



Registers of Scotland

Audit of Accounts 2009-10

Annual Report to Registers of Scotland and the Auditor General for Scotland

23 July 2010

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1 Executive Summary

Purpose of the report

- 1.1 We have audited the financial statements of the Registers of Scotland (RoS) for 2009-10, 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 A.

Audit conclusions

Financial results

- 1.3 At 31 March 2010, RoS reported a deficit for the financial year of £24.7 million (2009: £4.6 million deficit). The operating deficit was significantly greater than the budgeted deficit of £18.4 million. The deficit for the year reflects the continued depression of the housing market together with a planned reduction in Registers Direct pricing.
- 1.4 RoS has published its corporate plan for the period 2010-2013, and the current financial projections indicate that the organisation will continue to incur losses over the next three years, although the size of the losses will reduce due to structural changes in staffing and operational costs.
- 1.5 Fees for land registration activity are formally set by Scottish Ministers on advice from the Keeper. The Keeper has now introduced biennial fee reviews for registration and information fees, and a consultation is currently underway for the next fee review. Any increase in fees agreed by Scottish Ministers will improve RoS's financial position.

Financial Statements

- 1.6 We intend to provide an unqualified opinion on the 2009-10 financial statements of RoS, and on the regularity of transactions undertaken during the year following approval of the accounts by the Board on 2 September 2010.
- 1.7 We were presented with draft financial statements and accompanying working papers in line with the agreed timetable of 21 June 2010. As in previous years, the working papers were of a high standard.
- 1.8 The main audit issue for the financial statements was confirmation of the work in progress balance, which continues to be complex and reliant on spreadsheets that are subject to human error. The complexities of the system also lead to management relying on a number of assumptions to calculate the WIP year end balance. We have recommended that management reduce the complexity of the WIP calculation and improve the usefulness of the information generated.

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 only provide 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 effective management of the BT partnership remains a key strategic priority for the organisation. During 2009-10, there were significant changes to the management structure at RoS, and a new IT director has been appointed. Management are currently collating and reviewing outstanding audit points from across a range of reviews of the partnership, and specific management time has been set aside to tackle and clear these issues.
- 1.11 We reviewed the financial management and budgetary control procedures at RoS using the Audit Scotland financial management toolkit. The toolkit assesses financial management practices using a grade of basic, better or advanced. We concluded that the majority of practices at RoS are currently considered basic, although some specific elements of financial management were found to be better/advanced. We note that RoS are currently moving to a system of delegated budgeting and we expect this to make a significant contribution to RoS improving its overall financial management and budgetary control process and move towards the better/advanced ratings.

Performance

- 1.12 RoS has successfully achieved its statutory target on the Return on Capital Employed for 2009-10. However the internal efficiency target was not met by some margin, and this indicates that the organisation has more work to do to refine its structures, systems and processes to become more effective in the current climate. In addition, five of the Keeper's ten performance targets for the year were not met.
- 1.13 The Keeper has reviewed and revised the targets for 2010-11, and Ministers have set a new 2% cash releasing efficiency target. The new efficiency target is more in line with the targets set for other government departments, and gives greater control to RoS in being able to ensure the target is achievable.

Next Steps

- 1.14 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 B.

Use of this report

- 1.15 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.
- 1.16 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

- 1.17 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

23 July 2010

2 Financial results

Financial results

- 2.1 At 31 March 2010, RoS reported a loss for the financial year of £24.4 million, a significant increase from the reported loss of £4.1 million in 2009. Table 1 below summarises the financial results for the year:

Table 1: Financial results for the year ending 31 March 2010

	2010 £'000	2009 £'000
Turnover	43,554	55,605
Staff Costs	42,240	39,796
Depreciation	5,318	4,121
Other operating expenditure	20,666	21,748
Interest received	541	6,206
Interest paid	238	247
Loss for the year	(24,367)	(4,101)

- 2.2 Turnover has shown a continued reduction in the current year due to the ongoing downturn in the property market. Total land registration intakes declined by 122,000 cases, a reduction of 31% on 2009, whereas despatches declined by 128,000, a reduction of 30%. The most significant reductions have taken place in Dealings with Whole where intakes have dropped by 33% and despatches by 34%. Given the influence of the re-mortgage market on this income stream, this level of decline is expected and in line with the limited availability of mortgage finance in the current economic climate.
- 2.3 Staff costs have increased in the year, although the staff base on the whole has decreased. The increase results from the general pay award in the year and an exceptional charge of £1 million for early retirement costs.
- 2.4 Other operating costs have reduced in the year by £1.1 million (5%) on 2009, mainly due to the impact of 'buying out' the costs of staff secondments from the BT contract in 2008-09 resulting in a high charge last year (c£1million) and a corresponding nil charge for these costs in the current year. Cost savings have also been achieved due to the decline in activity, the closure of the canteen and a reduction in consultancy costs in the year.
- 2.5 Net interest income is significantly lower than the prior year due to the Bank of England base rate remaining at historic lows of 0.5% throughout the year.. This has been compounded by the lower level of investments with the National Loan Fund, and the reduction in the overall cash position of RoS.

Budget Outturn

- 2.6 RoS's 2009-10 financial projections forecast an operating deficit of £18.4 million for the year against the final outturn of an operating deficit of £24.4 million. The outturn variance against budget is explained by variances in both income and expenditure for the year. The budget outturn for 2009-10 is shown in Table 2 below:

Table 2: Budget outturn for the year ending 31 March 2010

	2010 £'000	Budget £'000
Turnover	43,554	55,605
Operating costs	68,278	76,295
Loss*	(24,367)	(18,447)

*Loss is shown after interest not included in operating costs above

- 2.7 Turnover is behind budget as anticipated volumes were significantly behind actual reflecting a more severe decline in the property market than predicted. Operating costs are behind budget due to lower than anticipated staff costs and management efforts towards the end of the year to contain costs and meet financial targets.

Reserves

- 2.8 The accumulated surplus on the Income and Expenditure Account as at 31 March 2010 was £103 million (2009: £127.7 million). The reduction in reserves reflects the reported deficit for the year.
- 2.9 RoS has continued to review its reserves policy during the year, and the latest review was undertaken in May 2010. The 2010-13 Corporate Plan assumes reserves will fall to £20 million by 31 March 2013. Management have, however, set revised reserves targets of £50 million for the period 2012-13, and £75 million to £100 million by 2014-15 following the May 2010 review. The ability of RoS to achieve the target reserves will depend on the outcomes of the fee review and cost reduction programs.
- 2.10 RoS previously included the costs of Land Register Extension (the costs of subsidising the transfer of properties from the General Register of Sasines to the Land Register). RoS no longer earmarks the costs of this in the current reserves policy but have indicated that reserves would need to increase to at least £100 million to adequately fund any extension. RoS have noted that it is for the Scottish Ministers to determine if this project is to go ahead and how it should be funded.

Return on Capital Employed

- 2.11 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".
- 2.12 Scottish Ministers had previously set the Keeper a financial target to achieve a 10% return on capital employed (ROCE) for the 3 year period to 31 March 2009. The target was not met in 2008-09 due to the slowdown in the property market and the target was reviewed at the end of 2008-09, and subsequently reduced to -6% for 2009-10.
- 2.13 For 2009-10, the actual 3 year ROCE achieved was -5.88%, and the statutory target has, therefore, been met for the year. This represents a significant achievement for RoS in the

current economic climate, and is in part due to more stringent financial control exercised during the year.

- 2.14 For 2010-11 onwards, the Scottish Ministers have decided not to set a Return on Capital Employed target for the Keeper. Instead a financial target to deliver "2% increasing cash releasing efficiencies in each year" has been set, which is in line with the targets set for other Scottish Government departments.

Looking forward

- 2.15 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.
- 2.16 RoS published its corporate plan for the 3 year period to 31 March 2013 in March 2010. The corporate plan provides substantial revisions to previous financial projections, as more up-to-date information becomes available on movements in house prices and the volume of transactions. 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 will start to decline due to cost reduction efforts. Table 3 highlights the financial projections from the plan:

Table 3: Three year projected outturn

	2010-11 £'000	2011-12 £'000	2012-13 £'000
Turnover	47,069	48,654	48,569
Operating costs	74,276	67,641	64,055
Loss*	(25,516)	(20,043)	(15,770)
Reserves	66,887	38,591	22,232

Source: Registers of Scotland Corporate Plan 2010-2013

*Loss stated after interest not included in operating costs above

- 2.17 RoS recognises the importance of managing cost and securing efficiency in its operations. The reduction in activity caused by the downturn in the property market, and the change in future projections around continued low levels of re-mortgaging activity going forward, highlight the need for a more detailed review of staffing levels and operational efficiency. The Director of Finance has been charged with taking forward this review and we anticipate progress in this area over the coming financial year.
- 2.18 The Keeper has submitted proposals for a review of the existing fee structure as a means of securing the financial position of the organisation. This review is currently out for consultation, but if implemented would have a significant impact on improving the financial position of the organisation. RoS plans to review its pricing structure at least every 2 years to ensure it continues to be able to respond flexibly and effectively to changes in levels of activity.
- 2.19 RoS has also continued to keep its reserve balances under close scrutiny, and expects reserve balances to move towards more sustainable levels (estimated to be £75 million) over the longer term.

- 2.20 Our 2010-11 audit will continue to closely monitor developments in improving both RoS's financial position and developments in securing economy, efficiency and effectiveness in its operations.

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 2010 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 (FRoM) 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 2009-10 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 Exhibit One below, the outcome of work completed.

Key risk	Work completed
<p>International Financial Reporting Standards (IFRS) Central government bodies are required to prepare their accounts on the basis of IFRS 2009-10.</p>	<p>We have reviewed and audited the IFRS adjustments between the 2008-09 closing balances and the IFRS adjusted balances. We noted no issues from this review and balances have been translated correctly as required by International standards.</p> <p>We have completed a financial statement disclosure checklist which has confirmed all accounting disclosures are appropriate and in line with IFRS.</p>

Key risk	Work completed
<p>WIP calculation and provision</p> <p>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.</p>	<p>Following our interim audit, we made a number of recommendations to improve the WIP calculation methodology and to ensure reconciliations between the registration system and the ledger were completed effectively.</p> <p>A summary of the work completed on WIP at the financial statements audit is included below.</p>
<p>Impairment</p> <p>There is an increased risk of asset impairment, in light of the economic downturn and continued downturn in the UK property market. This could potentially have a material impact on RoS's financial statements. RoS should assess whether indicators of impairment are present. If there are indicators of impairment, a full impairment review will need to be carried out</p>	<p>At the year end RoS had the Meadowbank House head office revalued. The valuation was completed by DTZ.</p> <p>Land and Buildings cost has been revalued by RoS to amounts per the DTZ valuation. Land values increased by £333,940 to £1,330,000 and Buildings values decreased by £3,487,262 to £4,790,000. The depreciation charged on the building, which equalled £854,891 at the year end, has been eliminated, in line with accounting requirements. The net of the journals to cost and depreciation (£2,294,495) has been agreed as adjusted in the revaluation reserve.</p> <p>We have concluded that the accounting for the asset revaluation has been completed in accordance with accounting standards.</p>
<p>IT</p> <p>We performed a follow up of outstanding IT control issues in 2008-09. The key findings of this report related to weaknesses in service continuity, and data management arrangements.</p> <p>We noted that there was no documented data management policy which had been issued to staff in order to ensure compliance with the Data Protection 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.</p> <p>RoS and BT are working together in a service continuity project to provide a more resilient system for the current IT infrastructure.</p>	<p>Our IT auditor has completed a follow up review of the outstanding action plan points from the 2008-09 IT review.</p> <p>We identified 4 performance improvement opportunities and categorised 2 of our findings as medium risk as outlined below:</p> <ul style="list-style-type: none"> • RoS does not have a secure data transfer mechanism that meets Scottish Government Security Group requirements • RoS and BT have not yet agreed a process to address the system vulnerabilities identified following the recent penetration testing of the security of IT systems.
<p>Indemnity provisions</p> <p>Under the Land Registration (Scotland) Act, 1979 the Keeper is required to indemnify against losses resulting from errors made by RoS. Provision is made in the accounts for indemnity claims, based on the expected value and result of each individual claim. There is a risk that the accounts could be materially misstated if estimated outcomes prove sufficiently wrong, or if the list of claims is not complete.</p>	<p>We selected a sample of cases and reviewed these against the case files to establish the facts and arguments put forward by each party. We assessed the details of each case to provide us with comfort that the provision established for each case is adequate.</p> <p>We also compared the provision of the prior year against the amounts paid in the year to provide comfort over the controls in place to set provision levels.</p> <p>Our audit concluded that the provision was reasonable, calculated in line with accounting standards, subject to one immaterial audit adjustment.</p>

3.5 The Audit Committee has confirmed that it is not aware of any additional material risk areas facing RoS, including 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 3 November 2009. Our audit is substantially complete, subject to the following finalisation procedures:
- review of the final version of the financial statements (including the annual report and the foreword)
 - obtaining and reviewing the signed letter of representation
 - updating our post balance sheet events review, to the date of signing the accounts
 - obtaining and reviewing the letter from the solicitors on legal claims.

Matters arising from the financial statements audit

- 3.8 We were presented with draft accounts on 18 June 2010, in line with the agreed timetable. The working papers provided continue to be of good quality.
- 3.9 2009-10 is the first year that central government bodies are required to prepare accounts in accordance with International Financial Reporting Standards (IFRS). Our letter to the Accountable Officer on the shadow IFRS accounts issued earlier in the year, confirmed that RoS had made good progress in restating its 2008-09 comparatives. This progress has been followed through to the final accounts.
- 3.10 Matters arising from the financial statements audit are set out below. Where appropriate, we have made recommendations for improvement, as set out in the agreed action plan at Appendix B.

Inventories (Work in Progress)

- 3.11 RoS records significant amounts of inventories in its balance sheet at the end of the financial year (2009-10: £3.6 million). This represents the value of land registration transactions processed in the period for cases that are not yet completed. The calculation of Work in Progress (WIP) requires the finance team to collect significant amounts of financial information on cases and the calculation process can be complex. The downturn in the Scottish housing market has reduced the level of intakes and changed the dynamics of cases to be processed, with an increased focus on clearing the backlog of "complex cases".
- 3.12 Our 2009-10 audit identified a number of audit adjustments to the WIP balance:
- As we have reported previously, the WIP valuation continues to be based on the assumption that all cases in WIP at the year end are at the start of a process. This assumption is likely to cause an understatement of costs incurred to date. We would recommend that RoS review this assumption going forward.
 - In the current period, management have used costs and through-puts for the final two months of the year, in order to calculate standard costs. The rationale for this is that RoS continued to incur unusually high training costs as a result of the economic down turn in the first 10 months of the year, which would unfairly inflate

the costs incurred in processing a case if included in the WIP calculation. In order to justify this assumption, we are awaiting a paper from the RoS, supporting the assertion that February and March represent "normal" months in terms of WIP.

- WIP reports were not run at the year end, necessitating an additional stage of reconciliation, increasing the risk of error. We recommend that BT are requested to provide reports concurrent with the year end going forward.
- As in the prior year, small value errors were noted in case numbers between the financial and land registry system. In some cases these appear to have arisen from an IT failure in the transmission of data between the systems. Audit adjustments totalling £39,000 have been posted in respect of unreconciled differences between the two systems. We recommend RoS discuss these variances with IT, to prevent the issue from recurring.

3.13 The WIP calculation continues to remain complex and involves a high number of linked spreadsheets, and this can give rise to calculation errors. In addition, we noted other weaknesses in the WIP system, including:

- the system does not allow RoS to review the WIP balance in year
- the lack of detailed staff timesheets for production leads management to adopt complex assumptions on production statistics during the year.

3.14 We are aware that management are currently reviewing the current system for recording WIP, and are looking at ways of improving the financial information that can be produced from the system. We will continue to monitor progress in this area as part of our 2010-11 audit.

Action plan point 1

Adjusted misstatements

3.15 Our audit identified five adjustments in relation to WIP valuation, amortisation of retirement provisions, and indemnity provisions, all of which have been processed by management.

Table 4: List of adjusted misstatements

Adjustments affecting reported results	Operating Income Statement		Statement of Financial Position	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Work in Progress <ul style="list-style-type: none"> • To adjust WIP figures for unreconciled difference at the year end • To adjust WIP figures for inclusion of scanning costs • To adjust Arrears figures to show year end figures 	WIP Movement 78	WIP Movement 391	WIP 391	WIP 78
Indemnity claim provision To update indemnity provision for one case following post year end settlement.		Legal Expenses 13	Indemnity claim provision 13	

Adjustments affecting reported results	Operating Income Statement		Statement of Financial Position	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Early Retirement Provision To adjust the early retirement provision in line with fair value.		Restructuring Costs 40	Early retirement provision 40	
	78	444	444	78

3.16 The overall effect of the adjustments is to reduce the deficit for the year by £366,000.

3.17 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

3.18 A review of post balance sheet events identified an amendment to the accounts of £128,000 in respect of staff bonuses which has not been processed by management on the basis of materiality. The overall effect of the unadjusted misstatement would be to reduce the reported loss for the year by £128,000 and increase net worth by £128,000.

Table 5: List of unadjusted misstatements

Adjustments affecting reported results	Operating Income Statement		Statement of Financial Position	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Staff bonuses To reduce the accrual for staff bonuses in line with the decision to pay bonuses based on post year end decision on the achievement of the year's financial and performance targets.		Staff costs 128	Creditors 128	

Evaluation of key controls

3.19 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 some key reporting points in relation to work in progress. We reported our findings to management in our interim management report, which was presented to the April 2010 audit committee.

3.20 We performed a high level review of the general IT control environment as part of the overall review of the internal control system and concluded that there were no material weaknesses within the IT arrangements that could adversely impact on our audit of the accounts.

- 3.21 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. The opinion reflects the fact the internal auditor's could only provide limited assurance over the effectiveness of RoS's arrangements for managing its partnership with BT.

Statement on Internal Control (SIC)

- 3.22 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.
- 3.23 We reviewed the draft SIC are satisfied that it complies with guidance contained in the Scottish Public Finance Manual that the process put in place by the Accountable Officer to obtain assurances on systems of internal control is adequate, and that the contents of the Statement are consistent with the information obtained from our normal audit work.

Annual report

- 3.24 We considered RoS's arrangements for compilation and submission of the 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.
- 3.25 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 2009-10 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 2009-10 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
<p>Financial management and budgetary control</p> <p>The last two 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 2010.</p> <p>The downturn will continue to impact on the land registration business and the reported results for 2009-10.</p> <p>As a result of the Section 22 report issued by the Auditor General for Scotland in 2009, RoS will experience increased scrutiny of its financial management and budgetary control systems in 2009-10 and going forward.</p>	<p>In order to assess the effectiveness of the financial management and budgetary control regime, we have applied the financial management toolkit developed by Audit Scotland. The toolkit provides guidance on the effectiveness of financial management arrangements and will allow us to assess whether RoS operates with 'basic practice', 'better practice' or 'advanced practice' arrangements.</p> <p>A summary of our review is shown in below.</p>
<p>Capital programme & the BT contract</p> <p>The overall expected outturn for the BT project is now £119.5 million, including new projects, compared to the original contract value of £78.2 million, a variance of £41.3 million (52%). The variance reflects the cost of new projects commissioned since the partnership commenced, some changes to existing projects, the cost of maintaining some legacy systems for longer than anticipated, and inflation costs.</p> <p>Slippage is forecast across both the Back Office Systems Initiative (BOSI) and the Public Facing Systems Initiative (PFSI).</p> <p>RoS may not obtain best value from capital projects if they are not carefully monitored and managed.</p>	<p>During our audit we considered the progress to date on the outstanding action plan points from previous audits and noted that although many of the recommendation are currently being progressed, only two of the nine areas we reviewed have been fully implemented.</p> <p>A summary of our review is shown in below.</p>

Key risk	Work completed
<p>Reserves</p> <p>As part of our 2008-09 audit findings we suggested that RoS undertake a scenario planning exercise to ensure that the Corporate plan and Reserves policy is sufficiently flexible to respond to further fluctuations in the housing market.</p>	<p>RoS has updated its reserve policy during the year for the updated financial position, a summary of the reserves position is at paragraph 2.8.</p>

Financial management and budgetary control

- 4.4 At our interim audit, we completed a review of the financial management and budgetary control regime, we have applied the financial management toolkit developed by Audit Scotland.
- 4.5 The toolkit has 30 questions on 11 key areas of financial management, and we assessed RoS on each question against basic, better and advanced criteria. Table 6 provides a summary of results:

Table 6: Summary of results from the financial toolkit

Rating	Number
Basic	18
Better	11
Advanced	1
	30

- 4.6 Our review concluded that RoS are in the basic category for the majority of the questions in the toolkit. However, there were a number of strengths noted from the review, including:
- the audit committee continues to provide independent and effective financial scrutiny
 - the reserves policy is regularly reviewed and updated for changes in financial projections
 - the capital budget is closely monitored with partnership boards established for key capital projects.
- 4.7 During the year, RoS was in the process of implementing a delegated budgeting system. This is expected to increase operational staff involvement in the budgeting process, and strengthen links between finance and the rest of the business. It is anticipated that the introduction of delegated budgeting will improve the overall financial management and budgetary control framework and RoS will then begin to move from a majority of "basic" defined practices into the "better" and "advanced" categories in the toolkit.
- 4.8 As part of our 2010-11, we will continue to monitor the implementation of the delegated budgeting system and its impact on the overall framework of control.

Capital programme and the BT contract

- 4.9 The effective management of the BT partnership remains a key strategic priority for the organisation. During 2009-10, there were significant changes to the management structure at RoS, and a new IT director has been appointed.
- 4.10 Internal audit completed a review of the overall management of the BT partnership during the year and reported their findings in October 2009. The internal audit report identified one critical and two high risk recommendations relating to the following matters:
- the complexities of the systems being developed by BT make it difficult to deliver a system which can pass the required user acceptance testing. This leads to delays and additional costs in delivering the projects to RoS (Critical)
 - a lack of partnership ethos between the senior management of RoS and BT (High)
 - the significant management changes in RoS during 2009-10 and the risk that delays in appointing staff will impact project delivery (High).

As a result of the findings of their review, internal audit could only provide limited assurance on the overall management of the BT partnership.

- 4.11 A key task for the new management team has been to prioritise the action plan points from external and internal audit reviews of the partnership and the outcomes of the Gartner review. During our interim audit we considered the progress to date on the outstanding action plan points and noted that although many of the recommendation are currently being progressed, only two of the nine areas we reviewed have been fully implemented. Management are currently preparing a detailed action plan incorporating all the outstanding action plan points with the aim of prioritising the most urgent points based on a risk assessment.
- 4.12 We will continue to monitor RoS's progress in managing this key risk and priority area as part of our 2010-11 audit.

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.

Efficiency

- 5.3 RoS is committed to improving the efficiency of its operations, although the significant reduction in land registration production is impacting on the organisation's performance efficiency measures. Previously RoS reported on the Standard Production Cost Index (SPCI) which is a ratio of total costs to weighted outputs over a three year period.
- 5.4 For the year ending 31 March 2010, RoS set a target of limiting the decrease in efficiency to 5%, while outturn figures show an actual decrease of 12% in efficiency. The significant decline in efficiency performance indicates that the organisation has more work to do to refine its structures, systems and processes to become more effective in the current climate. Although a decline in productivity is expected due to the corresponding decline in intakes, RoS will not be able to continue to sustain the current levels of decline in productivity.

Action plan point 2

- 5.5 In a reorganisation of the performance targets, the Keeper has decided to abolish the SPCI and instead RoS will report efficiencies through the new Ministerial target to deliver 2% increasing cash releasing efficiencies in each year. We will undertake a review of RoS's arrangements to meet this new performance target as part of our 2010-11 audit.

The Keeper's performance targets

- 5.6 The Keeper sets performance targets for the organisation to achieve. Table 7 below highlights the key performance targets for registration for 2008-09 and the outturn position.

Table 7: Keeper's performance targets outturn

Detail	Target	Outturn
Sasine turnaround time	To complete the registration of 80% of Sasine writs within 20 working days, with no writ taking longer than 40 working days	Achieved 84% within 20 working days and none over 40 days.
Dealings with whole turnaround time	To complete the registration of 80% of Dealings with Whole within 30 working days; with the remainder to be completed within 100 working days.	Achieved 81.5% within 30 working days and none over 100 days.

Detail	Target	Outturn
First Registrations turnaround time	To complete the registration of 80% of standard First Registration applications within 70 working days	Achieved 84%
Complex cases	1. Complete the registration of 40,000 Transfers of Part cases along with their consequential Dealings with Whole 2. Eliminate all pre-October 2008 First Registration casework	Not achieved 1. 24,104 Transfers of Part cases along with their consequential Dealings with Whole. 2. 3,539 cases not despatched.
Registration accuracy	To achieve a registration accuracy rate of 98.5% for applications despatched during the previous 12 months	Not achieved 98.3%
Customer enquiries	Process 98% of all customer enquiries in compliance with RoS's published response standards	Achieved 99%

Source: Registers of Scotland

- 5.7 RoS has not, therefore, achieved 2 of its key targets for the year, although performance in registration accuracy was only marginally behind target. It is, however, disappointing that the significant re-alignment of resource to address complex cases and caseload backlog during the year has not resulted in better performance in clearing these cases. Management have indicated that the ambitious targets set for these areas at the start of the year were too stretching overall and plan to revise the targets to more meaningful levels.
- 5.8 A target was set to achieve 98% in the annual customer satisfaction survey, however the data was not collected to measure this target.

Audit Scotland National Reports

- 5.9 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.
- 5.10 As part of our audit, we have considered the response to the national reports issued during the year.

Report	Response
Scotland's Public Finances	As RoS is a trading fund, it does not receive funding from the Scottish Government. However RoS have their own corporate plan projection on financing, and will be adopting a cash releasing efficiency target for 2010-11.
Improving Public Sector Purchasing	RoS did not review this report. However RoS did undertake an external assessment of procurement under the Central Government Centre of Procurement Expertise Procurement Capability Assessment programme in October 2009. An action plan was developed from this review for action.

- 5.11 We noted that RoS does not have a formal procedure in place to ensure Audit Scotland national reports are reviewed and considered by the relevant management committee to ensure good practice from these reports is identified and incorporated into the organisation.

Action plan point 3

A Reporting requirements of ISA 260

The principal purpose of the ISA 260 report is:

To reach a mutual understanding of the scope of the audit and the respective responsibilities of the auditor and those charged with governance.

To share information to assist both the auditor and those charged with governance fulfil their respective responsibilities.

To provide to those charged with governance constructive observations arising from the audit process.

ISA260 reporting requirement	Key messages
Independence	<p>We are able to confirm our independence and objectivity as auditors and draw attention to the following points:</p> <ul style="list-style-type: none"> • We are independently appointed by the Auditor General for Scotland. • The firm has been assessed by Audit Scotland as complying with its required quality standards. • The engagement lead and client service manager are subject to rotation in line with the firm's requirements. • We comply with the Auditing Practices Board's Ethical Standards. • We have not provided any non audit services in 2009-10.
Audit Approach	<p>Our approach to the audit was set out in our 2009-10 audit plan. We have planned our audit in accordance with auditing standards and Audit Scotland's Code of Audit Practice. Other key factors to highlight include:</p> <ul style="list-style-type: none"> • We consider the materiality of items in the financial statements in determining the audit approach and in determining the impact of any errors. • We have been able to place appropriate reliance on the key accounting systems operating at RoS for financial statement audit purposes.
Accounting Policies	<p>RoS has adopted appropriate accounting policies in the areas covered by our testing. Accounting policies are in accordance with the FReM.</p> <p>The Audit Committee has confirmed that it is satisfied that the accounting policies adopted are the most appropriate, as required by IAS 8.</p> <p>We have considered RoS's financial plans and consider it appropriate for the RoS to continue to account on a going concern basis.</p>

ISA260 reporting requirement	Key messages
Material Risks	<p>The Audit Committee should confirm that it is not aware of any additional material risk areas facing RoS, including significant fraud risks.</p> <p>We have requested from the Accountable Officer, a Letter of Representation, to state that there are no additional material risks and exposures as at the date of signing the accounts, which should be reflected in the financial statements.</p> <p>We will also perform our own audit procedures to ensure that all significant risks and exposures to RoS have been recognised in the accounts as at September 2010. We will focus on accounting provisions and cash flow forecasting over the next 12 months.</p>
Audit Adjustments	<p>We have discussed with management the adjustments to the accounts, primarily to improve the fair presentation of the financial statements, as well as the clarity and presentation of disclosure notes.</p> <p>These adjustment are summarised at Section 3.13</p>
Unadjusted Errors	<p>We have identified one unadjusted error to the accounts which requires reporting to those charged with governance. The unadjusted error relates to reduction in staff bonuses accrual, based on the decision to pay bonuses in line with the achievement of the financial and performance targets of RoS for 2009-10.</p> <p>The Audit Committee needs to satisfy itself of the appropriateness of the approach taken by management not to adjust and to minute its decision.</p>
Other Matters	<p>We have made recommendations in respect of some areas for improvement in internal control. Recommendations and agreed action are listed in the Action Plan at Appendix B.</p>

B Action Plan

Rec. No.	Para Ref	Recommendation	Risk	Management response	Implementation date and responsibility
1		<p>Work in Progress (WIP)</p> <p>The calculation of the WIP balance remains complex and we noted the following issues during the audit:</p> <ul style="list-style-type: none"> • 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. <p>RoS should investigate alternative methods of calculating WIP, which would be more efficient and useful to the financial management process.</p>	High	<p>Accepted</p> <p>The model for calculating WIP needs to be rebuilt and significantly simplified. This will be done in 2010-11</p>	<p>LAP</p> <p>December 2010</p>

Rec. No.	Para Ref	Recommendation	Risk	Management response	Implementation date and responsibility
2		<p>Efficiency</p> <p>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.</p> <p>We recommend that RoS reviews the efficiency of the organisation to ensure that costs are more aligned with the production requirements.</p>	High	<p>Accepted</p> <p>RoS is currently carrying out a strategic review of its processes to ensure that they are cost effective and efficient.</p> <p>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.</p>	<p>EMT</p> <p>Completion of baseline analysis 31 August 2010-07-22</p> <p>Proposal for re-engineering processes. – 31/12/2010</p>
3		<p>Audit Scotland national reports</p> <p>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.</p>	Low	<p>Noted</p> <p>Audit Scotland reports are received and reviewed. Where appropriate these are circulated to the relevant managers.</p> <p>I am happy to put in place a more formal note of this process.</p>	<p>LAP</p> <p>Immediate.</p>



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