



National Audit Office



European Agricultural Funds Accounts 2016

**(The Scottish Government Rural
Payments and Inspection Division)**

**Report by the United Kingdom's
Certification Body**

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SECTION A - EAGF

1. Executive Summary

1.1. Introduction

- 1.1.1. Following our appointment as auditors by the UK Co-ordinating Body acting on behalf of the UK Competent Authority, Audit Scotland has performed an audit of the Scottish Government Rural Payments and Inspection Division pursuant to Article 9 (2) of Regulation (EU) No. 1306/2013 of the European Parliament and of the Council in relation to its role as paying agency. This audit related to the paying agency's operation of the European Agricultural Guarantee Fund (EAGF) for the financial year ended 15 October 2016. The audit was undertaken in accordance with internationally accepted auditing standards and entailed consideration of the matters, set out in Article 5 (4) of Commission Implementing Regulation (EU) No. 908/2014.
- 1.1.2. We are also required to provide an opinion as to whether the annual accounts for the EAGF year ended 15 October 2016 are a true, complete and accurate record of the amounts charged to the Fund, that the expenditure declared to the Fund is legal and regular and that the internal control procedures have operated satisfactorily. This opinion is contained in the Audit Opinion presented as section C of this report. We are further required to indicate whether our examination puts in doubts any assertions made in the Management Declaration. A separate section of the opinion deals with the Management Declaration.
- 1.1.3. Our work was performed in accordance with the requirements of Article 9 of Regulation (EU) No. 1306/2013 and Articles 5 to 7 of Commission Implementing Regulation (EU) No. 908/2014. The format of this report is in accordance with the Commission Guidelines.
- 1.1.4. Our work covered the paying agency's compliance with the accreditation criteria, the existence and functioning of the key internal controls and the procedures for ensuring compliance with EU rules, the legality and regularity of expenditure claimed for reimbursement from the Commission and the procedures for the protection of the financial interests of the EU. The findings and recommendations arising from our work are summarised in this Chapter and detailed under the relevant Chapters.
- 1.1.5. This report results primarily from the body of work undertaken by us since our appointment as a Certification Body to the paying agency in relation to the financial year ended 15 October 2016. Annex 1 to this Report contains a Glossary of Abbreviations used.

1.2. Conclusions

- 1.2.1. Article 5 (4) of Commission Implementing Regulation (EU) No. 908/2014, sets the questions which the Certification Body is required to respond to. These questions and our conclusions are set out below.

Table 1.1: Conclusions

Requirement per Article 5 of Regulation No. 908/2014	Conclusion
The paying agency complies with the accreditation criteria.	For our overall opinion in this respect, refer to the Audit Opinion (see also the internal control system). In general, the paying agency complies with the accreditation criteria. Key recommendations are summarised in sections 1.8 and 1.9 below and are elaborated on in more details in the relevant sections of this report.
The paying agency's procedures are such as to give reasonable assurance that the expenditure charged to the EAGF was effected in compliance with Union rules, thus ensuring that the underlying transactions are legal and regular, and that recommendations for improvements, if any, have been followed-up.	For details of our opinion in this respect see the Audit Opinion.
The annual accounts referred to in Article 29 (chapter III) of Regulation No. 908/2014 are in accordance with the books and records of the paying agency.	For details of our opinion in this respect see the Audit Opinion.
The statements of expenditure are a materially true, complete and accurate record of the operations charged to the EAGF.	For details of our opinion in this respect see the Audit Opinion.
The financial interests of the Union are properly protected as regards amounts to be collected.	The completeness of Annex II is ensured and detailed observations are included in section 6 of the report.

1.3. Compliance with the Commission Guidelines

Table 1.2: Compliance with the Commission's Guidelines

Guideline	Conclusion
Guideline No. 1 on Accreditation	Our report complies with the Guideline.
Guideline No. 2 on the annual certification audit	Our report complies with the Guideline.
Guideline No. 3 on the reporting requirements and opinions of the Certification Body.	Our report and opinion comply with the Guideline.
Guideline No. 5 on reporting irregularities	Our report complies with the Guideline.

- 1.3.1. Guideline No. 1 on accreditation and Guideline No. 4 on the Management Declaration were considered in carrying out our audit examination.

1.4. Overall error evaluation

1.4.1. The total financial error resulting from our audit, determined in accordance with point 5 of Annex 4 of Guideline No. 2, is as follows:

Table 1.3: Overall error evaluation

Audit Steps	Established Errors	Amount Considered €
Review of Internal Control System	Financial errors from compliance testing or assessment of internal control system (considered as known errors)	0.00
Validation of Legality and Regularity of expenditure	Financial errors from substantive testing – statistical sampling (Most Likely Errors + Known errors)	9,337,703
	Financial errors from substantive testing – non-statistical sampling (established error rate in monetary value)	0.00
	Other financial errors	0.00
Validation of Accounts	Financial errors found in the reconciliation (considered as known errors)	0.00
Total Financial Impact		9,337,703

1.5. Assessment of the internal control system and the compliance with the accreditation criteria

Standard

1.5.1. Our assessment is based on our review of the internal control system (ICS) of the paying agency, including its compliance with the accreditation criteria. It is summarised in the matrix below using the following assessment criteria:

(1) Not working. There is a clear non-respect of one or more accreditation criteria or there are serious deficiencies. The seriousness of the deficiencies are such that the paying agency cannot fulfil the tasks set out in Article 7 of the Regulation (EU) No. 1306/2013. Not all risks are addressed by controls and/or there are likely to be frequent control failures. The impact on the effective functioning of the key requirements is significant. The deficiencies are systemic and wide-ranging. As a consequence, no assurance can be obtained from the system. Scores = [1 – 1.5]

(2) Works partially. There are other deficiencies which do not fall under (1), but which would have to be followed-up according to Article 2 (1) of Commission Implementing Regulation (EU) No. 908/2014. All risks are addressed to a limited extent by controls, but which are not always working as intended. The impact on the effective functioning of the key requirements is significant. Recommendations have been, or should be issued, and an action plan has been, or should have been put in place. Scores = [1.51 – 2.5]

(3) Works. Minor issues were detected but there is scope for improvement. All risks are adequately addressed by the controls which are likely to operate effectively with some deficiencies having a low or moderate impact on the functioning of the key requirements. Recommendations have been formulated. Scores = [2.51 – 3.5]

(4) Works well. No deficiencies or only minor deficiencies were found. All risks are adequately addressed by the controls which are likely to operate effectively. Scores = [3.51 – 4.0]

1.5.2. In cases where the procedure / component is not valid, it is indicated as not-applicable (N/A). Our assessment is partly based on reviews carried out in previous financial years, where we have confirmed that no major changes in the procedures / components have occurred; in such cases our assessment is indicated in brackets "()". As regards our assessment of the Internal Audit service, if certain areas are still to be audited by Internal Audit, we base our assessment on the adequacy of the five year audit plan. In such circumstances our assessment is also indicated in brackets "()".

Detailed Assessment

1.5.3. Matrix I and Matrix II below concerns schemes (strata) under EAGF covered by the IACS, i.e. support schemes under EAGF established under Chapter II of Title V (Articles 67 to 78) of Regulation No. 1306/2013 of the European Parliament and of the Council. The general conclusion (overall scores at IACS level) are provided in accordance with Section 5.4 of Guideline No. 2 and reflected in our Audit Opinion.

1.5.4. Gross expenditure on the EAGF Non-IACS has been assessed as de-minimis. We have therefore not undertaken any testing of this population in accordance with the provisions set out in paragraph 6.7.3 of Guideline No.2.

IACS

Matrix I – Assessment of the IACS strata – Basic Payment Scheme

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MATRIX - Assessment of the ICS for EAGF IACS strata [Basic Payment Scheme]																					
Assessment Component Procedure		Internal environment						Control activities		Information and Communication				Monitoring				Evaluation at assessment criteria		General conclusion	
		Organisation		HR		Delegation (**)				Communication		ISS		On-going monitoring		Internal audit		W	T		
Weighting / Scoring		S	T at 10% or 15%	S	T at 5%	S	T at 5%	S	T at 50%	S	T at 5%	S	T at 10%	S	T at 10%	S	T at 5%	W	T	Weighted total	
Operations	Claim processing including validation and authorisation	Administrative controls	2	0.30	2	0.10	N/A	0.00	2	1.00	2	0.10	2	0.20	2	0.20	2	0.10	20%	2.00	0.40
		On-the-spot controls	2	0.30	3	0.15	N/A	0.00	3	1.50	3	0.15	2	0.20	3	0.30	2	0.10	20%	2.70	0.54
Payments	Execution of payments		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Accounting		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Advances and securities (*)		N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	0.00
	Debts management		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59
General conclusion																				2.33	
Assessment of ICS														works partially (significant impact)							

Key to the table:

S – Score – should correspond to the assessments in Chapter 4

W – Weight given to each assessment criteria and the Internal Control System – corresponding to section 5.4 of Guideline No. 2

T – Total = Weight * Score

* – Scotland does not have any transactions for Advances & Securities. Guideline No.1 (section 4.2) - corresponding weighting % divided equally between Execution of Payments and Accounting

** – There are no delegated bodies. Weightings have been transferred to Organisation.

1.5.5. The overall assessment of the Internal Control System for this IACS strata is **works partially**.

Matrix II – Assessment of the IACS strata – Livestock schemes [Beef and Sheep]

MATRIX - Assessment of the ICS for EAGF IACS strata - LIVESTOCK [Beef and Sheep]																					
Assessment Component Procedure		Internal environment						Control activities		Information and Communication				Monitoring				Evaluation at assessment criteria		General conclusion	
		Organisation		HR		Delegation (**)				Communication		ISS		On-going monitoring		Internal audit		W	T		
Weighting / Scoring		S	T at 10% or 15%	S	T at 5%	S	T at 5%	S	T at 50%	S	T at 5%	S	T at 10%	S	T at 10%	S	T at 5%	W	T	Weighted total	
Operations	Claim processing including validation and authorisation	Administrative controls	2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	2	0.20	2	0.20	2	0.10	20%	2.00	0.40
		On-the-spot controls	3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	2	0.20	3	0.30	2	0.10	20%	2.85	0.57
Payments	Execution of payments		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Accounting		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Advances and securities (*)		N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	0.00
	Debts management		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59
General conclusion																				2.36	
Assessment of ICS														works partially (significant impact)							

Key to the table:

S – Score – should correspond to the assessments in Chapter 4

W – Weight given to each assessment criteria and the Internal Control System – corresponding to section 5.4 of Guideline No. 2

T – Total = Weight * Score

* – Scotland does not have any transactions for Advances & Securities. Guideline No.1 (section 4.2) corresponding % divided equally between Execution of Payments and Accounting

** – There are no delegated bodies. Weightings have been transferred to Organisation.

- 1.5.6. The overall assessment of the Internal Control System for this IACS strata is **works partially**.

Non IACS

- 1.5.7. As noted in our audit strategy, we assessed the EAGF Non-IACS population as de-minimis. We have confirmed that the EAGF Non-IACS expenditure is less than 2 per cent of the EAGF expenditure.

Overall assessment of the Internal Control System

- 1.5.8. Our overall assessment of the internal control system and compliance with the accreditation criteria for the EAGF is as follows:

Strata	Assessment
EAGF IACS (BPS)	Works partially
EAGF IACS (Livestock)	Works partially

1.6. Detailed Error Evaluation

Error evaluation for the operational expenditure

1.6.1. Our error evaluation of the statistical sample populations is outlined below:

Table 1.4: EAGF statistical sample error evaluation – error rate

Basic data	EAGF IACS BPS €	EAGF IACS Livestock €	EAGF IACS Total €
Amount of gross expenditure	474,572,556	49,093,262	523,665,818
Materiality	9,491,451	981,865	10,473,316
Estimated error	1,898,290	196,373	2,094,663
Sampling interval	3,081,640	1,636,442	2,846,010
Confidence level	90%	90%	90%
Sample size in terms of hits	154	30	184
Number of files checked	154	30	184
Financial errors found from sampling			
According to Annex 3:			
• Number of Formal errors			35
• Number of Substantive errors			5
Most likely error			1,807,238
Calculation of Total Error:			
Precision			7,530,465
Total Upper Error Limit (including precision)			9,337,703
Known errors: According to Annex 3			
Known errors: from compliance testing			
Known errors: from other sources			
Conclusion:			
Total Error			9,337,703
Materiality			10,473,316

1.6.2. A detailed table of all cases checked and the detected errors including their financial values is attached (see Annex 3 Sample reviewed in substantive testing – EAGF – IACS to this report). We also attach (in Annex 5: Reconciliation of gross amount of tested expenditure to the Annual Declaration) a summary of the budget lines, reconciled to the gross amount of expenditure declared and tested, apportioned for both the IACS strata.

- 1.6.3. **Overall conclusion** – It is our opinion that the detected formal errors have no financial consequences, and that these are not of a recurrent nature. The substantive errors are mainly the result of not taking the results of inspections into the payment calculations for the sheep and beef schemes. These errors are explained in more detail in chapter 5.

Evaluation of Incompliance rate – IACS strata

- 1.6.4. We have not evaluated the incompliance rate for the same statistical sample strata due to concerns about the accuracy of the control statistics (para 6.7.4 refers)
- 1.6.5. A detailed table of all cases checked and the detected errors including their financial value is attached (see Annex 4: Incompliance Rate – EAGF - Livestock) to this report.

Evaluation of residual risk

- 1.6.6. Taking into consideration the incompliance rate calculated and the overall evaluation of the internal control system we conclude on a residual risk below 2 %:

EAGF IACS

Assessment of internal control system	2 Works partially
PA's error rate (control statistics, Management Declaration)	0.25%
Evaluation of the residual risk	We are unable to conclude on the residual error risk.

- 1.6.7. Our evaluation is reflected in the Opinion.

Certifying error rate for reduction of control rate

- 1.6.8. In accordance with Article 41 of Regulation (EU) No. 908/2014 for the purpose of reduction of the control rate the error rate for the concerned population needs to be certified. For the claim year 2015, for the scheme BPS we have tested 40 files of the random OTSC sample of the PA and calculated the respective error rate (Annex 3).
- 1.6.9. For claim year 2015, for the schemes Suckler Beef and Upland Sheep we have tested 26 files of the random OTSC sample of the paying agency (Annex 3). We found one financial error.
- 1.6.10. Our evaluation is reflected in the Opinion.

Error evaluation – Non-statistical population – operational expenditure

- 1.6.11. There were no transactions within non –statistical populations

Error evaluation for non-operational expenditure: debts, advances and securities

- 1.6.12. As regards debts our detailed error evaluation is provided in Annex 6. Based on this evaluation the error rate established at the level of Annex II Table is 0%.

- 1.6.13. The UK authorities include debts arising from cross-compliance breaches within the Annex II table. The Annex III table contains only details of multi-annual sanctions, which have not been subject to error evaluation. For further information please see section 6.3.
- 1.6.14. A detailed table of all cases checked and the detected errors including their financial value is attached (see Annex 7: Sample reviewed in substantive testing – EAGF and EAFRD Annex II Tables) to this report.
- 1.6.15. The paying agency does not have any transactions with regard to advances and securities.
- 1.6.16. **Overall conclusion** – In our opinion, there are no errors.

1.7. Nature of Findings

- 1.7.1. Our work resulted in a number of findings which led to various recommendations. We have categorised these findings and recommendations into two groups (accreditation findings and legality and regularity findings). For each finding, a level of importance was attributed in accordance with the following grading.
- 1.7.2. The categories we used to classify our findings in respect of **Accreditation** issues are as follows:

Major Findings	Matters which require immediate attention by the Competent Authority and the Head of the paying agency, corresponding to grade (1) in the accreditation matrix (see to Guideline No. 1 in respect of accreditation).
Intermediate Findings	Matters which concern the general control environment and require prompt attention at a senior level within the paying agency and the Competent Authority, corresponding to grade (2) in the accreditation matrix.
Minor Findings	Minor issues highlighted, which require attention at an appropriate level within the paying agency, corresponding to grade (3) in the accreditation matrix.

- 1.7.3. The categories we used to classify our findings in respect of the **legality and regularity of expenditure** are as follows:

Major Findings	Matters relating to weaknesses in the key controls - which require immediate attention at a senior level within the paying agency.
Intermediate Findings	Matters relating to weaknesses in the ancillary controls - which require prompt attention at an appropriate level within the paying agency.
Minor findings	Matters relating to other weaknesses which require attention at an appropriate level.

- 1.7.4. Recommendations related to minor findings are not included in this report but are communicated separately to the paying agency's management in our letter of recommendations. A list of minor recommendations is available to the Commission on request.

1.8. Major Findings

- 1.8.1. There are no issues giving rise to major recommendations.

1.9. Intermediate Findings

1.9.1. We have identified a number of issues giving rise to intermediate recommendations which are summarised in the table below.

Finding	Section	Recommendation	Response of Paying Agency	CB assessment of PA response
<p>Administrative controls</p> <p>We found that the incremental development and implementation of the RP&S system has impacted on the quality of the audit trail during 2016. The paying agency's focus on delivering core compliance functionality has meant that the audit trail is not always visible or readily accessible through the user interface. System users are able to request a range of reports to assist in processing claim enquiries whilst the system develops. However, these are centrally generated and have a turn-around time cost. Further complexity was introduced by the need to utilise interim workarounds to compensate for delays and issues with the delivery of key processing components. The development of the RP&S system remains on-going with further functionality being added. However, deficiencies in the accessibility and quality of the audit trail have the potential to impact on the paying agency's capacity to process claims promptly and accurately.</p>	4.3.9	The Certification Body recommends that the paying agency addresses the deficiencies in the audit trail to minimise the risk of delayed or inaccurate claims processing.	Accepted – the tactical reports developed for 2015 are being worked on to improve the responsiveness and turnaround time for 2016, while an action plan is implemented to strategically address the visualisation elements of the audit trail on RP&S where appropriate.	The Certification Body notes the paying agency's response and will monitor progress in 2017.
<p>Procedure for payments</p> <p>We found that delays in the delivery of the new RP&S system impacted significantly on the paying agency's planned programme to make payments to BPS beneficiaries.</p>	4.3.31	The Certification Body recommends that the paying agency takes steps to address the remaining issues in the new IT system to ensure that in future payments are made as promptly as possible and within the payment window.	Accepted - We have taken steps to improve the IT system and improve on payment delivery performance for 2016. This area is being monitored closely through the PDRC.	The Certification Body notes the paying agency's response and will monitor progress in 2017.
<p>Accounting arrangements</p> <p>We found that the paying agency relied upon inefficient processes to draw together the accounting information required for submission. We recorded that this placed a significant burden on the paying agency's finance function;</p>	4.3.38	The Certification Body recommends that management takes action to address the inefficiencies inherent in the existing accounting	The Paying Agency plans to implement the Scheme Accounting and Customer Account Management (SACAMs) over	The Certification Body notes the paying agency's response and will monitor progress in

Finding	Section	Recommendation	Response of Paying Agency	CB assessment of PA response
<p>increased the risk of error and omission and introduces delays to the accounts preparation process. The paying agency had planned a replacement system but delivery has been deferred and our intermediate recommendation from 2015 has not been implemented. The Certification Body therefore reiterates its recommendation from 2015.</p>		<p>processes and implements alternative processes, and procedures, which are fit for purpose.</p>	<p>the course of 2017 providing an integrated solution with Scheme Application systems.</p>	<p>2017.</p>
<p>Accounting arrangements The accounts preparation process suffered a significant decline in performance in 2016. The Certification Body recognises that the inefficient processes have been exacerbated, this year, by the issues with the delivery of the RP&S system. However, we are of the view that the finance team is under resourced, and does not have the capacity to manage the demands on its time effectively.</p>	<p>4.3.40</p>	<p>The Certification Body recommends that the paying agency reviews the duties and staffing of the finance team to ensure that it has the capacity to fulfil its functions adequately.</p>	<p>Delays in the delivery of RPS functionality and use of interim and solutions during 2016 had a significant impact on the ability of the finance team to complete the EU Accounts in a timely manner.</p> <p>Nevertheless, the Paying Agency will review staffing levels and duties to ensure it has the capacity to fulfil its functions adequately in 2017.</p>	<p>The Certification Body notes the paying agency's response and will monitor progress in 2017.</p>
<p>Internal Audit We found that Internal Audit has been represented on boards responsible for the delivery of RP&S, namely the Futures Project Management Board (from 2013 until December 2016) and the Futures Executive Steering Committee (from December 2016). The terms of reference of these boards record IAD representatives as being full voting members. Their role on a further board, the Futures Delivery Board, is less clearly defined, although minutes of these meetings report IAD attendance at some meetings. Over a period of time, IAD were represented on these boards by a number of individuals of varying seniority, although attendance by</p>	<p>4.4.101</p>	<p>The Certification Body notes that IAD has taken immediate steps to address this potential conflict of interest and recommends that it adopts appropriate procedures to ensure that it remains demonstrably independent of the paying agency's other departments.</p>	<p>Whilst the findings are accepted IAD has acted promptly to ensure its independence is not compromised. IAD has undertaken its own review of the three forums mentioned and the evidence from that exercise provides no conclusive proof that IAD have breached the accreditation principle. Although there was one instance</p>	<p>The Certification Body notes the response and the prompt action taken by IAD.</p>

Finding	Section	Recommendation	Response of Paying Agency	CB assessment of PA response
each individual was sporadic.			where a terms of reference document listed IAD as a voting member of the Executive Steering Committee, this was an error on the part of the secretariat. IAD have provided Audit Scotland with evidence that they contacted the secretariat promptly and asked for the terms of reference to be amended to reflect that IAD should not have voting rights.	
<p>Control statistics</p> <p>Our audit testing has identified a number of penalty cases which have not been included in the control statistics. We are unable therefore to conclude on the reliability of the data submitted by management.</p>	6.6.3	The Certification Body recommends that the paying agency reviews the submitted control statistics to ensure their completeness and accuracy.	Accepted – The paying agency will review the control statistics.	The Certification Body will monitor the review exercise.

1.9.2. There were no intermediate findings in respect of legality and regularity issues.

2. Audit Strategy of the Certification Body

2.1. Summary of Audit Strategy and Audit Plan

Audit scope and objectives

2.1.1. Under Article 5 of Commission Regulation (EU) No. 908/2014, the Certification Body is required to prepare a separate audit certificate opinion for each of the paying agencies stating that it has gained reasonable assurance that the Accounts submitted to the European Commission are in all material respects true, complete and accurate. The Certification Body is also required to prepare a Report in accordance with Guideline No.3.

Audit assurance and materiality

2.1.2. We based our assessment of the internal control system on the previous year's report adjusted to reflect the development and implementation of the new IT system. Our work was planned in accordance with the provisions of Commission Regulation (EU) No. 908/2014 and related European Commission Guidelines. In line with Guideline No.2 "Annual Certification Audit", the reporting materiality threshold was set at 2 per cent of declared net expenditure excluding clearance decisions. We have also adopted the confidence level of 95% for reporting suggested by the Commission's Guidelines. That is, our audit opinion will provide 95% assurance that the accounts in all material respects give a true, complete and accurate record of operations charged to the accounts. This is consistent with our audit approach generally. For planning and statistical sampling purposes materiality was set at 2% of positive expenditure for each population.

Systems and controls

2.1.3. The Audit Strategy describes the main systems and controls in detail. This is available on request. The systems in place and the control framework for the paying agency feature four main procedures:

- **authorisation of payments** – comprising administrative controls (involving detailed checking and authorisation of claims based on established checklist and segregation of key functions, often enforced under computerised systems) and on-the-spot controls (involving pre-payment and post-payment checks, including on-the-spot physical checks, and the examination of claimant and producer records);
- **execution of payments** – these are standardised and involve checks to confirm that only authorised claims are passed for payment and that payment is properly effected;
- **accounting for payments** – controls over ledger postings and the reconciliations against feeder systems and to bank; they also include controls over the transmission and reconciliation of the Monthly Table 104s;
- **recognition of debts** – comprising controls relating to the recognition of all amounts due and the recording of all such debts in a debtors' ledger.

Risk assessment

2.1.4. We performed risk assessment procedures to identify and assess the significant risks of material misstatement. Our risk assessment included the following work:

- we gained an understanding of the entity and its control environment, including the applicable legal and regulatory framework in place. We considered risks identified in prior periods for each measure involving a material level of expenditure. We reviewed the findings of the EC and ECA and the actions taken by the paying agency in response to any observations; we gained an understanding of the principle control activities and the information systems, including the main processes. This included procedures and controls regarding the performance of the on-the-spot-inspections and other physical checks to confirm whether the Commission's regulatory requirements relating to the quantity and detail of the checks have been achieved;
- we assessed any changes to the internal control system since the last audit. We assessed the impact of changes in the organisational and procedural arrangements since the previous audit, thereby indicating the extent to which the paying agency continues to meet the accreditation criteria;
- we assessed the effectiveness of risk management, and identified controls addressing the key risks, including fraud risks;
- we reviewed the paying agency's arrangements to establish whether controls operated by third parties are in accordance with scheme requirements, satisfy accreditation criteria and that the controls are of an appropriate standard. We also considered the effectiveness of the paying agency's monitoring of Delegated Bodies;
- we reviewed the paying agency's procedures for operating its debtors ledger and for accounting for recoveries and other negative expenditures. The control risk in respect of recoveries and debtors is low as a result of improved systems and management practices.

The audit approach

- 2.1.5. Our audit approach was to assess the risk of significant monetary error capable of affecting the annual accounts being present and tailor the nature, timing and scope of the audit accordingly. We reviewed and assessed the homogeneity of controls over the transactions to determine the number of strata. For each strata we documented the controls over the schemes and evaluated these controls through walk through testing. We carried out detailed compliance testing and assessed whether we could rely on the controls. We also took into account our previous experience of the paying agency and the fact that it has been fully accredited since 1995. From this we determined the extent to which we needed to take assurance from substantive testing.
- 2.1.6. Having reviewed and assessed the homogeneity of controls over the transactions we determined the following strata:
- IACS – Strata 1: Basic Payment Scheme, including greening
 - IACS – Strata 2: Scottish Suckler Beef and Upland Sheep Support Schemes
- 2.1.7. Gross expenditure on the EAGF Non-IACS Beekeeping scheme was €64,324 and is less than 2% of the total gross annual fund expenditure. We have therefore not undertaken any testing of this de-minimis population in accordance with the provisions set out in paragraph 6.7.3 of Guideline No.2.

Re-verification of on-the-spot controls

- 2.1.8. The paying agency uses classical GPS methodology to determine and validate areas claimed. Article 71 of delegated Regulation (EU) 809/2014 permits paying agencies to sample half of all parcels, at each holding, for the purposes of on-the-spot-checks. The paying agency for Scotland normally inspects all parcels at each holding.
- 2.1.9. For each farm location selected for re-verification, we selected 10 parcels from the original inspection. Our step 1 re-verification of on-the spot-checks involved a review of

inspection files and checklists prepared by inspectors in addition to physical re-verification of inspections using the paying agency's inspectors and GPS equipment. The timing of re-verification was subject to full completion of the original inspection including inspection file paperwork and availability of paying agency inspectors and audit staff.

The nature and extent of the CB's reliance on the work of Internal Audit

- 2.1.10. In arriving at our opinion on the EAGF account we have taken account of the results of the statutory audits of the paying agency's accounts. We have also considered the agreed findings of the Commission's Services. We have reviewed Internal Audit reports and liaised with them throughout the audit. We did not, however, place reliance on their work.

Any assumptions and estimations made during the course of the review

- 2.1.11. We have used the prior year Single Farm Payment (SFP) entitlement value in order to select an MUS sample of on-the-spot checks for re-verification. In all other respects, we have followed the guidelines and made no contrary assumptions.

Plan of audit activities

- 2.1.12. We reviewed the paying agency's procedures governing scheme design and scheme control reviews and the controls governing the implementation of changes in Commission Regulations to establish whether they are implemented promptly.
- 2.1.13. We carried out detailed compliance testing and assessed the extent to which we could rely on the controls. Our compliance and substantive testing was carried out on the same sample in accordance with the provision for dual testing set out in paragraph 5.3 of Guideline No. 2.
- 2.1.14. We reviewed the general control environment and considered compliance with the Accreditation Criteria.
- 2.1.15. We reviewed the paying agency's procedures and controls regarding the performance of on-the-spot inspections to establish whether the Commission's regulatory requirements relating to the quantity and quality were achieved. We re-verified samples of on-the-spot checks in accordance with Guideline No. 2 to establish whether the paying agency's arrangements for ensuring the Legality and Regularity of claims were appropriate.
- 2.1.16. We reviewed the paying agency's arrangements to establish whether controls carried out by third parties are in accordance with scheme requirements and that evidence exists to verify that the controls are of an appropriate standard. We also considered the effectiveness of the paying agency's monitoring of Delegated Bodies.
- 2.1.17. Guideline No. 2 permits the merging of the EAGF and EAFRD populations for non-operational transactions, where it can be demonstrated that debt movements are managed using a common system. The debt management system operated by the paying agency is common to EAGF and EAFRD. We have therefore merged the EAGF and EAFRD populations for substantive testing of non-operational transactions.
- 2.1.18. We reviewed the paying agency's arrangements for operating its debtors' ledger and for accounting for recoveries and other negative expenditures. We tested whether debts are recognised promptly and accurately recorded in the paying agency's books of account. We also performed focused testing on balances disclosed in the Annex II Tables to ensure they comply with the Commission's requirements.

- 2.1.19. In addition, we also tested the completeness of the record of debts by checking that the Annex II included, where necessary, the cases with financial errors identified in the:
- review of the control statistics;
 - re-verification of on-the-spot-checks; and
 - substantive testing of expenditure.
- 2.1.20. We reviewed the controls in place over statistical returns, financial ceilings, and entitlements as well as a follow-up of previous years' recommendations.
- 2.1.21. Our Audit Strategy is available to the Commission upon request.
- 2.1.22. **Assessment:** Our overall assessment of the functioning of the internal control systems and compliance with the accreditation criteria, including an indication of the level of assurance required from the substantive testing and the related sample sizes, are set out in the table below:

Table 2.1: Summary of expenditure populations and assurance levels (EAGF)

Population / Strata	Inherent Risk High (100%) / not high (60%)	Assurance required from substantive testing (confidence level required)	Expected Error Rate	Minimum sample size (Appendix 3.1 of Annex 3)
Strata 1 – EAGF IACS Basic Payment Scheme (BPS)	High (100%)	Works partially (90%)	15-20%	154
Strata 2 – EAGF IACS Scottish Suckler Beef and Upland Sheep Support Schemes	Not high (60%)	Works partially (90%)	15-20%	30*
EAGF NIACS Beekeeping	De minimis	De minimis	De minimis	De minimis

*Minimum sample required at strata level

- 2.1.23. The overall sample size for the EAGF IACS population was 171 and this was apportioned across the two strata using projected expenditure: Basic Payment Scheme 154 transactions and 17 transactions for the Scottish Suckler Beef and Upland Sheep Support Schemes. The sample for the beef and sheep schemes was increased to 30 items, the minimum required by Guideline No. 2. This has been updated since our initial strategy submitted to the Commission on the 2 September 2016.

2.2. Work done

- 2.2.1. The audit was carried out based on the two strata in relation to which the nature and rigour of the detailed compliance and substantive tests differed. The testing done on each strata is outlined in the table below:

Table 2.2: Outline approach to each population

Population	DOC	AR	CT	ST	OR	CRM	IAS	2016 Expenditure € / £
1) EAGF – IACS [Basic Payment Scheme (including greening)]								€ 471,673,695
Authorisation – on-the-spot controls	√		√		√			
Authorisation – administrative controls	√		√	√				
Execution of payments	√		√	√				
Accounting	√		√	√				
2) EAGF – IACS [Scottish Suckler Beef and Upland Sheep Support Schemes]								€ 49,094,131
Authorisation – on-the-spot controls	√		√		√			
Authorisation – administrative controls	√		√	√				
Execution of payments	√		√	√				
Accounting	√		√	√				
3) Debtors – EAGF	√		√	√	n/a			£ 536,511.38

Note	
DOC:	Scheme documentation and walkthrough
AR:	Analytical review, discussion
CT:	Compliance testing of procedures and controls
ST:	Substantive testing of selected files
OR:	On-the-spot controls re-verification
CRM:	Computer risk management based system testing using Computer Assisted Audit Techniques
IAS:	Review of Internal Audit Service reports

2.3. Resources

2.3.1. The audit team of the Certification Body in respect of the EAGF and EAFRD which performed the work comprised 10 professional staff. The resources dedicated to the project varied during the year as required. The qualifications of the personnel involved are summarised as follows:

Chartered Accountants	Others	TOTAL
Person days	Person days	Person days
1,010	947	1,957

3. Accreditation of the Paying Agency

3.1. Institutional framework – the Competent Authority and the Coordinating Body

- 3.1.1. The functions of the Competent Authority, as stipulated in Article 1(2) of Commission Delegated Regulation (EU) No 907/2014, and the Co-ordinating Body, are held by the Secretary of State for Environment, Food and Rural Affairs, the Scottish Ministers, the Welsh Ministers and the Department of Agriculture, Environment and Rural Affairs in Northern Ireland, acting jointly. The legal basis for the Competent Authority and the Co-ordinating Body is by way of Statutory Instrument No. 3260 of 2014.

3.2. Accreditation status of the Paying Agency

- 3.2.1. The Scottish Government Rural Payments and Inspection Division (SGRPID) was established and accredited as a paying agency by the UK Competent Authority on 16 October 1995. As a paying agency previously accredited in accordance with Commission Regulation (EU) No. 1663/1995, the SGRPID was formally re-accredited in accordance with Articles 1.3 and 17.1 of Commission Regulation 885/2006 with effect from 16 October 2007.
- 3.2.2. It is one of four accredited UK paying agencies under EC legislation. The Instruments of Appointment to accredit all UK paying agencies are held by the UK Co-ordinating Body, which also monitors the implementation of relevant corrective actions.

4. Compliance with Accreditation Criteria – Review of the Internal Control System

4.1 Introduction

- 4.1.1. This section outlines the current status of the accreditation and provides the basis for the overall assessment of the internal control system and for our assessment in respect of the paying agency's compliance with the accreditation criteria per internal control procedure / component as indicated in Matrices I and II. We have assessed the compliance with the accreditation criteria by using the grading "1" to "4". Our overall assessment is outlined in section 1.5 above.

4.2. Compliance testing – Control Activities

- 4.2.1. We confirmed our assessment of the accreditation procedures against the control activities by carrying out the following compliance tests as suggested in Guideline No. 2:

Procedure	IACS [BPS]	IACS [Livestock]	Findings
Administrative controls	20	10	<i>Paragraphs 4.3.2 – 4.3.10</i>
On-the-spot controls	40	26	<i>Paragraphs 4.3.11 – 4.3.26</i>
Payment procedures	20	10	<i>Paragraphs 4.3.27 – 4.3.33</i>
Accounting procedures	12 monthly returns	12 monthly returns	<i>Paragraphs 4.3.34 – 4.3.43</i>
Procedures for debts	4 *		<i>Paragraphs 4.3.46 – 4.3.48</i>

* Debtors for EAGF and EAFRD are managed under a common administrative system. We have tested the minimum required sample of 30 items [EAGF (4) and EAFRD (26)]

- 4.2.2. In line with Section 1.2 of Annex 3 to Guideline No. 2, where the Certification Body does not expect to find exceptions, the minimum sample size at Fund level is 30 items. We have tested the minimum required sample of 30 items to assess the paying agency's compliance with the accreditation criteria.

4.3. Evaluation per accreditation criterion

- 4.3.1. Annex I of Commission Delegated Regulation (EU) No. 907/2014 sets out the accreditation criteria. We performed our review following the requirements of those standards.

Control activities: Authorisation of payments – Administrative controls

- 4.3.2. Payments under the Basic Payment Scheme were made through the paying agency's new IACS - Rural Payments and Services system (RP&S). The paying agency's CAP Futures IT programme aimed to provide new IT systems to implement CAP 2014-2020. The programme has, however, proved more complex and challenging than anticipated and has suffered considerable problems, lengthy delays and significant defects. Key regulatory and self-determined milestones and targets were not met.
- 4.3.3. RP&S opened on time for 2015 applications in March 2015. However, the system was slow and did not function as expected. Errors in the IT infrastructure and software had to be fixed during the application period. The paying agency utilised the derogation provided by Regulation (EU) 2015/747 to extend the deadline for submission to 15 June 2015.
- 4.3.4. The paying agency commenced making partial payments to some BPS beneficiaries in late December 2015. In February 2016 the Scottish Government announced a

programme of nationally funded loans available to all beneficiaries who had not received their first payment. The loans were provided on an opt-out basis restricted to the lesser of £20,000 or 60% of the estimated payment due, and were recovered by offset against eventual subsidy payments.

- 4.3.5. The paying agency gave priority to the processing of BPS over other schemes but was unable to process all claims by 30 June. However, the paying agency benefitted from the derogation provided by the Commission in accordance with Article 5(4) of Commission Delegated Regulation (EU) No 907/2014.
- 4.3.6. For livestock cases, claims were recorded and validated on RP&S and the audit trail was more evident. However, the functionality to record and process inspection outcomes was not available and these were processed on the previous SIACS1 system with an alternative payment mechanism (spreadsheet) used to merge the data from the two sources and generate payments.

Findings

- 4.3.7. We reviewed the procedures and tested 30 items from the IACS population in respect of administrative controls over the authorisation of payments. Our work confirmed that:
- controls and procedures were operating satisfactorily at area offices. Up to date desk instructions are in place, either as separate guidance or through the RP&S interface, for all administrative processes and controls leading up to a payment authorisation;
 - staff complete all checklists as required and that a manual or electronic record is maintained recording the procedures and checks carried out.
 - data input to RP&S was accurate and complete; and,
 - all automated validation and cross checks had been completed, and queries arising from RP&S checks were resolved, before the claim was authorised for payment.
- 4.3.8. The incremental development and implementation of the RP&S system has impacted on the quality of the audit trail during 2016. The paying agency's focus on delivering core compliance functionality has meant that the audit trail is not always visible or readily accessible through the user interface. System users are able to request a range of reports to assist in processing claim enquiries whilst the system develops. However, these are centrally generated and have a turn-around time cost. Further complexity was introduced by the need to utilise interim workarounds to compensate for delays and issues with the delivery of key processing components.
- 4.3.9. **The Certification Body recommends that the paying agency addresses the deficiencies in the accessibility and quality of the audit trail to minimise the potential impact on the paying agency's capacity to process claims promptly and accurately. (Classification: Intermediate).**

Assessment

- 4.3.10. Our review has identified deficiencies in the audit trail available to staff and management. In our opinion, the scoring for this criterion is 2.

Control activities: Authorisation of payments – On-the-spot controls

- 4.3.11. Due to the inspection preparation and performance functionality of the new RP&S system not being available at the time of the inspections the Land Inspections team had to make contingency arrangements to transfer inspection packs from RP&S to the GPS equipment to allow inspections to be completed. Further delays meant that the team had to utilise another contingency to upload the inspection outcomes to RP&S.

- 4.3.12. For livestock cases, the functionality to record and process inspection outcomes was not available in RP&S due to development delays. These cases were processed on the previous SIACS1 system with an alternative payment mechanism (spreadsheet) used to merge the data from the two sources and generate payments.

Findings

- 4.3.13. In respect of on-the-spot-controls, we reviewed the paying agency's methodology for selecting area-based and livestock claims for on-the-spot-checks. The paying agency selects cases annually; using a combination of risk based and random selection techniques. The selection process is controlled centrally by HQ officials, to ensure that all regulatory requirements are met.
- 4.3.14. We found that the claims selected for inspection satisfied the requirements set out in the regulations in terms of the number of inspections and the correct allocation between risk and random checks.
- 4.3.15. We reviewed a selection of guidance, instructions and documentation prepared by the Scheme and Inspections Division for managing the inspections process across area offices. We found that these were consistent with scheme regulations and operational arrangements.
- 4.3.16. All guidance and standard documents are available to users on the paying agency intranet and inspectors have access to electronic copies. Summary guidance notes are available to inspectors as 'flash cards' stored on the GPS equipment used to undertake area based inspections.
- 4.3.17. We confirmed, as part of our planning process, that the paying agency has a Divisional Training plan which is updated annually. We confirmed that arrangements are in place to ensure that only suitably qualified staff are appointed to inspector posts.
- 4.3.18. Inspectors undertaking area based on-the-spot-checks are trained in the use of GPS equipment. These officers undertake practical induction training and regular (annual) mandatory update courses.
- 4.3.19. The paying agency's training policy requires that all inspectors (area based and livestock) attend annual update/refresher courses. Additional specific courses are arranged to address regulatory changes and the introduction of new schemes and/or rules. For the 66 OTSC re-verifications undertaken for EAGF IACS (Land 40 cases; Livestock 26 cases) we confirmed that the inspectors had received relevant training.
- 4.3.20. The paying agency undertakes physical inspections using GPS technology for area based inspections and standard measuring equipment. GPS equipment is subject to annual calibration testing by the paying agency's specialist GPS team.
- 4.3.21. We confirmed that all random and risk based inspections (area based and livestock) are carried out by paying agency staff.
- 4.3.22. We reviewed the Monitoring and Supervision arrangements in relation to on-the-spot-checks. We found that the Monitoring and Supervision system put in place by the paying agency consists of a range of specific measures, including:
- inspections are completed by technical staff with practical backgrounds and relevant agricultural or environmental qualifications;
 - each Area Office has a specialist co-ordinator responsible for overseeing inspections. The co-ordinator also acts as a reference point for additional information and as the contact between the Area Office and HQ;
 - training for land inspectors is provided in three phases. Comprehensive training covering all requirements is delivered to all new staff. Co-ordinators also attend the new staff training to stimulate discussion and to impart their knowledge and

experience. Targeted refresher training is delivered to existing members of staff. Refresher training focuses on any regulatory changes and issues highlighted by audit visits or internal quality checks. The last phase is local area office training. Area office co-ordinators also deliver local training which focuses on the issues which are relevant to the locality. To ensure consistency the new staff and refresher training is developed in HQ and delivered by experienced staff including at least one member of staff from HQ;

- inspectors' guidance is developed and updated centrally by staff in HQ. It is web-based and easily accessible by all staff. Updates are circulated to the Knowledge Management mailbox system to ensure that all staff are aware of the changes;
- area inspections and livestock inspections are completed using standard control report forms. The report forms are intuitive and guide inspectors to ensure that all requirements are controlled effectively;
- central support is provided by a small team of staff in HQ. Questions and answers are relayed using the Customer Service Desk. Replies are sent to a Knowledge Management mailbox system and saved separately in the electronic management filing system as a reference library;
- line managers have a responsibility to ensure staff are competent and complete work to a high standard. Line managers undertake routine checks on completed inspections. The selection of line management checks varies depending on the experience and knowledge of the member of staff;
- a percentage of inspections are subjected to checks. The check is a pre-payment check that involves a member of staff at least one grade above that of the inspector completing a pro-forma check-list to assess the quality of case processing and the inspection report. Where the case selected had been inspected it is subject to a re-performance inspection. The results of checks are used for training purposes and could potentially lead to re-certification of the claim;

4.3.23. the work of inspectors is also evaluated by the GPS/GIS Team to ensure their competency. The primary focus of the evaluation is on new inspectors although the work of a sample of experienced staff is also reviewed each year.

4.3.24. We identified discrepancies in 18 out of 40 on-the-spot checks we re-verified within the EAGF IACS Basic Payment Scheme strata of which there were 44 compliance failures. Common errors identified included failure to record boundary changes, inaccuracies in the banding applied to technical assessments, exclusions not included or of incorrect size and incorrect changes in land cover. Only one of these issues resulted in a financial error. Please refer to paragraph 5.2.4 regarding issues identified on individual cases.

4.3.25. We identified discrepancies in 6 out of 26 on-the-spot checks which we re-verified within the EAGF IACS Livestock strata. Compliance failures included incomplete inspection packs and discrepancies between the inspection report and the producer's records. Please refer to paragraph 5.3.4 regarding issues identified on individual cases.

Assessment

4.3.26. The Certification Body's view is that the issues with the delivery of the IT system are organisation wide and as such are a weakness in the system of administrative controls. However, the weaknesses had a lesser impact upon the conduct of on-the-spot-checks and we have not therefore taken this into account in our assessment of the on-the-spot-inspection process. Our review has identified high number of compliance errors in our samples of area based and livestock inspections, however, these are of low impact and

we have only identified one financial error. We have made minor recommendations in our management letter. In our opinion, we have given this criterion an assessment of 3.

Control activities: Procedures for payment

Findings

- 4.3.27. We reviewed the procedures for payment in line with the requirements of Commission Delegated Regulation (EU) 907/2014 [Annex I Section 2(B)].
- 4.3.28. To assess the standard of procedures for payment we reviewed the records supporting a sample of 30 EAGF payments. Our testing was designed to confirm that the paying agency's procedures ensured that payments are; accurate, appropriately approved; made only to bank accounts belonging either to beneficiaries or to their assignees; made only from the paying agency's bank or a governmental payments office; made within five working days of the date of charge to the EAGF. Our testing also considered segregation of duties, approval procedures, and procedures for voiding payments which failed to transfer.
- 4.3.29. The paying agency usually pays approximately 96% of BPS beneficiaries by the end of December of the year of application. Delays in the delivery of the new RP&S IT system meant that this could not be achieved for claim year 2015. In view of these delays the paying agency considered options to expedite payments and ease the burdens on beneficiaries.
- 4.3.30. The paying agency elected to make interim payments to BPS beneficiaries based on a pre-determined percentage of their estimated claim. The decision to do this was taken to minimise the impact on farmers and the amounts paid were set at prudent levels to ensure that any adjustments to claims would be covered by the second instalment.
- 4.3.31. As recorded elsewhere in this report the paying agency experienced significant difficulties with the RP&S system and interim workarounds were required for some aspects of processing. The paying agency benefited from the derogation provided by the Commission in accordance with Article 5(4) of Commission Delegated Regulation (EU) No 907/2014.
- 4.3.32. **The Certification Body recommends that the paying agency takes steps to address the remaining issues in the new IT system to ensure that in future payments are made as promptly as possible and within the payment window. (Classification: Intermediate)**

Assessment

- 4.3.33. In our opinion, the scoring for this criterion is 2.

Control activities: Procedures for accounting

Findings

- 4.3.34. We reviewed the procedures for accounting in line with the requirements of Commission Delegated Regulation (EU) 907/2014 [Annex I Section 2(C)].
- 4.3.35. We performed the following tasks:
- reviewed the paying agency's procedures for preparing regular reconciliations and the accounts for adequacy and completeness;
 - reviewed monthly reconciliations to ensure that they had been prepared in accordance with requirements;

- re-verified sample of monthly reconciliations for particular schemes including the relevant year-end;
 - reconciled payments data provided for sampling purposes to the underlying financial records;
 - a review of all year-end reconciliations to ensure that they had been properly completed and that all reconciling items were cleared;
 - a test check of T104 balances to the ledger; and
 - investigation and resolution of any unusual items identified during review work.
- 4.3.36. We found that monthly and quarterly reconciliations were not being undertaken promptly, in some instances with delays of up to two months after the period end. However, reconciliations completed by the paying agency were found to be accurate and explanations for reconciling items were satisfactory. The delays in preparing these reconciliations had an adverse impact on the audit process due to the delayed submission of expenditure data required by the Certification Body for Step 2 substantive testing.
- 4.3.37. Our 2015 report noted that the paying agency relied upon inefficient processes to draw together the accounting information required for submission. We recorded that this placed a significant burden on the paying agency's finance function; increased the risk of error and omission and introduces delays to the accounts preparation process.
- 4.3.38. The paying agency had planned a replacement system but delivery has been deferred and our intermediate recommendation from 2015 has not been implemented. The Certification Body therefore re-iterates its recommendation from 2015.
- 4.3.39. **The Certification Body recommends that management takes action to address the inefficiencies inherent in the existing accounting processes and implements alternative processes, and procedures, which are fit for purpose. (Classification: Intermediate).**
- 4.3.40. The accounts preparation process suffered a significant decline in performance in 2016. The Certification Body recognises that the inefficient processes have been exacerbated, this year, by the issues with the delivery of the RP&S system. However, we are of the view that the finance team is under resourced, and does not have the capacity to manage the demands on its time effectively.
- 4.3.41. **The Certification Body recommends that the paying agency reviews the duties and staffing of the finance team to ensure that it has the capacity to fulfil its functions adequately. (Classification: Intermediate)**
- 4.3.42. Our testing identified that a suspense account containing amounts returned due to incorrect BACS or CHAPS details had not been appropriately reviewed and cleared resulting in a delay in the return of monies to the fund. The amounts involved are small and we have made a minor recommendation in this regard.

Assessment

- 4.3.43. Our review of the procedures for accounting was unsatisfactory. The intermediate recommendation from our 2015 report has not been addressed and we have noted a significant decline in the function. We have re-iterated our intermediate recommendation with regard to accounting processes and have made a further intermediate recommendation in regard to the staffing of the finance team. In our opinion, the scoring for this criterion is 2.

Control activities: Procedures for advances and securities

Findings

4.3.44. The paying agency does not have transactions under this heading.

Assessment

4.3.45. This criterion is not applicable to the paying agency.

Control activities: Procedures for debts

Findings

4.3.46. We reviewed the procedures for debts in line with the requirements of Commission Delegated Regulation (EU) No. 907/2014 [Annex I Section 2 (E)].

4.3.47. The arrangements for administering recoveries are common to EAGF and EAFRD debts. Our review, findings and overall assessment in this section are in respect of EAGF and EAFRD procedures for debts. We tested 30 items (EAGF: sample of 4; EAFRD: sample of 26) required by Annex 3 to Guideline No. 2. We undertook the following work:

- we reviewed the paying agency's guidance and desk instructions for debt management. We found, as in the prior year, that the recoveries desk instructions, although fit for purpose, require updating. As in the prior year, we have made a minor recommendation in our management letter.
- debt management is part of the role/remit of the finance function. We reviewed the Human Resources standard in relation to debt management and were satisfied that staff have appropriate qualifications and are adequately trained.
- our review of the paying agency's MIS, for the administration of EC debtors, confirmed that the system and its embedded controls are adequate for the recording of EC debt and recoveries.
- our compliance and substantive testing confirmed that the amounts to be recovered are identified and reported timeously; that invoices are raised and that the paying agency maintains an adequate audit trail for debtors and recoveries.
- we confirmed by inspection of management reports that overdue debtor balances are reviewed regularly to ensure that appropriate follow up action is taken.
- we reviewed the monthly reconciliations between the MIS and the Accounts Receivable module of the SEAS general ledger.
- we found that reconciliations relating to recoveries were accurate and that explanations for reconciling items were adequate.
- we reviewed debtor files for evidence that interest calculations had been checked.

Assessment

4.3.48. Our review found that procedures for debts were generally satisfactory. In our opinion, the scoring for this criterion is 3.

4.4. Other accreditation components

- 4.4.1. We confirmed our assessment of the other accreditation components against the standard (Annex I of Commission Delegated Regulation (EU) No. 907/2014) by carrying out reviews/tests to ensure the paying agency's compliance with the criteria.

Internal environment: Organisational structure

Description of the organisational structure

- 4.4.2. The paying agency operates under the Agriculture, Food and Rural Communities Directorate of the Scottish Government. The Directorate has 949 persons employed with an equivalent full time equivalent of 873. In terms of directly undertaking work for the paying agency, 678 people are employed; an equivalent of 615 FTEs.
- 4.4.3. The Headquarters of the paying agency are located at Saughton House, Broomhouse Drive Road, Edinburgh, UK. The Headquarters employ 386 persons corresponding to the full-time equivalent of 349 staff. The paying agency also has 16 regional offices. The total number of people employed at these offices is 563 persons corresponding to the full time equivalent of 524 staff.
- 4.4.4. The organisation chart of the paying agency is included in the Annex 8: Organisation Structure of the PA and regional/local offices of this report. The full-time equivalent is indicated by department.

Findings

- 4.4.5. Our work in this area included an assessment of the paying agency's organisational structure, as set out in the organisational chart provided by the paying agency at Annex 8 to this report, to establish whether the paying agency had:
- assigned authority and responsibility at relevant operational levels. We are satisfied that the organisational structure for HQ, and area offices, clearly establishes assigned authority and key responsibilities;
 - appropriate segregation of duties between authorisation of payments, processing payments and accounting. We found that there is a clear separation between the key duties as evidenced by the existence of specific departments/functions for administration of claims, authorisation payments, accounting and payment (Treasury and Banking); and
 - established independent lines of reporting for technical and internal audit services. Our review of Accreditation Committee minutes confirmed that there are appropriate arrangements in place for independent reporting for technical and internal audit services.
- 4.4.6. Paying agency staff have been under significant pressure during FY2016. Delays in developing and delivering the RP&S system, the processing of claims backlogs, the prioritisation of payments under the BPS, and the use of manual workarounds have impacted adversely on business as usual. The movement of staff across the paying agency also raises concerns around segregation of duties due to staff moving between teams.
- 4.4.7. The paying agency has also lost a number of key senior staff throughout the financial year. The loss of their cumulative experience has added to the level of pressure on staff and presents risks going forwards. There were a significant number of new staff in the Area Office GPS inspection teams; however, internal reports indicate that the paying

agency has 66 staff vacancies at present of which 20 are currently filled on a temporary basis.

- 4.4.8. A new Director took up position at the paying agency in September 2016 and has commenced a structural review of the organisation. Some early changes have been made, including the appointment of a Chief Operating Officer, and further changes are proposed. The Certification Body will monitor these changes and report in due course.

Assessment

- 4.4.9. Whilst there have been changes in senior management and a review of the departmental structure is on-going the paying agency has suffered significant pressures. The delays experienced in implementing the new RP&S IT system and the interim arrangements put in place to deliver business as usual have stretched the organisational capacity of the paying agency, to a significant degree impacting on its ability to make payments within its normal timescales. In our opinion, the scoring for this criterion is 2.

Internal environment: Human-resource standard

Findings

- 4.4.10. We reviewed the paying agency's human resource standard following the requirements of Commission Delegated Regulation (EU) No. 907/2014 [Annex I Section 1(B)].
- 4.4.11. We completed an examination of the job descriptions and training records for 30 staff selected from the area offices and headquarters, to confirm that they were up to date and complied with requirements. Overall, our review was satisfactory.
- 4.4.12. We found that training for headquarters staff was usually undertaken 'on the job' rather than by way of formalised training programme although there were formal training processes for SEAS (Scottish Government's financial ledger) and ERDM (Scottish Government's Electronic Records Data Management system).
- 4.4.13. We completed a review of measures to identify and avoid conflicts of interest (COI). The RP&S system contains a COI function which staff are required to complete and which can be reviewed at any time by senior staff at Area Offices and headquarters. We confirmed with senior staff at area offices and headquarters that they had reviewed COI reports for their staff. The COI functionality on the RP&S system restricts staff from 'write access' for those businesses they have declared as conflicts. We checked a sample of staff to ensure they did not have 'write access' to declared conflicts. We also noted that the three area offices visited operated a policy to rotate staff between districts/parishes, on a five year cycle. We reviewed the rotation records and confirmed that this control was operating satisfactorily.
- 4.4.14. The paying agency currently relies on the Scottish Government's overarching fraud response and the related arrangements for training staff in fraud awareness. These arrangements have been previously reviewed by the Certification Body and reported as satisfactory. Annex I to Delegated Regulation (EU) 907/2014 stipulates that paying agencies must take measures to prevent and detect fraud and irregularity in the context of their activities in the Multi Annual Financial Framework 2014-2020.
- 4.4.15. The Certification Body notes that the paying agency has not progressed the development of its proposed Fraud Strategy which was the subject of a minor recommendation in our 2015 report. We consider that the implementation of such a strategy would support the paying agency in protecting the fund.
- 4.4.16. Our compliance testing confirmed that segregation of duties was established and effective in relation to functions for authorising, paying and accounting for payments. Our work also confirmed that staff comply with the paying agency's arrangements for supervision and review by a second official.

Assessment

4.4.17. Our review of the Human Resource standard was satisfactory in most respects. We have made minor recommendations which have been included in our management letter. In our opinion, we have given this criterion an assessment of 3.

Internal environment: Delegation

Findings

4.4.18. The paying agency has not delegated any tasks to other institutions (referred to as "delegated bodies").

Assessment

4.4.19. This criterion is not applicable to the paying agency.

Information and communication: Communication

Findings

4.4.20. We reviewed the paying agency's communication following the requirements of Commission Delegated Regulation (EU) No. 907/2014 [Annex I Section 3(A)].

4.4.21. We reviewed the activities and minutes of the Accreditation Committee, which is chaired by the Director of the paying agency and monitors compliance with accreditation criteria, including implementation and progress with the schedule of Corrective Action and any required system developments.

4.4.22. Through our review of a selection of schemes and our transaction testing we were able to confirm that changes in relevant EC regulations were implemented and that appropriate databases, instructions, guidance and checklists were suitably amended. This testing also confirmed that the paying agency was using the current rates of aid and foreign exchange rates. We did not identify any instances when the paying agency was not applying the current regulations.

Assessment

4.4.23. In our opinion, the scoring for this criterion is 3.

Information and communication: Information Systems Security

Standard

4.4.24. We reviewed the paying agency's information systems security following the requirements of Commission Delegated Regulation (EU) No. 907/2014 [Annex I Section 3(B)].

Work Done

4.4.25. The table below indicates the overall situation as at 15 October 2016:

	Yes / Not Applicable	No / Not Applicable
The yearly expenditure of the Paying Agency is more than €400 million:	✓	
The Paying Agency has obtained ISO 27001:2013 certificate:		✓
The certificate covers all key tasks of the Paying Agency:		n/a
The certificate covers also delegated tasks:		n/a

Findings

4.4.26. Our review has found compliance to be rated “Satisfactory” in 10 out of the 14 security control areas.

Information Security Policies

4.4.27. The paying agency is part of the Agriculture, Food and Rural Communities Directorate (AFRC) within the Scottish Government and is subject to corporate IT security policies, procedures and controls. AFRC’s IT services are provided by ISIS which also manages overarching security standards.

4.4.28. We have confirmed through observation and inspection that the paying agency follows a group of policies in place covering ISO 27002 areas, including the central SG policies and the AFRC Information Systems Security Policy (ISSP). Many of the security related policies are SG owned policies (also adopted by other delegated bodies) and are subject to a review process outside the responsibility, or influence, of the paying agency.

4.4.29. SG information security policies and issues are communicated and promoted to all staff on the SG’s “Saltire” intranet and users must acknowledge commitment statements at computer sign-on for confirmation of acceptance of policies. Policies are also shared with third parties and delegated bodies as necessary, with contractual reference to these.

4.4.30. Policy compliance, communication and controls are also included in procedural documentation including the IT Code of Conduct.

4.4.31. A separate AFRC Information Systems Security Policy is maintained, which covers local security issues relating to the paying agency. This is supported by a number of local policies. As a part of the process to obtain ISO 27001 accreditation during 2016, the paying agency conducted a “due diligence” review of existing policies to determine the currency and level of ISO27002 compliance of each.

Organisation of Information Security

4.4.32. AFRC operates as an SG directorate. The SG corporate information security management framework directly influences all aspects of the Paying Agency. Over-arching SG Corporate security policy is managed by the Office of Protective Security (OPS) which sits within the Information Services and Information Systems (ISIS) division. The OPS reports

to the Senior Information Security Officer who is a member of the ISIS Senior Leadership Team.

- 4.4.33. Our 2015 report raised no issues in this domain. We have confirmed that there have been no significant changes to the operation of corporate security organisation during 2016.
- 4.4.34. Within the structure of the over-arching SG policy, the paying agency has established and published a local management framework for information security. This includes policies which highlight the information security responsibilities incumbent on all employees of the paying agency, clear statements of what is and is not considered good information security practice, and specific guidance covering remote working.

Human Resource Security

- 4.4.35. Scottish Government procedures require that background verification checks are carried out for all staff before an offer of employment is made. These include verification of identity and nationality, criminal records checks and, where appropriate, immigration checks.
- 4.4.36. We note, however, that during the year the paying agency identified that the principal contractor developing the new RP&S IT system was found to be confirming security clearance for contract and sub-contract staff without ensuring that necessary security checks had been undertaken. This was identified by the paying agency itself and action was taken to rectify the situation. As these staff were necessary to the development of the new RP&S IT system the decision was taken to retain them but to ensure that a full programme of retrospective checks, including criminal records checks, was undertaken.
- 4.4.37. A Disciplinary Policy on the acceptable use of SG and Agency facilities and IT systems, and an Access Control Policy are in place.

Asset Management

- 4.4.38. The SG's Software and Hardware Asset Management Strategy lays out the paying agency's responsibility specifically for the software assets owned and acquired for their exclusive use, and to meet the obligation to comply with the principles set out by the Federation Against Software Theft (FAST). We confirmed that individuals with access to systems agree to an IT Code of Conduct. The strategy is due for a refresh, to reflect changes brought about by the implementation of the new Futures IT system.
- 4.4.39. Hardware assets are owned, configured and issued by ISIS to all SG agencies. All asset movements (hardware/software), acquisitions and disposals are routed to the paying agency's Asset Manager.
- 4.4.40. During 2016 the paying agency developed a local policy to ensure the appropriate classification and treatment of information assets (documents and electronic records) in accordance with UK Government Secure Classification policy.

Access control

- 4.4.41. We have reviewed the Access Control Policy, Clear Desk Policy, and procedures on registration and deregistration, passwords, application access, new starts, movers and leavers, and line manager guidance.
- 4.4.42. Password policies for SCOTS network access are set by SG and are in line with best practice. Application standards are in line with those established by SG.
- 4.4.43. SIACS and RP&S access controls for SG staff are linked to user SCOTS accounts and for delegated bodies staff, sign on is via their user accounts for their respective organisations. Sign-on is achieved via an Oracle single sign-on procedure linked to the active directory for each organisation's network.

- 4.4.44. During 2016 the paying agency introduced a local “Systems Access Control Policy”, outlining controls over access to systems. This provides for access rights based on business needs and security requirements on a minimum access basis. Access to information is subject to physical and logical segregation. Access to information, system functions and documentation is controlled by user profile.
- 4.4.45. During interim testing of the new RP&S IT system certification body staff identified that access to the system was not properly controlled through the use of read and write passwords. On investigation the paying agency determined that this issue was restricted to audit staff (Certification Body and Internal Audit) and the matter was promptly rectified. We have made a minor recommendation in this regard.

Cryptography

- 4.4.46. Within the SG, the use of cryptographic controls to protect information has been considered at a corporate level. All staff wishing to send information out with the Public Sector Network, including those of the paying agency, are required to comply with these corporate policies.
- 4.4.47. A range of data encryption methods are available to meet the needs of those sending information including encrypted email, data discs or memory sticks and secure file transfer protocol for large files. All corporate laptop and tablet devices are protected by drive encryption software, pre-installed by ISIS prior to distribution for use.

Physical and Environmental Security

- 4.4.48. Servers for the AFRC IT system are securely located/ hosted within the Tier 3 SG data centre, which is subject to strict access controls. The data centre has a range of effective physical and environmental measures to prevent loss and/or damage to servers – including physical security measures, air conditioning, smoke detection and fire suppression systems.
- 4.4.49. As part of disaster recovery and business continuity procedures all critical SG IT Infrastructure servers are protected by an uninterruptible power supply (UPS), this includes critical business application servers owned by the paying agency.
- 4.4.50. Physical security controls are largely provided by the SG as the paying agency is housed in SG premises. The measures in place include security guards, doors and turnstiles with key pad entry and intrusion detection systems. Access to data centres within the secure area is controlled by pin access. Air conditioning, back up generator and uninterruptible power supply are in place for critical SG IT infrastructure servers (including those for the paying agency).
- 4.4.51. Automatic password locked screensavers are employed to protect unattended equipment. Users are required to lock their screens when leaving terminals. Work stations and terminals automatically blank and lock their display after a short period of inactivity and require authentication by the active user to re-gain access.
- 4.4.52. During 2016 the paying agency introduced a new, AFRC specific, Information Security Physical and Logical Environment Policy. This covers physical and logical environment security for AFRC sites, Data Centres and new facilities. This policy sets out the responsibilities of staff and managers to comply and ensure compliance with the principals contained in the policy.

Operations Security

- 4.4.53. The paying agency’s IT systems continue to operate within the boundary of the SG’s SCOTS environment and many aspects of operations management are governed by SG corporate policies and practices. All paying agency hardware and systems are deployed within the boundaries of the SCOTS network. A Memorandum of Understanding is in place with ISIS undertaking responsibility for managing the primary and secondary data

centres that host the paying agency's IT systems and servers, and providing, managing and protecting the SCOTS environment.

- 4.4.54. A key corporate SG focus during 2016 has been the general strengthening of defences against cyber threats. A joint Audit Scotland/ internal audit review, undertaken as part of the audit of the SG concluded that 'the SG has systems in place to identify and mitigate the risks associated with threats to the SG's IT and information systems'.
- 4.4.55. SG corporate policies are the prime authority with regard to operations management and security. However, the paying agency has, as a part of its pursuit of ISO 27001 certification, developed a number of additional policies which set the corporate requirements in a paying agency context. These include policies covering Systems Access Control Policy, Physical and Logical Environment and Change Management.

Communications Security

- 4.4.56. It continues to be the case that paying agency systems operate within the SG's SCOTS network environment. The operation and effectiveness of network communication controls is independently assessed on an annual basis by the UK Cabinet Office to allow the SG to maintain its connection to the UK Public Services Network (PSN).
- 4.4.57. The control areas covered under the PSN are in line with ISO 27001 requirements, and cover, Operational Security, Authentication and access control, Boundary protection and interfaces, Protecting data at rest and in transit, User and administrator separation of data, Users, and Testing your security (an annual IT health check).

System Acquisition Development and maintenance

- 4.4.58. 2016 was the first year that the paying agency's new RP&S IT system was used to process claims. The development of the RP&S IT system has been subject to lengthy delays. Pressure to make the system available in time to support applications resulted in a less than perfect release being implemented.
- 4.4.59. In May 2016 the Auditor General for Scotland issued the report "Common Agricultural Policy Futures Programme; An update". This report highlighted issues with the delivery of the IT system. In particular:
- the system opened on time for applications but, for the first six weeks, was slow and did not function as effectively as users needed. Errors in the IT infrastructure and software had to be fixed during the application period;
 - software to process and validate applications was still being developed when the applications period closed. This software continues to be in development to date;
 - manual interventions had to be put in place to select the required 1,300 farm inspections because the software was not ready in time.
- 4.4.60. We note that delays in the development of the software have continued to impact on the business as usual status of the paying agency. In particular:
- the paying agency was not able to provide beneficiaries with details of their entitlements by 1 April 2016 as required by Article 18 of Regulation (EU) No. 639/2014. Letters detailing final entitlements were not issued until November 2016, however, applicants registered on RP&S were able to access their entitlements earlier;
 - the system processed claims on an iterative basis, users did not have a readily available audit trail to information prior to the current status of the claim (i.e. initial claim submission, previous amendments);
 - significant difficulty was experienced in developing the Inspection Preparation and Performance application. Results from the programme of inspections were manually uploaded to the system to facilitate payments;

- the system was unable to provide information required for the production of the control statistics for 15 July 2016 as required by Article 9 of Regulation 809/2014;
- due to the emphasis on making Pillar 1 payments the paying agency was unable to make payments for a significant number of schemes under Pillar 2 within the financial year.

4.4.61. Issues with design specification, contractor performance, build quality and meeting delivery targets severely impacted on the paying agency's ability to make payments within the appropriate payment windows. This meant that the paying agency had to resort to instalments and nationally funded loans to reduce the impact of the delays on beneficiaries.

Supplier Relationships

4.4.62. The SG corporate Information Security Management framework directly influences all aspects of the paying agency including supplier relationships. Most purchasing is done through SG framework agreements controlled centrally by SG Procurement Commercial Directorate and there is little direct purchasing by the paying agency.

4.4.63. The Auditor General for Scotland's report highlighted a number of weaknesses in the internal and external supplier relationships surrounding the contract for the development of the new RP&S IT system. These contributed to the performance and build quality issues, and the delays in production, which severely impacted on the paying agency's operations.

Information Security Incident Management

4.4.64. We reviewed the SGRPID ISSP, Network Security Policy, Administrative and Procedural Security Policy and the Incident Management Policy, as well as incident management procedures and supporting forms.

4.4.65. We confirmed that any security incidents arising within AFRC are reported centrally and action taken in line with the policy in place. An Incident Log and a bespoke mailbox are in place to record all information security incidents.

4.4.66. During the course of our audit we noted two information security incidents which, in our view, should have been recorded in the paying agency's information security incident log. Subsequent to these incidents and as part of its progress towards an ISO 27001 ISMS, the paying agency has improved its local information security management procedures, providing clearer guidelines about incident classification through local training. This has resulted in a higher level of general awareness and improved reporting of incidents.

4.4.67. Whilst noting these improvements we are of the view that record keeping could be improved further and that a consistent naming convention and approach to summarising the nature of information security incidents would facilitate management review and trend analysis of causes.

Information Security aspects of Business continuity management

4.4.68. The paying agency's systems are hosted on the Scottish Government's SCOTs environment. This is maintained by ISIS which is responsible for business continuity and disaster recovery provisions. As the auditors of the SG, the certification body undertook a review of the services provided by ISIS. The review concluded that backup and contingency arrangements were satisfactory and that security policies and network security were satisfactory.

4.4.69. We note that, in terms of paying agency specific measures, improvements have been introduced as part of the drive towards achieving accreditation under ISO 27001. In particular we note that individual Business Continuity Plans, detailing potential threats and proposed responses, have been prepared for each local office.

4.4.70. For 2016 the consideration of business continuity and disaster recovery relating to paying agency developed systems has been extended to include the new RP&S IT system. However, many aspects of the paying agency's business still rely on the continuing operation and ready availability of some legacy systems. We note that comprehensive (integrated) business continuity arrangements still need to be developed and tested. We also note that no element of the IT Disaster Recovery plan has been subject to testing in 2016. There is a risk that system recovery may not be achieved in the required timescale and that plans may not be appropriately designed.

Compliance

4.4.71. We have confirmed that appropriate information security policies, referencing standards, guidance and the need for compliance with statutory and regulatory obligations, are in place. All staff are required to comply with an IT Code of Conduct which includes specific references to legislation including, the Data Protection Act 1998, Defamation Laws, Copyright Laws and the Computer Misuse Act 1990. This is reinforced by an information security user handbook. We note that the paying agency has implemented a Legal Compliance Policy to promote high ethical standards in its operational activities.

4.4.72. The paying agency utilises the SG's Data Handling Policy and sets out how the organisation should manage and handle information to ensure its security and appropriate use. The policy details both the organisational and legal requirements surrounding the use of SG information within the paying agency and other departments. The paying agency has also introduced policies covering the classification, control and destruction of information.

ISO 27001 Certification

4.4.73. Regulation (EU) No. 907/2014 Annex 1 3B(ii) requires that from 16 October 2016, a paying agency's information system security should be certified in accordance with ISO27001: Information Security management systems – Requirements (ISO).

4.4.74. The paying agency received confirmation that it had achieved certification on 16 December 2016.

4.4.75. With regard to the paying agency's ISO 27001 certificate the certification body makes the following observations:

- the scope of the ISO27001 certification covers only those systems directly operated by the paying agency to receive and process claims and does not extend to systems operated and maintained by the Scottish Government (e.g. email, data storage, ledger accounting and bank payments), or those maintained by delegated bodies. The certification body understands that the Scottish Government operates and maintains its Information Security Systems in accordance with ISO27002: Code of Practice for Information Security controls (ISO). However, the certification body notes that there is no independent verification of the adherence to this standard by these bodies;
- a number of the policies and procedures on which the ISO27001 certification is based are new or recently revised and their practical application has yet to be demonstrated;
- due to its on-going development the paying agency's new IT system is not yet fully complete and continued review will be required to ensure that all appropriate Information System Security controls continue to be applied as the system evolves.

Recommendations

4.4.76. Our joint review of Information Communication: Information Systems Security has identified some minor recommendations which have been reported in our management letter

Assessment

4.4.77. In our opinion, the scoring for this component is 3.

Monitoring: Ongoing monitoring via internal control activities

Findings

4.4.78. We reviewed the paying agency's on-going monitoring via internal control activities, completing the following procedures:

- an examination of the role of the paying agency's Accreditation Committee, which is chaired by the Accountable Officer and has overall responsibility for financial management, monitoring compliance with regulations, system developments and follow-up of our recommendations;
- a review of the Accreditation Committee minutes and supporting papers for the current year;
- a review of arrangements for developing and implementing changes to key IT systems;
- a review of exception reporting as part of systems evaluation work and compliance testing;
- a review of the inspection regime operated by the paying agency's technical services including the application of OTSCs (paragraph 4.3.11 refers);
- a review of the paying agency's fraud response strategy; and
- attendance at the meetings of the relevant Scottish Government Audit and Risk Committee which has oversight responsibility for the paying agency's activities.

4.4.79. We reviewed a sample of the monthly scheme manager reports presented to the Accreditation Committee, by the scheme managers with responsibility for the Basic Payment Scheme, Livestock Schemes, Cross Compliance and Mapping & Land Services. Overall, we consider that the Committee is generally provided with adequate information to support its review of Accreditation criteria.

4.4.80. Our review of meeting minutes and a sample of other supporting papers highlighted that, there is no formal, documented process to demonstrate on-going review of compliance with the accreditation criteria prescribed in Annex 1 of Regulation (EU) 907/2014 in particular with regard to services provided by internal audit.

4.4.81. The Accreditation Committee reviews Scheme Manager's Reports documenting the status of each scheme throughout the year. The requirement is for these reports to be submitted to each meeting of the Committee. We noted that one area, the Direct Payments Team, reports failed to submit regular reports in 2016..

4.4.82. The Direct Payments Team, along with a number of other schemes was highlighted as being "red" (high) risk. We note that, other than the Scheme Manager's reports, which are high level summaries, the Accreditation Committee does not clearly document its scrutiny of risks identified, the mitigating actions and the outcomes to help drive improvement.

4.4.83. We found that the paying agency's Fraud Strategy and Fraud Response was based on the overarching arrangements established by the Scottish Government. The Fraud Response is articulated in the Scottish Government Finance Manual (SPFM) and in the Staff Handbook. The SG's Fraud Response and Staff Code of Conduct are intended to address the risk of internal fraud. The paying agency has yet to implement a specific Fraud Response, and provide training to staff, to mitigate the risk of internal fraud and external frauds.

- 4.4.84. The paying agency's normal practice is to undertake quality Management Checks (QMCs) for land and livestock inspections to ensure that they are completed and recorded appropriately. Delays in delivery of the RP&S system, alternative payment mechanisms and an incomplete audit trail have prevented the effective completion of these checks in 2016. This translates into a risk around overpayments and irregularities as the current approach does not promote early identification of potential widespread problems and/or non-compliance.
- 4.4.85. Problems with the RP&S IT system meant that the paying agency did not submit the full suite of required control statistics reports by the 15th July 2016 deadline. Final submission of the EAGF statistics was made January 2017, sections 6.6 & 6.7 refer.

Recommendations

- 4.4.86. We have included a number of minor recommendations in our management letter.

Assessment

- 4.4.87. In our opinion, the scoring for this criterion is 3.

Monitoring: Separate evaluations via an internal audit service

Findings

- 4.4.88. We reviewed the paying agency's on-going monitoring via internal audit activities, following the requirements of Commission Delegated Regulation (EU) No. 907/2014 [Annex I Section 4(B)]. We have reviewed plans and report and maintained on-going liaison with Internal Audit throughout the audit period. A summary of reports issued by Internal Audit and reviewed by the Certification Body are included in Annex 2.
- 4.4.89. Audit Scotland's Scottish Government external audit team has undertaken an assessment of the internal audit function which is provided to the Scottish Government Rural Payments and Inspection Division (SGRPID) by the Scottish Government Internal Audit Directorate (IAD). The review covered the range and quality of work carried out by internal audit. Overall it concluded that the IAD continues to comply with Public Sector Internal Audit Standards. However, the review highlighted that IAD continued to face resource pressures in 2015/16 with further demands and competing priorities, particularly in relation to its European funds audit work. The review also noted that until resourcing is addressed fully, there is a risk to the successful delivery of the internal audit plan and the assurances that those charged with governance require.
- 4.4.90. As part of our planning work we reviewed the IAD 2015/16 audit plan for the paying agency and considered where we planned to place reliance on their work, subject to satisfactory progress being made against the intermediate recommendation made in our 2015 report.
- 4.4.91. In our 2015 report we reported that, due to the transition between the old and new programmes IAD had not prepared a 5 year plan to demonstrate how it would provide appropriate assurances over the period of the CAP. This should be supported by an annual plan, based on the Funds accounting year to ensure timeous reporting and that adequate resources were in place to allow the completion of the planned work. IAD's response indicated that an outline 5 year plan had been produced which was to be discussed with the paying agency's management.
- 4.4.92. We reported that, whilst it is appropriate for IAD to utilise a risk based approach to aspects of their plan, there are a number of obligations which must also be addressed to provide management assurances as to the working of the system of internal control. In order to ensure that the assertions in the Management Declaration are adequately supported the

internal audit plan should ensure that on an annual basis, adequate coverage is given to the following:

- Key controls: Detailed testing of key controls provides a snapshot in time as to whether controls are operational. Whilst assurances can be taken from work performed in prior years the quality of this assurance diminishes over time. It is important that key controls (as defined by the EC) are covered on a cyclical basis throughout the period of the IAD plan; this should cover those controls in operation at Local Action Groups and delegated bodies. In between cyclical reviews IAD should confirm on a regular basis that there have been no significant changes in the systems of internal controls; and
- Delegated Bodies: In the annual report to the Director in support of the Management Declaration for the year to 15 October 2015, internal audit took account of assurances provided by the internal auditors of Scottish National Heritage and Forestry Commission Scotland. However, the work of these third parties was not subject to review to ensure that staff with appropriate skills and experience were deployed, and that the scope and quality of the work undertaken was sufficient to support the assurances provided.

4.4.93. We concluded that, in view of the absence of key controls work and the limited scope of other work included within the 2015 internal audit plan, we would not place reliance on internal audit for the purposes of our 2015 audit. We also concluded that we did not consider the scope of the work planned by IAD was sufficient to provide adequate assurances for the Management Declaration for the year ending 15 October 2015.

4.4.94. Our 2015 report included an intermediate recommendation that management addressed promptly the issues raised, in order to ensure that the work of IAD provides appropriate and sufficient assurances to support the Management Declaration in future years.

4.4.95. The Certification Body notes that IAD has taken steps to address the matters raised, in particular:

- a five-year plan has been prepared and agreed by the paying agency's Accreditation Committee in August 2016. A review of the annual and 5 year plans indicates that key controls within headquarters and area offices will be covered throughout the period of the CAP including those controls in operation at local action groups and delegated bodies
- IAD's work plan has been adjusted to reflect the EAGF and EAFRD accounting year; and,
- a strategic review of IAD has resulted in greater resources being allocated to the paying agency aspects of IAD's work.

4.4.96. The Certification Body notes the steps taken to address the previously reported weaknesses in the internal audit arrangements. We note, however, that these changes occurred late within the 2016 accounting year and, in our view, require a further period of time before their effectiveness can be demonstrated. The Certification Body will continue to monitor progress.

4.4.97. The development and implementation of the paying agency's new IT system, RP&S, has been on-going for a number of years (since 2013) and has experienced and continues to experience significant problems. IAD has not reported on any of the system design and development issues that have been experienced.

4.4.98. The Certification Body has identified that IAD has been represented on boards responsible for the delivery of RP&S, namely the Futures Project Management Board (from 2013 until December 2016) and the Futures Executive Steering Committee (from December 2016). The terms of reference of these boards record IAD representatives as being full voting members. Their role on a further board, the Futures Delivery Board, is

less clearly defined, although minutes of these meetings report IAD attendance at some meetings. Over a period of time, IAD were represented on these boards by a number of individuals of varying seniority, although attendance by each individual was sporadic.

- 4.4.99. The Auditor General for Scotland reported in the May 2016 report, the *Common Agricultural Policy Futures Programme: an update*, that programme governance had not been effective. Significant decisions were made outwith the programme governance structures. The minutes of the board meetings do not clearly evidence when decisions were made. It is clear that IAD have placed themselves in a situation of potential conflict of interest. However, there is no evidence to suggest that IAD representatives influenced decisions in a way that compromised their independence.
- 4.4.100. The Certification Body acknowledges that IAD has now taken action to remove itself from these Boards.
- 4.4.101. **The Certification Body notes that IAD has taken immediate steps to address this potential conflict of interest and recommends that it adopts appropriate procedures to ensure that it remains demonstrably independent of the paying agency's other departments. (Classification: Intermediate)**

Assessment

- 4.4.102. In our opinion, the scoring for this criterion is 2.

5. Substantive Testing of Operational and Non-Operational transactions

5.1. Introduction

- 5.1.1. In this section we provide for each strata an assessment of the substantive testing results. The error evaluation is included in section 1.6.1 for the Error Rate, in section 1.6.4 for the Incompliance Rate. We have attached a list of all items selected for substantive testing, in the format proposed by the Annex to Guideline No. 3 on Reporting Requirements.
- 5.1.2. Guideline No. 2 'Annual Certification Audit' outlines the audit procedures for the validation of legality and regularity of expenditure. Following Guideline No. 2, we have adopted an integrated sampling approach for accomplishing audit objectives 1 and 2.

5.2. Test results in respect of the EAGF IACS strata – Basic Payment Scheme (BPS) – error rate

Overview

- 5.2.1. Our sample selection of 154 items was based on Guideline No. 2, Annex 3.

Standard

- 5.2.2. As per Guideline No. 2 – Annual Certification Audit.

Work Done

- 5.2.3. We reviewed in total 154 transactions in respect of EAGF IACS (BPS), which comprised our step 1 sample of 40 OTSCs and an additional MUS sample of 114 items drawn from x-table information. The list of all cases appears in the Annex 3: Sample reviewed in substantive testing – EAGF IACS.

Assessment and Findings

- 5.2.4. As a result of our audit, we have identified no financial errors but have identified 18 hits with minor compliance failures for the Basic Payment Scheme strata. These are summarised in the table below:

Hit	Details	Absolute error area in ha	Absolute error extrapolated across whole farm (ha)	Outcome
4	4 minor compliance failures: Technical assessment area increased reducing eligible area; rock pile missed; boundary movement; exclusion	0.114	0.524	No financial impact on the claim because claimant limited by entitlements
7	1 minor compliance failure: Incorrect exclusion of a midden resulting in area being reinstated	0.056	0.208	No financial impact on the claim because claimant limited by entitlements
9	1 minor compliance failure: Area of river excluded was incorrect; area between fences deemed white space i.e. ineligible.	0.106	0.186	No financial impact on the claim because claimant limited by entitlements

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Hit	Details	Absolute error area in ha	Absolute error extrapolated across whole farm (ha)	Outcome
10	1 minor compliance failure: Size of technically assessed area incorrect	0.046	0.127	No financial impact on the claim because claimant limited by entitlements
12	1 minor compliance failures: Boundary change along river bank, ordnance survey line had been used.	0.049	0.148	No financial impact on the claim because claimant limited by entitlements
18	1 minor compliance failure: The boundary was found to be incorrect because inspector had used Ordnance Survey lines which differed from actual boundary.	0.035	0.167	No financial impact on the claim because claimant limited by entitlements
19	1 minor compliance failure: Track removed by inspector on original inspection was found to be completely green on re-verification, added back in.	0.023	0.228	No financial impact on the claim because claimant limited by entitlements
21	2 minor compliance failures: Water feature wider than 2 metres had been included in eligible area; river between 2 merged parcels had been part of technical assessment but should have been fully removed with remaining area being technically assessed.	0.059	0.535	No financial impact on the claim because claimant limited by entitlements
23	1 minor compliance failure: Area of parcel was found to be ineligible on re-verification; Technical assessment area missed in parcel.	0.360	0.506	No financial impact on the claim because claimant limited by entitlements
25	1 minor compliance failure: Technical assessment on an area of bracken identified that incorrect area had been assessed along with incorrect banding.	0.099	0.435	No financial impact on the claim because claimant limited by entitlements
27	1 minor compliance failure: Remapping required along boundary as boundary from original inspection was beyond the actual boundary.	0.020	0.127	No financial impact on the claim because claimant limited by entitlements
28	1 compliance failure: The banding applied to a technical assessment was too high.	0.178	0.421	No financial impact on the claim because claimant limited by entitlements
31	1 compliance failure: Area of land was excluded but was found to be eligible, increasing eligible area	0.018	0.018	No financial impact on the claim because claimant limited by entitlements
34	1 minor compliance failure: Boundary had not been moved to fence. Movement increased eligible area	0.113	1.405	No financial impact on the claim because claimant limited by entitlements
35	2 minor compliance failures: A track that had been excluded was found to eligible and was reinstated. Change to move boundary onto new fence rather than ordnance survey	0.033	0.038	No financial impact on the claim because claimant limited by entitlements

Hit	Details	Absolute error area in ha	Absolute error extrapolated across whole farm (ha)	Outcome
	line. Reduction in eligible area			
37	2 minor compliance failures: Technical assessed areas had used wrong area and bandings; Track excluded from original inspection but found to be eligible.	0.449	1.066	No financial impact on the claim because claimant limited by entitlements
38	3 compliance failures: Track excluded by original inspection was fully green on re-verification. Track reinstated; the banding used for technical assessment of gorse was too high, reduced which increased eligible area; boundary found to be incorrect at re-verification and adjusted to reduce eligible area.	1.534	4.060	No financial impact on the claim because claimant limited by entitlements
40	4 compliance failures: Technical assessments with incorrect bandings applied; land cover error between FM and NFC; land incorrectly excluded; boundary changes	0.393	0.399	No financial impact on the claim because claimant limited by entitlements

Recommendations

5.2.5. We have not made any recommendations.

5.3. Test results in respect of the EAGF IACS strata – Livestock – error rate

Overview

5.3.1. Our sample selection of 30 items was based on Guideline No. 2, Annex 3.

Standard

5.3.2. As per Guideline No. 2 – Annual Certification Audit.

Work Done

5.3.3. We reviewed in total 30 transactions in respect of EAGF IACS (Livestock), which comprised our step 1 sample of 26 OTSCs re-verifications and an additional MUS sample of 4 items drawn from x-table information. The list of all cases appears in the Annex 3: Sample reviewed in substantive testing – EAGF IACS.

Assessment and Findings

5.3.4. For the **Scottish Suckler Beef Support Scheme and the Scottish Upland Sheep Scheme**, as a result of our audit, we have identified 6 hits with minor compliance failures, of which 1 resulted in a financial error for the Livestock strata. These are summarised in the table below:

Hit(s)	Details	Outcome
2, 7 & 16	<p>Area Office inspection reports</p> <p>For three of the claims sampled the Inspection report, prepared by the Area Office, contained discrepancies when compared to the producer's records i.e. the Inspector added incorrect dates of birth, DAM numbers and in one instance an incorrect (but still eligible) breed had been noted by the farmer.</p>	Compliance failures, no financial impact
15, 20	<p>Incomplete inspection packs</p> <p>On two occasions the inspection packs used by the Area Offices did not include a claimed animal; therefore, the animal had to be verified during the re-verification work conducted by Audit Scotland.</p>	Compliance failures, no financial impact
21	<p>Animal failed eligibility check</p> <p>The auditor was unable to confirm the death date added by the paying agency's inspector during the re-verification visit as there was no record noted within the producer's herd register. Further, there was no independent third party evidence to verify the 30 day retention period. Therefore, the claimed animal is not eligible and a penalty in line with scheme guidance should have been imposed.</p>	Compliance failure and financial impact Error resulted in a €204.13 overpayment

5.3.5. As part of our step 2 testing we identified 6 hits where the inspection results were not taken into consideration when making the payment calculation. Details are summarised below:

Hit(s)	Details	Outcome
1	During inspection two of the nine SSBSS claimed animals were found to have had their dates of birth altered in order to obtain a passport; therefore, a cross compliance and administrative penalty is applicable [the cross compliance penalty will be applied against 2016 SAF claims]. Nonetheless, although only seven SSBSS animals were eligible it was established that the beneficiary received a payment for nine calves with no administrative penalty applied.	Overpayment This equates to a €408.24 overpayment after financial discipline
4	273 animals were verified within RP&S; however, it was established that four of the 2015 SSBSS claimed animals were not eligible as they had died before reaching the minimum 30 day retention period i.e. assumed worse case scenario the animals could not be presented during the inspection. Therefore, an administrative penalty is applicable in line with scheme guidance. The actual payment made was based on 273 calves with no penalties.	Overpayment This equates to a €816.49 overpayment
6	77 animals were validated by RP&S. Payment should have been based on the 76 eligible calves. Further, an additional admin penalty was due to a tagging breach i.e. no replacement tag was ordered prior to inspection, was also applicable and not factored within the calculation.	Overpayment In total the above payment errors resulted in a €204.12 overpayment.
11	Eleven animals were not presented at the inspection with no prior notification of deaths etc. This results in a Level 2 breach i.e. less than 10%; therefore, the payment should be reduced by the error rate of 2% (11/613). However, the actual payment made was based on 624 animals with no administrative penalty applied.	Overpayment This translates into an overpayment of €1,696.18
15	There were 140 eligible animals; however, payment was based on 139 livestock. The discrepancy relates to a BCMS passport issue	Underpayment This equates to a €102.06 underpayment
17	The RP&S system only validated 209 of the 210 claimed animals as eligible for payment. However, following an inspection it was determined that the animal was deducted in error	Underpayment This equates to a €102.06 underpayment

Recommendations

- 5.3.6. We have made a minor recommendation regarding the treatment of overpayments and this is included in our management letter.

5.4. Overall test result of EAGF population

- 5.4.1. There are a number of errors identified from our work on EAGF IACS BPS and livestock strata. These have been documented in section 5.2 and 5.3 above.

5.5. Test results in respect of the EAGF IACS Basic Payment Scheme strata – non-compliance rate

Overview

- 5.5.1. Our sample selection of 154 was based on Guideline No. 2, Annex 3.

Standard

- 5.5.2. As per Guideline No. 2 – Annual Certification Audit.

Work done

- 5.5.3. We reviewed in total 154 transactions in respect of EAGF IACS Basic Payment Scheme strata, including 40 OTSC re-verifications following the requirements of the standard as stated above.

Assessment and Findings

- 5.5.4. As a result of our audit, we have identified 18 hits with non-compliance errors. None of these resulted in a financial error because in each case the claimant was limited by entitlements. The issues reflected in section 5.2 above remain applicable here.
- 5.5.5. However, we are not able to provide a non-compliance rate due to inadequacies in the control statistics provided by the paying agency.

Recommendations

- 5.5.6. We have not made any recommendations.

5.6. Test results in respect of the EAGF IACS strata – Livestock – incompliance rate

Overview

5.6.1. Our sample selection of 30 items was based on Guideline No 2, Annex 3

Standard

5.6.2. As per Guideline No. 2 – Annual Certification Audit.

Work done

- 5.6.3. We reviewed in total 30 transactions in respect of the EAGF IACS Livestock, including 26 OTSC re-verifications. Our sample of OTSCs selected for audit re-verification is based on the criteria for small populations, as defined in Guideline No. 2 – Annual Certification Audit.
- 5.6.4. For beef, we agreed animals claimed on the claim form(s) to the paying agency's inspection pack, which is drawn from the BCMS records. Where animals were still on the holding, animal passport details were agreed to the IBI pack and we confirmed that scheme eligibility conditions were met for animals claimed under the scheme. We reconciled IBI details to the Farm Register maintained by the beneficiary.
- 5.6.5. We attended 2 live inspections to observe the inspection process and to check the paying agency's procedures for agreeing the ear tags details to the IBI pack.
- 5.6.6. For sheep, we agreed animals claimed on the claim form(s) to the paying agency's inspection pack, which is drawn from the SAMU records. Where animals were still on the holding, animal passport details were agreed to the inspection pack and we confirmed that scheme eligibility conditions were met for animals claimed under the scheme. We reconciled inspection pack details to the Farm Register maintained by the beneficiary.
- 5.6.7. Annex 4: Incompliance Rate – EAGF (Livestock) contains a detailed list of all transactions checked and the detected errors, including their financial value.

Assessment and Findings

5.6.8. Our work did identify some compliance errors and these are documented in section 5.3 above.

Recommendations

5.6.9. We have not made any recommendations.

5.7. Test results of non-operational transactions

5.7.1. For each of the audited populations, an assessment of the results of our testing is provided. The error evaluation is included in section 1.4.1 above. The findings are further detailed below.

Test results of tables of Annex II – Irregularities

Standard

5.7.2. Annex I, 2 E of Commission Delegated Regulation (EU) No. 907/2014 and chapter 5.4 of Guideline No. 1. – "Accreditation" and Guideline No. 5 on the submission to the Commission of the Annexes II and III of Commission Implementing Regulation (EU) No. 908/2014.

Work Done

- 5.7.3. Annex 7 contains a detailed list of all transactions tested and the detected errors, including their financial value.
- 5.7.4. Guideline No 2 permits the merging of the EAGF and EAFRD populations for non-operational transactions, where it can be demonstrated that debt movements are managed using a common system. The debt management system operated by the paying agency is common to EAGF and EAFRD. We have therefore merged the EAGF and EAFRD populations for substantive testing of non-operational transactions.
- 5.7.5. Annex 3 to Guideline No.2 indicates that non-operational transactions such as debts' movements are not suitable for statistical sampling. The Annex provides recommended sample sizes based on inherent risk, assurance levels and the debtor population size. Based on this recommended approach, we have reviewed 28 items value: £8,164.78 (EU principal element) as listed in Annex 7.
- 5.7.6. A sample of 30 items was selected for compliance testing, as required by Annex 3 to Guideline No. 2. This section reports our findings in relation to EAGF debts. Our findings in relation to EAFRD debts are disclosed at section 12.8.

Assessment and Findings

- 5.7.7. The paying agency has reported total EAGF Annex II debts at 15 October 2016 of £536,511.38 and total EAFRD Annex II debts at 15 October 2016 of £209,670.51.
- 5.7.8. We examined a total of 28 debtor entries (2 EAGF and 26 EAFRD), auditing all relevant entries across the Annex II columns as indicated in the error evaluation at Annex 7.
- 5.7.9. We are satisfied that the paying agency is correctly splitting debtors between the respective funds and is properly accounting for administrative debts.
- 5.7.10. We have not identified any errors and we are satisfied that the Annex II presented by the paying agency is true, complete and accurate in all material respects.

Recommendations

- 5.7.11. We have not made any recommendations.

Test results on Tables of Annex III

Standard

- 5.7.12. Annex I, 2 E of Commission Delegated Regulation (EU) No. 907/2014 and chapter 5.4 of Guideline No. 1. – "Accreditation" and Guideline No. 5 on the submission to the Commission of the Annexes II and III of Commission Implementing Regulation (EU) No. 908/2014.

Work Done

- 5.7.13. Annex 7 contains a detailed list of all transactions tested and the detected errors, including their financial value.

Assessment and Findings

- 5.7.14. The UK authorities include debts arising from cross-compliance breaches within the Annex II table. The Annex III table contains only details of multi-annual sanctions, which have not been subject to testing. For further information please see section 6.3.
- 5.7.15. Annex 7 contains a detailed list of all transactions tested and the detected errors, including their financial value.

Recommendations

5.7.16. We have not made any recommendations.

6. Reconciliation of Monthly and Annual Declarations

6.1. Reconciliation of monthly and annual declarations of EAGF expenditure

Standard

6.1.1. To verify whether the final monthly indent (final table 104) agrees with the annual declaration for the 2016 EAGF financial year.

Work done

6.1.2. We have verified the differences and explanations in the electronic "diff." table provided by the paying agency.

6.1.3. In addition, we assessed the Administrative Errors declared in the Monthly Declarations and those declared separately in the Annual Declaration. We also verified that the amount of administrative errors are not included in the Annex II and Annex III tables, and we also reviewed whether these have been credited to the Fund, i.e. introduced as a negative amount in the Monthly or Annual Declarations.

Findings

Table 6.1: Reconciliation of EAGF Annual Account

Budget post	Final Monthly Indent €	Annual Account €	Difference €
05 02 15 06 2320 019	64,324.22	64,324.22	0.00
05 03 01 01 0000 032	76,825.43	76,825.43	0.00
05 03 01 01 0000 056	4,223.36	4,223.36	0.00
05 03 01 01 0000 071	4,102.86	4,102.86	0.00
05 03 01 01 0000 072	6,582.87	11,020.22	4,437.35
05 03 01 01 0000 073	277,037.97	277,037.97	0.00
05 03 01 10 0010 001	2,614,031.10	2,615,224.89	1,193.79
05 03 01 10 0010 002	249,130,674.02	246,361,052.52	-2,769,621.50
05 03 01 10 0010 003	58,258,338.09	58,761,534.15	503,196.06
05 03 01 10 0010 007	0.00	300,297.57	300,297.57
05 03 01 10 0010 008	0.00	2,743.81	2,743.81
05 03 01 11 0000 001	9,024,406.88	9,028,706.52	4,299.64
05 03 01 11 0000 002	146,469,122.29	147,049,393.16	580,270.87
05 03 01 13 0000 001	32,413.04	34,413.04	2,000
05 03 01 13 0000 002	1,985,991.36	1,988,976.25	2,984.89
05 03 02 44 0000 081	2,880.61	2,880.61	0.00
05 03 02 44 0000 082	119.04	119.05	0.01
05 03 02 44 0000 096	5,997.56	7,527.36	1,529.80
05 03 02 44 0000 097	94,548.63	94,548.63	0.00

Budget post	Final Monthly Indent €	Annual Account €	Difference €
05 03 02 60 0000 001	508,945.74	700,818.40	191,872.66
05 03 02 60 0000 002	48,459,996.82	48,286,943.69	-173,053.13
05 03 02 99 0000 339	0.00	-110.60	-110.60
05 03 02 99 0036 050	112.83	112.83	0.00
05 03 02 99 0036 116	1,290.75	1,290.75	0.00
05 03 09 00 0000 002	6,302,351.55	6,326,026.77	23,675.22
05 04 01 14 0000 001	0.00	-95,384.59	-95,384.59
67 02 00 00 0000 001	0.00	-266,077.15	-266,077.15
67 02 00 00 0000 002	0.00	-124,876.17	-124,876.17
67 02 00 00 0000 010	-95.02	-95.02	0.00
67 02 00 00 0000 014	0.00	-119.32	-119.32
67 02 00 00 0000 016	-26,232.33	-26,113.01	119.32
67 02 00 00 0000 018	-693,095.69	-719,542.62	-26,446.93
	-----	-----	-----
Total	522,604,893.98	520,767,825.58	-1,837,068.40
	=====	=====	=====

6.1.4. The differences are explained as follows:

- | | | |
|----|-----------------|--|
| 1) | - €1,810,707.71 | Due to pay over of administrative debt |
| 2) | - €13.69 | Due to rounding |
| 3) | €417,098.14 | Due to cut off (timing) error |
| 4) | - €81,703.69 | Due to payment error (payment pending in the bank) |
| 5) | €29,322.47 | Due to late payment correction in annual declaration |
| 6) | - €92,019.77 | Due to off-set of irrecoverable amount (50/50 rule) |
| 7) | - €298,933.55 | Due to correction for recovery of outstanding debts |
| 8) | - €110.60 | Due to modulation not declared |

Administrative Errors

6.1.5. We can confirm that the Administrative Errors have been refunded. The total amount included in the declarations amounts to:

Table 6.2: EAGF reported administrative errors

Administrative Errors (reported/deducted)	Amount (€)
1. Annual Declaration i.e. reported in 13 th period (as a difference between Final Monthly Indent and Annual Account).	-1,810,707.71
2. Monthly Declarations	0.00

Assessment

6.1.6. We can confirm that the provided electronic "diff." table is complete and accurate, and the explanations given are valid and justified.

Recommendations

6.1.7. We have not made any recommendations.

6.2. Reconciliation of annual declaration and X-table data of EAGF accounts

Standard

6.2.1. To verify whether the annual declaration agrees with the X-table data for the 2016 EAGF financial year.

Work done

6.2.2. We have reviewed the completeness, accuracy, and relevance of the electronic "diff." table provided by the paying agency.

Findings

Table 6.3: Reconciliation of Matrix and EAGF Annual Account

Budget post	Matrix (€)	Annual Account (€)	Difference (€)
05 02 15 06 2320 019	0.00	64,324.22	64,324.22
05 03 01 01 0000 032	76,825.42	76,825.43	0.01
05 03 01 01 0000 056	4,223.36	4,223.36	0.00
05 03 01 01 0000 071	4,102.86	4,102.86	0.00
05 03 01 01 0000 072	6,375.00	11,020.22	4,645.22
05 03 01 01 0000 073	277,089.03	277,037.97	-51.06
05 03 01 10 0010 001	2,626,752.36	2,615,224.89	-11,527.47
05 03 01 10 0010 002	247,870,222.74	246,361,052.52	-1,509,170.22
05 03 01 10 0010 003	58,842,723.60	58,761,534.15	-81,189.45
05 03 01 10 0010 007	300,297.57	300,297.57	0.00
05 03 01 10 0010 008	2,743.81	2,743.81	0.00
05 03 01 11 0000 001	9,047,918.24	9,028,706.52	-19,211.72
05 03 01 11 0000 002	147,237,589.24	147,049,393.16	-188,196.08
05 03 01 13 0000 001	34,413.01	34,413.04	0.03
05 03 01 13 0000 002	1,988,976.27	1,988,976.25	-0.02
05 03 02 44 0000 081	2,880.61	2,880.61	0.00
05 03 02 44 0000 082	96.51	119.05	22.54
05 03 02 44 0000 096	5,997.56	7,527.36	1,529.80
05 03 02 44 0000 097	94,548.73	94,548.63	-0.10

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Budget post	Matrix (€)	Annual Account (€)	Difference (€)
05 03 02 60 0000 001	700,818.40	700,818.40	0.00
05 03 02 60 0000 002	48,288,266.45	48,286,943.69	-1,322.76
05 03 02 99 0000 339	0.00	-110.60	-110.60
05 03 02 99 0036 050	112.82	112.83	0.01
05 03 02 99 0036 116	1,290.75	1,290.75	0.00
05 03 09 00 0000 002	6,303,276.94	6,326,026.77	22,749.83
05 04 01 14 0000 001	0.00	-95,384.59	-95,384.59
67 02 00 00 0000 001	-332,596.44	-266,077.15	66,519.29
67 02 00 00 0000 002	0.00	-124,876.17	-124,876.17
67 02 00 00 0000 010	0.00	-95.02	-95.02
67 02 00 00 0000 014	0.00	-119.32	-119.32
67 02 00 00 0000 016	0.00	-26,113.01	-26,113.01
67 02 00 00 0000 018	0.00	-719,542.62	-719,542.62
	-----	-----	-----
Total	523,384,944.84	520,767,825.58	-2,617,119.26
	=====	=====	=====

6.2.3. The differences are explained as follows:

- 1) - €1,810,707.71 Due to pay over of administrative debt
- 2) - €10.90 Due to rounding
- 3) - €51.00 Due to misposting error
- 4) €64,570.36 Due to cut off error (amount in annual declaration but not in matrix)
- 5) - €96,282.10 Due to payment error (payment pending in the bank)
- 6) €29,672.90 Due to a late payment correction in annual declaration
- 7) - €92,019.77 Due to offset of irrecoverable amount (50/50 rule)
- 8) €248,623.32 Due to 25% retention on amounts resulting from cross compliance
- 9) €66,519.28 Due to 20% retention on amounts recovered following irregularities
- 10) - €110.60 Due to old modulation not declared
- 11) - €1,027,323.04 Due to adjustments for cross compliance and multi annual sanctions

Assessment

6.2.4. We can confirm that the electronic "diff." table is complete and accurate, and the explanations given are relevant and justified.

Recommendations

6.2.5. We have not made any recommendations.

6.3. Reconciliation of the information required by Annex II and Annex III of Commission Implementing Regulation (EU) No. 908/2014 to the debtors' ledger – EAGF

Standard

- 6.3.1. To reconcile the closing balances of the previous financial year to the opening balances of the current financial year in respect of the debtors' ledger and the Annex II and Annex III tables.
- 6.3.2. To reconcile the data reported in Annex II and Annex III of Commission Implementing Regulation (EU) No. 908/2014 to the debtors' ledger in respect of the current financial year.
- 6.3.3. The UK Authorities consider that debts arising from cross-compliance breaches should be treated in the same manner as other claimant irregularities. These are therefore included, as agreed with the UK Co-ordinating Body, in the main Annex II declaration. Consequently the Annex III table contains only details of multi-annual sanctions. By agreement with the UK Co-ordinating Body we have not reconciled the contents of the Annex III table, however we can confirm that we are satisfied with the reasonableness of these figures.

Work done

- 6.3.4. We have reviewed the reconciliation of the closing balances of the previous financial year to the opening balances of the current financial year in respect of Annex II and the debtors' ledger.
- 6.3.5. We have reviewed the reconciliation of the data reported in Annex II of Commission Regulation (EC) No. 908/2014 to the debtors' ledger in respect of the current financial year.

Findings

Table 6.4: Reconciliation closing balance 2015 / opening balance 2016

	Closing balance 2015 (as at 15/10/15) £	Opening balance 2016 (as at 16/10/15) £	Difference £
Annex II	462,552.48	462,552.48	0
Debtors' ledger	462,552.48	462,552.48	0

- 6.3.6. We have reconciled the closing balances of the previous financial year to the opening balances of the current financial year in respect of Annex II and the debtors' ledger. We can confirm that there are no discrepancies.

Table 6.5: Reconciliation of Annex II and Annex III to the debtors' ledger

	Balance 16 October £	New cases £	Recovered amounts £	Corrected amounts £	Interest £	Total non-cleared amounts declared irrecoverable £	Amounts to be recovered by 15 October £
Annex II	462,552.48	346,739.00	-264,904.17	-6,661.51	705.79	-1,920.21	- 536,511.38
Annex III	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Debtors' ledger	462,552.48	346,739.00	-264,904.17	-6,661.51	705.79	-1,920.21	- 536,511.38
Differences	0	0	0	0	0	0	0
Explanation	n/a	n/a	n/a	n/a	n/a	n/a	n/a

6.3.7. There are no differences between Annex II and the debtors' ledger.

6.3.8. We furthermore confirm that the closing balances mentioned on the summary tables of, respectively, Annex II and Annex III (amounts to be recovered as at 15 October 16) tally with the sum of:

- Opening balances (amounts to be recovered as at 16 October 15 for respectively Annex II and Annex III)
- + New cases
- + / - corrected amounts
- – Recoveries
- – Irrecoverable amounts.

Confirmation of "50/50 tables"

6.3.9. As part of our tests on Annex II, we reviewed the tables established by the paying agency setting out the amounts to be borne by the Member States according to the 50/50 rule as well as the amounts to be borne in full by the EU budget due to being irrecoverable. We confirm the figures mentioned in the table below:

Table 6.6: Confirmation of "50/50 tables"

Paying Agency	50% to be charged to the Member State (Article 54(2) of Regulation (EU) No. 1306/2013 £	100% to be borne by the EU budget (Article 54(3) of Regulation (EU) No. 1306/2013 £
EAGF	63,158.10	1,920.21

Assessment

6.3.10. We confirm that the amounts mentioned in the "50/50" tables are complete and accurate.

Recommendations

6.3.11. We have not made any recommendations.

6.4. Reconciliation of annual Table 104 to the Annex II and Annex III of Commission Implementing Regulation (EU) No. 908/2014

Standard

6.4.1. There must be a clear audit trail to support the reconciliation between the annual Table 104 and the Annex II and Annex III information.

Work done

6.4.2. We have reviewed both the adequacy of the procedures in place, and the outcome of the reconciliations.

Findings

Table 6.7: Reconciliation of recoveries per annual Table 104 and recoveries included in Annex II and Annex III

	€	€
Assigned revenue per annual Table 104 – Irregularities 80% (net amount) Budget sub-item 67 02 00 00 0000 001	-266,077.15	
+ Assigned revenue per annual Table 104 – Irregularities not subject to 20% retention Budget sub-item 67 02 00 00 0000 002	-124,876.17	
+ Assigned revenue per annual Table 104 – Cross-compliance (75%)– net amount Budget sub-item 67 02 00 00 0000 006	-745,869.97	
+ Assigned revenue collected under one of the following budget sub-items 67 02 00 00 0000 55 to 71	0.00	
Total (1) = recoveries as per Table 104	-1,136,823.29	
Recoveries in Annex II	-332,596.44	
+ Recoveries in Annex III	n/a	
Total (2)		-332,596.44
Difference (2) – (1)		-804,226.85

6.4.3. Discrepancies between the amounts listed in the above table and the amounts indicated in the final Annex II provided by the paying agency are explained as follows:

1. 20% of retention related to revenue assigned on budget sub-item 67 02 00 00 0000 001: - €66,519.29
2. Multi-annual sanctions not subject to retention assigned on budget sub-item 67 02 00 00 0000 002: €870,746.14
3. Other differences: 0.00

Assessment

6.4.4. We can confirm that, except for the explanations listed above, the amounts recorded in the table 104 agree to the recoveries recorded in the Annex II.

Recommendations

6.4.5. We have not made any recommendations.

6.5. Confirmation of advances

6.5.1. Nil return.

6.6. Review of IACS statistics – area-related aid schemes to be provided on 15 July 2016 (claim year 2015) as referred to in Article 9(1) of Commission Implementing Regulation (EU) No. 809/2014

Objective

6.6.1. To assess the reconciliation of the paying agency for the control statistics reported under area-related aid schemes managed by the IACS (aid schemes under EAGF covered by the IACS, i.e. support schemes under EAGF established under Annex I of Regulation (EU) No. 1307/2013 of the European Parliament and of the Council as referred to in Article 67 of Regulation (EU) No. 1306/2013 of the European Parliament and of the Council), and provided to the Commission in the framework of Article 9(1) of Regulation (EC) No. 809/2014

Work done

6.6.2. The paying agency was unable to transmit the BPS control statistics (including greening and Young Farmer elements) before the 15th July 2016 due to issues with the new IT system. The paying agency submitted BPS in January 2017

6.6.3. In order to assess the compilation and transmission of the BPS control statistics we sought to

- assess the audit trail and agree the figures in the returns to the underlying data for on-the-spot-checks (inspections);
- confirm the arrangements in place at the paying agency for collating and analysing data and preparing the returns. We also confirmed that the returns had been prepared in accordance with relevant guidelines and explanatory notes;
- confirm that the paying agency undertakes a reconciliation of control statistics returns to the underlying database and that there were no unresolved discrepancies. We reviewed the relevant reconciliations prepared by the paying agency, and supporting documentary evidence, for reasonableness;
- complete a test check of the accuracy and completeness of data base entries, by comparing the database to the results of our Step 1 re-performance of on-the-spot-checks;
- trace a random sample of 20 inspection cases from the base data supporting the control statistics back to underlying database/records to ensure the information has been correctly recorded and therefore reported; and
- consider the completeness of the data and the return transmitted to the UK Co-ordinating Body.

Findings

6.6.4. The control statistics were extracted from the new RP&S system and were subject to significant delays by problems with the implementation of this system. Management sought to ensure that the completeness and accuracy of control statistics through manual checking of data. However they have been unable to confirm that the control statistics are complete

- 6.6.5. Our audit testing has identified a number of penalty cases which have not been included in the control statistics. We are unable therefore to conclude on the reliability of the data submitted by management.

Conclusion

- 6.6.6. We have been unable to confirm the completeness and accuracy of the submitted control statistics.

Recommendations

- 6.6.7. **The Certification Body recommends that the paying agency reviews the submitted control statistics to ensure their completeness and accuracy. (Classification: Intermediate)**

6.7. Reconciliation of IACS control statistics – animal aid schemes to be provided on 15 July 2016 (claim year 2015) as referred to Article 9(1) of Commission Implementing Regulation (EU) No 809/2014

Objective

- 6.7.1. To assess the reconciliation of the paying agency for the control statistics reported on animal aid scheme managed by the IACS and provided to the Commission in the framework of Regulation (EU) No. 809/2014.

Work done

- 6.7.2. In respect of the control statistics submitted to the UK Co-ordinating Body we have:
- assessed the audit trail and agreed the figures in the returns to the underlying data for on-the-spot-checks (inspections);
 - confirmed the arrangements in place at the paying agency for collating and analysing data and preparing the returns. We also confirmed that the returns had been prepared in accordance with relevant guidelines and explanatory notes;
 - enquired whether the paying agency undertakes a reconciliation of control statistics returns to the underlying database and that there were no unresolved discrepancies. We reviewed relevant reconciliations prepared by the paying agency, and supporting documentary evidence, for reasonableness;
 - completed a test check of the accuracy and completeness of data base entries, by comparing the database to the results of our Step 1 re-performance of on-the-spot-checks;
 - considered the completeness of the data and the return transmitted to the UK Co-ordinating Body.

Findings

- 6.7.3. We noted that, due to the delays in the implementation of the new RP&S system the paying agency was unable to submit the control statistics by 15 July as required. These were submitted on 17 January 2017.
- 6.7.4. Our detailed test check of the control statistics revealed a number errors.

Conclusion

6.7.5. We consider that the control statistics are not correctly completed.

Recommendations

6.7.6. We have made a minor recommendation which is included in our Management Letter..

6.8. Review of Non-IACS statistics – Regulation (EU) No. 1306/2013, Chapter III of Title V – Scrutiny of transactions – to be provided by 31 December each year

6.8.1. Nil return.

7. Other matters

7.1. Review of Financial Ceilings

Work done

- 7.1.1. We reviewed whether relevant procedures are in place to ensure that the total payments per budget line do not exceed the maximum financial ceilings.
- 7.1.2. Where measures are subject to quantitative limits, either in terms of total amounts paid, production or eligible areas, we have checked that procedures are in place to ensure that the total payments across all Paying Agencies are within these quantitative limits.
- 7.1.3. For the Basic Payment Scheme, the Commission has established the ceilings shown in Table 7.1 for the UK. These ceilings are set out in Council Regulation 1307/2013 as amended by Implementing Regulation 1089/2015. The UK authorities have translated these into individual country ceilings.

Table 7.1: National Ceilings

Budget item 2015	€'000
Redistributive payment	16,134
BPS	2,100,795
Greening	951,997
Young Farmer Scheme	51,798
Voluntary Coupled Support Scheme	52,600
UK Net National Ceiling	3,173,324

Conclusion

- 7.1.4. The UK Co-ordinating Body is responsible for the monitoring of the financial ceilings. For each scheme, it monitors the payments made and verifies the totals against the approved limits
- 7.1.5. The expenditure declared on Tables 104 is below the UK ceiling for each scheme year. UK expenditure is monitored on a monthly basis, with the amounts declared by each Paying Agency being compared to its regional ceiling.

Recommendations

- 7.1.6 We have not made any recommendations.

7.2. Basic Payment Scheme

Objective

7.2.1. We examined whether a proper system for the identification and registration of payment entitlements has been set up with regard to the Basic Payment Scheme (BPS) in accordance with Title III of Regulation (EU) No. 1307/2013.

Work done

7.2.2. As part of our Step 2 substantive testing, for a sample of 154, we re-verified the new payment entitlement values for BPS, using historic reference period data, and the number of entitlements. We are satisfied that the provisional values and number of entitlements were correctly allocated in the first year of the application for BPS.

7.2.3. Due to delays in the delivery of the RP&S system the paying agency was not in a position to establish and communicate the definitive number and value of entitlements to beneficiaries as at 1 April 2016 as required by Article 18 of Regulation (EU) 639/2014. Formal notices were issued to most beneficiaries in mid November 2016, however, beneficiaries registered on RP&S were able to access details earlier in the month.

Conclusion

7.2.4. The Certification Body notes the failure to establish and communicate the definitive number and value of entitlements. This relates to the first time allocation of payment entitlements under Article 24 of Regulation (EU) 1307/2013 therefore we have not made a recommendation in this regard. Except for this the paying agency system for identifying and registering BPS entitlements is satisfactory.

Recommendations

7.2.5. We have not made any recommendations.

7.3. Action Plans

Work done

7.3.1. We confirmed that the paying agency does not have an action plan in place for the EAGF.

Recommendations

7.3.2. Not applicable.

7.4. Follow-up of previous years' recommendations

7.4.1. The following tables include previous years' major and intermediate recommendations, the progress made against the outstanding recommendations, comments by the Paying Agency and the assessment of the response by the Certification Body. The follow-up of the financial errors is indicated in a separate table below.

Major recommendations

7.4.2. There were no major recommendations arising from our audit.

Intermediate recommendations

7.4.3. In respect of **accreditation** issues the situation is as follows:

Recommendation	Status	Response of Paying Agency	Position of the Certification Body
The Certification Body recommends that management takes action to address the inefficiencies inherent in the existing accounting processes and implements alternative processes, and procedures, which are fit for purpose.	Not implemented	Accepted and planning for this is already well underway.	The Certification Body has re-iterated its recommendation.
The Certification Body reported the absence of key controls work and the limited scope of other work included in the audit plan. The Certification Body recommends that management addresses promptly the issues raised, in order to ensure that the work of internal audit provides appropriate and sufficient assurances to support the Management Declaration in future years.	Implemented	In order to ensure that the work of DfIA provides appropriate and sufficient assurances to support the Management Declaration the Certification Body recommends that management addresses the issues raised in our report and implements the agreed action plan	The Certification Body notes the steps taken by management in this regard. These steps will take time to deliver the planned benefits. The Certification Body will monitor progress and report appropriately.
Review of Control Statistics Our comparison of underlying data to completed returns identified a significant number of errors within the return for the SBS. The errors occurred due to a combination of factors; figures were accurately transferred onto the return and misinterpretation of the data. Our findings resulted in the paying agency correcting the errors and the statistical return was re-submitted to the UK Co-ordinating Body	Not implemented	The paying agency has had significant issues in producing some of the control statistics data as mentioned elsewhere in this report. We were not able to fully implement these checks in 2016 but they will be incorporated into the planning for the 2017 returns.	The Certification Body notes the response and will review progress in 2017.

Recommendation	Status	Response of Paying Agency	Position of the Certification Body
on 14 January 2016. The paying agency accepts that completed returns should be subject to an independent check.			

7.4.4. There were no issues in respect of **conformity/legality and regularity**.

Financial errors

7.4.5. There were no financial errors in the EAGF IACS populations reported in our 2015 Report.

SECTION B – EAFRD

8. Executive Summary

8.1. Introduction

- 8.1.1. Following our appointment as auditors by the UK Co-ordinating Body acting on behalf of the UK Competent Authority, Audit Scotland has performed an audit of the Scottish Government Rural Payments and Inspection Division pursuant to Article 9 (2) of Regulation (EU) No. 1306/2013 of the European Parliament and of the Council in relation to its role as paying agency. This audit related to the paying agency's operation of the European Agricultural Fund for Rural Development (EAFRD) for the financial year ended 15 October 2016. The audit was undertaken in accordance with internationally accepted auditing standards and entailed consideration of the matters, set out in Article 5, paragraph 4 of Commission Implementing Regulation (EU) No. 908/2014.
- 8.1.2. We are also required to provide an opinion as to whether the annual accounts for the EAFRD year ended 15 October 2016 are a true, complete and accurate record of the amounts charged to the Fund, that the expenditure declared to the Fund is legal and regular and that the internal control procedures have operated satisfactorily. This opinion is contained in the Audit Opinion presented as section C of this report. We are further required to indicate whether our examination puts in doubt any assertions made in the management declaration. A separate section of the opinion deals with the Management Declaration.
- 8.1.3. Our work was performed in accordance with the requirements of Article 9 of Regulation (EU) No. 1306/2013 and Articles 5 to 7 of Commission Implementing Regulation (EU) No. 908/2014. The format of this report is also in accordance with the Commission Guidelines.
- 8.1.4. Our work covered the paying agency's compliance with the accreditation criteria, the existence and functioning of the key internal controls, and the procedures for ensuring compliance with EU rules, the legality and regularity of expenditure claimed for reimbursement from the Commission and the procedures for the protection of the financial interests of the Union. The findings and recommendations arising from our work are summarised in this Chapter and detailed under the relevant Chapters.
- 8.1.5. This report results primarily from the body of work undertaken by us since our appointment as a Certification Body to the paying agency in relation to the financial year ended 15 October 2016. Annex 1 to this Report contains a Glossary of Abbreviations used.

8.2. Conclusions

- 8.2.1. Article 5 (4) of Commission Implementing Regulation (EU) No. 908/2014, sets the questions which the Certification Body is required to respond to. These questions and our conclusions are set out below.

Table 8.1: Conclusions

Requirement per Article 5 of Regulation No. 908/2014	Conclusion
The paying agency complies with the accreditation criteria.	For our overall opinion in this respect, refer to the Audit Opinion (see also the internal control system). In general, the paying agency complies with the accreditation criteria. Key recommendations are summarised in subsections 8.8 and 8.9 below and are elaborated on in more details in the relevant sections of the report.
The paying agency's procedures are such as to give reasonable assurance that the expenditure charged to the EAFRD was effected in compliance with Union rules, thus ensuring that the underlying transactions are legal and regular, and that recommendations for improvements, if any, have been followed-up.	For details of our opinion in this respect see the Audit Opinion.
The annual accounts referred to in Article 29 (chapter III) of Regulation (EU) No. 908/2014 are in accordance with the books and records of the paying agency.	For details of our opinion in this respect see the Audit Opinion.
The statements of expenditure are a materially true, complete and accurate record of the operations charged to the EAFRD.	For details of our opinion in this respect see the Audit Opinion.
The financial interests of the Union are properly protected as regards amounts to be collected.	The completeness of Annex II/III is ensured and detailed observations are included in section 12 of the report.

8.3. Compliance with the Commission Guidelines

Table 8.2: Compliance with the Commission's Guidelines

Guideline	Conclusion
Guideline No. 1 on Accreditation	Our report complies with the Guideline.
Guideline No. 2 on the annual certification audit	Our report complies with the Guideline.
Guideline No. 3 – on the reporting requirements and opinions of the Certification Body.	Our report and opinion comply with the Guideline.
Guideline No. 5 on reporting irregularities	Our report complies with the Guideline.

8.3.1. Guideline No. 1 on accreditation and Guideline No. 4 on the Management Declaration were considered in carrying out our audit examination.

8.4. Overall assessment

8.4.1. The total financial error resulting from our audit is as follows:

Table 8.3: Overall error evaluation

Audit Steps	Established Errors	Amount Considered
Review of internal control system	Financial errors from compliance testing or assessment of internal control system (considered as known errors)	0.00
Validation of Legality and Regularity of expenditure	Financial errors from substantive testing – statistical sampling (Upper error limits + Known errors)	343,538
	Financial errors from substantive testing – non-statistical sampling (established error rate in monetary value)	0.00
	Other financial errors	0.00
Validation of accounts	Financial errors found in the reconciliation (considered as known errors)	0.00
Total Financial Impact		€ 343,538

8.5. Assessment of the internal control system and the compliance with the accreditation criteria

Standard

8.5.1. Our assessment is based on our review of the internal control system (ICS) of the paying agency, including its compliance with the accreditation criteria. It is summarised in the matrix below using the following assessment criteria:

(1) Not working. There is a clear non-respect of the accreditation criterion or there are serious deficiencies (the seriousness of the deficiencies are such that the paying agency cannot fulfil the tasks set out in Article 7 of the Regulation (EU) No. 1306/2013). Not all risks are addressed by controls and/or there are likely to be frequent control failures. The impact on the effective functioning of the key requirements is significant – the ICS functions poorly or does not function at all. The deficiencies are systemic and wide-ranging. As a consequence, no assurance can be obtained from the system. Scores = [1 – 1.5]

(2) Works partially. There are other deficiencies which do not fall under (1), but which would have to be followed-up according to Article 2 (1) of Commission Implementing Regulation (EU) No. 908/2014. All risks are addressed to some extent by controls but which are not always working as intended. The impact on the effective functioning of the key requirements is significant. Recommendations have been, or should be issued, and an action plan has been, or should have been put in place. Scores = [1.51 – 2.5]

(3) Works. Minor issues were detected but there is scope for improvement. All risks are adequately addressed by controls which are likely to operate effectively with some deficiencies having a low or moderate impact on the functioning of the key requirements. Recommendations have been formulated. Scores = [2.51 – 3.5]

(4) Works well. No deficiencies or only minor deficiencies were found. All risks are adequately addressed by controls which are likely to operate effectively. Scores = [3.51 – 4.0]

8.5.2. In cases where the procedure / component is not valid, it is indicated as not-applicable (N/A). Our assessment is partly based on reviews carried out in previous financial years, where we have confirmed that no major changes in the procedures / components have occurred; in such cases our assessment is indicated in brackets "()". As regards our assessment of the Internal Audit service, if certain areas are still to be audited by Internal Audit, we base our assessment on the adequacy of the five year audit plan. In such circumstances our assessment is also indicated in brackets "()".

Detailed Assessment

8.5.3. Matrix I and Matrix II below concerns schemes under EAFRD covered by the IACS, i.e. support schemes under EAFRD established under Chapter II of Title V (Articles 67 to 78) of Regulation No. 1306/2013 of the European Parliament and of the Council (refer to section 6.7.2 and Annex 5 of Guideline No. 2.). Matrix III below concerns schemes under EAFRD not covered by the IACS, i.e. support schemes under EAFRD established under Chapter III of Title V of Regulation (EU) No. 1306/2013 of the European Parliament and of the Council.

IACS

Matrix I - Assessment of the ICS for EAFRD IACS strata (RP&S)

MATRIX - Assessment of the ICS for EAFRD IACS [RP&S]																					
Assessment		Internal environment						Control activities		Information and Communication				Monitoring				Evaluation at assessment criteria		General conclusion	
		Organisation		HR		Delegation (**)				Communication		ISS		On-going monitoring		Internal audit					
Weighting / Scoring		S	T at 10% or 15%	S	T at 5%	S	T at 5%	S	T at 50%	S	T at 5%	S	T at 10%	S	T at 10%	S	T at 5%	W	T	Weighted total	
Operations	Claim processing including validation and authorisation	Administrative controls	2	0.20	2	0.10	3	0.15	2	1.00	3	0.15	2	0.20	2	0.20	2	0.10	20%	2.00	0.40
		On-the-spot controls	2	0.20	3	0.15	3	0.15	3	1.50	3	0.15	2	0.20	3	0.30	2	0.10	20%	2.75	0.55
Payments	Execution of payments		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Accounting		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Advances and securities (*)		N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	0.00
	Debts management		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59
General conclusion																				2,34	
Assessment of ICS														works partially (significant impact)							

Key to the table:

S – Score – should correspond to the assessments in Chapter 4

W – Weight given to each assessment criteria and the Internal Control System – corresponding to section 5.4 of Guideline No. 2

T – Total = Weight * Score

* – Scotland does not have any transactions for Advances & Securities. Guideline No.1 (section 4.2) corresponding % divided equally between Execution of Payments and Accounting

** – There are no delegated bodies in respect of Payments work. Weighting has been transferred to 'Organisation.

8.5.4. The overall assessment of the Internal Control System for the IACS population is **working partially**.

IACS

Matrix II - Assessment of the ICS for EAFRD IACS strata (SIACS)

MATRIX - Assessment of the ICS for EAFRD IACS [SIACS]																					
Assessment		Internal environment						Control activities		Information and Communication				Monitoring				Evaluation at assessment criteria		General conclusion	
		Organisation		HR		Delegation (**)				Communication		ISS		On-going monitoring		Internal audit					
Weighting / Scoring		S	T at 10% or 15%	S	T at 5%	S	T at 5%	S	T at 50%	S	T at 5%	S	T at 10%	S	T at 10%	S	T at 5%	W	T	Weighted total	
Operations	Claim processing including validation and authorisation	Administrative controls	3	0.30	3	0.15	3	0.15	3	1.50	3	0.15	2	0.20	2	0.20	2	0.10	20%	2.75	0.55
		On-the-spot controls	2	0.20	3	0.15	3	0.15	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.85	0.57
Payments	Execution of payments		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59
	Accounting		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40
	Advances and securities (*)		N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	0.00
	Debts management		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59
General conclusion																				2,70	
Assessment of ICS														works (medium impact)							

Key to the table:

S – Score – should correspond to the assessments in Chapter 4

W – Weight given to each assessment criteria and the Internal Control System – corresponding to section 5.4 of Guideline No. 2

T – Total = Weight * Score

* – Scotland does not have any transactions for Advances & Securities. Guideline No.1 (section 4.2) corresponding % divided equally between Execution of Payments and Accounting

** – There are no delegated bodies in respect of Payments work. Weighting has been transferred to 'Organisation.

8.5.5. The overall assessment of the Internal Control System for the Non-IACS population is **works**.

Non IACS

Matrix III - Assessment of the ICS for EAFRD Non-IACS

MATRIX - Assessment of the ICS for EAFRD Non-IACS																						
Assessment Component Procedure		Internal environment						Control activities		Information and Communication				Monitoring				Evaluation at assessment criteria		General conclusion		
		Organisation		HR		Delegation (**)				Communication		ISS		On-going monitoring		Internal audit		W	T			
Weighting / Scoring		S	T at 10% or 15%	S	T at 5%	S	T at 5%	S	T at 50%	S	T at 5%	S	T at 10%	S	T at 10%	S	T at 5%	W	T	Weighted total		
Operations	Claim processing including validation and authorisation	Administrative controls	3	0.30	3	0.15	3	0.15	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59	
		On-the-spot controls	3	0.30	3	0.15	3	0.15	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.80	0.56	
Payments	Execution of payments		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59	
	Accounting		2	0.30	3	0.15	N/A	0.00	2	1.00	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.00	0.40	
	Advances and securities (*)		N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	N/A	0.00	0.00	
	Debts management		3	0.45	3	0.15	N/A	0.00	3	1.50	3	0.15	3	0.30	3	0.30	2	0.10	20%	2.95	0.59	
General conclusion																						2.73
Assessment of ICS															works (medium impact)							

Key to the table:

S – Score – should correspond to the assessments in Chapter 4

W – Weight given to each assessment criteria and the Internal Control System – corresponding to section 5.4 of Guideline No. 2

T – Total = Weight * Score

* – Scotland does not have any transactions for Advances & Securities. Guideline No.1 (section 4.2) corresponding % divided equally between Execution of Payments and Accounting

** – There are no delegated bodies in respect of Payments work. Weighting has been transferred to 'Organisation'.

8.5.6. The overall assessment of the Internal Control System for the Non-IACS population is **works**.

Overall assessment of the Internal Control System

8.5.7. Our overall assessment of the internal control system and compliance with the accreditation criteria for the EAFRD is as follows:

Population / Strata	Assessment
EAFRD IACS strata – RP&S	Works partially
EAFRD IACS strata – SIACS	Works
EAFRD Non-IACS	Works

8.6. Detailed Error Evaluation

Error evaluation – Operational gross expenditure – IACS strata and Non-IACS population – Error rate

8.6.1. Our error evaluation of the statistical sample populations is outlined below:

Table 8.4: EAFRD statistical sample error evaluation – error rate

Basic data	EAFRD IACS-SIACS €	EAFRD IACS-RP&S €	EAFRD NIACS €	EAFRD Total €
Amount of gross expenditure	7,796,790	7,572,885	7,527,675	22,897,350
Materiality				457,947
Population size	6,842	2,485	850	10,177
Sample size	60	43	30	133
Financial errors found from sampling				
According to Annex 9				
• Number of Formal errors				9
• Number of Substantive errors				8
Extrapolated most likely error				165,768
Known errors				784.72
Total most likely error				166,553
Total Upper Error Limit				343,538
Materiality				457,947

8.6.2. A detailed table of all cases checked and the detected errors including their financial value is attached (see Annex 9: Sample reviewed in substantive testing – EAFRD) to this report.

8.6.3. We also attach (in Annex 10: Reconciliation of gross amount of tested expenditure to the Annual Declaration) a summary of the budget lines which reconcile to the gross amount of expenditure declared and tested, apportioned for both IACS and Non-IACS populations.

8.6.4. **Overall conclusion** – It is our opinion that the detected formal errors have no financial consequences, and that these are not of a recurrent nature. These errors are explained in more detail in chapter 12.

Evaluation of Incompliance rate – IACS strata and Non-IACS population

8.6.5. Our evaluation of the incompliance rate for the same statistical sample strata and population is outlined below:

Table 8.5: EAFRD statistical sample error evaluation – non-compliance rate

Basic data	EAFRD IACS Total €
Amount of gross expenditure	41,090,464
Materiality	821,809
Population size	14,343
Sample size	42
Financial errors found from sampling	
According to Annex 9	
• Number of Formal errors	9
• Number of Substantive errors	42
Extrapolated most likely error	4,430,491
Known errors	
Total most likely error	4,430,491
Total Upper Error Limit	1,539,919
Materiality	821,809

8.6.6. A detailed table of all cases checked and the detected errors including their financial value is attached (see Annex 11: Non-compliance Rate – EAFRD IACS) to this report.

8.6.7. **Overall conclusion** – It is our opinion that the errors identified have resulted in a breach of materiality. Details of the work undertaken can be found in section 12.6.

Evaluation of residual risk

EAFRD IACS

8.6.8. In the example below taking into consideration the non-compliance rate calculated and the overall evaluation of the internal control system we conclude on a residual risk greater than 2%:

Assessment of internal control system	2 Works partially
PA's error rate (control statistics, Management Declaration)	1.97%
Non-compliance rate	MLE & UEL >2 %
Evaluation of the residual risk	Risk is material; Results of control statistics cannot be confirmed

EAFRD Non IACS

8.6.9. For EAFRD Non-IACS no non-compliance rate can be calculated related to the 2016 audit sample, as the on the spot verifications done by the certifying body have covered FY 2016 payments and not the whole period of the control statistics that was of calendar year 2015. In our opinion the Management Declaration is based on the assessment of the internal control system, and the review of the reconciliation of the control statistics.

Assessment of internal control system	3 Works
Review of reconciliation of control statistics	Refer to conclusion in section 13.7

Certifying error rate for reduction of control rate

8.6.10. In accordance with Article 41 of Regulation (EU) No. 908/2014 2014 for the purpose of reduction of the control rate the error rate for the concerned population needs to be certified. For claim year 2016, we have tested 36 files of the random OTSC sample of the paying agency, of which only 3 of these fed through to payment in the year and therefore the controls statistics. We identified errors on all 3 hits, please refer to Annex 11.

8.6.11. Our evaluation is reflected in the Opinion.

Error evaluation – Non-statistical population – operational expenditure

8.6.12. There are no transactions within a non – statistical population.

Error evaluation – Non-operational expenditure: debts, advances and securities

8.6.13. As regards debts our detailed error evaluation is provided in Annex 6. Based on this evaluation the error rate established at the level of Annex II Table is 0%.

8.6.14. The UK authorities include debts arising from cross-compliance breaches within the Annex II table. The Annex III table contains only details of multi-annual sanctions, which have not been subject to error evaluation. For further information please see section 13.3.

8.6.15. A detailed table of all cases checked and the detected errors including their financial value is attached (see Annex 7: Sample reviewed in substantive testing – EAGF and EAFRD Annex II Tables) to this report.

8.6.16. The paying agency has no transactions in relation to advances and securities.

8.6.17. **Overall conclusion** not applicable

8.7. Nature of Findings

8.7.1. Our work resulted in a number of findings which led to various recommendations. We have categorised these findings and recommendations into two groups – accreditation findings and legality and regularity findings. For each finding, a level of importance was attributed in accordance with the following grading.

8.7.2. The categories we used to classify our findings in respect of **accreditation** issues are as follows:

Major Findings	Matters which require immediate attention by the Competent Authority and the Head of the paying agency (see to Guideline No. 1 in respect of accreditation).
Intermediate Findings	Matters which concern the general control environment and require prompt attention at a senior level within the paying agency and the Competent Authority – i.e. grade (2) in the accreditation matrix.
Minor Findings	Minor issues highlighted, which require attention at an appropriate level within the paying agency – i.e. grade (3) in the accreditation

	matrix.
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8.7.3. The categories we used to classify our findings in respect of the **legality and regularity of expenditure** are as follows:

Major Findings	Matters relating to weaknesses in the Key Controls – which require immediate attention at a senior level within the paying agency.
Intermediate Findings	Matters relating to weaknesses in the Ancillary Controls – which require prompt attention at an appropriate level within the paying agency.
Minor Findings	Matters relating to other weaknesses which require attention at an appropriate level.

8.7.4. Recommendations related to minor findings are (in principle) not included in this report but are communicated separately to the paying agency's management in our overall letter of recommendations. A list of minor recommendations is available to the Commission on request.

8.8. Major Findings

8.8.1. There were no major findings arising.

8.9. Intermediate Findings

8.9.1. We have identified a number of issues giving rise to intermediate recommendations. Which are applicable to EAGF and EAFRD. The findings have been reported in section 1.9.

8.9.2. There are no findings established in respect of legality and regularity issues.

9. Audit Strategy of the Certification Body

9.1. Summary of Audit Strategy and Audit Plan

Audit scope and objectives

9.1.1. Under Article 5 of Commission Regulation (EU) No. 908/2014, the Certification Body is required to prepare a separate audit certificate opinion for each of the paying agencies stating that it has gained reasonable assurance that the Accounts submitted to the European Commission are in all material respects true, complete and accurate. The Certification Body is also required to prepare a Report in accordance with Guideline No.3 Audit assurance and materiality.

Audit assurance and materiality

9.1.2. We based our assessment of the internal control system on the previous year's report adjusted to reflect the development and implementation of the new IT system. Our work was planned in accordance with the provisions of Commission Regulation (EU) No. 908/2014 and related European Commission Guidelines. In line with Guideline No.2 "Annual Certification Audit", the reporting materiality threshold was set at 2 per cent of declared net expenditure excluding clearance decisions. We have also adopted the confidence level of 95% for reporting suggested by the Commission's Guidelines. That is, our audit opinion will provide 95% assurance that the accounts in all material respects give a true, complete and accurate record of operations charged to the accounts. This is consistent with our audit approach generally. For planning and statistical sampling purposes materiality was set at 2% of positive expenditure for each population.

Systems and controls

9.1.3. The Audit Strategy describes the main systems and controls in detail. This is available on request. The systems in place and the control framework for the paying agency feature four main procedures:

- **authorisation of payments** – comprising administrative controls (involving detailed checking and authorisation of claims based on established checklist and segregation of key functions, often enforced under computerised systems) and on-the-spot controls (involving pre-payment and post-payment checks, including on-the-spot physical checks, and the examination of claimant and producer records);
- **execution of payments** – these are standardised and involve checks to confirm that only authorised claims are passed for payment and that payment is properly effected;
- **accounting for payments** – controls over ledger postings and the reconciliations against feeder systems and to bank; they also include controls over the transmission and reconciliation of the quarterly declarations of expenditure;
- **recognition of debts** – comprising controls relating to the recognition of all amounts due and the recording of all such debts in a debtors' ledger.

Risk assessment

9.1.4. We performed risk assessment procedures to identify and assess the significant risks of material misstatement. Our risk assessment included the following work:

- we gained an understanding of the entity and its control environment, including the applicable legal and regulatory framework in place. We considered risks identified in prior periods for each measure involving a material level of expenditure. We reviewed the findings of the EC and ECA and the actions taken by the paying agency in response to any observations;

- we gained an understanding of the principle control activities and the information systems, including the main processes. This included procedures and controls regarding the performance of the on-the-spot-inspections and other physical checks to confirm whether the Commission's regulatory requirements relating to the quantity and detail of the checks have been achieved;
- we assessed any changes to the internal control system since the last audit. We assessed the impact of changes in the organisational and procedural arrangements since the previous audit, thereby indicating the extent to which the paying agency continues to meet the accreditation criteria;
- we assessed the effectiveness of risk management, and identified controls addressing the key risks, including fraud risks;
- we reviewed the paying agency's arrangements to establish whether controls operated by third parties are in accordance with scheme requirements, satisfy accreditation criteria and that the controls are of an appropriate standard. We also considered the effectiveness of the paying agency's monitoring of Delegated Bodies;
- we reviewed the paying agency's procedures for operating its debtors ledger and for accounting for recoveries and other negative expenditures. The control risk in respect of recoveries and debtors is low as a result of improved systems and management practices.

The audit approach

- 9.1.5. Our audit approach was to assess the risk of significant monetary error capable of affecting the annual accounts being present and tailor the nature, timing and scope of the audit accordingly. We reviewed and assessed the homogeneity of controls over the transactions to determine the number of strata and/or populations. For each strata and/or population we documented the controls over the schemes and evaluated these controls through walk through testing. We carried out detailed compliance testing and assessed whether we could rely on the controls. We also took into account our previous experience of the paying agency and the fact that it has been fully accredited since 1995. From this we determined the extent to which we needed to take assurance from substantive testing.
- 9.1.6. Having reviewed and assessed the homogeneity of controls over the transactions we determined the following populations:
- EAFRD IACS – Population 1
 - EAFRD NIACS – Population 2
- 9.1.7. Our initial strategy reflected the paying agency's intention that all EAFRD land based schemes would be processed through the new IT system. The paying agency was introducing a number of new schemes and was unable to estimate their potential uptake. The Certification Body was therefore unable to use MUS to select its step 1 sample and used random sampling instead.
- 9.1.8. As a result of the delays in the delivery of the new IT system the paying agency used a combination of the new system (RP&S), the old IACS system (SIACS) and manual workarounds to process EAFRD land claims. We therefore adjusted our strategy for step 2 testing to reflect the new circumstances. Having re-assessed the controls over transactions we determined the following strata and populations:
- EAFRD IACS – Strata 1: IACS system (RP&S)
 - EAFRD IACS – Strata 2: IACS system (SIACS)
 - EAFRD NIACS – Population 1
- 9.1.9. As our step 1 sample was selected using random sampling our step 2 sample was also selected in this manner. We selected an initial sample of 30 transactions from each

strata. Analysis of testing results required further top up samples of 10 cases for (EAFRD IACS strata 1 – RP&S), and 30 cases for (EAFRD IACS – SIACS).

Re-verification of on-the-spot controls

- 9.1.10. The paying agency uses classical GPS methodology to determine and validate areas claimed. Article 71 of Regulation (EU) 809/2014 permits paying agencies to sample half of all parcels at each holding for the purposes of on-the-spot-checks. The paying agency for Scotland normally inspects all parcels at each holding.
- 9.1.11. For each farm location selected for re-verification, we selected 10 parcels from the original inspection. Our step 1 re-verification of on-the spot-checks involved a review of inspection files and checklists prepared by inspectors in addition to physical re-verification of inspections using the paying agency's inspectors and GPS equipment. The timing of re-verification was subject to full completion of the original inspection including inspection file paperwork and availability of paying agency inspectors and audit staff.

The nature and extent of the CB's reliance on the work of Internal Audit

- 9.1.12. In arriving at our opinion on the EAFRD Account we have taken account of the results of the statutory audits of the paying agency's accounts. We have also considered the agreed findings of the Commission's Services. We have reviewed Internal Audit reports and liaised with them throughout the audit. We did not, however, place reliance on their work.

Any assumptions and estimations made during the course of the review

- 9.1.13. We have followed the guidelines in all areas and made no contrary assumptions during the course of the review. Our step 1 sample of on-the-spot-checks was drawn from the population of claims submitted by beneficiaries, using a random number sampling technique.

Plan of audit activities

- 9.1.14. We reviewed the paying agency's procedures governing scheme design and scheme control reviews and the controls governing the implementation of changes in Commission Regulations to establish whether they are implemented promptly.
- 9.1.15. We carried out detailed compliance testing and assessed the extent to which we could rely on the controls. Our compliance and substantive testing was carried out on the same sample in accordance with the provision for dual testing set out in section 5.3 of Guideline No. 2.
- 9.1.16. We reviewed the general control environment and considered compliance with the Accreditation Criteria.
- 9.1.17. We reviewed the paying agency's procedures and controls regarding the performance of on-the-spot inspections to establish whether the Commission's regulatory requirements relating to the quantity and quality were achieved. We re-verified samples of on-the-spot-checks in accordance with Guideline No. 2 to establish whether the paying agency's arrangements for ensuring the Legality and Regularity of claims were appropriate.
- 9.1.18. We reviewed the paying agency's arrangements to establish whether controls carried out by third parties are in accordance with scheme requirements and that evidence exists to verify that the controls are of an appropriate standard. We also considered the effectiveness of the paying agency's monitoring of Delegated Bodies.
- 9.1.19. Guideline No. 2 permits the merging of the EAGF and EAFRD populations for non-operational transactions, where it can be demonstrated that debt movements are managed using a common system. The debt management system operated by the paying agency is common to EAGF and EAFRD. We have therefore merged the EAGF and EAFRD populations for substantive testing of non-operational transactions.

- 9.1.20. We reviewed the paying agency's arrangements for operating its debtors' ledger and for accounting for recoveries and other negative expenditures. We tested whether debts are recognised promptly and accurately recorded in the paying agency's books of account. We also performed focused testing on balances disclosed in the Annex II Tables to ensure they comply with the Commission's requirements.
- 9.1.21. In addition, we also tested the completeness of the record of debts by checking that the Annex II included, where necessary, the cases with financial errors identified in the:
- review of the control statistics;
 - re-verification of on-the-spot-checks; and
 - substantive testing of expenditure.
- 9.1.22. We reviewed the controls in place over statistical returns, financial ceilings, and entitlements as well as a follow-up of previous years' recommendations.
- 9.1.23. Our Audit Strategy is available to the Commission upon request.
- 9.1.24. **Assessment:** Our overall assessment of the functioning of the internal control systems and compliance with the accreditation criteria, including an indication of the level of assurance required from the substantive testing and the related sample sizes, are set out below.

Table 9.1: Summary of expenditure populations and assurance levels (EAFRD)

Population / Strata	Inherent Risk High (100%)/not high (60%)	Assurance required from substantive testing (confidence level required)	Expected Error Rate	Minimum sample size (appendix 3.1 of annex 3)
EAFRD – IACS	High 100%	Works partially (70%)	10-15%	*n/a
EAFRD – Non-IACS	High 100%	Works partially (70%)	10-15%	*n/a

(* Para. 9.1.9 refers)

9.2. Work done

9.2.1. The audit was carried out based on the three strata in relation to which the nature and rigour of the detailed compliance and substantive tests differed. The testing done on each strata is outlined in the table below:

Table 9.2: Outline approach to each population

Population	DOC	AR	CT	ST	OR	CRM	IAS	2016 Expenditure € / £
1) EAFRD IACS								€ 18,972,387
Authorisation – on-the-spot controls	√		√		√			
Authorisation – administrative controls	√		√	√				
Execution of payments	√		√	√				
Accounting	√		√	√				
3) EAFRD – Non-IACS								€ 7,520,998
Authorisation – on-the-spot controls	√		√		√			
Authorisation – administrative controls	√		√	√				
Execution of payments	√		√	√				
Accounting	√		√	√				
4) Debtors – EAFRD	√		√	√	n/a			£ 209,670.51

Note	
DOC:	Scheme documentation and walkthrough
AR:	Analytical review, discussion
CT:	Compliance testing of procedures and controls
ST:	Substantive testing of selected files
OR:	On-the-spot controls re-verification
CRM:	Computer risk management based system testing using Computer Assisted Audit Techniques
IAS:	Review of Internal Audit Service reports

9.3. Other Matters

9.3.1. The audit team of the Certification Body in respect of the EAGF and EAFRD is set out in section 2.3.

10. Accreditation of the Paying Agency

10.1. Institutional framework

10.1.1. The functions of the Competent Authority, as stipulated in Article 1(2) of Commission Delegated Regulation (EU) No 907/2014, and the Co-ordinating Body, are held by the Secretary of State for Environment, Food and Rural Affairs, the Scottish Ministers, the Welsh Ministers and the Department of Agriculture, Environment and Rural Affairs in Northern Ireland, acting jointly. The legal basis for the Competent Authority and the Co-ordinating Body is by way of Statutory Instrument No. 3260 of 2014.

10.2. Accreditation status of the Paying Agency

10.2.1. The Scottish Government Rural Payments and Inspection Division (SGRPID) was established and accredited as a paying agency by the UK Competent Authority on 16 October 1995. As a paying agency previously accredited in accordance with Commission Regulation (EU) No. 1663/1995, SGRPID was formally re-accredited in accordance with Articles 1.3 and 17.1 of Commission Regulation 885/2006 with effect from 16 October 2007. It is one of four accredited UK Paying Agencies under EC legislation. The Instruments of Appointment to accredit all UK Paying Agencies are held by the UK Co-ordinating Body, which also monitors the implementation of relevant corrective actions.

11. Compliance with Accreditation Criteria – Review of the Internal Control System

11.1.1. This section outlines the current status of the accreditation and provides the basis for the overall assessment of the internal control system and for our assessment in respect of the paying agency's compliance with the accreditation criteria per internal control procedure / component as indicated in the matrices. We have assessed the compliance with the accreditation criteria by using the grading "1" to "4". Our overall assessment is outlined in section 8.5 above.

11.2. Compliance testing – Control Activities

11.2.1. We confirmed our assessment of the accreditation procedures against the control activities by carrying out the following compliance tests as suggested in Guideline No. 2:

Procedure	IACS	Non-IACS	Findings
Administrative controls	20	10	Paragraphs 11.3.3 – 11.3.16
On-the-spot controls	36	9	Paragraphs 11.3.17 – 11.3.25
Payment procedures	20	10	Paragraphs 11.3.26 – 11.3.29
Accounting procedures	4 quarterly returns	4 quarterly returns	Paragraphs 11.3.30 – 11.3.31
Advances/securities	N/A	N/A	N/A
Procedures for debts	30 *		Paragraphs 11.3.33 – 11.3.34

*Debtors for EAGF and EAFRD are managed under a common administrative system. We have tested the minimum required sample of 30 items for both Funds (EAGF 4 and EAFRD 26).

11.2.2. In line with Section 1.2 of Annex 3 to Guideline No. 2, where the Certification Body does not expect to find exceptions, the minimum sample size at Fund level is 30 items. We have tested the minimum required sample of 30 items at Fund level, to assess the paying agency's compliance with the accreditation criteria.

11.2.3. Our initial controls assurance is based on accreditation scores for previous years adjusted to reflect the development and implementation of the new IT system. We adjust our controls assurance in accordance with the outcome of our compliance testing for the year subject to audit.

11.2.4. The allocation of the compliance tests among the two populations (IACS, Non-IACS) is based on the Certification Body's professional judgement and the findings reported in previous audits.

11.3. Evaluation per accreditation criterion

11.3.1. Annex I of Commission Delegated Regulation (EU) No. 907/2014 sets out the accreditation criteria. We performed our review following the requirements of those standards.

11.3.2. Many controls and accreditation criteria which have been assessed for EAGF are also applicable to EAFRD. Where this is the case, we have reported accordingly with a cross reference to the relevant section in the EAGF report (Chapter 4).

Control activities: Authorisation of payments – Administrative controls

- 11.3.3. The paying agency's CAP Futures IT programme aimed to provide new IT systems to implement CAP 2014-2020. The programme has, however, proved more complex and challenging than anticipated and has suffered considerable problems, lengthy delays and significant defects. Key regulatory and self-determined milestones and targets were not met.
- 11.3.4. RP&S opened on time for 2015 applications in March 2015. However, the system was slow and did not function as expected. Errors in the IT infrastructure and software had to be fixed during the application period. The paying agency utilised the derogation provided by Commission Implementing Regulation (EU) 2015/747 to extend the deadline for submission to 15 June 2015.
- 11.3.5. The paying agency's decision to focus on making BPS payments before the 15 October 2016 had a significant impact on Pillar II area based aid payments. No 2015 SAF payments were made in FY 2016 for the Less Favoured Area Support (LFASS) and Land Manager Option (LMO) schemes.
- 11.3.6. As with BPS, nationally funded loans were provided for the LFASS beneficiaries to offset delays in payment. Payments for the Rural priorities (RP) claims on the 2015 SAF have been made however, the majority of these payments were made manually which proved time consuming and placed additional demands on paying agency staff who were already under significant pressure.
- 11.3.7. The development of the RP&S system remains on-going with additional functionality being added and retrospective data being uploaded.

Findings

- 11.3.8. We reviewed the paying agency's administrative controls over the authorisation of payments following the requirements of Commission Delegated Regulation (EU) No. 907/2014 [Annex I].
- 11.3.9. We reviewed the procedures and tested 30 items from the IACS population in respect of administrative controls over the authorisation of payments. Our work confirmed that:
- controls and procedures were operating satisfactorily at area offices. Up to date desk instructions are in place, either as separate guidance or through the RP&S interface, for all administrative processes and controls leading up to a payment authorisation
 - staff complete all checklists as required and that a manual or electronic record is maintained recording the procedures and checks carried out
 - data input to RP&S was accurate and complete
 - all automated validation and cross checks had been completed, and queries arising from RP&S checks were resolved, before the claim was authorised for payment.

EAFRD IACS (RP&S)

- 11.3.10. We reviewed in total 76 transactions in respect of EAFRD IACS (RP&S), which comprised our step 1 sample of 36 OTSC re-verifications and an additional random sample of 40 items drawn from x-table information. The list of all cases appears in the Annex 3: Sample reviewed in substantive testing – EAGF IACS.
- 11.3.11. Our STEP 1 testing identified 7 minor compliance failures from our OTSC re-verification work. Our STEP 2 testing identified 4 financial errors resulting in 3 overpayments and 1 underpayment.

EAFRD IACS (SIACS)

- 11.3.12. We reviewed in total 60 transactions in respect of EAFRD IACS (RP&S) which was drawn from the x-table information. The list of all cases appears in the Annex 3: Sample reviewed in substantive testing – EAGF IACS.

11.3.13. We identified 6 cases which resulted in financial errors. Details of these cases can be found at section 12.3.4.

EAFRD Non-IACS

11.3.14. We reviewed in total 30 transactions in respect of EAFRD Non-IACS which comprised our step 1 sample of 9 OTSC re-verifications and an additional random sample of 21 items drawn from x-table information. The list of all cases appears in the Annex 9: Sample reviewed in substantive testing – EAFRD.

11.3.15. We identified one case from our sample of 30 which resulted in a financial error. Details on this case can be found in section 12.4.6.

Assessment

11.3.16. In our opinion, the scoring for this criterion for RP&S is 2 and for SIACS and EAFRD Non-IACS is 3.

Control activities: Authorisation of payments – On-the-spot controls

Findings

11.3.17. Control activities for authorisation of EAFRD IACS payments (on-the-spot-checks) are identical to EAGF IACS. Our findings and assessment in relation to EAGF IACS and EAFRD IACS can be found in sections 4.3.11 to 4.3.26.

11.3.18. In respect of EAFRD Non-IACS on-the-spot controls, including physical inspections, the elements we reviewed in detail following the requirements of Regulation (EU) No 907/2014, were as follows:

11.3.19. We confirmed that inspections for Non-IACS cases are subject to the same selection and monitoring regime as IACS cases. We reviewed the selection methodology for a sample of Non-IACS schemes and confirmed that it complies with the requirements set out in regulations. Central guidance is available to operational staff and this is supplemented by the use of specialist staff where required (e.g. clerk of works).

11.3.20. For EAFRD Non-IACS, we reviewed the guidance, instructions and standard documentation for a number of the new schemes. We confirmed that the guidance for 2016 has been reviewed by the paying agency and updated and we consider that the current guidance is consistent with scheme regulations and operational arrangements. Detailed guidance and standard documents on a scheme basis are available to users on the paying agency's intranet.

11.3.21. We confirmed that arrangements are in place to ensure that suitably qualified officers are assigned to inspections through reviewing the qualifications held and training undertaken for a sample of inspectors at three local offices. We confirmed that the paying agency's training policy requires that all inspectors attend annual update / refresher courses with additional specific courses arranged to address new schemes and any regulatory changes.

11.3.22. The paying agency has arrangements in place to allocate certain Non-IACS inspections to specialist, technically qualified staff such as quantity surveyors or clerks of works, with relevant experience.

11.3.23. Some EAFRD inspections are carried out by Forestry Commission Scotland (FCS), and Scottish Natural Heritage (SNH) staff. We confirmed that these are covered by an agreed SLA and that staff at FCS and SNH have access to all extant inspection guidance.

11.3.24. We examined a sample of 45 completed inspection reports apportioned across the populations; 36 IACS and 9 Non-IACS and found overall that inspection reports were completed to an acceptable standard.

Assessment

11.3.25. In our opinion, the EAFRD IACS scoring for this criterion is 3. The EAFRD NIACS scoring for this criterion is 3.

Control activities: Procedures for payment

Findings

11.3.26. We reviewed the procedures for payment in line with the requirements of Commission Delegated Regulation (EU) 907/2014 [Annex I Section 2(B)].

11.3.27. To assess the standard of procedures for payment we reviewed the records supporting a sample of 30 EAFRD payments. Our testing was designed to confirm that the paying agency's procedures ensured that payments are; accurate, appropriately approved; made only to bank accounts belonging either to beneficiaries or to their assignees; made only from the paying agency's bank or a governmental payments office; and made within five working days of the date of charge to the EAFRD. Our testing also considered segregation of duties, approval procedures, and procedures for voiding payments which failed to transfer.

11.3.28. We have not detected compliance or financial errors and we have not made any recommendations.

Assessment

11.3.29. In our opinion, the scoring for this criterion is 3.

Control activities: Procedures for accounting

Findings

11.3.30. Accounting arrangements are common to EAGF and EAFRD. Our assessment of procedures for accounting is reported at paragraphs 4.3.34 to 4.3.43 where we highlight a number of issues of concern which have an impact on accounting procedures.

Assessment

11.3.31. In our opinion, the scoring for this criterion is 2.

Control activities: Procedures for advances and securities

11.3.32. Nil return.

Control activities: Procedures for debts

Findings

11.3.33. The arrangements for administering recoveries are common to EAGF and EAFRD debts. Our assessment of Procedures for debts is reported at paragraphs 4.3.46 to 4.3.48. Our review, findings and overall assessment in this section are in respect of EAGF and EAFRD procedures for debts.

Assessment

11.3.34. In our opinion, the scoring for this criterion is 3.

11.4. Other accreditation components

- 11.4.1. We confirmed our assessment of the other accreditation components against the standard (Annex I of Commission Delegated Regulation (EU) No. 907/2014) by carrying out reviews/tests to ensure the paying agency's compliance with the criteria

Internal environment: Organisational structure

Findings

- 11.4.2. This criterion/component is common to EAGF and EAFRD. Our audit work, findings and assessment can be found at paragraphs 4.4.2 to 4.4.9.

Assessment

- 11.4.3. In our opinion, the scoring for this criterion for EAFRD IACS (RP&S) is 2 and for EAFRD IACS (SIACS) and EAFRD Non-IACS the score is 3.

Internal environment: Human-resource standard

Findings

- 11.4.4. This criterion/component is common to EAGF and EAFRD. Our audit work, findings and assessment can be found at paragraphs 4.4.10 to 4.4.17.

Assessment

- 11.4.5. In our opinion, the scoring for this criterion is 3.

Internal environment: Delegation

Summary of the delegated tasks

- 11.4.6. The paying agency has delegated tasks to other institutions (referred to as "delegated bodies") as per the table below:

Name of the Institution	Type of tasks delegated	Date of the delegation agreement
Forestry Commission Scotland (FCS)	Delivery partner for rural priorities schemes under the SRDP (EAFRD Non IACS). Scheme management and processing for functions for certain Forestry Grant Schemes	Framework agreement was signed on 13 February 2013 and FCS was operating under its provisions throughout the 2016 financial year
Scottish Natural Heritage	Delivery partner for Rural Priorities schemes under the SRDP	Framework agreement was signed on 22 April 2013 and SNH was operating under its provisions throughout the 2016 financial year
Scottish Environmental Protection Agency (SEPA)	Delegated tasks – cross compliance inspections relating to abstraction of water for irrigation and use of sewage sludge in agriculture	Framework agreement was signed on 22 April 2013 and SEPA was operating under its provisions throughout the 2016 financial year

- 11.4.7. We confirm that the rules and guidelines regarding the delegation of tasks are described in detail in the agreements listed. In addition, the paying agency issued a set of instructions for each specific scheme, which covers both the quality aspects of the delegated tasks and the reporting requirements.

Findings

11.4.8. FCS, SNH and SEPA do not have any delegated authority to make payments to beneficiaries. Each LAG is responsible for the appraisal, approval and payment to final beneficiaries on projects assessed under Axis 4. LAGs do not disburse European funds.

11.4.9. We noted that the last SLA monitoring meeting with Forestry Commission Scotland was in September 2014. The paying agency agreed that there had been some slippage in the regular quarterly meetings, but that FSC had been held to account through their regular attendance at (and reports to) the Accreditation Committee, Cross Scheme Committee and CAP Delivery Committee. We have concluded that there has been no diminution in the monitoring, or scrutiny, of FCS.

Assessment

11.4.10. In our opinion, the scoring for this criterion is 3.

Information and communication: Communication

Findings

11.4.11. The paying agency's arrangements for Information and Communication are common to EAGF and EAFRD schemes and we have assessed and our findings and assessment are reported at paragraphs 4.4.20 to 4.4.23.

Assessment

11.4.12. In our opinion, the scoring for this criterion is 3.

Information and communication: Information Systems Security

Standard

11.4.13. Annex I, 3 B of Regulation (EU) No. 907/2014.

Findings

11.4.14. The arrangements for Information Systems Security are common to both EAGF and EAFRD and our findings and assessment are reported at paragraphs 4.4.24 to 4.4.77.

Assessment

11.4.15. In our opinion, the scoring for this component is 3.

Monitoring: Ongoing monitoring via internal control activities

Findings

11.4.16. We reviewed the paying agency's on-going monitoring via internal control activities.

11.4.17. In all respects, on-going monitoring via internal control activities is the same for EAGF and EAFRD and our findings and assessment are reported at paragraphs 4.4.78 to 4.4.87.

Assessment

11.4.18. In our opinion, the scoring for this criterion is 3.

Monitoring: Separate evaluations via an internal audit service

Findings

11.4.19. We reviewed the paying agency's arrangements for separate evaluations via an internal audit service.

11.4.20. The internal audit service is common to both the EAGF and EAFRD funds and our findings and assessment are reported at paragraphs 4.4.88 to 4.4.102.

Assessment

Our evaluation of the internal audit service highlighted some significant issues, and we have made intermediate recommendations. In our opinion, the scoring for this criterion is 2.

12. Substantive Testing of Operational and Non-Operational transactions

12.1. Introduction

- 12.1.1. In this section we provide for each population and strata an assessment of the substantive testing results. The error evaluation in this respect is provided in section 8.6.1 for the Error Rate, in section 8.6.5 for the Incompliance Rate and in section 8.6.15 for non operational transactions. We have attached a list of all items selected for substantive testing, in the format proposed by the Annex to Guideline No. 3 on Reporting Requirements.
- 12.1.2. Guideline No. 2 'Annual Certification Audit' outlines the audit procedures for the validation of legality and regularity of expenditure. Following Guideline No. 2, we have adopted an integrated sampling approach for accomplishing audit objectives 1 and 2.
- 12.1.3. EAFRD was split into three strata (EAFRD IACS (RP&S), EAFRD IACS (SIACS) and EAFRD Non-IACS) following the recommended guidance contained in Guideline No. 2. The Certification Body was unable to use MUS to select its step 1 sample and used random sampling instead.

12.2. Test results in respect of the EAFRD IACS strata (RP&S) – error rate

Overview

- 12.2.1. Our sample selection of 43 items was based on Guideline No. 2, Annex 3.

Standard

- 12.2.2. As per Guideline No. 2 – Annual Certification Audit.

Work Done

- 12.2.3. We reviewed in total 43 in respect of EAFRD IACS (RP&S). This did not include 33 of the 36 OTSC re-verifications as no relevant payment was made in the financial year. The list of all cases appears in the Annex 9: Sample reviewed in substantive testing – EAFRD.

Assessment and Findings

- 12.2.4. As a result of our audit, we have identified no financial errors but have identified 7 hits with minor compliance errors:

Hit	Details	Absolute error area (ha / metres)	Outcome
13	2 minor compliance failures: There were number of small boundary errors and an area of one parcel which had been fenced off from remainder of parcel with no access, had not been excluded.	0.166 ha	No financial error as the producer holds more land than claimed per the contract
16	1 minor compliance failure: There were boundary errors.	0.045 ha	No financial error as the producer holds more land than claimed per the contract
18	1 minor compliance failure:	40 metres	No financial error as the producer holds more land

Hit	Details	Absolute error area (ha / metres)	Outcome
	Several gaps in hedgerow measuring 40 metres were identified on re-verification.	(hedgerows)	than claimed per the contract
19	1 minor compliance failure: There were a number of small exclusions that had not been identified by the original inspection.	0.299 ha	No financial error as the producer holds more land than claimed per the contract
25	1 minor compliance failure: There were areas assessed with an incorrect banding and some additional areas required assessment.	0.047 ha	No financial error as the producer holds more land than claimed per the contract
29	1 minor compliance failure: A number of adjustments to technical assessment due to the banding applied or the size of the area assessed.	1.804 ha	No financial error as the producer holds more land than claimed per the contract
32	2 minor compliance failure: There were adjustments to the length of dyke claimed and the amount of winter stubble recorded was also changed.	64.31 metres (dykes) 0.104 ha	No financial error as the producer holds more land than claimed per the contract

12.2.5. For our STEP 2 testing, we sampled 43 cases. We identified the following matters:

- hit 42 (Rural Priorities), the hit amount in the current year was confirmed as being the correct payment amount. There was an error in the calculation of the previous year where the payment included 0.09ha which was ineligible. This resulted in a prior year overpayment of €17.25.
- hit 61 (Rural Priorities), payment made in line with contract but an arithmetical error was made during processing resulting in an underpayment of £100 (€117.41). The EC element is £36.30 (€42.62).
- hit 64 (Rural Priorities), the claimed area of 12.87ha for 'management of species rich grassland' did not match the contract area of 12.89ha. The claim was overridden and the contract area has been paid which resulted in an overpayment of €1.06.
- hit 67 (Rural Priorities), the claimed area was 0.2ha for 'cropped mahair with FYM/Seaweed' less than that on the contract. The claim was overridden and the contract area has been paid which resulted in an overpayment of €64.78.

Recommendations

12.2.6. We have not made any recommendations.

12.3. Test results in respect of the EAFRD IACS (SIACS) strata – error rate

Overview

12.3.1. Our sample selection of 60 items was based on Guideline No. 2, Annex 3.

Standard

12.3.2. As per Guideline No. 2 – Annual Certification Audit.

Work Done

12.3.3. We reviewed in total 60 cases in respect of EAFRD IACS (SIACS). There were no OTSC re-verifications in this strata sample. The use of new and old IACS i.e. 2 strata came after the completion of the OTSC re-verification work. The list of all cases appears in the Annex 9: Sample reviewed in substantive testing – EAFRD.

Assessment and Findings

12.3.4. As a result of our audit, we have the following financial errors:

- hit 7 (Forestry Woodland Premium scheme, FWPS), the applicant has not inserted the areas to be claimed on his claim form. The paying agency paid the claim. The amount paid is in line with that expected and with prior claims. The applicant has claimed 0 ha but has been paid for 6.59 ha. An overpayment of £1,054.40 (€1,426.60) made up of £382.74 EC (€517.85) and £671.66 national (€908.75).
- hit 15 (Land Manager Option scheme, LMO), the claim reviewed included animal welfare schemes which require all claimants with cattle to be making the same claim. Two of the producers have suckler cows or cattle between 6-24 months old and do not have claims for animal welfare schemes. An overpayment of £658.00 (€890.27) made up of £238.85 EC (€323.16) and £419.15 national (€567.11).
- hit 22 (Less Favoured Area Support scheme, LFASS), a new entrant in 2014 paid at incorrect grazing category resulted in an overpayment of €50.39. A regular report run had identified a possible forfeit with this case so a stop was placed on the 2015 payment until this had been investigated and cleared. The potential forfeit flag was caused by this classification error and would have been noted and corrective action taken when staff investigated. No investigation had taken place at time of audit.
- hit 31 (Land Manager Option scheme, LMO), the applicant claimed for management of conservation headlands option on 12.57ha. The parcel was used for temporary grassland and was therefore not eligible for this LMO option. An overpayment of £1,698.71 (€2,161.76) made up of £616.63 EC (€784.72, known error) and £1,082.08 national (€1,377.04).
- hit 36 (Farm Woodland scheme, FWS), one claim (out of 3) not signed or dated on declaration page. This claim is for 0.2ha of broad leaves on improved land. This equates to an overpayment of €7.01 of EC funds. Paid €161.18 (EC), audit value (EC) €154.17.
- hit 39, (Forestry Premium scheme, FPS), claim for reduced size submitted in 2012 for 2.84 ha and paid correctly in 2013 scheme year. The Forestry database (SERGS) was not updated to reflect change in claim size and the next four claims paid as per the schedule at 2.87 ha. This has resulted in an overpayment of €1.80 (£1.29) (capped EU element link) each year for the next 4 years.

Recommendations

12.3.5. We have not made any recommendations.

12.4. Test results in respect of the EAFRD Non-IACS population – error rate

Overview

12.4.1. Our sample selection of 30 items was based on Guideline No 2, Annex 3.

Standard

12.4.2. As per Guideline No. 2 – Annual Certification Audit.

Work Done

12.4.3. We reviewed in total 30 transactions in respect of EAFRD Non-IACS, including 9 OTSC re-verifications following the requirements of the standard. A list of all cases appears in Annex 9: Sample reviewed in substantive testing – EAFRD.

12.4.4. The total number of Non-IACS on-the-spot-checks undertaken by the paying agency was less than 200 and was therefore considered to be a 'small population' for sampling purposes (Annex 3 to Guideline No. 2 on Sampling Methodology). We selected a random sample of 9 items.

12.4.5. Our step 2 sample of 30 payment transactions comprised our step 1 sample of 9 OTSCs leading to payment and an additional random sample of 21 transactions drawn from the x-table information received for the Non-IACS schemes.

Assessment and Findings

12.4.6. One case was confirmed as an overpayment. A final payment on a Rural Priorities capital case should have been limited to the state aid threshold. The paying agency had identified the error prior to audit testing but had not implemented recovery action. The grant rate paid was 50% of eligible expenditure with the amount payable limited to 200,000 Euros (£167,280) by State Aid rules. The total value of the interim and final payments was £171,820.67, an overpayment of £4,540.67. The EC element was €1,996.68 (hit 27).

Recommendations

12.4.7. We have not made any recommendations.

12.5. Overall test result of EAFRD population

12.5.1. We have identified a small number of financial errors but in totality these do not breach materiality.

12.6. Test results in respect of the EAFRD IACS strata – incompliance rate

Overview

12.6.1. Our sample selection of 136 items was based on Guideline No.2, Annex 3.

Standard

12.6.2. As per Guideline No. 2 – Annual Certification Audit.

Work done

12.6.3. We reviewed in total 136 transactions in respect of the EAGF IACS strata, including 36 OTSC re-performances, following the requirements of the standard as stated above. The list of all cases appears in the Annex 11: Incompliance Rate – EAFRD IACS.

Assessment and Findings

- 12.6.4. We reconciled our testing to the control statistics figures and identified material differences. This resulted in a breach of materiality as identified in table 8.5.
- 12.6.5. 94/136 cases did not relate to the 2015 calendar year.
- 12.6.6. 42/136 hits that did relate to the 2015 calendar year all had errors. We understand most of these are due to an averaging of co-financing and exchange rates when recorded in the control statistics. However, a number of differences were large and unexplained.

Recommendations

- 12.6.7. We have made an intermediate recommendation with regard to the compilation of the EAGF IACS control statistics (para 6.6.3 refers). That recommendation is also applicable to the EAFRD IACS control statistics.

12.7. Test results in respect of the EAFRD Non-IACS population – incompliance rate

- 12.7.1. For EAFRD Non IACS, no incompliance rate can be calculated as the on the spot re-verifications done by the Certification Body have covered financial year 2016 payments and not the whole period of the of the control statistics, that was of the calendar year 2015.

12.8. Test results of non-operational transactions.

12.8.1. For each of the audited populations, an assessment of the results of our testing is provided. The error evaluation is included in section 8.6.15. The findings are further detailed below.

Test results of tables of Annex II – Irregularities

Standard

12.8.2. Annex I, 2 E of Commission Delegated Regulation (EU) No. 907/2014 and chapter 5.4 of Guideline No. 1. – "Accreditation" and Guideline No. 5 on the submission to the Commission of the Annexes II and III of Commission Implementing Regulation (EU) No. 908/2014.

Work Done

12.8.3. Annex 7 contains a detailed list of all transactions tested and the detected errors, including their financial value.

12.8.4. Guideline No 2 permits the merging of the EAGF and EAFRD populations for non-operational transactions, where it can be demonstrated that debt movements are managed using a common system. The debt management system operated by the paying agency is common to EAGF and EAFRD. We have therefore merged the EAGF and EAFRD populations for substantive testing of non operational transactions.

12.8.5. The number of transactions recorded in the paying agency's debtors' system met the criteria for small populations, as defined in Annex 3 to Guideline 2. We have reviewed 28 items value: £8,164.78 as listed in Annex 7. A sample of 30 items was selected for compliance testing, as required by Annex 3 to Guideline No. 2. See section 11.3.33. This section reports our findings in relation to EAFRD debts.

Assessment and Findings

12.8.6. The paying agency has reported total EAFRD Annex II debts at 15 October 2016 of £209,670.51.

12.8.7. We examined a total of 28 debtor entries (2 EAGF and 26 EAFRD), auditing all relevant entries across the Annex II columns as indicated in the error evaluation at Annex 6.

12.8.8. We are satisfied that the paying agency is correctly splitting debtors between the respective funds and is properly accounting for administrative debts. We have not identified any errors and we are satisfied that the Annex II presented by the paying agency is true, complete and accurate in all material respects.

Recommendations

12.8.9. We have not made any recommendations.

13. Reconciliation of Quarterly and Annual Declarations

13.1. Reconciliation of quarterly and annual declarations of EAFRD expenditure

Standard

13.1.1. To verify whether the four quarterly reports agree with the annual declaration for the 2016 financial year.

Work done

13.1.2. We have verified the differences and explanations in the electronic "diff." table provided by the paying agency.

13.1.3. In addition, we assessed the Administrative Errors declared in the Quarterly Declarations and those declared separately in the Annual Declaration. We also verified that the administrative errors are not included in the Annex II and Annex III tables, and we also reviewed whether these have been credited to the Fund i.e. introduced as a negative amount in the Quarterly or Annual Declarations.

Findings

Table 13.1: Reconciliation of differences – Programming period 2014-2020

Budget post	Total of Quarterly reports (€)	Annual Account (€)	Difference (€)
050460010131103	18,423.97	18,423.97	0
050460010141103	96,985.48	97,252.73	267.25
050460010241103	70,672.21	70,672.21	0
050460010331103	414.93	494.20	79.27
050460010341103	2,838.28	2,759.01	-79.27
050460010431103	1,347,944.80	1,347,944.80	0
050460010441103	1,103,849.12	1,095,835.61	-8,013.51
050460010631103	680,102.45	679,774.42	-328.03
050460010641103	1,454,041.95	1,452,428.51	-1,613.44
050460010731103	3,394.30	3,394.30	0
050460010741103	6,220.63	4,690.97	-1,529.66
050460010831103	2,615,878.13	2,676,856.42	60,978.29
050460010835103	2,754,016.92	2,819,585.05	65,568.13
050460010837103	0	(7,303.73)	-7,303.73
050460010841103	2,576,238.92	2,664,154.12	87,915.20
050460010845103	2,891,592.90	2,998,607.10	107,014.20
050460010847103	0	(2,071.42)	-2071.42
050460011031103	2,202,581.13	2,188,976.15	-13,604.98
050460011041103	3,026,593.28	3,020,282.65	-6,310.63
050460011131103	44,572.86	40,939.49	-3,633.37
050460011141103	162,451.12	167,853.81	5,402.69

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Budget post	Total of Quarterly reports (€)	Annual Account (€)	Difference (€)
050460011331103	117,345.93	104,638.00	-12,707.93
050460011335103	0	(650.11)	-650.11
050460011337103	0	(218.11)	-218.11
050460011341103	177,761.14	170,068.96	-7,692.18
050460011345103	0	(843.39)	-843.39
050460011347103	0	(608.82)	-608.82
050460011431103	562,502.10	562,502.10	0
050460011441103	278,789.26	277,881.87	-907.39
050460011531103	244,695.20	245,240.96	545.76
050460011535103	443,692.73	443,692.73	0
050460011541103	227,416.91	281,652.83	54,235.92
050460011545103	319,543.18	321,150.66	1,607.48
050460011631103	8,621.60	8,621.60	0
050460011641103	154,270.04	154,270.04	0
050460011931103	257,257.12	253,351.64	-3,905.48
050460011941103	261,295.64	260,003.14	-1,292.50
050460012041103	2,071,080.73	2,071,080.73	0
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Total	26,183,084.96	26,493,385.20	310,300.24
	=====	=====	=====

13.1.4. The explanations for the differences are as follows:

- 1) - €5,736.69 Due to administration debt
- 2) - €81,192.70 Due to amounts recovered due to irregularities
- 3) €537,193.87 Due to cut off error (Amount in Annual Declaration but not reported in quarterly declarations)
- 4) - €139,964.24 Due to cut off error (Amount in quarterly declarations but not reported in Annual Declaration declarations)

Administrative Errors

13.1.5. We can confirm that the Administrative Errors have been refunded. The total amount included in the declarations amounts to:

Table 13.2: EAFRD reported administrative errors: Programming period 2014-2020

Administrative Errors (reported/deducted)	Amount (€)
1. Annual Declaration	-5,736.69
2. Quarterly Declarations	0

13.1.6. After the closure of the programme 2007-2013 (31 December 2015), the following administrative errors have been revealed.

Table 13.3: EAFRD reported administrative errors: Programming period 2007-2013

Administrative Errors (established)	Amount (€)
1 January 2016 – 15 October 2016	-7,884.34

Assessment

13.1.7. We can confirm that the provided electronic "diff." table is complete and accurate, and the explanations given are valid and justified.

Recommendations

13.1.8. We have not made any recommendations.

13.2. Reconciliation of annual declaration and X-table data of EAFRD accounts

Standard

13.2.1. To verify whether the four quarterly reports agree with the X-table data for the 2016 financial year.

Work done

13.2.2. We have reviewed the completeness, accuracy and relevance of the electronic "diff." table (explanation-reconciliation codes "C") provided by the Paying Agency.

Findings

Table 13.4: Reconciliation of differences for Programming period 2014-2020

Budget post	Matrix (€)	Annual Account (€)	Difference (€)
050460010131103	18,423.99	18,423.97	0.02
050460010141103	97,252.71	97,252.73	-0.02
050460010241103	70,672.18	70,672.21	-0.03
050460010331103	494.20	494.20	0
050460010341103	2,758.58	2,759.01	-0.43
050460010431103	1,355,532.63	1,347,944.80	7,587.83
050460010441103	1,080,289.86	1,095,835.61	-15,545.75
050460010631103	679,836.53	679,774.42	62.11
050460010641103	1,452,980.52	1,452,428.51	552.01
050460010731103	3,394.27	3,394.30	-0.03
050460010741103	6,220.59	4,690.97	1,529.62
050460010831103	3,092,179.99	2,676,856.42	415,323.57
050460010835103	-120.25	2,819,585.05	-2,819,705.30
050460010837103	-6,717.70	(7,303.73)	586.03
050460010841103	4,466,292.95	2,664,154.12	1,802,138.83
050460010845103	-239.20	2,998,607.10	-2,998,846.30
050460010847103	-1930.74	(2,071.42)	140.68
050460011031103	2,203,007.14	2,188,976.15	14,030.99
050460011041103	3,018,210.60	3,020,282.65	-2072.05
050460011131103	40,939.22	40,939.49	-0.27
050460011141103	147,011.78	167,853.81	-20,842.03
050460011331103	16,284.94	104,638.00	-88,353.06
050460011335103	160,914.87	(650.11)	161,564.98
050460011337103	79,501.86	(218.11)	79,719.97

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Budget post	Matrix (€)	Annual Account (€)	Difference (€)
050460011341103	25,273.65	170,068.96	-144,795.31
050460011345103	275,916.91	(843.39)	276,760.30
050460011347103	119,646.37	(608.82)	120,255.19
050460011431103	556,992.99	562,502.10	-5,509.11
050460011441103	283,979.14	277,881.87	6,097.27
050460011531103	406,552.54	245,240.96	161,311.58
050460011535103	0	443,692.73	-443,692.73
050460011541103	417,993.77	281,652.83	136,340.94
050460011545103	0	321,150.66	-321,150.66
050460011631103	8,621.61	8,621.60	0.01
050460011641103	154,270.09	154,270.04	0.05
050460011931103	247,051.66	253,351.64	-6,299.98
050460011941103	266,303.14	260,003.14	6,300.00
050460012041103	2,070,361.49	2,071,080.73	-719.24
	-----	-----	-----
Total	22,816,154.88	26,493,385.20	-3,677,230.32
	=====	=====	=====

13.2.3. The explanations for the differences are as follows:

- 1) €5,736.69 Recovered Administration debt – no x table information
- 2) - €15.48 Roundings
- 3) - €1,576.18 Misposting to incorrect regions, funding source and measure. The mispostings contra out apart from €1,576.18 which is to do with the EU element being calculated incorrectly in the x-table - the account is correct
- 4) - €53,580.12 Re-issued BACSs returns have been accounted for in previous Matrix and incorrect dates resulted in missing x-table data
- 5) €1,753.93 Duplicate payment corrections, Ineligible spend, Returned BACs and discovery of payment out with 2016 account all removed from account but remain in x-table
- 6) €3,937.38 Late correction to a payment and Cross Compliance information added to final account
- 7) €14,942.58 Removal of double entry in account, BRNs remain in x-table. Correct payment to BRNs - Account correct
- 8) - €3,638,741.53 Existing SIACS system cannot apply multiple funding sources to different Measures in the same Scheme. Therefore the X-table data applies the co-financing rate to the gross payment to beneficiary instead of the portion funded under Mainstream
- 9) - €9,659.93 Timing differences for x-table rates to account rates - account correct
- 10) - €27.66 Other

Assessment

13.2.4. We can confirm that the provided electronic "diff." table is complete and accurate, and the explanations given are relevant and justified.

Recommendations

13.2.5. We have not made any recommendations.

13.3. Reconciliation of the information required by Annex II and Annex III of Commission Implementing Regulation (EU) No. 908/2014 to the debtors' ledger – EAFRD

Standard

- 13.3.1. To reconcile the closing balances of the previous financial year to the opening balances of the current financial year in respect of the debtors' ledger and the Annex II and Annex III tables.
- 13.3.2. To reconcile the data reported in Annex II and Annex III of Commission Implementing Regulation (EU) No. 908/2014 to the debtors' ledger in respect of the current financial year.
- 13.3.3. The UK Authorities consider that debts arising from cross-compliance breaches should be treated in the same manner as other claimant irregularities. These are therefore included, as agreed with the UK Co-ordinating Body, in the main Annex II declaration. Consequently the Annex III table contains only details of multi-annual sanctions. By agreement with the UK Co-ordinating Body we have not reconciled the contents of the Annex III table, however we can confirm that we are satisfied with the reasonableness of these figures.

Work done

- 13.3.4. We have reviewed the reconciliation of the closing balances of the previous financial year to the opening balances of the current financial year in respect of Annex II and the debtors' ledger.
- 13.3.5. We have reviewed the reconciliation of the data reported in Annex II of Commission Regulation (EC) No. 908/2014 to the debtors' ledger in respect of the current financial year.

Findings

Table 13.5: Reconciliation closing balance 2015 / opening balance 2016

	Closing balance FY 2015 (as at 15/10/15)	Opening balance FY 2016 (as at 16/10/15)	Difference
Annex II	302,786.31	302,786.31	0
Debtors' ledger	302786.31	302,786.31	0

- 13.3.6. We have reconciled the closing balances of the previous year to the opening balances of the current financial year in respect of Annex II and the debtors' ledger. We can confirm that there are no discrepancies.

Table 13.6: Reconciliation of Annex II and Annex III to the debtors' ledger – Programming period 2007-2013

	Balance 16 October £	New cases £	Recovered amounts £	Corrected amounts £	Total non-cleared amounts declared irrecoverable £	Amounts to be recovered by 15 October £
Annex II	274,478.36	293,895.57	-310,591.00	-27,846.19	-47,431.76	182,504.97
Annex III	n/a	n/a	n/a	n/a	n/a	n/a
Debtors' ledger	302,786.31	358,586.81	-371,411.75	-32,730.21	-47,560.65	209,670.51
Differences	-28,307.96	-64,691.24	60,820.75	4,884.02	128.89	27,165.54
Explanation	1	1	1	1	1	1

13.3.7. The explanations of the differences by column are:

1. The differences represent the recoveries for the 2014-2020 programming period sitting in the debtors' ledger. See table 13.7 'reconciliation of Annex II and Annex III to the debtors' ledger - programming period 2014-2020'.

13.3.8. We furthermore confirm that the closing balances mentioned on the summary tables of, respectively, Annex II and Annex III (amounts to be recovered as at 15 October 2016) tally with the sum of:

Opening balances (amounts to be recovered as at 16 October 2015 for respectively Annex II and Annex III)

+ New cases

+ / - corrected amounts

– Recoveries

– Irrecoverable amounts.

Table 13.7: Reconciliation of Annex II and Annex III to the debtors' ledger – Programming period 2014-2020

	Balance 16 October £	New cases £	Recovered amounts £	Corrected amounts £	Total non-cleared amounts declared irrecoverable £	Amounts to be recovered by 15 October £
Annex II	28,307.96	64,691.24	-60,820.75	-4,884.02	-128.89	27,165.54
Annex III	n/a	n/a	n/a	n/a	n/a	n/a
Debtors' ledger	302,786.31	358,586.81	-371,411.75	-32,730.21	-47,560.65	209,670.51
Differences	-274,478.35	-293,895.57	310,591.00	27,846.19	47,431.76	182,504.97
Explanation	1	1	1	1	1	1

13.3.9. The explanations of the differences by column are:

1. The differences represent the recoveries for the 2007-2013 programming period sitting in the debtors' ledger. See table 13.6 'reconciliation of Annex II to the debtors' ledger for programming period 2007-2013'.

13.3.10. We furthermore confirm that the closing balances mentioned on the summary tables of, respectively, Annex II and Annex III (amounts to be recovered as at 15 October 2016) tally with the sum of:

Opening balances (amounts to be recovered as at 16 October 2015 for respectively Annex II and Annex III)

+ New cases

+ / - corrected amounts

– Recoveries

– Irrecoverable amounts.

Confirmation of "50/50 tables"

13.3.11. As part of our tests on Annexes II, we reviewed the tables established by the PA setting out the amounts to be borne by the Member States according to the 50%/50% rule as well as the amounts to be borne in full by the EU budget due to irrecoverability. We confirm the figures mentioned in the table below:

Table 13.8: Confirmation of "50/50 tables"

Paying Agency	50% to be charged to the Member State (Article 54(2) of Regulation (EU) No. 1306/2013 £	100% to be borne by the EU budget (Article 54(3) of Regulation (EU) No. 1306/2013 £
EAFRD Programming period 2007-2013	106.47	47,431.76
EAFRD Programming period 2014-2020	0	128.89

Assessment

13.3.12. We confirm that the "50/50" table is complete and accurate, and the explanations given are relevant and justified.

Recommendations

13.3.13. We have not made any recommendations.

13.4. Reconciliation of the recoveries as per the annual declaration of EAFRD to the Annex II and Annex III

Standard

13.4.1. There must be a clear audit trail to support the reconciliation between the figures of the reused amounts according to second paragraph Article 56 of Regulation (EU) No. 1306/2013, shown in the annual declaration of EAFRD expenditure, and the Annex II and Annex III information.

Work done

13.4.2. We have reviewed both the adequacy of the procedures in place and the outcome of the reconciliations.

Findings

Table 13.9: Reconciliation of recovered and reused amounts per annual declaration of EAFRD expenditure and recoveries included in Annex II and Annex III

	€	€
Recovered and reused amounts per annual declaration of EAFRD expenditure	-86,929.39	
Recoveries in Annex II	- 453,186.57	
Recoveries in Annex III	n/a	
Difference		-366,257.18

Explanations of differences:

- 1) - € 5,736.69 administration debt
- 2) - € 86,644.80 2007-13 Irregularities 5th Quarter submission (16/10/15 – 31/12/15). Recoveries already repaid as part of the 2007 -2013 RD Closure exercise.
- 3) - €273,875.69 2007-13 Irregularities 1st January – 15th October 2016

Assessment

13.4.3. We reviewed the Paying Agency's reconciliation process and are satisfied that it was performed properly.

Recommendations

13.4.4. We have not made any recommendations.

13.5. Confirmation of advances

13.5.1. Nil return.

13.6. Confirmation of advances related to financial instruments

13.6.1. Nil return.

13.7. Review of RD control statistics to be provided on 15 July 2016 as referred to in Article 9(1) of Regulation (EU) No 809/2014

Objective

13.7.1. To verify the reconciliation of the PA for the control statistics reported under Article 9(1) of Regulation (EU) No. 809/2014.

Work done

13.7.2. We note that the paying agency did not submit the returns to the UK Co-ordinating Body by 15 July 2016 as required.

13.7.3. We enquired whether the paying agency undertakes a reconciliation of control statistics returns to the underlying database and that there were no unresolved discrepancies. We reviewed reconciliations prepared by the paying agency, and supporting documentary evidence, for reasonableness.

13.7.4. We assessed the audit trail and agreed the figures in the returns to the underlying data for on-the-spot-checks (inspections). We also completed a test check of the accuracy and completeness of data base entries, by comparing the database to the results of our Step 1 re-performance of on-the-spot-checks (para 12.6.1 refers.).

13.7.5. We confirmed the arrangements in place at the paying agency for collating and analysing data and preparing the returns. We considered the completeness of the data and the return transmitted to the UK Co-ordinating Body. We also confirmed that the returns had been prepared in accordance with relevant guidelines and explanatory notes.

Findings

13.7.6. We note that the paying agency did not submit the returns to the UK Co-ordinating Body by 15 July 2016 as required. This was due to the issues surrounding the delivery of the new RP&S system. Submission was finally made on 17 January 2017.

13.7.7. We were able to reconcile the control statistics to the underlying database.

13.7.8. We reconciled our testing to the control statistics figures and identified material differences. This resulted in a breach of materiality as identified in table 8.5. 94/136 cases did not relate to the 2015 calendar year. 42/136 hits that did relate to the 2015 calendar year all had errors. We understand some of these are due to an averaging of co-financing and exchange rates when recorded in the control statistics. However, a number of differences were large and unexplained.

Conclusion

13.7.9. We conclude that because of the errors identified in the substantive testing, we cannot confirm the control statistics.

13.7.10. We have made an intermediate recommendation with regard to the compilation of the EAGF IACS control statistics (para 6.6.3 refers). That recommendation is also applicable to the EAFRD IACS control statistics.

13.7.11. Recommendations

13.7.12. We have made a minor recommendation and this is included in our Management Letter.

14. Other matters

14.1. Action Plans

Objective

- 14.1.1. The paying agency has developed a formal Rural Development scheme action plan with milestones, in order to address weaknesses in the operation of the scheme.
- 14.1.2. We reviewed the Rural Development Scheme Action Plan (2014 onwards) established by the Paying Agency to address deficiencies in the operation of the Rural Development Scheme. Our review included reviewing the plan and the latest progress reports.

Work Done

- 14.1.3. We reviewed progress against the action plan established by the paying agency in 2014 to address the serious weaknesses in:
- improving internal control and coordination procedures;
 - improvement of IT tools;
 - information, training and advice for beneficiaries;
 - improving internal control and coordination procedures;
 - programmes' amendments, simplification of measures, modification of contracts;
 - improving internal control and coordination procedures; and,
 - improving internal control and coordination procedures.

Findings and Assessment

- 14.1.4. From the key problem areas outlined, the Rural Development action plan aims to deliver improvement, namely:
- review of cattle identification inspection procedures;
 - farmers' diaries: new agri-environmental diaries issued;
 - review of the efficacy of action in relation to pre-contract review meetings/discussions with beneficiaries;
 - examination of the scope for undertaking cross-checks (plausibility checks) for animal related RD measures and options;
 - review of the scope for revision of any measures which cannot be checked administratively and are only controllable on the spot;
 - OTS checks for the 2015 year carried out by the P.A.; and,
 - evidence of full audit trail required on file regarding dating and supervision.
- 14.1.5. The Rural Development action plan now regards six of the seven actions as implemented with one on-going.

Recommendations

- 14.1.6. We have not made any recommendations.

14.2. Follow-up of previous years' recommendations

14.2.1. The following tables include previous years' major and intermediate recommendations, the progress made against the outstanding recommendations, comments by the Paying Agency and the assessment of the response by the Certification Body. The follow-up of financial errors is indicated in a separate table below.

Major recommendations

14.2.2. There were no major recommendations arising from our audit.

Intermediate recommendations

14.2.3. The intermediate recommendations in respect of accreditation were relevant to both EAGF and EAFRD and have been examined at section 7.4.3

14.2.4. There were no intermediate recommendations in respect of legality and regularity:

Financial errors

14.2.5. There were no financial errors in the EAFRD IACS and EAFRD Non-IACS populations reported in our 2015 Report.

Section C –AUDIT OPINION

OPINION OF THE CERTIFICATION BODY ON THE SCOTTISH GOVERNMENT RURAL PAYMENTS AND INSPECTIONS DIRECTORATE, TO THE EUROPEAN COMMISSION

I have audited the annual accounts of the Scottish Government Rural Payments and Inspections Directorate related to EAGF (final total net expenditure: EUR 520,767,826) and EAFRD (final total net expenditure: EUR 26,493,385) expenditure for the 2016 EAGF/EAFRD financial year and assessed the internal control procedures operated by the Scottish Government Rural Payments and Inspections Directorate. As required by article 9(1) or Regulation (EU) No 1306/2013 of the European Parliament and of the Council, I have also considered whether my examination puts in doubt the assertions made in the Management Declaration of the Director of the Scottish Government Rural Payments and Inspections Directorate for the financial year 16/10/2015 to 15/10/2016.

Management's responsibility for the annual accounts and the Director's responsibility for the Management Declaration

Management is responsible for the preparation and fair presentation of the annual accounts in accordance with Articles 29, 30 and 31 of Commission Implementing Regulation (EU) No 908/2014. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of annual accounts that are free from material misstatement, whether due to fraud or error.

The Director of the Scottish Government Rural Payments and Inspections Directorate is responsible for the preparation and fair presentation of this Management Declaration in accordance with Article 3 of Commission Implementing Regulation (EU) No 908/2014. This responsibility includes an assessment as to the veracity, completeness and accuracy of the annual accounts submitted to the Commission, and an assessment as to whether the control system established by the Scottish Government Rural Payments and Inspections Directorate management provides reasonable assurance as to the legality and regularity of underlying transactions. The Director of the Scottish Government Rural Payments and Inspections Directorate should base her assessment upon all information at her disposal, including the work of the internal audit service.

Responsibility of the Certification Body

My responsibility, acting as Certification Body, is to express an opinion on the annual accounts. I conducted my audit in accordance with Article 6 of Commission Implementing Regulation (EU) No 908/2014, and the audit methods specified in Guideline 2 issued thereunder. I have complied with ethical requirements, being the UK Auditing Practices Board's Ethical Standards for Auditors, and planned and performed the audit to obtain reasonable assurance whether the annual accounts transmitted to the Commission are free from material misstatement.

The audit included an examination, on a test basis, of evidence supporting the information in the annual accounts, and an examination of procedures and of a sample of transactions to obtain audit evidence about the amounts and disclosures in the annual accounts. My responsibility under Article 5(3) of Commission Implementing Regulation (EU) No 908/2014 extends to providing an opinion on the internal controls; my conclusion is based on the results of my assessment of the Paying Agency's compliance with the accreditation criteria as set out in Annex I of Commission Delegated Regulation (EU) No 907/2014. It is not my responsibility to conclude on whether all possible controls are present in the system.

In addition, my responsibility is to express an opinion on whether my examination puts in doubt the assertions made in the Management Declaration and whether the Management Declaration complies

with Article 3 of Commission Implementing Regulation (EU) No 908/2014 and Guideline 4 on the Management Declaration.

I have read all the financial and non-financial information included in the Management Declaration and its annexes to identify whether the Management Declaration is consistent with the results of my examination. This includes my evaluation of whether those results suggest a need for reservations to be made. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

I believe that my work provides a reasonable basis for my audit opinions as set out in Guideline 2, issued under Article 6 (4b) of Commission Implementing Regulation (EU) No 908/2014.

Opinion on the Annual accounts – Unqualified

In my opinion:

- the accounts to be transmitted to the Commission for the 2016 EAGF and EAFRD financial year ended 15/10/2016 are true, complete and accurate in all material respects as regards the total net expenditure charged to the EAGF and EAFRD; and
- based on my work to review the Paying Agency's compliance with the accreditation criteria, the internal control procedures of the Paying Agency have operated satisfactorily as regards both the EAGF and EAFRD.
- The expenditure for which reimbursement has been requested from the Commission for both EAGF and EAFRD is legal and regular in all material respects.

Basis for the Qualified Opinion on the Management Declaration

The Management Declaration notes that the EAGF IACS control statistics are incomplete and may contain inaccuracies. That limitation on the management assertion in relation to the Control Statistics means that the scope of my audit work on the management declaration has also been limited as it relates to the Analysis of the Control Statistics in Annex 2 of the Declaration.

Some components of the EAFRD IACS control statistics use the same underlying IT system as for the EAGF IACS control statistics. This combined with the results of my audit work puts into doubt the accuracy of the EAFRD IACS control statistics reported in the Analysis of the Control Statistics in Annex 2 of the Declaration.

Opinion on the Management Declaration – [Qualified]

Based on my examination, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, nothing has come to my attention that:

- puts into doubt the assertions made in the Management Declaration for the financial year 16/10/2015 to 15/10/2016;
- causes me to believe that the Management Declaration does not comply with the legal framework.

Our audit work was finalised on 02/03/2017. The opinions relate to the situation as at that date. A report on the conduct of the audit and my findings is delivered at the same date as this opinion and should be read in conjunction with it.

Sir Amyas CE Morse KCB

Comptroller and Auditor General

March 2017

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Section D – ANNEXES

- Annex 1: Glossary of Abbreviations
- Annex 2: Internal audit evidence
- Annex 3: Sample reviewed in substantive testing – EAGF IACS
- Annex 4: Incompliance Rate – EAGF (Livestock)
- Annex 5: Reconciliation of gross amount of tested expenditure to the Annual Declaration
- Annex 6: Evaluation of Errors – Debtors – EAGF and EAFRD
- Annex 7: Sample reviewed in testing – EAGF and EAFRD Annex II Tables
- Annex 8: Organisation Structure of the PA and regional/local offices
- Annex 9: Sample reviewed in substantive testing – EAFRD
- Annex 10: Reconciliation of gross amount of tested expenditure to the Annual Declaration
- Annex 11: Incompliance Rate – EAFRD IACS