

AUDIT and RISK COMMITTEE

DATE:	9 May 2022
TITLE OF REPORT:	Summary of Audit Scotland Technical Bulletins Ref. 36-22
AUTHOR AND CONTACT DETAILS	Keith McAllister keith.mcallister@slc.ac.uk
PURPOSE:	To inform the Committee of developments as notified to the Sector by Audit Scotland
KEY RECOMMENDATIONS/ DECISIONS:	Committee to note.
RISK	<ul style="list-style-type: none"> • That the Committee is not aware of developments in the public or college sector that may be pertinent to decision making.
RELEVANT STRATEGIC AIMS:	<ul style="list-style-type: none"> • Highest quality education and support. • Sustainable behaviours.
SUMMARY OF REPORT:	<ul style="list-style-type: none"> • The attached are excerpts from the Audit Scotland Technical Bulletins 2021/4 and 2022/1. • Of particular note is the section in 2021/4 concerned with effective audit planning.

Technical Bulletin

2021/4

Technical developments and emerging risks from
October to December 2021



 AUDIT SCOTLAND

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

14 December 2021

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1: Introduction

Purpose

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

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

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

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 download. However, hyperlinks in this bulletin indicated with an asterisk (*) link to files on 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 guidance on planning 2021/22 audits [see paragraph 1]	Professional Support has expressed views on some technical consultations with auditors [see paragraphs 4 and 37]	Professional Support has published guidance on risks of misstatement in 2021/22 local government annual accounts [see paragraph 5]

Highlighted items

CIPFA has issued guidance notes on the 2021/22 accounting code [see paragraph 9]	CIPFA has issued a consultation on proposed changes to the prudential code [see paragraph 12] and treasury management code [see paragraph 28]	The FRC has issued a paper on what makes a good audit [see paragraph 38]
The FRC has issued a report on IAS 37 disclosures [see paragraph 44]	The FRC has issued a factsheet on climate related financial reporting [see paragraph 46]	The FRC has issued a report on Alternative Performance Measures [see paragraph 52]

Contact point

The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – Pobrien@audit-scotland.gov.uk.

2: All sectors

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

Guidance on planning 2021/22 audits

1. Professional Support has issued guidance to assist all appointed auditors in planning their 2021/22 audits of public bodies. The guidance supplements the Code of Audit Practice, and **auditors are therefore required to plan their 2021/22 audits in accordance with it**. It is accessible by auditors with other supporting materials on [SharePoint](#)* but it is also freely available to download from the Audit Scotland [website](#).

2. The guidance covers the main activities that comprise core audit work and the products associated with each activity. It recognises the impact of COVID-19 on completing the 2020/21 audits and the consequent late start to 2021/22 audits, the challenges in performing audits remotely, and the additional complexities and uncertainties involved.

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

Nature of change	Relevant chapter
Submission dates for Annual Audit Plans have reverted to pre-COVID dates	1
Rates for additional audit work have been revised	1
Guidance on assessing going concern has been added	2
Target submission dates for audited annual accounts have been moved forward one month from last year	2
Auditors are not asked to carry out any new specific work on the audit dimension areas in addition to their own local risk assessments (with the exception of procurement fraud brought forward from previous years' planning guidance)	3A
Submission date for Best Value Audit Plans has reverted to pre-COVID dates	3B
Councils where a Best Value Assurance Report is required have been updated	3B
Auditors are required to complete a return to demonstrate when they have reported their audit work on each of the Best Value themes	3B
The removal of the requirement for auditors in local government to consider Strategic Audit Priorities has been extended to 2021/22	3C

Nature of change	Relevant chapter
The removal of the requirement for auditors to contribute to performance audit reports or impact reports has been extended to 2021/22	4
The number of local government grant claims requiring certification has been reduced to two	5E
Guidance has been updated on involvement in the National Fraud Initiative	5K

Technical consultations with auditors

Professional Support responds to requests from auditors for technical consultations

4. The following tables summarise requests from auditors for technical consultations with Professional Support in respect of complex issues arising from the audit of the 2020/21 annual accounts which may apply to public bodies in all sectors, along with the view offered:

How should cloud computing arrangements be accounted for?

Under cloud computing arrangements, public bodies access and use a supplier's underlying software as needed (e.g. through the internet or via a dedicated line). International Financial Reporting Standards (IFRS) do not contain explicit guidance on how a customer should account for cloud computing arrangements and therefore a body needs to use judgement in determining which standard is the most appropriate to apply. In Professional Support's view, the standards most likely to be applicable are:

- IAS 17 Leases and Similar Arrangements
- IAS 38 Intangible Assets.

In determining whether a cloud arrangement contains a lease, bodies should use IFRIC 4 and evaluate whether the arrangement conveys a right for them to control the use of the asset (e.g. underlying servers). The [IFRS Interpretations Committee](#) has decided that a right to receive future access to the supplier's infrastructure does not in itself give the customer any rights to control the use of the asset.

An intangible asset should be recognised by the body under IAS 38 if:

- it controls the software
- future economic or service benefits are expected
- the body can restrict others' access to those benefits.

Where a contract conveys the right simply to access the supplier's software over the contract term, it would not give the body control of the software and therefore it would not create an intangible asset for the body.

If the cloud arrangement does not fall within the scope of these standards, it is likely to be a service contract; expenditure would be recognised when the service is received.

The body has not included a senior employee in the Remuneration Report because the individual does not wish to be included. Is this acceptable?

Auditors should presume that information on named individuals will be given in all circumstances. However, the General Data Protection Regulation ([Article 21](#)) gives individuals the right to object to disclosure. The employee must give specific reasons, based upon their particular situation, for objecting to the disclosure. Bodies can still make the disclosure if they can demonstrate compelling legitimate grounds for disclosing the information which override the rights of the individual.

Professional Support expressed the following view to the auditor:

- The requirement for public accountability represents compelling legitimate grounds for the required disclosures to be made.
- The body may need to obtain legal advice, particularly if the objection is on the grounds that disclosure would cause the individual substantial damage or distress.
- Where non-disclosure is agreed, the body should instead disclose the fact that certain information has been omitted.

Bodies sometimes enter agreements with employees which attempt to restrict the disclosure of certain remuneration information (e.g. settlement agreements). For the avoidance of doubt, the requirement to disclose information on a relevant individual in the Remuneration Report is not affected by any 'settlement agreement'.

4: Professional matters

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

Paper on elements of good audit

38. The [Financial Reporting Council](#) (FRC) has issued a [paper](#) that sets out its views on the key elements of a high-quality audit. The elements are relevant to audit in any sector, including the public sector.

39. The paper recognises that auditing requires the application of judgement within a principles-based framework; it is not just a rules-based compliance exercise. As a result, it is vital for an audit team to not only have the necessary skills and experience, but also the right behaviours and mindset.

40. The FRC defines high-quality audits as those that:

- comply with the spirit and the letter of auditing standards
- are driven by a robust risk assessment
- are supported by rigorous due process and audit evidence
- involve the exercise of professional judgement and professional scepticism
- challenge management effectively
- report unambiguously the auditor's conclusion on the financial statements.

41. The paper discusses the following three key elements in conducting a good audit:

- Risk assessment and planning.
- Execution of the audit.
- Completion and reporting.

42. The following table summarises some key aspects of each element, and provides examples of associated attributes:

Risk assessment and planning

Key aspects	Examples of attributes
Robust risk assessment	<p>Risk assessment procedures should be based on the inherent (i.e. gross) risk.</p> <p>Procedures must take account of the risk of management bias.</p> <p>Audit planning must be appropriately tailored to the risks identified.</p>
Timely planning	<p>Planning must be performed on a timely basis, well in advance of the financial year end.</p> <p>Planning must be led by the appointment lead and include the key members of the audit team.</p> <p>Planning for more complex areas of the audit may involve relevant specialists.</p>
Knowledge and understanding	<p>The audit team's knowledge and understanding of a business must be tailored to the sector and the specific entity.</p> <p>Knowledge needs to be distilled down to the actual audit risks.</p>
Informed expectations	<p>Audit teams must clearly record their informed expectations relating to key financial metrics and performance indicators.</p> <p>The basis for these auditor expectations must be explained and referenced to source material.</p>
Appropriate resources	<p>The audit team must be appropriately resourced at all levels.</p> <p>Auditors need to agree with the entity that sufficient time is provided to enable the audit to be completed to the appropriate standard.</p> <p>More complex risk areas should have responsibility allocated to experienced team members and, where necessary, specialists.</p>
Planning analytical review	<p>Effective planning analytical review blends the team's knowledge and expectations with management information to identify counter-intuitive trends and relationships.</p> <p>The nature of these potential anomalies must be resolved before the start of fieldwork.</p>
Planning the group audit	<p>Auditors must communicate the group audit approach to component auditors.</p>
Communication to those charged with governance	<p>The audit approach must be clearly communicated to those charged with governance.</p> <p>There should be clear documentation of the detailed correspondence and discussion between the audit team, management and those charged with governance.</p>

Execution of the audit

Key aspects	Examples of attributes
Execution of the audit plan	<p>The fieldwork must comprise execution of the agreed audit plan.</p> <p>Audit team should demonstrate how they have applied high-quality judgement to assess the (corroborative and contradictory) evidence they have obtained.</p> <p>The oversight and direction of the work of the audit team is critical.</p> <p>The level of participation of the appointment lead should be greater for more complex, higher risk audits.</p> <p>The audit documentation needs to provide an easy to follow narrative of the audit and the critical thinking of the team members.</p>
Professional scepticism and challenge of management	<p>Professional scepticism may be particularly apparent when assessing management's judgements and estimates.</p> <p>Auditors must consult appropriately when carrying out the audit of complex areas.</p> <p>Auditors should persist in challenging management if their concerns are not addressed.</p> <p>Auditors are expected to challenge management over whether their narrative reporting is fair, balanced and understandable (and not simply tick off a compliance report).</p>
Specialists and experts	<p>Relevant audit specialists or experts should be brought into the audit team to ensure it has sufficient expertise to assess the risks or to design and perform procedures responsive to the risks.</p>
Group oversight	<p>Better quality audits have particularly close contact with the component audit teams to deal with issues as they arise.</p>
Consultation and oversight	<p>Appropriate consultation with others on complex technical matters is a strength of an audit team.</p> <p>It is essential that those consulted are provided with sufficient information and time.</p> <p>There must be a clear record of the consultation showing how the audit team reached its initial conclusions, how the challenges were dealt with and how any matters arising were subsequently resolved.</p>

Completion and reporting

Key aspects	Examples of attributes
Assess that sufficient, appropriate audit evidence has been obtained	Audit teams should stand-back and assess the level of work performed against the audit plan and ensure that sufficient, appropriate audit evidence has been obtained in support of the conclusions and judgements drawn.
Communicate matters of interest	<p>Auditors must communicate matters of interest to those charged with governance in a timely way.</p> <p>Where teams find themselves in a very time-pressured environment, they must seek to obtain more resource, or delay completion of the audit.</p> <p>If an audit report is delayed, audit teams should record the reasoning.</p>

43. Delivery of the various aspects within these elements depends on a high performing audit practice. The FRC consider that there are six elements to achieving this. These elements are summarised in the following table with examples of some attributes:

Key element	Examples of attributes
Assessing firm quality risks	Early adoption of ISQM (UK) 1 is strongly encouraged as this is expected to lead to improvements in audit quality.
Mindset, culture, governance and leadership	<p>Senior leadership must live and drive the right values, ethics and behaviours that support high audit quality.</p> <p>There must be a clear link between remuneration/promotion and audit quality.</p> <p>Learning from audit inspections (internal and external), including good practice, must be shared across the audit practice and understood.</p>
Performance monitoring and remediation	<p>There needs to be an effective feedback loop to monitor performance of the audit practice; deficiencies identified should trigger decisive corrective action.</p> <p>It is important to create a culture of trust, whereby people are encouraged to openly talk about mistakes and learn from them.</p>
Quality monitoring	Audit providers should re-evaluate the effectiveness of their quality monitoring approach, including hot reviews, and assess how it integrates with the other elements of the quality control system in order to effectively and sustainably remediate recurring deficiencies.

Key element	Examples of attributes
Resources (including recruitment and training)	<p>It is essential that firms have sufficient, suitably trained and experienced staff to service their existing portfolio and support growth plans.</p> <p>Audit firms should align their reward and performance management framework to the delivery of high-quality audits.</p> <p>There should be a consistently applied audit methodology, understood and delivered by appropriately trained people.</p>
Information and communications	<p>Audit providers should regularly communicate with their audit teams and ensure that they have appropriate knowledge and skills.</p> <p>Audit teams should be supported by access to central teams with in-depth knowledge over auditing, accounting and other relevant matters.</p>

Thematic review of IAS 37 disclosures

44. The FRC has issued a [report](#) summarising the findings from a thematic review of disclosures related to IAS 37 Provisions, Contingent Liabilities and Contingent Assets. The review considered how effectively a sample of UK companies met the disclosure requirements and provided other relevant information in their 2020/21 annual report and accounts

45. The report set out expected good disclosure for when a matter is material and relevant to the entity's financial reporting. Good practice in key areas is summarised in the following table:

Area	Explanation
Accounting policies	Concise and entity-specific descriptions of the significant accounting policies adopted in respect of provisions and contingencies
Basis for determining best estimate	Clear and specific descriptions of the nature of each material exposure, the timeframe over which it is expected to crystallise and the basis for determining the best estimate of the outflow
Contingent liabilities	Quantitative information about expected or maximum exposures to contingent liabilities, or a clear and justified statement that it is not practicable to provide an estimate of the financial effect; negative confirmation can be helpful where users may otherwise expect the entity to report an exposure
Indications of uncertainty	Indications of uncertainty in timing and/or amount that help users understand the potential financial effect (which may arise beyond the next financial year) of additional or reduced costs and/or earlier or later timing of outflows

Area	Explanation
Explanation of significant judgement	Explanation of significant judgement exercised by management in determining the recognition and measurement of provisions, setting out the rationale for management's conclusion and the effect on the financial statements of taking an alternative view
Information about critical estimation uncertainty	Quantitative and qualitative information about critical estimation uncertainty affecting the next financial year, including disclosure of key assumptions and sensitivities
Management commentary	Management commentary on significant year end balances and unrecognised exposures, and on significant movements recognised during the period

Factsheet on climate related reporting

46. The FRC has issued a [factsheet](#) on the financial reporting of climate-related matters. The factsheet informs preparers of annual accounts about climate-related matters that they may need to consider when preparing financial statements and associated narrative reporting.

47. Although, it is focussed on FRS 102, the principles in the factsheet apply equally to IFRS-based financial statements.

48. The first part of the factsheet outlines the ways in which climate-related matters may impact on a set of financial statements. Although there are no explicit references to climate-related matters in accounting standards, such matters should be considered in the same manner as any other matters which could have a material impact on the financial statements.

49. The guidance in the factsheet sets out the ways in which financial statements should take into account:

- the impact the entity has on climate change (such as investment in carbon-reducing technology)
- the impact climate change has on the entity (such as on the measurement of individual assets or on the long-term viability of the business).

50. Examples of areas where climate-related matters may impact on the financial statements are summarised in the following table:

Area	Examples of impact
Financial instruments	Measurement could be affected if the matters cause credit losses (e.g. through non-payment by borrowers) or impact an entity's ability to obtain finance. The fair value of financial instruments could be impacted.

Area	Examples of impact
Property, plant and equipment	<p>An entity may require to incur expenditure in ways not previously expected or experienced, such as altering existing assets to make machinery 'greener' or to comply with new legislation.</p> <p>Changes in the residual value or useful life of an asset may result from matters such as:</p> <ul style="list-style-type: none"> • a property being situated in a location expected to be negatively impacted by climate change, such as by rising sea levels • a machine being impacted by changes in legislation designed to reduce dependence on fossil fuels • vehicles becoming obsolete sooner than expected due to rapid technological change.
Provisions and contingencies	<p>Climate-related risks and uncertainties may require the recognition of additional provisions or disclosure of contingent liabilities (e.g. litigation from an increased focus on climate change).</p> <p>A provision for decommissioning an asset may increase if more stringent environmental regulations are put in place, or if the useful life of the asset is reduced (reducing the discount for time value of money).</p>

51. The second part of the factsheet considers narrative reporting. For example:

- Themes included by entities within the narrative reporting should be reflected in the financial statements.
- Entities need to consider the inclusion of climate-related risks in the reporting of their principal risks and uncertainties.

Thematic review of APMs

52. The FRC has issued a [report](#) following a thematic review which assesses the quality of the reporting of Alternative Performance Measures (APMs) in UK-listed companies. APMs are indicators of financial performance which involve adjustments to the amounts reported in the financial statements.

53. The review found that, while companies generally provided good quality APM disclosures, their context needs to be better explained, particularly as profit-based APMs tended to be more favourable than their results in the financial statements.

54. The report advises entities to:

- clearly define APMs and explain why they are needed
- ensure that APMs are not presented in ways that give them greater prominence than amounts stemming from the financial statements

- avoid comments that imply APMs have more authority than amounts stemming from the financial statements
- provide specific, tailored explanations for the inclusion of individual APMs
- explain terms such as 'underlying profit' or 'core operations' and the basis for identifying adjustments as 'non-underlying' or non-core'
- reconcile APMs to the most directly reconcilable line items, subtotals or totals presented in the financial statements.

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

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1: Introduction

Purpose

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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

The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – Pobrien@audit-scotland.gov.uk.

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	<p>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.</p> <hr/> <p>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.</p> <hr/> <p>There are also some minor wording clarifications.</p>
Application guidance	<p>Changes in the guidance include:</p> <ul style="list-style-type: none"> • 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.

6. Fraud and irregularities

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

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

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

Corporate procurement card

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

Key features

The employee used an emergency authorisation process to bypass the requirement to obtain authorisation at a local level. It was therefore not identified that the purchases were not legitimate. The employee also dishonestly accessed emails and misused a computer system to fraudulently authorise their own purchases.

The fraud was identified through budgetary control processes.

The employee has been dismissed and reported to the Procurator Fiscal. Two managers are also subject to the council's disciplinary procedures.

Detailed instructions and training have since been provided to staff outlining the proper process for the use and authorisation of corporate procurement cards.
