/22 audits that remain applicable. A separate note* summarises the main changes from 2021/22.

Flexibilities to fund 2022/23 pay award

13. The Scottish Government has sent a letter* to the Convention of Scottish Local Authorities (CoSLA) setting out permitted flexibilities to help fund the local government pay award for 2022/23. The flexibilities are intended to enable local authorities to replace Capital Financed from Current Revenue (CFCR) or other revenue reserves with the additional capital grant in 2022/23 and 2023/24 to allow the release of such revenue resources for use towards the pay award.

14. The flexibilities are summarised in the following table:

Area	Use of additional capital grant
Early Learning & Childcare funding (ELC)	To be substituted for existing ELC revenue funding currently ring-fenced to support capital projects. The grant award letter is to be amended to permit the release of ring-fenced revenue funding.
Affordable Housing Capital Programme	To be used to substitute for revenue reserves earmarked for the capital programme for affordable housing in order to release those reserves.
CFCR in Housing Revenue Account (HRA)	To be substituted for CFCR for HRA capital investment, allowing an equal amount of reserves to be released from the HRA.

15. Other flexibilities requested by CoSLA (such as using capital receipts to meet the pay award and using capital grant towards redundancy costs) are not currently permitted.

Draft revised statutory guidance on accounting for capital grant

16. The Scottish Government has issued a consultation draft* of statutory guidance which will adapt Finance Circular 3/2018 for 2022/23 and 2023/24 to permit local authorities flexibilities in the use of the additional capital grant. This is necessary to allow the above permitted flexibilities.

17. The flexibilities and the required accounting treatment are summarised in the following table:

Use of grant	Accounting
Fund loans fund repayments	The element of capital grant applied to the repayment of the principal of loans will be held within the General Fund and used to meet the loan repayments. Any capital grant not utilised by 31 March requires to be transferred from the General Fund to either the Capital Grants Unapplied Account or the Capital Adjustment Account.

Use of grant	Accounting
Replace reserves currently earmarked for capital investment in affordable housing in order to release an equivalent amount for use towards the pay award	Once the grant is utilised to meet capital investment in affordable housing it will be transferred from the General Fund to the Capital Adjustment Account.
Fund capital investment in the housing capital programme	The capital grant may replace housing CFCR or other revenue reserves which will generate a surplus on the Housing Revenue Account which may be released to the General Fund for use towards the pay award. Once the grant is utilised it will be transferred from the General Fund to the Capital Adjustment Account.

Update to accounting code

18. The CIPFA/LASAAC Local Authority Code Board has issued an update to the Code of Practice on Local Authority Accounting in the UK (accounting code). The update applies to England and Wales from 2021/22 until 2024/25.

19. The key change in the update is a temporary relief so that local authorities in England and Wales are not required to report the gross book value and accumulated depreciation for infrastructure assets. Where a local authority chooses to apply this temporary relief, the update requires information to be disclosed to explain an authority's rationale for this decision.

20. The scope of the update does not currently apply to Scottish local authorities as Finance Circular 9/2022 already overrides the relevant disclosure requirement (see Technical Bulletin 2022/3 – paragraph 11). However, the override lasts until 2023/24 and the application of the update to Scotland may be reconsidered in respect of 2024/25.

Revised guidance on audit committees

21. The Charted Institute of Public Finance and Accountancy (CIPFA) has issued revised guidance* on audit committees for local authorities. The revised guidance builds on the 2018 edition but targets the guidance at committee members and those who support them.

22. The Delivering Good Governance in Local Government Framework lists undertaking the core functions of an audit committee, as identified in this guidance, as a key element of an authority's governance arrangements.

23. The guidance comprises the following discrete sections:

- CIPFA audit committees position statement.
- Guidance for committee members in local authorities.

- Guidance for members of police audit committees.
- A supplement aimed at those who support the committee.

24. There are also various appendices including a self-assessment checklist.

25. The position statement represents CIPFA's view on the audit committee practice and principles that local authorities in the UK should adopt. Some key elements are summarised in the following table:

Element	Summary of statement
Purpose of the audit committee	The purpose of audit committees is to provide an independent and high-level focus on the adequacy of governance, risk and control arrangements in the local authority.
Independence	The audit committee should be independent of executive decision making and able to provide objective oversight.
Core functions	Specific functions should include: • being satisfied that the authority's Annual Governance Statement properly reflects the risk environment, and any improvement actions required, and demonstrate how governance supports the achievement of the authority's objectives • supporting the maintenance of effective arrangements for financial reporting • considering the arrangements in place to secure adequate assurance across the authority's full range of operations and collaborations with other entities • overseeing the authority's internal audit function • considering the opinions, reports and recommendations of external audit.
Effective Chair	Key personal skills for an effective audit committee chair include: • promoting apolitical open discussion • unbiased attitudes, and treating auditors, the executive and management fairly • the ability to challenge the executive and senior managers when required.
Membership	The members should be trained to fulfil their role. CIPFA recommends that each audit committee should include at least two co-opted independent members.

Element	Summary of statement
Operation	To discharge its responsibilities effectively, the committee should: • meet at least four times a year • be able to meet privately and separately with the external auditor and with the head of internal audit • report regularly on its work to those charged with governance • report annually in public on how the committee has complied with the position statement • annually self-assess its performance. • evaluate its impact and identify areas for improvement.

4: Central government sector

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2022/23 discount rates

26. HM Treasury has issued PES (2022)08* to announce changes in the discount rates for general provisions, post-employment benefit liabilities, leases, and financial instruments as at 31 March 2023.

General provisions

27. The nominal discount rates to be applied as at 31 March 2023 for discounting general provisions recognised under IAS 37 are set out in the following table:

Category	Period	Percentage
Short term	Within 5 years	3.27%
Medium term	Between 5 and 10 years	3.2%
Long term	Between 10 and 40 years	3.51%
Very long term	More than 40 years	3.0%

28. As nominal rates do not take inflation into account, cash flows require to be inflated separately. There is a rebuttable assumption that the inflation rates specified in the paper will be used (unless other rates are clearly more applicable). The specified rates are:

- 7.4% for up to one year from the year end
- 0.6% between one and two years
- 2% for after two years.

Post-employment benefits

29. The discount rates for post-employment benefits are set out in the following table:

Use	Rate from 31 March 2023
Real rate used for valuing unfunded pension scheme liabilities and early departure provisions	1.7%

Use	Rate from 31 March 2023
Nominal rate for unwinding discount on liabilities (interest)	4.15%
Rate used for funded pension schemes	Based on returns from AA corporate bonds at 31 March

Financial instruments

30. The financial instrument discount rates to be applied at 31 March 2023 are set out in the following table:

Type		Rate
Nominal rate when financial instrument is not linked to an inflationary index		1.9%
Real rate when financial instrument indexed to RPI	In excess of RPI:	
	Until February 2030	(1.3%)
	From February 2030	(0.2%)

Leases

31. Where a body cannot determine the interest rate implicit in the lease, they are required to use a nominal lease discount rate of 3.51%. This is relevant for transition to IFRS 16 and for new leases that commence or are remeasured between 1 January 2023 and 31 December 2023.

5: Health sector

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Review of 2021/22 IARs

32. Professional Support has issued a report* to set out findings from a review of the 2021/22 Independent Auditors' Report (IARs) of health boards. The review evaluated compliance with the model forms of IAR and application guidance provided to auditors.

33. A summary of review findings is provided at Section 1 of the report and specific areas for improvement are highlighted at Section 2. In addition, Section 3 addresses findings in respect of disclosures in the Remuneration and Staff Report that impacts on the ability of users to understand the IAR.

34. The review found a very good level of compliance with the application guidance. However, the following areas for improvement were identified by the review:

- An auditor at one health board used the board-only model instead of the model for group accounts.
- Two audit providers at six boards added around a page of text to the model wording. Each case related to the explanation of the extent to which the audit could detect irregularities. One audit provider did not consult with Professional Support on the amendments.

35. The review also identified other issues where it may not have been clear to users what statements had been audited. For example, in some cases:

- auditors did not precisely match the titles of the financial statements or other reports to those titles used by the board
- the board had not accurately or clearly identified the parts of the Remuneration and Staff Report that had been audited. This issue had previously been highlighted in Technical Bulletin 2022/2 (paragraph 9).

36. Auditors should ensure the areas for improvement are addressed for their IARs in 2022/23.

6: Professional matters

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Report on professional scepticism and challenge

37. The Financial Reporting Council (FRC) has issued a report that sets out the key attributes of a high-quality audit environment that enable professional scepticism and challenge.

38. Professional scepticism is an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence. A fundamental attribute of an auditor's mindset and behaviour is exercising professional scepticism and challenge as these are the foundations of a high-quality audit. The inconsistent application of scepticism and challenge results in the poor application of professional judgement.

39. The paper considers four key elements of an environment that enable scepticism and challenge. They are summarised in the following table:

Element	Requirements	Achieved by	Example of actions
Learning environment	An auditor needs to be equipped with the skills and expertise necessary to exercise professional scepticism and challenge the management of an audited entity.	Professional qualification and ongoing learning and development, including on-the job coaching.	Training in behaviours and mindset alongside technical training. Audit-based learning and coaching, built into an auditor's workload. Training in soft skills such as critical thinking and handling difficult conversations.
Culture	An audit firm needs to encourage auditors to display scepticism and challenge.	A culture that promotes and nurtures these behaviours including the elimination of barriers.	Communication of expected behaviours using a variety of formats. Promoting 'speaking up'. A culture of continual improvement and learning from mistakes. Engagement with employees to become advocates of desired behaviours.

Element	Requirements	Achieved by	Example of actions
Audit firm operating model	An audit firm needs to enable auditors to apply scepticism and challenge in their day-to-day audit work through the firm's operating model and processes.	Appropriate resources and processes at the audit firm including 'hot' reviews and a culture of consultation.	Sufficient and appropriate resources on every audit with strong project management. Effective use of specialists, experts and central technical teams to provide challenge in the most complex areas.
Ecosystem	Other parties in the ecosystem, including the audit committee and management at the audited entity, also play a part in enabling this mindset and behaviour.	Management and those charged with governance at the audited entities supporting these behaviours.	An engaged audit committee that supports the audit team with challenges. Management at the audited entity providing quality and timely information and engaging with the auditors to facilitate challenge.

Report on drivers and barriers to professional scepticism

40. The FRC has issued a report which is the output of research they commissioned to understand the drivers and barriers to auditors exercising professional scepticism and adequately challenging management. The research was carried out to inform the report on scepticism referred to above.

41. The research identified some key factors that encourage professional scepticism and effective challenge. Importantly, the most powerful drivers are dependent upon how staff and teams are influenced by more senior auditors (i.e. partners, directors and senior managers). Some of those factors are summarised in the following table:

Factor	Drivers
Teaching and embedding desired auditor behaviour	Bringing the specific behaviours to life through case studies and training highlighting the desired behaviours explicitly and explaining what they mean in practice. Training in soft skills, e.g. critical thinking and handling difficult conversations. Having the time and space to coach auditors by working collaboratively with them, sharing feedback, and identifying opportunities for them to be exposed to instances of scepticism and challenge in real-time work situations.
Consistently communicating and prompting desired audit behaviour	An ongoing, consistent commitment to scepticism and challenge is continually communicated and reinforced. An overall culture of continual improvement is implemented.

Factor	Drivers
Role modelling desired audit behaviour	Partners, directors and senior managers: • act as leaders in relation to scepticism and challenge, modelling these behaviours themselves • create opportunities for audit managers and junior level auditors to see them doing so in action • continually reasserting the behaviours in communications and feedback.

42. The research also highlighted the factors that can impede firms from establishing a culture that encourages auditors to consistently display the desired behaviours. They are summarised in the following table:

Factor	Barriers
Workplace environments that support desired auditor behaviour	Environments that discourage or fail to promote open, collaborative working practices. Cultural hierarchies that do not allow manager and junior level auditors to raise challenge upwards. This can be caused by a lack of transparency around the rationale behind decisions and ineffective feedback processes that do not give audit managers and junior auditors room to grow.
Resources to enable desired auditor behaviour	Time, workload, and resourcing pressures that squeeze out the time and space needed for auditors to be able to exercise scepticism and challenge, and apply the critical thinking needed for good judgement.
Alignment of reward and recognition with desired auditor behaviour	Inconsistencies in the extent to which the behaviours are explicitly linked to remuneration, reward, progression, and feedback.

43. Alongside these key drivers and barriers, the research also identified opportunities for audit firms to strengthen professional scepticism and effective challenge. These included effectively embedding hybrid working practices. Central to ensuring this is utilising virtual channels for informal as well as formal discussion between audit teams.

Revised standard on auditing group financial statements

44. The FRC has issued revised ISA (UK) 600 on audits of group financial statements. The revised ISA is effective for audits of periods beginning on or after 15 December 2023 (i.e. 2024/25 audits of public bodies), but early adoption is permitted.

Scope

45. The revised ISA (UK) 600:

- expands on the application of other relevant standards to an audit of group financial statements (a group audit)
- deals with special considerations that apply to a group audit, including those circumstances when component auditors are involved.

46. Group financial statements include the financial information of more than one entity or business unit through a consolidation process. This term refers to the:

- preparation of consolidated financial statements
- presentation of combined financial statements
- aggregation of the financial information of entities or business units such as branches or divisions.

47. ISA (UK) 600 (adapted as necessary) may also be useful in an audit of financial statements other than a group audit when the audit team includes individuals from another firm.

Group auditor

The audit team for a group audit comprises:

- the group auditor, which is the group engagement partner and members of the audit team
- component auditors (i.e. an auditor who performs audit work related to a component for purposes of the group audit) where the group auditor determines their involvement.

48. The responsibilities of the group auditor are summarised in the following table:

Area	Responsibility
Audit strategy and group audit plan	Establishing the overall group audit strategy and group audit plan. Determining the involvement of component auditors.
Direction, supervision and review	Directing and supervising component auditors and reviewing their work.
Evaluating conclusions	Evaluating the conclusions drawn from the audit evidence as the basis for forming an opinion on the group financial statements.
Audit evidence	Determining that audit evidence has been obtained to support the conclusions and for the auditor’s report on the group financial statements to be issued.

Area	Responsibility
Responding to risks of material misstatement	Determining an appropriate approach to planning and performing audit procedures to respond to the assessed risks of material misstatement in the group financial statements.
Components	Determining the components at which audit work will be performed.

Component auditors

49. Detection risk in a group audit includes the group auditor not detecting that a component auditor has not detected a misstatement that could cause a material misstatement in the group financial statements. Accordingly, paragraph 8 of ISA (UK) 600 requires involvement by the group auditor in the work of component auditors.

50. Paragraph 29 requires the group auditor to communicate with component auditors about their respective responsibilities and the group auditor's expectations.

51. When a component auditor is also performing an audit of the component financial statements, the group auditor may be able to use that audit work. In addition, component auditors may adapt their audit work to also meet the needs of the group auditor. In any event, the requirements of ISA (UK) 600 apply.

Materiality

52. Paragraph 35 requires the group auditor to determine:

- component performance materiality. This is set to reduce aggregation risk to an appropriately low level. Aggregation risk is the probability that the aggregate of misstatements exceeds materiality for the financial statements as a whole. Generally, aggregation risk increases as the number of components increases
- the threshold above which misstatements identified in the component financial information are to be communicated to the group auditor.

Consolidation process

53. Paragraph 38 requires the group auditor to take responsibility for further audit procedures to respond to the risks of material misstatement of the group financial statements arising from the consolidation process. This includes:

- evaluating whether all components have been included in the group financial statements
- evaluating the consolidation adjustments and reclassifications
- evaluating whether management’s judgments made in the consolidation process give rise to indicators of possible management bias

- responding to risks of material misstatement due to fraud arising from the consolidation process.

Communication from component auditors

54. Paragraph 45 requires the group auditor to request the component auditor to communicate relevant matters, including those summarised in the following table:

Area	Matters to be communicated
Financial information	Identification of the financial information on which the component auditor has been requested to perform audit procedures.
Performance of work	Confirmation that the component auditor has performed the work requested.
Laws or regulations	Instances of non-compliance with laws or regulations.
Misstatements	Misstatements identified by the component auditor that are above the threshold.
Fraud	Fraud involving component management or employees who have significant roles in the system of internal control.
Conclusions	The component auditor’s overall findings or conclusions.

55. The group auditor is required to:

- evaluate whether communications with the component auditor are adequate for the group auditor’s purposes
- determine whether it is necessary to review additional component auditor audit documentation
- determine if any additional audit procedures are to be performed, and by which auditor.

Proposed revisions to international standard on audit evidence

56. The International Auditing and Assurance Standards Board (IAASB) has issued an exposure draft of proposed revisions to ISA 500 on audit evidence. Comments on the proposals in the exposure draft should be submitted through the IAASB website by 24 April 2023.

57. The objectives of the proposed revisions are to:

- clarify the purpose and scope of ISA 500 and explain its relationship with other standards
- develop a principles-based approach to considering and making judgments about information to be used as audit evidence and evaluating whether sufficient appropriate audit evidence has been obtained

- modernize ISA 500 to be adaptable to the current business and audit environment, including the increased use of technology
- emphasize the role of professional scepticism.

58. Some key proposals in the exposure draft are summarised in the following table:

Area	Extant ISA 500	Proposals in exposure draft
Purpose and scope	Extant ISA 500 explains what constitutes audit evidence, and deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence.	The exposure draft retains this principles-based approach and proposes that ISA 500 serve as an overarching standard that deals with the auditor's responsibilities relating to audit evidence when designing and performing audit procedures.
Technology		There are various changes in application material to enable auditors to apply the standard in an evolving audit environment with the increasing use of technology. For example, the application material: • clarifies that the auditor may use manual or automated tools and techniques (paragraph A3) • explains how the use of automated tools and techniques may affect auditor bias, including automation bias (paragraphs A22 and A23) • uses examples that draw attention to the use of technology (2, 5, 6 and 10 in the Appendix).
Definition of audit evidence	ISA 500 defines audit evidence as information used by the auditor in arriving at the conclusions on which the auditor's opinion is based.	The proposed revised definition at paragraph 7(b) reflects that information (input) needs to be subject to audit procedures to become audit evidence (output). The term "information intended to be used as audit evidence" is used to describe the input. Paragraph A34 provides application material that explains the concept of information intended to be used as audit evidence.

Area	Extant ISA 500	Proposals in exposure draft
Sufficiency and appropriateness of audit evidence	ISA 500 refers to the sufficiency (quantity) and appropriateness (quality) of audit evidence.	The exposure draft retains the concepts of appropriateness and sufficiency, but more supporting application material has been added. For example, paragraph A13 explains that the appropriateness of audit evidence is affected by the: • relevance and reliability of information intended to be used as audit evidence • effectiveness of the design of audit procedures applied to the information • auditor's application of those audit procedures.
Persuasiveness of evidence		The exposure draft introduces the concept of persuasiveness. Application material explains the factors that may affect the persuasiveness of audit evidence. Paragraph A9 lists the following factors: • The information intended to be used as audit evidence, including the auditor's consideration of the attributes of relevance and reliability of the information. • Whether the information is from a single source or from multiple sources. • The design and performance of audit procedures, i.e. whether they are appropriate and have been properly applied. • Whether there are inconsistencies between multiple pieces of audit evidence.
Professional scepticism	ISA 500 requires the auditor to design and perform audit procedures that are appropriate in the circumstances	Paragraph 8 of the exposure draft reinforces the exercise of professional scepticism by requiring auditors to design and perform audit procedures in an unbiased manner. Paragraph A20 has been added to explain that this involves not being biased toward obtaining audit evidence that may corroborate the existence of risks of material misstatement or management's assertions, or toward excluding audit evidence that may contradict the existence of risks or such assertions.
Attributes of relevance and reliability		Paragraph 9(b) requires auditors to consider the attributes of relevance and reliability that are applicable in the circumstances. Paragraphs A54 to A62 describe the attributes. For example, paragraph A56 lists the following attributes in considering the degree to which information is reliable:

Area	Extant ISA 500	Proposals in exposure draft
		• The information is free from bias and error; reflects all of the underlying conditions, events, and circumstances; and has not been inappropriately altered. • The source actually generated the information, has the competence and capability to generate the information, and can be trusted. If the accuracy and completeness attributes are applicable, paragraph 10 requires auditors to obtain audit evidence. Paragraphs A63 to A65 explain the circumstances in which the auditor may consider accuracy and completeness to be applicable, and how audit evidence may be obtained.
Management expert	If information has been prepared using the work of a management's expert, the auditor is required, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes, to: • evaluate the expert’s competence, capabilities and objectivity • obtain an understanding of their work • evaluate the appropriateness of the work as audit evidence.	Paragraph 11 of the exposure draft adds a requirement for the auditor to obtain an understanding about how the information prepared by the expert has been used by management in the preparation of the financial statements. The current requirement to evaluate the appropriateness of the expert’s work has been removed as it was deemed redundant. The current conditionality requirement (“to the extent necessary, having regard to the significance of that expert’s work for the auditor’s purposes”) was considered unnecessary and has been deleted from the exposure draft.
Stand back		Paragraph 13 introduces a new “stand back” requirement for the auditor to evaluate whether sufficient appropriate audit evidence has been obtained. The ‘stand back’ requirement also emphasizes the exercise of professional scepticism by requiring the auditor to consider all audit evidence obtained.

Quality reviews of local audits in England

59. The FRC has issued a report that sets out findings from the 2021/22 audit quality inspections of major local audits in England (which include the larger health and local government bodies).

60. The following table provides a summary of the key areas where the FRC considers that improvements in audit quality are required, and which potentially have relevance to public audit in Scotland:

Area	Summary of key findings
Urgently improve financial statements review procedures and the evaluation of identified misstatements	The review identified the following failures to detect material errors in the audited financial statements: • Cash deposits were overstated by £1.7 billion caused by an error in accounts preparation. • Loss on disposal of non-current assets was overstated by £45 million caused by an incorrect audit adjustment. Also, the failure to evaluate the impact of unadjusted audit differences on each line item in the financial statements led to operating expenses being materially misstated.
Ensure there is sufficient justification to support modification of an audit opinion	The audit opinion on the financial statements was modified due to an inability to obtain sufficient appropriate evidence over inventory as a result of the auditor being unable to attend the stock counts. However, alternative procedures were performed over part of the inventory with no issues arising, and the residual balance was not material.
Improve the quality of audit procedures over pension asset valuation	Insufficient evidence was obtained on the valuation of investment assets. The primary substantive procedure was to compare valuations obtained from the custodian to those provided directly by fund managers, but there was insufficient evidence that they were independent. Insufficient evidence was obtained to rely on the valuation controls at fund managers. The service auditor reports were not properly evaluated. There was no evidence that audit procedures were performed to test the accuracy of the return on investments.
Improve the evaluation of assumptions used in investment property valuations	There was insufficient evaluation and challenge of key assumptions used in the valuation of investment property.
Improve the quality of audit procedures over the valuation and classification of financial assets	There was insufficient consideration and challenge of the financial model supporting the valuation and classification of a long-term debtor. There were insufficient procedures on whether financial assets should be classified as short-term investments or cash equivalents.

Area	Summary of key findings
Enhance audit procedures over expenditure	There was no testing of the completeness and accuracy of source data when performing substantive analytical procedures. Weaknesses were identified in the supporting evidence obtained when testing employee benefits, particularly where differences between amounts paid and supporting records were identified. No roll-forward procedures were undertaken when testing the operating effectiveness of controls at an interim date.
Enhance the testing of journal entries	Incorrect date ranges were entered into the firm's journals software when running reports. Journals recorded in the 20-day period after the year end were tested as that was the expected closedown period. The period tested should have been three months to align with the actual closedown period. Journal entries with the characteristics identified by the auditor were not tested for appropriate business rationale or authorisation.
Improve testing performed over business rates	Material debtors and creditors were not appropriately tested. A sufficiently precise expectation was not set when performing substantive analytical procedures over business rates income. Insufficient evaluation of key assumptions was used by the management expert when valuing the provision for appeals.
Audit methodology on going concern	The IAR contained a material uncertainty in relation to going concern, but the assessment focused on financial sustainability rather than the principle of service continuity. Standardised work programmes should be suitably tailored to the sector, including the continued provision of service approach.

61. Examples of good practice identified included the following:

- The audit team's fraud risk assessment demonstrated a good understanding of the sector and financial pressures at the local authority. Owing to the incentive for management to manipulate its reserves position, the audit team identified fraud risks for revenue expenditure funded from capital under statute, minimum revenue provision and the flexible use of capital receipts.
- The audit team appropriately evaluated the competence, capabilities and experience required to audit a highly specialised property. It engaged an auditor's expert to provide support in testing the valuation, which enhanced the team's audit evidence in this higher-risk area.
- The audit team's testing of yields when evaluating assumptions used in investment property valuations included evaluation of the comparators used by management's valuer against third-party market data.

- The audit team demonstrated rigour when challenging the assumptions made in setting the business rates appeals provision, in particular by benchmarking to other local authorities. The audit opinion was ultimately qualified as the auditor was unable to obtain sufficient appropriate audit evidence over the amount of the provision.
- The audit team robustly followed up on errors identified in its additions testing by extending its sample and challenging management to recognise a prior-year adjustment.
- The audit team consulted with an internal panel of senior public sector specialists on the audit procedures performed over a subsidiary whose financial performance had deteriorated in the year. There was clear evidence of challenge by the audit team in areas such as the disclosure of events after the balance sheet date and parent company guarantees.

Guidance on impact on ISAs of IAS 1 amendment

62. The IAASB has issued guidance on the impact on ISAs of an amendment to IAS 1 Presentation of Financial Statements. The amendment requires entities to disclose their material accounting policy information, instead of significant accounting policies. It is effective for reporting periods beginning on or after 1 January 2023, with early application permitted.

63. The guidance advises auditors to evaluate how management has addressed the effect of the amendments to IAS 1 on the entity's disclosures about accounting policies. This includes understanding the effect of these amendments on the entity's financial reporting processes.

64. Various ISAs contain requirements that are relevant to the auditor's work on disclosures in the financial statements. The guidance clarifies that the amendments to IAS 1 do not impact the principles-based requirements of the ISAs.

65. However, relevant references in the IAR to significant accounting policies will need to be revised to material accounting policy information. Professional Support will revise the model forms of IAR in all sectors from 2023/24 to refer to material accounting policy information.

Report on net zero disclosures

66. The FRC has issued a report on the disclosures entities should make on net zero or other greenhouse gas reduction commitments. The report focuses on three elements that the FRC considers that users want to understand from net zero disclosures.

67. Each element is explained in the following table, along with disclosures to be considered at both a basic and advanced level:

Level	Commitments	Impacts	Performance
	Level of ambition, and scope, nature and timing of the commitment	**How the commitment impacts strategy, business model, assumptions, uncertainties, risks and opportunities**	**How performance is being measured and high-quality data ensured, and the actions management is taking**
Foundational - providing a basic understanding of the commitment, including high-level targets, timelines and impacts	Types of greenhouse gases included Scopes of emissions included Type of reductions committed to Timelines for commitment Extent and nature of planned offsets Information on any exclusions or limitations to the commitment	Strategy for achieving net zero Risks and opportunities of the commitment framed to the business in a balanced way Estimates of potential future costs Explanation of uncertainties and assumptions in a manner consistent with financial statements	Frameworks and methodologies for setting targets and measuring progress Targets set Progress to date, and whether in line with expectations An understanding of the expected trajectory Explanation of relevant metrics
Advanced - providing updates on progress, refinements of goals, and more detailed information on impact and accountability	Consideration of whether the commitment will be updated, for example, a new approach or a more ambitious target	Updated views on impact and financing requirements Transition plans Quantitative estimates or additional scenario analysis helpful for users	Information on leading performance indicators Consideration of whether any external assurance would be appropriate

68. The report explains that effective processes and governance underpin commitments and plans, and lead to better disclosures. Robust systems and controls will enable entities to better understand their progress, and achieve their net-zero commitments over the longer term. The report sets out four stages summarised in the following table:

Define the commitment	Assess the impact	Measure progress	Refine the approach
What will be reduced and over what time period? What operation can be reduced, and what offsets can be used? What interim targets need to be set? How will goals be communicated internally?	How will the business model and strategy need to change? What resources are needed? What gaps are there? What new policies need to be put in place on business travel or new supplier relationships? How will the commitment embed into decision making? How much will it cost?	What internal targets and measures need to be in place? Are the systems, controls and processes in place to measure and monitor progress? Is there access to sufficient data? What internal review processes are needed? How do measures link to individual objectives?	What lessons have been learned to date? Are there areas that could be improved on? Do any commitments need to be redefined? Is any external review needed? How will lessons be shared with the wider workforce?

Report on a good annual report and accounts

69. The FRC has issued a report that sets out the attributes of a good annual report and accounts (ARA). In setting out these attributes, the FRC use a principles-based framework that identifies corporate reporting principles and effective communication characteristics. The report also provides examples to illustrate the underlying principles.

70. An assumption that underpins the report is that a good ARA must comply with the relevant legal, regulatory, financial reporting and code requirements. However, preparing a high-quality ARA is more than just a compliance exercise.

Materiality

71. Materiality is the bedrock of corporate reporting. It is the primary tool that helps entities to focus on key matters. Materiality informs the breadth and depth of what needs to be included in the ARA.

72. Materiality applies to all transactions, balances and disclosures (numerical and textual) in the ARA, not just those transactions affecting the financial statements. What is material in any part of the ARA will be determined by quantitative and qualitative factors as well as their nature or context.

73. A transaction, balance or disclosure would be considered quantitatively material if the size of its impact is likely to influence users' decisions or their perception of the entity's performance or future prospects. Determining whether something is quantitatively material is a matter of judgement, but the benchmark used should be the most appropriate in the context of the business and of greatest value and interest to the users.

74. Where auditor materiality is disclosed in the auditor's report, users are likely to assume that the entity has used a similar quantitative materiality in their approach to the preparation of the financial statements. When this is not the case, the entity may wish to disclose details of their assessment.

75. Qualitative factors are those factors other than size. Determining whether something is material as a result of a qualitative factor is also a matter of judgement.

Corporate reporting principles

76. Corporate reporting principles are the overarching qualitative characteristics of a good ARA. They are summarised in the following table:

Characteristics	Guidance
Accuracy	An accurate ARA is free from material misstatement and error. Accuracy depends on the quality of the underlying data supporting both financial and non-financial information. Appropriate disclosure is vital to explain estimation uncertainty which usually requires quantification of the key assumptions and a sensitivity analysis. Entities are encouraged to disclose the sources of significant facts and claims made in narrative reporting. Language used in narrative reporting needs to be specific, not open to misinterpretation by users, and balanced.
Connected and Consistent	An ARA is connected when information on related subject matter is linked together so that users can understand how the elements interact. ARAs should be consistent both internally and with other public information produced by the entity. Narrative reports should discuss the material transactions and balances reported elsewhere in the ARA. Information in narrative reports should be consistent with the information presented in the financial statements.
Complete	Completeness reflects the breadth, rather than depth, of information. Achieving completeness is not a tick box exercise and materiality should be applied to determine what must be disclosed. An ARA should include all the positive and negative material information needed by a user to understand the financial performance and position, development, and future prospects.
On-time	Although the FRC encourages entities not to compromise quality by compressing reporting timetables, long lead times between the balance sheet date and the date of publication reduce the usefulness of the ARA.

Characteristics	Guidance
Unbiased	Information is unbiased if it is balanced. A balanced ARA should refer to both positive and negative aspects of performance, position and future prospects as well as the risks and opportunities the entity faces. The ARA as a whole should present an open and honest account of the entity's activities and performance and future prospects.
Navigable	ARAs on websites should be navigable which means they should include detailed contents pages, navigation panes, clear titles and descriptions, specific cross references and hyperlinked cross references. They should also be searchable to enable users to perform text searches for specific words and phrases.
Transparent	Any significant judgements should be disclosed. Additional disclosures over and above stated requirements may be necessary for users to fully understand certain transactions. Audited and unaudited information should be clearly labelled.

Effective communication principles

77. Communication principles focus on how information should be delivered to users. They are summarised in the following table:

Characteristics	Guidance
Company-specific	An ARA should provide insights into decision making, and explain the business model in jargon-free language. Key judgements and estimates should be explained with details of how the figures would change if they were altered. Entities should replace boilerplate disclosure with information that is tailored to their specific circumstances.
Clear, concise and understandable	A clear, concise and understandable ARA: • uses straightforward language and short sentences • uses specialist terms only where necessary and makes sure they are used consistently • focuses on content that is important to stakeholders • excludes irrelevant information • does not repeat information clearly shown in diagrams, tables or other narrative • defines specialist terms and acronyms in a glossary • uses diagrams, images and tables only if it makes the information easier to understand.

Characteristics	Guidance
Clutter free and relevant	Irrelevant material obscures the important information that users need to make informed decisions and judgements. If rolling forward last year's publication, preparers should: • review the draft carefully and remove information that is no longer relevant • include relevant disclosures required by amended requirements or new circumstances.
Comparable	A comparable ARA contains metrics that are calculated consistently year on year, clearly defined, and reconciled to GAAP measures. If there has been a significant change to the calculation of a metric, the entity should: • describe the change • explain why it results in more reliable and relevant information • restate the comparatives.

Report on corporate reporting 2021/22

78. The FRC has issued a report on the outcomes of reviews of the corporate reporting of companies in the year to 31 March 2022. This report sets out the FRC's view of:

- the current state of corporate reporting in the UK
- the elements of better-quality reporting
- shortcomings that require improvement.

79. Cash flow statements is highlighted in the report as an area of considerable concern. The report advises entities to ensure that

- reported cash flows are consistent with amounts reported elsewhere in the annual report and accounts
- non-cash items are excluded from the statement and adjustments for material non-cash transactions are disclosed
- classification of cash flows, cash and cash equivalents comply with relevant definitions and criteria in the standard
- cash flows are not inappropriately netted.

80. The report also explains the FRC's expectations for 2022/23 accounts. These are shaped by their findings, as well as developments in reporting requirements and the business environment. Expectations that also apply in the public sector are summarised in the following table:

Area	Expectation
Risks	Unambiguous description in the narrative reporting of risks facing the entity, their impact on strategy, business model, cross-referenced to relevant detail in the reports and accounts.
Impact of climate change	Specific, balanced and well-integrated information about the impact of climate change in narrative reporting, and appropriate reflection of material climate-related commitments, risks and uncertainties in the financial statements.
Impairment	Impairment disclosures that assign values to, and explain how, the key assumptions used have been determined.
Judgements and estimates	Clear disclosure of significant judgements and key assumptions underlying major sources of estimation uncertainty, including information about the sensitivity of reported amounts.
Financial instruments	Transparent disclosure of the nature and extent of material risks arising from financial instruments, including significant assumptions made in the measurement of expected credit losses.
Objectives of accounting standards	Specific information that meets the disclosure objectives of the relevant accounting standards and not just the specific disclosure requirements. Additional information (beyond the standards' requirements) should be included where needed to understand the impact of particular transactions, events or circumstances.
Inflation	Clear explanation of the nature of significant inflationary features in revenue, supply, leasing and other financing contracts, and their effect on the financial statements.
Materiality	Clear, concise and understandable disclosure that omits immaterial information.

7: Fraud and irregularities

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This chapter contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their audited bodies and take the appropriate action.

Expenditure

School funds

81. A head teacher embezzled over £5,300 from a school fund.

Key features

The teacher fraudulently used the school fund purchase card, which was held in the name of another member of staff, for personal purchases. The teacher also falsified an invoice to disguise the payment of a personal membership fee, and misappropriated school fund concert cash that had been entrusted to the teacher.

The fraud was identified after concerns were raised regarding misappropriation of the school fund purchase card.

Subsequent investigations identified that high value items purchased from the school fund could not be located on the school premises. These items were subsequently recovered from the teacher's home.

The fraud was possible as due to the seniority of the teacher; the actions were not challenged by other staff. In practice, there was no segregation of duties.

The council has:

- revised school fund procedures
- introduced random sampling of purchase card transactions
- provided fraud awareness and procurement training to school staff.

The case has been reported to the Procurator Fiscal. The teacher resigned following the instigation of disciplinary proceedings.

Items to the value of £1,600 have been recovered.

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Technical developments and emerging risks from October to December 2022

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