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National Records of Scotland

Annual Report to the Registrar General and Keeper of the Records of Scotland, the Accountable Officer and the Auditor General for Scotland

Final Report

3 September 2012

pwc

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X August 2012

We are pleased to enclose our External Audit Annual Report to the Registrar General and Keeper of the Records of Scotland, the Accountable Officer and the Auditor General for Scotland for the financial year ended 31 March 2012. This report also discharges our obligations under International Standards of Auditing ("ISA") 260: Reporting to those charged with Governance. We have assumed that the responsibility for governance has been discharged to the Accountable Officer. The primary purpose of this report is to communicate the more significant findings arising from our external audit that we believe are relevant to those charged with governance, and to meet our obligations as set out within the Audit Scotland Code of Practice.

The scope and proposed focus of our audit work was summarised in our audit plan, which we presented to the Audit and Risk Committee in February 2012. We have subsequently reviewed our audit plan and concluded that our original risk assessment remains appropriate. The procedures we have performed in response to our assessment of significant audit risks are detailed within the Key Areas of Audit Focus section of this report for information.

We have completed our year end external audit work on the financial statements and have issued an unqualified audit opinion.

We would like to take this opportunity to thank NRS Management and staff for their cooperation and assistance throughout the year.

Yours faithfully

PricewaterhouseCoopers LLP

3 September 2012

Contents

Section 1: Introduction

We have the pleasure in presenting this report relating to our audit of the financial statements of the National Records of Scotland (NRS) for the year ended 31 March 2012.

We have discussed this report with the Accountable Officer and Strategic Head of Finance as part of our audit process. The purpose of this report is to update the Audit Committee on the output of the audit and of any significant matters that have arisen during the course of our work.

Scope, nature and extent of our audit

Our overall responsibility as external auditor of NRS is to undertake our audit in accordance with the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011. In this regard, the Code sets out the need for public sector audits to be planned and undertaken from a wider perspective than in the private sector, involving not only assurance on the financial statements but also consideration of areas such as regularity, propriety, performance and the use of resources. It also sets out the need to recognise that the overall audit process is a co-ordinated approach involving the "appointed auditor" and the Auditor General for Scotland.

Our audit has been planned and conducted to take account of these wider perspectives. Under the requirements of International Standard on Auditing (UK and Ireland) ('ISA') 260: "Communication of audit matters to those charged with governance", we are required to communicate audit matters arising from the audit of financial statements to those charged with governance of an entity. This Annual Audit Report to the RG Keeper and Accountable Officer, together with previous reports to the Audit and Risk Committee throughout the year, discharges the requirements of ISA 260.

Management responsibility

It is the responsibility of the Accountable Officer, to prepare financial statements for each financial year in the form and on the basis determined by the Scottish Ministers. This means:

- acting within the law and ensuring the regularity of transactions by putting in place systems of internal control to ensure that financial transactions are in accordance with the appropriate authority;
- maintaining proper accounting records;
- preparing financial statements timeously which give a true and fair view of the financial position of NRS and its expenditure and income for the period ended 31 March 2012; and
- preparing a Governance Statement and a Remuneration Report.

Auditor's responsibilities

We audit the financial statements and the part of the Remuneration Report to be audited and give an opinion on whether the financial statements:

- 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 of the state of the body's affairs as at 31 March 2012 and of its net operating cost for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2011/12 FReM; and
- have been prepared in accordance with the requirements of the Public Finance and Accountability (Scotland) Act 2000 and directions made thereunder by the Scottish Ministers.

In respect of the relevant (audited) parts of the regulatory opinion:

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

We also review the Governance Statement by considering the adequacy of the processes put in place by the Accountable Officer to obtain assurances on systems of internal control; and assess whether disclosures in the statement are consistent with our knowledge of NRS.

Status

Our audit work on the draft financial statements for the year ended 31 March 2012 was primarily carried out over a three week period commencing 11 June 2012. At the time of drafting this report we still need to review the final updated financial statements, receive the signed letter of representation (signed when accounts signed) and receive Audit Scotland's final third party assurance report to allow us to determine reliance on the controls operated by the Scottish Government on behalf of NRS.

The audit process

A complete draft set of accounts with supporting working papers were received within the timetable agreed and were generally of a standard expected. However in the case of certain working papers provided information was not always complete and reconciled to the trial balance and in the case of year end cut off procedures these could have been followed more robustly. In addition, for the areas of the accounts which rely on audit evidence provided by the Scottish Government, this would have benefited from an additional review/sense check.

Having completed the first full audit cycle as NRS's external auditors, we feel that we have developed good working relationships with NRS's management. Agreed ways of working were established between the audit team and NRS's finance team, which included holding weekly catch-up meetings to discuss emerging issues. We will discuss potential improvements that could be made with management before our next on site visit with a view to agreeing an approach for future years.

Opinion

We have issued an unqualified audit opinion on the financial statements, including the regularity of expenditure and income. In addition, our opinion is unqualified in respect of those elements of the Remuneration Report subject to audit.

Significant auditing and accounting matters

Section 4 contains other matters for the attention of those charged with governance, including elements of communication required under International Standard on Auditing "Communication with those charged with governance". This section includes communication regarding identified misstatements, a summary of which is included in **Appendix 1**.

We are also required to communicate with you regarding any significant deficiencies in internal control of which we are aware. We identified some future recommendations for improving NRS's systems of internal control, with the more significant matters included in **Appendix 2**.

Staff Assistance

We would also like to take this opportunity to express our thanks for the co-operation and assistance we have received from management and staff throughout our work.

Section 2: Financial performance

Financial performance 2011/12

	2011/12 (actual) £m	2011/12 (budget) £m	Variance £m
EXPENDITURE			
Staff costs	14,657	14,986	(0.329)
Administration Expenditure	24,294	24,515	(0.221)
	38,951	39,501	(0.550)
INCOME			
Administration Income	(7,875)	(7,270)	(0.605)
NET OPERATING EXPENDITURE*	31,076	32,231	(1,155)

* extracted from the 2011/12 Operating Cost Statement, within the final financial statements.

NRS was established in April 2011 from the amalgamation of National Archives of Scotland (NAS) and General Registers of Scotland (GROS) and hence the 2011/12 financial statements have no prior year comparative figures. The 2011/12 budget was created at the 2011/12 Autumn Budget Revision, after amalgamating budgets set for GROS and NAS.

The results for the year show Net Operating Expenditure of £31.076 million with an underspend of £1.155 million against budget resulting primarily from a contribution for the cost of the Melville papers, a capital acquisition. Scottish Government Finance approved an overspend of £0.625 million on capital expenditure with a corresponding underspend on operating costs to support this acquisition, allowing NRS to remain within the overall parliamentary approved budget.

The remaining operating costs underspend of £0.530million was primarily derived from lower than expected staff costs (£0.329 million) due to delays in filling key ICT and statistician posts and lower than anticipated depreciation charges (£0.190 million) as certain ICT projects were completed later than planned.

During the year NRS management reported that they exceeded the agreed Scottish Government efficiency savings target of £1.036 million by £2.114 million. This was achieved through savings within the Census, procurement savings and IT. The majority of the savings were Census based, where a significant element was realised through negotiations and collaborative contracts.

Financial outlook – 2012/13 and beyond

The NRS budget for 2012/13 has been prepared by management and shared with Board Members.

	2012/13 (budget) £m	2011/12 (actual) £m	Variance £m
EXPENDITURE			
Staff costs	14,880	14,657	0.143
Administration Expenditure	13,643	24,294	(10,651)
	28,523	38,951	(10,428)
INCOME			
Administration Income	(7,014)	(7,875)	0.861
NET OPERATING EXPENDITURE	21,509	31,076	(9,567)

The budget for total net operating expenditure shows a decrease of £9.6m on the 2011/12 year due primarily to a corresponding decrease in the administration expenses. There is also a decrease in the administration income of £0.9m (11%) whilst staff costs are only budgeted to increase by 1%.

The significant decrease in the administration expenses for 2012/13 is due to the census budget which was £9.2m in 2011/12 and only £1.2m in 2012/13, as the exercise has been completed.

NRS have been successful in securing additional capital funding of £0.900 million for 2012/13, which will be used to meet the costs of a new roof for Thomas Thomson House.

Management complete the initial draft of the budget after the first quarter each year to allow managers time to review the financial position of their respective divisions within NRS. Subsequent to that management perform an internal exercise to identify pressures and savings in advance of the Autumn Budget Revision published by the Scottish Government in October. In addition, management have submitted information to the Scottish Government's 2013/14 draft budget, which is expected to be presented to the Scottish Parliament in October 2012.

Section 3: Key areas of audit focus

Our audit followed the strategy set out in our Audit Plan which was presented to the Audit and Risk Committee on 1 February 2012. We confirm that there has been no cause for us to vary the planned scope of our work.

Risk identified/area of audit focus	Audit response
Management override of controls	In accordance with our audit plan, we have reviewed management's overall fraud arrangements and policies. We have reviewed a sample of significant journal entries (determined on the basis of risk) and examined management's accounting estimates for bias in particular provisions and accruals. We also carried out testing in respect of the use of government procurement cards. This work did not identify any material errors that required adjustment to the financial statements.
Revenue recognition	We examined the revenue and receivables process as part of our interim audit. We also performed substantive testing on a sample of income transactions with additional focus on ensuring that income is recognised in the period to which it relates. The work around cut off testing did not identify any significant errors that required adjustment to the financial statements. However, we have highlighted in **Appendix 2** the need for Management to review the controls in respect of the accounting treatment of accruals and prepayments where appropriate to ensure income and expenditure are accounted for in the correct financial year.
Recognition of operating expenditure	We obtained an understanding of the purchasing and payables process as part of our interim audit. We performed substantive testing on a sample of expenditure transactions and reviewed management's estimates of future expenditure, such as accruals and provisions. We have undertaken specific cut-off testing to identify potentially unrecorded liabilities. This work did identify immaterial errors that were adjusted in the financial statements. We have highlighted these in **Appendix 1**.
Accounting for accruals and provisions	As part of our consideration of accounts payable balances, we examined a sample of accrued expenses and the related supporting documentation. In particular, we had had detailed discussions with management around the holiday accrual and early retirement provision as these were areas highlighted by the previous external auditors. Our work highlighted an incorrect posting of an accrual balance to NRS's ledger account codes by the Scottish Government which did not relate to NRS. We have highlighted this in **Appendix 1**.
Capitalisation of Staff Costs	We reviewed the fixed asset additions made in year to verify that any staff costs capitalised had been correctly accounted for. It was noted through our review that no staff costs were capitalised in 2011/12. This is in line with our understanding in that the digitisation of records project was scheduled to finish in early 2011.

Risk identified/area of audit focus	Audit response
Professional scepticism	As auditors, we are required to display professional scepticism when we plan and perform our audits. This involves providing challenge to management in areas such as critical assumptions, judgements, explanations and inconsistencies. During this audit, we have displayed professional scepticism in a range of areas including, for example, • **BACS Accrual**: we discussed the large historic accruals balance with management and involved the Scottish Government representatives in order to obtain a satisfactory explanation of this balance which resulted in an adjustment; • **Holiday Accrual**: we challenged the assumptions included within the holiday accrual calculations to ensure appropriate judgement had been applied; and • **Provisions**: We have considered Managements approach to the early retirement provision and the underlying assumptions.

Section 4: Significant audit and accounting matters

Required communications on significant matters

The following table contains communication required under ISA 260 (revised and re-drafted) "Communication with those charged with governance".

Requirement	Delivery of requirement
Uncorrected and corrected misstatements	We identified 2 misstatements that we discussed and agreed with the Accountable Officer, which have been corrected in the final financial statements. Details of these can be found in **Appendix 1**. In addition, we identified a number of disclosure changes which have been processed in the final accounts.
Significant accounting principles and policies	Significant accounting principles and policies are disclosed in the notes to the financial statements. We ask the Accountable Officer to represent to us that they have considered the accounting policies and that here have not been any material changes in the accounting principles and policies used during the year (letter of representation attached in **Appendix 3** to this report for information)
Significant qualitative aspects of accounting practices and financial reporting, management's judgments and accounting estimates	We reviewed management's judgements and accounting estimates in respect of provisions for early retirement liabilities and the holiday accrual. We will continue to review the assumptions used in estimating the early retirement provision to ensure that it remains appropriate in future years.
Deficiencies in the internal control environment	The purpose of our audit was to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that were appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. Our more significant findings in respect of controls are outlined in Appendix 2.
Details of material uncertainties related to events and conditions that may cast significant doubt on NRS's ability to continue as a going concern	We have not encountered any material uncertainties which cast doubt upon the ability of NRS to continue as a going concern.
Significant difficulties encountered during the audit	While we did not encounter any significant difficulties which would prevent us from undertaking the audit, we have identified some improvements with a view to streamlining the audit process for future years. This will be discussed and agreed with management before the commencement o f the next audit cycle.
Confirmation of audit independence	We confirm that, in our professional judgment, as at the date of this document, we are independent auditors with respect to NRS within the meaning of UK regulatory and professional requirements and that the objectivity of the audit engagement leader and the audit staff is not impaired.

Format of the financial statements

The format of the accounts is set out in the FReM, and interpreted by the Scottish Government. NRS currently disclose a detailed operating cost statement and a statement of comprehensive net expenditure (SOCNE). The SOCNE is the primary financial statement and there is merit to management considering the amalgamation of the SOCNE and operating cost statement in future years. In addition, it is recognised that due to no prior year comparatives as this is the first year of NRS, budget information is shown on the operating cost statement. It is emphasised that this information is not subject to audit. Going forward, it is recognised this is useful information to inform the reader of the accounts but could be presented out with one of the primary statements.

Action 1

Section 5: Governance, accountability and internal control

As part of our wider external audit remit, stemming from our responsibilities under Audit Scotland's Code of Audit Practice, we are required to consider NRS's governance and accountability arrangements in our audit work. For 2011/12, a major part of this work has been our follow up of Audit Scotland's national performance report, The Role of Boards. A separate report of our findings will be prepared for the Audit and Risk Committee and will be presented separately. This work has enabled us to gain an understanding of NRS's existing governance arrangements as they concern:

- corporate governance and systems of internal control,
- the prevention and detection of fraud and irregularity and
- standards of conduct and arrangements for the prevention and detection of corruption.

We provide brief commentary on NRS's key governance systems and structures below.

Governance Statement

As your external auditors, we are required to review the governance statement before publication and report as to whether the statement complies with relevant guidance, is misleading, or is inconsistent with other information obtained during the audit. We do not consider whether the statement covers all risks and controls, or form an opinion on the effectiveness of internal control or risk management arrangements. We have reviewed the governance statement and confirm that there are no matters to report.

Corporate governance and internal control

NSS are a non-ministerial Government Department, headed by the statutory roles of the Registrar General and the Keeper of the Records of Scotland. NRS are associated with the Scottish Government and are part of the Scottish Administration under Section 128(6) of the Scotland Act 1998.

The RG Keeper and the Accountable Officer is responsible for ensuring that NRS fulfils the aims and objectives set by Scottish Ministers. The role of the Board is to provide an advisory function in respect of the overall strategic direction of NRS, monitoring performance against agreed objectives and considering the arrangements in place for NRS to meet its statutory requirements.

The Keeper and the Accountable Officer are supported by an Advisory Board and an Audit and Risk Committee, both of which provide an advisory role in respect of governance, financial performance, risk and internal control. In particular, the Board plays a key advisory role in supporting the Keeper deliver his statutory roles.

We have considered internal control as it concerns the key financial systems and to an extent based on our audit risk assessment. The purpose of our audit is for us to express an opinion on the financial statements. This includes consideration of internal control relevant to preparation of the financial statements in order to design appropriate audit procedures. It does not extend to expressing an opinion on the effectiveness of internal control.

We are required by ISA 265 to report to those charged with governance and management deficiencies in internal controls that the auditor has indentified during the audit and that, in the auditor's professional judgment, are of sufficient importance to merit their respective attentions.

We have not identified any significant weaknesses in the current system of internal controls. However, we have noted four areas for further development during the course of our audit which are raised within the action plan in **Appendix 2**.

Prevention and detection of fraud

Audited bodies are responsible for establishing arrangements to prevent and detect fraud and other irregularity. As part of our external audit, we have reviewed NRS's high level arrangements for preventing and detecting instances of fraud and corruption. During the year management have established a fraud policy statement, a guide to reporting fraud including links to supporting guidance and various Scottish Government policies and guidance notes, and a fraud response plan. In respect of whistleblowing arrangements, NRS have adopted the Scottish Government whistleblowing policy. Any frauds or suspected frauds are reported to the Audit and Risk Committee. During 2011/12 no frauds were reported.

Standards of conduct

Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and have proper arrangements in place for implementing and monitoring compliance with standards and codes of conduct, standing orders and financial instructions. We have not become aware of any issues concerning NRS's arrangements that we need to identify in this report.

Internal Audit

NRS's internal audit service is provided by the Scottish Government internal audit team. During the year internal audit planned to undertake 5 specific reviews for NRS:

- Conservation Services;
- Corporate Governance and Risk Management;
- Estate Management (including accommodation and facilities)

However, the overall timing of the Internal Audit plan slipped and one review was subsequently dropped (NHSCR) and the planned audit of payments, procurement systems, contract management arrangements and income and banking was delayed and therefore agreed work in this area would be completed during 2012/13. Based on the 3 reviews completed, internal audit have classed the assurance as "substantial".

We have not placed reliance on the work of internal audit, due to the nature and timing of the work completed. However, we did use the work completed to inform our overall understanding of NRS and certain aspects of the NRS control environment.

Looking ahead to the 2012/13 internal audit plan, NRS management should continue to liaise with Internal Audit to ensure that work is commenced and finalised where possible during the financial year under review, with areas critical to the Governance Statement prioritised. .

Action 2

Risk Management arrangements

NRS has in place a risk management framework, including a strategic risk register supported by tactical and operational risk registers. Risks are scored according to impact and likelihood, and are assigned relevant owners. Risk management arrangements, and strategic risks are considered as a standing item by the Audit Committee. The key risk reflected in the strategic risk register is that staff resource is not available to allow delivery of objectives, and mitigating controls have been identified and continually reviewed.

For 2012/13 Management plan to review the risk management framework, and reflect on the strategic risks identified now that NRS has been in place for a year.

Reliance on Scottish Government Systems

NRS used SEAS, the Scottish Government financial ledger and receive certain financial services on behalf of the Scottish Government, including certain accounts payable, payroll and banking services on an annual basis the Accountable Officer receives assurance from the Director of Finance at the Scottish Government. In addition, for the 2011/12 financial year, Audit Scotland, in its role of external auditor to the Scottish Government, produced a third party assurance report for certain financial and payroll services.

During course of our year end external audit testing we identified a balance of £0.5 million which had been posted to the NRS ledger in error by the Scottish Government finance team. As a result, we would highlight that during 12/13, NRS management should consider introducing more robust controls to verify that what is classed as NRS transactions are appropriate and recorded accurately. This will be helped by the production of monthly management accounts.

Action 3

Succession planning

The Registrar General and Keeper of the Records of Scotland retires at the end of September 2012. A recruitment process is currently underway with an appointment anticipated in October 2012. In the interim period the Accountable Officer will also fulfil the functions of the Keeper.

Appendices

Appendix 1: Summary of corrected misstatements

In the course of our audit work, we record the errors or misstatements we identify except those that are clearly trivial, which in the case of NRS are those considered to be less than £20,000 (this represents 2.5% of our overall materiality level as set out in our External Audit Planning document presented to the Audit and Risk Committee).

Presented below is a record of those misstatements which have been corrected by Management.

No	Description of misstatement (factual (F), judgemental (J), projected (P))		Income statement		Balance sheet	
			Dr	Cr	Dr	Cr
1	Dr Accruals Cr Administration Expenditure Being an adjustment to accruals for the incorrect inclusion of VAT within the accrual calculation **Status: corrected**	F		£56k	£56k	
2	Dr Accruals Cr Administration Expenditure Being an adjustment to accruals for the incorrect BACS accrual posting to NRS account codes by the Scottish Government **Status: corrected**	F		£499k	£499k	
Total corrected misstatements				**£373k**	**£373k**	

Disclosure Adjustments

In addition to the number adjustments presented above, we have proposed and agreed a number of disclosure adjustments to the draft financial statements namely to correct formatting errors, ensuring relevant notes cross cast to the primary statements and rounding errors.

Appendix 2: Action plan

We have identified a number of areas for development during the course of our audit. Our recommendations for improvement are as follows:

No	Finding	Risk	Recommendation
1	For the 2012/13 Financial statements, Management should review the layout of the Operating Cost Statement and the Statement of Comprehensive Expenditure, with a view to amalgamating the statements.	Producing primary statements in line with the FrEM and other Scottish Government organisations	**Management response:** Agreed. **Agreed owner:** C Stewart **Timetable:** 31 March 2013
2	NRS management should continue to liaise with Internal Audit to ensure that work is commenced and finalised where possible during the financial year under review, with areas critical to the Governance Statement prioritised.	Internal Audit work may not support the overall Governance Statement within the Financial Statements	**Management response:**-Agreed **Agreed owner:**-C Stewart **Timetable:**-Throughout 2012/13
2	NRS management should consider introducing more robust controls to verify that what is classed as NRS transactions are appropriate and recorded accurately within SEAS. This will be helped by the production of monthly management accounts.	Balances may be incorrectly coded to NRS by the Scottish Government finance team, and go unidentified.	**Management response:** Agreed in principle, although in practice we have limited opportunity to review the few transactions that are carried out by SG on our behalf. We will introduce a fuller trial balance review, as part of our month-end work. Work will also be undertaken to ensure that the finance team have copies of all journals, highlighting branch authorisation, where such journals are processed by SG on behalf of NRS. **Agreed owner:** J Grady **Timetable:** 30 September 2012
4	We found through several audit tests performed that NRS have weak cut-off procedures in place. The following errors were identified: • 1 item totalling £71k was included as expenditure but should have been included as a prepayment; • 2 items totalling £12k which should have been treated as accruals for 11/12 were put through as expenditure for 12/13. • 2 items totalling £12k was recognised as income in 11/12 but related to 12/13 and was	If robust cut off procedures are not maintained at year end there is risk that income and expenditure may be materiality misstated.	Management should tighten up the general cut-off procedures to ensure that all material transactions are correctly accounted for in the financial statements. **Management response:** Agreed. A review of cut-off procedures will take place as part of our internal wash-up exercise so to ensure that we tighten up in advance of preparing the 2012-13 Accounts. **Agreed owner:** J Grady **Timetable**: 30 September 2012

No	Finding	Risk	Recommendation
	excluded from 11/12 accrued income. • 3 items of expenditure totalling £4.5k which related to 10/11 was included as 11/12 expenditure as it hadn't been accounted for in the previous year.		
5	No register of interests or annual confirmation of NRS directors' and senior staff members interests took place during 2011/12.	Material transactions and relationships may not be identified and correctly disclosed in the financial statements.	A register of interests for all directors should be maintained and updated annually. **Management response:** Agreed. **Agreed owner:** Corporate Planning Team **Timetable:** 30 September 2012
5	In 6 of 51 transactions tested the report from SG (which confirms receipt of income to the bank account) was not received by NRS. No action was taken to follow these absences up.	Incorrect postings to the NRS ledger by the Scottish Government may not be detected.	Management should obtain and routinely review all procedures performed by the Scottish Government to ensure the accuracy and completeness of the ledger. **Management response:** Agreed. **Agreed owner:** J Grady **Timetable:** 30 September **2012**
6	We tested a sample of 34 journals in the year and found that 3 were not signed off as authorised and approved for posting to the general ledger.	Unauthorised journals are posted undetected to the ledger	Management should ensure a robust process is in place to ensure all journals posted to the ledger are reviewed by an appropriate member of staff. **Management response:** Agreed. **Agreed owner:** J Grady **Timetable:** 30 September 2012