KPMG

cutting through complexity™

East Lothian Council

Annual audit report to the Members of East Lothian Council and the Controller of Audit

DRAFT - Year ended 31 March 2012

12 September 2012

Contents

The contacts at KPMG in connection with this report are:

Stephen Reid
Director, KPMG LLP
Tel: 0131 527 6795
Fax: 0131 527 6666
stephen.reid@kpmg.co.uk

Andy Shaw
Senior Manager, KPMG LLP
Tel: 0131 527 6673
Fax: 0131 527 6666
andrew.shaw@kpmg.co.uk

Sarah Burden
Assistant Manager, KPMG LLP
Tel: 0131 527 6611
Fax: 0131 527 6666
sarah.burden@kpmg.co.uk

About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ("the *Code*").

This report is for the benefit of East Lothian Council ("the Council") and is made available to Audit Scotland and the Accounts Commission (together "the beneficiaries"). It has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes, but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scope and objectives section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the beneficiaries) for any purpose or in any context. Any party other than the beneficiaries that obtains access to this report or a copy and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the beneficiaries.

We also draw your attention to the following:

- management of East Lothian Council are responsible for preparing financial statements that show a true and fair view and for implementing appropriate internal control systems;
- weaknesses or risks identified by us are only those which have come to our attention during our normal audit work in accordance with the Code, and may not be all that exist; and
- communication by us of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve East Lothian Council management from its responsibility to address the issues raised and to maintain an adequate system of control.

Headlines

Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practise* ("the *Code*"). This specifies a number of objectives for our audit.

We reported, in our audit strategy, our responsibilities in respect of the audit. The Council's responsibilities are set out in appendix two.

This report summarises our work for the year ended 31 March 2012.

We wish to record our appreciation of the co-operation and assistance extended to us by Council staff during the course of our work.

Financial statements	
Draft 2011-12 financial statements were provided on 28 June 2012, in line with the agreed timetable; we have issued an unqualified audit opinion. The year end bank reconciliation was not available until 29 August and the receipt of a satisfactory response from the Council's external property valuer was subject to delay, both causing inefficiencies in the audit process. Management agreed that there was a material error in the 2010-11 financial statements; a prior year adjustment has been processed in the 2011-12 financial statements to correct the error.	-
Use of resources	
The Council had a statutory deficit of £7.5 million in 2011-12 (2010-11: £5.9 million surplus). This resulted in a decrease in the general fund reserves of £4.1 million and housing revenue account and capital fund reserves of £3.4 million.	Page 3
Total capital expenditure in 2011-12 was £71.5 million, lower than the approved capital plan of £77.3 million. This level of capital investment represented a 26% increase over 2010-11 levels. From Audit Scotland's analysis of the 32 local authorities, the Council has the highest level of net external debt of all Scottish local authorities, representing a significant risk to future revenue budgets.	Page 5
The 2012-13 budget forecasts a breakeven position, incorporating a further £4 million utilisation of reserves. The Council is planning to utilise most usable un-earmarked general reserves by 31 March 2014. In 2014-15 the Council is budgeting for a break-even position.	Page 7
Performance management	
We have considered the Council's arrangements in responding to Audit Scotland and Accounts Commission national studies, preparing short returns to Audit Scotland as appropriate. We have identified some opportunities for improvement.	Page 14
The Council has developed an improvement framework which should support management's ongoing assessment of the extent to which the Council is achieving Best Value and support the Council's drive for continuous improvement.	Page 17
Governance	
Following local government elections, there have been revisions to the membership of the Council and its committees. The governance statement confirms the existence of a comprehensive framework of internal control.	Page 21
Arrangements to prevent and detect fraud are embedded in internal controls, including processes to comply with the National Fraud Initiative.	Page 23
Internal audit completed their plan, reporting a number of weaknesses during the year, and were able to conclude that reasonable assurance could be placed on the adequacy and effectiveness of the Council's internal control systems for the year. We have made a number of recommendations to improve the control framework .	Page 23

Financial position

The Council had a statutory deficit of £7.5 million in 2011-12 (2010-11: £5.9 million surplus). This resulted in a decrease in the general fund reserves of £4.1 million and housing revenue account and capital fund reserves of £3.4 million.

2011-12 has been a landmark year for the Council, due in part to reserves being used for the first time. This practice will continue, with further planned use of reserves included in the approved three-year financial plan.

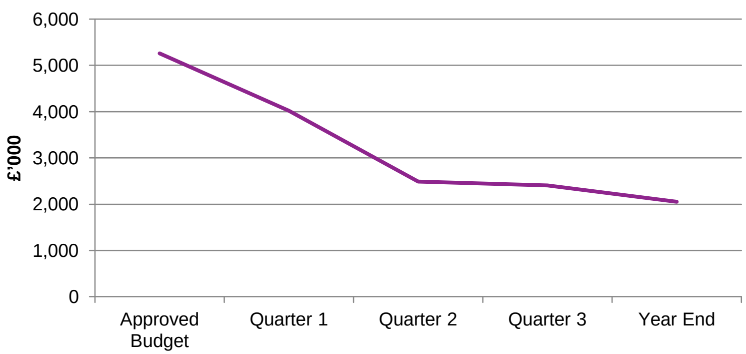
Financial outturn

The Council had a statutory deficit of £7.5 million in 2011-12 (2010-11: £5.9 million surplus). This resulted in a decrease in the general fund reserves of £4.1 million and housing revenue account and capital fund reserves of £3.4 million.

The decrease in the housing revenue account related primarily to £4 million capital expenditure financed from revenue as part of the Council's open market acquisition strategy. Additionally, management transferred £2.5 million from the capital fund to the housing revenue account at year end to provide sufficient funds to cover planned expenditure in 2012-13.

2011-12 was the first year that the Council planned to utilise brought forward reserves, having expected to utilise £5.3 million. The final outturn position was a £2.1 million utilisation, representing 24% of opening useable reserves. The lower utilisation was mainly a result of the lower than planned primary school numbers and higher than expected funding from the Scottish Government for teacher employment. The movement in the planned use of reserves over the year is summarised below.

Planned use of reserves



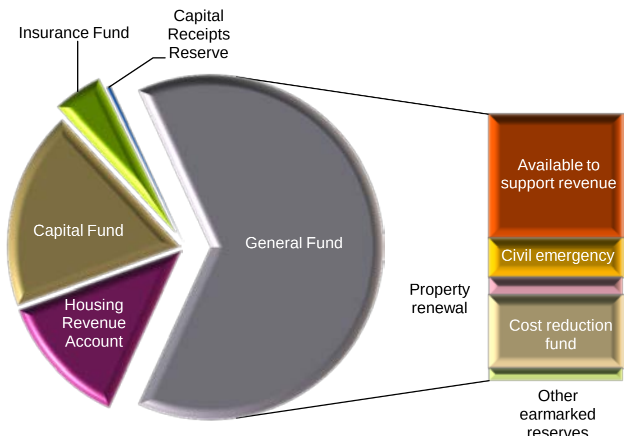
Source: East Lothian Council

Further utilisation of reserves was incurred in respect of committed elements of the general fund, mainly in relation to £1.3 million of the cost reduction fund. This was primarily due to the cost of staff restructuring and rationalisation.

Based on an Audit Scotland survey of the 32 Scottish local authorities, only four others utilised reserves in 2011-12. However, the total usable reserves carried forward as a proportion of revenue expenditure is of a similar ratio to other councils. This indicates that in previous years the Council held a higher proportion of reserves when compared to other councils.

As at 31 March 2012, the Council had usable reserves of £21.5 million. These consisted of the general fund (£13.7 million), the housing revenue account (£2.8 million), and the capital fund (£4.0 million) - which is used to fund capital expenditure within the housing revenue account. The funds are illustrated in the diagram below.

Analysis of reserves



Source: KPMG LLP

Financial position (continued)

An open market acquisition strategy was approved, which provided a set of criteria to determine which houses could be purchased. A budget of £11.2 million was set aside for this strategy and to date £6.4 million has been spent to acquire 57 houses.

Despite the investment in affordable housing during 2011-12, achievement of the Scottish Government's target that all homeless people are offered permanent accommodation remains increasingly challenging.

The table below shows the variance against budget for each department at the year end.

	Budget 2011-12 £000	Actual 2011-12 £000	Variance £000
Education and children's services	288,058	287,520	(538)
Community services	107,252	106,760	(492)
Chief executive's office	3,344	4,101	757
Environment	25,920	25,972	52
Corporate resources	1,924	1,632	(292)
Corporate management	(421,238)	(421,726)	(488)
Other movements	-	(149)	(149)
Decrease in usable revenue reserves	**5,260**	**4,110**	**(1,050)**

Source: East Lothian Council

The largest deficit compared to budget is in the chief executive's office, which relates to costs for exit packages agreed as part of the restructuring.

The decrease of £4.1 million primarily represents £2.1 million required to support the revenue budget and £1.3 million use of the cost reduction fund.

As part of the financial reporting process, each service group is given a financial risk rating (low, medium or high). Management has identified that all groups rated as 'high' overspent against their approved budgets. There are risks going forward of achievement of a sustainable financial position.

Housing revenue account ("HRA")

The outturn position on the HRA is a deficit of £4.4 million. However, after making the adjustments between the accounting basis and funding basis under statute (credit of £0.2 million) and a transfer from the capital fund (£2.5 million) the decrease in the year was £2 million, giving a carry forward balance at 31 March 2012 of £2.7 million. The deficit on the HRA was due to rental income being below budget, reflecting lower numbers of affordable house completions.

Open market acquisition

The Council is required to provide dwellings for homeless people as part of new legislation that comes into effect later in 2012. Due to the economic climate, there has been a slowdown in the completion of new build affordable housing, and consequently the Council approved the purchase of houses from the open market.

An open market acquisition strategy was approved, which provided a set of criteria to determine which houses could be purchased. A budget of £11.2 million was set aside for this strategy and to date £6.4 million has been spent to acquire 57 houses. The scheme is currently on hold while the Council brings the acquired houses up to the appropriate standards.

As part of this strategy, the Council approved £4 million capital expenditure to be funded by revenue. This amount was fully utilised during the year and substantially accounts for the net decrease in the HRA. This strategy had a direct impact on the housing revenue account revenue reserves during 2011-12.

Despite the investment during 2011-12 in affordable housing, achievement of the Scottish Government's target that all homeless people are offered permanent accommodation remains increasingly challenging.

Financial position (continued)

Total capital expenditure in 2011-12 was £71.5 million, below the approved capital plan of £77.3 million. This level of capital investment represented a 26% increase over 2010-11 levels.

Management has commenced a review of the capital plan. This will include consideration of the timescale of the plan, the timings of individual projects and the associated costs. As part of this review management is considering the overall affordability of the plan in the context of ensuring financial sustainability.

Capital programme

Total capital expenditure in 2011-12 was £71.5 million, below the approved capital plan of £77.3 million. This level of capital investment represented a 26%, or £14.7 million increase over 2010-11. The table below provides an analysis of capital expenditure across general services and the housing revenue account; comparing actual capital expenditure to budget and prior year.

Year	Total	Housing Revenue Account	General Services
2011-12 (£m)	71.5	33.2	38.3
Capital plan budget (£m)	77.3	37.4	39.9
Under / (over) spend (£m)	5.8	4.2	1.6
2010-11(£m)	56.8	30.1	26.7
Increase from 10-11 (£m)	14.7	3.1	11.6
Increase from 10-11	26%	10%	43%

Source: East Lothian Council

In respect of the housing revenue account the largest element of the capital underspend (£4.6 million) was on the Council's approved open market acquisition strategy. The scheme is currently on hold while the Council brings those acquired properties to appropriate standards and management reflects on the strategy.

Actual capital expenditure on general services was £38.3 million and the most significant capital projects undertaken are set out below. A small underspend of £1.6 million against the approved budget was achieved. This related to a number of small underspends, the more significant of which were projects that have taken longer than expected to initiate, including the Musselburgh care home and the Gullane day centre projects.

Management has also identified some areas of capital overspends totalling around £1.5 million. These are in respect of the Brunton hall refurbishment, Dunbar community facility and Ormiston community facility. Management estimate that a significant proportion of the additional cost will impact the available resources in 2012-13; putting pressure on achievement of the 2012-13 capital plan. Management has initiated a review of these projects.

In addition, as part of the approach to medium to long-term financial planning, management has commenced a review of the capital plan. This will include consideration of the timescale of the plan, the timings of individual projects and the associated costs. As part of this review management is considering the overall affordability of the plan in the context of achieving recurring financial balance.

Analysis of capital projects: 2011-12

Project	Expenditure £ m
New affordable homes (HRA)	14.2
Modernisation (HRA)	11.0
Roads	7.0
Open market acquisition (HRA)	6.4
Haddington joint school	4.3
Dunbar community facility	4.0
John Grey centre	3.7

Source: East Lothian Council

Financial position (continued)

Of all Scottish local authorities, the Council has the highest level of net external debt as a proportion of revenue spend, representing a significant risk.

The level of external debt needs to be considered in the context of the medium to long-term financial position to ensure that a sustainable financial position is achieved over the medium to long-term.

Borrowing

The Council's capital expenditure is largely funded through borrowing, which has the effect of increasing the level of indebtedness which the Council must repay, with interest, from future revenue budgets.

Borrowing increased in 2011-12 by £38.9 million (15%), compared to a 26% increase in capital expenditure. Taking account the impact of increased capital grants and capital funded from revenue, the increase in capital expenditure funded from borrowing was approximately 13%; comparable with the increase in borrowing.

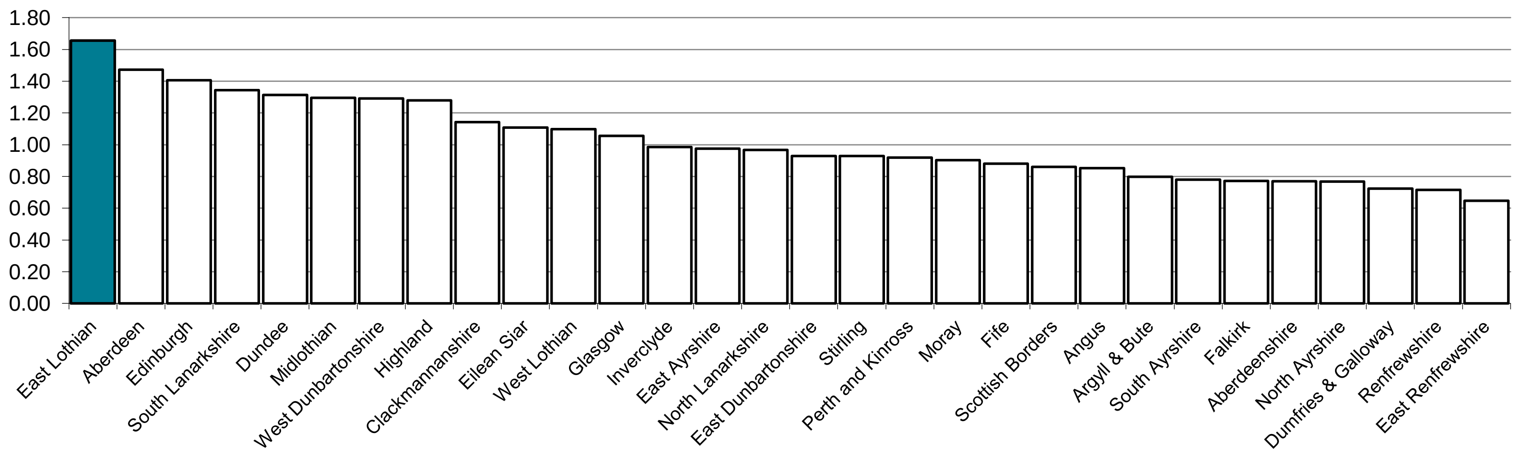
In benchmarking undertaken by Audit Scotland, from analysis of the unaudited accounts of Scotland's 32 local authorities, the Council has the highest level of net external debt when taken as a proportion of revenue expenditure (166%) and per head of population (£3,500 per head). In addition, the Council has the fourth highest level of debt as a proportion of fixed assets, with a ratio of 0.75.

Interest payable and similar charges as a proportion of net revenue spend is 7%, being the ninth highest percentage of the 32 other local authorities within Audit Scotland's analysis.

The Council's level of debt places significant pressures on future available revenue funding as debt and associated interest must be repaid. This represents a significant risk for the Council, placing a strain on available revenue resources in future years. The level of external debt needs to be considered in the context of the medium to long-term financial position of the Council to ensure that a sustainable financial position is achieved over the medium to long-term.

Recommendation one

External debt as a proportion of revenue spend – 32 Scottish local authorities



Source: Audit Scotland

Financial planning

The 2012-13 budget forecasts a breakeven position, incorporating a further £4 million utilisation of reserves.

Revenue budget

A three year revenue budget was approved by council in February 2012. This used the 2011-12 budget as a base and reflected changes for known items of income and expenditure in future years. The 2012-13 budget forecasts a breakeven position, incorporating a further £4 million utilisation of reserves. This budget has been set on the assumption that council tax will remain frozen in 2012-13.

The main changes over the period to 2014-15, by department, are summarised below. These are based on the previous departmental structure, which has now changed following the chief officer restructuring exercise. The changes detailed below are incorporated in the approved budgets and comprise of both known changes and agreed efficiency savings / measures.

A significant element of the efficiency savings relate to streamlined workforce management, group savings targets to meet from service redesign, removal of current or future vacancies and tighter management of variable staffing costs, such as overtime.

The changes have been projected across each of the three years, to obtain the budget figures to 2014-15, which will be the first year when reserves are forecast not be used to meet recurring expenditure. The increased level debt charges represent the largest movements within corporate commitments, reflecting the increased borrowing requirements.

Department	Budget 2011-12 £000	Changes 2012-13 £000	Changes 2013-14 £000)	Changes 2014-15 £000	Cumulative 2015 £000
Chief executive	3,644	(34)	(127)	23	3,506
Community services	70,427	(167)	(903)	297	69,654
Corporate resources	8,802	(339)	(404)	94	8,153
Education and children's services	94,870	(556)	(654)	940	94,600
Environment	15,600	(214)	20	274	15,680
Net expenditure	**193,343**	**(1,310)**	**(2,067)**	**1,627**	**191,593**
Corporate income	(217,028)	(1,744)	(1,324)	(5,599)	(225,695)
Transfer to/(from) reserves	(5,260)	1,187	1,789	2,284	-
Corporate commitments	28,945	1,867	1,602	1,688	34,102
(Surplus) / deficit	**-**	**-**	**-**	**-**	**-**

Source: East Lothian Council

Financial planning (continued)

The Council is planning to utilise most usable un-earmarked general reserves by 31 March 2014. In 2014-15 the Council is budgeting for a break-even position.

While as at 31 March 2012, management confirmed that the Council remains on track with its existing financial strategy, significant financial risks continue to emerge, including the inability of certain services to constrain and reduce costs and overspends on elements of the capital plan.

Management are planning to undertake a mid-year financial review for presentation to council in October 2012.

Cost reduction fund

The Council has a cost reduction fund, set up in October 2009 with £1 million, and later revised in February 2011 to £5 million. This was set up to provide earmarked reserves for cost reduction activities. As at 31 March 2012, £3.7 million was available to cover the cost of further service reviews.

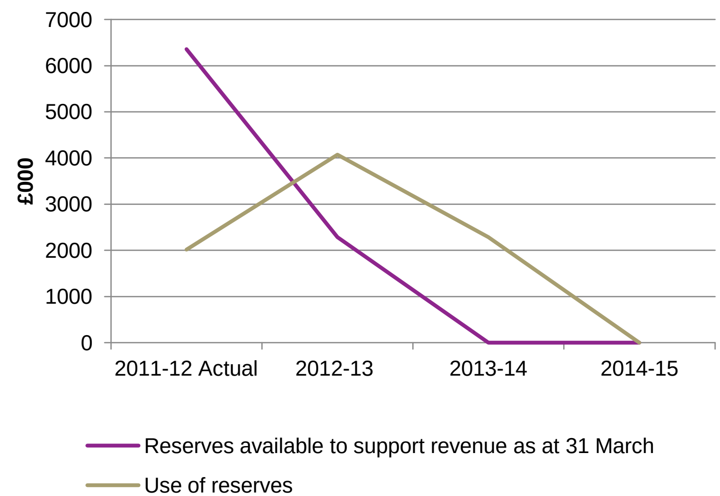
Use of reserves

The Council is planning to utilise most usable un-earmarked general reserves by 31 March 2014. In 2014-15 the Council is budgeting for a break-even position. Theoretically, while reserves are not planned to be required in 2014-15, this clearly gives rise to significant challenge and risk for the Council, requiring it to achieve budget in each of the next two financial years and to ensure that the level of required change is delivered to achieve an underlying recurring financial balance from 2014-15.

While as at 31 March 2012, management confirmed that the Council remains on track with its existing financial strategy, significant financial risks continue to emerge, including the inability of certain services to constrain and reduce costs and overspends on elements of the capital plan.

Management are planning to undertake a mid-year financial review for presentation to council in October 2012. We understand this will consider the current financial position against the targets set. This is a key element of ensuring assessment and challenge of the financial position and will help enable decisions to be taken in order to facilitate achievement of the medium to long-term financial strategy and achievement of recurring financial balance. As part of the planned mid-year review, management will incorporate a review of the capital plan.

The results for quarter one of 2013, to 30 June 2012, show an underspend compared to budget and consequently an improved reserves position. However, management have identified areas of potential overspend in the remainder of the year and are proactively monitoring over the next quarter in order to manage reserves use for the full year.



Source: KPMG LLP

Other issues

The Council has established a strategic welfare reform group to consider and plan for the associated risks and to ensure the Council is prepared to respond to the changes.

An agreement was reached to share the post of executive director of education with Midlothian Council. A decision has yet to be taken in respect of whether this arrangement will continue into 2013 and beyond. Following the change in administration the decision to appoint a joint head of education with Midlothian Council was rescinded.

Welfare reform

As a result of the Welfare Reform Act 2012, a number of significant changes will be required in how councils deliver benefit services. The most significant change is the introduction of 'universal credits', which is an integrated working age benefit which will replace existing benefits, including housing benefit. Universal credits will be administered by the Department of Work and Pensions ("DWP"). Changes to current arrangements are expected to commence during 2013.

The Council has established a strategic welfare reform group to consider and plan for the associated risks and to ensure the Council is prepared to respond to the changes that are required. Officers have provided a number of briefings to members on the impending changes and the likely consequences for benefit claimants and Council staff. Additional briefings are planned once more information is available.

While responding to the introduction of universal credits, which not only impacts the nature of benefits available in the future, but also the Council's role in the administration of these benefits, will present challenges for the Council, it is clear that action has commenced by officers to mitigate the associated risks. Given the significance of this matter it is important that continued regular updates are provided to members and there is continued senior officer involvement in ensuring the timely implementation of transition arrangements.

Recommendation two

Partnership working

During 2011-12, following the retirement of the director of education at Midlothian Council, an agreement was reached to share the post of executive director of education across the two councils from 1 April 2012 until 31 December 2012. A decision has yet to be taken in respect of whether this arrangement will continue into 2013 and beyond.

In addition, the Council approved an education shared services initiative with Midlothian Council which included the appointment of a joint head of education. However, following the change in administration as a result of the May 2012 local government elections the decision to appoint a joint head of education was rescinded.

At a recent meeting of the joint liaison group, a group comprising of senior officers and members from both the Council and Midlothian Council, the sharing of a health and safety manager across East and Midlothian councils on a six month trial basis was approved. This will help the Council to draw on the expertise and resources of the current manager at Midlothian, while providing team resources to Midlothian council.

Police & Fire and Rescue

The Police and Fire & Rescue Reform (Scotland) Act 2012 ("the Act") created a national police force and a national fire and rescue force. This replaces local authorities' current role as police authorities and fire & rescue authorities. The Act includes a framework for the delivery of local scrutiny and engagement arrangements, which all local authorities and the new services will need to implement when the legislation is enacted from April 2013.

The Council has participated in the *Local Scrutiny and Engagement Implementation Network* and formed a pathfinder with Lothian and Borders Fire & Rescue and Lothian & Borders Police. Discussions are ongoing with these bodies and pilot arrangements have been established.

On 26 June 2012, the Council agreed to establish a shadow police and fire & rescue services board for the period running up to the establishment of the new national bodies.

Audit risks were identified in respect of opening balances, financial position, senior staff structure, group accounts, valuation of property, plant and equipment and heritage assets.

Management agreed that there was a material error in the 2010-11 financial statements; a prior year adjustment has been processed in the 2011-12 financial statements to correct the error.

Issue	Key risk and implications	KPMG comment
Opening balances	International Standard on Auditing (UK and Ireland) 510: *Initial audit engagements – opening balances* requires auditors to obtain sufficient, appropriate audit evidence that opening balances do not contain misstatements that materially affect the financial statements. The standard also requires auditors to verify that appropriate accounting policies are reflected in the opening balances and that they have been consistently applied in the current period's financial statements.	We have: ▪ held discussions with the Council's previous external auditors in respect of prior year audit focus areas, corporate governance and general risk assessment; and ▪ reviewed the prior year financial statements, annual audit reports and other reports issued by the previous external auditors. As a result of this work we identified a number of areas for further enquiry and review across the primary financial statements and associated notes, including group financial statements, investments and the valuation of other land and buildings. Our consideration of these, and other technical accounting matters, are set out on the following pages.
Valuation of property, plant and equipment – *other land and buildings*	A valuation of *other land and buildings* was performed by an external valuer engaged by the Council, as at 1 April 2011. While the final valuation report was not available to the Council at the time of preparing the 2010-11 financial statements, it was received in August 2011, prior to the 2010-11 financial statements being finalised. The report was not analysed until after the financial statements were signed and it showed a net valuation decrease to other land and buildings of around £95 million, after adjusting for the componentisation of secondary school assets.	In accordance with accounting standards, we highlighted to management that the valuation provided evidence of fair value at 31 March 2011. Therefore, in our view, this matter should have been treated as an adjusting 'post-balance sheet event' and reflected within the 2010-11 financial statements. Further to our discussions, management accept that there was a material error in the 2010-11 financial statements and a prior year adjustment has been processed in the 2011-12 financial statements to correct the error. Following consideration by management the Council's external valuers has confirmed that the decline in residential development land values occurred mid to late 2008, consequently the prior year adjustment has been applied to the earliest date possible within the financial statements; opening reserves as at 1 April 2009. We have reviewed the prior year adjustment disclosures and are content that they are materially correct.

There are different valuation cycles across property, plant and equipment categories; management has made assumptions regarding the fair value of certain categories, most notably 'council dwellings' which have not been formally revalued since 1 April 2009.

Due to the potential complications that may arise from revaluing council dwellings we recommended management review and take action on the current approach to the valuation of council dwellings.

Following detailed discussions with us, the Council has consolidated the joint boards into the group financial statements having concluded that they have significant influence.

Issue	Key risk and implications	KPMG comment
Valuation of property, plant and equipment – *policy on valuations and componentisation*	The Code, in line with IAS 16 property, plant and equipment, requires that where property, plant and equipment are held at fair value, valuations shall be carried out at intervals of no more than five years. Valuations may be carried out on a rolling basis or once every five years. In addition, the Code requires that each item of property, plant and equipment with a cost that is significant in relation to the total cost of the item should be depreciated separately. Componentisation of property, plant and equipment is applicable from the earliest date a revaluation is carried out after 1 April 2010.	In our view the level of clarity in respect of the Council's policy of valuations; the programme of valuations and the assessment of the appropriateness of carrying values at the balance sheet date could be improved. To address these matters we have recommended that management should review the valuation policy and procedures to ensure compliance with the Code and accounting standards. Council dwellings were last revalued as at 1 April 2009; at our request management has obtained confirmation from the district valuer that the value of council dwellings reflected within the financial statements at 31 March 2012 remain appropriate. We have also sought, and obtained, management representations regarding the value of council dwellings. Due to the potential complications that may arise from revaluing council dwellings (since they are held as one line item with enhancements also held as one line item) we have recommended that management review and take action on the current approach to the valuation of council dwellings.
Group financial statements	The Council has interests in a number of different organisations, including Lothian and Borders Fire and Rescue Board, Lothian and Borders Police Board and Lothian Valuation Joint Board. These joint boards were included as associates in the group financial statements in 2010-11. This continued approach to accounting for these interests was subject to discussion during the interim audit process.	During the audit we discussed with management the group structure and, specifically, management's rationale for possible non-inclusion of the joint boards. Although the Council does not have more than 20% of the voting rights of each joint board, which would indicate the Council has significant influence, there are other indicators of significant influence, as outlined in IAS 28 *investments in associates.* As part of our analysis we concluded that the requirements of IAS 28 *investments in associates* were met and that the joint boards should be accounted for as associates. Before the financial statements were completed management concluded that it was appropriate to include the joint boards in the group accounts and account for them as associates. The disclosures relating to the group accounts have been updated to reflect the requirements of the Code.

During 2011-12 changes to the chief officer structure were implemented. We did not identify any material non-compliance with internal procedures or legislation, however we noted that there were opportunities to improve the documentation of internal meetings and discussions and human resources and legal advice received.

Payments to individuals were made in line with procedures. We have reviewed the exit packages disclosure within the remuneration report, where appropriate and concluded that they are appropriate.

Issue	Key risk and implications	KPMG comment
Chief officer structure	Following agreement of the three-year council plan and approval of the budget, in early 2012, the chief executive proposed changes to the chief officer structure to ensure the efficient and effective delivery of council services.	During 2011-12 changes to the chief officer structure were implemented. The proposals were considered and approved by the Council on 28 February 2012 and the revised chief officer structure came in to effect from 1 April 2012. The need for restructuring arose primarily from the discussions around the most efficient and effective way to deliver the 2012-17 council plan. The posts subject to restructure were: ▪ four director posts were reduced to three; and ▪ 11 heads of service; reduced to seven. The chief executive led and implemented a restructuring process that was based on internal and external consultation. We did not identify non-compliance with internal procedures or legislation, however we noted that there were opportunities to improve the documentation of internal meetings and discussions and human resources and legal advice received. In addition, we noted that while the monitoring and section 95 officers jointly commissioned legal advice from a different source, the existence of this separate legal advice was not mentioned in the council paper (28 February 2012). However, in the chief executive’s view, some of the content informed, indirectly, the content of the council paper. Payments to individuals were made in line with procedures. We have reviewed the exit packages disclosure within the remuneration report, where appropriate and concluded that they are appropriate.

We discussed changes to the Code with management. During our final financial statement audit, we confirmed that these changes had been appropriately applied. However, we identified a number of disclosure amendments which have been correctly updated in the financial statements.

Issue	Key risk and implications	KPMG comment
Code 2011-12	The Council is required to prepare financial statements in accordance with the Code. The Code 2011-12 has been updated and a number of changes required consideration by management for any impact on the reporting requirements and financial statements	We discussed changes to the Code with management. The main changes impacting the financial statements were: ▪ applicability of FRS 30 *Heritage Assets*; ▪ additional guidance added in respect of leases; ▪ new disclosure requirement in respect of exit packages; and ▪ new requirement for a specific statement in the annual governance statement / statement on the system of internal financial control on whether financial management arrangements conform with the governance requirements of the statement on "the role of the chief financial officer in local government." During our final financial statement audit, we confirmed that these changes had been appropriately applied. Following completion of the Code disclosure checklist and consideration of Audit Scotland 's Notes for Guidance, we identified a number of disclosure amendments which have now been correctly updated in the financial statements.

Local response to national studies

As part of our annual audit process, we consider the Council's arrangements in respect of performance management and in responding to Audit Scotland and Accounts Commission national studies.

Audit area	Overview	Findings
Local response to national studies	Audit Scotland and the Accounts Commission periodically undertakes national studies on topics relevant to the performance of public sector bodies. To ensure that added value is secured through the role of Audit Scotland and the Accounts Commission and its appointed auditors, auditors will continue to ensure that audited bodies respond appropriately to reports from the programme of national performance audits.	We have considered the Council's response to the following national reports: ▪ Scotland's public finances: responding to the challenge; ▪ transport for health; ▪ community health partnerships; and ▪ modernising the planning system. We have prepared a short return to Audit Scotland for each report. Our assessment concluded that reports are considered by the audit and governance committee, except in respect of *transport for health* and *modernising the planning system* which were not formally considered. In addition, we noted that management has not performed a self-assessment of local arrangements against the recommendations in any of the reports. We raised a recommendation in our interim management report that management should ensure that the content of all relevant national reports are discussed by the council or a sub-committee, that self-assessments are performed and that appropriate action plans and timetables are agreed to feedback local actions. In March 2012 the Accounts Commission published their overview report on local government in Scotland. At the audit and governance committee meeting on 18 September 2012, the committee agreed to consider the Council's position against the key findings of this report, including utilising the 'How Good is Our Council (HGIOC") framework to inform debate. Management has identified several improvements which have been incorporated in to the Council improvement plan for 2012-13.

Local response to national studies (continued)

As part of its targeted approach to following-up a small number of performance audit reports each year, Audit Scotland has identified *Maintaining Scotland's roads: a follow-up report* for follow-up in 2011-12.

We carried out follow-up work to consider the Council's response to the report.

Maintaining Scotland's roads: a follow up

As part of its targeted approach to following-up a small number of performance audit reports each year, Audit Scotland has identified the *Maintaining Scotland's road – follow-up report* for follow-up by local auditors in 2011-12. The aim of the follow-up work is to assess the progress that councils have made in driving forward road maintenance activities, managing the performance of road maintenance activities, and maximising value for money in road maintenance services. Set out below are our findings from our follow up work.

Question	Audit Scotland prompt	Findings
How did the council respond to *Maintaining Scotland's roads: a follow-up report* following publication?	Was the report formally considered by the: ▪ full council? ▪ audit committee? ▪ senior management team? ▪ other committee? Please provide the date the report was considered and the key actions in any action plan developed.	Audit Scotland and the senior transportation manager attended the March 2011 audit and governance committee where the report was discussed in detail. The report was also discussed at the April 2011 meeting of the policy and performance review committee. This was also attended by the senior transportation manager.
Does the Council have appropriate plans to drive road maintenance activities?	Does the Council have a comprehensive road asset management plan, developed in accordance with the SCOTS road asset management project? Does the Council adequately monitor progress against the road asset management plan and do monitoring results demonstrate satisfactory progress?	A road asset management plan was prepared by the senior transportation manager and approved by the environment policy and performance review committee in June 2010. A copy of the road asset management plan was provided to us as part of our follow-up work. It is detailed and has been developed in accordance with the SCOTS road asset management project. The Council monitors progress against the road asset management plan annually through the policy and performance review committee. It was last considered at the June 2012 meeting. The report submitted to the committee demonstrates satisfactory progress.

Local response to national studies (continued)

Question	Audit Scotland prompt	Findings
How does the Council manage performance of its road maintenance activities?	Is the Council using relevant performance indicators to help manage its road maintenance service? ▪ To what extent have SCOTS' core performance indicators been adopted? ▪ To what extent have SCOTS' secondary and statistical indicators been adopted? In which areas is the Council performing particularly well against its performance indicators? In which areas does the Council need to improve its performance and what plans are in place to address this? The Council did not meet its target in relation to number of working days lost due to sickness absence. However, this had reduced considerably since 2008-09 and there is a strict sickness absence policy.	The Council uses a road network management scorecard which includes a number of performance indicators. All SCOTS performance indicators have been adopted, including core performance indicators and secondary statistical indicators. The Council is performing particularly well against customer service indicators, such as response to routine correspondence and operations indicators, such as repairs times. The Council did not meet its target in relation to number of working days lost due to sickness absence. However, this had reduced considerably since 2008-09 and there is a strict sickness absence policy.
What is the Council doing to maximise value for money in its road maintenance service?	What is the Council doing to maximise value for money in its road maintenance service? Within the last 18 months to what extent has the Council investigated the following opportunities to improve value for money in its road maintenance service: comparison of costs and performance with other councils, Transport Scotland or the private sector; partnership working with other councils, Transport Scotland or the private sector; service reconfiguration; pooling and flexible use of resources; innovative practices; and any other opportunities? What improvements in economy or service has the Council achieved as a result of these initiatives to date? If planned improvements have still to be achieved, when is this likely to happen? What other steps are being taken in response to the national review of roads maintenance?	The Council is a member of the Association for Public Service Excellence ("APSE") thus it is benchmarked across similar councils across the UK for highways and winter maintenance. This includes benchmarking against financial indicators, such as cost of gritting roads. The Council is a member of the Edinburgh, Lothian, Borders and Fife ("ELBF") forum. As part of this the use of sharing roads maintenance was looked into, but has not progressed following advice from the Council's legal team. For capital works to roads, the Council uses Scotland Excel, the local government procurement centre of expertise. Through inclusion in APSE the Council has improved on sickness absence among the transportation team. There is now a strict regime over refilling posts to ensure staff costs remain controlled.

Improvement framework; Best Value

Under the Local Government in Scotland Act 2003 ("the 2003 Act"), auditors have a duty to be satisfied that councils have made proper arrangements to secure best value.

The timing, nature and extent of Best Value work is determined as part of the shared risk assessment process.

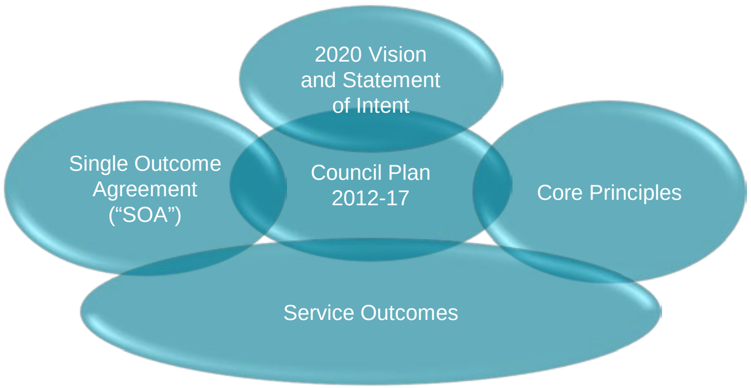
In accordance with the principles of Best Value, the Council seeks to pursue 'continuous improvement'. The Council has developed an improvement framework, approved on 27 March 2012, which sets out five inter-related elements:

- setting clear outcomes and priorities.;
- self-evaluation;
- service and improvement planning and management;
- performance management, monitoring and reporting; and
- external assessment and accreditation.

This framework can be considered best practice, and should support management's ongoing assessment of the extent to which the Council is achieving Best Value and support the Council's drive for continuous improvement.

Setting clear outcomes and priorities

Setting clear service outcomes and priorities is derived from a number of sources. The framework is illustrated in the diagram below.



Source: East Lothian Council

The council approved the draft Council plan 2012-17 in January 2012. Following the May 2012 local government elections the Council plan was updated to reflect the manifestos of the new coalition administration. In developing the Council plan management has aligned it to the requirements of the agreed outcomes within Single Outcome Agreement ("SOA") and the broader public sector reform agenda. Additionally, the Council plan has been developed to take into account the local priorities of East Lothian. The revised Council plan was approved in August 2012.

The Council plan has four key objectives, all of which are aligned to the SOA: grow our economy; grow our people; grow our communities; and growing the capacity of our Council. Furthermore, agreed service plan outcome areas are aligned with the Council plan. This approach ensures that there is clear and transparent alignment of objectives.

East Lothian Community Planning Partnership ("ELCPP") is a partnership of organisations from the public, voluntary, private and community sectors who are working together for community planning. The partnership is led by the Council leader. Achievement of the agreed SOA outcomes is the responsibility of ELCPP, with all members of the partnership contributing to achievement of the agreed outcomes.

Each performance indicator for the Council is linked to one of the SOA outcomes. Performance against these is reported in the Council's annual performance report. The Council intends to review the SOA during 2012-13, in line with guidance to be issued for SOA 2013. As part of the panned future approach we understand that management intend to bring an increased focus to reporting on agreed priority areas.

Improvement framework; Best Value (continued)

Single outcome agreements align public sector activity to national priorities. While there are no audit requirements in respect of the Council's performance against its SOA, the Council is expected to have suitable arrangements to:

- develop governance and accountability arrangements to support its SOA;
- ensure clear links between high-level SOA outcomes and more detailed service-level outcomes, both within the Council and across it's community planning partners;
- ensure the SOA is supported by robust performance management and reporting arrangements;
- report progress towards SOA outcomes to the Scottish Government; and
- undertake public performance reporting on progress towards SOA outcomes.

Source: Audit Scotland

Self-evaluation

The Council utilises the 'How Good Is Our Council?' ("HGIOC") self-evaluation model. This model collates information on service performance across five key questions. A facilitation team helps services to complete this work. Self evaluations, using the HGIOC framework, were performed during February and March 2012, based on the previous 12 months performance. These were performed at different levels across departments.

During 2011-12 internal audit completed a review of the HGIOC process. A number of recommendations were made to improve the process. The key recommendations were in respect of duplication of questions, confusion about the definitions of stakeholders, leadership and management. We understand that the recommendations from the audit were implemented.

The corporate policy unit has also produced a report evaluating the current process. This makes a number of suggestions for enhancement to the current arrangements. These include broadening the approach to service reviews to support the Council's focus on continuous improvement and achievement of Best Value by introducing increased senior officer review and challenge, allowing additional comparisons and contrasting of performance to be undertaken to support service improvement. As part of planned changes to future arrangements we understand that management are also planning to introduce a more risk based approach to undertaking service reviews.

To ensure effective preparation, management have incorporated questions from the Best Value 2 toolkits in to HGIOC.

Service and improvement planning and management

Service plans are required to recognise the improvement actions from the HGIOC self-evaluation process. In the corporate policy unit service plan information on the level of resource required to meet each agreed activity / SOA outcome has been included. As part of the continuous improvement agenda, there would be benefit in reviewing the effectiveness of this approach and rolling this out, where applicable / appropriate across the other service and operational plans.

Additionally, in the long-term it is anticipated that the timeline for the self-evaluation and service planning will be brought forward to enable resource requirements to inform the Council's budget setting process; supporting a 'bottom-up' approach to budget setting. This will have benefits in ensuring resources are appropriately allocated to areas of priority and the use of resources can be more directly linked and evaluated against performance achieved against agreed outcomes.

Improvement framework; Best Value (continued)

The Council approved a council improvement plan ("CIP") for 2012-13. This draws on actions from the HGIOC self-evaluation process and the corporate governance self-evaluation process, prepared by management to inform the annual governance statement disclosure within the 2011-12 financial statements. In addition it captures the 2012 employment survey results and identified focus areas arising from the AIP. A review of progress against the CIP 2011-12 was undertaken and a number of action points have been carried forward to the 2012-13 CIP.

Performance management

Together with the focus on self-evaluation, the main element of performance management takes place through monitoring service performance against agreed performance indicators. Elected member scrutiny is primarily performed by the policy and performance review committee and the audit and governance committee. In addition the corporate management team reviews performance on a continuous basis.

External accreditation

Management are seeking to achieve Council-wide accreditation for Investors in People ("IiP") and Customer Service Excellence ("CSE"). Management consider there are close links and alignment between these accreditation schemes and the current work being undertaken on enhancement to the self-evaluation arrangements. These links will support the Council to continue to build a sustainable and integrated improvement approach.

Shared risk assessment

The Council's Assurance and Improvement Plan ("AIP") assessed no areas as being areas of operational scrutiny risk, three as areas of 'uncertainty' and the remaining 35 as 'no significant risk'. The three areas of 'uncertainty' are corporate services, challenge and improvement and use of resources – asset management. These were also assessed as areas requiring ongoing scrutiny in the previous AIP.

. The AIP concludes that *"there are no significant concerns about East Lothian Council's overall performance. The LAN recognises the Council's ongoing commitment to continuous improvement and self-evaluation. There is a clear vision and direction for the work of the Council and a number of improvement activities are already underway and progressing well."*

The Council considered the updated AIP on 28 August 2012. It is expected that this will assist in service planning and in supporting the development and implementation of the Council's improvement framework.

Shared risk assessment

- A key aspect of the Scottish Government's scrutiny agenda is to better coordinate and streamline scrutiny and achieve greater effectiveness, while protecting the independence of scrutiny bodies.
- The local area network ("LAN") met during 2012 to update the three year rolling Assurance and Improvement Plan ("AIP") for the Council.
- The Council's updated AIP was published in May 2012, in conjunction with the National Scrutiny Plan for Local Government.

Source: Audit Scotland

Statutory performance indicators

Framework

The statutory deadline for publication by the Council of statutory performance indicators ("SPIs") is 30 September 2012. Since 2009-10, there has been a significant shift in approach to SPIs, with a significant reduction in the number of specific indicators that councils are required to use, while including measures designed to encourage councils to use a greater range of information as part of their mainstream performance management and reporting activities.

The Council is responsible for having appropriate arrangements to collect, record and publish complete and accurate data, so far as is practicable.

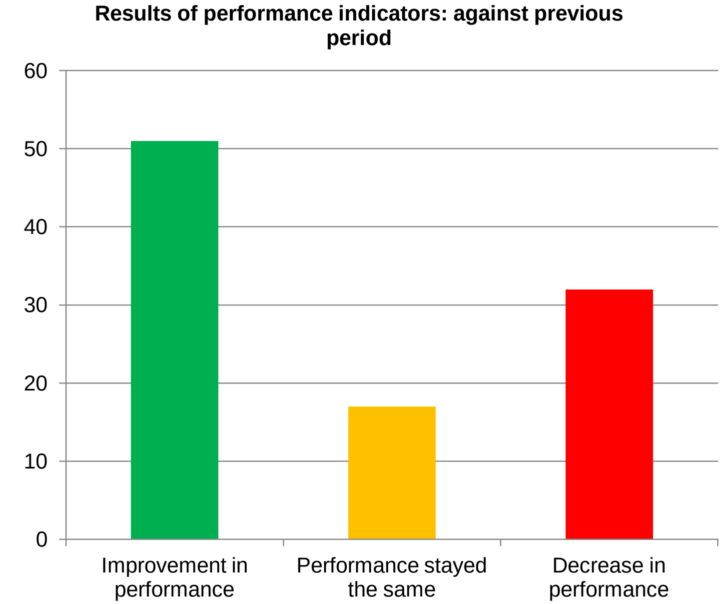
Our responsibilities, as the Council's external auditors, extend to understanding the arrangements and systems that the Council uses to generate performance results and reports.

The Council reports on the 25 set SPIs and also has a suite of other performance indicators which it has developed. Each performance indicator is linked to one of the outcomes in the SOA.

The Council uses the *Aspireview* system to input, manage, interrogate and present data. Inherent within the system are IT controls. For each indicator a performance indicator verification certificate is produced. Management consider that there are adequate checks and controls to provide comfort over the completeness and accuracy of data. Internal audit are currently completing a review of the SPI arrangements, and will complete sample testing on the completeness and accuracy of data used. Once complete, we will review this work in order to consider placing reliance on it and provide any further comments.

Performance against the Council's performance indicators is reported in an annual performance report, publically available and discussed at the policy and performance review committee. The 2011-12 performance report highlighted that the Council has achieved or exceeded agreed targets for 61% of the performance indicators.

In comparing performance against 2010-11 for 51% of performance indicators there was an improvement in performance, for 49% of indicators there was no demonstration of improvement, with 32% of performance indicators actually showing a decrease in performance.



Source: East Lothian Council

Corporate governance framework and supporting arrangements

Over-arching and supporting corporate governance arrangements provide a framework for organisational decision-making.

Corporate governance	The Council operates a committee based structure with the Council supported through five committees: planning, education, policy and performance, audit and governance and the petitions committees. The audit and governance committee and the policy and performance committee are chaired by members of opposition parties. These provide scrutiny and challenge to strategic decisions and performance. The Council maintains an integrated governance framework to provide an appropriate structure for maintaining decision-making, accountability, control and behaviour. Although there has been no changes in the overall governance framework, there have been a number of changes in councillor composition as a result of the local elections in May 2012. One notable change is the implementation of the monthly joint group, a new arrangement for an interface between administration members and officers. Under the former administration an equivalent group was in place, being the 'Leader's Briefing'. Following our interim audit we reported that the risk management strategy and supporting documentation, including service and corporate risk registers, demonstrated a commitment to good practice and increased focus by senior officers since 2009. The strategy remains under review and we would encourage management to use this revision to clearly define 'risk appetite'. This would support the Council in using risk management as a strategic and operational tool to drive decision-making and strategic developments, and mitigate the risk of the process increasing bureaucracy. At the same time, management recognises the need to embed risk management at an operational level and increase cultural awareness that it is everyone's responsibility to manage risk on a day to day basis.
Political landscape	The May 2012 elections saw a change in administration; changing from an SNP / Liberal Democratic coalition to a Labour / Conservative coalition. An elected member induction pack was submitted to the members' library service during April 2012. This included induction events relevant to the work, role and responsibilities of the Council. Management are also planning on completing a '100 day review', to assess progress since the elections and help identify the continuing induction and development needs of members. In addition, a session is being planned for members of the audit and governance committee, as part of the overall induction arrangements, which will be led by CIPFA to facilitate a session on challenge and scrutiny. Also, consideration is being given to the potential benefits to members of attending and observing the operation of the other audit committees across other areas of the public sector. In their *Overview of local government in Scotland*, published in March 2012, the Accounts Commission included a checklist for new and returning elected members to use to assess their own understanding and training needs. We recommend that this checklist is utilised as part of management's '100 day review' process, to inform additional training needs but also as a basis for reviewing the effectiveness of the induction arrangements completed to date. ***Recommendation three***

Corporate governance framework and supporting arrangements (continued)

Our reporting throughout the year has identified a number of significant weaknesses and risks arising from gaps in the strategic and financial control framework, including in respect of procurement arrangements, bank and other reconciliation and journal authorisation processes.

Annual governance statement	The governance statement provides details of the purpose of the framework of internal control, along with an analysis of its effectiveness. It describes a number of sources of assurance for the accountable officer and identifies areas for improvements to be focussed on in the future. We reviewed the governance statement and requested a number of amendments to ensure compliance with guidance and our understanding of the Council. We requested a change to the annual governance statement to identify how the Council's arrangements comply with the CIPFA *statement on the role of the chief financial officer in local government* (2010) to ensure compliance with the requirements of the Code.
Remuneration report	Scottish Statutory Instrument 2011 number 64, *The Local Authority Accounts (Scotland) Amendment Regulations 2011 amended the Local Authority Accounts (Scotland) Regulations 1985* added the requirement for local authority bodies to prepare a remuneration report. The Local Government Finance Circular number 8/2011, issued by the Scottish Government, provides guidance that the remuneration report is a statement in its own right and not a note to the financial statements. While there is no statutory prescription on its placement in the financial statements, it suggests a suitable placement would be after the governance statement. The remuneration report follows the annual governance statement at the end of the financial statements.
Internal controls	Our reporting throughout the year has identified a number of significant weaknesses and risks arising from gaps in the strategic and financial control framework, including in respect of procurement arrangements, bank and other reconciliation and journal authorisation processes. As the financial and operating environment in which the Council operates continues to change, with developing priorities and new and emerging financial and non-financial risks, it is increasingly important that the Council plan, supporting service plans and other developments are underpinned by effective organisation-wide controls, robust financial management processes and effective key financial controls.

Corporate governance framework and supporting arrangements (continued)

The absence of a number of controls identified by us as part of the audit process, does, in our view increases the risk of fraud, or other irregularity not being prevented or detected on a timely basis.

Prevention and detection of fraud	The Council has policies and codes of conduct for staff and councillors including a whistle blowing policy. Management has confirmed that no significant fraud or irregularities have been identified during the year. However, the absence of a number of controls identified by us as part of the audit process, does, in our view increases the risk of fraud, or other irregularity not being prevented or detected on a timely basis.
National fraud initiative	NFI helps participating bodies to identify possible cases of fraud and to detect and correct under or overpayments. NFI also helps auditors to satisfy their duties to assess bodies' arrangements for preventing, deterring and detecting fraud. The Council has an established process for investigating cases of potential fraud highlighted by the NFI and although some departments have resource constraints and are unable to follow-up matches themselves, suitable arrangements are in place to ensure this work is covered. As a result of the corporate restructuring, the investigations team which deals with most of the NFI work now reports to internal audit. This is beneficial as the Council's internal audit department will now be working more closely with those involved in investigating NFI cases.
Internal audit	As set out in our audit plan and strategy, we have evaluated the work of internal audit and concluded that we can rely, where relevant, on their work. The content of the internal audit plan is in line with our expectations. Internal audit reported that *"subject to the weaknesses outlined in the controls assurance statements, that reasonable assurance can be placed on the adequacy and effectiveness of the Council's internal control systems for the year to 31 March 2012."* The most significant areas where internal audit identified weaknesses in the design or operation of internal controls included procurement arrangements, the effects of organisational culture on internal financial controls, bank reconciliations, income collection from PPP facilities, software licenses, compliance with financial procedures, administration of the LEADER program and tender evaluation arrangements.

Appendices

Action plan

The action plan summarises specific recommendations, together with related risks and management's responses.

Priority rating for recommendations		
Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the organisation or systems under consideration. The weaknesses may therefore give rise to loss or error.	**Grade two** (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.	**Grade three** (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the control to meet their objectives in any significant way. These are less significant observations than grades one or two, but we still consider they merit attention.

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
1 Borrowing		**Grade one**
The Council's capital expenditure is largely funded through borrowing, which has the effect of increasing the level of indebtedness which the council must pay, with interest, from future revenue budgets. Borrowing increased in 2011-12 by £38.9 million, being a 15% rise. In benchmarking undertaken by Audit Scotland, from analysis of the unaudited accounts of Scotland's 32 local authorities, the Council has the highest level of net external debt of all the local authorities.	The Council's level of debt places significant pressures on future available revenue funding as debt and associated interest must be repaid. This represents a significant risk for the Council, placing a strain on available revenue resources in future years. The level of external debt needs to be considered in the context of the medium to long-term financial position of the Council to ensure that a sustainable financial position is achieved over the medium to long-term.	The Council has already commenced a review of capital programmes and expect to report on this to the October meeting of the Council. **Responsible officer:** Head of Council Resources **Implementation date:** 31 October 2012

Action plan (continued)

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
2 Welfare reform		**Grade three**
As a result of the Welfare Reform Act 2012, a number of significant changes will be required in how councils deliver benefit services. The Council has established a strategic welfare reform group to consider and plan for the associated risks and to ensure that Council is prepared to respond to the changes that are required.	While responding to the changes, such as the introduction of universal credits, will present challenges for the Council, it is clear that action has commenced by officers to mitigate the associated risks. Given the significance of this matter it is important that continued regular updates are provided to members and there is continued senior involvement in ensuring the timely implementation of transition arrangements.	Agreed. **Responsible officer:** Executive Director of Support Services **Implementation date:** January 2013
3 New member training		**Grade three**
Although there has been no changes in the overall governance framework, there have been a number of changes in councillor composition as a result of the local elections in May 2012. An elected member induction pack was submitted to the members library service during April 2012 and was approved by Council (through noting of documents in the members library service) on 15 May 2012. This included induction events relevant to the work, role and responsibilities of the Council.	It is recommended that the new and returning member checklist, included as part of the *Overview of local government in Scotland*, published in March 2012 by the Accounts Commission, is used by members as a tool to inform training needs or review the effectiveness of the Council's arrangements.	Continuing professional development ("CPD") for elected members will be launched on 30 October 2012. The CPD approach (self-evaluation, identification of training and development needs on an individual and tailored basis) is more comprehensive than the generalised checklist approach set out in the Overview of Local Government in Scotland report. The key issues in the checklist will be covered in the competency based self-evaluation used in the CPD process to identify individual councillors' training needs. **Responsible officer:** Corporate Policy Manager **Implementation date:** 30 October 2012

Action plan (continued)

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
4 Remuneration report		**Grade three**
The Council includes the remuneration report after the primary statements and notes, at the back of the financial statements. While not out of line with some other local authorities, it is inconsistent with our experience of good practice in other sectors.	It is recommended that the Council considers whether the existing presentation of the remuneration report demonstrates a continued commitment to transparency. Consideration should be given to repositioning the annual governance statement and remuneration report to follow the foreword, prior to the primary financial statements, to set the context up front for the preparation of the financial statements.	Consideration will be given as part of 2012-13 accounts arrangements. **Responsible officer:** Business Finance Manager **Implementation date:** June 2013

Audit Scotland code of audit practice – responsibilities of the Council

Financial statements

Audited bodies' financial statements are an essential part of accounting for their stewardship of the resources made available to them and their performance in the use of those resources. Audited bodies are responsible for:

- ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority;
- maintaining proper accounting records;
- preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the relevant financial reporting framework (eg, the Financial Reporting Manual or an Accounting Code of Practice);
- preparing and publishing with their financial statements an annual governance statement, statement on internal control or statement on internal financial control and a remuneration report; and
- preparing consolidation packs and, in larger bodies, preparing a Whole of Government Accounts return.

Systems of internal control

Audited bodies are responsible for developing and implementing systems of internal control, including risk management, financial, operational and compliance controls. They are required to conduct annual reviews of the effectiveness of their governance, systems of internal control, or internal financial control, and report publicly that they have done so. Such reviews should take account of the work of internal audit and be carried out by those charged with governance, usually through bodies' audit committees.

Prevention and detection of fraud and irregularities

Audited bodies are responsible for establishing arrangements to prevent and detect fraud and other irregularity. This includes:

- developing, promoting and monitoring compliance with standing orders and financial instructions;
- developing and implementing strategies to prevent and detect fraud and other irregularity;
- receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity; and
- participating, when required, in data matching exercises carried out by Audit Scotland.

Standards of conduct and arrangements for the prevention and detection of bribery and corruption

Audited bodies are responsible for ensuring that their affairs are managed in accordance with proper standards of conduct and should put proper arrangements in place for:

- implementing and monitoring compliance with appropriate guidance on standards of conduct and codes of conduct for members and officers;
- promoting appropriate values and standards; and
- developing, promoting and monitoring compliance with standing orders and financial instructions.

Financial position

Audited bodies are responsible for conducting their affairs and for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:

- such financial monitoring and reporting arrangements as may be specified;
- compliance with any statutory financial requirements and achievement of financial targets;
- balances and reserves, including strategies about levels and future use; and
- the impact of planned future policies and foreseeable developments on their financial position.

Best Value

Achievement of Best Value or value for money depends on the existence of sound management arrangements for services, including procedures for planning, appraisal, authorisation and control, accountability and evaluation of the use of resources. Audited bodies are responsible for ensuring that these matters are given due priority and resources, and that proper procedures are established and operate satisfactorily.

cutting through complexity™