



# Historic Environment Scotland

Report to the Audit, Risk and Assurance Committee, the Board and the Auditor  
General for Scotland, on the 2020/21 audit

Issued on 1 October for the Committee meeting on 8 October 2021 (reissued on 13 October for the Board meeting on 21 October 2021)

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# Introduction

## The key messages in this report

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

I have pleasure in presenting our final report to the Audit, Risk and Assurance Committee (“ARAC”) of Historic Environment Scotland (“HES”) for the year ending 31 March 2021 audit. The scope of our audit was set out within our planning report presented to ARAC in January 2021.

The 2020/21 audit was carried out in challenging circumstances, with the continued effects of remote working, the full impact of COVID-19 on the Annual Report and Accounts being evident in the year (with a consequent impact on the level of materiality, our risk assessment and procedures performed, as set out in our Audit Plan), the introduction of new auditing standards, and changes within HES (for example, the introduction of a new finance system). Notwithstanding this, the Annual Report and Accounts and audit process have been completed in advance of the statutory deadlines, and there has been no requirement to utilise extensions to this timeline offered in response to the pandemic.

This report summarises our findings and conclusions in relation to:

- The audit of the **Annual Report and Accounts**; and
- Consideration of the **four audit dimensions** that frame the wider scope of public sector audit requirements as illustrated in the following diagram. This includes our consideration of the Accountable Officer’s duty to secure Best Value.



# Introduction (continued)

## The key messages in this report (continued)

I would like to draw your attention to the key messages of this paper:

### **Conclusions from our testing**

We expect to issue an unmodified audit opinion.

We are satisfied that the Performance Report and Governance Statement comply with the statutory guidance and proper practice and are consistent with the accounts and our knowledge of HES.

We are satisfied that, following the amendments set out on page 48, the auditable parts of the Remuneration and Staff Report have been prepared in accordance with the relevant regulations.

A summary of our work on the significant risks is provided in the dashboard on page 11.

One disclosure error and 10 audit adjustments in excess of our reporting threshold (see page 46 – 49) have been identified during the audit and corrected by management. The disclosure error related to the Remuneration and Staff Report was deemed qualitatively material. In relation to the audit adjustments, two were quantitatively material – relating to classification of expenditure between ‘support costs’ and ‘charitable activities’, and recording of transactions with HESe – while the remainder were material in aggregate.

One adjustment identified during the audit (page 45) relating to overstatement of expenditure has not been corrected by management.

We have identified one control deficiency which should be addressed by HES, set out on page 18.

The adjustments and other issues identified during the audit (page 8 – 9) had a significant impact on the level of audit work required. As a result, it was not possible to adhere to the originally agreed timeline for the audit, although HES and the audit team have worked together effectively to ensure that a quality audit has still been completed ahead of the statutory deadline for completion.

### **Status of the financial statements audit**

Our audit is complete.

# Introduction (continued)

## The key messages in this report (continued)

### Conclusions on audit dimensions

As set out on page 3, our audit work covered the four audit dimensions. Our audit work was risk based and proportionate, covering each of the four dimensions. As discussed in our audit plan, the risk profile of public bodies for the 2020/21 audits is significantly affected by the COVID-19 pandemic. Our audit work across each dimension has therefore been specifically focussed on how HES has responded to these risks.

Our overall conclusions on each dimension are summarised below, with full details provided in the main body of the report:

**Financial management** – HES continues to have strong financial management processes in place. It has been significantly impacted by COVID-19, with commercial income dropping 87% during 2020/21 and revised financial controls were put in place to manage this impact.

HES continues to have a sufficiently qualified and experienced finance team to support the financial management of the organisation. While the capacity of the finance team was impacted with the implementation of a new finance system in the year, management has noted improvements in 2021/22.

**Financial sustainability** – HES achieved short-term financial balance in 2020/21 and has set a balanced budget for 2021/22. There is a robust budget setting and monitoring process in place for achieving savings, incorporating early involvement of the Board. It is also positive to note that HES is actively assessing the financial impact of COVID-19 and has completed scenario planning for 2021/22. However, the impact of COVID-19 on the ability to achieve financial sustainability remains a risk to HES.

The impact of COVID-19 is expected to have a significant impact over the medium to longer term, and therefore HES needs to assess the estimated impact as the landscape becomes more certain. Savings targets need to be identified in a more targeted way linking to service review activity and workforce planning.

HES has made good progress during 2020/21 in relation to its Programme for Success (“PFS”) and has taken the opportunity to reconsider projects in light of the COVID-19 pandemic. We are pleased to note that progress is being made with the implementation of a Project Management Office (“PMO”), which incorporates the development of benefits trackers and a resource plan. We will continue to monitor implementation during our 2021/22 audit.

**Governance and transparency** – HES continues to have strong leadership in place. This has been particularly evident in the response to COVID-19. The proposed review of the management structure is a positive step as HES moves to a more collaborative working model.

HES also continues to have robust governance and scrutiny arrangements in place and appropriate arrangements have been in place throughout the COVID-19 pandemic.

While key corporate documents are published on the website, openness and transparency for both the public and staff could be improved to bring HES into line with other public sector organisations. Areas to consider include holding meetings in public and limiting closed sessions to private or confidential information only.

**Value for money** – HES continues to have a clear performance management framework in place. It has consistently performed above 90% against annual operating plans and has again performed well in 2020/21 against action plans. HES should consider whether targets set are sufficiently focussed on measuring the impact of the actions. It may be useful for an independent assessment of the self-assessment of performance to be carried out, for example through a peer review.

**Best Value** – HES has sufficient arrangements in place to secure Best Value with a strong focus on continuous improvement. It has a clear understanding of areas which require further development.

# Introduction (continued)

## The key messages in this report (continued)

### **Emerging issues**

Deloitte's wider public sector team prepare a number of publications to share research, informed perspective and best practice across different sectors. We have provided a summary of those most relevant to HES on page 43 of this report.

### **Next steps**

An agreed Action Plan is included on pages 50 and 51 of this report, including a follow-up of progress against prior year actions. We will consider progress with the agreed actions as part of our 2021/22 audit.

### **Added value**

Our aim is to add value to HES by providing insight into, and offering foresight on, financial sustainability, risk and performance by identifying areas for improvement and recommending and encouraging good practice. In so doing, we aim to help HES promote improved standards of governance, better management and decision making, and more effective use of resources.

This is provided throughout the report. In addition we invited the Chair of ARAC to the "Resilient Leader: Thriving in uncertain times" webinar in March 2021.

**Pat Kenny**  
**Audit Director**

# Financial statements audit



# Quality indicators

## Impact on the execution of our audit

Management and those charged with governance are in a position to influence the effectiveness of our audit, through timely formulation of judgements, provision of accurate information, and responsiveness to issues identified in the course of the audit. This slide summarises some key metrics related to your control environment which can significantly impact the execution of the audit. We consider these metrics important in assessing the reliability of your financial reporting and provide context for other messages in this report.

Area	Grading	Reason
Timing of key accounting judgements		<p>Documentation supporting management's assessment of key estimates – including provisions and property valuations – was provided on time and was significantly improved on 2019/20.</p> <p>Management took a decision to 'opt to tax' a key property for VAT purposes and the impact on valuation wasn't considered until late in the audit and wasn't reflected in the draft Annual Report and Accounts. This required additional audit work, including consultation with our internal specialists and requesting management obtain a revised valuation from its independent expert. This resulted in an adjustment of £357k (page 46). We are satisfied that this is a single year issue which is unlikely to recur.</p>
Adherence to deliverables timetable		<p>The draft Annual Report and Accounts were provided on 31 May 2021, which is in line with the agreed timetable. However, the provided draft was not complete. Management provided information for approximately two-thirds of audit requests on time. It is important to recognise the context of both COVID-19 and the rollout of the new IT system in the year in these areas. Due to this and the adjustments identified (page 45 – 48), it was agreed to revise the audit reporting deadline from July 2021 to October 2021. It should be noted this is within the statutory reporting deadlines.</p>
Access to finance team and other key personnel		<p>Deloitte and HES have worked together to facilitate remote communication during the audit which has been successful. We are aware that the finance team has been under significant pressure from implementing the new system which has meant a backlog in business-as-usual work affecting the preparation of the Annual Report and Accounts, but this has not impacted on our access to them.</p>



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# Quality indicators (continued)

## Impact on the execution of our audit (continued)

Area	Grading	Reason
Quality and accuracy of management accounting papers		Documentation provided has been a good standard in the majority of cases. However, the audit team needed to resubmit audit requests in a number of cases as the information provided did not reconcile to the draft Annual Report and Accounts or was incomplete. In addition, a number of HES's accounting records were aggregated at a high level, which required sub-sampling a number of areas which increased sample sizes during the audit.
Quality of draft financial statements		The quality of the Annual Report and Accounts has improved since 2019/20, with a consequent decline in the number of amendments required. Whilst generally compliant with reporting requirements, a number of amendments were required to ensure compliance with the Financial Reporting Manual ("FReM") and Charities Statement of Recommended Practice ("SORP"). These are discussed further on page 21. An enhanced management review of the draft Annual Report and Accounts should be undertaken prior to submission to audit in future years to continue on HES's improvement journey.
Response to control deficiencies identified		One control deficiency has been identified, relating to management review of the Annual Report and Accounts. Management have accepted this and put plans in place to address them going forward. This is discussed further on page 18.
Volume and magnitude of identified errors		<p>11 adjustments have been identified during our audit, as set out on pages 45 – 48. Of these, 2 were individually material, while the remainder (8) were material in aggregate.</p> <p>In addition to these audit adjustments, one qualitatively material disclosure error has been identified, set out on page 49. No other reportable disclosure errors were identified.</p> <p>Management have accepted these adjustments and corrected them in all but one immaterial instance.</p>



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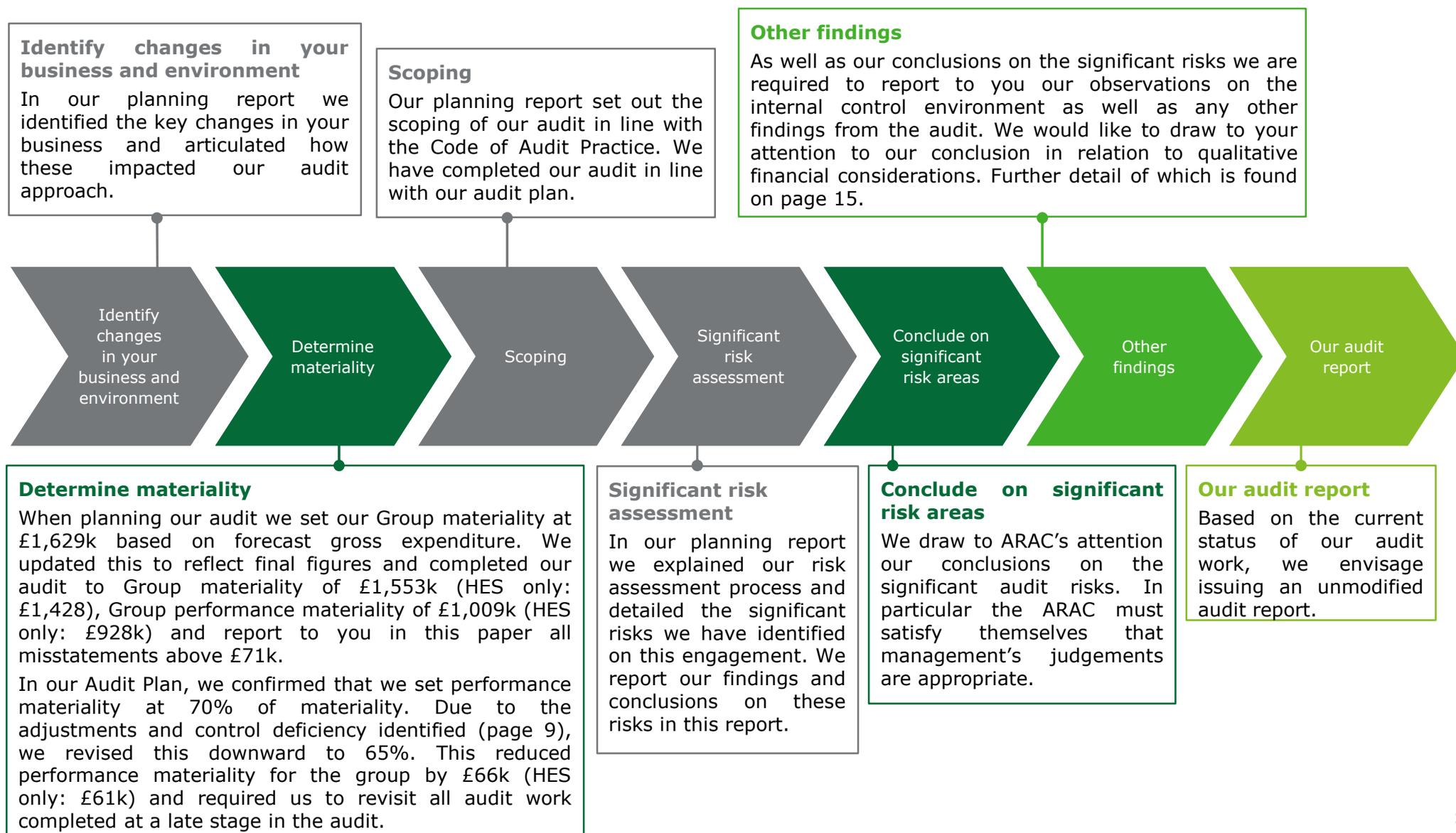
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# Our audit explained

We tailor our audit to your business and your strategy



# Significant risks Dashboard

Risk	Material	Fraud risk	Planned approach to controls testing	Controls testing conclusion	Consistency of judgements with Deloitte's expectations	Comments	Page no.
Government assistance programmes			D+I	Satisfactory		No issues noted	12
Management override of controls			D+I	Satisfactory		Adjustments identified relating to property valuations and provisions (page 46)	13

Overly prudent, likely to lead to future credit



Overly optimistic, likely to lead to future debit.

**D+I:** Testing of the design and implementation of key controls

# Significant risks (continued)

## Government Assistance Programmes



### Risk identified and key judgements

HES have utilised the job retention scheme – commonly referred to as the furlough scheme - offered by the UK government in response to the COVID-19 pandemic.

Due to the rapid development of the schemes and regular short-notice changes to scheme criteria, applicability and operations, there is a heightened risk of fraud within these schemes.

Given the heightened risk highlighted above, in addition to the material nature of the amounts received (£4.2m), the complexities involved in the schemes and the potential penalties for any non-compliance with scheme requirements, we identified this as a significant audit risk, pinpointed to the occurrence of furlough income (i.e. the validity of claims made), and the completeness of any associated clawback provision.



### Deloitte response and challenge

In considering the fraud risk of occurrence of furlough income, we have performed the following audit procedures that directly address this risk:

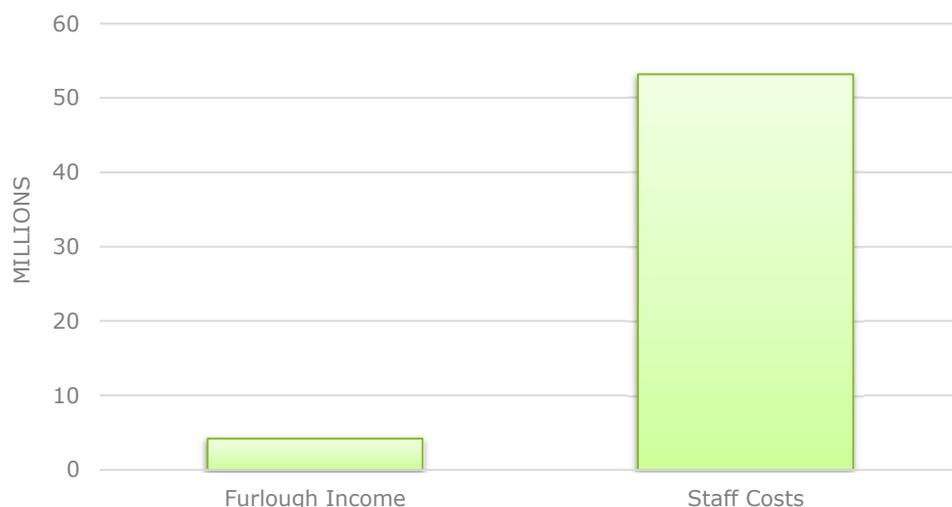
- Completed design and implementation procedures on the controls over the furlough income process;
- Tested a sample of the monthly claims submitted and amounts received from HMRC throughout the year;
- Selected a sample of employees from the claims submitted and review the validity of the claim;
- Selected a sample of employees from the payroll and cross check to the claims submitted; and
- Reviewed the disclosures presented in the Annual Report and Accounts ensuring the income is clearly presented and in line with SORP/FRS 102.

### Deloitte view

We have not identified any issues with regards to the amount of furlough income claimed in the year.

Given the significance of furlough income and the change in the year, the funding has been appropriately explained within the Performance Report and the notes to the Accounts.

Furlough Income vs Staff Costs



# Significant risks (continued)

## Management override of controls



### Risk identified

Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Although management is responsible for safeguarding the assets of the entity, we planned our audit so that we had a reasonable expectation of detecting material misstatements to the annual report and financial statements and accounting records.



### Deloitte response and challenge

In considering the risk of management override, we have performed the following audit procedures that directly address this risk:

#### Journals

We have tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the annual report and financial statements. In designing and performing audit procedures for such tests, we have:

- Tested the design and implementation of controls over journal entry processing;
- Made inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments;
- Selected journal entries and other adjustments made at the end of a reporting period; and
- Considered the need to test journal entries and other adjustments throughout the period.

### Accounting estimates and judgements

We have reviewed accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud. In performing this review, we have:

- Evaluated whether the judgments and decisions made by management in making the accounting estimates included in the annual report and financial statements, even if they are individually reasonable, indicate a possible bias on the part of the entity's management that may represent a risk of material misstatement due to fraud. From our testing we did not identify any indications of bias. A summary of the key estimates and judgements considered is provided on the next page; and
- Performed a retrospective review of management judgements and assumptions related to significant accounting estimates reflected in the annual report and financial statements of the prior year.

### Significant and unusual transactions

We did not identify any significant transactions outside the normal course of business or any transactions where the business rationale was not clear.

#### Deloitte view

We have not identified any instances of management override of controls in relation to the specific transactions tested.

We have identified adjustments relating to accounting estimates on property valuations (page 15) and provisions (page 14).

# Significant risks (continued)

## Management override of controls (continued)

**Key estimates and judgements** The key estimate and judgment in the Annual Report and Accounts is that which we have selected to be a significant audit risk around recognition of income from government assistance programmes (see page 12). This is inherently the area in which management has the potential to use their judgement to influence the Annual Report and Accounts. As part of our work on management override of controls, we reviewed and challenge management's other key estimates and judgements including:

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Dilapidations Provision	<p>HES provide for legal or constructive obligations that are of uncertain timing or amount at the balance sheet date on the basis of the best estimate of the expenditure required to settle the obligation.</p> <p>Adjustments were identified in the 2019/20 audit, increasing the dilapidations provision from £521k to £1,347k.</p> <p>In 2020/21, management reassessed the provision and increased it further by £494k (to a total of £1,841k) in light of changes in circumstances in the year.</p>	<p>The dilapidations provision has increased in the year to become quantitatively material. The provision relates to properties leased by HES, and has moved in the year due to updated valuations in relation to relevant properties.</p> <p>We have reviewed the 2020/21 provision, including management's judgements and supporting documentation. During our procedures, it was confirmed that a number of properties not included in the amount provided would have similar obligations. Further work was undertaken by management in light of this, and we reviewed the adjustments identified. This resulted in an additional £122k being included in the provision (page 45).</p>
Legal Provision	<p>HES provides for any legal claims for which HES has a probable liability and which can be measured reliably.</p> <p>Adjustments were identified in the 2019/20 audit as management had originally offset anticipated reimbursement against the legal provision, with an adjustment to recognise a £944k reimbursement asset and to consequently increase the amount provided by £960k.</p> <p>In 2020/21, management reassessed the provision and reduced it by £115k in light of changes in the year (to a total of £969k). The reimbursement asset reduced by £15k in the year (to a total of £931k).</p>	<p>We have assessed the legal claims outstanding at 31 March 2021 alongside the legal team to determine the probability of HES having liability. In line with FRS 102, the recognition criteria for provisions and reimbursement assets are separate and management have recognised these separately.</p> <p><b>Provision:</b> We reviewed and requested information from the HES legal team and HES insurance providers regarding ongoing cases including those covered by insurance. We considered management's estimate and supporting documentation, and concluded that the amount provided was reasonable.</p> <p><b>Reimbursement Asset:</b> We reviewed evidence provided by insurers to consider whether the reimbursement was virtually certain in line with FRS 102. We considered management's estimate and based on this and our audit work, concluded that the amount recognised was reasonable.</p>

# Significant risks (continued)

## Management override of controls (continued)

Estimate / judgement	Details of management's position	Deloitte Challenge and conclusions
Grant Commitments	<p>Under the Charities SORP the award of a grant is recognised as a liability when the criteria for a constructive obligation are met, payment is probable, it can be measured reliably, and there are no conditions attached to its payment that limit its recognition.</p> <p>HES has recognised £31.2m of grant commitments as at 31 March 2021, down from £35.5m at 31 March 2020.</p>	<p>We have tested a sample of grant accruals, commitments and retentions at the year-end to assess whether they have been accounted for in accordance with the SORP. The significant decline is due to the impact of COVID-19 on the submission of applications for grant funding from HES, and on the ability of HES to commit to future grant awards. We have not identified any issues through our work.</p>
Property Valuations	<p>HES is required to hold property assets within Property, Plant and Equipment at a modern equivalent use valuation. The valuations are, by nature, significant estimates based on specialist and management assumptions and which can be subject to material changes in value.</p> <p>HES has had an independent valuation carried out at 31 March 2021 by its independent valuers in accordance with its 5-year rolling programme.</p> <p>The valuation method has not changed from the prior year and is in line with FRS 102.</p>	<p>We did not identify this as a significant risk in our Audit Plan as our property specialists, Deloitte Real Estate, reviewed the methodology applied by HES's valuer in previous years and concluded it was robust. We have confirmed that the valuer and the methodology applied has not changed in the year.</p> <p>We have challenged management's assessment and consulted with our internal property specialists. For those valued on Existing Use Value on a market comparable basis, our property experts have confirmed that minimal market value would be expected in 2020/21. For those valued on a Depreciated Replacement Cost basis, which would be impacted by changes in build costs during the year, we have performed an analysis of changes in the Build Costs Information Service index and concluded that no material movement would be expected. We are therefore satisfied that there is no indication of a material movement in assets not formally revalued during the year.</p> <p>We have reviewed the valuer's report, specifically considering the impact of COVID-19. The valuer has not included a 'material valuation uncertainty' clause in their report in 2020/21, which is in line with our expectations given the property types owned by HES and the sectors within which they operate.</p> <p>During our audit, a revised valuation was obtained relating to the Engine Shed property due to a decision by management to 'opt to tax' for VAT. This resulted in a net decrease in the value of HES' overall property portfolio of £202k (page 46).</p>

# Other areas of focus

## Implementation of the CMIS system



### Risk identified and key judgements

In October 2020 HES implemented phase one of a new integrated system – 'Corporate Management Information System (CMIS)'. This is a significant project and we identified a risk that the data transferred from Integra to the new system was incomplete or that it had been transferred in a way that did not enable accurate recording of transactions throughout the year.

The risk has been pinpointed to completeness and accuracy of the data transfer. Given the ongoing involvement of the internal audit team, the project governance in place including reporting to the Board and the Scottish Government Gateway reviews, we concluded that this was not a significant audit risk. However, given the significance to the financial reporting, we concluded that it was an area of audit focus.



### Deloitte response and challenge

In considering the risk of the implementation of the CMIS system, we performed the following audit procedures that directly address this risk:

- Utilised IT specialists to update our understanding of controls surrounding HES's information systems – particularly CMIS;
- Gained an understanding of the implementation process and the controls in place relating to the data transfer;
- Reviewed the reconciliation from the 2019/20 closing trial balance to the closing Integra trial balance at 30 September 2020;
- Reviewed the reconciliation of the closing Integra trial balance to the opening CMIS trial balance using management's account mapping documentation; and
- Assessed the completeness of transactions through our journal entry testing reconciliations.

### Deloitte view

We did not identify any issues with regards to the completeness of the transfer of data from Integra to CMIS.

There were challenges mapping the new chart of accounts for the Annual Report and Accounts for consistency with the prior year, resulting in audit adjustments being raised to ensure that the 2020/21 amounts in the Annual Report and Accounts were comparable with the 2019/20 figures, as set out on page 45 – 46.

HES acknowledge that further work is needed to fully integrate the new system, through the use of interfaces, thereby reducing the risk associated with manual entries which existed on the previous system and which remains a risk at present. We are aware that work is taking place on this in 2021/22 to further reduce that residual risk.

# Other areas of focus (continued)

## Inventory



### Risk identified and key judgements

ISA 501 requires auditors to perform inventory count procedures (including attendance at the inventory count) over the inventory balance. In 2019/20, we were unable to complete these procedures due to government restrictions. This resulted in a limitation of scope in our 2019/20 audit opinion.

The risk in relation to inventory has been pinpointed to the existence and condition of inventory given that restrictions have meant that HES was unable to complete its normal counting process. Given the stock controls in place during the closure period and that the gross value of the movement of stock between the stock count date and year-end is expected to be below materiality, we concluded that this was not a significant risk.

However, given the significance of the balance to the consolidated figures, we have treated it as an other area of audit focus.



### Deloitte response and challenge

In considering the risk in relation to inventory existence and condition, we performed the following procedures that directly address this risk:

- Gained an understanding of the inventory processes in place;
- Attended inventory counts;
- Performed rollback/roll-forward procedures from the stock count date to year-end (as necessary);
- Reviewed the inventory obsolescence provision; and
- Tested a sample of items to ensure inventory is held at the appropriate value (the lower of cost and net realisable value).

We considered the results of the above procedures when determining whether a modified opinion (limitation of scope in the prior year) is required for inventory in the current year.

### Deloitte view

In 2020/21, HES performed counts of inventory, with the audit team in attendance to observe a sample of the count. No issues were identified during the inventory count. Similarly, no issues were identified during the rollback (to 2019/20) to rollforward (to 2020/21) from the inventory count.

We concluded that the amount is inventory deemed to be obsolescent was reasonable, and that inventory was appropriately held at the lower of cost and net reliable value.

Given our understanding of the products held by HES, the processes and controls in place, our attendance at the inventory count and observation of the storage facilities, and our rollback/rollforward procedures, we were satisfied that there was sufficient and appropriate audit evidence to conclude on the existence and condition of inventory in 2019/20 and 2020/21, with no issues noted.

# Other significant findings

## Internal control

During the course of our audit we have identified one internal control finding, which we have included below for information.

Area	Observation	Priority
Management Review	As set out on page 45 – 49, we have identified a number of adjustments during our audit. We would have expected a detailed management review, acting as a detective and corrective control, to have identified a number of these. In future years, we would encourage HES to further enhance their existing processes in reviewing the Annual Report and Accounts and key supporting working papers in advance of the audit before submitting the draft Annual Report and Accounts for audit, to minimise the number of adjustments.	

The purpose of the audit was for us to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters being reported are limited to those deficiencies that we have identified during the audit and that we have concluded are of sufficient importance to merit being reported to you.

Low Priority

Medium Priority

High Priority

# Other significant findings (continued)

## Financial reporting findings

Below are the findings from our audit surrounding your financial reporting process.

### **Qualitative aspects of your accounting practices:**

The HES Annual Report and Accounts have been prepared in accordance with the Charities SORP and FReM. In 2020/21 management have made changes to accounting policies which we assessed during our audit work. Following our audit work, we are satisfied that the changes to accounting policies in the year are appropriate and that appropriate disclosure of the changes have been made.

### **Significant matters discussed with management:**

Significant matters discussed with management related primarily to the impact of COVID-19 on the organisation, the basis of assessment relation to the going concern assumption, the assessment of significant judgements and estimates and revisions to the audit timetable.

### **Other matters relevant to financial reporting:**

We have not identified other matters arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process.

We will obtain written representations from the Board on matters material to the financial statements when other sufficient appropriate audit evidence cannot reasonably be expected to exist. A copy of the draft representations letter has been circulated separately.

# Our audit report

## Other matters relating to the form and content of our report

Here we discuss how the results of the audit impact on other significant sections of our audit report.



### **Our opinion on the financial statements**

Our opinion on the financial statements is expected to be unmodified.

In 2019/20, we included a 'limitation of scope' in relation to the existence and condition of inventory. Through procedures performed during 2020/21, we were able to obtain sufficient and appropriate audit evidence to support a conclusion on the existence and condition of inventory in 2019/20 and have consequently not included a limitation of scope relating to the comparative figures in 2020/21.



### **Material uncertainty related to going concern**

We have not identified a material uncertainty related to going concern and will report by exception regarding the appropriateness of the use of the going concern basis of accounting.

Practice Note 10 provides guidance on applying ISA (UK) 570 Going Concern to the audit of public sector bodies. The anticipated continued provision of the service is more relevant to the assessment that the continued existence of a particular body.



### **Emphasis of matter and other matter paragraphs**

There are no matters we judge to be of fundamental importance in the financial statements that we consider it necessary to draw attention to in an emphasis of matter paragraph.

There are no matters relevant to users' understanding of the audit that we consider necessary to communicate in an other matter paragraph.



### **Other reporting responsibilities**

The Annual Report is reviewed in its entirety for material consistency with the financial statements and the audit work performance and to ensure that they are fair, balanced and reasonable.

### **Opinion on regularity**

In our opinion in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

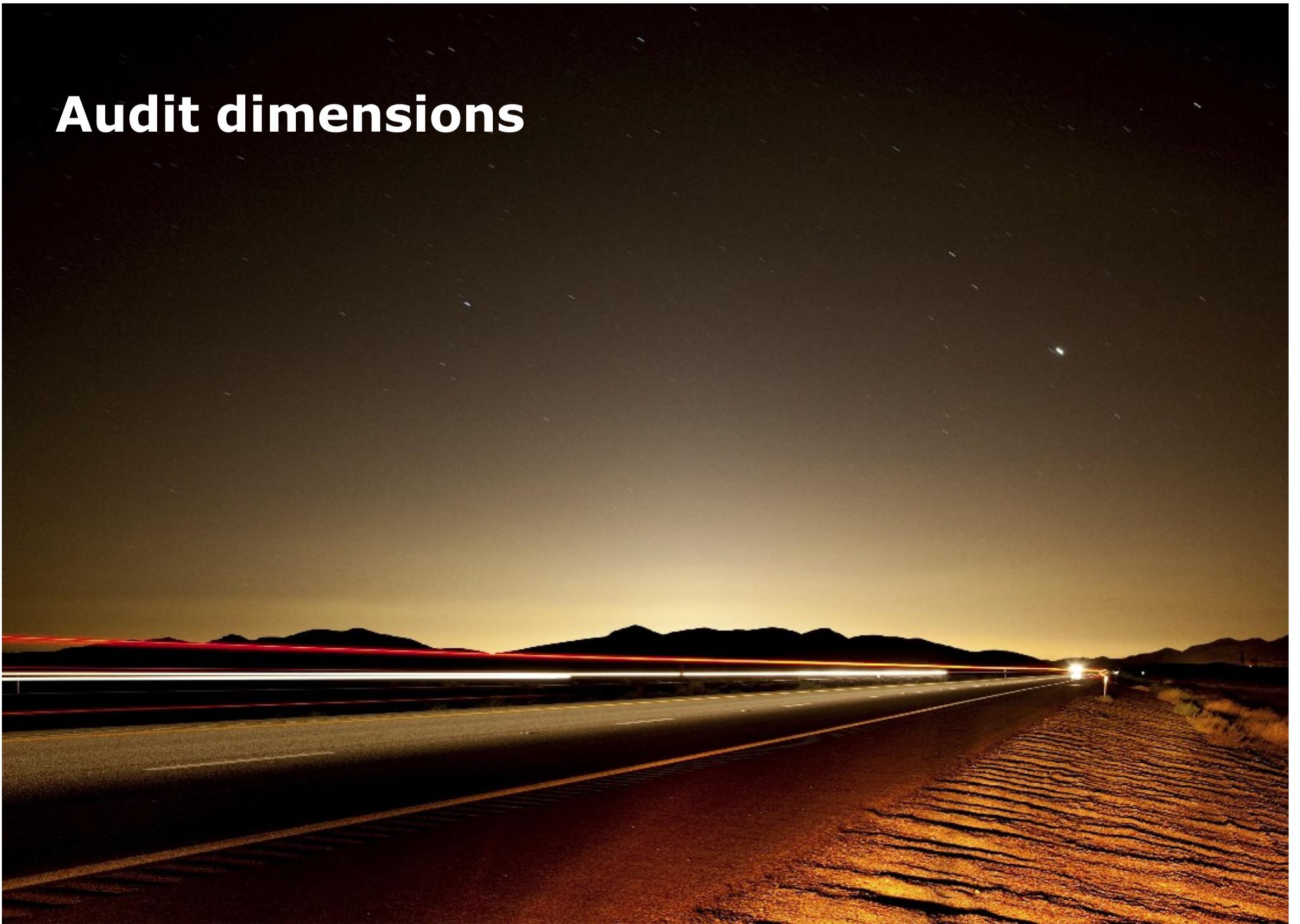
Our opinion on matters prescribed by the Auditor General for Scotland are discussed further on page 21.

# Your Annual Report

We are required to provide an opinion on the auditable parts of the Remuneration and Staff Report, the Governance Statement and whether the Performance Report is consistent with the disclosures in the Accounts.

	Requirement	Deloitte response
The Performance Report	The report outlines HES' performance, both financial and non-financial. It also sets out the key risks and uncertainty as set out in the Annual Operating Plan.	<p>We have assessed whether the Performance Report has been prepared in accordance with the accounts direction.</p> <p>We have also read the Performance Report and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading.</p> <p>We provided management with comments and suggested changes to ensure the Performance Report is in line with the requirements of the FReM, and have received an updated version reflecting these changes. Following these changes, we have concluded that the Performance Report has been properly prepared and is not misleading.</p>
The Accountability Report	Management have ensured that the accountability report meets the requirements of the FReM, comprising the Governance Statement and the Remuneration and Staff Report.	<p>We have assessed whether the information given in the Governance Statement is consistent with the financial statements and has been prepared in accordance with the accounts direction.</p> <p>We have also read the Accountability Report and confirmed that the information contained within is materially correct and consistent with our knowledge acquired during the course of performing the audit, and is not otherwise misleading. A number of changes were identified during the course of the audit, which management have actioned, ensuring that the Governance Statement and Accountability Report have been properly prepared and are not misleading.</p> <p>We have also audited the auditable parts of the Remuneration and Staff Report and confirmed that, following updates made by management as set out on page 48, it has been prepared in accordance with the accounts direction.</p>
Going Concern	Management has made appropriate disclosure relating to Going Concern matters.	We are satisfied from a review of the 2021/22 budget, correspondence with the Scottish Government, consideration of the actual position to date in 2021/22, and the assumption of continued provision of services set out in the FReM and Practice Note 10, that it is appropriate to prepare the accounts on a going concern basis, and that no material uncertainty on going concern exists. Management have appropriately included going concern as a critical judgement in the notes to the accounts.

# Audit dimensions

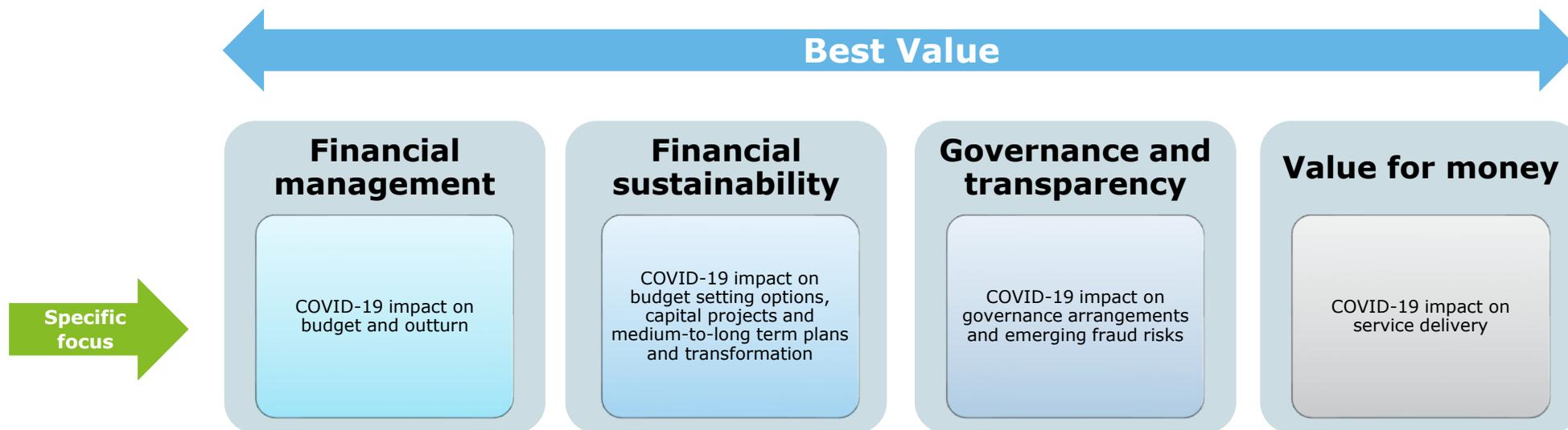


# Audit Dimensions and Best Value

## Overview

As set out in our audit plan, public audit in Scotland is wider in scope than financial audits. This section of the report sets out our findings and conclusions on our audit work covering the areas set out below.

The risk profile of public bodies for the 2020/21 audits is significantly affected by the COVID-19 pandemic. Our audit work across each dimension has therefore been specifically focussed on how HES has responded to these risks.



# Financial management

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



## Areas considered

Our approach to the audit dimensions is risk focused. Within our audit plan we confirmed that while there was no significant risk in relation to financial management, since the start of the pandemic, the risk of fraud and error has increased as the control environment and internal control change. In accordance with Audit Scotland planning guidance, we have considered fraud as a particular focus area in 2020/21.

## Current year financial performance

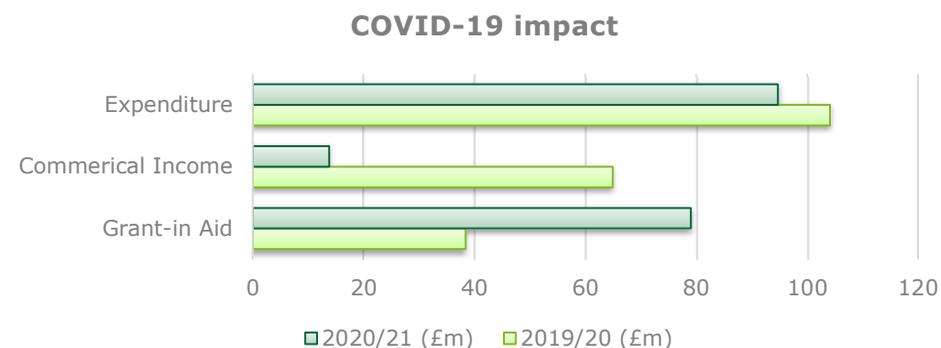
**2019/20 conclusion:** HES achieved a small surplus of £74,000 at the year end. Forecast deficits were reported throughout the year, and similar to 2018/19, over commitments were carefully managed.

**2020/21 update:** A draft full year budget was considered by the Board in early March 2020, in advance of the national lockdown. Following this, due to the impact of the COVID-19 pandemic, a 6 month budget was approved by the Board in April 2020 and the final 6 month budget was approved by the Board in September 2020. The first 6 month budget recognised the impact of the closure of sites on commercial income and reduced expenditure to business critical costs only as a result of the COVID-19 pandemic. The second 6 month budget incorporated the additional Grant in Aid (GiA) agreed by the Scottish Government, a continuation of business critical expenditure and a reduction in the investment plan. HES incurred net expenditure of £82.5m and a small deficit of £0.1m against its Scottish Government funding target

As part of the 2021/22 budget setting, HES created a designated reserve of £1.5m (now increased to £2m) to fund repairs to properties in care in future years. The fund was set up from membership income which has not been utilised for repairs during 2020/21 as a result of COVID-19 restrictions.

The financial performance has been consistently reported to the Board throughout the year, with limited variances between budget and projected actual, demonstrating the robust budget management in place.

COVID-19 has had a significant impact on HES during the year as illustrated below, with a 87% reduction in commercial income, offset in part by an increase in Grant-in Aid. As a result, HES has had to constrain spending to ensure that it operate within its budget allocation.



# Financial management (continued)

## Current year financial performance (continued)

HES has an *Investment Plan* in place. Progress against this plan is also reported regularly to the Board. £4.5m of capital investment was incurred during 2020/21. The most significant projects included:

- Corporate Management Information System - £2m has been spent on the system during 2020/21 to progress the phase one implementation; and
- Intranet and Electronic Document Records Management System ("EDRMS") - £0.6m.

COVID-19 has resulted in a significant reduction in activity, with the Investment Plan budget reducing from £9.5m to £5m as HES focused on business critical expenditure.

**2020/21 conclusion:** In line with previous years, HES continues to have effective short-term financial planning and management arrangements in place, with an underspend achieved against the revised budget. Variances were clearly reported throughout the year, along with regular progress on the investment programme. COVID-19 has had a significant impact on the organisation with commercial revenue decreasing by 87%. This has been mitigated by increased Grant-in-Aid, use of the furlough scheme, tight cost controls and targeted reduction in activity to reach a balanced position.

## Savings Plans

**2019/20 conclusion:** Similar to 2018/19, the Board approved a vacancy factor of 7.5% in the 2019/20 budget. This was largely achieved with some departments performing better than others. As part of the Financial Strategy (approved pre COVID-19 pandemic), HES planned to review its operational expenditure and develop a targeted efficiency programme for future years to ensure maximum value for money is being achieved. This was a positive step forward and we highlighted that this should be progressed to help ensure that realistic and achievable savings targets are set at the start of the budget process.

**2020/21 update:** In line with previous years, budget savings for staff costs are realised through applying a vacancy target. Staff costs are £0.5m underspent with the majority of directorates meeting or exceeding their vacancy targets.

The vacancy target relates to an approach taken to reduce staff costs in the year by setting a mandatory three month vacancy target following a post being vacated. As reported in our previous audit reports, while this is a blunt instrument, HES has adopted this approach as it is bound by the Scottish Government pay policies of no compulsory redundancies and yearly pay increases. This makes it difficult to identify staff cost savings, therefore departments are encouraged to identify means other than permanent staff to fill any resource gaps created by vacancies. This could be using fixed term contracts or redeployment from other areas of the organisation.

In 2020/21 HES have made significant savings by being on an emergency footing and have successfully reduced expenditure by £9.4m in comparison with previous years through tight cost controls and targeted reduction in activity. While the use of vacancy targets has been successful in managing the overall budget, this is not sustainable in the medium-to-longer term. Given that staff costs make up more than 50% of the overall budget, it is important that a workforce plan and a programme of service reviews and redesign are progressed, as these could identify other untapped efficiency savings.

**2020/21 conclusion:** All savings targets have been met or exceeded during 2020/21. Efficiency savings have been recovered across business area's during the year out of necessity due to the exceptional circumstances of the pandemic. While the use of vacancy targets has been effective in the short term, this is not sustainable. It is important that service reviews and workforce planning is progressed to develop longer-term efficiencies programmes. **[Recommendation 1]**

# Financial management (continued)

## Financial reporting

**2019/20 conclusion:** Senior management and Board members regularly review progress against budget. The Senior Management Team (SMT) and the Board review financial performance monthly and quarterly respectively. In year financial reporting therefore continued to be robust with explanations for variances transparently reported throughout the year.

**2020/21 update:** HES approved its revised 2020/21 first 6 month budget on 23 April 2020 which was necessitated by the COVID-19 pandemic. The Senior Management Team and Board members regularly reviewed progress against budget throughout the year, with reporting to the SMT and Board meetings. As a result of operating on an emergency footing, revised financial controls were put in place resulting in expenditure being monitored at a more granular level and from a corporate perspective rather than at directorate level. From review of the reporting throughout the year, variances are clearly reported and explained, with additional reporting made to the Board during the year in relation to the business case for additional funding as part of the Scottish Government Spending Review.

**2020/21 conclusion:** HES continues to have strong financial management arrangements in place, with clear reporting of the impact of COVID-19.

## Financial capacity

**2019/20 conclusion:** The team remained consistent with previous year. We were therefore satisfied that the finance team capacity continued to be sufficient to support HES's financial management arrangements.

**2020/21 update:** The Director of Finance, Head of Finance and Head of Finance Business Support have remained consistent throughout the year. A new Financial Accountant was appointed during 2020/21, following the departure of the previous post holder in June 2020. The appointment started in September 2020 meaning that there was an increased workload for the Head of Finance during this time.

Whilst the finance team capacity was impacted during 2020/21 with implementation of the new system, management has confirmed that capacity has improved in 2021/22 with initial automation of transactional activity and is expected to improve further with increased integrations of systems.

As set out on page 16, HES acknowledge that further work is needed to fully integrate the new system, through the use of interfaces, thereby reducing the risk associated with manual entries which existed on the previous system and which remains a risk at present. We are aware that work is taking place on this in 2021/22 to further reduce that residual risk.

**2020/21 conclusion:** HES continues to have a sufficiently qualified and experienced finance team to support the financial management of the organisation. While the capacity of the finance team was impacted with the implementation of the new system, improvements have been noted in 2021/22, with further improvements expected when all interfaces are fully operational.

# Financial management (continued)

## Internal audit

We have assessed the internal audit function, including its nature, organisational status and activities performed. We have analysed the work performed by internal audit, including the number of recommendations made in the year compared to previous years and how promptly recommendations have been addressed. The conclusions have helped inform our audit work, although no specific reliance has been placed on the work of internal audit.

The 2020/21 Internal Audit Plan was approved by ARAC in March 2020. This comprised five projects for the year, three of which were carried out by the external co-source partner.

The internal audit function has completed COVID-19 reflections reviews to ascertain any learning for the organisation for future which have fed into the reimagine work which is currently ongoing. The Internal Audit team is also increasingly involved in business improvement activity which limits their ability to provide independent assurance activities in these areas. Although these risks are monitored, care should be taken around the cumulative impact of this work on the internal audit functions independence overall, not only on an individual project basis. Management should assess the level of resourcing required and the split between the internal audit team and the co-source partner to enable the organisation to deliver a robust internal audit programme in future years. As internal audit increase the amount of business improvement work undertaken cumulatively ARAC should also continue to keep this cumulative effect on independence under review.

The Internal audit programme was reduced compared with previous years due to the impact of the COVID-19 pandemic, however, did not impact on the overall opinion for the year, which was "satisfactory" - meaning "A few specific control weaknesses were noted; generally however, controls evaluated are adequate, appropriate, and effective to provide reasonable assurance that risks are being managed and objectives should be met".

12.5% of recommendations made were classified as high and there were some consistent findings for example regarding project management which have been raised in previous years.

We also consider the work of internal audit as part of our audit work on the Governance Statement and our conclusions are reported on page 21.

## Standards of conduct for prevention and detection of fraud and error

We have assessed HES's arrangements for the prevention and detection of fraud and irregularities. This has included specific considerations in response to the increased risk of fraud as a result of COVID-19. Overall we found HES's arrangements to be to be designed and implemented appropriately.

### Deloitte view – financial management

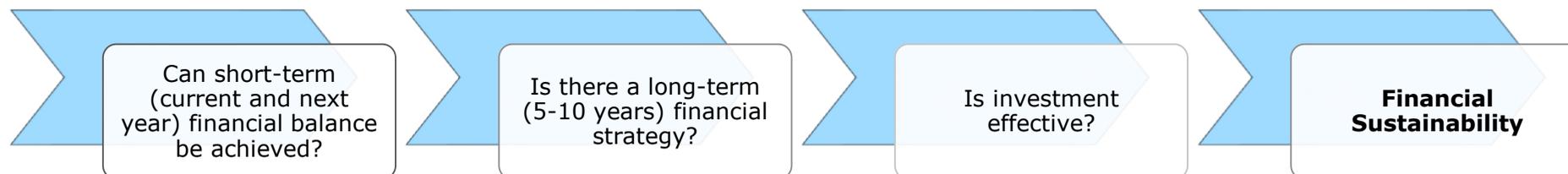
HES Continues to have strong financial management processes in place which are sufficiently robust to manage financial activity and capture and address any challenges to the achievement of financial targets. HES has been significantly impacted by COVID-19, with commercial income dropping 87% during 2020/21 and revised financial controls were put in place to manage this impact. Efficiency savings have been recovered across business area's during the year out of necessity due to the exceptional circumstances of the pandemic. While the use of vacancy targets has been effective in the short term, this is not sustainable. It is important that service reviews and workforce planning is progressed to develop longer-term efficiencies programmes

HES continues to have a sufficiently qualified and experienced finance team to support the financial management of the organisation. While the capacity of the finance team was impacted with the implementation of the new system, management have noted improvements in 2021/22.

The Internal Audit team have completed a reduced programme of audits during 2020/21, however have been able to provide a satisfactory opinion. There is a risk relating to the increased involvement in business improvement activity that should continue to be kept under review.

# Financial sustainability

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



## Areas considered

Our approach to the audit dimensions is risk focused. Within our audit plan we identified the following risk:

*"The financial impact of the pandemic includes a projected reduction in income of £53m for 2020/21. Additional funding of £37.6m has been confirmed by the Scottish Government to partly offset this. Future year funding has not yet been confirmed. While HES has historically achieved short-term financial balance and had made some progress prior to the pandemic with its updated Financial Strategy and Programme for Success, there remains a significant risk that robust long-term planning arrangements are not in place to ensure that HES can manage its finances sustainably and deliver services effectively, identify issues and challenges early and act on them promptly."*

## Budget setting

**2019/20 conclusion:** Despite the challenging position, we were satisfied HES continued to have a robust budget setting process in place. A significant risk of not achieving short term financial balance remained.

**2020/21 update:** In preparing for the 2021/22 budget, detailed papers were considered by the Board between November 2020 and February 2021 to discuss high level projections, the Scottish Government Spending Review and agreement of strategic priorities. The Board then approved a balanced budget of £79.9m for 2021/22 on 11 March 2021. This incorporated a vacancy factor of £3m which is £1m higher than previous years, of which £0.8m relates to seasonal staffing.

As noted on page 24, this is the same approach to savings as previous years. The increased vacancy factor reflects the decision not to open seasonal staffed sites during 2021/22 based on the uncertainty remaining regarding the COVID-19 pandemic. The grants budget has been reduced from £14.5m to £11.5m following the outcome of the Scottish Government spending review. In setting the budget the finance team presented different scenarios, particularly relating to commercial income forecasts and assumptions.

The impact of EU withdrawal has not been specifically considered in the budget paper presented to the Board. This has however been considered by HES in other areas of planning and is not considered to represent a significant risk for the organisation.

COVID-19 has had a significant impact on the budget proposals discussed and decisions taken. The income profile of the organisation has been reversed with the majority of funding received from the Scottish Government rather than commercial income. This has necessitated a reduction in spending across the organisation.

The approved budget is linked to the Annual Operating Plan, structured around the five Corporate Plan outcomes. We are aware that this is an action within the longer term Financial Strategy to move to an outcomes-based approach to planning, linking the activities undertaken and associated require requirement through to the outcome HES want to achieve, but not yet progressed given the focus during 2020/21 in responding to the pandemic.

# Financial sustainability (continued)

## Budget setting (continued)

As noted on page 24, a number of detailed papers were considered by the Board between November 2020 and March 2021, therefore Board members have been heavily involved in the 2021/22 budget process. In addition to the formal considerations, a Board Finance working group was formed in October 2020, which formally transitioned to the Finance Committee, who met for the first time 1 March 2021 to consider the draft 2021/22 budget in detail.

There has not been any specific stakeholder engagement on the budget during the year, however, other sector engagement has been conducted throughout the year. This has helped set strategic themes for reimagine work which were incorporated where possible into the budget preparations. HES identified a number of key risks, as illustrated opposite.

**2020/21 conclusion:** A balanced budget has been approved for 2021/22 and there is a robust budget setting and monitoring process in place for achieving savings. This includes early involvement of the Board as part of this process, with a formal Finance Committee now in place. It is also positive to note that HES is actively assessing the financial impact of COVID-19 and has completed scenario planning. However, the impact of COVID-19 on the ability to achieve short-term financial sustainability remains a risk. Further work is also required to develop outcome based budgeting.

### **[Recommendation 2]**

#### **Key risks and opportunities to the 2021-22 budget:**

- Continued uncertainty regarding COVID-19 and in particular the pace at which lockdown restrictions will be lifted and the rate at which visitor numbers will recover once restrictions are lifted. This will primarily impact the commercial income generation but may also impact the ability to deliver its core activities. (Risk: High)
- The COVID restrictions may impact the deliverability of the Grants programme with grantees being unable to progress work in line with initial expectations. This could lead to underspends against the programme in year and increase the level of commitments for future years. (Risk: High)
- There may be external pressure to return the Grants programme to the historic £14.5m level of funding. (Risk: Medium)
- Additional funding, particularly Capital funding, may become available in year as consequential of UK Government decisions which may allow for an expansion of the proposed Investment Plan programme. (Opportunity: Medium)

# Financial sustainability (continued)

## Medium-to long-term financial planning

**2019/20 conclusion:** The Financial Strategy was refreshed in November 2019. This incorporates a baseline, worst, and best case net outturn scenario for the 10 year period to 2029/30 the most likely scenario is an annual funding gap of £26.9m by 2029/30. This was an increase of £5.4m compared to the funding gap estimated in the November 2018 Financial Strategy so was showing an increasingly challenging position. Given the impact of COVID-19 on both the financial position and operational activity of HES, there is a need for a refresh of the Financial Strategy to re-assess the likely position and actions required.

**2020/21 update:** The Financial Strategy has not been updated in 2020/21 due to the level of uncertainty as a result of the COVID-19 pandemic. Many of the assumptions made within the Financial Strategy are now outdated given the impact of COVID-19, therefore the gaps identified above are likely to be higher. As HES emerges from the pandemic, we recommend it invests in a strategic service review and redesign as part of its reimagine and transformational activities. Financial sustainability in the medium to long-term remains a significant risk for HES.

The impact of EU exit in relation to supplier activity has been limited due to the lack of expenditure following the UK's exit. There are risks in relation to the equivalent to state aid rules for the grants programme not being finalised however processes are currently shadowing the previous EU rules and the Scottish Government are aware. HES has therefore done everything it can at present to mitigate the risk, including setting up its own replacement scheme.

**2020/21 conclusion:** The impact of COVID-19 is expected to have a significant impact over the medium to longer term, and therefore HES needs to assess the estimated impact as the landscape becomes more certain. The medium to long-term financial strategy should be updated to reflect the assumptions the organisation is currently planning to including the impact of COVID-19. As noted on page 25, savings targets need to be identified in a more targeted way linking to service review activity and workforce planning.

## Programme for Success

**2019/20 conclusion:** In view of the impact of COVID-19, planned projects to review the Headquarter facilities and Archives and Collections accommodation were put on hold were being fully re-considered through an options appraisal. The development of the programme was a positive step, as was the appointment of a Programme Manager to drive these forward. We highlighted that it was important that clear benefits tracker is in place to monitor the success of these projects against plan. The impact on COVID-19 increases the risk of successful delivery of these projects.

**2020/21 update:** HES has a Programme for Success in place which is a collection of key projects including:

- Corporate Management Information System ("CMIS");
- Document Centre and HESNet;
- Properties in Care Asset Management Plan ("PICAMS");
- HQ Transformation and Archive House; and
- IT Enablement including Unified Comms.

The internal audit function has carried out a review of the programme for success and made a number of recommendations. These centred around four categories:

- Benefits Management;
- Risk Management;
- Dependency Management; and
- Resource Management.

The key recurring recommendation from this audit and other internal audits is an inconsistent approach to project and change management. An update on the establishment of a Programme Management Office and the transition of projects from PFS to the PMO was provided to the Board in May and August 2021, which includes the development of a robust project management methodology. The PMO Board held its first meeting in July 2021, transitioning from the previous Corporate Programme Governance Board, with the key timelines agreed.

# Financial sustainability (continued)

## Programme for Success (continued)

As the end of the initial phases of the PfS projects approaches, and given the significant financial challenges faced by HES and the impact that COVID-19 has had on the operations, HES has taken the opportunity to reconsider what is needed and either re-frame projects or stopping those that are no longer relevant. The PfS projects have transition to the PMO.

It is important that, as the PMO is embedded, HES ensure that the projects are fully aligned to the updated Financial Strategy and Investment Plan and that any cross-cutting themes are identified to ensure there is a clear corporate view. Staff should also have opportunities to shape the projects and have involvement in redesign of their service areas. It should ensure aims and objectives are clearly defines and a robust benefits realisation tracker is implemented to monitor progress. We are pleased to note that "Benefits" is one of the five workstreams identified within the new PMO.

In delivering the PfS, HES has a number of experienced individuals both at Board and SMT level which has resulted in projects being delivered. As further projects are progressed, it is important that HES assesses the skills and capacity to implement change once the detailed plans have been identified. We are places to note that as part of the PMO work, a resource plan is being drafted.

COVID-19 has delayed some of the programme for success projects and some elements have not been progressed. Instead, COVID-19 has instigated a stream of work named "reimagine" which is looking at transformation type activities.

As a **recovery plan**, HES published a 6 month action plan for the second half of 2020/21. It then developed an Annual Operating Plan for 2021/22 which includes and continues the themes from the Corporate Plan. The Corporate Plan objectives are still relevant although some actions have been prioritised during the pandemic. There are also some where the action will need to be re-visited for the post pandemic world.

The revision of the Corporate Plan and other key corporate documents is a key focus for the recovery plan including:

- Revision of the climate change action plan;
- Review of the digital strategy, digitisation of archives and collections and redesign the online digital services;
- Develop a new equality outcomes and action plan;
- Develop a long-term PiC strategy;
- Develop a green recovery statement and climate change adaption plan;
- Deliver a revised year 2 of the research strategy;
- Develop a creative new learning offer; and
- Deliver a revised year 2 of the international strategy.

There are different approaches being used for delivery of priorities at this time. The plans have been revised to accommodate the impact of the pandemic reducing the volume of work including reducing the actions and/ or moving targets where required.

HES have conducted some stakeholder surveys although not held specific engagement for the action plans released to date.

Leadership has been effective adopting a lead by example approach. The communication during the pandemic by leadership has been regular and open with the use of blogs and question and answer sessions. These have been led by both the CEO and Directors.

**2020/21 conclusion:** HES has made good progress during 2020/21 in relation to the Programme for Success. HES has taken the opportunity to reconsider projects in light of the COVID-19 pandemic to determine what is needed and either re-frame projects or stopping those that are no longer relevant.

We are pleased to note that progress is being made with the implementation of a PMO and will continue to monitor the implementation during our 2021/22 audit.

# Financial sustainability (continued)

## Workforce Planning

**2019/20 conclusion:** Not specifically reported on within our 2019/20 report.

**2020/21 update:** Strategic planning, financial planning and workforce planning are intrinsically linked and critical to the future success of any organisation. Given staff and staff related costs account for over 65% of the overall annual budget, planning and managing workforce is essential to the overall process.

**Workforce Plans** are completed on a directorate level with no strategic workforce plan in place. Workforce planning is also more reactive rather than proactive and does not currently plan for the medium to long-term.

Workforce plans have not been updated since the start of the pandemic or the implementation of CMIS or the voluntary exit programme. These items, amongst other, are significant to the organisation's workforce. Without workforce planning reflecting these there are potentially key workforce risks which are not identified.

We understand that management are reviewing their approach to workforce planning as part of its recovery and re-imagine phase. During 2020/21, work has started to identify the future skills requirements for each directorate which was used to create the "Skills Action Plan" within the People Strategy. In addition, the SMT review workforce statistics on a quarterly basis to review absence, turnover and vacancies.

In developing a workforce plan, it is important that the key workforce statistics such as demographics, sickness, working pattern and turnover levels are clearly considered. It should also define the future workforce, building on the work already done. HES should be able to make assumptions based on experience or the intended benefits of key projects as to how they will affect the workforce. Plans should also define how the organisation is going to get to the future workforce identified. We are pleased to note that as part of the Annual Operating Plan for 2021/22, HES have committed to developing a strategic workforce plan by 31 March 2022.

HES have developed a new **People Strategy** with four pillars of activity.

- Engage our people;
- Employee experience;
- Release Potential; and
- Lead into the Future.

The strategy contains actions and targeted outcomes, however HES should consider whether it is fully considering and measuring the impact of the targeted outcomes. As an example for the outcome "employee's own the people strategy" the success measurement is currently "implementation of the communications plan", but could be more robust by referring to the level and impact of the engagement evidenced through future staff surveys.

As a result of the impact of COVID-19 staff have received regular check-in's from their line manager, SMT have held briefings with their directorates and the CEO has posted blogs and vlogs to keep people informed, supported and motivated since the start of the pandemic.

For those staff who were not on furlough and are able to work from home, the majority had laptops already which eased the change to remote working. There were some issues adapting to remote working in the initial months due to HES's traditional reliance on paper-based methods meaning that some information was not stored electronically. For example all grant claims were held in paper folders and all HR information stored in hardcopy at the office.

# Financial sustainability (continued)

## Workforce Planning (continued)

We are aware as part of the reimagining work ongoing that HES is reviewing its approach to the future ways of working. HES should continue to consider the new frontiers report by the Scottish Futures Trust when completing this exercise.

**Staff feedback** has been gathered in both June and September 2020 through pulse surveys. SMT have then issued “you said we did” articles on the intranet to update staff on progress against issues raised in the surveys. Return to work and health and safety were raised and management have revised the HES car policy to allow staff to use their car rather than public transport and staggered start and finish times to avoid peak travel times. Management of poor performance was highlighted as a development area and management have committed to providing leadership development including coaching skills and how to have difficult conversations.

There has been a reduction in both the staff turnover and sickness absence, as illustrated below, which is consistent with other public sector organisations as a result of the impact of the COVID-19 pandemic on working arrangements.

	<b>Sickness</b>	<b>Turnover</b>
2019/20	11 days	17%
2020/21	7 days	4%

HES have approved a voluntary exit programme which has resulted in 27 staff leaving the organisation during 2021/22 with associated costs of £701k. The SMT prepared a business case which was then approved by the Board and Scottish Government to commence the process. The process was delivered between January and March 2021 with a 10 working day period for applications. Each application was reviewed by the appropriate Director with those approved then being scrutinised by a Panel before communications were issued to employees.

**2020/21 conclusion:** Workforce planning needs to be developed on a strategic basis and updated for key organisational developments. HES should consider whether the organisation is challenging itself enough when setting targets including in relation to its people strategy. HES’s response to the COVID-19 pandemic has been well received on the whole.

## Deloitte view – Financial sustainability

As discussed on page 24, HES achieved short-term financial balance in 2020/21 and has set a balanced budget for 2021/22. There is a robust budget setting and monitoring process in place for achieving savings. This includes early involvement of the Board as part of this process, with a formal Finance Committee now in place. It is also positive to note that HES is actively assessing the financial impact of COVID-19 and has completed scenario planning for 2021/22. However, the impact of COVID-19 on the ability to achieve financial sustainability remains a risk to HES.

The impact of COVID-19 is expected to have a significant impact over the medium to longer term, and therefore HES needs to assess the estimated impact as the landscape becomes more certain. The medium to long-term financial strategy should be updated to reflect the assumptions the organisation is currently planning to including the impact of COVID-19. Savings targets need to be identified in a more targeted way linking to service review activity and workforce planning.

HES has made good progress during 2020/21 in relation to the programme for success and has taken the opportunity to reconsider projects in light of the COVID-19 pandemic. We are pleased to note that progress is being made with the implementation of a PMO, which incorporates the development of benefits trackers and a resource plan. We will continue to monitor the implementation during our 2021/22 audit.

Workforce planning needs to be developed on a strategic basis and updated for key organisational developments. HES have committed to developing a strategic workforce plan by 31 March 2022.

# Governance and transparency

**Governance and transparency** is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information



## Areas considered

Our approach to the audit dimensions is risk focused. Within our audit plan we highlighted the following risk:

*“Following the changes made to the governance arrangements in response to the pandemic, including the establishment of a recovery group, there is a risk that revised arrangements are not appropriate or operating effectively. The Board and its Committees have continued to meet virtually since the start of the pandemic.*”

*While risk management processes continue to be in place, the likelihood and impact of existing risks and the emergence of new risks will need to be monitored carefully. There is a risk that officers and the ARAC members have not considered how sustainable any changes to the risk appetite will be in the longer term. We are aware that ARAC has considered both the COVID-19 risk register and more recently the combined risk register at its meetings.”*

## Leadership

**2019/20 conclusion:** HES continued to have a strong executive leadership, with positive relations between Board members and staff.

**2020/21 update:** There have been no changes at SMT level, however, there have been various changes in the Board membership of HES over the last 12 months. This includes the departure of those whose terms had come to an end and the appointment of those who have been recruited to replace them. All Board members completed both the Scottish Government induction and were provided with a HES specific induction.

HES has a management structure in place which was devised as part of its inception as an organisation, and expanded over the years such as the additional posts of Director of Development and Partnership and Director of People. There are clear lines of responsibility within the structure. HES also have a Scheme of Internal Delegation (“SOID”) in place to make clear which decisions should be made at different levels.

The Chief Executive has instigated a management restructure which is intended to be completed during 2021/22. This was a project which was paused as a result of the pandemic. The Chief Executive currently has 10 people reporting directly to him with eight of those being Directors. Beneath them there are over 30 Head’s of department. From a review of the structure there are opportunities to create a more effective structure which fosters cross-organisational collaboration.

The majority of responses to the staff survey indicated that there is a positive culture, with the employee experience pillars all reporting in excess of 75% positive responses (and 90% of respondents noting they feel respected and valued by teammates. However there was also some indicators that raise concern. These include 25% of respondents indicated that they had experienced or witnessed bullying or harassment and 38% indicated that the process when someone is not performing well in their role is not managed well. 27% of respondents are not confident that action has been taken on the back of previous staff surveys. HES have formulated an action plan and progress against this is shared with staff via intranet articles.

# Governance and transparency (continued)

## *Leadership (continued)*

**2020/21 conclusion:** HES continues to have strong leadership in place. This has been particularly evident in the response to COVID-19, communications and the development of the action plans. The proposed review of the management structure is a positive step as HES move to a more collaborative working model. The staff survey responses indicate that there is a positive culture in place although there are areas to improve. We will monitor managements progress with the restructure and staff survey action plan during 2021/22.

## *Governance and scrutiny arrangements*

**2019/20 conclusion:** HES's governance framework and arrangements continued to support good governance and accountability. There was evidence of strong and effective scrutiny, particularly through the ARAC. There was a positive response to the challenges faced by the COVID-19 pandemic, with appropriate arrangements in place to ensure sufficient support and oversight.

**2020/21 update:** As a result of the COVID-19 pandemic, changes were made to the governance arrangements including:

- The Board and ARAC meetings were conducted virtually throughout the pandemic with only one meeting cancelled during this period.
- The Board and Chief Executive held regular update calls during the pandemic and particularly in the response phase. Board meeting frequency was also stepped up to monthly meetings throughout 2020/21. Although this shows the Board's involvement in the organisation, It should take care that the increased frequency does not stray into operational management or have a detrimental impact on the capacity of senior leaders within the organisation.

We have assessed the number of meetings that have taken place over the last year and level of attendance, and pleased to note that the average attendance at Board meetings was 97% and ARAC 92%. From discussion with both Board members and officers and from our own observations at the Committee, we are satisfied that there has been sufficient and effective scrutiny and challenge.

The ARAC continues to play a key role in the governance and scrutiny arrangements of the Board. In line with good practice, the ARAC completed its annual self-assessment exercise in May 2021 identifying two areas for further progress, although no deficiencies were identified. The self-assessment uses the NAO checklist and there was good discussion during the ARAC meeting itself.

The ARAC considers reports from internal audit throughout the year and has also considered the risk management framework and associated risk reports bi-annually. The risk reporting now coming to the ARAC has improved significantly over the past few years. Reports are comprehensive and have good summarisation that sets out the key risks facing the organisation and the reasons for changes in risk ratings.

HES has effectively responded to the risks identified as part of Audit Scotland's emerging fraud risks report. Existing controls have been enhanced by installing further cyber security measures and financial pressures meant that increased financial controls were put in place.

The ARAC has reviewed the guidance made available and considered the emerging risks and issues within public bodies. The Committee has focused on the key risks and significant issues for HES as an organisation challenging management while allowing them to complete the necessary response work.

**2020/21 conclusion:** HES continues to have robust governance and scrutiny arrangements in place and appropriate arrangements have been in place throughout the COVID-19 pandemic. The ARAC self-assessment and risk reporting are areas of good practice for the organisation. HES and its ARAC have responded appropriately to the risks faced from COVID-19.

# Governance and transparency (continued)

## *Openness and transparency*

**2019/20 conclusion:** The Board continued to be open and transparent in its decision making and demonstrated a commitment to continuous improvement through the action plan developed following the 2018 staff survey. The impact of these actions need to be assessed when the next staff survey is carried out.

**2020/21 update:** Minutes of Board meetings are uploaded onto the website. At March 2021 the latest Board minutes available were December 2020 despite there being a Board meeting in February 2021. No papers are published on the website which is considered standard practice within many public sector organisations. HES does publish key documents, however as noted below the website could be updated for the latest documents in some cases.

The Board hold regular closed sessions which are restricted to the Board members only. In the spirit of openness and transparency, the use of these should be reviewed to ensure that only private and confidential information is discussed in private and all other information is recorded within the minutes that are publicly available. Open sessions are meeting with the Board and SMT members present rather than open to the public. HES do not currently hold public board meetings due to perceived concerns regarding commercial sensitivity. It is considered best practice within the public sector and is increasingly expected by stakeholders including the Scottish Parliament. HES should investigate methods for inviting the public to attend meetings and this could be considered when reviewing the format of meetings.

The "guide to information" published on the HES website and last updated in 2018 contains a number of items where the links are broken or do not link to a specific document. In addition, there are a number of areas where information is available on request. The "guide to information" should be reviewed to ensure it is up to date. For those items where it is currently available on request, HES should consider publishing them on the website in electronic format e.g. Finance, HR policies and risk registers. When policies are due for their review, we recommend that they are considered for publication and if it is possible then it should be published on the website.

It is increasingly the expectation that as much as possible is published for the public to access in the interest of openness and transparency. This also has the added benefit of reducing FOI requests and the resource investment required to respond.

Openness and transparency was an issue identified within the 2018 staff survey. This is a recurring issue within the 2020 staff survey with 27% of respondents not confident that action has been taken based on the previous survey.

**2020/21 conclusion:** While key corporate documents are published on the website, openness and transparency for both the public and staff could be improved to bring HES into line with other public sector organisations. It is expected that all public sector organisations should hold meetings in public and HES should consider this in future. The Board should also limit any closed sessions to private confidential information only. Currently in comparison to other organisations there is a high use of closed sessions with minutes from these sessions not available to the public.

HES should review its guide to information to ensure it is up to date. When reviewing policies they should be considered for publication. If more information is publicly available then this could reduce FOI requests. **[Recommendation 3]**

## Governance and transparency (continued)

### **Deloitte view – Governance and transparency**

HES continues to have strong leadership in place. This has been particularly evident in the response to COVID-19, communications. The proposed review of the management structure is a positive step as HES move to a more collaborative working model. We will monitor managements progress with the restructure and staff survey action plan during 2021/22.

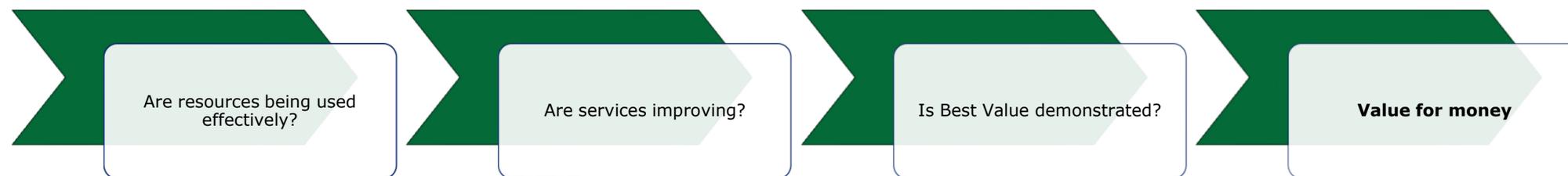
HES continues to have robust governance and scrutiny arrangements in place and appropriate arrangements have been in place throughout the COVID-19 pandemic. The ARAC self-assessment and risk reporting are areas of good practice for the organisation. HES and its ARAC have responded appropriately to the risks faced from COVID-19.

While key corporate documents are published on the website, openness and transparency for both the public and staff could be improved to bring HES into line with other public sector organisations. It is expected that all public sector organisations should hold meetings in public and HES should consider this in future. The Board should also limit any closed sessions to private confidential information only. Currently in comparison to other organisations there is a high use of closed sessions with minutes from these sessions not available to the public.

HES should review it guide to information to ensure it is up to date. When reviewing policies they should be considered for publication. If more information is publicly available then this could reduce FOI requests.

# Value for money

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



## Areas considered

Our approach to the audit dimensions is risk focused. Within our audit plan we identified the following risk:

*"The pandemic is expected to have had a substantial impact on performance measures, particularly for services which have been temporarily suspended, or are provided at a reduced level. The pandemic has had a significant impact on HES' operations, in particular, the operation of visitor sites as well as the conservation and research work normally undertaken. HES has implemented two 6 month action plans in place of the usual annual operating plan for 2020/21 which it has measured performance against. There is a risk that performance reporting has not been timely, reliable, balanced, transparent and appropriate to users' needs."*

## Performance management framework

**2019/20 conclusion:** HES had a clear and effective performance monitoring framework in place to ensure that its performance is monitored and reported in line with KPIs set out in the 3 year Corporate Plan and Annual Operating Plan. These address both HES priorities and wider national outcomes.

**2020/21 update:** HES's performance management framework was altered during 2020/21 to accommodate the impact of the pandemic. As highlighted in other areas of the report HES adopted two six-month action plans. Actions within plans are aligned to the Corporate Plan.

Reporting during the year was unaffected by the pandemic with quarterly reporting to the Board against the actions identified in both action plans.

**2020/21 conclusion:** HES continues to have a clear performance management framework in place through the Action plans developed during 2020/21 which linked to the Corporate Plan outcomes.

## Performance data

**2019/20 conclusion:** HES continued to perform well against its performance targets and had a clear understanding of areas requiring further development. The impact of COVID-19 will have an impact on performance during 2020/21, as set out within the Action Plan for the first six months of 2020/21.

**2020/21 update:** Five outcomes are included within the Corporate Plan with corresponding actions. These are:

- The historic environment makes a real difference to people's lives;
- The historic environment is looked after, protected and managed for the generations to come;
- The historic environment makes a broader contribution to the economy of Scotland and its people;
- The historic environment inspires a creative and vibrant Scotland; and
- The historic environment is cared for and championed by a high-performing organisation.

# Value for money (continued)

## Performance data (continued)

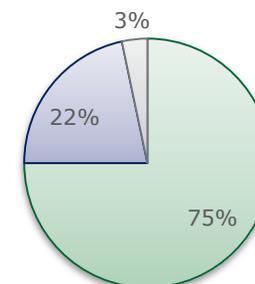
We have made some observations based on the latest available performance reporting:

- There are two KPIs for each outcome, however, these do not detail specific targets which would allow independent assessment of whether the KPI has or has not been achieved. Management has confirmed that the KPIs track long term outcomes and are directional, focussed on trending direction rather than specific targets similar to the national indicators in the NPF. However, over the next 18 months, HES will be reviewing the framework with a view to incorporating more quantifiable long-term outcomes and interim goals at the Corporate Plan level and inform Annual Operating Plans, where possible;
- Success factors determined focus on actions taken rather than the impact which they have on the outcomes HES aim to achieve. There is therefore a risk that HES could be investing time and resources on actions that are having little or no impact on the intended outcome;
- Some actions within the action plans are not specific enough and do not identify a qualitative consideration to assess impact. HES have explained that the planning approach in 2020/21 was adapted in the context of the pandemic, with the content was deliberately framed in a broad way taking account of the uncertainties at the time, which created flexibility to allow for changes in the rapidly changing operational context. For 2021/22, HES have reverted to their standard Annual Operating Plan format with indicators and success measures which are more specific. Where appropriate, these contain quantified targets. HES acknowledge that further work is to be done to measure impacts;
- Performance is assessed via self-assessment. In considering areas for continuous improvement, HES should consider whether an independent assessment of the self-assessment process and of performance achievements could be performed, such as through a peer review; and
- HES has consistently performed above 90% against its annual operating plans and it has again performed well in 2020/21 despite the challenging circumstances. HES should consider whether the targets are sufficiently focussed on measuring impact of the actions.

HES is reporting the impact of COVID-19 to the Board via update calls and reports submitted to monthly Board meetings. HES have published information regarding the COVID-19 impact on the sector and in 2020/21, HES provided a written submission and oral evidence to the Scottish Parliament's Culture, Tourism, Europe and External Affairs enquiry into the impact of COVID-19, which included the impact on HES and the sector.

There are currently no items triggering improvement actions from performance reports presented to the Board.

## 2020/21 Operating Plan



■ Achieved ■ Partially Achieved ■ Not Achieved

**2020/21 conclusion:** HES has consistently performed above 90% against annual operating plans and has again performed well in 2020/21 against action plans. HES should consider whether targets set are sufficiently focussed on measuring the impact of the actions. In striving for continuous improvement. It may be useful for an independent assessment of the self-assessment of performance to be carried out, for example through a peer review. **[Recommendation 4]**

### Deloitte view – Value for money

HES continues to have a clear performance management framework in place through the Action plans developed during 2020/21 which linked to the Corporate Plan outcomes.

HES has consistently performed above 90% against annual operating plans and has again performed well in 2020/21 against action plans. HES should consider whether targets set are sufficiently focussed on measuring the impact of the actions. It may be useful for an independent assessment of the self-assessment of performance to be carried out, for example through a peer review.

# Best value

The Scottish Public Finance Manual ("SPFM") explains that accountable officers have a specific responsibility to ensure that arrangements have been made to secure **Best Value**.

## The duty of Best Value, as set out in the SPFM

- To make arrangements to secure continuous improvement in performance whilst maintaining an appropriate balance between quality and cost; and in making those arrangements and securing that balance.
- To have regard to economy, efficiency, effectiveness, the equal opportunities requirement and to contribute to the achievement of sustainable development.

The SPFM sets out nine characteristics of Best Value which public bodies are expected to demonstrate. The refreshed guidance issued by the Scottish Government in 2011 focused on 5 generic themes and 2 cross-cutting themes, which now define the expectations placed on Accountable Officers by the duty of Best Value.

Five themes:

1. Vision and Leadership
2. Effective Partnerships
3. Governance and Accountability
4. Use of Resources
5. Performance Management

Cross-cutting themes:

1. Equality
2. Sustainability

## Best Value arrangements

HES has a number of arrangements in place to secure Best Value. This is evidenced through the Corporate Plan and the Annual Performance Reporting.

As noted elsewhere within this report, HES has an established governance framework and strong leadership. Staff survey results show a generally positive culture.

HES has a culture of continuous improvement as evidenced by the progress in relation to the programme for success and its reimagining work. This is supported by internal audit business improvement activity.

HES recognises that it must deliver services within the financial resources available and, as noted elsewhere in this report, further work is required to achieve medium to longer term financial sustainability.

## Deloitte view – Best Value

HES has sufficient arrangements in place to secure best value with a strong focus on continuous improvement. It has a clear understanding of areas which require further development.

# Purpose of our report and responsibility statement

## Our report is designed to help you meet your governance duties

### What we report

Our report is designed to help the Audit, Risk and Assurance Committee and the Board discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA (UK) 260 to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements and our observations on the quality of your Annual Report and Accounts;
- Our work on the audit dimensions;
- Our internal control observations; and
- Other insights we have identified from our audit.

### The scope of our work

Our observations are developed in the context of our audit of the Annual Report and Accounts.

We described the scope of our work in our audit plan.

### Use of this report

This report has been prepared for HES, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.

### What we don't report

As you will be aware, our audit was not designed to identify all matters that may be relevant to the Committee.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the procedures performed in fulfilling our audit plan.

We welcome the opportunity to discuss our report with you and receive your feedback.



**Pat Kenny, CPFA**

**For and on behalf of Deloitte LLP**

Glasgow | 1 October 2021

# Sector developments



# Scottish Futures Trust - New Frontiers for Smarter Working, Work and Workplace post COVID-19

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## Background and overview

**COVID-19 has fast-tracked a social revolution where a wider range of working choices could be on the horizon for hundreds of thousands of workers.**

A new report by infrastructure experts, the Scottish Futures Trust reveals that the workforce of the future - predominantly those who have been office based - will want to make informed choices of where and how to work most productively and more beneficially for their wellbeing.

Post the pandemic, organisations should consider the three 'Hs' of working - from Home, a nearby hub or local location, where employees can meet clients or have time to concentrate on projects, or the HQ and head office, where people can gather to socialise, brainstorm ideas or collaborate face-to-face.

The "New Frontiers for Smarter Working, Work and Workplace Report" also finds that this new blended future will depend on how employers gauge the benefits from the improved working set up while ensuring the wellbeing of employees.

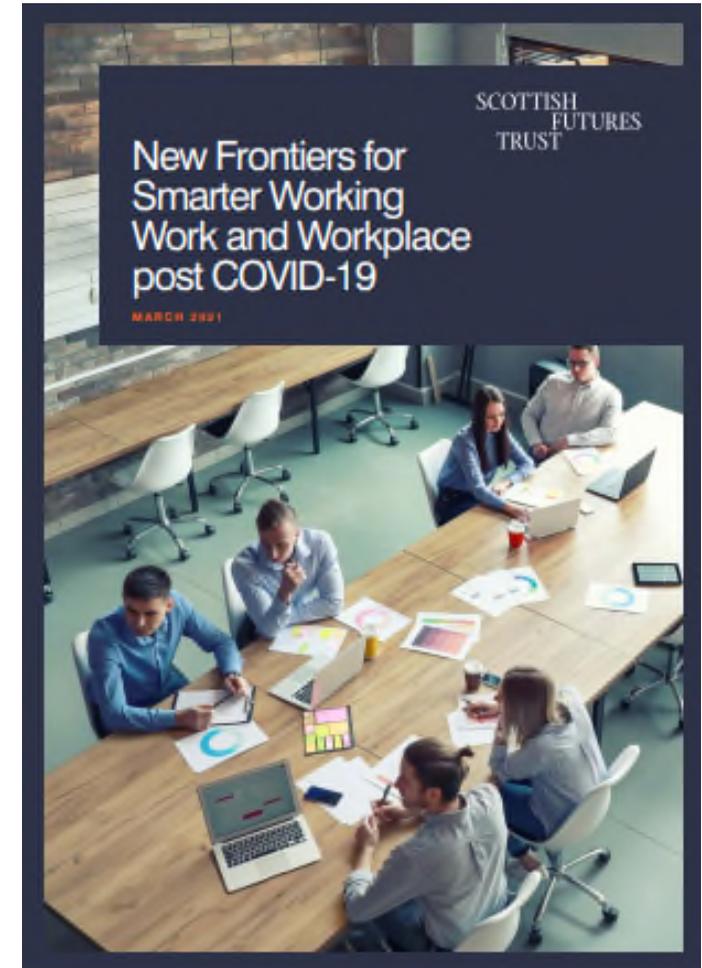
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## Next steps

The report reveals a new future for best work, productivity and wellbeing. The full report is available at:

[https://www.scottishfuturestrust.org.uk/storage/uploads/new\\_frontiers\\_report\\_march2021.pdf](https://www.scottishfuturestrust.org.uk/storage/uploads/new_frontiers_report_march2021.pdf)

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# Appendices



# Audit adjustments

## Uncorrected misstatements

The following uncorrected misstatements have been identified during our audit, which we request that you ask management to correct as required by ISAs (UK). The overall impact on the Statement of Financial Activity is an increase in net income of £0.234m, with a corresponding increase in net assets.

		Debit/(credit) SoFA £m	Debit/(credit) in net assets £m	Debit/(credit) prior year Funds £m	Debit/(credit) OCI/Funds £m
<b>Support Costs</b>	[1]	(0.234)	0.234		

[1] During the audit, a significant movement in the 'Information Systems' category of 'Support Costs' was noted. A detailed analysis was performed of this movement, with this analysis identifying a number of invoices which were incorrectly recorded in 2020/21 due to human error, which consequently overstated expenditure by £0.234m, and understated net assets by the same amount.

# Audit adjustments (continued)

## Corrected misstatements

The following adjustments have been updated by management. We communicate them to you to assist you in fulfilling your governance responsibilities, including reviewing the effectiveness of the system of internal control.

		Debit/(credit) SoFA £m	Debit/(credit) in net assets £m	Debit/(credit) prior year Funds £m	Debit/(credit) OCI/Funds £m
<b>Intercompany transactions</b>	[1]				
Increase HES Income due to HESe recharges		(2.119)			
Income HES Expenditure due to HESe recharges		2.119			
Reduce intercompany debtors due to offset			(1.117)		
Reduce intercompany creditors due to offset			1.117		
<b>Recognition of Grant in Aid</b>	[2]	(0.450)	0.450		
<b>Classification of Assets Under Construction</b>	[3]				
Increase Intangible Assets			0.134		
Decrease Property, Plant and Equipment			(0.134)		
<b>Dilapidations Provisions</b>	[4]	0.122	(0.122)		
<b>Grant Accruals</b>	[5]	(0.316)	0.316		
<b>Classification of Expenditure</b>	[6]				
Increase Support Costs		1.984			
Decrease Charitable Activities		(1.984)			

# Audit adjustments (continued)

## Corrected misstatements (continued)

		Debit/(credit) SoFA £m	Debit/(credit) in net assets £m	Debit/(credit) prior year Funds £m	Debit/(credit) OCI/Funds £m
<b>Prepayments on Rent</b>	[7]	(0.167)	0.167		
<b>Late Accruals</b>	[8]	0.089	(0.089)		
<b>Transfer between Funds</b>	[9]				
Increase Designated Fund					0.500
Decrease General Fund					(0.500)
<b>Valuation of Engine Shed</b>	[10]	(0.357)	0.223		0.134
<b>Total</b>		<b>(1.079)</b>	<b>0.945</b>	<b>-</b>	<b>0.134</b>

[1] HES's CMIS system has an auto-reconciliation feature for intercompany transactions, however, this did not identify all the transactions between HES and HESe and there were difficulties undertaking a manual reconciliation. A full reconciliation was completed, with corresponding adjustments to 'gross up' the HES recharge of salaries to HESe, and offset amounts owing to/from HESe to enable comparison with 2019/20.

[2] HES drew down its full Grant in Aid allocation but this was £0.450m more than required as the full allocation for the additional Historic Environment Recovery Fund was not required. The SPFM and FReM set out, respectively, that there is no mechanism for excess Grant in Aid to be reclaimed through clawback, and that Grant in Aid should be recognised in the year it is received. This adjustment is to recognise the full Grant in Aid in 2020/21, rather than deferring a portion of it not used in the year.

[3] In the draft Annual Report and Accounts, software 'assets under construction' were recorded within 'Tangible Assets'. Following review of the underlying assets, it was agreed that these should be recorded as 'Intangible Assets'.

[4] During the audit, HES undertook a review of other properties subject to lease agreements to identify if there were obligations similar to those properties for which they recognised a dilapidation provision. For a number of these properties, similar obligations existed and an adjustment was raised to ensure that these obligations were captured in the overall dilapidations provision.

[5] In 2020/21, HES did not complete a reconciliation of grants on a Charities SORP basis due to competing priorities. When this reconciliation was performed, it was identified that an adjustment was required to reduce the amount of grant accruals to reflect amounts owing.

# Audit adjustments (continued)

## Corrected misstatements (continued)

[6] There were errors in mapping the new CMIS account codes to the Annual Report and Accounts, which resulted in too many 'expenditure' codes being classified as Charitable Activities and too few being classified as Support Costs. This adjustment was made to rectify the issue identified, ensuring comparability between the 2019/20 and 2020/21 figures.

[7] HES pays rent for Longmore House in advance, with these rental payments consequently being recorded as prepayments for the period covered. In 2020/21, HES paid for the first quarter of 2021/22 prior to the 2020/21 year-end but did not record this as a prepayment. This adjustment was raised to record the amount paid as a 2020/21 prepayment.

[8] During the audit, HES identified that there were a number of accruals of procurement card spend which were not identified when preparing the draft Annual Report and Accounts. An adjustment was raised to ensure these accruals were reflected in the 2020/21 figures.

[9] In 2020/21, the Board approved a transfer of up to £2m between the General Fund and Designated Funds, limited by HES's financial outturn. Due to the net impact of other adjustments identified during the audit process, the amount available for transfer was increased, with this adjustment reflecting that additional transfer.

[10] When the Engine Shed was most recently valued prior to 2020/21, it was valued on the basis that VAT would not be recoverable. In 2020/21, management decided to 'opt to tax' for the Engine Shed, with VAT partially recoverable as a consequence. As the basis for the valuation had changed, we requested a revised valuation report from HES's independent valuers. This adjustment reflects the revised valuation and the partial release of additional VAT recovered through the decision to 'opt to tax'.

# Audit adjustments (continued)

## Disclosures

### Disclosure misstatements

The following disclosure adjustments have been updated by management. We communicate them to you to assist you in fulfilling your governance responsibilities, including reviewing the effectiveness of the system of internal control.

Disclosure	Summary of disclosure requirement	Quantitative or qualitative consideration
<i>Remuneration and Staff Report</i>		
<p>Through our testing of the Remuneration and Staff Report we highlighted a number of adjustments:</p> <ul style="list-style-type: none"><li>- Fair pay disclosure was incorrectly calculated; and</li><li>- Errors in amounts recorded for remuneration and pension contributions for certain individuals.</li></ul>	FReM 6.5 sets out the method of calculation for these disclosures	Qualitatively material – Relates to the Remuneration and Staff Report, which is a key area of public interest.

# Action plan

## Recommendations for improvement – Audit Dimensions

No.	Area	Recommendation	Management Response	Responsible person	Target Date	Priority
1	<i>Financial Management</i>	Future savings plans, particularly in the medium to longer term, should be clearly linked to service reviews and workforce plans. (As initially planned as part of the 2019 Financial Strategy)	The financial strategy will be refreshed in 21/22 and consideration will be given to the need for savings plans linked to service reviews. Any requirement will be reflected in the action plan linked to the strategy.	Head of Financial Business Support	March 2022	Medium
2	<i>Financial Sustainability</i>	The budget should make explicit links to the Corporate Plan and the outcomes the budget expects to progress with the resources expended, in order to enable the Committee to scrutinise whether the focus being placed on the Board's priorities is appropriately resourced. (As initially planned as part of the 2019 Financial Strategy)	The budget development for 22/23 will link activities to corporate plan outcomes and the level of resource committed to each of the outcomes will be presented as part of the budget paper approved by the Board. In addition specific costs associated with Annual Operating Plan measures will be highlighted in the budget paper.	Head of Financial Business Support	March 2022	Medium
3	<i>Governance &amp; Transparency</i>	HES should review its approach to openness and transparency including: the publication of information, use closed sessions of Board meetings and public Board meetings.	Management will work with the new Chair of the Board, when appointed, to consider and take forward this recommendation.	Head of Chief Executive's Office	December 2022	Medium
4	<i>Value for Money</i>	HES should review its performance management assessment process to consider how the impact of actions can be measured. Consideration should also be given to having an independent review of the self-assessment process, for example through a peer review.	The performance management assessment process will be reviewed to consider how the impact of actions can be measured and we will consider having an independent assessment of the self-assessment process after the end of the current Corporate Plan period and as part of the next full review of the Corporate Plan.	Head of Corporate Analysis and Performance	March 2023	Medium

# Action plan (continued)

## Recommendations for improvement – Annual Report and Accounts

No.	Area	Recommendation	Management Response	Responsible person	Target Date	Priority
1	<i>Management review</i>	Management should enhance and document their review of key supporting working papers and the draft Annual Report and Accounts prior to their submission to audit.	The number of challenges we faced with the 2020-21 Annual Report and Accounts including the introduction of a new Finance system and continued impact of COVID-19 limited our ability to complete an effective management review. Our plans for the preparation of the 2021-22 Annual Report and Report will build into sufficient time for an enhanced and documented review.	Head of Finance	Dependent on 2021/22 audit timeline	Medium
2	<i>'After action review'</i>	Given the issues identified during the audit, HES should undertake an 'after action review' to identify lessons learned to improve the Annual Report and Accounts and audit process in future years.	Fundamentally, most of the issues with the 2020-21 Annual Report and Accounts were a result of a move to new finance system in the middle of the year and this will not be repeated. But we will undertake a 'lessons learned' review to inform our planning for the 2021-22 Annual Report and Accounts.	Head of Finance	March 2022	Medium
3	<i>Reconciliations</i>	<p>A number of audit adjustments identified occurred due to full reconciliations not being performed (for example, grant accruals and intercompany transactions), primarily as a result of changes to the system and competing priorities. HES should ensure that appropriate reconciliations and preparatory work are carried out and reviewed prior to preparation of the draft Annual Report and Accounts.</p> <p>To achieve this, there may be a need to consider the Annual Report and Accounts and audit timeline to ensure sufficient time is available for HES to perform the necessary procedures.</p>	Management accept and agree with this recommendation.	Head of Finance	April 2022	Medium

# Our other responsibilities explained

## Fraud responsibilities and representations



### Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.



### Required representations:

We have asked the Board to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the entity or group.

We have also asked the Board to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.



### Audit work performed:

In our planning we identified the risk of fraud in relation to income from government assistance programmes and management override of controls as a key audit risk for your organisation.

During course of our audit, we have had discussions with management and those charged with governance.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the financial statements

We have reviewed the paper prepared by management for ARAC on the process for identifying, evaluating and managing the system of internal financial control.

# Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

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## Independence confirmation

We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of HES and our objectivity is not compromised.

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## Fees

The audit fee for 2020/21, in line with the expected fee provided by Audit Scotland, is £96,440, as analysed below:

	£
Auditor remuneration	78,860
Audit Scotland fixed charges:	
Pooled costs	14,390
Audit support costs	3,190
<b>Total fee</b>	<b>96,440</b>

The audit adjustments identified, the revision of performance materiality and our risk assessment, and the impact of COVID-19 have all impacted on the level of audit work required. We have yet to fully assess this impact. Once completed, we will discuss any impact on the fee with management.

No non-audit services fees have been charged for the period.

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## Non-audit services

In our opinion there are no inconsistencies between the FRC's Ethical Standard and the company's policy for the supply of non-audit services or any apparent breach of that policy. We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.

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## Relationships

We are required to provide written details of all relationships (including the provision of non-audit services) between us and the organisation, its board and senior management and its affiliates, including all services provided by us and the DTTL network to the audited entity, its board and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our objectivity and independence.

We are not aware of any relationships which are required to be disclosed.

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