

Government and Public Sector

October 2006

# National Galleries of Scotland

Annual Report to Board Members

2005/06 Audit

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October 2006

Our ref: LP/SD/LL

Ladies and Gentlemen

**Annual Report to Board Members 2005/06**

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

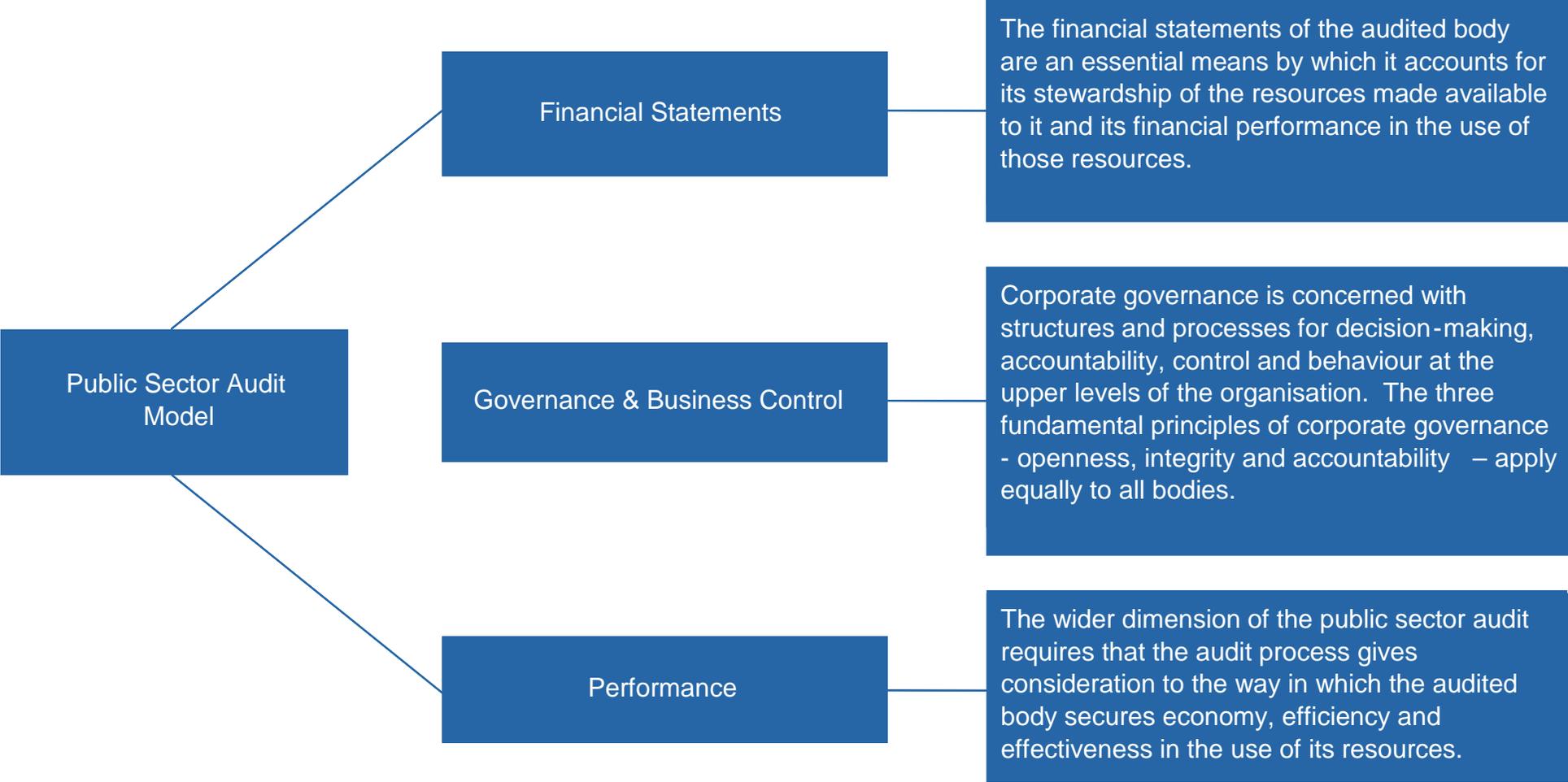
The Annual Report which follows is primarily designed to direct your attention to the key matters that have arisen out of the 2005/06 audit process and to confirm what action is planned by management to address the more significant matters identified for improvement.

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

# Our Report Structure



# 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 NGS'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 NGS's key financial target is to manage expenditure within income on a year by year basis. In 2005/06, this target was achieved. NGS has no other financial targets set for it by the Scottish Executive or other bodies, though it is expected that Value for Money is achieved. A summary of the financial performance of NGS during 2005/06 is given in Section 2 of this report.

## 2. Financial Performance and Position

### Overall Financial Performance for 2005/06

	Actual 2006 (£'000)	Actual 2005 (£'000)
<b>Income</b>		
Grant - in - aid received for running costs	10,944	10,622
Gross Income from grant-aided activities	3,750	1,854
Net income from Revenue Earning activities	-269	141
Grant - in - aid utilised for the purchase of assets	0	8,124
HMLF Grant for Dean Gallery and Playfair Project	420	1,443
Donation for Portrait Gallery redevelopment project	50	0
Donations for Playfair Project	1,507	2,225
<b>Total income</b>	<b>16,402</b>	<b>24,409</b>
<b>Expenditure</b>		
Staff costs	6,915	6,693
Depreciation and permanent diminution in value	1,753	1,374
Less released from Capital Assets Fund	-1,518	-1,223
Less released from Donated Asset Reserve	-201	-117
Other operating charges	6,380	5,783
Transfer to Capital Assets Fund	420	9,567
Transfer to Donated Assets Reserve	1,116	2,225
<b>Total operating expenditure</b>	<b>14,865</b>	<b>22,077</b>
<b>Operating surplus / deficit</b>	<b>1,537</b>	<b>2,332</b>
Investment and Other income	539	387
Notional cost of capital	-2004	-1,822
<b>Surplus for the financial year (after notional cost)</b>	<b>72</b>	<b>897</b>
Reversal of notional cost of capital	2004	1,822
Release from General Fund Revaluation Reserve	34	34
<b>Surplus for financial year transferred to reserves</b>	<b>2,110</b>	<b>2,753</b>

## Financial Out-turn 2005/06 - Commentary

- 2.1 As can be seen from the figures on the previous page, NGS achieved an overall surplus of £2.11million against a projected net budget deficit of £260,000. The main reason for this turnaround can be attributed to a VAT refund of £1.5 million arising from the favourable outcome of a VAT tribunal and the repayment of overpaid VAT in respect of the Playfair Project.
- 2.2 This VAT refund also had a favourable impact upon the cash flow position of NGS which was highlighted as a concern on our Annual Report last year and was a focus for management in the year.
- 2.3 Because of concerns over NGS's cashflow position, certain restrictions were placed upon expenditure during the year 2005/06. These restrictions included putting a hold on capital projects, including the upgrade of the Finance System and website development, meaning there have been no additions to fixed assets during the year. The exception to this is artworks which are separately funded by the Scottish Executive. A freeze on overtime and recruitment for a number of posts was also in place during the year. These restrictions on expenditure have contributed to the favourable financial performance this year. However they are short term measures which cannot be sustained in the long term.
- 2.4 The favourable variances above have been offset by poor financial performance within both retail and exhibitions.
- 2.5 A review of retail stock has resulted in a stock write off of £353,000. This write off, together with a concerted sales effort in the year, has resulted in a reduction in the year end stock position of £679,000 compared with the position at 31 March 2005. Whilst the reduction in stock levels is welcomed and has helped the overall working capital position, it has come at a significant financial cost to NGS.
- 2.6 Taking account of this stock write off, retail operations produced a deficit of £558,000. Whilst clearly the stock write off was a large proportion of this deficit, there are significant issues surrounding the costs of running the retail department. In particular, wages costs attributed to retail operations amount to 40% of retail turnover, which seems high.
- 2.7 Exhibitions continued to perform poorly in financial terms during 2005/06. The overall performance of the exhibitions showed a deficit of £273,000, against a projected deficit of £110,000. In particular, this performance can be attributed to:
- Landseer: a projected surplus of £15,000 compared with an actual deficit of £90,000 deficit;
  - Charles Rennie Mackintosh: a projected surplus of £117,000 compared with an actual surplus of £63,000; and
  - Gaugin: a projected deficit of £20,000 compared with an actual deficit of £73,000.
- 2.8 In our Annual Report for 2004/05, we highlighted the inaccuracy of budget setting, particularly in respect of exhibitions and retail and the fact that these had been consistently over-optimistic. The figures above highlight that this trend has continued in 2005/06.
- 2.9 In summary, whilst NGS has improved its financial position, much of this is due to the VAT refund received during the year. This windfall has masked a number of underlying financial pressures which will need to be addressed if NGS is to achieve a break even situation in future years, in particular in retail and exhibitions. These will remain areas which will require management attention going forward.

### Action Point 1

# 3. Forecast Financial Position for 2006/07

3.1 We have summarised the projected 2006/07 financial position for the National Galleries of Scotland in the table below:

<b>SEED Funded Revenue</b>	<b>£'000</b>
Grant-in-Aid	11,165
Self Generated Income	623
<b>Total income</b>	<b>11,788</b>
Salary costs	-7,320
Non staff costs	-2,144
Buildings and Minor Capital costs	-1,964
Exhibition costs	-93
New projects	-255
<b>Total costs</b>	<b>-11,776</b>
<b>Total SEED Funded surplus / (deficit)</b>	<b>12</b>
<b>Revenue Earning Activities</b>	
Retail	-100
Licensing	60
Friends	121
Enterprise Finance	-38
Enterprise Central	210
<b>Total revenue earning surplus</b>	<b>253</b>
<b>Net Projected Surplus</b>	<b>265</b>

## **Projected Position**

- 3.2 The table on the previous page shows that a surplus of £265,000 for the financial year 2006/07 has been projected.
- 3.3 Within this figure, a projected deficit of £100,000 has been included in respect of Retail operations. Whilst this appears prudent, it should be noted that the 2005/06 results retained an overall deficit on Retail activities of £558,000, including the stock write off of £350,000. This means that the underlying retail performance will have to improve significantly in order to meet the budgeted figure.
- 3.4 Of the eleven exhibitions planned for 2006/07, four are budgeted to make a surplus – Van Gogh, Ron Mueck, Fizzers and Harry Benson, with two forecasting a break even position (Oilworkers and Makers / Faces of Craft). This gives an overall projected surplus of £6,500. However, given the experience of out-turn performance of exhibitions, a contingency of £100,000 has been allowed for, resulting in a projected deficit of £93,000 for exhibitions.
- 3.5 One of the key issues in prior years for NGS has been the inaccuracy of budgets, particularly in respect of exhibitions and revenue-earning activities such as retail and catering. The budgets for these areas have been consistently over-optimistic, making it harder to manage the organisation's financial position. A key reason for the inaccuracies in the budgets has been the need to rely on estimates of visitor numbers, which have again been consistently over-optimistic, both for general visitors and those attending specific exhibitions. This trend of overly optimistic budget setting for exhibitions has continued during 2005/06.
- 3.6 Management should review the process by which visitor numbers are estimated, to determine whether there are any improvements that could make the estimates more accurate. Consideration should be given to liaising with other similar organisations, to understand how they prepare their forecasts and how they perform against them. Any areas of good practice identified should be adopted.
- 3.7 Furthermore, given the potential impact of retail and exhibitions on the overall financial performance of NGS, it is important that these areas in particular continue to be the subject of ongoing management scrutiny.

**Action Point 2**

**Action Point 3**

# 4. The Audit Process and Accounting Issues

## **Audit Process**

- 4.1 The annual financial statements preparation process was complicated by the absence of a Director of Finance and Corporate Services and a Head of Finance. This impacted on NGS's ability to produce a complete draft set of financial statements within the agreed timescales. Whilst we were able to start our audit in June 2006 in line with our Audit Service Plan 2005/06, the absence of a complete set of accounts did create certain inefficiencies in the audit process. However, we acknowledge the considerable efforts made by the finance team to prepare the accounts in difficult circumstances and would like to thank all NGS staff involved for their assistance throughout the audit process.

## **Preparation of Financial Statements**

- 4.2 The financial statements were prepared in accordance with the accounting requirements contained in the Charities SORP 2005 and the Government Financial Reporting Manual.

## **Accounts Approval**

- 4.3 The Annual Accounts were noted by the Audit Committee on 24 July 2006, and then recommended to the Board of Trustees where they were approved and adopted.

## **Audit Adjustments**

- 4.4 Management has been informed of audit adjustments required to the format of or figures within the financial statements presented to us for audit. These have been accepted by management and changes made as advised.

# 5. Systems of Internal Control

## Statement of Internal Control

- 5.1 We do not disagree with NGS's disclosures contained in the Statement on Internal Control. NGS has used the format prescribed in the Scottish Public Finance Manual and has outlined its risk management process. In addition, key elements of NGS's control framework have been highlighted including internal and external audit. Finally, the control issues around the retail area and stock have been disclosed, along with the controls implemented to address these.

## Follow Up Report on previous control matters

- 5.2 Our follow up report on our 2004/05 control recommendations was issued to NGS in February 2006. Of the 44 agreed recommendations made in our 2004/05 reports, 18 were classed as not yet implemented, with 5 recommendations being partially implemented.
- 5.3 A number of the recommendations which remain outstanding require the attention of the Head of Finance and the Director of Finance and Corporate Services, both of which posts have been vacant since October 2005. This has therefore had an adverse impact on NGS's overall performance in implementing action plans within the agreed timescales.
- 5.4 Key outstanding issues noted in our follow up report can be summarised as follows:
- The absence of a robust **risk management** process, which should be linked to the Corporate Planning process;
  - The absence of **stock** policies and procedures;
  - The need to improve **budget management** through the use of exception reporting and the requirement for budget monitoring to be an objective for each budget holder; and
  - The need to improve the budget setting process in relation to **exhibitions**.

## Action Point 4

- 5.5 Our follow-up report will be provided to next year's external auditors, Audit Scotland, in order that NGS's ongoing actions will continue to be monitored and reported. However, we are pleased to note that action has been taken to address a number of the outstanding points since the date of our review in February.

## **Financial Systems and our 2005/06 Internal Controls Report**

5.6 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.

5.7 A total of twelve control issues were reported to management in our Interim Management Letter in April 2006. The key issues identified related to budgetary control matters (see paragraphs 2.07-2.09) and the stock system (see paragraphs 2.16-2.18). Further minor control issues are presented in our Final Management Letter. Both reports provide details of the actions recommended to address these issues.

### **Finance Management and Budgetary Control**

5.8 During the year, the finance department has suffered from management shortages following the departure of both the Head of Finance and the Director of Finance and Corporate Services in October 2005. This staffing gap has been filled by key staff taking on greater responsibility, as well as through the appointment of an Interim Director of Finance and Corporate Services.

5.9 In our Interim Management Letter 2005/06, we commented on the fact that during our audit visit of February 2006, the most recent management accounts available were the October 2005 accounts. During our final visit in July 2006, the cashflow forecast for 2006/07 had yet to be prepared and no management accounts for the financial year 2006/07 had been prepared. The absence of such key financial information will hinder effective financial management and is particularly important given the financial challenges faced by NGS in recent years.

**Action Point 5**  
**Action Point 6**

### **Retail and Stock**

5.10 As in prior years, we have noted a number of issues in relation to the control of stock within the retail department. In particular, we highlighted the need to reconcile the stock and finance systems and mis-recording of stock balances. However, we were pleased to note that no significant audit adjustments were required in this area, as a significant review and write off of old and obsolete stock was undertaken by management at the year end.

5.11 NGS's internal auditors have recently undertaken a detailed review of retail operations and made a number of recommendations. A detailed action plan should be drawn up to address the actions outlined in their report and regular progress monitoring should be undertaken. It is likely that this will be progressed by the newly appointed Head of Retail who will have responsibility for this area.

## **Internal Audit's Report on the Galleries' Internal Controls**

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

*On the basis of the work undertaken in the year to 31 March 2006 and improvements undertaken following our reports, The National Galleries of Scotland has, in our opinion, an adequate framework of control over the systems we examined [, i.e. Retail Operations and Retail Cash & Banking Procedures].*

# 6. Governance Arrangements

## **Governance Arrangements at National Galleries 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 NGS for ensuring appropriate financial governance arrangements. Our findings and recommendations from this review were included in our Interim Management Letter. The key issue identified in respect of financial governance related to the absence of management accounts for budget holders. Furthermore, at the time of our final audit in June 2006, the cashflow forecast had not yet been prepared and no management accounts for 2006/07 had been produced.
- 6.2 In addition to that review we followed-up on prior year recommendations (refer also to Section 5), relating to financial governance arrangements. At the time of our review, action was still needed to address recommendations raised in respect of budgetary control, exhibition budgeting and the monitoring of retail costs.
- 6.3 These issues can largely be attributed to staff shortages within the finance team and we are aware that trustees feel they have received sufficient financial information. However, we do recommend that the production of management information is given the appropriate level of priority.

**Action Point 6**

## **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 critical importance to the public sector as adverse consequences of risk could place limitations on the quality of health care delivery, and put a strain on staff and financial resources. To fulfil this requirement NGS 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 NGS has both Operational and Corporate risk registers in place. Action plans have been developed for risks identified, and lead officers have been allocated responsibility for individual risks. However, at the time of our follow up visit in February 2006, the Management and Trustees Risk Registers had not been updated for 18 months, reducing the effectiveness of this control. However, we are pleased to note that this update has since been completed.

# 7. Prevention and Detection of Fraud and Irregularities

## Fraud and Corruption Reviews

- 7.1 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 NGS. Our findings were included in our Interim Management Letter which highlighted the following:
- Controls over till income for retail and exhibitions should be reviewed and strengthened in light of control weaknesses identified by management;
  - There are currently no policies and procedures in place outlining how functions within the retail operation should be performed; and
  - Issues were also noted with regard to the reconciliation between the finance and stock systems.
- 7.2 We are aware that Internal Audit has carried out further work in these areas and that a number of recommendations to improve procedures have been highlighted.

**Action Point 7**

## Fraud and Irregularities Guidance

- 7.3 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

- 7.4 A return is submitted to Audit Scotland of all reported frauds during the year. During the course of our work, we were made aware of a potential fraud relating to exhibition income whereby a member of staff was selling tickets whilst appearing to be under-ringing the till. The member of staff has since resigned her post and NGS was unable to take legal action. Despite investigations performed by NGS, it was not possible to quantify the amount which may have been misappropriated and as a result, in keeping with Audit Scotland guidance on this matter, a nil return was submitted by NGS.

## Termination Packages

- 7.5 A termination package was paid during the year a result of a compromise agreement between NGS and a former member of staff. This transaction was subject to appropriate approval.

## 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 NGS has now agreed the action plan arising from that review, with work already completed for some of the agreed actions. However, a number of the actions are not due to be completed until March 2007 and therefore have not yet been subject to audit follow up.

# Appendix 1 – Action Plan

1.

Report Reference	Issue	Risk	Recommendation	Management Response	Responsible Officer/Due Date
2.8	The financial out-turn in both retail and exhibitions for 2005/06 were significantly worse than budgeted. Whilst budgets appear to have been set more prudently for 2006/07, it will still require an improvement in underlying performance in these areas if the 2006/07 out-turn is to be achieved.	Budgeted figures may not be realistic. Lack of monitoring and remedial action could lead to NGS not achieving a balanced outturn for 2006/07.	Detailed and regular monitoring of the financial performance of retail operations and exhibitions should be undertaken throughout the remainder of the financial year and remedial action taken as necessary.	Agreed. Revised policies and procedures will be in place to take forward the next budget for 2007/8	Management Group December 2006.

	Report Reference	Issue	Risk	Recommendation	Management Response	Responsible Officer/Due Date
2.	3.6	A budgeted deficit of £110,000 in respect of exhibitions was forecast for 2005/06. However, an actual deficit of £273,000 was achieved. It is understood that adverse variances against budget are occurring as a result of inaccurate forecasting of visitor numbers.	Budgeted figures may not be realistic. Lack of monitoring and remedial action could lead to NGS not achieving a balanced outturn for 2006/07.	Management should review the process by which visitor numbers are estimated to determine whether there are any improvements that could make the estimates more accurate. Consideration should be given to liaising with other similar organisations to understand how they prepare their forecasts and how they perform against them. Any areas of good practice identified should be adopted.	As Above	As Above
3.	3.7	A number of issues have been highlighted in respect of retail operations (for example, stock levels and staff costs) which have had an adverse impact upon the financial position of NGS.	Poor performance in retail operations will continue to impact the overall financial performance of NGS.	The new Head of Retail should carry out a detailed assessment of the retail operations with a view to turning around financial performance.	Agreed. This again will lead into the budget for 2007/08. Internal Audit will follow up progress on their recommendations from previous reports in February 2007.	Head of Retail. March 2007.

	Report Reference	Issue	Risk	Recommendation	Management Response	Responsible Officer/Due Date
4.	5.2	Recommendations from previous reports are not being implemented within agreed timescales.	Absence of controls could mean that loss of errors remain undetected.	Management should ensure that agreed recommendations are implemented as a matter of priority.	Agreed.	Head of Finance. March 2007.
5.	5.9	As at July 2006, the cashflow forecast for 2006/07 had not been prepared.	NGS is unaware of its projected cashflow position for the year. Significant cashflow problems have been noted in prior years. A lack of information in this area prevents forward planning which could in turn adversely affect cash management.	Management should ensure that the cashflow forecast for 2006/07 is prepared at an early date. In the coming years, such forecasts should be prepared well in advance of the financial year in question to ensure that all relevant staff are aware of and understand the projected position of the organisation, to allow for appropriate action for the whole of the financial year. This will allow planning to be undertaken, to ensure that working capital requirements are managed throughout the year.	Agreed. This will form part of an ongoing revision to the management accounts information.	Head of Finance March 2007

	Report Reference	Issue	Risk	Recommendation	Management Response	Responsible Officer/Due Date
6	5.9 and 6.3	As at July 2006, no management accounts for the financial year 06/07 had been prepared.	<p>Management is not monitoring the financial position of NGS.</p> <p>Inadequate information may result in poor performance, which could impact upon NGS's ability to achieve a break-even position at the year end.</p>	Management accounts should be prepared on a monthly basis, with the exception of month one. These should be prepared within two weeks of month-end and circulated to all relevant officers for their information.	As Above	As Above
7.	7.2	A number of issues have been highlighted in respect of the controls in operation within retail.	Poor procedures increase the risk of loss whether through fraud or mis-management.	Management should draw up an action plan to address the weaknesses identified in retail operations.	Agreed. The newly appointed Head of Retail has started this process	Head of Retail. March 2007.

# Appendix 2 – Responsibilities of External Audit and the National Galleries 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 Galleries 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 Galleries 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 Galleries of Scotland and we accept no responsibility to such persons. Specifically, the report should not be interpreted as providing legal advice to the National Galleries of Scotland or any other party.

The prime responsibility for the prevention and detection of fraud and irregularities rests with the National Galleries 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 Galleries 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 Galleries 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 Galleries 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 Galleries 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 Galleries of Scotland during the year and as listed at **Appendix 4**.

# Appendix 3 – Audit Opinion

## **Independent auditor's report to the members of National Galleries of Scotland, the Auditor General for Scotland and the Scottish Parliament**

We have audited the financial statements of the National Galleries of Scotland for the year ended 31 March 2006 under the National Heritage (Scotland) Act 1985. These comprise the Income and Expenditure Account, the Statement of Financial Activities, the Balance Sheet, the Cash Flow Statement and the 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 or 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 board, Accountable Officer and auditor**

The board and Accountable Officer are responsible for preparing the annual report and the financial statements in accordance with the National Heritage (Scotland) Act 1985 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 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 National Heritage (Scotland) Act 1985 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. We also report if, in our opinion, the Foreword is not consistent with the financial statements, if the body 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 body's compliance with the Scottish Executive's 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 body'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 Chairman's Foreword and the Report of the Trustees. 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. It also includes an assessment of the significant estimates and judgements made by the board and Accountable Officer in the preparation of the financial statements, and of whether the accounting policies are appropriate to the body'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 National Heritage (Scotland) Act 1985 and directions made thereunder by the Scottish Ministers, of the state of affairs of the body as at 31 March 2006 and of its surplus, total 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 National Heritage (Scotland) Act 1985 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.

*PricewaterhouseCoopers LLP  
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Edinburgh, EH2 4NH*

*August 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	✓	✓	-
• 2005/06 Final Management Letter	-	✓	-

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