

Government and Public Sector

October 2006

The National Archives of Scotland

Annual Report to Board Members

2005/06 Audit

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Ladies and Gentlemen

Annual Report to Board Members 2005/06

We have completed our audit of the National Archives of Scotland (“NAS”) and its financial statements for the year ended 31 March 2006.

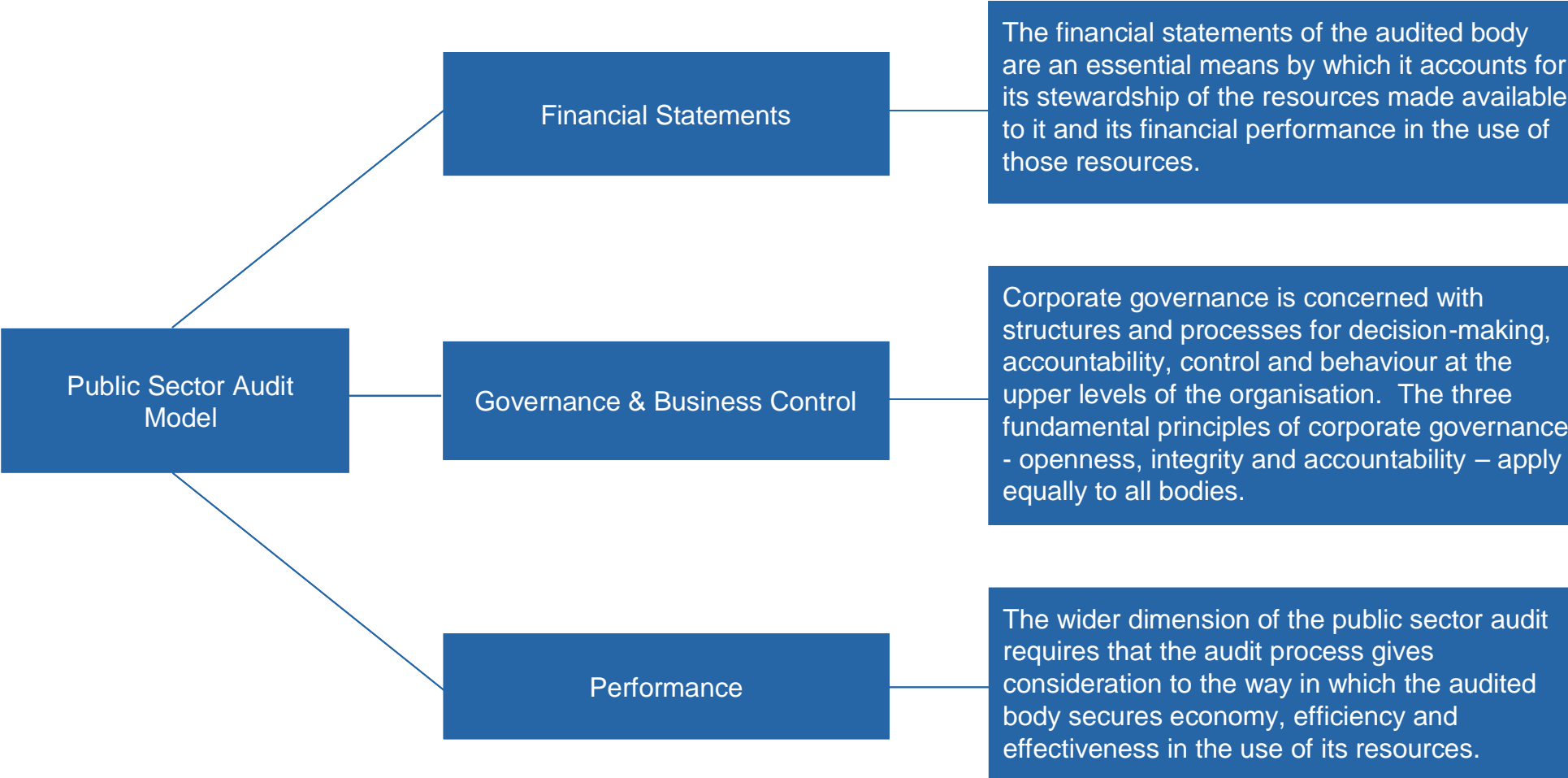
The Annual Report which follows is primarily designed to direct your attention to the key matters that have arisen out of the 2005/06 audit process and to confirm what action is planned by management to address the more significant matters identified for improvement.

We would like to take this opportunity to offer our thanks to those members of management and staff who have assisted us during the course of the audit.

Yours faithfully

PricewaterhouseCoopers LLP

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Our report structure (continued)

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1. Audit Opinions and Financial Targets

Our Audit Opinion

- 1.1 Our audit opinion concerns both the true and fair statement of NAS's financial results for the year ended 31 March 2006 (2005/06) and the regularity of its income and expenditure in the year.
- 1.2 Our true and fair opinion on the financial statements is unqualified.
- 1.3 Our regularity opinion on income and expenditure is unqualified.
- 1.4 Our opinion is set out in full in **Appendix 3**

Financial Targets

- 1.5 NAS has the key financial target of ensuring expenditure does not exceed the level in the budget approved by the Scottish Ministers. This objective was achieved and NAS is disclosing an underspend of £88,000 in its 2005/06 Departmental Outturn Statement.
- 1.6 A summary of the financial performance of NAS is given in Section 2 of this report.
- 1.7 In addition, NAS is expected to ensure that arrangements are in place to secure Best Value. We performed a review of the Best Value arrangements in place at NAS as part of our 2004/05 audit cycle and we have discussed ongoing arrangements in this area with key NAS staff as part of work in the current year. A summary of current progress against agreed recommendations is provided in Section 8 of this report.

Financial Targets

- 1.8 NAS has a variety of Performance Targets, as detailed in its Corporate Plan. These are linked to the stated corporate objectives of the organisation and performance against these targets is monitored throughout the year. NAS does not include performance results within the annual accounts.

2. Financial Performance and Position

Overall Financial Performance for 2005/06

	Actual 2006 (£'000)	Budget 2006 (£'000)	Variance 2006 (£'000)
Departmental Expenditure Limit			
Staff Costs			
Directly Employed Staff	3,310	3,440	(130)
Casual Staff	222	90	132
Other Staff	900	870	30
Administration Expenditure			
Accommodation	1,440	1,378	62
Travel	29	26	3
Transport	4	5	(1)
Supplies & Services	399	364	35
Training	24	40	(16)
Hospitality	3	2	1
Depreciation	778	840	(62)
Cost of Capital Charges	421	460	(39)
Auditors Remuneration	56	0	56
Other	2	0	2
Grants	173	180	(7)
Administration Income			
Accommodation Charges	(78)	(79)	1
Fees & Charges	(869)	(707)	(162)
Miscellaneous Income	(7)	(14)	7
Total DEL and Expenditure	6,807	6,895	(88)

Financial Out-turn 2005/06 - Commentary

- 2.1 A number of compensating under- and over-spends account for the overall underspend of £88,000 against the Total (DEL) Operating Budget, including the following:
- an overspend of £62,000 on accommodation costs;
 - an overspend of £35,000 on supplies and services; and
 - an overspend of £30,000 on staff costs in relation to pension costs; offset by
 - an underspend of £101,000 on depreciation and cost of capital charges; and
 - a positive variance in income against budget of £154,000, mainly as a result of the internet service Scotland On-Line.
- 2.2 The audit fee of £56,000 is not budgeted for in the Total (DEL) Operating Budget.
- 2.3 Accommodation costs at NAS have decreased from the prior year due to the capitalisation of spend on the Scottish Family History Service. This is in contrast to the significant revenue elements included in prior years within the refurbishment of GRH. However revenue spend on the refurbishment in 2005/06 remained significant at around £500,000 and the increased cost of utilities also contributed to the overspend noted above.
- 2.4 In common with organisations across the public sector NAS salary costs have increased significantly, albeit this increase was budgeted for. The spend on casual staff to fill a number of sick leave vacancies remains high and we are aware that addressing this issue remains a high priority for NAS management and is a regular subject for discussion at management meetings. NAS should continue to try and reduce the costs associated with sick leave.
- 2.5 Overall, NAS needs to ensure that it addresses the cost pressures identified and seeks to ensure it can meet its budget in future years.

Action Point 1

Action Point 2

3. Forecast Financial Position for 2006/07

Projected Position

3.1 We have summarised the projected 2006/07 budget as given in the Corporate Plan for the National Archives of Scotland in the table below:

Budget Summary

	£'000
Staff Costs	4,400
Accommodation Costs	1,500
Other running costs	841
Capital Charges	1,256
Grants	29
Total Revenue Expenditure	8,026
Fees and Charges	(715)
Miscellaneous Income	(10)
Accommodation Charges	(75)
Net Revenue Expenditure	7,226

3.2 As in prior years, NAS has not received a budgetary increase to cover staff pay-rises. Therefore this will need to be an area of particular focus for management if the budget above is to be met. We understand that NAS is currently reviewing its future staffing levels in order to ensure that the workforce does not expand to unsustainable levels.

Ongoing Capital Projects

3.3 The programme to redevelop the NAS estate has been ongoing in the year, with the commencement of work on the Scottish Family History Service including the refurbishment of the public access areas.

3.4 Budgeted spend for 2005/06 was £2.6 million. However as a result of slippage identified early in the year, expenditure of only £2.0 million was incurred, resulting in £600,000 to be carried forward into 2006/07.

3.5 The main contractor on this project (Peter Walker Group Ltd) went into receivership on 5 April 2006, leaving work unfinished and some areas of the site unsafe. NAS staff worked closely with staff from the partner organisation, General Register Office for Scotland (GROS) to address the consequences of this, including the contracting of works to render the construction site safe and the full re-tender of the remaining works in accordance with OJEC tender procedures.

Ongoing Capital Projects (continued)

- 3.6 It is our understanding that these problems are likely to lead to a delay of up to 1 year in the completion of the project.
- 3.7 At the time of our final audit visit we noted that final settlement of the bill for works done by Peter Walker Group Ltd has not been reached between NAS and the receivers. NAS has made a counter claim of almost £1.3 million for estimated losses suffered and is also in correspondence with the holders of the Performance Bond for the contract (Britsuisse Garantie). NAS is hopeful of being able to make good some of the financial losses through these means.

4. The Audit Process and Accounting Issues

Audit Process

- 4.1 The draft financial statements were audited during August 2006. We are pleased to report that we received a set of draft financial statements and supporting schedules at the start of the audit. Overall, the audit process took place largely in line with our Audit Service Plan 2005/06, albeit we had to delay the audit by one week. We would like to thank all NAS staff involved for their assistance throughout the audit process.

Preparation of Financial Statements

- 4.2 NAS prepares its financial statements to comply with the Accounting Direction given by Scottish Ministers, the Financial Reporting Manual issued by the Treasury (as amended by the Scottish Executive) and in accordance with the Public Finance and Accountability (Scotland) Act 2000.

Accounts Approval

- 4.3 The Annual Accounts are to be noted by the Audit Committee on 12 October 2006 and signed by the Accountable Officer in due course in October 2006. These arrangements and timescales have been agreed with Management.

Audit Adjustments

- 4.4 A number of audit adjustments were required to the financial statements presented to us for audit. These have been accepted by management and changes made as advised. Significant adjustments have been noted below:
- £412,000 relating to the final bill issued by Peter Walker Group Ltd had not been accrued in the draft financial statements; and
 - £57,000 relating to capital expenditure had been expensed in the draft financial statements. This was in addition to the £134,000 of revenue expenditure that was identified by NAS and transferred to capital.

5. Prevention and Detection of Fraud and Irregularities

Fraud and Corruption Reviews

- 5.1 As part of our rotational plan to review the key systems and methods for the prevention and detection of fraud and corruption we have conducted a review of the overall policies and arrangements at NAS, together with key controls surrounding asset management. Our findings in relation to this review were included in our Interim Management Letter. We identified one issue in respect of Fraud & Corruption relating to the need to maintain a cheque log for all cheques received in the mail and for this log to be signed by two members of staff as evidence of receipt.

Fraud and Irregularities Guidance

- 5.2 We have reviewed the fraud and irregularities guidance issued by Audit Scotland during 2005/06 and undertaken work accordingly. There were no matters for reporting here from this work.

Fraud Submission

- 5.3 A return is submitted to Audit Scotland of all reported frauds during the year. NAS submitted a nil return for the year.

Termination Packages

- 5.4 We are unaware of any termination packages negotiated during the year.

6. Governance Arrangements

Governance Arrangements at National Archives of Scotland

- 6.1 As part of the requirements of the Code of Audit Practice we undertook a review of the arrangements in place within NAS for ensuring appropriate financial governance arrangements. Our findings and recommendations from this review were included in our Interim Management Letter, in which we made the following recommendations regarding financial management and budgetary control:
- future budget setting processes should be initiated at an earlier stage and all budgets completed and approved in advance of the start of the new financial year;
 - the formal approval of the Corporate Plan should be recorded in the Management Board meeting minutes;
 - formal budget-setting training, such as that available from the Scottish Executive Accountancy Service, should be provided to branch heads;
 - management should liaise with the external building consultants to ensure that capital project reports in relation to SHFS are regularly reviewed and that greater effort is taken to ensure that all plans presented to Finance reflect future capital expenditure requirements; and
 - management should liaise with the Scottish Executive to ensure that relevant terms of reference are established for the Governance Board.
- 6.2 In addition to that review we followed-up on prior year recommendations (refer also to Section 7), including the recommendations made in prior years in relation to the arrangements in place for securing appropriate governance. Our findings and recommendations from this review were included in our Follow Up Report 2005/06 and included a recommendation that management should review and, where relevant update, its SLAs before arranging for them to be signed by both parties to each agreement. This point has been agreed with management and appropriate action is being undertaken to implement this recommendation for the start of 2006/07.
- 6.3 We also noted that Internal Audit undertook a review of the Corporate Governance Framework at NAS during the year. We have obtained a copy of the report issued by the internal auditors and are pleased to note that only one minor recommendation was made in relation to the introduction of an asset form to be used for all acquisitions, transfers and disposals.

Risk Management

- 6.4 Risk management is defined as “a systematic process for identifying, assessing, controlling, monitoring, reviewing and auditing risk.” Effective risk management is of importance to NAS as adverse consequences of risk could place limitations on service delivery and put a strain on staff and financial resources. To fulfil this requirement management is required to implement a robust and effective framework for the management and understanding of risk. The framework should be developed by building on existing good practice and should be used to facilitate the organisation’s planning and decision making process.
- 6.5 We understand that Local Risk Registers for each branch have been prepared and submitted to the Deputy Keeper for review and our work performed in this area did not identify any areas of concern. In addition we were pleased to note that NAS encourages all staff to take an active role in identifying and managing risk.

7. Systems of Internal Control

Statement on Internal Control

- 7.1 We do not disagree with NAS's disclosures contained in the Statement on Internal Control. NAS has used the format prescribed in the Scottish Public Finance Manual and has outlined its processes for identifying and evaluating risks. In addition, key elements of the NAS control framework have been highlighted including the risk management framework and internal and external audit input.

Follow Up Report on previous control matters

- 7.2 Our follow up report on our 2004/05 control recommendations was issued to NAS in March 2006. Of the 45 agreed recommendations made in our 2004/05 Follow up Report, 2004/05 Interim Management Letter, 2003/04 Annual Report to Management and 2004/05 Final Management Letter, nine were classed as not yet implemented, with ten recommendations that were partially implemented or where implementation was ongoing.
- 7.3 The key areas where further actions remained at the time of our review were in respect of:
- The investigation of variances against budget and the implementation of actions to address any issues identified;
 - The update of Service Level Agreements (SLAs), including the one between NAS and Internal Audit;
 - The agreement of a fee structure in relation to the Scottish Family History Service (SFHS);
 - The revaluation of land and buildings and the completion of the fixed asset verification exercise; and
 - The arrangements for ensuring that payroll records are complete and accurate and the consideration of the level of service provided by the Scottish Executive Human Resources (SEHR) function.
- 7.4 Our Follow-Up report will be provided to next year's external auditors to enable them to continue to monitor and report on progress. **Action Point 3**

Financial Systems and our 2005/06 Internal Controls Report

- 7.5 At our interim visit, we reviewed the following areas, relying on the work of internal audit where appropriate:
- internal audit;
 - financial management and budgetary control;
 - prevention and detection of fraud and corruption;
 - the legality of financial transactions; and
 - rotational review of key systems of financial control including payroll, the purchasing and payables cycle and the revenue and receivables cycle.

- 7.6 A total of seven control issues were reported to management in our Interim Management Letter 2005/06. The key issues related to the budget-setting process and capital reporting in relation to the SFHS (refer also to 6.1).
- 7.7 Our Interim Management Letter will be provided to next year's external auditors to enable them to continue to monitor and report on progress.

Action Point 3

Internal Audit's Report on NAS' Internal Controls

- 7.8 The extract of the Internal Auditor's opinion for 2005/06 is reproduced below:

On the basis of the work undertaken, we are able to provide substantial assurance in respect of NAS's risk management, control and governance arrangements. Whilst we have identified opportunities for systems' improvements and although one of the reports issued was given a limited assurance none of the issues highlighted were of a fundamental nature.

8. Best Value Follow Up

- 8.1 As part of the 2004/05 audit process, we undertook a Best Value review. This review was in the form of a self-assessment based upon initial guidance provided by the Scottish Executive.
- 8.2 An action plan was agreed with management and we noted that action is progressing against all five agreed recommendations. In particular, we noted the following:
- NAS has set up a Scottish People User Group, which meets on a quarterly basis to aid stakeholder consultation;
 - NAS is a member of the National Collections Forum, which meets to share best practice with the other collections organisations in Scotland;
 - NAS is a member of the Data Preservation Coalition and the Deputy Keeper chairs the Society of Archivists, which also encourages sharing of best practice; and
 - NAS has drafted a Departmental Sustainable Development Policy to confirm commitment to sustainability.
- 8.3 Our Best Value report will be provided to next year's external auditors to enable them to continue to monitor and report on progress.

Action Point 3

Appendix 1: Action Plan

Report Reference	Issue	Risk	Recommendation	Management Response	Responsible Officer/Due Date
1 2.4	NAS' spend on casual staff to cover sick leave remains high.	NAS may not be able to ensure that casual staff expenditure remains within the NAS approved budget.	<p>NAS should continue to try and reduce the costs associated with sick leave.</p> <p>We are aware that this is already a priority for NAS management and is regularly discussed at management meetings.</p>	<p>Agreed. We have taken steps to ensure that our line managers carry out the agreed attendance management procedures. We are now keeping our own sickness absence records to ensure that HR are fully aware of problem cases. Our service from the Sc Exec has suffered during the major HR transformation exercise which has gone on over the past few months. Things are now settling down and formal action is being taken against officers with poor sickness records</p>	Keeper of the Records Ongoing

	Report Reference	Issue	Risk	Recommendation	Management Response	Responsible Officer/Due Date
2	2.5	As in prior years NAS has not received an increase in budget to meet pay rises. In addition, there may be additional costs incurred due to the delays in relation to the SFHS.	NAS may not meet its key target of meeting its budget as approved by Scottish Ministers.	Overall, NAS needs to ensure that it addresses the cost pressures identified and seeks to ensure it can meet its budget in future years.	Agreed. We have now published a Workforce Plan and Resourcing Policy to ensure that very tight control of pay costs is maintained	D Brownlee Ongoing
3	7.4 7.7 8.3	<p>Recommendations remain outstanding from the following reports.</p> <ul style="list-style-type: none"> • 2005/06 Follow Up Report; • Interim Management Letter – 2005/06; and • Best Value Report – 2004/05. 	Identified weaknesses in NAS systems may not have been corrected.	Management should ensure that agreed recommendations are implemented with agreed timescales.	Accepted. We believe that the recommendations have now been implemented as far as possible and are content that these are notified and followed up at the next external audit.	D Brownlee 31 st March 2007

Appendix 2: Responsibilities of External Audit and the National Archives of Scotland and its Management

The matters dealt with in this report came to our notice during the conduct of our normal audit procedures which we carried out in accordance with the framework and principles contained within the Audit Scotland's Code of Audit Practice.

As a result, we may not have identified all the issues and matters that may exist. It is the responsibility of the National Archives of Scotland and its management to maintain adequate and effective financial systems and to arrange for a system of internal controls. To discharge our audit responsibility we evaluate significant financial systems and associated internal controls and where appropriate, report to management any weaknesses identified. In practice, we do not examine every financial activity and accounting procedure and we cannot substitute for management's responsibility to maintain adequate systems of internal control.

This report is intended to assist the National Archives of Scotland regarding its arrangements to implement appropriate controls surrounding the production of certain management information and processing systems. The report does not purport to provide information or advice to any person not associated with the National Archives of Scotland and we accept no responsibility to such persons. Specifically, the report should not be interpreted as providing legal advice to the National Archives of Scotland or any other party.

The prime responsibility for the prevention and detection of fraud and irregularities rests with the National Archives of Scotland. It also has a duty to take reasonable steps to limit the opportunity for corrupt practices. As part of our approach we consider these arrangements, but our work does not remove the possibility that fraud, corruption or irregularity has occurred and remained undetected.

It is the responsibility of the National Archives of Scotland and its officers to prepare the Accounts in compliance with statutory and other relevant requirements. We are responsible for providing an opinion on the Accounts.

It is the responsibility of the National Archives of Scotland to put in place proper arrangements to ensure the proper conduct of its financial affairs, and to monitor their adequacy and effectiveness in practice. We have a responsibility to review and, where appropriate, report on the financial aspects of the audited body's corporate governance arrangements, as they relate to:

- The legality of transactions that might have significant financial consequences;
- The financial standing of the audited body;
- Systems of internal financial control; and
- Standards of financial conduct, and the prevention and detection of fraud and corruption.

It is the responsibility of the National Archives of Scotland to put in place proper arrangements to manage its performance, to secure economy, efficiency and effectiveness in its use of resources. We have a responsibility to review and, where appropriate, report on the arrangements that the National Archives of Scotland has put in place to secure economy, efficiency and effectiveness in its use of resources.

We also have a responsibility to undertake reviews arising from national studies commissioned by Audit Scotland where these have been designated as mandatory studies.

For more details on any of the issues raised in this document reference should be made to those detailed reports issued by us to the National Archives of Scotland during the year and as listed at **Appendix 4**.

Appendix 3: Audit Opinion

Independent auditor's report to the National Archives of Scotland, the Auditor General for Scotland and the Scottish Parliament

We have audited the financial statements of the National Archives of Scotland for the year ended 31 March 2006 under the Public Finance and Accountability (Scotland) Act 2000. These comprise the Operating Cost Statement, the Balance Sheet, the Cash Flow Statement and the Statement of Recognised Gains and Losses and related notes. These financial statements have been prepared under the accounting policies set out within them.

This report is made solely to the parties to whom it is addressed in accordance with the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice approved by the Auditor General for Scotland and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by Audit Scotland, dated July 2001.

We do not, in giving this opinion, accept or assume responsibility for any other purpose of to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Respective responsibilities of the Agency, the Keeper of the Records of Scotland, the Accountable Officer and the Auditors

The agency and the Keeper of the Records of Scotland are responsible for preparing the annual report and the financial statements in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers. The Accountable Officer is also responsible for ensuring the regularity of expenditure and receipts. These responsibilities are set out in the Statement of Keeper of Records of Scotland's and Accountable Officer's Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and with International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Auditor General for Scotland.

We report our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers. We also report whether, in all material respects:

- the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers, the Budget (Scotland) Act covering the financial year and sections 4 to 7 of the Public Finance and Accountability (Scotland) Act 2000; and
- the sums paid out of the Scottish Consolidated Fund for the purpose of meeting the expenditure shown in the financial statements were applied in accordance with section 65 of the Scotland Act 1998.

We also report if, in our opinion, the Foreword is not consistent with the financial statements, if the agency has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by relevant authorities regarding remuneration and other transactions is not disclosed.

We review whether the Statement on Internal Control reflects the agency's compliance with the Scottish Executive guidance. We report if, in our opinion, it does not comply with the guidance or if it is misleading or inconsistent with other information we are aware of from our audit of the financial statements. We are not required to consider, nor have we considered, whether the statement covers all risks and controls. Neither are we required to form an opinion on the effectiveness of the agency's corporate governance procedures or its risk and control procedures.

We read the other information contained in the annual report and consider whether it is consistent with the audited financial statements. This other information comprises only the Foreword and the Statement of Keeper of Records of Scotland's and Accountable Officer's Responsibilities.. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with the Public Finance and Accountability (Scotland) Act 2000 and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board as required by the Code of Audit Practice approved by the Auditor General for Scotland. An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of expenditure and receipts included in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the agency and the Keeper of the Records of Scotland in the preparation of the financial statements, and of whether the accounting policies are appropriate to the agency's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinion

Financial statements

In our opinion

- the financial statements give a true and fair view, in accordance with the Public Finance and Accountability (Scotland) Act 2000 and the directions made thereunder by the Scottish Ministers, of the state of affairs of the agency as at 31 March 2006 and the net cost of operations, recognised gains and losses and cash flows for the year then ended; and
- the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers.

Regularity

In our opinion in all material respects

- the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers, the Budget (Scotland) Act covering the financial year and sections 4 to 7 of the Public Finance and Accountability (Scotland) Act 2000; and
- the sums paid out of the Scottish Consolidated Fund for the purpose of meeting the expenditure shown in the financial statements were applied in accordance with section 65 of the Scotland Act 1998.

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October 2006

Appendix 4: Other formal reports submitted during the 2005/06 process

	Financial Statements	Governance & Business Control	Performance
• Annual Service Plan 2005/06	-	-	-
• Follow Up of 2004/05 Audit Recommendations	✓	✓	✓
• 2005/06 Interim Management Letter	✓	✓	-

This report is intended solely for the information of the National Archives of Scotland (NAS). In the event that, pursuant to a request which the Agency has received under the Freedom of Information (Scotland) Act 2002, it is required to disclose any information contained in this External Audit Report, it will notify PwC promptly and consult with PwC prior to disclosing such External Audit Report. NAS agrees to pay due regard to any representations which PwC may make in connection with such disclosure and NAS shall apply any relevant exemptions which may exist under the Act to such External Audit Report. If, following consultation with PwC, NAS disclose this External Audit Report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

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