Technical Bulletin 2022/1

Technical developments and emerging risks from January to March 2022

AUDIT SCOTLAND

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

23 March 2022

Contents

1: Introduction

Purpose

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

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

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

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

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

Highlighted items

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

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1**]	Professional Support has published a Good Practice Note on related party disclosures [**paragraph 6**]	RICS has withdrawn its COVID-19 practice alert [**paragraph 10**]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

Contact point

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2: All sectors

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Independent auditor's reports for 2021/22

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

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

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

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

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

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

5. Auditors should for 2021/22 audits:

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

Good practice in disclosing related parties

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

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

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

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

Withdrawal of valuation practice alert

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

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

3: Local government sector

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Audit assurance protocols for 2021/22

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

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

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

13. Auditors should:

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

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

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

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

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

2021/22 disclosure checklist

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

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

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

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

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

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

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

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

Amendment regulations on loans fund and accounts deadlines

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

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

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

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

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

Guidance on cost-of-living award

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

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

Revised prudential code

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

25. The main changes are in respect of:

- borrowing in advance of need
- commercial investments

- prudential indicators.

Borrowing in advance of need

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

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

- paragraph 50 setting out examples of legitimate prudent borrowing, e.g. financing capital expenditure primarily related to the delivery of a local authority's functions

- paragraph 51 stating that an authority must not borrow to invest primarily for financial return.

Commercial investments

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

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

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

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

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

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

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

Prudential indicators

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

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

34. The following changes have been made to definitions:

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

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

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

Revised treasury management code

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

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

38. Other changes include the following:

- Treasury Management Practice (TMP) 1 has been amended to require that the formal counterparty policy should set out the body's policy and practices relating to Environmental, Social and Governance investment considerations.
- A requirement has been added to TMP 10 for a knowledge and skills schedule. Page 55 of the guidance notes set out suggestions for the schedule.

2020/21 financial overview

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

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

Section 106 charities accounts

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

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

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

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

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

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

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

4: Central government sector

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TGN on risks of misstatement in 2021/22

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

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

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

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

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

Revised 2021/22 FReM

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

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

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

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

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

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

Revised guidance on fair pay disclosure

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

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

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

2021/22 discount rates

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

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

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

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

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

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

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

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

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

2021/22 GBS account information

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

2022/23 FReM

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Amendments to SPFM

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

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

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

5: Health sector

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TGN on risks of misstatement in 2021/22

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

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

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

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

2021/22 accounts manual

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

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

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

Performance Report

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

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

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

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

Remuneration and Staff Report

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

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

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

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

2021/22 CAM

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

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

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

2020/21 NHS overview

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

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

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

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

6. Fraud and irregularities

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

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

Corporate procurement card

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

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

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Technical developments and emerging risks from January to March 2022

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