Grant Thornton

Registers of Scotland

Audit of Accounts 2010-11
Annual Report to Registers of Scotland and the Auditor General for Scotland

10 August 2011

Contents

1 Executive Summary

Purpose of the report

1.1 We have audited the financial statements of the Registers of Scotland (RoS) for 2010-11, and examined aspects of RoS's performance and governance arrangements. This report sets out our key findings.

1.2 This report meets the mandatory requirements of International Standard on Auditing 260 (ISA 260) to report the outcome of the audit to 'those charged with governance', designated as the Audit Committee. The requirements of ISA260, and how we have discharged them, are set out in more detail at Appendix C.

Audit conclusions

Financial results

1.3 At 31 March 2011, RoS reported a loss for the financial year of £30.4 million (2010: £24.3 million). The deficit for the year reflects the continued depression of the housing market.

1.4 The financial results for the year are also impacted by an impairment charge of £3.1 million caused by the abandonment of the e-Settle and Content Management System (CMS) IT projects in the year. These projects formed part of a larger IT development project operated in partnership with BT.

1.5 Looking forward, RoS currently project that activity in the housing market will remain low for the foreseeable future and it therefore expects to continue to operate at a trading loss over the business planning period. The latest corporate plan projections to 2014, however, indicate that expected losses will be lower than originally anticipated due to the reduction in costs emerging from the restructuring exercise during the year and the increase in fees from 2011. However, there remains a risk that RoS may not achieve its target level of reserves of £75 million by 2014.

Financial Statements

1.6 We intend to provide an unqualified opinion on the 2010-11 financial statements of RoS, and on the regularity of transactions undertaken during the year following approval of the accounts by the Board on 25 August 2011.

1.7 We were presented with draft financial statements and accompanying working papers in line with the agreed timetable of 20 June 2011. As in previous years, the working papers were of a high standard.

1.8 The main audit issues for the financial statements related to the asset impairment referred to above and the valuation of Work In Progress.

Governance

1.9 We found that RoS's governance arrangements continue to operate well and within a generally sound control environment, although we noted that internal audit could provide only limited assurance on the management of the BT Partnership. We confirm that RoS complies with good practice guidance in relation to governance, as outlined in the Scottish Public Finance Manual, in so far as it is relevant to the role of RoS.

1.10 The successful completion of IT projects under the Strategic Partnership Agreement (SPA) continues to represent the key area of management risk. The SPA was subject to a Gateway review by the Scottish Government during 2010-11 which highlighted significant challenges in delivering the vision of the Partnership and questioned whether key outcomes remained achievable. The completion of these IT projects remains under constant management review continues to be a key senior management priority.

1.11 The total cost of the various IT projects and services operating under the SPA arrangement was £102 million at 30 April 2011, against an original budget of £66 million. The total cost of all projects to the end of the partnership in 2014 is currently estimated to be £132 million.

1.12 A number of projects have however, been impacted by delays and there remains a significant risk that they will not be completed by the time the 2014 contract ends. In addition, new registration requirements emerging from proposed changes from the new Land Registration Act may change existing processing arrangements with a consequent impact on IT system requirements. The future of some of the projects currently being developed under the SPA therefore remains uncertain.

Performance

1.13 RoS has successfully achieved its statutory target on efficiencies and 10 out of 15 of the Keeper's KPIs have been achieved. The 5 targets not achieved were only missed by a small margin and performance overall is regarded as satisfactory.

1.14 RoS has not yet fully updated its assessment of compliance with the principles of Best Value and more work needs to be done to complete this assessment and to support the Accountable Officer in discharging her duty to demonstrate the delivery of best value in the use of resources.

Next Steps

1.15 Matters arising from the financial statements audit have been discussed with the Director of Finance. We have made a number of recommendations, which are set out in the action plan at Appendix A. A summary of progress against prior year recommendations is set out at Appendix B.

Use of this report

1.16 This report has been prepared solely for use by RoS to discharge our responsibilities under the Code of Audit Practice, and should not be used for any other purpose. This report is part of a continuing dialogue between RoS and Grant Thornton and is not, therefore, intended to cover every matter which came to our attention. Our procedures are designed to support our audit opinion and they cannot be expected to identify all weaknesses or inefficiencies in RoS's systems and work practices.

1.17 The report is not intended for use by third parties and we do not accept responsibility for any reliance that third parties may place on it. The report will be submitted to the Auditor General for Scotland and will be published by him on his website at **www.audit-scotland.gov.uk**.

Acknowledgements

1.18 We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the RoS's staff.

Grant Thornton UK LLP

10 August 2011

2 Financial results

Financial results

2.1 At 31 March 2011, RoS reported a loss for the financial year of £30.4 million (2010: £24.3 million). Table 1 below summarises the financial results for the year:

Table 1: Financial results for the year ending 31 March 2011

	2011 £'000s	2010 £'000s
Turnover	47,755	43,554
Staff Costs	46,073	42,240
Depreciation	5,091	5,318
Other operating expenditure	24,138	20,666
Asset Impairment	3,102	23
Interest received	438	541
Interest paid	229	238
Gain/loss on sale of fixed asset	4	
Loss for the year	**(30,444)**	**(24,367)**

2.2 Turnover has increased by £4.2 million to £47.7 million in the year. The increase in turnover is mainly due to: higher dispatches for transfers of part (6,426/27%) and dealings with whole (21,745/11%), together with higher prices following the implementation of the Fees in the Registers of Scotland Amendment Order 2010, which took effect from January 2011.

2.3 The asset impairment of £3.1 million reflects the losses incurred in writing off the costs associated with the development of the e-Settle and Content Management System (CMS) projects.

2.4 Staff costs have increased by £3.8 million (9%) to £46 million. This increase largely reflects the £6.4 million additional costs incurred by RoS in completing its staff restructuring programme. Average staff numbers have fallen from 1,327 in 2010 to 1,262 in 2011 following that restructuring programme and wages and salaries fell by £1.7 million during the year.

2.5 Other operating costs have increased by £3.4 million (17%). The majority of this relates to additional service charges by BT for the review of e-Settle, and increased costs for maintaining legacy systems as e-Settle and CMS will not now proceed and the overall IT project has encountered significant delays in completion.

Budget Outturn

2.6 RoS's 2010-11 financial projections forecast an operating deficit of £28.5 million for the year against the final outturn of an operating deficit of £25.4 million. The outturn variance against budget is explained by variances in both income and expenditure for the year. The budget outturn for 2010-11 is shown in Table 2 below:

Table 2: Budget outturn for the year ending 31 March 2011

	2011 £'000	Corporate Plan £'000
Turnover	47,775	48,760
Operating costs	(78,404)	(77,267)
Loss (before interest)	**(30,629)**	**(28,507)**

2.7 Although income in the year is higher than predicted in the corporate plan, there has been a decline in work in progress (£0.8 million) in the year versus a budgeted increase (£1.4 million). Expenditure is higher reflecting mainly the impact of asset impairment costs that were not included in the budget (£3.1 million) offset by lower than expected costs in communications and legal services (£1.6 million).

Financial position

Corporate Plan

2.8 In 2008-09, the Auditor General for Scotland published a report under Section 22(3) of the Public Finance and Accountability (Scotland) Act 2000 to bring to the Scottish Parliament's attention the impact of the economic downturn on the financial position of RoS. As part of our audit, we have reviewed the financial position and future financial strategy of RoS in the current difficult economic conditions.

2.9 RoS published its corporate plan for the 3 year period to 31 March 2014 in March 2011. The corporate plan provides substantial revisions to previous financial projections, following restructuring within the organisation and the impact of the 2011 fee order price increases.

2.10 The revised financial projections included in the corporate plan indicate that RoS will continue to report an operating loss for the next three years, although this is smaller than previously predicted and in the 2010 to 2013 corporate plan. Table 3 highlights the financial projections from the plan over the next three years:

Table 3: Three year projected outturn

	2011-12 £'000	2012-13 £'000	2013-14 £'000
Turnover	59,352	57,344	58,089
Operating costs	(67,594)	(66,580)	(66,884)
Loss	**(7,892)**	**(10,068)**	**(8,890)**
Reserves	64,238	54,351	49,085

Source: Registers of Scotland Corporate Plan 2011-2014

2.11 The current financial projections estimate a combined loss of £26.7 million over the next three financial years to 2014. The rate of losses is significantly lower than the previous corporate plan of £35 million to 2013, reflecting mainly the impact of reductions in staff and the increase in fees from January 2011.

2.12 The current projections indicate a stable financial position for RoS based on the current forecasts and reserves position. Despite the reduction in anticipated losses, there are a number of challenges and uncertainties for the organisation over the next few years that may impact on finances:

- a new land registration bill which may alter how the organisation currently operates
- the end of the Strategic Partnership Agreement (SPA) with BT in 2014, and decisions on future provision of IT services
- any moves to extend coverage of the land register.

2.13 We note that the action taken by RoS over the last year to increase fees and reduce costs has stabilised the financial position and reduced the rate of annual losses expected, however, the introduction of the new Land Registration Act, the land register extension project and ongoing challenges in managing and completing the SPA project, continue to present an increased financial risk. In our view, management are alert to these challenges and the financial position is subject to continuous review and robust scrutiny.

Reserves

2.14 The accumulated retained profit as at 31 March 2011 was £72.9 million (2010: £103.3 million). The reduction in reserves reflects the reported deficit for the year.

2.15 RoS has continued to review its reserves policy during the year, and the latest review was undertaken in April 2011. The organisation's reserve targets versus corporate plan expectations are shown in the table below:

Table 4: Reserves

	2011-12 £'000	2012-13 £'000	2013-14 £'000
Reserves per the corporate plan	64,238	54,351	49,085
Reserves target	50,000	50,000	75,000
Variance	14,238	4,351	(25,915)

Source: Registers of Scotland Corporate Plan 2011-14/Reserves paper 28 April 2011

2.16 The current reserves policy requires minimum reserves of £50 million to meet operational requirements (market downturns and indemnity claims) and investment (IT and restructuring). RoS estimate this should increase to £75 million by 2014 in order to cover increased provision for market downturns.

2.17 On current projections, the reserves paper indicates that although RoS may be financially able to meet the financial challenges of the next three years, there will not be sufficient reserves by the end of the corporate plan period based on current projections of losses.

Action plan point 2

3 Financial statements

Introduction

3.1 This section provides a summary of matters arising from our audit of the financial statements. This includes matters arising from our evaluation of key controls and misstatements arising from the audit.

3.2 We audit the financial statements and give an opinion on whether:

- they give a true and fair view, in accordance with the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers, on the state of affairs of RoS as at 31 March 2011 and of its net expenditure, recognised gains and losses and cash flows for the year then ended
- they, and the part of the Remuneration Report to be audited, have been properly prepared in accordance with the Government Financial Reporting Manual (FReM) and directions made thereunder by the Scottish Ministers
- 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.

3.3 We also review the Statement on Internal Control by:

- considering compliance with Scottish Government guidance
- considering the adequacy of the process put in place by the Accountable Officer to obtain assurances on systems of internal control
- assessing whether disclosures in the Statement are consistent with the information emerging from our normal audit work.

Key risks

3.4 Our Audit Approach Memorandum for 2010-11 set out the key risks we identified relating to the audit of the financial statements. As part of our interim audit, we completed work in a number of areas to consider these risks and reported our findings in our Interim Audit Report. As part of our final accounts audit, we reviewed some remaining risk areas and have set out in below, the outcome of work completed.

Key risk	Work completed
Impairment of capital works in progress Management were currently considering whether to abandon or curtail the e-settle project. There had already been significant capital spend to date on this project and an assessment of impairment at the balance sheet date under IAS 36, *Impairment of Assets*, was required to assess if any write down was necessary.	Management carried a full impairment review of capital works in progress related to the BT contract and the following projects were impaired: • e-settle • CMS See section 3.10 for more details.
WIP calculation and provision ROS records significant amounts of 'work in progress' in its balance sheet at the end of the financial year. The identification and calculation of work in progress can be complex, and there is a risk of material misstatement of the financial position should systems to identify and calculate work in progress not operate effectively. During 2009-10, we highlighted that the complexities of the system also lead to management relying on a number of assumptions to calculate the WIP year end balance. We recommended that management reduce the complexity of the WIP calculation to improve the usefulness of the information generated from the system.	We updated our prior year review of the systems to record WIP, and attended the count of WIP cases at the year end. See section 3.19 for more details.

3.5 The Audit Committee has confirmed that it is not aware of any additional material risk areas facing RoS that we have not addressed in our audit. In particular, there are no significant fraud risks that we are required to consider for the purposes of our audit.

Audit conclusions

3.6 We intend to provide an unqualified opinion on RoS's financial statements, and on the regularity of transactions undertaken during the year, following approval of the accounts by the Audit Committee and the Board.

3.7 We carried out our audit in accordance with the Audit Approach Memorandum presented to the Audit Committee on 29 March 2011. Additional work was required to support the review of the BT capital projects as outlined in section 3.10.

3.8 Our audit is substantially complete, subject to the following finalisation procedures:

- receipt of the signed letter of representation

Matters arising from the financial statements audit

3.9 We were presented with draft accounts on 13 June 2011, in line with the agreed timetable. The working papers provided continue to be of good quality.

Impairment of capital projects

3.10 In 2003, RoS entered into a Strategic Partnership Agreement (SPA) with BT to provide and upgrade the organisation's IT systems. A key feature of the SPA since its inception has been both the large overspend against budget, and ongoing delays in project completion. Since the new management structure of RoS came into effect in 2010, management have prioritised their review of the SPA and responded to audit recommendations to improve the management of the BT contract.

3.11 Two issues arose in 2010-11 that prompted an impairment review of all the projects under the SPA:

- the CMS project was completed, however it was identified that revenue costs would be in excess of £1 million and were significant and unaffordable, and management decided to return to using the relevant legacy system.
- testing of the effectiveness of the e-Settle system identified that it did not achieve the required levels of accuracy in processing registration cases. Management paused the implementation of e-Settle early on in the financial year, and subsequently decided that the project should not proceed.

3.12 As these assets have been effectively abandoned in the course of construction, management have processed an impairment charge of £3.1 million to remove their net book value from the Statement of Financial Position.

3.13 Management's impairment review did not highlight any other projects that were impaired, however £0.6 million of capitalised costs were released as management did not consider they added any value to the organisation.

ARTL

3.14 The Automated Registration of Title to Land (ARTL) project is one of the more significant elements of the BT project. The project enables solicitors to process dealings with whole transactions remotely and securely, which is more efficient and lower cost than the traditional process. However, since the project became operational, the uptake of ARTL has been much lower than expected, mainly due to the slowdown in the property market. As such, a more detailed impairment review was carried out of the project.

3.15 The Government Financial Reporting Manual (the i-FReM) requires government bodies to follow International Accounting Standard 36, *Impairment of Assets*, for calculating the impairment charge for assets. In line with IAS 36, management have considered independent cash flows in the form of savings in staff costs due to the uptake in use of ARTL by users rather than the traditional method using RoS staff. The independent cost savings from using ARTL can then be discounted to ascertain the value in use of the asset.

3.16 Management concluded from their review that the expected uptake of ARTL over the next 3 year period would approach 20% of capacity from the current position of 8%. Achieving this forecast would indicate that the asset is not impaired as the cost savings associated with operating at 20% capacity would exceed the net book value of the asset. We note, however, that there remain a number of risks and uncertainties in relation to the calculation and achievement of the forecast level of uptake, including:

- decisions by lenders to mandate the use of ARTL in transactions for their panel of solicitors, with a decision already taken by the Lloyds Banking Group, the largest mortgage lender in Scotland. This is expected to significantly increase the uptake of ARTL

- other uses of ARTL that benefit the Scottish economy, such as:
    - provision of a service for the secure transfer for legal documents
    - the collection of Stamp Duty Land Tax in Scotland, which will become important when this tax is devolved to the Scottish Parliament.

3.17 Whilst management's impairment review is based on a number of assumptions, our assessment indicates that these assumptions are robust and we agree with management's conclusion that there is no indication of impairment at this stage.

3.18 We have however, recommend that the ARTL project is regularly reviewed to ensure its carrying value remains appropriate in line with IAS 36.

Action plan point 3

Work in progress

3.19 The RoS balance sheet records a significant inventory balance at the end of each financial year (2010-11: £2 million). This represents work in progress (WIP) in the form of the value of land registration transactions processed in the period for cases that are not yet completed. The calculation of WIP requires the finance team to collect significant amounts of financial information on cases and the calculation process can be complex.

3.20 Our 2009-10 audit identified a number of audit adjustments to the WIP balance:

- WIP reports were not run at the year-end date, which added to the complexity of the reconciliation process
- the use of linked spreadsheets is subject to human error
- the lack of detailed employee information from timesheets leads to the adoption of complex assumptions
- the lack of management information from the registration system means RoS cannot calculate a WIP balance in year.

We noted that management have not yet implemented a new system for calculating WIP and as a result are still using the linked spreadsheet approach and complex assumptions on employee time. However, a number of modifications to the system have taken place which have improved the process, including:

- WIP reports were produced to enable a reconciliation between the IRIS and e-financial systems to be undertaken at the year date
- more detailed information from registration staff has been gathered to allow a more accurate reflection of time spend on particular tasks to be recorded.

3.21 Our audit of the year end WIP balance did not identify any significant errors, although we would recommend that RoS continue to seek to simplify the system. An adjustment of £1.3 million was processed by management to correct an error in the WIP balance after the initial accounts had been drafted. The error was caused by the knock on effect of a change to the expense figures used to calculate WIP.

Employee benefits accrual

3.22 During the year, RoS changed the methodology used to calculate the year-end holiday pay accrual. Due to a lack of a centralised and automated system for recording holiday pay, RoS uses a sample approach to calculating the holiday pay liability at the balance sheet date.

3.23 In prior years, a sample size of 100% was used, and this was reduced to 50% in 2009-10. The sample was reduced further to 10% in 2010-11, in an effort to save on the organisational effort to review holiday returns for a large number of staff.

3.24 We concluded that the reduced sample size remained sufficient for the calculation of the liability. However in the absence of an automated system, we have recommend that a basis for determining the sample adopted for the calculation of holiday pay is reviewed to ensure it captures different pay scales and job types, in order to obtain a more representative sample of the workforce.

Adjusted misstatements

3.25 Management identified four adjustments to the draft financial statements as listed in table 5 below.

Table 5: List of management adjustments

Adjustments affecting reported results	Operating Income Statement		Statement of Financial Position	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Prepayments To bring prepayment into line with altered project length.	BT Expenses 174			Prepayments 174
Software and computer inventory To write off capitalised software subsequently considered revenue in nature.	Software inventory 130	Software deprecation 28 Software inventory 102	Software acc dep'n 28 Software permanent diminution 102	Software asset 130
Permanent Diminution Being client identified over provision for permanent diminution.		Permanent diminution 620	Hardware permanent diminution 620	
Work in Progress Impact of expenses adjustments on the WIP.	Movement in WIP 1,357			WIP 730 WIP Provision 627
	1,661	**750**	**750**	**1,661**

In addition, the following adjustment identified by the audit process has been processed by management:

Table 6: List of adjusted misstatements

Adjustments affecting reported results	Operating Income Statement		Statement of Financial Position	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Indemnity claim provision To update indemnity provision for one case following post year end correspondence and to reduce a provision for one case after re-evaluation.		Legal expenses 33	Indemnity claim provision 33	

3.26 The overall effect of the management and audit adjustments is to increase the deficit for the year by £878,207.

3.27 In addition to the matters raised above, there were a number of other minor presentational changes that arose during the course of our audit and these have been processed through the accounts.

Unadjusted misstatements

3.28 The following adjustments were proposed by the audit team but have not been amended in the draft accounts. Had they been amended, the loss for the year would have been increased by £58,000.

Table 7: List of unadjusted misstatements

Adjustments affecting reported results	Operating Income Statement		Statement of Financial Position	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Bad debt provision A provision was proposed for debts outstanding from other government bodies as we could not see any evidence that they were recoverable.	Bad debt expense 18			Bad debt provision 18
Missing accrual An invoice was identified which should have been accrued at the year end for the refurbishment work.	Refurbishment costs 40			Accruals 40
	58			**58**

3.29 These adjustments both individually and combined are not material to the financial statements by size or nature and therefore we will accept them as unadjusted.

Evaluation of key controls

3.30 We have undertaken sufficient work on key financial controls for the purpose of designing our programme of work for the financial statements audit. Our evaluation of RoS's key financial control systems did not identify any control issues that present a material risk to the accuracy of the financial statements, with the exception of one key reporting point in relation to processing of journals:

- some journals are processed and authorised by the same individual. This increases the risk that fraud or error in journal entry processing will not be detected and represents a segregation of duties control weakness.

Action plan point 4

3.31 We carried out a high level review of the general IT control environment as part of our review of the internal control system and concluded that there are no material weaknesses within the IT arrangements that could adversely impact on our audit of the accounts. We issued a separate report on IT controls in July 2011.

3.32 The Internal Auditors, Pricewaterhouse Coopers LLP, have issued their opinion on the effectiveness of the system of internal control. Pricewaterhouse Coopers LLP confirm that moderate assurance can be taken on the design, adequacy and effectiveness of the system of internal control. Their opinion reflects the fact that they could provide only limited assurance over the effectiveness of RoS's arrangements for managing its partnership with BT.

Statement on Internal Control (SIC)

3.33 The Statement on Internal Control sets out the arrangements established and operated by RoS for reviewing the effectiveness of the system of internal control and the identification and management of risk. We have examined RoS's arrangements and processes for compiling the SIC. In addition, we read the SIC and considered whether the statement is in accordance with our knowledge of RoS.

3.34 We reviewed the draft SIC and are satisfied that it complies with guidance contained in the Scottish Public Finance Manual. We are also satisfied that the process put in place by the Accountable Officer to obtain assurances on systems of internal control are adequate, and that the contents of the Statement are consistent with the information obtained from our normal audit work.

3.35 The main weakness identified in the SIC relates to controls over the management of the SPA with BT and these disclosures are consistent with the findings of internal audit and of the Gateway review report.

Annual report

3.36 We considered RoS's arrangements for compilation and submission of its annual report and received a complete draft annual report in sufficient time to undertake the required audit procedures prior to reporting to the Audit Committee.

3.37 We reviewed the draft annual report and are satisfied that the content of the annual report, including the remuneration report, is in accordance with the Government Financial Reporting Manual and our knowledge of RoS.

4 Governance

Introduction

4.1 Corporate governance is the system by which organisations direct and control their functions and relate to their stakeholders, and incorporates the way in which an organisation manages its business, determines strategy and objectives and goes about achieving those objectives. It is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of the organisation.

4.2 As part of our 2010-11 audit, we assessed the adequacy of RoS's governance arrangements against good practice standards for the public sector. Overall, we found that RoS's governance arrangements operated well and within a generally sound control environment, although we noted that internal audit could only provide limited assurance on the management of the BT partnership. RoS complies with the good practice guidance in relation to governance, as outlined in the Scottish Public Finance Manual, in so far as it is relevant to the role of RoS.

4.3 Our Audit Approach Memorandum for 2010-11 set out the key risks relating to the governance aspects of our audit. Exhibit two below highlights the work completed against each risk area.

Key risk	Work completed
Financial management and budgetary control The last three years have seen a significant decline in the housing market in the United Kingdom, and the impact of this is expected to continue to be felt into 2011. The downturn will continue to impact on the land registration business and the reported results for 2010-11. Since the appointment of the new management team in 2009-10, RoS has been moving to stabalise its financial position, and has initiated a number of actions to achieve this: • restructuring of processes and reduction in staff counts • move to delegated budgeting • improving the quality and usefulness of management accounts. For the year to end of January 2011, RoS reported a loss of £20.9 million, with a forecast loss for the financial year of £27.2 million . This compares to the corporate plan predictions for 2010-11 of a loss of £28.2 million.	RoS implemented a delegated budgeting system during the year, although full use of the system has been delayed until 2011-12 due to operational capacity issues. This change is expected to increase operational staff involvement in the budgeting process, and strengthen links between finance and the rest of the business. In 2010-11, internal audit produced a report, *Budgetary Controls Review*, which highlighted that management were making good progress in implementing the new delegated budgeted system. This report included one high risk finding relating to the lack of formal monthly review and challenge of budget variances. Management plan to incorporate such a review into their monthly process. As part of our audit, we considered management's updated response to Audit Scotland's financial management toolkit. We noted that good progress is being made to move towards better and advanced practice from the new system procedures.

<table>
<tr><th>Key risk</th><th>Work completed</th></tr>
<tr><td>Capital programme and the BT contract
The effective management of the BT partnership remains a key strategic priority for the organisation. However there are a number of ongoing issues relating to the partnership relevant to our audit:
During 2009-10, there were significant changes to the management structure at RoS, and a new IT director was appointed. However the IT director has now resigned, and RoS is recruiting consultants to replace this key resource.
A number of recommendations from internal and external audit and the Gartner review remain outstanding. Management are considering an action plan to identify and prioritise these outstanding recommendations.
RoS may abandon or curtail the e-settle project, which has already seen significant capital spend to date.
There remains a risk that RoS may not obtain best value from capital projects if they are not carefully monitored and managed. In addition, there is a reputational risk to the organisation if high value capital projects are not seen to achieve value for money or deliver anticipated benefits for its users.</td><td>We considered the governance and control arrangements for monitoring the BT Contract and on-going capital programme, and reviewed the Gateway report issued by the Scottish Government.

This included liaison with the internal auditors in co-ordinating and prioritising the number of audit recommendations outstanding on the contract.

See section 4.4 for more details.</td></tr>
<tr><td>IT controls
We carried out a follow up of outstanding IT control issues in 2008-09. The key findings of this report were around service continuity, and data management.

We noted that there was no documented data management policy which has been issued to staff in order to ensure compliance with the Act. RoS will be providing detailed training on data protection to ensure compliance with the Act and will be aiming to formalise procedures at this time.

RoS and BT are working together in a service continuity project to provide a more resilient system for the current IT infrastructure.</td><td>We have issued a separate report on the progress of implementation of outstanding IT recommendations.

We note that only two prior recommendations have been fully implemented at this stage. We note that of the eight recommendations not fully implemented, four are rated as higher risk and these are detailed below:
a secure data transfer mechanism should be implemented
password settings should be enabled in the e-financials system
the privileged user account password in e-financials should be encrypted and not presented in clear text onscreen
the service continuity project should be completed to enable effective disaster recovery procedures to be implemented.</td></tr>
</table>

Key risk	Work completed
Public Service Reform (Scotland) Act The Public Services Reform (Scotland) Act 2010 received Royal Assent on 28 April 2010. Part 3 of the Act will require RoS to publish a statement of expenditure which has been incurred during the financial year in relation to: public relations, overseas travel, hospitality and entertainment, external consultancy. In addition, disclosures of persons earning over £150,000 will be required Draft guidance has been published by the Scottish Government on how public bodies should respond to Part 3 of the Act.	RoS has taken steps to ensure the finance systems can capture and report this information. There are plans in place to ensure the required information is collected and reported in line with Scottish Government requirements.

The Strategic Partnership Agreement

4.4 On 1 December 2004, RoS entered into a Strategic Partnership Agreement (SPA) with BT for the provision of all information systems and IT services. Under the terms of the SPA, all existing IT assets of RoS where transferred to BT. The SPA agreement covers 2 parts: the ongoing IT service provision which runs to 2014; and specific change programmes to update the IT systems and applications.

4.5 The main projects as part of the agreement are as follows:

- BOSI (Back Office System Initiatives)- projects to automate the registration process at RoS. This includes e-Settle, a project to automate the registration process.
- PFSI (Public Facing System Initiatives)- projects which are public facing, ie used by third parties. This includes ARTL (Automated Registration of Title to Land), an electronic system used by solicitors.

4.6 Since the time period the SPA has been in operation a number of issues have arisen:

- a number of projects are significantly over the original budget
- a number of projects are delayed in terms of implementation
- there has been a significant change in the conditions in the housing market since 2004, particularly from 2007/2008 with the significant falls in Scottish house prices, and a corresponding drop in mortgage activity by the UK banks and building societies.

4.7 Throughout this process, the SPA has been subject to internal and external scrutiny from both auditors, independent consultants (Gartner), management, and the Scottish Government (Gateway review). This process has led to a number of issues being identified in relation to the management of the SPA and its future direction. Specifically for the 2010-11 audit, management have now identified that a significant amount of capital and revenue expenditure on certain projects in the SPA will have to be written off as these projects will either no longer be brought into use, or will be significantly curtailed.

Financial position

4.8 As at 30 April 2011, the total contract spend on the SPA was £102.2 million versus the original budget of £66.3 million. Table 8 below highlights the main areas of expenditure to date.

Table 8: SPA expenditure breakdown

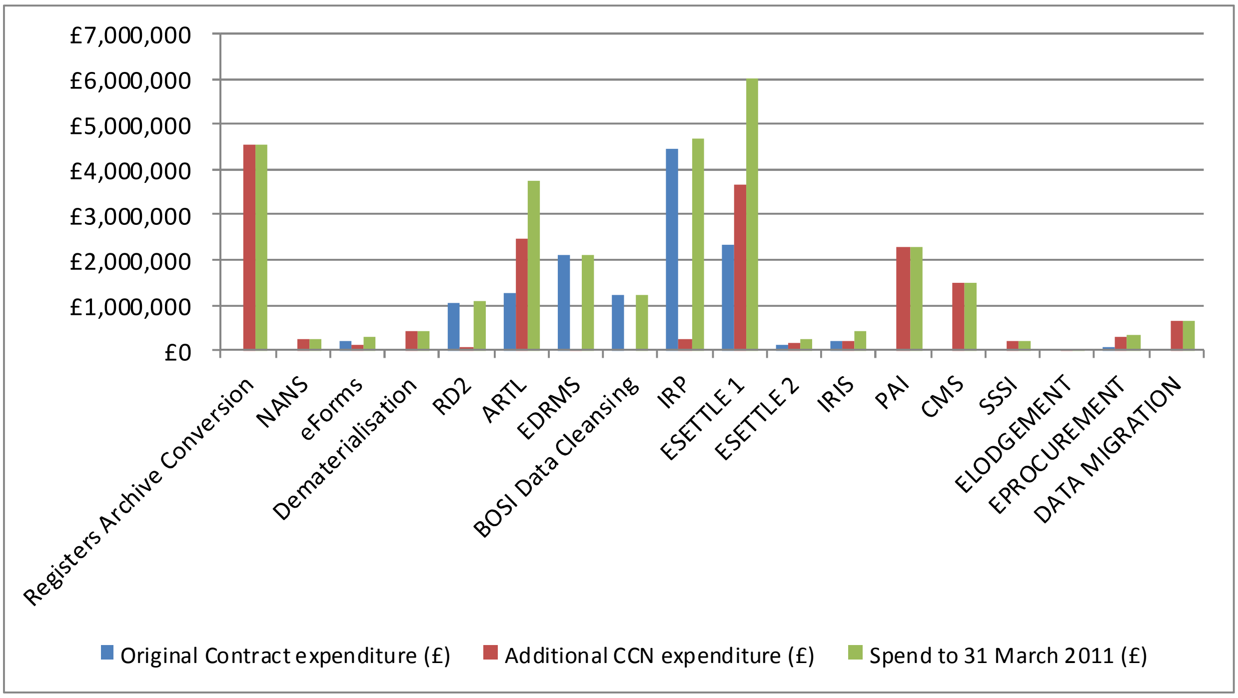
	Budget (£)
Original budget	£ 66,300,000
Current spend (to 30 April 2011)	£102,178,778
Analysis of key budget variances:	
Core Service Charges	£ 46,631,110
New IT Projects	£ 30,162,202
Maintenance of Legacy Systems	£ 9,230,792
Replacement IT infrastructure (eg desktops)	£ 7,852,911
Smaller Projects	£ 5,713,786
Secondees	£ 1,358,000
Unallocated	£ 1,229,977
Total Spend to 30 April 2011	**£102,178,778**

Source: Internal audit, ***Analysis of expenditure on BT Contract for the period covering 1 April 2004 to 30 April 2011***

4.9 RoS currently estimate that the total cost of the SPA to completion in 2014 will be £132.3 million. This will be some £66 million higher than originally forecast but, as outlined in Table 5 above, the scope and scale of the SPA has changed significantly since its original inception.

The overspend against budget is caused by a number of factors, but mainly due to programme changes emerging after the original contract was agreed. The total value of change control notices (CCNs) for key contracts to date is £17.1 million. Exhibit 1 below highlights the movements in key projects from the original contract expenditure to current budgeted figures once change notes have been processed. Many of these projects, whilst shown separately in this analysis, form part of the development of a larger, shared, IT system.

Exhibit 1: Analysis of SPA Cost Variances by Project



The main projected variances are listed below:

- Additional ARTL- £1.4 million for incorporation of digital signatures
- Registers Archive Conversion- a joint project with National Archives of Scotland to digitise the Register of Sasines- £4.8 million

- Register of Floating Charges- a new statutory register brought in with the Bankruptcy and Diligence etc. (Scotland) Act 2007- £1.9 million
- Integrated Registration Project- £1.4 million for additional changes after the SPA was agreed

In addition, the continuing operation of Legacy Systems by BT due to delays in completing projects has also significantly increased the costs of the contract. These excess costs fall across a number of project headings and now exceed £3 million.

Gateway review

4.10 The Gateway review is published by the Scottish Government with the purpose of establishing if the benefits set out in the project's business case are being achieved and if the operational service is running smoothly. The gateway 5 review on the Strategic Partnership Agreement was published by the Scottish Government in January 2011.

4.11 The overall conclusion from the review was to grade the SPA Project as "*red*", which is defined as "Successful delivery of the project/programme appears to be unachievable. There are major issues on project/programme definition, schedule, budget required quality or benefits delivery, which at this stage do not appear to be manageable or resolvable. The Project/Programme may need re-baselining and/or overall viability re-assessed".

4.12 The main areas highlighted include:

- failure to deliver the vision of 'transformational change' described in the Final Business Case
- there have been significant issues with the time, cost and quality of project delivery
- RoS lost sight of the forecast benefits and the contractual relationship has not functioned as a partnership.

4.13 The findings from the Gateway review highlight the significance of the challenge facing RoS management to gain full control over the SPA and ensure it delivers the key benefits identified at the outset.

Internal and external audit recommendations

4.14 Over the course of our appointment as external auditors to RoS, there have been a number of recommendations made to improve the management and operation of the SPA following a number of different reviews and including reviews by internal audit and external consultants. During the year, we worked with the internal auditors and RoS management to review and restate these recommendations, which can be broadly fitted into four themes as shown below:

Exhibit 2: Analysis of internal and external audit recommendations

Governance	Delegated budgeting
• The business case for the BT Partnership did not adequately state the purpose and benefits to be delivered from the partnership with BT meaning that the benefits cannot be measured appropriately. • Additional costs were approved through Change Control Notices (CCNs) at project level, with limited consideration of the impact of CCNs on individual projects or indeed on the overall BT contract. • There was a tendency (given the positive financial position at the time) to default to superior specifications (e.g. bespoke IT products) without challenge that these were really necessary. There was also a tendency for RoS management to proceed straight to solution mode without necessarily considering all the possible options.	• Previously at RoS, budgets were not delegated resulting in a lack of accountability/responsibility regarding expenditure and cost control
Skills and Capacity	**Culture**
• The BT contract was entered into as a major IT transformation programme and RoS may not have had sufficient IT skills and expertise to manage and cope with the scale of the IT project. The basis of the contract was that BT would understand RoS' business and IT requirements and deliver these. When delivery then became an issue, RoS attempted to specify in detail to manage this position. They did not have the skills to carry out this detailed specification role. • The programme was expanded to meet changing business needs and customer expectations and the failure to prioritise and phase developments resulted in a large number of projects being undertaken at the same time. This gave rise to strain on both BT's ability to deliver and also on the capacity of RoS management to manage.	• Decisions were made without the use of formal and robust options appraisals which were subject to detailed scrutiny. • Setting unreasonable targets (eg 100% accuracy) which may not be achievable • A culture was in place where issues were not escalated. This resulted in issues being contained at a lower level within the organisation meaning that senior RoS staff did not have visibility of the overall issues impacting projects. • Not completing post project reviews

4.15 Internal audit have grouped these recommendations into a report, *BT Partnership- Contract Review*, which was presented to the audit committee in March 2011. The report has an action plan of management responses to the audit recommendations. Progress in implementing these recommendations is monitored and reported regularly.

2010-11 issues

4.16 As noted in Section 3.11, there is a significant impairment charge of £3.1 million resulting from the abandonment of two key projects: e-settle (£2.7 million) and the Case Management System (£0.4 million). However the total constructive loss is £6.8 million of which £4.6 million is capital costs and £2.2 million revenue costs.

4.17 With regards to e-settle, the project was abandoned due to the failure of the system to meet the required level of registration accuracy. The Case Management System (CMS) was abandoned due to excessive running costs that were not identified at the business planning stage.

4.18 The costs associated with the write off of these assets and the associated revenue costs are significant to the organisation. These costs are indicative of significant weakness in the project management arrangements adopted by RoS in authorising these projects from the outset, as they failed to identify significant potential costs and risks associated with the planning, monitoring, reporting, delivery and benefits realisation for these projects.

Action plan point 5

Looking forward

4.19 A new Chief Information Officer was appointed in June 2011 to fill the vacancy left following the resignation of the previous IT director in January 2011. In the interim period the Deputy Keeper assumed responsibility for the Information Services division, supported by external consultants.

4.20 RoS has however, lacked an effective client commissioning and monitoring function and this represents one of the key weaknesses in its arrangements for managing the SPA with BT. The recent appointment of a new IT director presents a significant opportunity to mitigate this key risk and to improve the ongoing relationship with BT. However there remains a number of key risks going forward that the organisation must continue to address:

Financial

- the costs of the SPA remain high and significantly above that reported in the original business case. There remains a significant challenge to ensure the project remains within existing budget projections and represents 'best value' for the organisation
- significant capital investment has already been written off and there is a risk that more capital may need to be written off due to changes in delivery requirements or new legislation with a potential impact on the overall financial position.

Operational

- the SPA continues to take up a large proportion of senior management time in the organisation, and there is a risk that other strategic areas of the business may not receive adequate oversight as a result
- there remains a challenge to improve and development the working relationship between BT and RoS staff to maximise the effectiveness of project outcomes.

Governance and Regularity

- there is significant risk in operating the partnership, and there must be processes to ensure RoS delivers the partnership in line with governance and regularity requirements as identified in the Gateway Review. Relevant factors include ensuring there is a proper client function, effective strategic oversight of key decisions, sufficient budgetary control and monitoring procedures, ensuring business cases are robust and sustainable, budget holders are identified and accountable and success criteria are clearly articulated and performance monitored
- ensuring significant changes to projects are supported by a robust business case which is reviewed and authorised by management at the appropriate level
- appropriate governance procedures for end date of the project in 2014, including procedures for the retender exercise and for evaluating the impact of potentially ending the relationship BT.

Reputational

- RoS has incurred significant costs through the SPA and many projects have not been delivered or are behind schedule – increasing the reputational risk to the organisation and its management
- RoS may face a loss of confidence from its stakeholders if it is felt that the SPA has not delivered value for money in a time of constraint in the Scottish economy generally

Action plan point 6

5 Performance

Introduction

5.1 Public audit is more wide-ranging than in the private sector and covers the examination of, and reporting on, performance and value for money issues. As part of our annual audit we are required to plan reviews of aspects of the arrangements to manage performance, as they relate to economy, efficiency and effectiveness in the use of resources.

5.2 The Accountable Officer has a duty to ensure public resources are used economically, efficiently and effectively. These arrangements were extended in April 2002 to include a duty to ensure best value in the use of resources.

Best Value

5.3 RoS has not formally updated its overall approach to best value since 2007-08, when the Scottish Government's best value checklist was completed. The organisation has undergone significant change since this original review and the Scottish Government has recently issued updated guidance to Accountable Officers on compliance with best value principles. In light of these changes, RoS should complete a further review of its performance in relation to best value principles in 2011-12. We note that specific work was carried out in relation to financial management and budgetary control (see 4.3).

Action plan point 7

Statutory targets

5.4 Section 9 of the Public Finance and Accountability (Scotland) Act 2000 sets out the financial arrangements for RoS and states that the Keeper of the Registers of Scotland is required "to achieve such financial targets as the Scottish Ministers may from time to time determine".

5.5 Up to 2010-11, Scottish Ministers had traditionally set the Keeper a financial target to achieve a specified return on capital employed. This was altered for 2010-11, whereby a target was set to achieve 2% cash releasing efficiency statements for the year to 31 March 2011, a move taking the organisation into line with the targets imposed on other Scottish Government bodies.

5.6 For the year to 31 March 2011, RoS has recorded efficiencies of 3% (£2 million), which is in excess of the target. The bulk of the identified efficiency savings come from savings in overtime payments (£1.2 million) with the rest coming from procurement (£0.8 million).

5.7 The target set by Scottish Ministers for the year 2011-12 is 3%, and RoS has plans in place to achieve this target, with procedures agreed by management to record progress against the target throughout the year.

The Keeper's performance targets

5.8 The Keeper sets performance targets for the organisation to achieve. Table 9 below highlights the key performance targets for registration for 2009-10 and the outturn position.

Table 9: Keeper's performance targets outturn

Detail	Target	Outturn
Standard FR applications within 60 working days	80%	96.52%
Standard FR applications despatched within 60 to 120 working days	20%	3.48%
Standard FR applications taking longer than 120 days	0%	0%
Standard DW applications within 60 working days	80%	98.99%
Standard DW applications despatched within 60 to 120 working days	20%	1.01%
Standard DW applications taking longer than 120 days	0%	0%
Sasine writs within 20 working days	80%	99.9%
Sasines Despatched within 21 to 40 working days	20%	0. 1%
No writ taking longer than 40 working days	0%	0%
ARTL Transactions within 24 hours	100%	99.84%
Record all applications for registration on the application record within one working day.	100.0%	99.9%
Registration accuracy	98.5%	98.45
Backlog reduction- FR	20,259	19,956
Backlog reduction- TP	30,029	30,566
Customer Service enquiries cleared on time	98%	98.5%
Achieving a 98% rating for overall customer care in the annual customer satisfaction survey	98%	94%

Source: Registers of Scotland

5.9 Overall, RoS achieved 10 out of the 15 key performance targets. The following targets were not achieved:

1 The ARTL turnaround target was not achieved due to a technical problem during the years
2 The application recording target was also not achieved due to technical problems arising from a server outage, and technical problems following the implementation of the new fees system
3 The registration accuracy target was not achieved by a marginal result of 0.1%
4 The backlog reduction in first registrations was also not achieved
5 Customer service target was not achieved following the results of the customer care survey.

Audit Scotland National Reports

5.10 Audit Scotland periodically undertakes national studies on topics relevant to the performance of central government bodies. While the recommendations from some of the studies may have a national application, elements of the recommendations are also capable of implementation at local level, as appropriate.

Procurement

5.11 In July 2009, Audit Scotland published a report, Improving Public Sector Purchasing, which made a number of recommendations for public bodies to improve procurement practices. As part of our audit, we have consider RoS's response to the report

5.12 Currently RoS spends around £16.3 million in procurement each year, the bulk of which is through national government collaborative contracts. Our audit confirms that RoS has a dedicated procurement function and does not operate a delegated purchasing authority system. We also noted that RoS include procurement savings in its annual efficiency savings target.

5.13 We note that RoS is participating in the Scottish Government's Procurement Capacity Assessment (PCA) programme. The results of the PCA exercise for both 2009-10 and 2010-11 were at "Superior" level for RoS, which is the highest award.

5.14 There are no recommendations based on our follow up work relating to procurement.

Use of consultants

5.15 In January 2009, Audit Scotland published a report, Use of Consultancy Services, which made a number of recommendations for the Scottish Government and central government bodies to improve practice and value for money from the use of consultants. As part of our audit, we have considered RoS's response to the report.

5.16 The total estimated spend on consultants at RoS is £1 million (6% of total expenditure[1]). RoS considers it has sufficient controls over the use of consultancy expenditure, with requirements for analysing consultancy expenditure and obtaining value for money embedded into the process for obtaining business plans and by performing post implementation reviews.

[1] Data from Audit Scotland/Scottish Government Information Hub for 2009-10

A Action Plan

Rec. No.	Para Ref	Recommendation	Risk	Management response	Implementation date and responsibility
1	2.8	**Financial projections** The current financial projections estimate a combined loss of £26.7 million over the next three financial years to 2014. The rate of losses is significantly lower than the previous corporate plan of £35 million to 2013. Despite the reduction in anticipated losses, there are a number of challenges and uncertainties for the organisation over the next few years that may impact on finances. In particular the current corporate plan indicates that the target level of reserves will not be achieved by 2014. We recognise that management are aware of the financial challenges facing the organisation, and we would recommend that the financial projects continue to updated and subject to scrutiny on the robustness of the financial projections.	**High**	**Accepted** Financial projections are reviewed each month, as part of the quarterly budget reviews and as part of the corporate planning process. Market conditions are also reviewed monthly.	LAP Ongoing but specifically in Corporate Plan 2012- 15

Rec. No.	Para Ref	Recommendation	Risk	Management response	Implementation date and responsibility
2	3.10	**Impairment of capital projects** The 2010-11 accounts record a significant impairment charge for projects under the SPA that will either no longer continue, or will not be utilised. We recommend that a formal review of impairment is undertaken at each balance sheet date for ongoing capital projects, and consider: • delays in project implementation • projects that are not achieving their planned benefits and which ultimately may not be utilised • any incidences of planned obsolescence (eg from the new land registration bill) • utilisation levels for any key systems such as ARTL.	Medium	**Agreed** We intend to review the fixed assets together with our FA policies in 2011-12 and will conduct an impairment review for 31 Match 2012	LAP 31 March 2012
3	3.22	**Holiday pay accrual** We noted that the methodology for the holiday pay accrual was reduced from a 50% sample of employees to 10% in 2010-11. Although we were satisfied with the accuracy of the overall liability as calculated under this approach, there was no defined methodology for ensuring a representative sample of employees was obtained. The holiday pay accrual methodology using the 10% sample threshold should incorporate the methodology for selecting the sample to ensure an adequate representative sample is obtained for an accurate calculation of the liability.	Low	**Agreed**	Stephen Welham February 2012

Rec. No.	Para Ref	Recommendation	Risk	Management response	Implementation date and responsibility
4	3.30	**Journals** We noted that a large majority of journals were processed and authorised by the same individuals. This increases the risk that inappropriate journal entries or errors are processed through the financial statements. There should be adequate segregation of duties between the preparer and authoriser of journals. All journals should be reviewed and authorised independently of the preparer.	Low	**Agreed** We intend to review the process for year-end journals to ensure that they are timely and also that there is adequate segregation. This will apply with immediate effect.	Stephen Welham Immediate.
5	4.16	**Constructive losses** There was total constructive loss is £6.8 million relating to e-settle and CMS systems after those projects were abandoned in the year. Management should learn the lessons from the abandonment of these projects in particular: • ensuring relevant costs are identified in the business plan to ensure projects offer value for money • problems in the delivery of projects are identified and acted upon in a timely manner.	**High**	PPRs will be conducted for both projects. The CMS PPR is underway. Training on business cases is to be provided by NSG.	LAP 31 December 2012

Rec. No.	Para Ref	Recommendation	Risk	Management response	Implementation date and responsibility
6	4.19	**BT Contract and Future** The SPA is due to formally end in 2014, and management are looking ahead to the future to determine IT requirements beyond this date. Management need to consider their responses to the key risks surrounding the operation of the contract and consider future options in order to deliver best value for the organisation.	**High**	Agreed Management have already begun the preparation of exit and transition strategies for the end of the BT contract.	LAP December 2012
7	5.3	**Performance and Best Value** We would recommend that management complete the relevant best value checklist from the Scottish Government as part of a formal review of the organisation's approach to demonstrating compliance with best value principles.	Medium	We had updated our BV approach by using the Audit Scotland Financial management Checklist and intended to roll this out further in 2011-12. We will carry out a further self-assessment.	LAP December 2012

B Summary of progress against prior year recommendations

Rec. No.	Recommendation and Risk	Management response	Position at July 2011
1	**Work in Progress (WIP)** The calculation of the WIP balance remains complex and we noted the following issues during the audit: • WIP reports were not run at the year end date, which adds to the complexity of the reconciliation process • the use of linked spreadsheets which are subject to human • error • the lack of detailed employee information from timesheets which leads management to employ complex assumptions • the lack of management information from the registration system which means RoS cannot calculate a WIP balance in year. RoS should investigate alternative methods of calculating WIP, which would be more efficient and useful to the financial management process. Risk: **High**	Accepted The model for calculating WIP needs to rebuilt and significantly simplified. This will be done in 2010-11. LAP December 2010	**Partially implemented** The process for calculation of the WIP balance has improved, but some of the inherent complexities remain (eg use of linked spreadsheets, lack of detailed timesheets and inability to calculate WIP throughout the year).

Rec. No.	Recommendation and Risk	Management response	Position at July 2011
2	**Efficiency** The internal efficiency target for the year to 31 March 2010 was not achieved. The year end performance indicates that efficiency declined by 12% in the year, and this may provide evidence that the organisation has more work to do to refine its structures, systems and processes to become more effective in the current climate. We recommend that RoS reviews the efficiency of the organisation to ensure that costs are more aligned with the production requirements. Risk: **High**	Accepted RoS is currently carrying out a strategic review of its processes to ensure that they are cost effective and efficient. This review will take up to two years to carry out and implement effectively. The first two milestones are recorded to enable the Committee to monitor progress.	The SPCI calculation of efficiency is no longer calculated, and instead RoS records efficiency against the Scottish Government target of 2% efficiency savings. The efficiency target for 2010-11 was achieved and a summary of performance against this target is reported at section 4.
	Audit Scotland national reports Management should ensure all relevant national reports produced by Audit Scotland are received and reviewed in a timely manner. Reports should be considered by relevant management committees and if appropriate, an action plan to implement performance improvement recommendation should be produced. Risk: Low	Noted Audit Scotland reports are received and reviewed. Where appropriate these are circulated to the relevant managers. I am happy to put in place a more formal note of this process. LAP Immediate	Implemented Relevant reports are issued and summary of action taken reported to the audit committee.

C The small print

Purpose of memorandum

This Report has been prepared for the benefit of discussions between Grant Thornton, the Audit Committee and the Board of Registers of Scotland (RoS).

The purpose of this memorandum is to highlight the key issues affecting the results of RoS and the preparation of the organisation's financial statements for the year ending 31 March 2011.

This document is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

We would point out that the matters dealt with in this report came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements of the organisation.

This memorandum is strictly confidential and although it has been made available to management to facilitate discussions, it may not be taken as altering our responsibilities to the organisation arising under the Code of Audit Practice.

The report will be submitted to the Auditor General for Scotland and will be published by him on his website at **www.audit-scotland.gov.uk.**

Responsibilities of the Board, Accountable Officer and auditors

The Board and Accountable Officer are responsible for the preparation of the financial statements and for making available to us all of the information and explanations we consider necessary. Therefore, it is essential that the Board and Accountable Officer confirm that our understanding of all the matters in this memorandum is appropriate, having regard to their knowledge of the particular circumstances.

Clarification of roles and responsibilities with respect to internal controls

RoS's management is responsible for the identification, assessment, management and monitoring of risk, for developing, operating and monitoring the system of internal control and for providing assurance to the Board and Accountable Officer that it has done so.

The Board and Accountable Officer are required to review the organisation's internal financial controls. In addition, they are required to review all other internal controls and approve the statements included in the annual report in relation to internal control and the management of risk.

The Board and Accountable Officer should receive reports from management as to the effectiveness of the systems they have established as well as the conclusions of any testing conducted by internal audit or ourselves.

We have applied our audit approach to document, evaluate and assess your internal controls over the financial reporting process in line with the requirements of auditing standards.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you.

In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify.

We would be pleased to discuss any further work in this regard with the Board and Accountable Officer.

Independence and robustness

Ethical standards require us to give you full and fair disclosure of matters relating to our independence.

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opnინion on the financial statements.

In accordance with best practice, we analyse our fees below:

	£ incl VAT
Grant Thornton UK LLP	55,000
Audit Scotland fixed charge	3,900
Additional fees charged for 2010-11 audit	24,000
Total	82,900
*** Fees are inclusive of VAT**	

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