

# The Skills Development Scotland Co. Limited

Annual Audit Plan 2018/19



 AUDIT SCOTLAND

Prepared for Skills Development Scotland  
November 2018

## Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



## About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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# Risks and planned work

1. This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice](#), and any other relevant guidance. This plan sets out the work necessary to allow us to provide an independent auditor's report on the financial statements and meet the wider scope requirements of public sector audit.

2. The wider scope of public audit contributes to assessments and conclusions on financial management, financial sustainability, governance and transparency and value for money.

## Adding value

3. We aim to add value to Skills Development Scotland (SDS) through our external audit work by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. In so doing, we intend to help SDS promote improved standards of governance, better management and decision-making and more effective use of resources.

## Audit risks

4. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for our audit of The Skills Development Scotland Co. Limited. We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

## Exhibit 1 2018/19 Key audit risks

 Audit Risk	Source of assurance	Planned audit work
<b>Financial statements issues and risks</b>		
<p>1 <b>Risk of management override of controls</b></p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes the risk of management override of controls to change the position disclosed in the financial statements.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance.</p>	<ul style="list-style-type: none"> <li>• Detailed testing of journal entries.</li> <li>• Review of accounting estimates.</li> <li>• Focused testing of accruals and prepayments.</li> <li>• Detailed testing of transactions after the year end to confirm expenditure and income have been accounted for in the correct financial year.</li> <li>• Evaluation of significant transactions that are outside the normal course of business.</li> </ul>

 <b>Audit Risk</b>	<b>Source of assurance</b>	<b>Planned audit work</b>
<p><b>2 Risk of fraud over income</b></p> <p>SDS received around £18 million in income from sources other than government grants in 2017/18. SDS expects this to increase to £33 million in 2018/19 mainly due to expected increases in European funding. The extent and nature of this income means that, in accordance with ISA240, there is an inherent risk of fraud.</p>	<p>Procedures and management checks in place to ensure that eligible expenditure is identified for the purpose of claiming ESF grant income.</p>	<ul style="list-style-type: none"> <li>• Review of SDS' anti-fraud arrangements.</li> <li>• Walk-through of controls over receivables.</li> <li>• Analytical procedures on income streams.</li> <li>• Detailed testing of revenue transactions focusing on the areas of greatest risk such as European income.</li> </ul>
<p><b>3 Risk of fraud over expenditure</b></p> <p>Most public-sector bodies are net expenditure bodies and therefore the risk of fraud is more likely to occur in expenditure. Most of SDS' operating expenditure is on multi-year national training programmes. The mid-year finance report forecasts spend of £134 million in this area, representing 56 per cent of the total 2018/19 expenditure budget. While these are contracted annually, SDS has a commitment to support them over several years. Due to the nature of SDS expenditure there is an inherent risk of fraud over expenditure.</p>	<p>Compliance team's annual checks of contracts for national training programmes.</p> <p>Compliance team's retrospective payments assurance.</p> <p>Internal audit's review of national training programmes including assurance mapping (a review of monitoring and governance arrangements across modern apprenticeships).</p>	<ul style="list-style-type: none"> <li>• Review of SDS' anti-fraud arrangements.</li> <li>• Walk-through of controls over national training programmes, including the corporate training system (CTS) and funding information and processing system (FIPS).</li> <li>• Walk-through of controls over payables.</li> <li>• Analytical procedures on expenditure streams.</li> <li>• Detailed testing of expenditure transactions focusing on the areas of greatest risk such as apprenticeship expenditure.</li> <li>• Consideration of internal audit's review of national training programmes including assurance mapping.</li> </ul>
<p><b>4 Estimation and judgements</b></p> <p>There is a significant degree of subjectivity in the measurement and valuation of the material account areas of pensions and provisions. This subjectivity represents an increased risk of misstatement in the financial statements.</p>	<p>Controls are in place to ensure accurate provision of data to actuaries.</p>	<ul style="list-style-type: none"> <li>• Completion of 'review of the work of an expert' in respect of the actuary including a review of actuarial assumptions.</li> <li>• Focused testing of pension disclosures, including data that SDS provides to actuaries.</li> <li>• Testing of provisions and related disclosures.</li> </ul>
<p><b>5 Data migration from CTS to FIPS</b></p> <p>SDS is planning to transfer all national training programme data from CTS to FIPS by the end of March 2019. There is a risk that migration of data adversely affects information used to produce the financial statements.</p>	<p>Planning and user acceptance testing of data transfer.</p> <p>Data reconciliation and sampling.</p> <p>Internal audit's review of national training programmes including assurance mapping (a review of monitoring and</p>	<ul style="list-style-type: none"> <li>• Review of the implementation of the data transfer and controls over data transfer.</li> <li>• Focused testing of national training programmes transactions such as modern apprenticeship payments.</li> </ul>

	Audit Risk	Source of assurance	Planned audit work
		governance arrangements across modern apprenticeships).	<ul style="list-style-type: none"> <li>• Consideration of internal audit's review of national training programmes including assurance mapping.</li> </ul>
<b>Wider dimension issues and risks</b>			
<b>6</b>	<b>Financial management</b>	Continued discussions on affordability and programme delivery at board level and with the Scottish Government.	<ul style="list-style-type: none"> <li>• We will monitor financial reports provided to board/committee over the year and will compare to year-end result in the financial statements.</li> <li>• We will attend an SDS board meeting to observe the scrutiny undertaken with respect to the financial position.</li> </ul>
	<p>The approved SDS' budget for 2018/19 shows income and expenditure of £242 million. As in previous years, part of the core funding from the Scottish Government (£16 million) was to be confirmed through the Autumn and Spring Budget Revisions. Effective budget monitoring and accurate reporting of SDS' financial position and projected outturn to the board is therefore essential to support effective scrutiny. There is a risk that SDS will not receive sufficient funding to deliver its core services and fails to break even in 2018/19.</p>		
<b>7</b>	<b>Financial sustainability</b>	<p>Five-year financial plan in place with scenario planning and sensitivity analysis to identify the impact of potential spending review requirements.</p> <p>Risk recognised in the strategic risk register and discussed at board meetings and with the Scottish Government.</p>	<ul style="list-style-type: none"> <li>• Attendance at the budget-setting board meeting to observe any financial sustainability discussions.</li> <li>• Consideration of internal audit's review of financial planning.</li> </ul>
	<p>SDS maintains a five-year financial model to forecast expenditure based on a series of underlying assumptions and variables such as pay awards and volumes of activity in relation to the apprenticeship family. The financial model shows a significant funding gap going forward due to uncertainties over SDS' longer-term funding. This and increasing expectations such as rising apprenticeship targets present risks to the financial sustainability of SDS.</p>		
<b>8</b>	<b>Openness and transparency</b>	<p>SDS has previously agreed to review its publication policy regarding the availability of board and committee papers and committee minutes, and to further enhance disclosures in its 2018/19 financial statements.</p>	<ul style="list-style-type: none"> <li>• Consider SDS' review of the availability of board and committee papers and committee meeting minutes.</li> <li>• Review disclosures in the 2018/19 financial statements.</li> </ul>
	<p>There is an increasing focus on how public money is used and outcomes achieved. Openness and transparency supports understanding and scrutiny of the use of public money. SDS does not publish board and committee papers and committee meeting minutes on its website and there is scope for SDS to further enhance disclosures in the financial statements. There is a risk that SDS' activities and performance are not transparent to the public, impacting on the public's understanding of how SDS has</p>		

	Audit Risk	Source of assurance	Planned audit work
	applied public funds and what has been achieved.		
<b>9</b>	<p><b>Enterprise and skills review - strategic plan</b></p> <p>In October 2018, the enterprise and skills strategic board published its first strategic plan. The plan aims to provide clarity around strategic direction to SDS and other enterprise and skills agencies with the overall aim to increase productivity and drive inclusive and sustainable economic growth in Scotland. The agencies are expected to progress actions set out in the strategic plan through enhanced collaboration and alignment.</p> <p>There is a risk that transitioning to the new enterprise and skills arrangements has an adverse short-term impact on SDS' business and performance.</p>	<p>Regular chief executive's reports to the board.</p> <p>On-going engagement with the strategic board and the Scottish Government.</p> <p>Effective financial management and workforce planning arrangements.</p> <p>Rolling five-year financial model with scenario planning.</p>	<p>We will review how SDS is responding to the strategic plan and what impact the new enterprise and skills arrangements are having on SDS':</p> <ul style="list-style-type: none"> <li>governance arrangements regarding clarity over new roles, responsibilities and accountabilities</li> <li>strategic direction and its operations including its capacity to deliver on the existing and new duties and responsibilities and its income and expenditure</li> <li>performance management arrangements, in particular whether appropriate measures are in place to determine and report on the impact of the new arrangements.</li> </ul>
<b>10</b>	<p><b>European Union (EU) withdrawal</b></p> <p>The UK's decision to leave the EU on 29 March 2019 represents a major constitutional change for Scotland. It will affect everyone in Scotland to some degree including SDS. What these effects will be remains uncertain, but they will unfold over both the short and the long term. There is a risk that withdrawal from the EU adversely affects SDS' business.</p>	<p>Board's consideration of skills implications of the EU withdrawal.</p> <p>Rolling five-year financial model with well-developed scenario planning.</p> <p>Risk recognised in the strategic risk register and discussed at board meetings.</p>	<ul style="list-style-type: none"> <li>We will assess SDS' response to EU withdrawal.</li> </ul>

Source: Audit Scotland

## Reporting arrangements

**5.** Audit reporting is the visible output from the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

**6.** Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

**7.** We will provide an independent auditor's report to The Skills Development Scotland Co. Limited, the Scottish Parliament and the Auditor General for Scotland setting out our opinions on the annual accounts. We will provide the Accountable Officer and Auditor General for Scotland with an annual report on the audit

containing observations and recommendations on significant matters which have arisen during the audit.

## Exhibit 2

### 2018/19 Audit outputs

Audit Output	Target date	Committee Date
Interim Management Report	7 March 2019	14 March 2019
Annual Audit Report	TBC (June 2019)	TBC (June 2019)
Independent Auditor's Report	TBC (June 2019)	TBC (June 2019)

Source: Audit Scotland

### Audit fee

**8.** The proposed audit fee for the 2018/19 audit of SDS is £TBC [2017/18: £84,016]. In determining the audit fee, we have taken account of the risk exposure of SDS and the planned management assurances in place. Our audit approach assumes receipt of the unaudited annual report and financial statements, with a complete set of working papers package on 7 May 2019.

**9.** Where our audit cannot proceed as planned through, for example, late receipt of unaudited annual report and financial statements or delays in responding to our draft reports, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises out with our planned audit activity.

### Responsibilities

#### Audit and Risk Committee and Accountable Officer

**10.** Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

**11.** The audit of the annual accounts does not relieve management or the Audit and Risk Committee as those charged with governance, of their responsibilities.

#### Appointed auditor

**12.** Our responsibilities as independent auditors are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice (including supplementary guidance) and guided by the Financial Reporting Council's Ethical Standard.

**13.** Auditors in the public sector give an independent opinion on the financial statements and other information within the annual accounts. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

# Audit scope and timing

## Annual report and financial statements

**14.** The annual report and financial statements, will be the foundation and source for most of the audit work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of SDS and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how SDS will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free of material misstatement.

**15.** We will give an opinion on whether the financial statements:

- give a true and fair view in accordance with the directions made under the Public Finance and Accountability (Scotland) Act 2000 of the state of affairs of the company and its group as at 31 March 2019 and of the group's total comprehensive income for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2018/19 FReM; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and directions made under the Public Finance and Accountability (Scotland) Act 2000 by the Scottish Ministers.



characteristics



responsibilities



principal activities



risks



governance arrangements

## Other information in the annual accounts

**16.** We also review and report on other information published within the annual report and financial statements including the strategic report, directors' report, governance statement and the remuneration report. We give an opinion on whether these have been compiled in accordance with the appropriate regulations and frameworks in our independent auditor's report.

**17.** We also read and consider any information in the annual report and financial statements other than the financial statements and audited part of the remuneration report and report any uncorrected material misstatements.

## Materiality

**18.** We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinions in the independent auditor's report.

19. We calculate materiality at different levels as described below. The calculated materiality values for SDS are set out in [Exhibit 3](#).

### Exhibit 3 Materiality values

Materiality	Amount
<b>Planning materiality</b> – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross expenditure for the year ended 31 March 2019 based on the budget for 2018/19.	£2.42 million
<b>Performance materiality</b> – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement, we have calculated performance materiality at 60% of planning materiality.	£1.45 million
<b>Reporting threshold (i.e., clearly trivial)</b> – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount. This has been calculated at 1% of planning materiality.	£25,000

Source: Audit Scotland

### Timetable

20. To support the efficient use of resources it is critical that the annual report and financial statements timetable is agreed with us to produce the unaudited accounts. We have included an agreed timetable at [Exhibit 4](#).

### Exhibit 4 Annual report and financial statements timetable

 Key stage	 Date
Latest submission date of unaudited annual report and financial statements with complete working papers package	7 May 2019
Latest date for final clearance meeting with Senior Director Enabling Services	TBC (early June)
Issue of Letter of Representation and proposed independent auditor's report	TBC (early June)
Agreement of audited unsigned annual report and financial statements	TBC (mid June)
Issue of Annual Audit Report to those charged with governance	TBC (mid June)
Independent auditor's report signed	TBC (late June)

### Internal audit

21. Internal audit is provided by Scott Moncrieff. As part of our planning process we carry out an annual assessment of the internal audit function to ensure that it operates in accordance with Public Sector Internal Audit Standards (PSIAS). Subject to completion of this review, we plan to consider internal audit's work as outlined below.

### Using the work of internal audit

**22.** Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible to avoid duplication. We plan to consider the findings of the work of internal audit as part of our planning process to minimise duplication of effort and to ensure the total resource is used efficiently or effectively.

**23.** From our initial review of internal audit plans we plan to consider internal audit work in the following areas:

- GDPR
- Financial planning
- Assurance mapping
- National training programmes
- HR management information
- Business continuity planning.

**24.** To ensure a joined-up approach, we are also planning to liaise with the Highlands and Islands Enterprise (HIE) and Scottish Enterprise (SE) auditors on internal audit arrangements for Enterprise Information Systems (EIS) which deliver ICT services to SDS, HIE and SE. Internal audit for EIS is provided by Ernst and Young. From our initial review of internal audit plan, we will consider placing reliance on internal audit work carried out on general IT controls (previously known as the ISAE 3402 audit). We will also consider internal audit work in the following areas:

- Business continuity planning and disaster recovery
- Cyber security arrangements
- Digital strategy and governance arrangements.

### Audit dimensions

**25.** Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#).

## Exhibit 5

### Audit dimensions



Source: Code of Audit Practice

### Financial sustainability

**26.** As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on SDS' financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. We will consider internal audit's review of financial planning in the context of our own work in previous years and report on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability
- the appropriateness and effectiveness of arrangements in place to address any identified funding gaps.

### Financial management

**27.** Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We will review, conclude and report on:

- whether SDS has arrangements in place to ensure systems of internal control are operating effectively
- whether SDS can demonstrate the effectiveness of budgetary control system in communicating accurate and timely financial performance
- how SDS has assured itself that its financial capacity and skills are appropriate
- whether SDS has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

### Governance and transparency

**28.** Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information. We will review, conclude and report on:

- whether SDS can demonstrate that the governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency on the decision-making and finance and performance reports
- the quality and timeliness of financial and performance reporting.

### Value for money

**29.** Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether:

- SDS can provide evidence that it is demonstrating value for money in the use of its resources
- SDS can demonstrate that there is a clear link between money spent, output and outcomes delivered
- SDS can demonstrate that outcomes are improving and there is sufficient focus on improvement and the pace of it
- SDS' performance management framework supports the disclosures in the strategic report
- SDS has arrangements in place to support the Accountable Officer in his duty to secure best value in line with the Scottish Public Finance Manual.

### Independence and objectivity

**30.** Auditors appointed by the Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. The arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland's Ethics Partner.

**31.** The engagement lead (i.e. appointed auditor) for SDS is Gordon Smal, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of SDS.

### Quality control

**32.** International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

**33.** The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice (and supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews and internal quality reviews. Additionally, the Institute of Chartered Accountants of Scotland (ICAS) have been commissioned to carry out external quality reviews.

**34.** As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision.

We welcome feedback at any time and this may be directed to the engagement lead.

# Skills Development Scotland

## Annual Audit Plan 2018/19

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or [info@audit-scotland.gov.uk](mailto:info@audit-scotland.gov.uk)

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