

# Scottish Enterprise

2019/20 Annual Audit Report



 AUDIT SCOTLAND

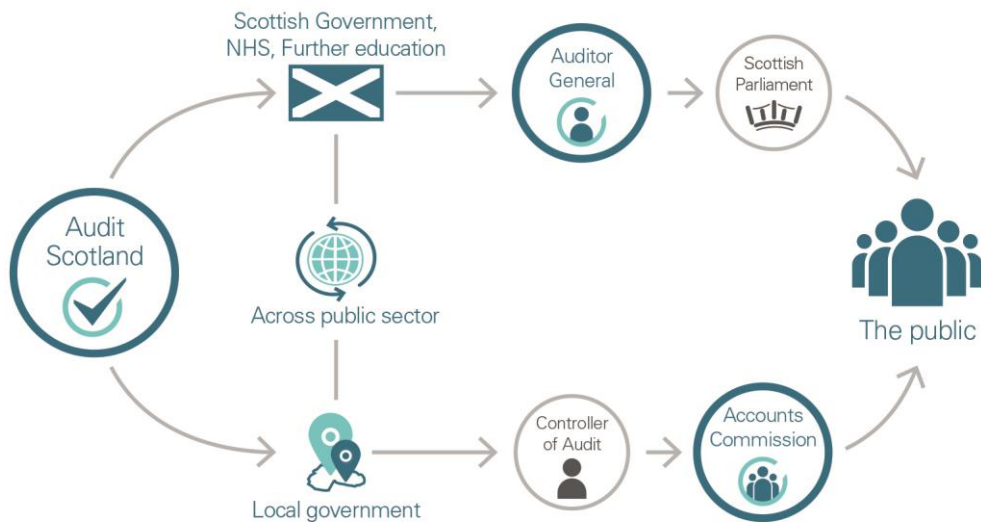
Prepared for Scottish Enterprise and the Auditor General for Scotland

16 July 2020

## 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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# Key messages

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## 2019/20 annual report and accounts

- 1** The financial statements of Scottish Enterprise and its group give a true and fair view of the financial position at 31 March 2020 and their net expenditure for the year.
- 2** The expenditure and income in the financial statements were incurred or applied in accordance with applicable enactments and guidance.
- 3** The other information in the annual report and accounts is consistent with the financial statements and was prepared in accordance with legal requirements.
- 4** An 'Emphasis of Matter' paragraph is included in the independent auditor's report to draw attention to the impact of Covid-19 on property valuations. The audit opinion is not modified in respect of this matter.
- 5** Due to the impact of Covid-19, the accounts and subsequent audit was delayed by about three weeks. Management provided good support, and the year-end audit ran smoothly.

## Financial management

- 6** Scottish Enterprise has effective financial management arrangements. It remained within the overall grant in aid budget for 2019/20.
- 7** Scottish Enterprise took action to address a forecast year-end overspend. This, together with an unanticipated reduction in planned investments due to Covid-19, resulted in an underspend against budget in 2019/20.
- 8** Systems of internal control operated appropriately and effectively in 2019/20, with scope for improvements in some areas.

## Financial sustainability

- 9** Scottish Enterprise does not yet have a longer-term financial plan. Continuing uncertainties about its operations, including the set-up of the Scottish National Investment Bank, have caused delays.
- 10** Scottish Enterprise is updating its 2020/21 financial plan to reflect the impact of Covid-19. It has yet to evaluate the longer-term effects on its business and finances.

## Governance and transparency

- 11** Scottish Enterprise has appropriate and effective governance arrangements in place. It made changes to its operating environment and governance arrangements in response to the impact of Covid-19.
- 12** The performance report included in the annual report and accounts meets the requirements of the FReM, with scope for further development.

## Value for money

- 13** Scottish Enterprise has an appropriate and effective best value framework in place.
- 14** Scottish Enterprise achieved its five primary outcome measures in 2019/20, exceeding their target ranges.

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# Introduction

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1. This report summarises the findings from our 2019/20 audit of Scottish Enterprise
2. The scope of our audit was set out in our Annual Audit Plan presented to the November 2019 meeting of the Audit and Risk Committee. This report comprises the findings from:
  - an audit of Scottish Enterprise's annual report and accounts
  - consideration of the four audit dimensions that frame the wider scope of public audit set out in the [Code of Audit Practice 2016](#) as illustrated in [Exhibit 1](#).

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## Exhibit 1 Audit dimensions



Source: *Code of Audit Practice 2016*

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3. The main elements of our audit work in 2019/20 have been:
  - a review of Scottish Enterprise's key financial systems
  - an audit of Scottish Enterprise's 2019/20 annual report and accounts including the issue of an independent auditor's report setting out my opinions
  - consideration of the four audit dimensions.
4. In common with all public bodies, Scottish Enterprise has had to respond to the global coronavirus (Covid-19) pandemic. This affected the final weeks of the financial year and will continue to have significant impact in 2020/21. Scottish

Enterprise together with the other enterprise agencies are managing the Scottish Government Covid-19 related business support funds. This includes the Creative, Tourism & Hospitality Enterprises Hardship Fund (£30 million) and the Pivotal Enterprise Resilience Fund (£120 million).

**5.** Our planned audit work has had to adapt to new emerging risks as they relate to the audit of the financial statements and the wider dimensions of audit. We had regular discussions with management following the lockdown in March 2020 to discuss the impact on Scottish Enterprise's work and the year-end audit.

**6.** As we undertook our audit planning work prior to the pandemic, we reviewed our assessment of audit risks and the planned audit work again in May 2020 and concluded that they remained relevant.

## Adding value through the audit

**7.** We add value to the body through the audit by:

- identifying and providing insight on significant risks, and making clear and relevant recommendations that have been accepted by management
- reporting our findings and conclusions in public
- sharing intelligence and good practice through our national reports ([Appendix 3](#)) and good practice guides
- providing clear and focused conclusions on the appropriateness, effectiveness and impact of corporate governance, performance management arrangements and financial sustainability.

## Responsibilities and reporting

**8.** Scottish Enterprise has primary responsibility for ensuring the proper financial stewardship of public funds. This includes preparing an annual report and accounts that are in accordance with the accounts' direction from the Scottish Ministers.

**9.** Scottish Enterprise is also responsible for establishing appropriate and effective arrangements for governance, propriety and regularity that enable the board to successfully deliver its objectives.

**10.** Our responsibilities as independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the [Code of Audit Practice 2016](#), and supplementary guidance and International Standards on Auditing in the UK. As public sector auditors we give independent opinions on the annual report and accounts.

**11.** Additionally, we conclude on the appropriateness and effectiveness of the performance management arrangements, the suitability and effectiveness of corporate governance arrangements, the financial position and arrangements for securing financial sustainability. Further details of the respective responsibilities of management and the auditor can be found in the [Code of Audit Practice 2016](#) and supplementary guidance.

**12.** This report raises matters from our audit. Weaknesses or risks identified are only those which have come to our attention during our normal audit work and may not be all that exist. Communicating these does not absolve management from its responsibility to address the issues we raise and to maintain adequate systems of control.

**13.** Our annual audit report contains an agreed action plan at [Appendix 1](#). It sets out specific recommendations, the responsible officer(s) and dates for implementation. It also includes any outstanding actions from last year and progress against these.

## Auditor independence

**14.** Auditors appointed by the Auditor General for Scotland 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.

**15.** We can confirm that we comply with the Financial Reporting Council's Ethical Standard. We can also confirm that we have not undertaken any non-audit related services and therefore the 2019/20 audit fee of £164,820 as set out in our Annual Audit Plan remains unchanged. We are not aware of any relationships that could compromise our objectivity and independence.

**16.** This report is addressed to both the body and the Auditor General for Scotland and will be published on Audit Scotland's website [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk) in due course.

**17.** We would like to thank the management and staff who have been involved in our work for their cooperation and assistance during the audit, particularly given the current challenges presented by the impact of Covid-19.



# Part 1

## Audit of 2019/20 annual report and accounts



### Main judgements

The financial statements of Scottish Enterprise and its group give a true and fair view of the financial position and their net expenditure.

The expenditure and income in the financial statements were incurred or applied in accordance with applicable enactments and guidance.

The other information in the annual report and accounts is consistent with the financial statements and prepared in accordance with legal requirements.

An 'Emphasis of Matter' paragraph is included in the independent auditor's report to draw attention to the impact of Covid-19 on property valuations. The audit opinion is not modified in respect of this matter.

Due to the impact of Covid-19, the accounts and subsequent audit was delayed by about three weeks. Management provided good support, and the year-end audit ran smoothly.

The annual report and accounts are the principal means of accounting for the stewardship of resources and performance.

### Our audit opinions on the annual report and accounts are unmodified

**18.** The annual report and accounts for the year ended 31 March 2020 were approved by the board on 15 July 2020. We reported within the independent auditor's report that:

- the financial statements give a true and fair view and were properly prepared
- expenditure and income were regular and in accordance with applicable enactments and guidance
- the audited part of the remuneration and staff report, performance report and governance statement were all consistent with the financial statements and properly prepared in accordance with the relevant legislation and directions made by Scottish Ministers.

**19.** We have included an 'Emphasis of Matter' paragraph in our independent auditor's report which refers to the impact of Covid-19 on the valuations of land and buildings. Emphasis of Matter paragraphs are added to auditors' reports where the auditor considers it necessary to draw users' attention to matters which are fundamental to the understanding of the accounts. The Statement of Accounting Policies in the financial statements describes the uncertainty caused. The audit opinion is not modified in respect of this matter. Further information is contained in [Exhibit 3](#) below.

**20.** In accordance with the WGA guidance we aim to complete the required assurance statement and submitted to the National Audit Office (NAO). We await

confirmation of the revised deadline for completing the assurance statement, but understand that this will be 30 November 2020 at the earliest.

## The annual report and accounts were signed off later than intended because of Covid-19

**21.** Scottish Enterprise and Audit Scotland staff worked from home for the duration of the audit because of the Covid-19 pandemic. We kept in regular communication with management throughout and revised the initial planned audit timetable.

**22.** Despite the challenges of remote working faced by Scottish Enterprise staff and the audit team, the audit was completed only three weeks later than originally planned.

**23.** The working papers provided to support the accounts were of a good standard. The audit team received good support from finance staff who responded quickly to audit queries which helped ensure the final accounts audit process ran smoothly.

**24.** As we have reported in previous years, the timetable for the financial statements audit is challenging for Scottish Enterprise and the audit team. The performance and accountability reports contain key financial and performance information which require close consideration. We do not receive these at the start of the audit, which increases the time pressures on Scottish Enterprise and the audit team later in the process. We shall discuss this again with management in planning next year's audit, taking account of the experience of the 2019/20 audit timetable.



### Recommendation 1

**Scottish Enterprise together with Audit Scotland should review the year end preparation and audit timetables. ([Appendix 1, action plan point 1](#))**

## Overall materiality is £3.4 million

**25.** The assessment of what is material is a matter of professional judgement. It involves considering both the amount and the nature of a misstatement in the financial statements.

**26.** On receipt of the unaudited annual report and accounts we reviewed our materiality calculations and concluded that they remained appropriate. We updated our calculation of materiality as shown in [Exhibit 2](#).

## Exhibit 2 Materiality values

Materiality level	Scottish Enterprise Group	Scottish Enterprise Single Entity
Overall materiality	£3.45 million	£3.4 million
Performance materiality	£2.07 million	£2.04 million
Reporting threshold	£150,000	£150,000

Source: Audit Scotland, Scottish Enterprise Annual Audit Plan 2019/20

## The main risks of material misstatement and our related work

**27.** [Appendix 2](#) provides our assessment of risks of material misstatement in the annual report and accounts and any wider audit dimension risks. These risks influence our overall audit strategy, the allocation of staff resources to the audit and indicate how the efforts of the audit team were directed. [Appendix 2](#) also identifies the work we undertook to address these risks and our conclusions.

**28.** We undertook our planning work and issued our 2019/20 annual audit plan in November 2019, prior to the Covid-19 pandemic. In line with auditing standards and professional advice, including the [Financial Reporting Council's Covid-19 bulletin](#) published in March 2020, we reviewed our assessment of audit risks and the planned audit work in May 2020 and concluded that they remained relevant. There have not been any changes to audit risks or our audit approach, and there was no significant impact on the timing of our audit.

**29.** Matters arising from our work on the risks of material misstatements include risks relating to management judgement and estimation and are discussed further at [Exhibit 3](#) below.

## Findings to report on the annual report and accounts

**30.** International Standard on Auditing (UK) 260 requires us to communicate significant findings from the audit to those charged with governance, including our view about the qualitative aspects of the body's accounting practices. The more significant findings are summarised in [Exhibit 3](#). Where a finding has resulted in a recommendation to management, a cross-reference to the Action Plan in [Appendix 1](#) is included.

## Exhibit 3

### Significant findings from the audit of financial statements

Issue	Resolution
<p><b>1. Impact of Covid-19 on the valuations of land and buildings</b></p> <p>Scottish Enterprise's land and buildings (£146 million) are revalued annually by an external valuer, Montagu Evans. The final valuation report was delayed due to the impact of Covid-19.</p> <p>Montagu Evans' report contains a 'material valuation uncertainty' clause regarding the impact of Covid-19. It points out that a higher degree of caution should be attached to the valuation than would normally be the case.</p> <p>The unaudited accounts did not make reference to this material uncertainty as the final wording of the clause was to be confirmed by the valuer.</p>	<p>We discussed this with Finance staff who agreed to include an appropriate disclosure in the accounting policy on critical accounting estimates and judgements.</p> <p>We added an Emphasis of Matter paragraph to the independent auditor's report because we believe the disclosure is fundamental to users' understanding of the accounts.</p> <p>The audit opinion is not modified in respect of this matter.</p> <p>We have sought and received the Accountable Officer's assurances on management's assessment of the fair value of land and property in the ISA 580 representation letter.</p>
<p><b>2. Impact of Covid-19 on the fair value of financial instruments</b></p> <p>The financial statements include financial assets (£317 million), mainly valued by the Scottish Investment Bank (SIB), Scottish Enterprise's in-house investments team. The majority of these are early-stage, unlisted investments and loans to start-up companies.</p>	<p>We discussed this with Finance staff who agreed to incorporate an appropriate disclosure in the accounting policy on critical accounting estimates and judgements.</p> <p>We assessed a sample of SIB's valuations and assessed SIB under ISA 620 'Using the Work of an Expert'. We were satisfied that their approach was reasonable.</p>

Issue	Resolution
<p>Due to the nature of the investment portfolio, the majority of these (£306 million) are categorised as 'level 3' in accordance with IFRS 13 'Fair Value'. These require a higher level of professional judgement and subjectivity because the valuation is not based on observable market data (e.g. quoted share price).</p> <p>SIB's valuation took account of International Private Equity and Venture Capital Valuation (IPEV) guidelines and considered the level of risk across the investment portfolio. These valuations included a preliminary assessment of the impact of Covid-19.</p> <p>The unaudited accounts presented for audit did not make reference to the potential impact of Covid-19 on the fair value of investments.</p>	<p>We have sought and received the Accountable Officer's assurances on management's assessment of the fair value of financial instruments in the ISA 580 representation letter.</p>
<p><b>3. Support for subsidiaries</b></p> <p>Each year, Scottish Enterprise provides a letter of support to each 'live' subsidiary confirming its continuing financial commitment.</p> <p>Due to current circumstances involving the impact of Covid-19, two of Scottish Enterprise's subsidiaries are facing specific financial challenges that may require assistance from their parent company.</p> <p>The unaudited accounts presented for audit did not make reference to this matter.</p>	<p>We discussed the impact on Scottish Enterprise's budget for 2020/21 and management agreed that appropriate disclosure should be made in the financial statements.</p> <p>Management added a reference to the potential support required within note 19, contingent liabilities.</p> <p>We are content with this disclosure.</p>

Source: Audit Scotland

## The financial statements were adjusted to reflect the late receipt of information and other identified misstatements of £4.3 million

**31.** Presentational and monetary adjustments to the accounts identified during the audit were discussed with management who agreed to amend the financial statements. There are no remaining unadjusted misstatements in excess of our reporting thresholds.

**32.** There were material adjustments to the unaudited annual report and accounts which arose from the late receipt of the land and property valuation report. Of the total adjustments processed (£4.3 million), £2.6 million were in relation to the updated valuation figures. This is an isolated issue and does not represent systemic error. The balance of the adjustment related to a land disposal transaction at Dover Heights where both income and expenditure were adjusted by £1.7 million with no impact on the reported financial position.

**33.** The net effect of the adjustments identified during the audit and processed by management was to increase the Scottish Enterprise single entity net expenditure by £1.3 million and decrease net assets by £1.8 million. The group accounts were affected by the changes in the Scottish Enterprise single entity: the net effect of the adjustments processed increased net expenditure by £0.7 million and increase net assets by £1.7 million.

## Other matters arising from the audit of the accounts

**34.** We highlighted below other significant matters identified during our audit.

**35. Financial instruments: expected credit loss (ECL).** IFRS 9 Financial Instruments was adopted from 1 April 2018. This requires an assessment of the expected credit loss and consideration of the general impairment methodology. Scottish Enterprise has reviewed its financial assets and recognised a total ECL on its financial assets held at amortised cost of £12.3 million, which is a £7.3 million increase since 2018/19. This ECL reflects the current economic climate in relation to the impact of Covid-19 and other business factors. We consider the estimation methodology applied by Scottish Enterprise is reasonable.

**36.** We note that the process could be improved by better documenting the estimation rationale to demonstrate the assessment of past experience together with future assessments of future economic performance. We have sought and received the Accountable Officer's assurances on management's assessment of the fair value of financial instruments in the ISA 580 representation letter.



### Recommendation 2

**Management should fully document their processes for assessing expected credit loss. The review process should include liaison with other public and private sector partners to share best practice in the assessment of ECL. ([Appendix 1, action plan point 2](#))**

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**37. Trade and other receivables: accrued EU income.** Scottish Enterprise's accounts include £4.77 million of accrued income for EU funded grants. In previous years, we have reported that Scottish Enterprise has written down the level of accrued income. This is because the standard of evidence required from third parties to support Scottish Enterprise's claims for European funding was, in many cases, insufficient.

**38.** We reviewed the methodology for accruing EU income and concluded that the methodology was reasonable. We have sought and received the Accountable Officer's assurances on management's assessment of the amount receivable in the ISA 580 representation letter.

**39. Guaranteed Minimum Pension (GMP).** The courts have ruled that UK defined benefit pension schemes must compensate members for differences attributable to guaranteed minimum pensions. In line with 2018/19, Scottish Enterprise's actuary has advised that a 'trigger event' is yet to occur. Scottish Enterprise has added a contingent liability note to its accounts to explain and disclose this matter. We are content with the disclosures.

**40. Impairments.** There are a number of impairments of amounts due to Scottish Enterprise recorded in the financial statements which are due to be written off or have been impaired for several years without any change to the balances. Management has agreed to commence approving the write-off of these balances.

**41. Intangible assets.** The 2019/20 accounts included four capitalised intangible assets. These projects did not have separate account codes, and the split of contractor costs was calculated retrospectively by management based on their knowledge of the workload and project each contractor was working on. Evidence detailing the basis for the split was not retained. Whilst we consider that the costs capitalised are appropriate, management has agreed to create separate ledger accounts for each intangible asset in future to allow the costs to be more clearly identified.

## Some progress was made on prior year recommendations

**42.** Scottish Enterprise has made some progress in implementing our prior year audit recommendations. For actions not yet implemented, revised responses and timescales have been agreed with management, and are set out in [Appendix 1](#).

**43.** We are pleased to note that Scottish Enterprise has capitalised expenditure resulting in intangible assets, including assets in development (£2.0 million). Previously, expenditure of this nature was treated as revenue expenditure.

# Part 2

## Financial management



### Main judgements

Scottish Enterprise has effective financial management arrangements, and it remained within its overall grant in aid budget for 2019/20.

Scottish Enterprise took action to address a forecast year-end overspend. This, together with an unanticipated reduction in planned investments due to Covid-19, resulted in an underspend against budget in 2019/20.

Systems of internal control operated appropriately and effectively in 2019/20, with scope for improvements in some areas.

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

### Scottish Enterprise operated within budget in 2019/20

44. Scottish Enterprise's overall objective is to fully utilise available resources to maximise economic development outcomes, whilst ensuring that the financial outturn for the year is within the budget allocated by Scottish Ministers.

45. In 2019/20, Scottish Enterprise reported an outturn of £263.6 million, remaining within its overall budget with an underspend of £7.3 million. The financial performance against Departmental Expenditure Limits (DEL) is shown in [Exhibit 4](#).

### Exhibit 4 Performance against DEL in 2019/20

Performance	Initial budget £m	Autumn Budget Review £m	Spring Budget Review £m	Final budget £m	Outturn £m	Over/(under) spend £m
Resource DEL	133.820	+3.470	+4.678	141.968	139.680	(2.288)
Capital DEL	42.035	-0.500	+16.149	57.684	57.213	(0.471)
Financial Transactions	68.500	-	+7.800	76.300	70.661	(5.639)
Financial Transactions Income	-		(5.000)	(5.000)	(3.923)	1.077
<b>Total DEL</b>	<b>£244.355</b>	<b>2.97</b>	<b>23.627</b>	<b>270.952</b>	<b>263.631</b>	<b>(7.321)</b>

Source: Grant in Aid Letters from Scottish Government to Scottish Enterprise; Scottish Enterprise 2019/20 Annual Report and Accounts



## Budget processes were appropriate but required particularly close management towards the year-end

46. Scottish Enterprise had an initial grant in aid budget of £244.4m. As shown in the table above, it received additional funding from the Scottish Government in the Autumn and Spring Budget Revision. An anticipated late allocation was confirmed in May 2020 to cover additional costs incurred arising from Brexit preparations and the set-up of South of Scotland Enterprise.

47. We have previously highlighted that Scottish Enterprise's budget contained a high level of commitments with expenditure phased towards the end of the financial year. We reviewed Scottish Enterprise's budget management processes during 2019/20 and noted that most of the committed expenditure took place, with less slippage compared with previous years.

48. Scottish Enterprise generated additional income of £9.2 million in 2019/20, largely through its investments and from property disposals. Management planned to use the income to offset committed expenditure but was required to remit it to the Scottish Government. Scottish Enterprise returned £8.6 million in 2019/20, with the remainder due to be returned in 2020/21.

49. At the beginning of the final quarter of the financial year, Scottish Enterprise was forecasting an overall underspend of £2.2m with very limited headroom on Resource and Capital budgets. To ensure that a balanced budget was achieved, management introduced a recruitment freeze and restricted planned expenditure which had not been legally committed. This, together with a slowdown of expenditure in the final weeks of 2019/20 linked to Covid-19, contributed to a reduction in expenditure and an overall underspend against budget.

50. Scottish Enterprise re-profiles its budget on a monthly basis. A comprehensive mid-year budget rebasing took place in August 2109 to reallocate funding and to achieve a balanced budget.

51. We concluded that Scottish Enterprise's finance reports provide a good level of detail to management and board members to allow them to assess financial performance and take informed actions. This included deferring planned investment, restricting uncommitted planned expenditure, and information about proposed savings in business areas.

## Financial systems of internal control are operating effectively

52. As part of our audit we identify and inspect the key internal controls in those accounting systems which we regard as significant to produce the financial statements. Our objective is to gain assurance that the systems of recording and processing transactions provide a sound basis for the preparation of the financial statements.

53. Our interim Management Report which we presented to the Audit and Risk Committee in April 2020 identified areas for improvement and related management actions. Additionally, as part of our year-end audit, we identified that there was no formal reconciliation between the Investment Management Reporting System (IMRS) and the financial general ledger (SUN). Management confirmed that SUN is the primary system for financial management of the investments and noted IMRS reads financial information from SUN. Management should formalise the reconciliation between SUN and IMRS to further improve the control environment.



### Recommendation 3

**Management should formally reconcile the SUN and IMRS systems to further improve the control environment. (Appendix 1, action plan point 3)**



**54.** Overall, we are content that Scottish Enterprise's control environment operates effectively.

### **Internal audit is effective**

**55.** Scottish Enterprise has an in-house internal audit department. Specialist IT audit services are provided by an independent third party on behalf of Scottish Enterprise and their partners in Enterprise Information Services (EIS), the shared IT arrangement with Skills Development Scotland (SDS) and Highlands and Islands Enterprise (HIE).

**56.** In 2019/20, Scottish Enterprise started to share internal audit arrangements with SDS. In 2020/21, it further extended these arrangements to include the Scottish Funding Council and South of Scotland Enterprise. The internal audit team was restructured to facilitate the expanded service. Partner organisations contribute to the costs of services to ensure it is cost neutral to Scottish Enterprise.

**57.** We reviewed Scottish Enterprise's internal audit arrangements in accordance with International Standard on Auditing (UK) 610 'Using the Work of Internal Auditors' and were able to take account of its findings as planned.

### **Standards of conduct and arrangements for the prevention and detection of fraud and error are appropriate**

**58.** Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.

**59.** We reviewed the arrangements in place at Scottish Enterprise to maintain standards of conduct including the Staff and Members' Codes of Conduct. We also reviewed the counter fraud policy, response plan and whistleblowing policy.

**60.** We concluded that there are established procedures for preventing and detecting any breaches of these standards including any instances of corruption. We are not aware of any specific issues that we need to bring to your attention.

### **Arrangements for preventing fraud and corruption in the procurement function are appropriate**

**61.** Our consideration of financial management included an evaluation of Scottish Enterprise's arrangements for preventing and detecting fraud and corruption in its procurement function.

**62.** We reported the findings in our interim Management Report which was presented to the Audit and Risk Committee in April 2020. We concluded that management's procedures to address the risk of fraud and corruption were largely appropriate, with the need to document procurement delegation limits in the procurement guidance.

### **Finance team capacity remains under review**

**63.** We have previously highlighted potential risks relating to capacity within Scottish Enterprise's finance function. There was a significant reorganisation of the finance team during 2019/20. The Head of Financial Accounting and the Chief Finance Officer left Scottish Enterprise in July and September 2019 respectively.

**64.** From April 2019, the Chief Finance Officer's (CFO) role was merged with the Chief People Officer (CPO). The Director of Finance reported to the CPO and the role was widened to include risk, legal and procurement. The Director of Finance provided a support role to the Board and Executive Leadership Team on financial matters and presented the finance performance reports.

**65.** In April 2020, the CFO role was reinstated within the Executive Leadership Team and the Director of Finance role was merged with the CFO role. Except for risk, all other responsibilities remain with the CPO.

**66.** This change, only 12 months after the initial restructure, recognises the significance of financial knowledge and experience at the highest level of the organisation. Financial input to strategic decisions is particularly important, given the in-year volatility in Scottish Enterprise's budget and the ongoing changes including: the move to a simplified grant product portfolio; the creation of the Scottish National Investment Bank (SNIB), and the South of Scotland Enterprise Agency (SoSE); and, now, the impact of Covid-19.

**67.** We noted in our interim Management Report that two of the four posts in the financial accounting team had been vacant since Summer 2019. These vacancies exacerbated the pressure on the Finance team during a period of ongoing change and following the loss of significant experience. These posts remain unfilled, but we understand that Scottish Enterprise is making good progress in its recruitment.

# Part 3

## Financial sustainability



### Main judgements

**Scottish Enterprise does not yet have a longer-term financial plan. Continuing uncertainties about its operations, including the set-up of the Scottish National Investment Bank, have caused delays.**

**Scottish Enterprise is updating its 2020/21 financial plan to reflect the impact of Covid-19. It has yet to evaluate the longer-term effects on its business and finances.**

Financial sustainability looks forward to the medium and longer-term to consider whether a body is planning effectively to continue to deliver its services or the way in which they should be delivered.

### The 2020/21 budget is under review for the impact of Covid-19

**68.** The draft 2020/21 budget was approved by the Board in March 2020. This was later revised to take account of changes to budget requirements and income projections in light of Covid-19. The initial projected deficit for 2020/21 of £10.5 million was revised to a deficit of £7.9 million.

**69.** In response to Covid-19, the Scottish Government issued an interim letter of guidance to all enterprise and skills bodies in April 2020. This noted that the challenges caused by the pandemic would likely supersede 2020/21 business planning. The guidance acknowledged that, whilst agencies would need to deliver contractual commitments, all other resources should be prioritised to meet the emerging fiscal, economic and social challenges posed by Covid-19.

**70.** Given the ongoing impact of Covid-19 and changes to its operating environment, Scottish Enterprise is reviewing its 2020/21 budget regularly to reflect the evolving position. As at the end of May 2020, the forecast position is an overall deficit of £3.5 million, including a deficit on the resource budget of £6.3 million. The June 2020 board meeting was advised of a range of key risks affecting the financial position together with additional demand on each element of the budget. Scottish Enterprise has requested additional funding from the Scottish Government.

**71.** Since April 2020, Scottish Enterprise has worked with public sector partners, including HIE, SoSE, Creative Scotland and Visit Scotland to deliver grant funding to support businesses adversely impacted by Covid-19. This has been done through the Creative, Tourism & Hospitality Enterprises Hardship Fund and the Pivotal Enterprise Resilience Fund, which have a combined total £150 million funding. As at mid-June, 2,982 applications had been successful with awards of over £124 million offered to applicants.

**72.** Scottish Enterprise has also considered alternative support that can be provided to private sector bodies. In accordance with Scottish Government guidance, it has allowed rental concessions for commercial property tenants and loan repayments have been rescheduled.

## Scottish Enterprise has yet to develop a longer-term plan

**73.** Scottish Enterprise has a one-year financial plan but does not have a medium or longer-term financial plan. The June 2020 board meeting was provided with a high-level assessment of planned expenditure, projected income and future commitments across 2021/22 and 2022/23. This highlighted the level of contractual commitments and the resulting discretionary budget available to spend.

**74.** Management informed us that the delay in implementing longer-term plans was as a result of ongoing uncertainty. This was firstly as a result of the Enterprise and Skills Review and then the subsequent announcements regarding South of Scotland Enterprise and the Scottish National Investment Bank (SNIB). SoSE became operational in June 2020, with the SNIB expected to become operational later in 2020. The transfer of Scottish Enterprise's financial assets to SNIB is planned to take place over the next three years.

**75.** As noted, the 2020/21 budget identifies a deficit which will require management to take action to ensure a balanced position at the year end. The rescheduling of loan repayments as a consequence of Covid-19 will potentially affect the planned Financial Transactions income which forms part of Scottish Enterprise's overall funding.

**76.** Scottish Enterprise has committed to making grant expenditure and other funding in future years. A longer-term plan would highlight committed expenditure and would provide further information to help identify and manage future spending pressures.



### Recommendation 4

**Scottish Enterprise should develop a longer-term financial strategy, supported by clear and detailed financial plans which align with the corporate plan. ([Appendix 1, action plan point 4](#))**

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# Part 4

## Governance and transparency



### Main judgements

**Scottish Enterprise has appropriate and effective governance arrangements in place. It made changes to its operating environment and governance arrangements in response to the impact of Covid-19.**

**The performance report included in the annual report and accounts meets the requirements of the FReM, with scope for further development.**

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.

### Overall governance arrangements were appropriate

**77.** Scottish Enterprise is governed by a board that is accountable to the Scottish Ministers. At 31 March 2020, the board consisted of the chair, eight non-executive members and the chief executive. Lord Smith of Kelvin was appointed as Chair from 1 August 2019. The Chair of the Audit and Risk Committee was acting Chair until Lord Smith's appointment.

**78.** There were six board meetings during 2019/20. The board is also supported by three committees: Audit and Risk, Nominations and Governance; and Remuneration.

**79.** In assessing governance and transparency, we consider:

- board and committee structure and conduct
- overall arrangements and standards of conduct including those for the prevention and detection of fraud, error, bribery and corruption. This includes action in response to the National Fraud Initiative
- openness of board and committees
- public access to information via websites
- reporting of performance and whether this is fair, balanced and understandable.

**80.** We concluded that Scottish Enterprise had appropriate governance arrangements in place during 2019/20.

### Covid-19 has affected governance

**81.** Actions taken by Scottish Enterprise in response to the impact of Covid-19 are set out in its 2019/20 annual report and accounts. There is a specific Covid-19 response team which has workstreams across operational areas and daily

Executive Leadership Team meetings. Governance arrangements were adapted to record decisions and weekly board catch-ups are held to discuss the situation.

**82.** Internal audit has reviewed on a real time basis, Scottish Enterprise's Covid-19 response and reported to the Audit and Risk Committee in April 2020. From our work and internal audit's report, we note the following steps:

- All staff have been working remotely from home since 23 March 2020 following the UK government's lockdown guidance. Guidance for staff/people managers has been prepared and updated regularly. There has been regular communication with staff.
- Finance staff have reconfigured processes to allow payments and other financial transactions to take place remotely. Management has confirmed that segregation of duties and other key controls remain in place.

**83.** We have had preliminary discussions with management about these new arrangements and will assess them as part of our 2020/21 audit.

**84.** Overall, Scottish Enterprise is proactive in dealing with the changed operating environment. The scale and pace of change as a result of Covid-19 poses a risk to the key financial controls within the finance department, including those relating to new grants designed to support the economy. Management should ensure that the new processes and grants are effective and that there is sufficient, well-documented governance to inform and support all decisions.



### Recommendation 5

**Scottish Enterprise should ensure that internal controls remain effective during this period of uncertainty and new ways of working. ([Appendix 1, action plan point 5](#))**

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## Risk management arrangements are effective

**85.** We reviewed Scottish Enterprise's risk management arrangements and the risks identified during the year. The board reviews risk management annually and considers the risk appetite for different categories of risk. The corporate risk register is presented to each meeting of the Audit and Risk Committee and is managed by the Executive Leadership Team. Each business area has its own risk register, which feeds into the corporate risk register.

**86.** During 2019/20, the approach to risk was reviewed and is now presented in a 'dashboard' format which is presented to each meeting of the board alongside the performance report. This highlights the risk appetite across the corporate risks and major projects. These new arrangements continue to evolve and bed in.

**87.** Internal audit reviewed risk management and concluded that Scottish Enterprise has most of the key elements of a positive risk management framework. Internal audit found that there is scope for further development, which would further support a successful risk culture and enhance consistency of the approach across all areas of the business.

**88.** Overall, we concluded that Scottish Enterprise's risk management arrangements are effective and reporting arrangements are appropriate.

## Openness and transparency remain a focus for attention

**89.** There continues to be a focus on how public organisations demonstrate the best use of public money. Openness and transparency in how a body operates and makes decisions is key to supporting understanding and scrutiny. Transparency

means that the public have access to understandable, relevant and timely information about how the board is taking decisions and how it is using resources such as money, people and assets.

**90.** We reported previously that board and committee meetings are not open to the public. Board minutes are published on the Scottish Enterprise website, but no other papers or minutes are available. Management considers that, due to the confidential and sensitive nature of much of the board's business, (e.g. deciding whether to award grants and investments), it would not be inappropriate to publish all board and committee papers. In our view, this area should be kept under review to ensure practices are in line with good practice and public expectations.

### The performance report could be further improved

**91.** In addition to the opinion on the performance report covered in Part 1 of our Annual Audit Report, we also consider the qualitative aspects of the performance report. The purpose of a performance report is to provide information on the main objectives and strategies, and the principal risks that it faces. It is required to provide a fair, balanced and understandable analysis of performance and is essential in helping stakeholders understand the financial statements. The performance report is an opportunity for the organisation to 'tell its story' about what it has achieved with the funding made available to it.

**92.** From our review of the annual report presented for audit, we concluded that there was scope to provide a more balanced picture of performance in 2019/20. We discussed a range of matters with management who agreed to update the narrative. We consider that the revised narrative provides a more complete picture of the challenges, activities and actions across 2019/20 and we concluded that Scottish Enterprise's performance report met the requirements of the FReM.

**93.** Annex 5 of the FReM gives additional guidance for narrative reporting. It refers to the use of trend analysis, balanced reporting, plain English, use of infographics and advises the preparer to go beyond the minimum requirements. In our view, Scottish Enterprise's performance report could be enhanced by using diagrams and tables and by linking better the individual sections. Further guidance can be found in Audit Scotland's 2019 report: [Good Practice Note on Performance Reports in Central Government](#).



#### Recommendation 6

**Scottish Enterprise should review the content and presentation of its performance report to ensure it takes full advantage of the opportunity to communicate directly to stakeholders about its activities. ([Appendix 1, action plan point 6](#))**

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### EIS governance arrangements have improved and work is ongoing to strengthen cyber security

**94.** Scottish Enterprise's information technology services are mostly managed by the Enterprise Information Services (EIS). EIS is the shared IT arrangement with Skills Development Scotland (SDS) and Highlands and Islands Enterprise (HIE). The EIS Partnership Board provides the strategic oversight of the EIS partners, which has been in place for just over 10 years. From April 2020, South of Scotland Enterprise has also joined the partnership.

**95.** The partnership has appointed a specialist internal auditor for EIS. Its September 2019 report on cyber security was graded 4 (the second highest priority for attention) with a recommendation to carry out a cyber maturity assessment. EIS is currently implementing this recommendation with the assessment due to conclude in summer 2020. Going forward, the partnership will need to consider the



maturity level it wants to achieve. After any identified gaps are addressed, the partnership may look to achieve Cyber Essentials+ accreditation.

**96.** Internal audit also assessed EIS governance and strategy at grade 3. We noted that EIS strengthened its governance arrangements in response to this report:

- the shared services programme board has been introduced which deals with day-to-day management matters
- the security council has been introduced to deal with security matters, including cyber security
- the product council is responsible for creating, discussing and putting in place shared services and products. Its role has changed and is now partner led instead of technology led.

**97.** All partners agree that EIS is an appropriate delivery vehicle for information technology and that greater convergence of digital provision is desirable. More work is ongoing, and we will continue to monitor developments as part of our audit.

### **South of Scotland Enterprise was established from 1 April 2020**

**98.** During 2019/20, Scottish Enterprise continued to work with other enterprise agencies to support the establishment of SoSE. SoSE assumed its functions on 1 April 2020 and transitional arrangements are documented in a Memorandum of Understanding.

**99.** Covid-19 delayed the passage of legislation in the Scottish Parliament and, as a result, Scottish Enterprise transferred land and buildings (£2.4 million) to SoSE on 1 June 2020. £2.3 million of Scottish Enterprise's funding has been transferred to SoSE in 2020/21. Scottish Enterprise still has staff working in the South of Scotland area to deliver Scotland-wide enterprise activity in line with Scottish Enterprise's continuing remit.

**100.** Internal audit reviewed the SoSE transition and reported during the year. It found that the South of Scotland Transition Team within Scottish Enterprise provided oversight of the activities undertaken by SoSE and facilitated engagement with key stakeholders and Scottish Enterprise staff. A transition plan was established to manage the process, with further internal controls and a separate risk register.

### **Scottish National Investment Bank is expected to be operational later in 2020**

**101.** SNIB is expected to be operational later in 2020. Scottish Enterprise's financial assets were due to be transferred to SNIB on its inception. Scottish Enterprise has indicated that this is now subject to further review and will not take place until 1 to 3 years after SNIB's creation to allow SNIB to identify its investment priorities.

**102.** Internal audit reviewed Scottish Enterprise's work on the SNIB transition and reported during the year. It found that good governance arrangements were in place, including a joint transition governance group and regular contact with the Scottish Government. Scottish Enterprise undertook a legal due diligence exercise to ensure that there are transfer clauses for the financial assets that are due to transfer to SNIB.

**103.** Internal audit noted that the SNIB transfer is likely to affect Scottish Enterprise's future funding, with Financial Transactions funding for new investments directed to SNIB. Internal audit noted the risk that the delay in transferring assets may lead to uncertainty regarding the respective roles of Scottish Enterprise and SNIB and ongoing uncertainty for staff in the Scottish



Investment Bank. Management should continue to work to address these risks and ensure that Scottish Enterprise remains prepared for the SNIB transition.

### Good practice

**104.** The [Code of Audit Practice 2016](#) encourages auditors to identify good practice which in their opinion is worth sharing more widely.

**105.** Scottish Enterprise's Head of Legal presented a review of laws and regulations that affect Scottish Enterprise to the Audit and Risk Committee in November 2019. This was a thorough review and demonstrated effective governance and provided assurance to the Audit and Risk Committee. We consider that this review demonstrates good practice.

# Part 5

## Value for money



### Main judgements

**Scottish Enterprise has an appropriate and effective best value framework in place.**

**Scottish Enterprise achieved its five primary outcome measures in 2019/20, exceeding their target ranges.**

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

### Scottish Enterprise has an appropriate best value framework

**106.** *Ministerial guidance to Accountable Officers* for public bodies and the *Scottish Public Finance Manual* (SPFM) sets out the accountable officer's duty to ensure that arrangements are in place to secure best value. The guidance sets out the key principles of best value and the requirement to have a systematic approach to self-evaluation and continuous improvement.

**107.** The Chief Executive of Scottish Enterprise is the designated Accountable Officer. A range of processes are in place to help the Accountable Officer demonstrate best value. The annual report and accounts outline how the best value attributes and practices are embedded through its assurance and self-assessment processes. These include:

- sound and developing corporate governance arrangements to reflect the changing roles and structures within the organisation
- the development of a three-year strategic plan together with an annual business plan
- budgets and resources are regular monitored
- a systematic risk management approach

### Covid-19 has an impact on performance

**108.** Covid-19 has had an impact on Scottish Enterprise's performance, and recent performance reporting to the board reflect the very fast-moving environment as the enterprise agencies and Scottish Government react. Performance reports now focus more on the workstreams and activities that will help to restart the economy. No target ranges have been set for the 2020/21 primary outcome measures due to the ongoing uncertainties although performance to date is being measured and compared against 2019/20. There is no 2020/21 operating plan given these uncertainties.

## Performance reporting is changing

**109.** The Enterprise and Skills Strategic Board (ESSB) is designed to align and coordinate the activities of Scotland's enterprise and skills agencies, including Scottish Enterprise, Skills Development Scotland, Highlands and Islands Enterprise and the Scottish Funding Council.

**110.** In October 2018, the ESSB published a Strategic Plan, which contained common policy missions that the enterprise and skills agencies are required to work towards. It also contained a high-level performance framework, against which the ESSB can assess the bodies' progress to achieving these missions.

**111.** Scottish Enterprise's 2019-22 Corporate Strategy is designed to align Scottish Enterprise's performance management framework to the ESSB's Strategic Plan. The 2019/20 Operating Plan includes five key measures, which are also used to demonstrate alignment with the ESSB Strategic Plan.

**112.** The Scottish Government has established an Analytical Unit to support the Strategic Board in its decision-making and assessment of the agency's performance. Scottish Enterprise works closely with the Unit to lead or support analytical activities.

**113.** To support the ESSB and coordinate collaboration between the Agencies, the Strategic Plan Joint Working Group (SPJWG) was formed. Membership of the SPJWG is drawn from each of the agencies along with the Sponsor Division and Analytical Unit. The initial focus of the SPJWG was to support the ESSB in developing its strategic plan and ensuring that each agency's own strategic plan aligned. Following publication of the ESSB's strategic plan in October 2018, and the aligned agency plans in April 2019, the group is now focusing on further developing the aligned agency plans and developing the performance framework which was included in the ESSB's strategic plan.

**114.** Internal audit undertook a review of Scottish Enterprise's arrangements and considered whether they were appropriate to ensure alignment with the ESSB, including successful partnership and collaboration with the other agencies. Internal audit found that:

- Scottish Enterprise's Strategic Framework demonstrates clear alignment with the ESSB plan and includes sections which are common to all agency plans, for example a table outlining how each agency will collaborate and contribute towards the actions and recommendations recorded in the ESSB Plan.
- Scottish Enterprise is playing its part in delivering the Scottish Government's objectives, through chairing the SPJWG, providing support and advice to the ESSB's Programme Management Office and the Analytical Unit and by leading and/or participating in the Mission Groups, which are tasked with delivering on the mission actions and recommendations'.

**115.** The day to day performance of individual agencies against their own performance measures is reported to their own boards and management teams, rather than to the ESSB. Scottish Enterprise presents a regular performance report to the board. These report against the five primary outcomes (also known as published measures) in Scottish Enterprise's 2019/20 operating plan. The primary outcomes are supported by several supporting measures, all of which will help to achieve the overall objective. The report also includes details of performance against the Inclusive and Sustainable Growth measures outlined in the Scottish Government's National Performance Framework. Arrangements are in place to monitor the achievement of outcomes.

## **Scottish Enterprise achieved its primary outcome measures in 2019/20**

**116.** The 2019/20 annual report and accounts highlights the achievement of the five primary outcome measures with all exceeding their related target ranges. The report also refers to the challenges of achieving the target range for new and safeguarded jobs paying at least the real living wage which was only achieved very late in the financial year.

## **National performance audit reports**

**117.** Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. In 2019/20 several reports were published which are of direct interest to Scottish Enterprise. These are outlined in [Appendix 3](#). Those reports which are of particular interest to Scottish Enterprise are provided to the Audit and Risk Committee.

# Appendix 1

## Action plan 2019/20



No.	Issue/risk	Recommendation	Agreed management action/timing
1	<p><b>Timetable of preparation of accounts and subsequent audit</b></p> <p>The timetable for the financial statements audit is challenging for Scottish Enterprise and the audit team. We do not receive the performance and accountability reports at the start of the audit, which increases the time pressures on Scottish Enterprise and the audit team later in the process.</p> <p><b>Risk.</b> There is a risk that the audit is not completed in accordance with agreed timescales.</p>	<p>Scottish Enterprise together with Audit Scotland should review the year end preparation and audit timetables</p> <p><a href="#">Recommendation 1, paragraph 24</a></p>	<p>Scottish Enterprise will work collaboratively with Audit Scotland to review the year end preparation and audit timetables.</p> <p>Douglas Colquhoun, Chief Financial Officer</p> <p>December 2020</p>
2	<p><b>Financial Instruments: Expected Credit Loss</b></p> <p>Management undertakes an estimation of the expected credit loss of assets held at amortised cost, as required by IFRS 9.</p> <p>We agreed that the estimation was reasonable. However, management could improve this by documenting the estimation methodology and sharing best practice with public and private sector partners.</p>	<p>Management should document their processes for assessing expected credit loss. This should include liaison with other public and private sector partners to share best practice in the assessment of ECL.</p> <p><a href="#">Recommendation 2, paragraph 36</a></p>	<p>Scottish Enterprise will fully document the methodology for assessing expected credit losses. We will consider opportunities for continuous improvement including assessment of best practice across the public and private sectors.</p> <p>Douglas Colquhoun, Chief Financial Officer</p> <p>March 2021</p>
3	<p><b>SUN/IMRS Reconciliation</b></p> <p>There is no formal reconciliation between the Investment Management Reporting System (IMRS) and the financial general ledger (SUN). Management confirmed that SUN is the primary system for financial management of the investments and noted IMRS</p>	<p>Management should formally reconcile the SUN and IMRS to further improve the control environment.</p> <p><a href="#">Recommendation 3, paragraph 53</a></p>	<p>The Finance team will work alongside colleagues in the Scottish Investment Bank to consider a formal reconciliation process that will support management information within SIB.</p> <p>Douglas Colquhoun, Chief Financial Officer</p> <p>September 2020</p>



No.	Issue/risk	Recommendation	Agreed management action/timing
	reads financial information from SUN.		
4	<p><b>Longer term financial planning</b></p> <p>Longer-term financial planning was deferred by Scottish Enterprise due to current circumstances.</p> <p><b>Risk.</b> In the absence of longer-term financial planning there is a risk that the impact of budget assumptions on agreed or projected outputs is not effectively recognised.</p>	<p>A longer-term financial strategy should be developed, supported by clear and detailed financial plans. Financial planning should align with the corporate plan</p> <p><a href="#">Recommendation 4, paragraph 76</a></p>	<p>Scottish Enterprise has already started work on medium and longer-term financial planning as highlighted in this report. We will continue to develop this work over the next year.</p> <p>Douglas Colquhoun, Chief Financial Officer</p> <p>March 2021</p>
5	<p><b>Internal control arrangements</b></p> <p>The scale and pace of change as a result of Covid-19 poses a risk to Scottish Enterprise's governance arrangements.</p> <p><b>Risk.</b> There are risks around the operation of key controls within the finance department and the introduction of significant new grant products.</p>	<p>Scottish Enterprise should ensure that internal controls remain effective during this period of uncertainty and new way of working.</p> <p><a href="#">Recommendation 5, paragraph 84</a></p>	<p>Internal control arrangements have been kept under review during the period since Covid-19 disrupted the normal business model. A key consideration during this period has been appropriate segregation of duties and appropriate approval processes. This work will continue.</p> <p>Douglas Colquhoun, Chief Financial Officer</p> <p>Ongoing</p>
6	<p><b>Annual report narrative</b></p> <p>The annual report narrative could be improved to ensure it is balanced, readable and transparent to the reader.</p> <p><b>Risk.</b> There is a risk that Scottish Enterprise fails to communicate effectively to stakeholders.</p>	<p>Scottish Enterprise should review the content and presentation of its performance report to ensure it takes full advantage of the opportunity to communicate directly to stakeholders about its activities</p> <p><a href="#">Recommendation 6, paragraph 93</a></p>	<p>Scottish Enterprise will consider further improvements to the annual report narrative to aid understanding and transparency. We will benchmark against other public bodies.</p> <p>Douglas Colquhoun, Chief Financial Officer</p> <p>December 2020</p>

### Follow up of prior year recommendations

b/f 1	<p><b>EU Income</b></p> <p>There have been further write-downs of the level of accrued EU income due to the</p>	<p>Scottish Enterprise should ensure that all relevant grant conditions are met including</p>	<p><b>In progress</b></p> <p>Scottish Enterprise continue to review and reassess the accrued grant level and work</p>
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No.	Issue/risk	Recommendation	Agreed management action/timing
	<p>inadequacy of evidence required to support Scottish Enterprise's claims for European funding. Management continue to review the eligibility of expenditure and the related EU income accrual.</p> <p>Risk: There remains a risk that the level of accrued EU expenditure is overstated. There also remains a risk that Scottish Enterprise's ability to use available EU funding will be adversely impacted.</p>	<p>the retention of the required documentation.</p>	<p>to ensure all relevant information is retained.</p> <p>Refer to <a href="#">paragraphs 37-38</a> above</p>
b/f 2	<p><b>Intangible Assets</b></p> <p>Scottish Enterprise upgraded and renewed IT systems during the year. These costs have been charged to revenue rather than being capitalised.</p> <p>These could potentially have been capitalised as intangible assets under IAS 38.</p> <p><b>Risk:</b> There is a risk that revenue and capital expenditure is inaccurately reported.</p>	<p>Management should review and amend the accounting for intangible assets and their related policies.</p>	<p><b>Complete</b></p> <p>Scottish Enterprise capitalised four intangible asset additions in 2019/20, totalling £1.997m.</p> <p>We assessed the accounting policies for these assets and the capitalisation of these. No issues were identified.</p>
b/f 3	<p><b>Governance and Transparency: Performance Report</b></p> <p>The performance report could enhance openness and transparency by providing a more rounded and accessible narrative around performance. Clear linkages should be provided to the National Performance Framework.</p> <p><b>Risk:</b> There is a risk that the Performance Report does not maximise its potential as a means of communicating performance.</p>	<p>Scottish Enterprise should review the content and presentation of its performance report to ensure that the information provided is understandable, accessible and transparent and provides the relevant information. The report should provide clear links and explanation of performance against national outcomes.</p>	<p><b>Ongoing</b></p> <p>Refer to <a href="#">paragraphs 91-93</a> above</p>
b/f 4	<p><b>Governance and Transparency: Restructuring</b></p> <p>There is a significant amount of organisational change underway within the organisation.</p>	<p>The operation of internal controls and the overall control framework should be emphasised to all staff.</p> <p>Management should ensure there is sufficient capacity in the Finance department to</p>	<p><b>Ongoing</b></p> <p>We have confirmed that an additional 2 posts have been added to the financial accounting team. However, these have not yet been filled.</p>



No.	Issue/risk	Recommendation	Agreed management action/timing
	<p>Risk: There is a risk that controls may not operate effectively during this period of change.</p> <p>There is a risk that the restructuring adversely affects Scottish Enterprise's financial capacity and its ability to meet the challenging year-end accounts preparation and audit timetable</p>	<p>avoid any impact on key finance processes.</p>	<p>The Chief Financial Officer's role was reinstated in April 2020, after the role was made redundant and combined with the Chief People Officer's role in summer 2019.</p> <p>Refer to <a href="#">paragraphs 63-67</a> above.</p>
<b>b/f 5</b>	<p><b>Cyber Security</b></p> <p>Cyber essentials has not yet been achieved.</p> <p>Risk: There is a risk that key systems are not resilient enough to evade a cyber-attack.</p>	<p>Scottish Enterprise should continue to work with its EIS partners to ensure cyber essentials is achieved.</p>	<p><b>Ongoing</b></p> <p>EIS has not yet achieved Cyber essentials accreditation.</p> <p>Internal Audit undertook a review of EIS arrangements.</p> <p>See <a href="#">paragraphs 94-97</a> above</p>



# Appendix 2

## Significant audit risks identified during planning

The table below sets out the audit risks we identified during our planning of the audit and how we addressed each risk in arriving at our conclusion. The risks are categorised between those where there is a risk of material misstatement in the annual report and accounts and those relating to our wider responsibility under the [Code of Audit Practice 2016](#).

**Add in any additional audit risks arising from COVID-19 along with any new 'standard risks' identified in the revised 2019/20 Audit Planning Guidance**

Audit Risk	Assurance procedure	Results and conclusions
<b>Risks of material misstatement in the financial statements</b>		
<p><b>1 Risk of material misstatement caused by management override of controls</b></p> <p>Auditing Standards require that audits are planned to consider the risk of material misstatement caused by fraud, which is presumed to be a significant risk in any audit. This includes the risk of management override of controls that results in fraudulent financial statements.</p>	<p>Testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Testing of accruals and prepayments.</p> <p>Cut-off testing, to ensure income and expenditure is recognised in the correct financial year.</p> <p>Evaluation of any significant transactions that are outside the normal course of business.</p>	<p><b>Result</b></p> <p>We did not identify any issues as a result of our audit work that would indicate management override of controls affecting the year-end position.</p> <p>We considered the impact of Covid-19 on year-end valuations (See point 4 below)</p> <p>There were no significant transactions outside the normal course of business.</p> <p><b>Conclusion:</b> Satisfactory</p>
<p><b>2 Risk of material misstatement caused by fraud in income recognition</b></p> <p>As set out in ISA 240, there is a presumed risk of fraud in the recognition of income. There is a risk that income may be misstated resulting in a material misstatement in the financial statements.</p> <p>Scottish Enterprise's October 2019 financial performance report forecasts that £66m (18%) of its income will come from sources other than central government funding, including income from properties and investments. The extent, nature and complexity of this income means that there is an inherent risk of fraud.</p>	<p>Review Scottish Enterprise's anti-fraud arrangements.</p> <p>Walk-through of controls over income / receivables.</p> <p>Detailed testing of revenue transactions focusing on the areas of greatest risk.</p> <p>Substantive cut-off testing of income to ensure that it has been recognised in the correct financial year.</p>	<p><b>Result</b></p> <p>No issues identified with anti-fraud arrangements.</p> <p>We identified some matters in relation to reconciliations and reported these in our management report. We followed up as part of our year end audit and established that the matters had been addressed.</p> <p>No significant issues identified from revenue transactions or cut-off testing of income.</p> <p><b>Conclusion:</b> Satisfactory</p>

Audit Risk	Assurance procedure	Results and conclusions
<p><b>3 Risk of material misstatement caused by fraud in expenditure</b></p> <p>As most public bodies are net spending bodies, we are also required to consider the risk of fraud over expenditure.</p> <p>In 2018/19, Scottish Enterprise recorded gross expenditure of £313m. This includes a material level of grants to third parties. Given the extent, nature and complexity of expenditure, there is an inherent risk of fraud.</p>	<p>Review Scottish Enterprise's anti-fraud arrangements.</p> <p>Walk-through of controls over payables, including grant expenditure.</p> <p>Substantive testing of grant expenditure.</p> <p>Substantive cut-off testing of expenditure to ensure that it has been recognised in the correct financial year.</p> <p>Review of procurement practices.</p>	<p><b>Result:</b> No significant issues were identified from our audit testing.</p> <p>Review of procurement practices found no significant issues arising.</p> <p><b>Conclusion:</b> Satisfactory</p>
<p><b>4 Estimation and judgements</b></p> <p>ISA 540 is concerned with the auditor's responsibilities relating to accounting estimates and related disclosures in financial statements.</p> <p>There is a significant degree of subjectivity in the measurement and valuation of investments (£320m), land and buildings (£155m) and pension assets (£63m). There is also a degree of estimation and judgement in accrued expenditure (£36m), accrued income (£7m), provisions (£6m) and debt impairment (£6m).</p> <p>Estimates and judgements in these areas represent an increased risk of misstatement in the financial statements.</p>	<p>Test management's controls and procedures over these estimations and judgements.</p> <p>Substantive testing of selected year-end valuation reports.</p> <p>Review of the work of management's expert valuers, including a review of the processes for valuing investments.</p> <p>Review management's assessment of the appropriateness of the assumptions used in the valuation of certain assets and liabilities.</p> <p>Substantive testing of year-end accruals, provisions and bad debt provisions. Review of accrued EU income.</p>	<p><b>Result:</b></p> <p>No issues identified with management's controls over the year-end valuation process or the work of expert valuers.</p> <p>We considered the work undertaken by management and its expert valuers in light of the Covid-19 pandemic and considered the impact on the year-end valuations.</p> <p>Refer to <a href="#">Exhibit 1, points 1 and 2</a></p> <p><b>Conclusion:</b> Satisfactory</p>
<p><b>Risks identified from the auditor's wider responsibility under the Code of Audit Practice</b></p>		
<p><b>5 Financial management</b></p> <p>Scottish Enterprise's October 2019 financial performance report forecasts that the majority of expenditure will be incurred in the second half of the financial year.</p> <p>There is a risk that management's forecast of expenditure is not achieved, leading to under-spending of grant in aid (including financial transactions) and EU funding. There is also a risk that the effectiveness of key controls is compromised due to pressures to achieve budgets</p>	<p>Review budget monitoring processes across capital and revenue streams.</p> <p>Review management action to make full use of the budget.</p> <p>Review the work of the Financial Transactions working group.</p> <p>Substantive cut-off testing of expenditure.</p> <p>Review the level of EU-funded expenditure.</p>	<p><b>Results:</b> Scottish Enterprise addressed the forecast deficit through restricting expenditure. This action together with the impact of Covid-19, led to an underspend. There are strong budget monitoring arrangements in place.</p> <p>No issues identified.</p> <p>Refer to <a href="#">paragraphs 46-51</a> above.</p> <p><b>Conclusion:</b> Satisfactory</p>

Audit Risk	Assurance procedure	Results and conclusions
<p><b>6 Value for money</b></p> <p>Scottish Enterprise is developing its performance management and reporting arrangements to reflect significant changes in its internal and external operating environments.</p> <p>There is a risk that performance management arrangements are not aligned with new structures within the organisation and with the Enterprise and Skills Strategic Board's missions and that, as a result, Scottish Enterprise is unable to demonstrate progress and its contribution to the Scottish Government's National Performance Framework.</p>	<p>Review internal audit's work on performance measurement and Strategic Board alignment. Review progress on achieving the primary outcomes.</p> <p>Consider the work undertaken by internal audit on transition arrangements relating to South of Scotland Agency, Scottish National Investment Bank and Performance Measurement.</p> <p>Review progress on the reporting of achievement of objectives and the effectiveness of the underlying systems.</p>	<p><b>Results:</b> No issues identified. Refer to <a href="#">paragraphs 106-115</a> above.</p> <p><b>Conclusion:</b> Satisfactory</p>
<p><b>7 Cyber Security</b></p> <p>Organisations are increasingly threatened by cyber-attacks. Scottish Enterprise has a shared Enterprise Information Service (EIS) IT arrangement with Skills Development Scotland (SDS) and Highlands and Islands Enterprise (HIE). Internal audit reported in August 2019 and identified key areas for improvement. There is a risk that a cyber-attack could disrupt Scottish Enterprise's</p>	<p>Review progress in addressing the recommendations raised by internal audit and coordinate our work with the external auditors of SDS and HIE.</p> <p>Place reliance on any internal audit follow-up work.</p>	<p><b>Results:</b> Although internal audit noted that EIS made good progress in addressing its recommendations, the remaining recommendations are expected to be addressed once EIS has undertaken a Cyber Maturity Assessment.</p> <p>Refer to <a href="#">paragraphs 94-97</a> above.</p> <p><b>Conclusion:</b> EIS has made good progress but there is still a risk that a cyber-attack could disrupt Scottish Enterprise's systems.</p>

# Appendix 3

## Summary of national performance reports 2019/20

		 <b>2019/20 Reports</b>	
		Apr	
Social security: Implementing the devolved powers		<b>May</b>	
Scotland's colleges 2019		<b>Jun</b>	 Enabling digital government
		Jul	
NHS workforce planning - part 2		<b>Aug</b>	
Finances of Scottish universities		<b>Sept</b>	
NHS in Scotland 2019		<b>Oct</b>	
		Nov	
Local government in Scotland: Financial overview 2018/19		<b>Dec</b>	
Scotland's City Region and Growth Deals		<b>Jan</b>	 Privately financed infrastructure investment: The Non-Profit Distributing (NPD) and hub models
		Feb	
		<b>Mar</b>	 Early learning and childcare: follow-up

### Central Government relevant reports

[\*Social security: Implementing the devolved powers\*](#) – May 2019

[\*Enabling digital government\*](#) – June 2019

[\*Scotland's City Region and Growth Deals\*](#) – October 2019

[\*Privately financed infrastructure investment: The Non-Profit Distributing \(NPD\) and hub models\*](#) – Jan 2020

[\*Early learning and childcare: follow-up\*](#) – March 2020

# Scottish Enterprise

## 2019/20 Annual Audit Report

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