Scottish Canals

2022/23 Annual Audit Report

Prepared for the Scottish Canals and the Auditor General for Scotland

March 2024

Contents

Key messages

2022/23 annual report and accounts

1. Audit opinions on the annual report and accounts are unmodified. This is a significant change from the disclaimer opinion issued on the 2021/22 accounts.
2. Additional finance staffing in 2023 has had a significant impact on the quality of accounts and support provided to the audit process. The non-current asset valuation and accounting process has substantially improved.
3. However, there were still significant adjustments to the unaudited accounts and further improvements are required. Adjustments of £11.2 million were made in 2022/23 and 2021/22 comparatives were also revised by £48.4 million.
4. We found that the EY model for valuation was reasonable, but we note that Scottish Canals needs to plan for further revaluation exercises over the period to 31 March 2027.
5. There were also issues with Corporation Tax, accounting for pensions and deferred capital grants, which were adjusted.

Financial management and sustainability

6. Scottish Canals had appropriate budget processes during 2022/23.
7. Scottish Canals exceeded its budget in 2022/23, however Transport Scotland have confirmed this overspend will be managed within its budget.
8. There were significant weaknesses in financial control arrangements.
9. Scottish Canals does not have a medium-term financial outlook/ strategy.

Introduction

1. This report summarises the findings from the 2022/23 annual audit of Scottish Canals. The scope of the audit was set out in an annual audit plan presented to the meeting of the Audit and Risk Committee on 7 September 2024. This Annual Audit Report comprises significant matters arising from the audit of Scottish Canals annual report and accounts and conclusions on the following wider scope areas that frame public audit as set out in the *Code of Audit Practice 2021.*

2. This report is addressed to the board of Scottish Canals and the Auditor General for Scotland and will be published on Audit Scotland's website www.audit-scotland.gov.uk in due course. We would like to thank board members, audit and risk committee members, executive directors, and other staff, particularly those in finance, for their co-operation and assistance in this year and we look forward to working together constructively over the course of the five-year appointment.

Responsibilities and reporting

3. Scottish Canals has primary responsibility for ensuring the proper financial stewardship of public funds. This includes preparing an annual report and accounts that are in accordance with the account's direction from the Scottish Ministers. Scottish Canals is also responsible for establishing appropriate and effective arrangements for governance, propriety, and regularity. The responsibilities of the independent auditor are established by the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice 2021 and supplementary guidance and International Standards on Auditing in the UK.

4. Weaknesses or risks identified are only those which have come to our attention during our normal audit work and may not be all that exist. Communicating these does not absolve management of Scottish Canals from its responsibility to address the issues we raise and from maintaining adequate systems of control. This report contains an agreed action plan at Appendix 1. It sets out specific recommendations, the responsible officers and dates for implementation.

Auditor Independence

5. We can confirm that we comply with the Financial Reporting Council's Ethical Standard. We can also confirm that we have not undertaken any non-audit related services and therefore the 2022/23 audit fee of £95,000 as set out in our 2022/23 Annual Audit Plan remains unchanged. We are not aware of any relationships that could compromise our objectivity and independence.

1. Audit of 2022/23 annual report and accounts

Public bodies are required to prepare annual reports and accounts comprising financial statements and other related reports. These are principal means of accounting for the stewardship public funds.

Main judgements

Audit opinions on the annual report and accounts are unmodified.

Additional finance staffing in 2023 has had a significant impact on the quality of accounts and support provided to the audit process. The non-current asset valuation and accounting process has substantially improved.

However, there were still significant adjustments to the unaudited accounts and further improvements are required. Adjustments of £11.2 million were made in 2022/23 and 2021/22 comparatives were also revised by £48.4 million.

We found that the EY model for valuation was reasonable, but we note that Scottish Canals needs to plan for further revaluation exercises over the period to 31 March 2027.

There were also issues with Corporation Tax, accounting for pensions and deferred capital grants, which were adjusted.

Audit opinions on the annual report and accounts are unmodified

6. The board approved the annual report and accounts for Scottish Canals for the year ended 31 March 2023 on 21 March 2024. As reported in the independent auditor’s report, in my opinion as the appointed auditor:

- the financial statements give a true and fair view and were properly prepared in accordance with the financial reporting framework
- expenditure and income were in accordance with applicable enactments and guidance

- the audited part of the remuneration and staff report was prepared in accordance with the financial reporting framework
- the performance report and governance statement were consistent with the financial statements and properly prepared in accordance with the relevant legislation and directions made by Scottish Ministers.

The unaudited accounts were received just after the agreed audit timetable.

7. The unaudited annual report and accounts were received on 3 November 2023, two days later than originally agreed.

8. The unaudited accounts were substantially complete and were accompanied by a trial balance and ledger that agreed to the accounts apart from a few minor issues. The accounts were also supported by a fixed asset register for the first time, based on valuation information provided by management's experts and contained in the EY valuation model and in valuations provided by Gerald Eve.

9. We were unable to undertake our planned early work on the EY fixed asset model. We anticipated that it would be provided in August or September but was not available to Scottish Canals until October and was not submitted for audit until early November.

10. Our audit fieldwork was not substantially completed until 8 February 2024, with Christmas holidays and the early lost time taken to understand and audit the EY model being the most significant factors in the time taken.

The information and support for audit is greatly improved, but there were still some significant changes to the accounts.

11. The additional finance staffing put in place in 2023 has had a significant impact on the quality of accounts submitted for audit and in the support provided to the audit process. The key focus has obviously been on the non-current asset valuation and accounting and while this has substantially improved the evidence provided for audit over the previous year, there were still issues with the capital accounting processes and errors with completeness and valuation with a marginal number of assets, which were material to the accounts. There were also issues with areas which perhaps have not had the focus due to the much bigger issues of non-current asset valuation. These included corporation tax, treatment of which should have been reviewed and agreed with HMRC when Scottish Canals became a Non-Departmental Public Body (NDPB) in 2020,and deferred grant accounting which required further adjustment. Across the public sector this year there have also been challenges with the recognition of pensions assets and the introduction of IFRS16 covering leases which also affected Scottish Canals.

12. There were significant misstatements that were agreed during the course of the audit with Scottish Canals and have been subsequently adjusted. These totalled £11.2 million, with 2021/22 comparatives also revised by £48.4 million by Scottish Canals as a result. There are identified in more detail in Paragraph 24.

Overall materiality was assessed as £9.6 million

13. Broadly, the concept of materiality is applied by auditors to determine whether misstatements identified during the audit could reasonably be expected to influence the economic decisions of users of the financial statements, and hence impact their opinion set out in the independent auditor's report. Auditors set a monetary threshold when considering materiality, although some issues may be considered material by their nature. It is ultimately a matter of the auditor's professional judgement.

14. Our initial assessment of materiality was carried out during the risk assessment and planning phase of the audit. This was reviewed and revised on receipt of the unaudited annual report and accounts and is summarised in Exhibit 1.

Exhibit 1
Materiality values

Materiality level	Amount
Overall materiality	£9.6 million
Performance materiality	£5.2 million
Reporting threshold	£250 thousand

15. The overall materiality threshold was set with reference to gross assets, which we judged as the figure most relevant to the users of the financial statements.

16. Performance materiality is used by auditors when undertaking work on individual areas of the financial statements. It is a lower materiality threshold, set to reduce the probability of aggregated misstatements exceeding overall materiality. Performance materiality was set at 55% of overall materiality.

Lower specific materiality levels for the 2022/23 audit

17. In addition to overall materiality, we can set lower, specific materiality levels for certain classes of transaction, account balances or disclosures where lesser amounts could influence the decisions of the users of the financial statements.

18. The asset position of Scottish Canals is a significantly higher value than the annual operating expenditure. We recognise that income and expenditure streams of Scottish Canals are likely to be of key interest to the users of the financial statements and we set specific materiality levels as shown in Exhibit 2.

Exhibit 2
Specific lower materiality levels

Materiality level	Amount
Specific materiality	£ 596 thousand
Specific Performance materiality	£ 328 thousand

19. It is our responsibility to request that all misstatements, other than those below our reporting threshold, are corrected, although the final decision on making the correction lies with those charged with governance.

Significant findings and key audit matters

20. Under International Standard on Auditing (UK) 260 we communicate significant findings from the audit to the board, including our view about the qualitative aspects of the body's accounting practices.

21. The Code of Audit Practice also requires all audits to communicate key audit matters within the annual audit report under International Standard on Auditing (UK) 701. These are matters that we judged to be of most significance in our audit of the financial statements.

22. The significant findings are summarised in Exhibit 3.

Exhibit 3
Significant findings and key audit matters from the audit of the annual report and accounts

Issue	Resolution
1. Assets incorrectly excluded from NBV (MA 77002) We identified 132 assets that were not revalued using a Depreciated Replacement Cost valuation method. These were still held at depreciated historical cost. These assets include Access Roads and Car Parks that were determined as out with	Scottish Canals obtained valuations for the car parks and access roads in February 2024. The valuation exercise highlighted that one significant asset (A1144 Bowling Viaduct Access for £4.7 million) was not an access road but represented the value of works undertaken on the

Issue	Resolution
the scope of the EY valuation, as they were not considered part of the canal infrastructure. They were also omitted from the Gerald Eve valuation exercise as they are operational rather than investment properties. These assets also included non-operational land. The net book value (NBV) of these assets is £6.8 million in 2021/22 and they had not been subject to revaluation in 2021/22 or 2022/23. **(MA 77384)** A formula error was also identified in the Fixed Asset Register which omitted adjustments relating to the 'Include at NBV' assets in 2022/23.	Bowline viaduct project and formed part of the revaluation of Bowline – item 5 below). Not all items were fully valued but the net impact of the assets valued was £0.3 million. Scottish Canals decided not to amend the audited accounts to recognise this revised treatment and we are content the impact is not material. The formula error was corrected in the audited financial statements and resulted in an increase of £21.1 million of NBV of assets. **Recommendation 1 and 2**
2. Revaluation Reserve movements **(MA 77198 & 76137)** The 2021/22 and 2022/23 revaluation reserve movements in the Fixed Asset Register did not reconcile to unaudited accounts and it is not clear where 'In-year amortised to P&L' movements have been posted. Revaluation movements on Investment Property had been included in the revaluation reserve in error.	Management amended the FAR to ensure Investment Property revaluation movements were not taken to the revaluation reserve in line with accounting policy. A revised FAR was provided that reconciled to Note 6 and the Statement of Changes in Taxpayers' Equity (SoCTE). The impact of this revision was a £3.4m reduction in the revaluation reserve balance.
3. Ownership and Completeness of Fixed Asset Register (MA 77347) We performed audit procedures to confirm assets on the Statement of Financial Position were owned by Scottish Canals and that assets owned by Scottish Canals were reflected in the FAR and SOFP. We identified one asset (Duntreath Avenue Bridge) valued at £5.4m that was on the FAR but not owned by Scottish Canals. This was omitted in error as part of a review of assets across the canal network where ownership was contentious. We performed further audit procedures and identified no other assets where ownership could not be confirmed. We performed further procedures on assets within management's ownership review and identified	Scottish Canals removed the Duntreath Avenue Bridge asset from the audited accounts. This resulted in a decrease of £5.7m in the NBV of non-current assets.

Issue	Resolution
several assets that were owned but had not been valued.	
4. Opening PPE balances as at 1 April 2021 and 2021/22 revaluation amounts **(MA 77265)** An example asset was selected to understand revaluation movements in the fixed asset register, before we undertook sample testing of the movements. This included a review of the rollback methodology from the valuation as at 31 March 2022 to obtain opening balances for 2021/22. The Gondola structures at the Falkirk Wheel (SC-100726 and SC-100727) had no opening value due to their capitalisation date being recorded after 31 March 2021. This was inconsistent with auditor knowledge as the Falkirk Wheel assets were operational before 2021 therefore should have had values. This identified an error in the FAR relating to incorrect capitalisation dates. A wider review of rollback working paper identified 55 assets with AMX capitalisation dates after March 2021 and no opening value at 1 April 2021 in the Fixed Asset Register. Management performed a review of assets with values in the 2022/23 but had missing values in the 21/22 FAR and assessed these on an asset-by-asset basis.	Scottish Canals decided not to amend the audited accounts to recognise this capitalisation date error in the prior year fixed asset registers. The analysis provided by Scottish Canals estimated that the unadjusted misstatement in prior year NBV would be £3.05 million. This would increase opening balances at 1 April 2021 and reduce 2021/22 revaluation adjustments. It does not affect the 2022/23 accounts and no adjustment was necessary in the 2022/23 accounts for this. **Recommendation 2**
5. Bowling Bridge **(MA 76835)** Our review of transfers from Assets Under Construction identified expenditure on pathworks on Bridge 50, Bowling Railway Bridge. We originally identified that the Fixed Asset Register did not include the underlying bridge structure asset on the FAR. Further review of this issue identified that assets relating to the Bowline project (including Bridge 50) had not been correctly reflected in the EY valuation model.	Management engaged with EY to review the valuation of the Bowline project. A revised valuation was provided for assets along the Bowline to provide an accurate Depreciated Replacement Cost (DRC) valuation for the relevant viaduct assets. We reviewed the methodology and assumptions applied to this valuation and concluded a reasonable approach was adopted. The impact was a reduction in Net Book Value of £5.4 million, which Scottish Canals decided not to adjust for due to materiality.

Issue	Resolution
6.Corporation Tax calculations **(MA 76176)** Following a meeting with KPMG staff on 11 December 2023 we were able to establish that corporation tax calculations had continued to treat all expenditure as deductible since Scottish Canals status had changed to an NDPB. This was incorrect as expenditure funded from Government Grant in Aid is out with the scope of Corporation Tax, and the treatment should be agreed with HMRC.	KPMG revised the calculations mid-February 2024 to remove costs which were funded from GIA. This increased the amount payable under Corporation Tax since Scottish Canals became an NDPB, but as the organisation has accumulated tax losses brought forward it did not result in a liability for Corporation Tax at the 31 March 2023. We recommend that future financial projections are revised to take account of the additional corporation tax payable once accumulated losses are extinguished or expired, and an agreement on the required treatment is arranged with HMRC to provide clarity going forward. **Recommendation 3**
7. Accounting for pensions assets **(MA 75047)** The unaudited accounts identified a pensions asset of £1.2 million. The pension accounting standard (IAS 19) limits any pension asset to the lower of the surplus and what is described as an asset ceiling. Further guidance on calculating the asset ceiling is provided in IFRIC 14. It refers to the impact of a ‘minimum funding requirement’ which stipulates a minimum amount of contributions that must be paid over a given period. The existence of a minimum funding requirement limits the ability of a body to reduce future contributions. Where the present value of the minimum funding requirement contributions exceeds the future service cost, IFRIC 14 advises that no asset should be recognised. Initially Scottish Canals had not asked for an IFRIC 14 calculation before identifying a pensions asset in the unaudited accounts.	An IFRIC 14 report was obtained from Hymans Robertson, which confirmed there should be an asset ceiling in place. The pensions note in the audited accounts was amended accordingly, with the amount of Strathclyde Pension Fund balance being reduced to £nil.
8. Deferred capital grants **(MA 77185 & 77186)**	Scottish Canals amended the audited accounts to recognise this revised treatment.

Issue	Resolution
Scottish Canals had been amortising capital grants over the lifetime of the associated asset. The Financial Reporting Manual (FreM) interprets the treatment of government grants in a different way to the underlying accounting standard (IAS 20) "The option provided in IAS 20 to defer grant income relating to an asset is restricted to income where the funder imposes a condition". The majority of government grants received by Scottish Canals had no grant conditions beyond the construction of associated assets and the deferred grant should be recognised when conditions have been met.	
9. Late recognition of capital grants **(MA 76397)** The unaudited accounts omitted £3.7 million of capital grants for 2022/23, which had been received after 31 March 2023 but had not been included in the grant summary working paper, the draft accounts note or the ledger. This omission was identified by Scottish Canals during the audit.	Scottish Canals amended the audited accounts to recognise these capital grants relating to 2022/23. **Recommendation 4**
10. Depreciation included in accruals in Note 15 **(MA 74675)** The unaudited accounts included £4.9 million of depreciation within accruals, which meant that Note 15 did not agree to the statement of financial position. The error was amended in the master spreadsheet, but not in the initial draft of the Annual Report & Accounts.	Scottish Canals amended the audited accounts to recognise the correct treatment of depreciation in the note and ensured it agreed to the statement of financial position.
11. Review of Assets Under Construction and disposals at year-end **(MA 76836)** Seven Assets Under Construction balances totalling £17.2 million were tested. One item (Townhead Reservoir) for £814,000 was found to be incorrectly classified as the work was completed and so deemed operational at year-end. **(MA 76834)** We also tested transfers from Assets Under Construction to other PPE categories. We tested 99% of transfers in 2022/23 (£31.5 million). Five of the sampled items were incorrectly classified, as	Management adjusted for the incorrect classification of Townhead Reservoir. This resulted in £814,000 being transferred from Assets Under Construction to PPE. Management decided not to adjust for the error regarding when assets should have been historically transferred. This had no impact on the 2022/23 accounts, as it related to 2021/22. The errors impact the classification of assets and depreciation charge in the prior year.

Issue	Resolution
the assets were operational prior to 1 April 2022 and therefore should have been transferred in prior years. This represented £2.7 million of transfers. **(MA 77110)** Disposals of PPE are not material, however our sample testing of one disposal of £550,000 (from a total population of £4.9 million), indicated that this was treated as a disposal in error. This error occurred due to a communication issue between engineers/project managers and the finance team.	Management adjusted for the disposal error. The impact of this adjustment was a £0.2 million increase in Property, plant and equipment. We considered whether further audit procedures were necessary but decided that this was not required as our testing was extensive and any error found did not represent a risk of material misstatement in the untested items. Taken together, these indicate that there are issues around year-end processes and controls over capital that still need to be addressed. **Recommendation 5**
12. Investment Property **(MA 75080 and 75081)** The Fixed Asset Register did not reconcile to Note 8 - Investment Property disclosures: Opening balances and closing balances did not agree across years 2020/21, 2021/22, and 2022/23 Two Investment Property assets (100 Borron Street and Units 1A-3D Payne Street) had been incorrectly classified as Real Estate – Operational assets. The assets were acquired by Scottish Canals as part of an asset swap in 2021/22. This transaction was incorrectly recorded in the FAR with the assets recorded as a revaluation movement instead of an addition. The Fixed Asset Register included depreciation for some Investment Property assets. This is inconsistent with Scottish Canals accounting policy as Investment Property assets are held at Fair Value using the Market Value approach and therefore not depreciated.	Scottish Canals amended the audited accounts and Fixed Asset Register to correct these issues with investment properties.
13. Incorrect depreciation accounting and formula **(MA 75079)** The unaudited accounts included an error in the depreciation charge of £2.7 million. 2021/22	Scottish Canals amended the FAR and audited accounts to correct the depreciation errors. Scottish Canals engaged with experienced and qualified engineers to revise the Useful Economic Lives of the assets impacted. We reviewed the

Issue	Resolution
depreciation was incorrectly posted directly to the General Fund rather than through the SoCNE. **(MA 77000)** In the 2021/22 FAR, we noted there were 641 assets with positive NBVs (£37.8 million) and no depreciation charge. In 2022/23 there were 591 assets with positive NBVs (£30.2 million) and no depreciation charge. This omission in the depreciation charge was due to an error in the formula used in the FAR to calculate depreciation in instances where the age of the asset exceeds the Usable Expected Life.	methodology applied for this exercise and concluded it was reasonable. This resulted in a £2.5m increase in the depreciation charge in 2022/23. **Recommendation 2**
14. Dredging **(MA 76783)** We reviewed the treatment of capitalised dredging costs in the unaudited financial statements, which were being disclosed as an intangible asset. We found that the dredging costs could be deemed to be improving the underlying tangible asset (the canal network) and the dredging asset may not be seen as separable to be sold and transferred in its own right as it is an integral part of the underlying tangible asset and concluded that the asset should be disclosed as an enhancement to the underlying asset in accordance with IAS16. **(MA 76970)** Negative depreciation of £304,000 was identified as being credited to the unaudited financial statements on the costs of dredging (asset SC-102719). This was an error due to the asset being treated as an asset under construction in 2021/22.	Scottish Canals amended the Fixed Asset Register and audited accounts to correct these issues with classification and depreciation
15. Scottish Canals Group and preparation of Group Accounts **(MA 76463)** Our review found that Millennium Link Trust (MLT), was effectively controlled by Scottish Canals and should have been treated as a subsidiary prior to 2021/22. MLT is an organisation where two of the four trustees were Scottish Canals directors. Scottish Canals provided management support to MLT in previous financial years and letters of comfort in	Scottish Canals amended the audited accounts to correct these issues with disclosure of the land transactions with BIGG Regeneration Ltd Partnership. Our review identified that group transactions and balances were not material in either 2021/22 or 2022/23 to require group accounts to be prepared, but we believe that the historic issues with MLT and the recent changes in Bigg Regeneration Ltd Partnership

Issue	Resolution
2022. MLT's assets should have been recognised in Scottish Canals since the termination of an existing lease arrangement in 2015, however this only took place on the valuation of the canal infrastructure. The overall control was with Scottish Canals and the four trustees of MLT agreed to dissolve the charity as it no longer served its original purpose. Scottish Canals has historically adopted an accounting judgement that group accounts are not required on the basis of materiality. The assets and transactions of MLT were material, up to the transfer of canal infrastructure to Scottish Canals in 2020/21. Since then, the transactions have not been material. Our conclusion is that Scottish Canals should have been preparing group accounts prior to 2021/22. **(MA 76809)** We are also aware of changes in one of the joint venture bodies. In 2021/22, the Partnership (BIGG Regeneration Ltd Partnership) transferred its investments in Borron Street and Payne Street to Scottish Canals (£7.4 million) and received three development plots at Dundashill (Value £3.854m), with a balancing payment from canals of £3.546m. A review of BIGG regeneration Ltd Partnership accounts provide evidence of this transaction. Scottish Canals unaudited accounts did not fully disclose this transaction. The two partners used this transaction to vary the financing arrangements of the company. (Deed of Variation) with one partner PFPC taking £2.3 million of their investment out and Scottish Canals increasing their investment by way of a partner loan to the amount equivalent to the amount taken out by PFPC (£2.3 million loan).	should result in Scottish Canals reviewing its Group structure and re-examining the judgement that group accounts are not required on materiality grounds and that this needs to be reassessed each year as part of the final accounts process. Any increase in value in Bigg Regeneration Ltd Partnership may result in a change to this materiality assessment. **Recommendation 2**
16. Future revaluation exercises required by the FReM **(MA 77264)** The Financial Reporting Manual (FreM) (Para 10.1.2) requires that "entities should value their PPE using the most appropriate valuation process. Such processes might include:	Scottish Canals have undertaken a full valuation in 2021/22 but will need to consider how they will programme future valuation exercise to ensure compliance with FReM requirements. **Recommendation 7**

Issue	Resolution
• a quinquennial valuation supplemented by either annual indexation or regular desktop valuation update • a quinquennial valuation supplemented by an interim professional valuation in year 3 • annual valuations • a rolling programme of valuations • for non-property assets only, appropriate indices" The current valuation process was undertaken at 31 March 2022, with the application of indexation adjustments to arrive at PPE valuations on 31 March 2023.	
17. Disclosure improvements The audit identified many disclosure issues including: • clarification of key judgements and estimates • disclosure of land swap arrangement in 2020/21 • justification for not preparing group accounts • clarification on the internal control arrangements • disclosure of contingent liabilities • disclosure around leases • disclosure on pension reserve • clarification on the historic records held by Scottish Canals	Scottish Canals amended the audited accounts to correct the majority of disclosure issues, but we believe that future incremental improvements are still required in some areas including sensitivity analysis of key estimate assumptions. **Recommendation 8**

Our audit work responded to the risks of material misstatement we identified in the annual report and accounts

23. We have obtained audit assurances over the identified significant risks of material misstatement in the annual report and accounts. Exhibit 4 sets out the significant risks of material misstatement to the financial statements we identified in our 2022/23 Annual Audit Plan. It also summarises the further audit procedures we performed during the year to obtain assurances over these risks and the conclusions from the work completed.

Exhibit 4
Significant risks of material misstatement in the annual report and accounts

Audit risk	Audit response	Results and conclusions
1. Risk of material misstatement due to fraud caused by management override of controls As stated in International Standard on Auditing (UK) 240, management is in a unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively.	Assess the design and implementation of controls over journal entry processing. Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual journal entries and other adjustments. Test journals at the year-end focussing on significant risk areas. Consider the need to test journal entries and other adjustments during the period. Evaluate any significant transactions outside the normal course of business. Assess the adequacy of controls in place for identifying and disclosing related party relationships and transactions in the financial statements. Assess any changes to the methods and underlying assumptions used to prepare accounting estimates compared to the prior year. Substantively test income and expenditure transactions around the year-end to confirm they are accounted for in the correct financial year	We assessed journal controls and assessed that this provides us with reasonable assurance that journals are controlled and limited to senior finance officers. Finance staff were not aware of any unusual activity relating to the processing of journals or other adjustments. We undertook detailed substantive testing of a sample of journals with no issues identified. We reviewed payroll journals throughout the year, reconciled these to the payroll system and completed an overall review of monthly values. We reviewed unusual transactions connected with the transfer of MLT; land swap arrangements with Bigg Regeneration Partnership; NCA revaluations and VAT settlement. We reviewed the approach for identifying and recognising related parties and for identifying registers of interest and found these insufficient We assessed changes in the methods of assessing accounting estimates including non-current assets (NCA) valuation, pensions, deferred capital grants and corporation tax. We also reviewed accounting estimates and transactions for appropriateness. We tested a sample of income and expenditure items to confirm that they had been accounted for in the correct financial year.

Audit risk	Audit response	Results and conclusions
		Conclusion: We found a number of issues with key estimates and processes such as related parties, NCA valuation, pensions deferred grants and corporation tax, however we did not identify any incidents of management override of controls.
2. Risk of fraud over income recognition As set out in International Standard on Auditing (UK) 240, there is a presumed risk of fraud over the recognition of revenue. Scottish Canals generate income from retail and other sources totalling £8 million.	Perform a walkthrough of the controls in place around point-of-sale income. Review the accounting policies around revenue recognition. Test income transactions at the year end with a focus on material income streams. Review the judgements and estimates made by management when recognising accrued and deferred income at the year end.	Total retail sales were £3.4 million. This increased from the prior year which reflected the lifting of covid-19 restrictions. We did not undertake a review of controls as our effective audit engagement began in July 2023 - after the financial period, but we did note the control arrangements in place. We undertook significant sample testing of income and cut off. We confirmed that grant-in-aid is accounted for on a cash basis. We tested grant income and deferred capital grants and found issues with the amortisation of capital grants. Testing of bank statements and reconciliations did not identify any issues. **Conclusion: We found issues with the accounting treatment of deferred capital grants, which were corrected. We did not identify any issues with the recognition of income in other areas.**
3. Insufficient audit evidence and quality of working papers The previous auditor identified extensive	Early engagements with officers on the PPE supporting documentation to allow us to establish if it is sufficient.	We were unable to undertake early engagement on PPE valuation processes as the data from EY model was not available until early November 2023.

Audit risk	Audit response	Results and conclusions
issues with the quality, completeness, and accuracy of working papers. "Overall, the quality of the working papers provided alongside suitable audit evidence to support balances in the financial statements was not of the standard we would expect. This led to significant additional time being required for audit, where audit evidence submitted…was sent back as insufficient and/ or incomplete." The previous auditor recommended that "management work with the new auditors closely over the requirements of the audit and are more readily able to support the audit process through good quality, self-reviewed, complete and accurate working papers. This extends beyond PPE, to other material areas of the accounts." There is a risk that existing records do not adequately support the audit of the 2022/23 transactions and balances at 31 March 2023, leading to a further disclaimer opinion.	Establish that financial statements submitted for audit are substantially complete. Confirm that financial statements are supported by a valid trial balance that reconciles to the ledger. Confirm that a fixed asset register exists that agrees to the trial balance. Confirm that reconciliations are all complete including the bank reconciliation and any feeder system control accounts. Review the working papers in each audit area to ensure they are complete and sufficient to commence the audit	Apart from updated investment information and corporation tax calculations, we were content that the accounts submitted on 3 November were substantially complete. A trial balance was provided which reconciled back to the accounts, with a few minor issues noted. A complete Fixed Asset Register was provided for audit alongside the EY valuation model, however the FAR could not be reconciled to Note 8 - Investment Property. Our review confirmed the bank statement reconciliation. Reconciliations were reviewed to confirm they match accounts and that any significant reconciling differences are investigated and explained. Only minor issues have been identified with the quality of initial information provided. **Conclusion: The quality of working papers were adequate to support the 2022/23 audit of the transactions and balances.**
4. Existence, accuracy completeness and	Complete a walk-through of the valuation model (E&Y).	The lack of an established routine process for the Fixed Asset Register meant that we could not

Audit risk	Audit response	Results and conclusions
operation of Fixed Asset Register (FAR) The previous auditors noted several issues in their 2021/22 annual audit report relating to the existence, accuracy, completeness and operation of the fixed asset register (FAR) during the 2021/22 audit: • A complete, up-to-date FAR was not available at the time of audit • There were significant delays in provision of supporting working papers for property, plant and equipment assets subject to audit testing. • Manual depreciation calculations were undertaken in the absence of system generated information. • An inadequate control environment existed around the FAR and underlying asset records. The auditors identified a number of areas requiring management consideration, including: • The need for accurate and timely recording of source data in AMX (the project management system) and subsequent reflection of asset additions and	Establish and confirm the operation of key controls over the FAR to ensure controls exists over recognition, addition and enhancements, disposals, derecognition and reconciliation to the AMX/ capital project information. Review and confirm a sample of significant assumptions/ evidence to source including AMX data. Asses the adequacy of key assumptions including cost or rebuild estimates (The assumptions over residual lives and index movements are covered in separate risks below). Establish that an operational, complete and accurate FAR exists and reconciles to the E&Y model. Test a significant sample of closing values at 31 March 2023 to the evidence. Test a reduced sample of closing values at 31 March 2022 and 31 March 2022 to the evidence Confirm or test 2022/23 transactions to supporting evidence. Including additions, depreciation, disposals and transfers, where material. Confirm or test 2021/22 transactions to supporting evidence. Including additions, depreciation, disposals and transfers, where material. Undertake sample testing of existence of assets. Review a sample of physical assets and wider records to ensure the asset register is complete.	establish and test key controls early. We undertook extensive substantive testing. We reviewed the valuation treatment for assets across the different treatment categories. We identified 132 assets that had not been revalued using a DRC methodology. We also identified issues with the existence and completeness of a small number of assets, which were of potentially significant value. The source of cost data for each asset and the methodology applied were assessed for reasonableness. Where necessary, further information was sought from EY to understand the assumptions applied in the valuations. A full revaluation of canal infrastructure assets and investment property has been undertaken in 2021/22 and we also assessed the indexation applied to 'roll forward' to 2022/23 and 'roll back' to arrive at opening balance for 2021/22. The methodology has been assessed as reasonable and uses indices from BCIS General Civil Engineering Cost Index (GCECI). We identified some land swap assets: 100 Borron Street and Units 1A-3D Payne Street that were incorrectly classified as 'Real Estate - Operational' rather than Investment Property and recorded as revaluations rather than additions in 2021/22. Revaluations agreed back to EY valuation model or GE/CBRE reports.

Audit risk	Audit response	Results and conclusions
modifications in the FAR • An appropriate interface between AMX and FAR to correctly componentise spend. • A clear process to maintain a complete and accurate FAR including recognition and accounting for assets under construction, additions and disposals. The need for additional, specific finance resource to support the process. There is a risk that the accounts are misstated. This risk extends to the previous two financial years where the auditor opinion was disclaimed due to lack of robust reliable evidence.		The depreciation calculation was reperformed. We identified 591 assets in 2022/23 with no depreciation charge due to formulas not charging depreciation in instances where the age of the asset exceeds the UEL. The accounting policy for operational land has been reviewed including land valuation assumptions and measurements. Disposals were not material, but one of the disposals we tested was incorrectly recorded as a disposal. We identified one bridge asset (Bowling 50) and a number of access road and car park assets that had been omitted from the revaluation exercise. We also identified a bridge asset where Scottish Canals had identified that they did not own, that still appeared on the asset register (Duntreath Avenue Bridge). 55 assets had incorrect data used by AMX which detailed the wrong capitalisation date. This meant that opening asset values at 1 April 2021, and subsequent revaluation adjustments were materially mis-stated. **Conclusion: The valuation methodology is considered reasonable. There were significant issues with ownership and completeness of the asset base and completeness of the valuation exercise, which were identified during the audit and reported. These issues were fully resolved by Scottish Canals.**

Audit risk	Audit response	Results and conclusions
		There were also issues with the Fixed Asset Register calculation of depreciation, revaluation and opening values which were resolved by Scottish Canals. **More minor issues with additions/ assets under construction and disposals indicated that capital accounting processes and controls are not yet fully established.**
5. Scope and basis for the valuation experts The previous auditor determined that "the 'Valuer' must prepare a written 'Terms of Engagement' document. This is a mandatory requirement of the RICS Valuation – Global Standards 2022. Scottish Canals should ensure these are obtained from the valuers on an annual basis. Additionally, Scottish Canals should ensure that formal 'Letter of Instructions' are agreed upon and signed by the relevant individual on an annual basis as these outline the base requirements and form a vital and mandatory part of the valuation process. " We expect that the engagement and scope of valuation exercises will be clearly identified in documentation.	Review information provided by management to E&Y and Gerald Eve to assess completeness of valuation process. Establish the scope and basis of E&Y and Gerald Eve contract and any valuation process. Review the handover procedures between E&Y and Scottish Canals for the asset valuation model. Consider the appointment and scope of any valuer providing current value valuation advice	The source data is described in EY methodology and appeared to be comprehensive including data from multiple sources. Our testing did identify the omission of Bowling Bridge 50 from the EY valuation. We reviewed the 'Book Asset Value (BAV)' listing that was provided to Gerald Eve and omissions were identified in this list provided for valuation. The EY model has not been fully handed over to Scottish Canals. We understand this will happen once Scottish Canals reach a stable position, and the audit opinion is clean. The valuations were completed by RICS members, and the valuations are prepared in line with RICS guidance. No reputational issues have been identified.

Audit risk	Audit response	Results and conclusions
There is a risk that the terms of engagement are outdated.		
6. Value of assets not subject to full in year valuation The Government Financial Reporting Manual (FReM) requires "the most appropriate methodology for obtaining either a current value in existing use or a fair value" and describes a number of methods for keeping valuations updated at the balance sheet date. The previous auditors noted "*Canals will need to consider whether indices will be used, and the most appropriate indices, in between intervening valuation years, and whether to value all assets once in a five-year period or a rolling valuation programme.*" There is a risk that assets not fully revalued in year are not held at an appropriate value.	Establish and review methodology used by management to provide year end current cost reassessments for assets not subject to full revaluation in year. Walkthrough the process and understand the systems for in-year current cost review. Confirm the process is completed by a valuation expert. Assess the use and uprating of key assumptions in the valuation methodology. Review and assess the dredging capitalisation policy and application. Review valuation of Bowling viaduct access.	A full revaluation of canal infrastructure assets and investment property has been undertaken in 2021/22 and we also assessed the indexation applied to 'roll forward' to 2022/23 and 'roll back' to arrive at opening balance for 2021/22. The methodology has been assessed as reasonable and uses indices from BCIS General Civil Engineering Cost Index (GCECI). The dredging costs had been incorrectly classified as intangible assets rather as an improvement in the underlying tangible asset (the canal network) Bridge 50, Bowling Railway Bridge had been omitted from the valuation model and the access road had not been valued either due to an omission from Gerald Eve's instruction. **Conclusion: We found indexation had been applied to assets, based on BCIS movements.** **Dredging costs were reclassified in the audited accounts.** **Assets at the Bowline project (including Bridge 50, Bowling Railway Bridge) had not been appropriately valued and Scottish Canals decided not to adjust for this in the audited accounts**.
7. Estimated residual lives Scottish Canals' asset portfolio includes a	Review and assess the basis for residual life estimates of assets.	Scottish Canals has adopted useful lives that are an estimate of the period over which an asset

Audit risk	Audit response	Results and conclusions
significant number of assets that are over 200 years old. The previous auditors, Grant Thornton, noted "*we were unable to obtain sufficient assurance over the assumptions relating to residual values for assets where the valuation reflected a residual value equating to 12 years remaining. This assumption is highly sensitive".* There is a risk that the carrying value of assets is materially misstated due to insufficient evidence to support assumptions around residual lives and movement during the year.		is expected to be available for use by Scottish Canals. We confirmed that management has reviewed the Useful Expected Lives (UELSs) and have arrived at a reasonable range through benchmarking with other public bodies and consultation with experienced personnel who have knowledge of the assets. The useful lives have been reviewed and amended as at 31 March 2023, and prior year adjustments have been made to the valuations as at 31 March 2022 and 1 April 2021. However, it is noted that the impact of this change had not been disclosed explicitly. The impact on the depreciation charge for the year had not been noted. **Conclusion: We found that the revised estimated residual were reasonable. However additional disclosures of the impact were required. These enhanced disclosures were not fully resolved by Scottish Canals.**
8. VAT liability Scottish Canals are concluding negotiations with HMRC on a VAT liability. The 2021/22 accounts include a liability of £15.5m at 31 March 2022. Additional funding has been provided by Scottish Government to assist in the settlement, however going forward	Review correspondence between HMRC and Scottish Canals for the VAT liability Assess the completeness and accuracy of the provision/creditor balances as at 31 March 2023. Review the impact of changes in VAT accounting on future financial projections and planning.	We reviewed workings and evidence back to HMRC agreements for amounts due and confirmed. Evidence was checked of any amounts paid. Creditor balance due at year end is based on KPMG calculation which has been agreed with HMRC. There is no provision as its unknown if outstanding fines will be applied, but there was no

Audit risk	Audit response	Results and conclusions
any VAT liability will be funded from the core budget. There are significant cash and provision/creditor balances that will require to be included on the closing balance sheet at 31/3/2023. There is a risk that these balances do not reflect the most up-to-date settlement position. Depending on the outcome and value of settlement with HMRC, there may be implications on future savings plans, or a requirement to return funding to Scottish Government.		disclosure of this within contingent liability. New VAT calculation method from KPMG has been agreed with HMRC which will allow planning for future costs. **Recommendation 2** **Conclusion: Scottish Canals had not recognised a contingent liability for a possible penalty due to the conditions not being met pending methodology agreement, but this was revised in the audited accounts.**
9. Deferred capital grants The 2021/22 accounts include £25 million of deferred capital grants. The Financial Reporting Manual (FReM) interprets the accounting standards for grants in such a way that so that only grants from government which have conditions which have not been met at 31 March can be deferred. There is a risk that the value of deferred capital grants is misstated due to incorrect accounting treatment of grants received.	Review the accounting policy in relation to deferring capital grants. Sample testing of deferred capital grants to supporting documentation and conditions to ensure there are significant conditions that have not been met.	We reviewed the agreements for a sample of deferred capital grants and noted Scottish Canals were amortising this income over the life of the asset. This treatment was incorrect and did not accord with the requirements of FreM. Refer to issue 1 in Exhibit 3 **Conclusion: The accounting treatment of deferred capital grants was incorrect. These issues were fully resolved by Scottish Canals in the audited accounts**

Audit risk	Audit response	Results and conclusions
10. IFRS 16 leases Accounting standard IFRS 16 replaces IAS 17 and is mandatory for central government bodies in 2022/23. This requires lessees to recognise assets and liabilities for the rights and obligations arising from leases previously classified as operating leases. The 2021/22 accounts state that the standard is expected to result in the recognition of additional right-of-use assets and an associated lease liability. This has not yet been reviewed by Scottish Canals and there is a risk that the accounting treatment is not correct for leases.	Review the treatment of leases to ensure they are in line with IFRS 16 requirements. Test a sample of lease assets to contract, payment and other evidence.	We reviewed the implementation of IFRS 16 and noted that a few minor amendments were required to disclosures. **Conclusion: The accounting treatment for IFRS 16 leases has been corrected within the audited accounts.**
11. Key estimations and judgements Grant Thornton reported that "*The annual report and accounts include an accounting policy on management judgements and critical estimates. The current disclosures could be further improved, to demonstrate full compliance with the FReM. For example: not all that is currently included meets the definition of a*	Critically assess which are the key judgements and estimates that require disclosure in the accounting policies. Review disclosures to ensure that they are complete. Assess the narrative and any information required to determine the importance or sensitivity of these estimates.	We reviewed the disclosures of key estimates in the accounting policies and found that these could be improved. **Conclusion: Disclosures of key estimates and judgements were revised within the audited accounts.**

Audit risk	Audit response	Results and conclusions
judgement or critical estimate". Scottish Canals do not currently produce group accounts on the grounds of materiality. Evidence is needed to support this and an assessment of the impact of consolidating their various group bodies, and this should be classified as a key judgement and included within the note. There is a risk that narrative on significant judgements and estimates within the financial statements is insufficient.		
Other non-significant risk of material misstatement		
12. Related party disclosures Grant Thornton noted "*As part of our audit work, we completed a review over the completeness of the register of interest forms completed by members. From this review, we identified certain related parties which had not been disclosed within the signed forms, which are completed and updated on an annual basis*". There is a risk that related party forms are not correctly completed, and the disclosure within the annual report	Review the process for identification of related parties throughout the year and at the year end. Determine whether registers of interest are up to date and complete/accurate and related party disclosures are in line with guidance. Review the related party disclosures within the annual report and accounts.	**Conclusion: We found an inconsistent approach across organisation for identifying and recognising related parties and register of interests** **Recommendation 9**

Audit risk	Audit response	Results and conclusions
and accounts is therefore incomplete.		

Significant misstatements were adjusted within the audited accounts, with one unadjusted issue relating to the Bowline project valuation.

24. There were significant misstatements, which were adjusted in the audited accounts, which total £11.2 million. The total net assets of Scottish Canals increased by £3.9 million from the unaudited accounts. This included a £7.9 million increase in property valuations and a £2.2 million increase in investment valuations, offset by re-categorisations and changes in other areas.

25. There were also significant adjustments between reserves with the revaluation reserve increasing by £193 million.

26. The disclaimer audit opinion on the 2021/22 accounts also led to Scottish Canals revising the comparative amounts in the 2022/23 accounts, as well as there being further changes to comparatives as a result of this year's audit. The total assets were amended by £48.4 million and net assets by £43.6 million. This includes changes to property valuations of £34 million and an increase of £14,4 million to investment property.

27. Net operating expenditure also increased by £2 million in audited 2022/23 accounts and reduced by £4.5 million in the prior year: mostly as a result of depreciation errors, investment gains and recognition of income from capital grants.

28. We identified one misstatement which was not corrected by management in the audited accounts. The error exceeded our performance materiality but not our overall materiality. The unadjusted error related to the valuation of the Bowline project and the impact of an adjustment would decrease in the value of non-current assets by £5.6m. Scottish Canals decided not to adjust this item on the grounds of materiality. We considered the size, nature and circumstances leading to this uncorrected misstatement and concluded that this was an isolated issue that did not represent an additional risk of material misstatement.

Reasonable progress has been made on prior year recommendations.

29. Scottish Canals has made reasonable progress in implementing the audit recommendations identified by Grant Thornton, Scottish Canals previous external auditor. 12 of 21 (57 per cent) recommendations have been completed, with a further five recommendations have been superseded by our recommendations for the year. The final 4 (19 per cent) recommendations are on-going, however there has been no update to the timescale for implementation with the dates remaining as agreed with Grant Thornton. For these actions not yet implemented, revised responses and timescales have been agreed with management, and are set out as brought-forward (b/f) recommendations in Appendix 1.

2. Financial management and sustainability

Financial management means having sound budgetary processes, and the ability to understand the financial environment and whether internal controls are operating effectively. Financial Sustainability means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs.

Conclusion

Scottish Canals had appropriate budget processes during 2022/23

Scottish Canals exceeded its budget in 2022/23, however Transport Scotland have confirmed this overspend will be managed within its budget.

There were weaknesses in financial system control arrangements.

Scottish Canals does not have a medium-term financial outlook/ strategy.

Scottish Canals exceeded its budget in 2022/23

30. The main financial objective for Scottish Canals is to ensure that the financial outturn for the year is within the budget allocated by Scottish Ministers.

31. The body has reported an outturn of £37.651 million against its overall budget for 2022/23 with an underspend/overspend of £0.282 million. The financial performance against fiscal resources is shown in Exhibit 5. Transport Scotland has confirmed that the overspend will be managed within its budget.

Exhibit 5
Performance against fiscal resource in 2022/23

Performance	Budget £m	Outturn £m	Over/(under) spend £m

Revenue	11.119	11.370	0.251
Capital	9.950	9.981	0.31
VAT funding	16.582	16.582	-
Total	**37.651**	**37.933**	**0.282**

Source: Scottish Canals Annual report & Accounts 2022/23

Scottish Canals had appropriate budget processes during 2022/23

32. Scottish Canals produces regular budget monitoring to the Board on a quarterly basis showing the position for the year-to-date, and the projected year-end outturn. These reports were considered by the Executive Management Team during 2022/23 to enable them to respond to any emerging issues and take corrective action. In addition to this, financial governance reports are taken to the Audit and Risk Committee which updates on financial issues, revenue forecasting and issues identified by audit.

There were weaknesses in the financial system controls

33. Our review of the design and implementation of systems of internal control (including those relating to IT) identified a number of internal control weaknesses which were due toa higher than normal turnover of finance staff. Below details the control weaknesses:

- user access controls around the general ledger had not been implemented during 2022/23, therefore we were unable to test the operation of this control. We completed additional procedures as part of our substantive testing and found no substantive issues.
- the leavers process for systems access was not completed in a timely manner and we completed substantive testing during the financial statements audit. No issues were noted.

34. Scottish Canals internal audit function is carried out by Audit Glasgow. Their Annual Audit Report was presented to the September 2023 Audit and Risk Committee.

35. The overall opinion was that limited assurance can be placed upon the adequacy and effectiveness of the governance and control environment which operated during 2022/23 in Scottish Canals. This opinion was based on audit reports during the year, which contained one unsatisfactory opinion and three limited assurance opinions. There were also 29 improvement recommendations, including 14 high priority ones contained in these reports,

36. We did not place reliance on the controls in operation in 2022/23 and we increased our substantive sample sizes as a result.

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

37. Scottish Canals has adequate arrangements in place to prevent and detect fraud or other irregularities.

Scottish Canals does not have a medium-term financial outlook/ strategy

38. Scottish Canals does not have a medium-term financial strategy (MTFS) or outlook in place as at November 2023. Due to the staffing changing within the Scottish Canals finance team, there has not been the time or resource to prepare an overarching strategy.

39. The investment strategy is being reviewed by Transport Scotland, along with the grant-in-aid funded capital investment plan, and medium-term projections have been prepared. These will need further review and included within the MTFS.

Recommendation 3

Scottish Canals should review and revise future financial forecasts and issue a 3-year medium term financial plan.

Appendix 1. Action plan 2022/23

2022/23 recommendations

Issue/risk	Recommendation	Agreed management action/timing
1. Review of valuation status of assets We found some assets that hadn't been subject to revaluation review process, and these were obtained late in the audit process but not adjusted in the accounts Risk – valuations are not fully reflected in the accounts	Scottish Canals undertake a review of all DRC assets to check that that a valuation report has been obtained and is reflected in the Asset Register Exhibit 3	Agreed A review of all the valuations will be conducted for the 31 March 2024 year-end to ensure assets requiring revaluation have been incorporated in the valuation. 31 July 2024 (Director of Finance & Business Services)
2. Asset register formula checking We found errors in the Fixed Asset Register formulae. Risk Amounts used in the Accounts are incorrect due to errors in FAR formulae	Management should review the formulae in the FAR as part of the FAR closedown procedures. Exhibit 3	Agreed Although a review of the 31 March 2023 Fixed Asset Register (FAR) was undertaken, this formulae error was not identified prior to audit. Time for both peer review and manager review of the completed FAR will be incorporated within the year-end timetable. 31 July 2024 (Director of Finance & Business Services)
3. Medium term financial strategy/ outlook projections and Corporation Tax /VAT	Scottish Canals should review and revise future financial forecasts and issue a 3-year medium term financial plan.	Agreed a. Adjustments to the final proposition for calculating VAT are being collated, with an expected final position

Issue/risk	Recommendation	Agreed management action/timing
Scottish Canals does not have a medium-term financial strategy (MTFS) in place as at November 2023. Recent changes to the calculation of tax may not be fully reflected in future financial plans. Risk – That future financial position is unsustainable	Exhibit 3 Paragraph 38-39 Exhibit 3	expected in April 2024. b. The methodology for the organisation's corporation tax since becoming a non-departmental public body will also be reviewed. Discussions with HMRC have not begun pending the VAT work, however HMRC have been informed of the intention to reach a written agreement on the treatment of grant-in-aid and associated expenditure. (June 2024) c. Draft medium term projections were shared with Transport Scotland in July 2023,with an investment strategy shared in February 2024. Once the VAT position has been finalised, a full projection on investments has been conducted, a more robust medium-term financial strategy will be completed. 31 July 2024 (Director of Finance & Business Services)
4. Late capital grants As significant amount of capital grants were not identified till after the accounts were submitted for audit. Risk – capital grant funding is not recognised in the accounts	Accounts closedown procedures should include a process to identify capital grants to ensure these are complete Exhibit 3	Agreed As part of the internal audit on project management, procedures on Stagegate completion of projects (SG5) are being reviewed and improved within the Project Assurance Committee. Part of this review includes a financial review of any third-party funding agreements going forward. An additional review will be timetabled as part of the year-end procedures prior to the first draft of the 31March 2024 accounts being collated

Issue/risk	Recommendation	Agreed management action/timing
		31July 2024 (Director of Finance & Business Services)
5. Procedures and controls over asset movements and completion/ disposal Some assets were incorrectly recorded as Assets under construction when they had been completed and the unaudited accounts included an asset disposal in error. Risk – Movements in assets are not correctly recorded.	Scottish Canals should establish processes and controls to ensure asset additions, disposals and transfers are correctly recorded and communicated to Finance Exhibit 3	Agreed. As detailed above, the Stagegate reports on project completion (SG5) are being improved. These were not all completed timeously for the 31 March 2023 financial year. These will form part of the Project Assurance Committee timeline during April and May going forward. 15 June 2024 (Director of Finance & Business Services)
6. Review of the group and group accounts Millennium Link Trust **(**MLT) was effectively a subsidiary body prior to 2021/22 and had material assets, which should have led to Scottish Canals preparing group accounts. The status of ownership of Bigg Regeneration Ltd Partnership changed possibly, due to the consequences of the land swap deal. Any growth in value of the joint ventures could mean that these become material group bodies Risk – that Scottish Canals wrongly continues to rely on the immateriality of its group and continues not to prepare group accounts.	Scottish Canals should review the status of each of its group entities for accounts purposes, with legal advice if necessary. The accounts closedown process should include an explicit review of the materiality of group entities. Exhibit 3	This has been reviewed each year with previous auditors, Scottish Government and Azets during the 31 March 2023 financial year who all concurred no consolidation was necessary. However, this will continue to be reviewed annually on the basis of any material increase in the value in Bigg Regeneration as advised above. A special resolution to wind up MLT was lodged with Companies house in November 2023, and Johnston Carmichael are managing that voluntary liquidation process. Edinburgh Quay Limited and Edinburgh Quay (Three) Limited were both dissolved on 2 January 2024. The only remaining related organisations are:

Issue/risk	Recommendation	Agreed management action/timing
		• BwB (General Partner) Limited • Bigg Regeneration (General Partner)Limited • Bigg Regeneration Limited Partnership 30 April 2024 (Director of Finance & Business Services)
7.Approach to future revaluations The current valuation of assets was undertaken at 31 March 2022. Revaluations must be redone within five years in accordance with the FreM. Risk - Valuations become out of date and accounting policies are not FreM compliant.	Scottish Canals should outline plans for the future revaluation of its assets within the FreM framework. Exhibit 3	Agreed A handover piece of work from EY is due in March 2024, with an initial proposal to use indices to update the valuation for the 31 March 2024 year-end. 31 March 2024 (Director of Finance & Business Services) A full proposition for the year-ended 31 March 2025, 31 March 2026 and 31 March 2027 will be collated and provided to Audit Scotland during the 2023/24 audit.
8. Review of disclosures Significant improvements were made in the accounting disclosures in 2022/23, but there is further scope to review these and make further improvements. For example in describing the sensitivity of key assumptions in estimates Risk: important disclosures that assist in the	Scottish Canals should further review their disclosures as part of preparing 2023/24 financial statements Exhibit 3	Agreed A technical review of disclosure requirements will be conducted as part of the timetable for the 31 March 2024 year-end. 31 July 2024 (Director of Finance & Business Services)

Issue/risk	Recommendation	Agreed management action/timing
understanding of the accounts might be omitted		
9. Related party interests and register of interests We found an inconsistent approach for identifying and recognising other related parties, which did not consider recording or reporting any related party responsibilities undertaken by Heads of departments.	Scottish Canals should review its process for recording and related parties Exhibit 4	Agreed A review of our Senior Management Team will now be incorporated as part of the annual review. 31 July 2024 (Director of People, Safety & Governance)
b/f 1. Disaster Recovery Plan	Scottish Canals should establish a formal Disaster recovery plan.	Agreed This is being monitored as part of our key requirements in internal audit. A working group will be established to work through this during quarter one. 31 July 2024(Director of Finance & Business Services)
b/f 2. Dundashill	Scottish Canals still own certain Dundashill plots, which are currently valued as an investment property. It is recommended that the Board review this strategy.	Agreed The Board has been updated since the 2021/22 financial year on the progress and updated strategy at Dundashill as part of the overriding Investment Strategy. This will continue to be reported to Board, however there has been no change in strategy recently whilst the existing plots are being developed out through the BIGG joint venture. 30 September 2024 (Chief Operating Officer)
b/f 3. Workforce planning	Scottish Canals should develop a workforce plan.	Agreed

Issue/risk	Recommendation	Agreed management action/timing
		Recent years have focussed around workstreams within the job evaluation project. Establishing a workforce plan is key to the medium-term financial strategy going forward. Re-setting the establishment , a review of working hours and rotas, defining business and customer needs, and embedding succession planning throughout the organisation, consolidating into a new People Strategy will be targeted during the calendar year. 31 December 2024 (Director of People, Safety & Governance)
b/f 4. VAT position	If the VAT settlement is less than forecasted, Scottish Canals need to agree how the funding, not used, will be transferred back to Scottish Government.	Agreed It is anticipated that the VAT settlement will be finalised over the next two months. Transport Scotland has intimated that any overpayment should be repaid as part of a capital grant-in-aid return back to Transport Scotland for distribution. Based on the latest revised estimations, the likelihood of there being a large repayment is low. 31 May 2024 (Director of Finance & Business Services)

Scottish Canals
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Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk

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