AUDIT AND GOVERNANCE COMMITTEE

9 SEPTEMBER 2014

PUBLIC DOCUMENT PACK

East Lothian
Council

MINUTES OF THE MEETING OF THE
AUDIT AND GOVERNANCE COMMITTEE

TUESDAY 15 JULY 2014
COUNCIL CHAMBER, TOWN HOUSE, HADDINGTON

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Committee Members Present:
Councillor K McLeod (Convener)
Councillor S Brown
Councillor J Caldwell
Councillor S Currie
Councillor F McAllister
Councillor J Williamson

Council Officials Present:
Mrs A Leitch, Chief Executive
Mr A McCrorie, Depute Chief Executive - Resources and People Services
Mr R Montgomery, Head of Infrastructure
Mr T Shearer, Head of Communities & Partnerships
Mr J Lamond, Head of Council Resources
Ms S Fortune, Service Manager – Business Finance
Mr D Christie, Service Manager – Business Finance
Ms K Maguire, Service Manager – Corporate Finance
Mr P Moore, Senior Auditor

Clerk:
Miss F Currie, Committees Assistant

Visitors Present:
Ms S Burden, Assistant Manager, KPMG LLP
Ms L Nelson, KPMG LLP

Apologies:
Councillor A Forrest
Councillor J Goodfellow

Declarations of Interest:
None

1. **MINUTES OF THE MEETING OF THE AUDIT & GOVERNANCE COMMITTEE ON 20 MAY 2014**

The minutes of the meeting of the Audit & Governance Committee on 20 May 2014 were approved.

2. **EAST LOTHIAN COUNCIL ANNUAL STATEMENT OF ACCOUNTS (DRAFT) 2013/14**

The Head of Council Resources, Jim Lamond, presented the Council's draft Statement of Accounts for 2013/14. He emphasised the accounts were unaudited at this stage and would be subject to modification following discussions with the external auditors. Mr Lamond indicated that he would provide a summary of the accounts and then David Christie, Service Manager – Business Finance, would provide a more detailed look at some of the key statements.

Mr Lamond began by briefly explaining the layout of the accounts and highlighting the significant changes from previous years. He summarised the key results for the year noting that there had been favourable movement in the use of reserves with an overall decrease of £3.608 million during 2013/14, this was less than anticipated. Service Expenditure had largely been as forecast at the Q3 reporting stage but there had been a significant underspend on debt charges due to significantly lower than planned capital expenditure and high performing Loans Fund pool rates.

Drawing attention to the Council's Statutory Trading Operations (STOs), Mr Lamond explained that 2 out of the 3 had met their targets for 2013/14 and, following a report by Internal Audit, a review of STOs was planned for the coming year. He also pointed out that borrowing had increased by 7.7% over the year, recognising the Council was still operating in an under-borrowed position, and that the overall Capital spend figure was £45.6 million.

Mr Christie provided a more detailed look through the accounts, focusing on several key areas:

Movement in Reserves – showed a reduction in the general fund and housing revenue fund balances and an overall decrease in usable reserves of £3.6 million.

Balance Sheet – an increase in the valuation of Council dwellings had resulted in an overall increase in the value of assets. The increase in debtors was due in part to the timing of payments and mainly related to VAT and non-domestic rates payments. There were no long term issues with debtors.

Capital Finance – the total capital spend of £45.6 million was funded through capital grants (£13.2m), other receipts (£2.6m), direct revenue contributions (£1.7m) and loans fund (£28.4m).

Debtors and Provisions – the amounts owed by central Government and NHS bodies had reduced, however monies owed by other organisations and individuals, some of long standing, had increased.

Borrowing – the Public Works Loan Board accounted for the majority of loans. The figures included the loan repayment profile showing the split between long and short term borrowing.

Housing Revenue Account – although the revenue reserves had decreased by £64,000, it was noted that the HRA had capital reserves of almost £2.6 million.

Common Good Funds – there had been no material movement in overall fund levels during 2013/14. However, attention was drawn to the difference in individual fund balances.

Mr Christie ended by summarising the financial reporting timetable confirming that the audited Statement of Accounts would hopefully be signed off by the end of September. Mr Lamond concluded that these financial results showed a continuing reduction in reliance placed upon the use of reserves and pointed to the success of the financial strategy which placed the Council in a stronger position to meet future fiscal challenges.

The Convenor thanked Mr Lamond and Mr Christie for their helpful overview and invited questions from Members.

Councillor Currie asked how much of the reduction in Capital spending was due to financial planning and how much as a result of cancelled or delayed projects. Mr Lamond explained that previous financial planning had had an impact in the reduction of loan charges. As far as individual capital projects were concerned, it was hard to give an exact figure but he acknowledged that some slippage in any capital programme was inevitable. He agreed to provide further information to Councillor Currie.

In response to questions on Housing Revenue Account, Mr Lamond advised that £20 million of new expenditure had increased the level of debt but the plan remained to keep overall housing debt repayments below 40% of turnover. He pointed out that the underspend of around £4.5 million on the HRA capital budget was not due to any deliberate suppression of spending but rather natural slippage on a number of delayed projects. The Chief Executive, Angela Leitch, concurred; reminding Members that the delivery of affordable housing remained a key priority for the Council.

In relation to the continuation of the council tax freeze, Mr Lamond indicated that this was subject to annual settlements and he could not predict with any certainty what either the Council or the Scottish Government would decide to do in coming years.

Mr Lamond and Mr Christie answered a number of questions from Members on borrowing. They explained that the trend for short term borrowing had increased during the past 2 – 3 years to take advantage of very low short term interest rates. Although this provided some immediate economic gain it was not sustainable in the longer term and therefore this strategy would be kept under constant review. Borrowing was used for a variety of purposes including managing cash flow, funding of capital investment and refinancing of existing loans. The current rate of borrowing was likely to continue in the short term and Mr Lamond indicated that further detail was provided in the Treasury Management Review report to be discussed later on the agenda.

Councillor Currie asked whether the Council would be liable for any debts incurred by the Musselburgh Joint Racing Committee. Mr Lamond confirmed that within the terms of the Minute of Agreement, the Council could potentially become liable for any financial losses incurred by the Joint Racing Committee. The Councillor also asked about the potential borrowing power of Common Good Committees. Mr Lamond was

unsure whether or not Common Goods had the power to borrow but agreed to research this matter and provide any relevant information.

Councillor Caldwell asked about the impact of the Voluntary Early Release scheme (VERs) on the Council's pension liability. The Depute Chief Executive (Resources and People Services), Alex McCrorie, advised that the pension funds were performing well and that there had been no increase in employee contributions as a result of VERs.

Decision

The Committee noted the report.

3. ANNUAL TREASURY MANAGEMENT REVIEW 2013/14

A report was presented by the Depute Chief Executive (Resources and People Services) to provide the Committee with an update on Treasury Management activity during 2013/14.

Mr Lamond commended the report as a relevant and useful complementary addition to the Audit & Governance Committee's consideration of the draft Statement of Accounts. He indicated that the Council was required by the CIPFA Code of Practice to produce an annual treasury management review of activity and that this report followed on from the annual Treasury Strategy prepared in February 2013 and the mid-year review presented to this Committee in November 2013. He drew Members attention to the overall treasury and borrowing positions as outlined, and the details of borrowing rates and outturn for 2013/14.

Mr Lamond and Kirsten Maguire, Service Manager – Corporate Finance, responded to questions from Members on the impact of fluctuations in borrowing rates and whether current low rates should encourage the Council to increase borrowing for capital projects. Ms Maguire reassured Members that the majority of loans were fixed rate and any rate changes would apply to new borrowing rather than existing loans. Mr Lamond added that the Council's debt portfolio contained a range of rates and repayment periods which allowed for a degree of stability when dealing with fluctuating interest rates. Mr McCrorie advised Members that the Council could not borrow in advance of need and that, at present, it was better value to use short term borrowing to repay longer term, higher rate loans. Mr Lamond suggested that it may be of benefit for his team to provide additional information to Members on this aspect of treasury management and that this would be taken into account when finalising a briefing to members that was proposed for later in the calendar year.

In response to questions on the role of CAPITA, Ms Maguire confirmed that they had been appointed to provide treasury management advice following a comprehensive procurement exercise in 2013. She pointed out that CAPITA acted as advisers to several other local authorities and that East Lothian Council had benefited from their additional experience, support and sharing of good practice.

Decision

The Committee noted the report.

Signed   ....
                  Councillor Kenny McLeod
                  Convener of the Audit and Governance Committee

KPMG

cutting through complexity

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East Lothian Council

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

Audit: year ended 31 March 2014

DRAFT: 1 September 2014

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The contacts at KPMG in connection with this report are:

Andy Shaw
Director, KPMG LLP

Tel: 0131 527 6673
Fax: 0131 527 6666
andrew.shaw@kpmg.co.uk

Michael Wilkie
Senior Manager, KPMG LLP

Tel: 0141 300 5890
Fax: 0141 204 1584
michael.wilkie@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 the East Lothian Council ('the Council') and is made available to Audit Scotland and the Controller of Audit (together 'the beneficiaries'), and 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 circumstances set out in the executive summary: scope and objectives.

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.

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This annual audit report summarises our findings in relation to the audit for the year ended 31 March 2014. Our audit work is undertaken in accordance with Audit Scotland's *Code of Audit Practice* ('the Code').

This report also sets out those matters specified by ISA (UK and Ireland) 260: *Communication with those charged with governance* in relation to the financial statements for the year ended 31 March 2014.

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

Area	Summary observations	Analysis
Strategic overview and use of resources		
Key issues and challenges	There are a number of service challenges emerging, with demand and resource pressures growing against a backdrop of reform in public services. Management undertake regular analysis of the key areas of public reform, which should support achievement of strategic priorities in a changing environment.	Pages 6-7
Financial position	The Council recorded a statutory deficit of £3.6 million in 2013-14 (2012-13: £2.5 million), £2.6 million lower than the budgeted statutory deficit. This gave rise to a decrease in the general fund reserves of £2.7 million and housing revenue account and capital fund reserves of £0.9 million. Of this decrease, £3.6 million related to the utilisation of the cost reduction fund, primarily to cover the in year costs of the voluntary early release scheme (VERS). There was a £0.6 million increase in general service funds, including earmarked reserves. £2.9 million of remaining non-earmarked general fund reserves was allocated to the general services capital fund, which will be used to directly fund future capital expenditure to reduce the need for further borrowing. The capital underspend has led to lower than budgeted borrowing requirement and consequently a reduced interest cost than budgeted. Short term borrowing has significantly increased (£20 million) in contrast to the smaller increase in long term borrowing (£4.8 million). The key driver is in respect of taking advantage of competitive interest rates on short term borrowing; decreasing the short term interest costs.	Pages 8 – 11
Financial planning	The 2014-15 budget forecasts a breakeven position, after a further £0.2 million utilisation of reserves. The Council is planning to utilise most usable un-earmarked general reserves by 31 March 2016. In 2016-17 the Council is budgeting a break-even position.	Pages 12-13
Financial statements and accounting		
Audit conclusions	We have issued unqualified audit opinions on the 2013-14 financial statements, following their approval in September 2014. An emphasis of matter paragraph is included in our audit opinion with respect to the facilities management significant trading operation not meeting the statutory requirement to break even on a three year rolling basis. The financial statements, foreword, governance statement and remuneration report were received by the start of audit fieldwork. There are opportunities for further improvement in the financial statement process to achieve sector leading practice.	Pages 15, 23
Significant risks and audit focus areas	We have considered inherent significant risks that the ISAs would require us to raise with you covering risks in relation to revenue recognition and management override of controls and have satisfactorily concluded our work in these areas. Other significant risks and other areas of audit focus have been considered and satisfactorily concluded.	Pages 16 - 21
Accounting policies	There are no substantial changes in accounting policies compared to the prior year. The Council applied IAS 19 (revised) and we concur with the decision to not restate prior year comparatives, due to the immaterial nature of the adjustment. No newly effective accounting standards are expected to have a material impact on next year's financial statements. The financial statements have been appropriately prepared on a going concern basis.	Page 22

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Governance and narrative reporting		
Governance arrangements	Over-arching and supporting corporate governance arrangements provide a sound framework for organisational decision-making. Risk management practices have been considered throughout the year, and the whistle blowing policy updated. Weaknesses were noted in the remuneration report and in procurement procedures.	Pages 25 – 29
Control observations	Our testing of the design and operation of financial controls over significant risk points confirms that generally controls relating to financial systems and procedures are designed appropriately and operating effectively. In our interim management report we noted opportunities for management to further strength the control environment in relation to council wide policies, bank reconciliations and journals. We have identified eight recommendations in the action plan in this report at appendix five. These relate to accounts preparation, accounting for property, plant and equipment, provisions and bank accounts.	Page 29
Performance management arrangements		
Performance management	The Council has developed Best Value and performance management arrangements further during the year and demonstrates commitment to continuous improvement. The Council monitors statutory performance indicators throughout the year and completes the Local Government Benchmarking Framework exercise. The Accounts Commission report on public performance reporting highlighted many areas of good practice and management are considering the identified areas for improvement, particularly in respect of procurement.	Pages 31 – 33
National reports	In response to the Audit Scotland national study *Health Inequalities in Scotland*, the East Lothian Partnership is developing a health inequalities strategy. Audit Scotland's *Major Capital Investment in Councils* and *Arms Length External Organisations: Are you getting it right?* reports have been considered by the audit and governance committee. Good progress has been made against the action plan for capital investment, however no action plan was prepared in response to the latter report.	Page 32

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Our annual audit report is designed to summarise our opinion and conclusions on significant issues arising from our audit of the Council's financial statements for 2013-14. It is addressed to both those charged with governance at the Council and the Controller of Audit. The scope and nature of our audit were set out in our audit strategy document which was presented to the audit and governance committee at the outset of our audit.

The context of our audit is one of an overall reduced level of risk, based on the shared risk assessment of the Council's arrangements.

Responsibilities

Audit Scotland's Code of Audit Practice ('the Code') sets out the Council's responsibilities in respect of preparation of financial statements, systems of internal control, prevention and detection of fraud and irregularities, standards of conduct and arrangements for the prevention and detection of bribery and corruption, financial position and Best Value.

This report reflects our overall responsibility to carry out an audit in accordance with our statutory responsibilities under the Act and in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board and the Code.

The Code sets out the wider dimensions of public sector audit which involves not only the audit of the financial statements, but also consideration of areas such as financial performance and corporate governance.

An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. Weaknesses or risks identified are only those which have come to our attention during our audit work in accordance with the Code, and may not be all that exist. Communication of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised or to maintain an adequate system of control.

Under the requirements of International Standard on Auditing (UK and Ireland) ('ISA') 260 Communication with 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 members and our presentation to the audit committee, together with previous reports to that committee during the year, discharges the requirements of ISA 260.

Context of the audit

The Scottish Government's response to the Crerar report in 2007 was to simplify the approach to delivering local government scrutiny. As a result, scrutiny bodies that engage with local government established a shared assessment of the risks in each Council and developed a range of proportionate approaches in response to the risk assessment. A local area network ('LAN') of local audit and inspection representatives undertake a shared risk assessment for each local authority in Scotland, to identify targeted, risk-based scrutiny. Following a review of the shared risk assessment process in 2013, there has been a shift in focus to identifying the Council's position in implementing the Scottish Government's reform agenda.

This results in each council receiving an annual Assurance and Improvement Plan ('AIP'). During 2013-14, a refresh of the Council's AIP for the period 2014-17 was undertaken, which was subsequently published in June 2014. The change in focus from the review of the shared risk assessment process is reflected in the structure of the AIP.

The Council's AIP reported that there continued to be areas of strong performance and a number of improvement activities continue to make good progress. Inspection and audit work during 2013-14, including a joint inspection of services for children and young people in the East Lothian Community Planning Partnership area, resulted in broadly positive reports.

No areas were assessed as 'scrutiny required', one area as 'further information required' and the remaining 18 as 'no scrutiny required'. There is further activity planned as a follow up to the Children's Services inspection and a Scottish Housing Regulator performance inquiry on rent arrears management. This is an improvement on the 2013-16 AIP when two areas were identified as 'scrutiny required', 15 as 'further information required' and the remaining 21 as 'no scrutiny required', albeit there was a different focus and different areas assessed in the 2013-16 AIP.

Strategic overview and use of resources

Our perspective on the Council's approach to key issues affecting the local government sector, and its use of resources

There are a number of service challenges emerging, with demand and resource pressures continuing to build, against a backdrop of reform in public services.

Management undertake regular analysis of the key areas of public reform, which should support achievement of strategic priorities in a changing environment.

Sector overview

Audit Scotland's report An overview of local government in Scotland 2014 highlighted the challenges of reducing budgets and increasing demands. This is coupled with further expected budget reductions, the public's expectation of service delivery and demographics becoming more biased towards older people, who typically need more public services.

In previous years management prepared an analysis of the contents of the report, considering the Council's position against each report recommendation. This process was considered an example of best practice and completing the exercise for the 2014 report will allow management to identify opportunities for continuous improvement.

Quarterly reports to Cabinet or Council outline the financial position, forecast position and a financial risk assessment of the overall Council and individual departments. An underlying surplus on the general fund was achieved in 2013-14, excluding the costs of the voluntary early release scheme. Additional reserves have been earmarked to a general services capital fund to support the capital plan and alleviate the need for further additional borrowing. Continued monitoring against the financial strategy and planned use of reserves is needed to support achievement of financial sustainability.

Management undertakes regular analysis of the key areas of public reform, which should support achievement of strategic priorities in a changing environment.

A new Single Outcome Agreement ('SOA') has been developed by the Council and related partners. The SOA is an agreement between the East Lothian Partnership and the Scottish Government, setting out how each party will work to improve outcomes and reduce inequalities for East Lothian residents.

Integration of health and social care

In March 2014 the Public Bodies (Joint Working) (Scotland) Act was passed by the Scottish Government. This requires all Councils and NHS Boards to formally and legally establish integration of health and social care by April 2016. Detailed legislation and broader statutory guidance is being devised. Two sets of regulations have been released for consultation and management are writing responses.

The Council has agreed that in conjunction with NHS Lothian, the body corporate model should be adopted and the scheme of integration should be based on this model. A shadow board has been formed and has been meeting during the year. A jointly accountable officer took up post on 1 August 2013, working in adult wellbeing services with responsibility for NHS services in East Lothian. This position is jointly accountable to the chief executive of the Council and Lothian NHS Board. Management feel reasonably well placed to implement the changes but recognise the challenge of developing the integration plan.

Welfare reform

As a result of the Welfare Reform Act 2012, a number of significant changes were implemented on 1 April 2013, changing how councils deliver benefit services. Further reform will see 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).

The Council's welfare reform task group continues to consider the service implications. An action plan has been produced and a reference group, which meets quarterly, has facilitated liaison between council services, partners and stakeholders.

The Scottish Government's council tax reduction scheme came into force from 1 April 2013. There is little or no change financially to recipients and therefore this has had a low financial impact on the Council. Funding will remain the same in 2014-15, however there is greater financial risk due to the an increase in the number of properties in the Council boundaries as the funding is a fixed sum instead of being demand led.

The housing benefit under occupancy supplement was introduced on 1 April 2013, although mitigated by the payment of discretionary housing payments. The welfare cap was implemented from 15 July 2013, with the Council identifying that 18 households were affected. Continued monitoring of the welfare reform changes will ensure that the council is able to respond in an agile manner and ensure it continues to support its most vulnerable constituents.

The benefits team have been administering the two year interim Scottish welfare fund since 1 April 2013 which covers crisis grants and community care grants. The government has confirmed this will become a permanent scheme from April 2015. The Council achieved 100% disbursement of its share of the Scottish welfare fund, and will receive the same budget in 2014-15. The additional work involved has led to a 26% rise in caseload. Management are developing a Scottish welfare fund policy to support administration of the fund within an East Lothian context.

Workforce planning

A voluntary early release scheme was approved by Cabinet on 12 March 2013. 96 members of staff were approved on the basis that their departure would not adversely impact upon services and that they satisfied certain financial criteria. Of these, 94 left the Council in 2013-14 and the remaining two had left by August 2014.

Management analysis in May 2014 identified savings of £2.9 million has been secured against a £3 million budget. Further savings of £1.5 million have been secured from the ongoing workforce management

plan secured from the ongoing workforce management plan against a budget of £1.8 million, which relate to the outcomes of service reviews and tighter management of casual workers, overtime and agency workers.

Management recognises that it is not yet possible to fully assess the impact on service delivery, although feedback has indicated that workloads remain challenging, coupled with an inherent loss of tacit knowledge. A staff engagement survey was undertaken in March 2014; management is analysing the results of this process, with initial results indicating the level of participation and positive engagement remaining consistent with previous surveys. The results have also been fed into the How Good Is Our Council ('HGIOC') process to identify areas of concern and inform the development of improvement plans.

Efficiency savings and change projects

To ensure the Council is best placed to mitigate the changing service requirements and reducing funding a number of change projects have been implemented.

Each change project is listed within the Rivo software and assigned to a department and responsible officer. Alongside this information the start and expected completion date are documented. Reminders are sent to the responsible officer on a quarterly basis to ensure progress is noted. Quarterly progress reports will then be produced with RAG ratings against each projects likely achievement of the expected completion date.

The 2014 – 2017 budget requires efficiency savings to be achieved to deliver a balanced budget. Each efficiency saving has also been assigned to a responsible officer in Rivo detailing the expected efficiency saving or increased income. Achievement of these savings will be monitored through quarterly reports to the chief executive. Internal audit are facilitating the implementation and monitoring of the reports.

The Council recorded a statutory deficit of £3.6 million in 2013-14 (2012-13: £2.5 million), including £3.6 million in respect of VERS from the cost reduction fund.

The budgeted use of reserves was £5.2 million, including £3 million in respect of the cost reduction fund.

Financial position

The Council recorded a statutory deficit of £3.6 million in 2012-13 (2012-13: £2.5 million). This resulted in a decrease in the general fund and insurance fund reserves of £2.7 million and in the housing revenue account and capital fund reserves of £0.9 million.

Use of reserves – general fund

A three-year budget was approved on 12 February 2013, which assumed a £5.2 million utilisation of reserves in 2013-14. Management's forecast, prepared in quarter three, projected a reduced utilisation of £4.9 million. The final outturn utilisation was £3 million (2012-13: £1.4 million), representing 25% of opening useable reserves (2012-13: 11%). In line with the Council's financial strategy, the lower than budgeted utilisation has been earmarked in a new general services capital fund within the general fund.

The key changes in the general fund against budget are illustrated in the table below.

£m	Budgeted utilisation of reserves	Actual utilisation of reserves
General fund[a]	2.2	(0.6)
Cost reduction fund	3.0	3.6
Total	**5.2**	**3.0**

Note: (a) Includes actual utilisation £0.2 million of earmarked reserves; excludes insurance fund.
Source: East Lothian Council.

£2.9 million of remaining non-earmarked general fund reserves has been allocated to the general services capital fund which will be used to directly fund future capital expenditure to reduce the need for further borrowing.

The cost of VERS is accounted within the utilisation of the cost reduction fund. The outturn of each budget against utilisation of reserves is reconciled in the table below.

General fund budget	
	£m
Budgeted use of reserves	**2.2**
Resources and people services	(0.8)
Health and adult care partnership	0.5
Partnerships and services for communities	(2.5)
Actual utilisation of reserves	**(0.6)**

The key variance to budget within resources and people services relates to the receipt of windfall income relating to the PPP contract of £0.7 million in the secondary school budget. Within partnerships and services for communities the key budget movements are:

■ underspends within the community housing group and surpluses produced by the property services trading activity; and

■ underspends in landscape and countryside management (£0.8 million) due to non-recruitment to vacant posts.

As in previous years there is an underspend against budget, and there is an inherent risk that this could impact on service delivery. Management monitors the budget throughout the year, although as identified in previous years, the majority of underspend is presented in the final quarter of the financial year.

Management presented the salient features of the financial statements to the audit and governance committee in July 2014. This facilitated an early discussion by members of the financial position reflected within the unaudited financial statements. We consider this to be an example of good practice in the governance of council resources.

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The outturn on the housing revenue account is a deficit of £1.9 million. Following adjustments between the accounting basis and funding basis and transfers between reserves, the decrease in the year was £0.1 million.

Housing revenue account ('HRA')

The outturn on the HRA is a deficit of £1.9 million. After making adjustments between the accounting basis and funding basis under statute (credit of £2.9 million) and recognising a transfer from the capital fund (£1.1 million), netted against a transfer (£1 million) to the general fund, the decrease in the year was £0.1 million. The carry forward balance at 31 March 2014 is £2 million. The use of reserve including the housing capital fund in 2013-14 is £0.9 million, against a budget of £0.9 million.

Rental income was below budget, reflecting delayed delivery of affordable homes. Repair costs were £0.4 million more than budgeted, of which half relates to costs for repairing fire damage. Further repair costs were in relation to bringing some of the open market acquisition and mortgage to rent properties to the appropriate standard.

These costs are net against compensating variations in the budget including debt charges being £1.2 million under budget.

Composition of reserves

As at 31 March 2014, the Council had usable reserves of £15.3 million. These consisted of the general fund (£9.2 million), the housing revenue account (£2 million), the housing capital fund (£2.6 million) and the insurance fund (£1.5 million). The housing capital fund is used to fund capital expenditure within the housing revenue account. The funds are illustrated in the diagram opposite.

In benchmarking undertaken by Audit Scotland from analysis of the 2013-14 unaudited financial statements of Scotland's 32 local authorities, the Council's decrease in usable reserves is the tenth highest, clearly impacted by utilisation of the cost reduction fund. More than half of all councils utilised usable reserves in 2013-14.
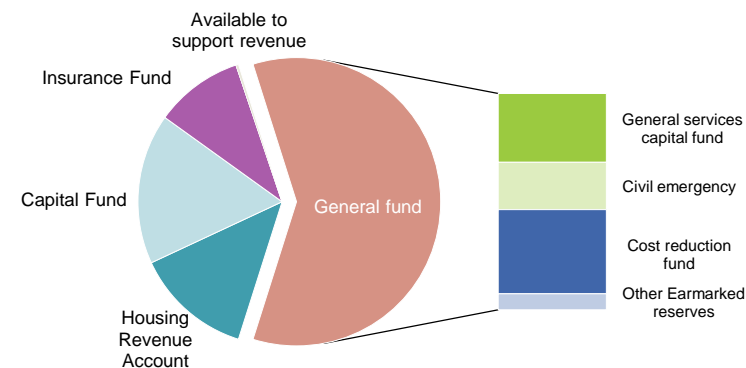
Source: East Lothian Council

The Council has the third lowest amount of usable revenue reserves as a percentage of net revenue stream plus dwelling rents (2012-13: fifth lowest). Regular financial monitoring performed by management, against budgets which include limited utilisation of reserves, will continue to improve the financial position.

HRA dwelling rents per council dwelling is the second lowest in Scotland, indicating that rental charges for residents continue to be lower than the majority of Councils. The Council had the highest level of gross rent arrears as a proportion of dwelling rents in Scotland. We have considered the overall profile of Council debtor balances and related provisions at page 21.

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Total capital expenditure in 2013-14 was £45.6 million, below the approved capital plan of £58 million. This level of capital investment represented a 13% decrease over 2012-13 levels and reflects the lower limits approved in October 2012.

Capital programme

Total capital expenditure in 2013-14 was £45.6 million, below the original revised capital plan of £58 million. This level of capital investment represented a 13% (£6.6 million) decrease from 2012-13. The table below provides analysis across general services and the housing revenue account, comparing actual capital expenditure to budget and the prior year.

£m			
	Total	**HRA**	**General services**
2013-14 budget	58.0	25.6	32.4
2013-14 actual spend	45.6	20.8	24.8
(Under)/overspend	**(12.4)**	**(4.8)**	**(7.6)**
Financed by			
Grant	12.5		
Asset sales	1.6		
Other receipts	3.6		
Borrowing	27.9		
Total	**45.6**		

Source: East Lothian Council.

In respect of the housing revenue account the largest element of the capital under spend (£4.8 million) was in relation to extensions, roughcasting and building envelope works.

Actual capital expenditure on general services was £24.8 million and the largest projects are shown opposite, including significant HRA projects. The outturn was an under spend of £7.6 million against budget.

The largest underspends were in relation to replacement vehicles (£1.7 million), coastal car parks and toilets (£0.7 million), support for business - land Acquisition, infrastructure and broadband (£0.5 million) and reprovision of pathways home (£0.5 million).

A significant amount of the capital underspend is due to slippage and therefore could affect future years capital budgets, albeit management apply the capital limits flexibly over the rolling five year period. A refreshed capital plan will be presented as part of the ongoing quarterly monitoring reports in 2014-15. Initial changes to the capital plan were presented to the Council in April 2014 which advised of changes to six projects.

Summary of key capital projects: 2013-14

£m	
Project	**Expenditure**
Modernisation (HRA)	10.9
Affordable housing	9.9
Tranent care centre	7.2
Roads	5.7
Gullane medical centre	2.7
House purchases	2.1

Source: East Lothian Council analysis.

The lower capital limits approved in October 2012 gave rise to lower than budgeted borrowing requirement and consequently a reduced interest cost.

The Council's level of debt places significant pressure on future revenue funding as debt and associated interest is paid. Robust monitoring will continue to be required.

Borrowing

The Council's capital expenditure is largely funded through borrowing, which inherently increases the level of indebtedness which the Council must repay, with interest, from future revenue budgets. East Lothian has one of the fastest growing populations in Scotland and this gives rise to higher demand for investment in new and refurbished service facilities, such as schools and a growing need for affordable housing.

The additional in year borrowing of £24.8 million was lower than that of the previous year of £30.7 million. This is due to the impact of increased capital grants and project income. The table below shows the split between HRA and general services capital expenditure and borrowing in 2013-14.

Sources of funding	HRA £m		General Services £m	
	Budget	*Actual*	*Budget*	*Actual*
Borrowing	18.8	14.5	18.7	13.4
Grants	5.7	5.5	7.0	7.0
Project income	-	-	4.6	2.8
Asset sales	1.1	0.8	1.4	0.8
Developer contrib.	-	-	0.7	0.8
Total	**25.6**	**20.8**	**32.4**	**24.8**

Source: East Lothian Council.

The proportion of capital expenditure funded from borrowing is higher for HRA projects (70%) than general services projects (54%). Management expects borrowing for HRA projects to be fully repaid from associated rental income generated.

The capital underspend has led to lower than budgeted borrowing requirement and consequently a reduced interest cost than budgeted. Short term borrowing has significantly increased (£20 million) in contrast to the smaller increase in long term borrowing (£4.8 million).

The key driver has been in taking advantage of competitive interest rates available on short term borrowing, therefore decreasing the short term interest costs.

Whilst interest rates have been at a historical low over the past years, inevitably these will increase. Increases to interest rates will only affect new borrowing or variable rate loans, instead of existing fixed rate loans which accounts for a significant proportion of the Council's borrowing portfolio.

The Council is forecasting a slower increase in debt repayments over the next two years. In 2016-17 debt repayments will increase faster than in prior years. These will be paid from the general services and housing revenue account budgets and have been included in the next three years' budgets. The Council's level of debt places pressure on future available revenue funding as debt and associated interest is repaid. There are further risks is capital expenditure is deferred and associated borrowing is taken out at higher interest rates, potentially leading to larger debt charges.

In benchmarking undertaken by Audit Scotland from analysis of the 2013-14 unaudited financial statements of Scotland's 32 local authorities, the Council continues to have the highest level of net external debt when taken as a proportion of revenue expenditure (166%; 2012-13:171%) and second highest per head of population (£3,930 per head; 2012-13: £3,700). However it is recognised that this benchmarking does not differentiate between demographic differences or the split between general services and housing related borrowing.

The Council has the eighth (2012-13: fifth) highest level of debt as a proportion of fixed assets, with a ratio of 0.6 (2012-13: 0.5). Borrowing continues to rise to fund the Council's capital programme, although the active reduction in capital expenditure limits to support no new borrowing from 2014-15 should support a longer term decrease in borrowing levels.

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The 2014-15 budget forecasts a breakeven position, incorporating a further £0.2 million utilisation of reserves.

Lower staff costs as a result of VERS will facilitate achievement of the budget.

Background

Local government finance settlements have been agreed for 2014-15 and 2015-16. The table below shows the profile of revenue and capital grants over this period.

£m		
	Revenue allocation	**Capital grant funding**
2013-14	166.4	7.5
2014-15	163.6	10.8
2015-16	164.3	11.6

Source: Scottish Government website

Revenue budget

A three year revenue budget was approved by council in February 2014. This used the 2013-14 budget as a base and reflected changes for known items of income and expenditure in future years. The 2014-15 budget forecasts a breakeven position, incorporating a further £0.2 million utilisation of reserves.

This budget has been set on the assumption that council tax will remain frozen in 2014-15. The main changes over the period to 2016-17, by service, are summarised below. The changes are incorporated in the approved budgets and comprise of both known changes and agreed efficiency savings/measures.

2016-17 will be the first year when reserves are not forecast to be utilised to meet recurring expenditure. The reallocation of savings from VERS represents the largest movement within corporate commitments in 2014-15 (£2 million reallocated to departments) and increased debt charges (£0.3 million increase). Corporate income is expected to increase in 2014-15 due to forecast increases in revenue support grant budgeted in 2014-15. The main expenditure savings will be in partnership and community services, with total savings of 5.3% required to achieve budget, with the majority of these savings in 2014-15 from the removal of costs relating to staff who left through VERS.

£000					
Department	**Budget 2013-14**	**Changes 2014-15**	**Changes 2015-16**	**Changes 2016-17**	**Cumulative 2017**
Resources and people services	102,520	124	346	1,944	104,934
Health and social care partnership	44,839	(444)	(1,069)	4	43,330
Partnership and community services	48,455	(1,775)	(220)	(572)	45,888
Net expenditure	**195,813**	**(2,095)**	**(943)**	**1,376**	**194,152**
Corporate income	(215,552)	(2,572)	(551)	(571)	(219,245)
Transfer to/(from) reserves	(2,236)	2,406	1,438	(1,608)	-
Corporate commitments	21,975	2,260	56	803	25,093
(Surplus)/deficit	**-**	**-**	**-**	**-**	**-**

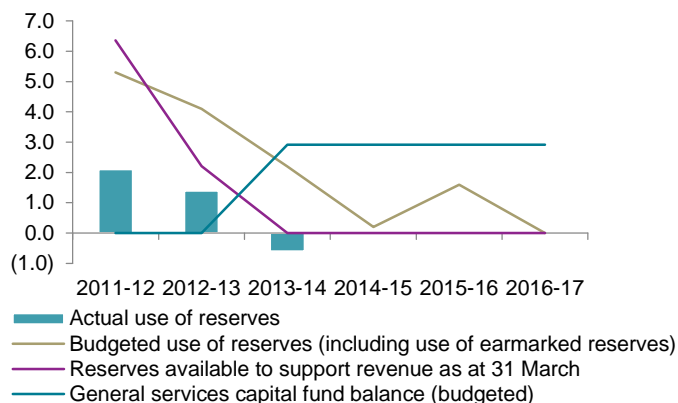Source: East Lothian Council budget.

The Council is planning to utilise most useable un-earmarked general reserves by 31 March 2016. In 2016-17 the Council is budgeting a break-even position.

Capital expenditure limits have been set to limit additional borrowing after 2013-14. The capital programme will require ongoing monitoring and review to ensure it continues to meet the financial strategy.

Use of reserves

The Council is planning to utilise most usable un-earmarked general reserves by 31 March 2016. In 2016-17 the Council is budgeting a break-even position. While reserves are not planned to be required in 2016-17, there is risk for the Council in requiring it to achieve budget in each of the next two financial years to achieve a recurring financial balance from 2016-17.

The chart below illustrates the use of reserves over a six year period, in accordance with the approved council budget for 2014-15 to 2016-17, against reserves available.

■ Actual use of reserves
— Budgeted use of reserves (including use of earmarked reserves)
— Reserves available to support revenue as at 31 March
— General services capital fund balance (budgeted)

Source: : East Lothian Council budget.

While, as at 31 March 2014, management confirmed that the Council remains on track with its financial strategy, continued monitoring will be required to ensure savings are achieved. Quarterly reports tracking progress with efficiency savings will help to support management in this task.

Cost reduction fund

The Council's cost reduction fund was £7.1 million as at 1 April 2013, being available to cover the cost of further service reviews and other potential efficiency savings. £3.6 million was utilised from this fund in 2013-14, primarily to fund the cost of VERS. As at 31 March 2014, £3.7 million remains earmarked as the cost reduction fund. A clear strategy and allocation of this fund will be needed to best utilise these reserves to support ongoing change projects.

Capital expenditure

Under statutory regulation the Council sets an annual limit on the maximum amount to allocate to capital expenditure. The financial strategy's capital limits, as set out below, seek to limit additional borrowing after 2013-14.

£m		
Year	Capital expenditure limits	Capital projects budget
2013-14 (actual)	33.0	24.8
2014-15	21.0	23.2
2015-16	21.0	21.1
2016-17	21.0	18.4
Totals	**96.0**	**87.5**

The cumulative budget over the four year period is within the cumulative capital limit. Management recognise the need for limits to be applied flexibly to incorporate project slippage, inter-year transfers and additional capital income. Elimination of additional borrowing, leading to reduced debt costs will support management's achievement of a sustainable financial position. Initial changes to the capital plan were presented to the Council in April 2014 which advised of changes to six projects.

Financial statements and accounting

Our perspective on the preparation of the financial statements and key accounting judgements made by management

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We have issued an unqualified audit opinion on the financial statements.

Audit conclusions

Our audit work is substantially complete pending receipt of management's representations and update of subsequent events. We have issued an unqualified opinion on the truth and fairness of the state of the Council's affairs as at 31 March 2014, and of the Council's deficit for the year then ended. An emphasis of matter paragraph is included within our audit opinion in respect of the facilities service significant trading operation not meeting the statutory target to break even over a three year rolling period as set out on page 22. There are no other matters identified on which we are required to report by exception.

In gathering the evidence for our opinion we have:

- performed a mixture of substantive and controls testing to ensure an efficient approach that covers all the key risks;

- liaised with internal audit and reviewed their reports to ensure all key risk areas having a potential financial statements impact have been considered;

- reviewed assumptions and judgements made by management and considered these for appropriateness;

- considered if the financial statements may be affected by fraud through discussions with senior management and internal audit to gain a better understanding of their work in relation to prevention and detection of fraud with the potential to impact on the financial statements; and

- attended the audit and governance committee to communicate our findings to those charged with governance, but also to update our understanding of the key governance processes and obtain key stakeholder insights.

Materiality

Planning materiality was provided in the audit strategy and plan 2013-14 dated 9 January 2014. We revised materiality prior to the commencement of the final audit, following updated internal sector guidance and receipt of the financial statements. Materiality has been set at £5.76 million (previously £9 million) which is approximately 2% of total expenditure in 2013-14. We have design our procedures to detect errors at a lower level of precision, i.e. £4.3 million. We report identified errors greater than £288,000 to the audit and governance committee.

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The main audit focus areas are discussed on the following pages.

These were identified in the audit strategy and plan and are significant risks in respect of:

- **management override of controls;**
- **revenue recognition fraud risk;**
- **the Council's financial position; and**
- **valuation of council dwellings;**

and other focus areas of:

- **employee benefits;**

during the audit we also identified further focus areas of:

- **accounting for depreciation;**
- **significant trading operations; and**
- **provisions.**

Significant risks that ISAs require us to raise in all cases

Professional standards require us to consider two specific risks for all organisations:

- management override of controls; and
- fraudulent revenue recognition.

Our audit approach to address these was set out in our audit plan and strategy. We do not consider fraudulent revenue recognition to be a significant risk for the Council as there are limited incentives and opportunities to manipulate the way income is recognised given the nature of grant funding. We therefore rebut this risk and did not incorporate specific work into our audit plan in this area over and above our standard fraud procedures. Although we do not consider the presumed risk of fraud from revenue recognition to be applicable, we remained alert to indications of fraud during the course of the audit.

As part of our work to address the significant risk of management override of controls we performed the following tests:

- testing of journals at the year end, and during the year;
- review of unusual transactions in the year;
- enquiries with employees outside the finance department;
- a test of unpredictability; and
- controls testing, including higher level controls.

We do not have any findings to bring to your attention in relation to these matters. No control overrides were identified.

Other areas of audit focus

Our audit strategy and plan included the following other significant risks:

- the Council's financial position, including revenue and capital and the impact on borrowing which we have considered in the strategic overview; and
- valuation of council dwellings;

and other areas of audit focus we have reported on other matters related to:

- accounting for the Council's participation in the Lothian Pension Fund;
- accounting for depreciation on enhancements to existing assets;
- significant trading operations; and
- provisions.

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We have considered key accounting issues, in relation to valuation of property, plant and equipment.

We concur with management's judgements regarding the valuation of property, plant and equipment.

Key accounting judgements	
Area	**KPMG comment**
Valuation of property, plant and equipment	■ Under the Council's rolling basis of revaluations, Council dwellings were revalued as at 31 March 2014, using the Beacon approach (adjusted vacant possession). The revaluation has increased the value of Council dwellings by £5.6 million. Our audit of the accounting for the revaluation includes evaluation of the valuer as a third party expert and consideration of the data underlying the valuation report. We found that the valuer as a third party expert was objective and had the appropriate experience and expertise to provide the information for use by the Council. Our testing included review of actual data against that used in the valuation report. No issues were identified. The valuer uses a number of assumptions in its calculations based on market conditions at the year end. Using our own internal valuation specialist reviewed the methodology and assumptions used. There were no issues identified from this review. We reviewed the revaluation adjustments processed in the financial statements and identified that these had been appropriately recognised and disclosed. ■ As in previous years Council dwellings are recognised as a single line item, by road or area, in the fixed asset register with total annual enhancements recognised as separate assets. It was not possible for management to specifically allocate the valuation based on this recognition in the fixed asset register. As at 31 March 2014, management elected to recognise council dwellings as a single line item in the fixed asset register, and additions and enhancements to council dwellings will be recognised on this one line. This does not enable componentisation of assets. Management are undertaking a review of the fixed asset register to ensure appropriate data is held on individual council dwelling assets. The current fixed asset register treatment also does not enable management to remove the relevant component on disposal or replacement in future years. There is a further risk to the depreciation calculation as individual assets and components useful lives cannot efficiently be applied to accurately calculate the depreciation amount for 2014-15. *Recommendation one* ■ Improvements were made to the annual impairment review process in 2012-13, with management putting in place an effective consultation procedure within the Council. Due to staffing changes there were difficulties in receiving all manager reviews on a timely basis and the review was still on an informal basis. There is opportunity to further enhance the impairment review by tracking all manager reviews, potential impairments identified and conclusions in an overall document. We suggested to management that the review could be performed as at 28 February, thereby providing greater time for consideration and implementation of impairments. No impairments were identified in 2013-14. *Recommendation two*

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In respect of employee benefits, each of the assumptions used to value the Council's net pension deficit are within an acceptable range of KPMG's expectations.

We are of the view that this therefore represents a reasonable and balanced approach, in accordance with the requirements of IAS 19.

Other accounting and audit matters	
Area	**KPMG comment**
Employee benefits valuation	The Council accounts for its participation in the Lothian Pension Fund in accordance with IAS 19: *Employee benefits* on a defined benefits basis using valuation information prepared by actuarial consultants. Our audit of the accounting for employee benefits includes evaluation of the actuarial consultants as a third party expert, consideration of the data underlying the actuarial report, including the level of contributions made during the year, the financial assumptions and membership data provided to the actuary by the Council, and estimates of the Council's share of the pension fund assets.
	We found that the actuarial consultants as a third party expert was objective and had the appropriate experience and expertise to provide the information for use by the Council. The level of contributions made in the year is estimated based on data prior to the year end. It is important that this number is accurate as it is used to inform the calculation of the liabilities at the period end. Our testing included review of actual data against that used in the actuarial calculations. No issues were identified. The actuaries use a number of assumptions in their calculations based on market conditions at the year end, including a discount rate to derive the anticipated future liabilities back to the period end date and assumptions on future salary increases. Using our own actuarial specialists, we reviewed the assumptions and concluded that the overall assumptions proposed represented a balanced position for the net deficit within our expected range. Further information is given in Appendix four.
	The Council has appropriately applied IAS 19 *(revised)* in the financial statements. If the standard had been adopted early in 2012-13, the estimated change to finance costs would be £2.9 million. We do not consider this to be a material amount and therefore agree with management's decision not to restate the prior year comparatives. There would be no impact on the prior year net assets position if the Council had restated the prior year comparatives. An audit adjustment of £5.1 million was processed to correct the accounting for the return on plan assets, which had been incorrectly recognised in other comprehensive income and expenditure instead of financing and investment income and expenditure.

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We have considered key accounting issues, in relation to depreciation on additions to existing assets.

We have raised a recommendation to review the depreciation policy.

Other accounting and audit matters	
Area	**KPMG comment**
Depreciation	In a previous year, we reported that depreciation on additions to existing assets is calculated using the method set out below and illustrated in the diagram. This method gives rise to immaterial differences to a depreciation charge we would expect, although may give rise to larger errors in the future.

1. Depreciation on the cost or valuation of an existing asset is applied, based on its useful economic life and calculated on a daily basis from 1 April to 1 October.

2. The net book value ('NBV') of the existing asset is calculated as at 1 October, being the opening NBV less the depreciation calculated above.

3. The cost of any additions is added to this 'enhanced' carrying value, to provide a depreciable value of the asset.

4. The depreciable value of the asset is depreciated on a daily basis from 2 October to 31 March and added to the first six months of depreciation to give the depreciation charge for the year.

Existing asset brought forward with cost/valuation and accumulated depreciation

Carrying value (NBV) calculated on existing asset

Cost of additions/ enhancements added to existing asset NBV to give depreciable amount

Asset carried forward , carrying amount recognised on balance sheet as cost/valuation less total accumulated depreciation

1 April 2013   **1 October 2013**   **31 March 2014**

Depreciated calculated based on cost/valuation and useful economic life

Depreciation calculated based on depreciable amount of asset and useful economic life

We identified further focus areas in relation to depreciation and significant trading operations.

We have raised a recommendation to review the depreciation policy.

An emphasis of matter paragraph is included within our audit opinion in relation to the facilities services significant trading operation not meeting the statutory three year breakeven target.

Other accounting and audit matters	
Area	**KPMG comment**
Depreciation (cont.)	This method of calculating depreciation is unique amongst our client base. We analysed the depreciation charge on those assets where capital expenditure has been incurred and accounted for as an enhancement. We consider that depreciation is understated on council dwellings by £1.6 million however, due to the revaluation at year end, this understatement does not impact on the carrying value of these assets, since if processed it would simply increase the revaluation journals. For other property, plant and equipment, we consider depreciation to be understated by £0.5 million.
	An unadjusted audit difference has been presented on page 36. This would result in a net decrease to net assets of £0.5 million if adjusted.
	We recommend management reviews the current depreciation policy, and considers revising the current methodology. This should take account of how enhancements to council dwellings are recognised in the fixed asset register as there is a risk that the audit adjustment could become material in value.
	Recommendation three
Significant trading operations	■ The Council has three significant trading operations ('STOs'). The Local Government in Scotland Act 2003 requires that each STO breaks-even over a rolling three year period. The financial statements identify that facility services did not meet this statutory target and made a three year rolling deficit of £98,000 as at 31 March 2014. We reviewed the consistency of allocation of income and expenditure to each of the STOs, ensuring that no ineligible costs had been allocated to each STO. We recalculated the net surplus/deficit over the three year period. Property maintenance and roads services met this statutory target in 2013-14.
	■ An emphasis of matter paragraph is included in our audit opinion in relation to this matter. Management has identified that in the first quarter of 2014-15 facilities services has met the rolling three year break even target. Furthermore, management is investigating options to perform a review of STOs to ensure they best meet the Council's requirements.
	■ Non-material adjustments were required to the disclosed surplus for the year to ensure expenditure included was consistent with prior year disclosures. The narrative for facilities services was also updated to better reflect the three year cumulative position.

We identified further areas of audit focus in respect of provisions.

We have raised a recommendation to enhance the basis of the bad debt provision calculation.

Other accounting and audit matters	
Area	**KPMG comment**
Bad debt provision	■ The bad debt provision is calculated separately for council tax, housing rents, housing benefit and general bad debt. The council tax, housing rents and housing benefit provisions are calculated on a historic methodology, meaning they may not accurately reflect the bad debt the Council will face.
	■ Overall, the Council provides for 73.5% (2012-13: 66.3%) of gross debtors. We have reviewed the provision policy and compared to other authorities, we consider that council tax, rents and housing benefit provisions are prudent, although recognise that a policy of writing-off debtors or retaining the gross debtor with provision impacts on benchmarking analysis. Our view is that the calculation methods used should be revised to more accurately reflect debtor payment trends.
	Recommendation four
Provisions - other	■ In 2012-13 we discussed with management a potential provision for VERS. Management did not recognise a provision in the financial statements as they did not consider a constructive obligation to be present as at 31 March 2013 or that a reliable estimate was possible at that date. Management has recognised the cost of VERS as expenditure within the 2013-14 accounts. The difference of interpretation led to an unadjusted audit difference of £3.1 million in 2012-13. If this difference had been adjusted in 2012-13, the 2013-14 decrease in usable reserves balance would be £0.5 million (2013-14 accounts £3.6 million).
	■ Following a European Court of Justice ruling in May 2014, employers are required to pay holiday pay to staff at a rate commensurate with any commission or over time that they regularly earn, instead of at their basic pay level. Following legal advice, management has implemented this process for holiday pay going forward. It is anticipated this will cost approximately £0.2 million per year. Management is reviewing any potential retrospective liability.
	■ Whilst the Council do not operate any landfill sites, coal mines or other sites which carry significant liabilities to restore, there is one Council owned former landfill site and one present private operation. Management monitors the environmental impact of the former landfill site and state that there are known issues with it. There is sector-wide consideration of operations with obligations to restore and potential financial stability of operators, following the liquidation of a coal mine operator in another area. Further analysis is required by management to identify any potential liability and ensure they have appropriate monitoring procedures in place. Management needs to review any site (including wind farms and quarries) with a decommissioning or rectification obligation. This is considered to be an area of limited risk for the Council and there are no known issues.
	Recommendation five

There have been no substantive changes to the financial reporting framework as set out in the *Code of Practice on Local Authority Accounting in the United Kingdom 2013-14* **('the Code of Practice').**

There have been no changes to accounting policies in 2013-14. All accounting policies have been applied consistently.

Disclosure has been included in respect of the impact of revisions to IAS 19 *Employee benefits.*

The financial statements have been prepared on a going concern basis.

Accounting framework and application of accounting policies	
Area	**KPMG comment**
Code of Practice on Local Authority Accounting in the United Kingdom 2013-14 ('the Code')	The 2013-14 financial statements have been prepared in accordance with the Code of Practice which is based upon International Financial Reporting Standards ('IFRS'). During the year there have been no substantive changes in financial reporting requirements, and consequently there are no material changes to the Council's accounting policies. We are satisfied that the accounting policies adopted remain appropriate to the business.
Impact of revised accounting standards	■ The Council has applied the revisions to IAS 19 *Employee Benefits,* opting not to restate the prior year comparatives on grounds of materiality. We concur with this approach as there were no changes to the balance sheet as a result of the retrospective application of IAS19R, and the impact on the comprehensive income and expenditure account are not material. The employee benefits accounting policy in the draft financial statements required updating to reflect IAS19R and disclose that no prior year restatement had occurred. Amendments to the pension disclosure notes were required to ensure the disclosures were in line with the changes in IAS19R.
Going concern	■ The Council had net assets at the balance sheet date, although reduced by £12.6 million in the year; due primarily to the movement in general fund and housing revenue account (£3.6 million) and increases in pension liability (£17.9 million), offset by the upwards revaluation (£6 million) and other smaller movements in debtors and cash balances. ■ Management has considered the funding available to the Council, which is approved for 2014-15, combined with longer-term funding expectations and the fact that the net liability obligations do not fall due within one year. Over the past few years there has been a reduction in the overall cost base and further efficiency savings are incorporated in budgets. There is tight financial control and this will be further supported by quarterly reporting on efficiency savings. Management considers it appropriate to adopt a going concern basis for the preparation of these financial statements, and disclosed these circumstances within the financial statements. We are satisfied that this disclosure remains appropriate, noting that the pension deficit and long term borrowing does not become due in the next 12 months.
Impact of revised accounting standards	■ There are no newly effective accounting standards that are considered to have a material impact on the Council's financial statements in the current year. Appropriate disclosure to this effect is included within the accounting policies note to the financial statements.

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The financial statements and draft governance statement were made available on a timely basis.

There are further opportunities for continuous improvement in the financial statements preparation.

Financial statements preparation

- Management provided full draft financial statements on 26 June 2014, in line with the agreed timetable. This included the explanatory foreword, remuneration report and governance statement. A prepared by client audit file, was made available at the start of the final audit fieldwork on 7 July 2014. The finance team underwent change during the year, with the audit being performed during a period of a temporary finance manager.

- The majority of supporting documentation was received in a timely basis, and queries were answered promptly. We provided feedback to management on the content of the financial statements, annual report and governance statement, and we are pleased to report that these were consequently prepared appropriately. A number of presentational adjustments were needed to the draft financial statements, which would benefit from a more robust review prior to release. There is further opportunity for continuous improvement in the financial statement preparation. For example in the use and preparation of the CIPFA pro-forma financial statements in advance of the year end and in determining the approach to key judgements prior to the year end.

- The audit clearance meeting was held on 6 August 2014, in line with the prior year timetable. Management has indicated their desire to achieve a faster close of financial statements in 2014-15. We will meet with management to support an improvement in the financial statements close process.

- The Local Authority Accounts (Scotland) Regulations 2014 will come into force on 10 October 2014. The regulations contain provision for the unaudited annual financial statements as submitted to the auditor to be considered by the audit and governance committee no later than 31 August, and the audited financial statements to be presented to the audit and governance committee for consideration and approval prior to auditor signature before 30 September. Whilst the audit and governance committee already consider the unaudited financial statements, management will need to review the financial statements timetable to ensure the audited financial statements are also considered by the audit and governance committee.

Recommendation six

- All charitable trust funds registered with the Office of the Scottish Charity Regulator ('OSCR') require an audit. Management identified the Dr Bruce Fund as the only charity requiring an audit. We reviewed and agreed with OSCR confirmation that this is the only fund requiring an audit. Our audit work on the Dr Bruce Fund complete. The charity financial statements are required to be approved and signed by 30 September 2014, in line with the timetable for the Council's accounts.

- There is one adjusted audit difference of £5.1 million in relation to the changes to IAS19 presentation and one unadjusted audit difference of £2.1 million in relation to the calculation of depreciation.

- There are no significant matters in respect of (i) auditor independence and non-audit fees and (ii) management representation letter content, as reported in appendix one.

Governance and narrative reporting

Update on your governance arrangements

Our overall perspective on your narrative reporting, including the remuneration report and annual governance statement

Although there have been changes to the management structure and further staffing changes as a result of VERS, the corporate governance arrangements remain appropriate for the Council.

Risk management arrangements have been reviewed during the year, and a corporate risk management group is in place.

Corporate governance	The Council has overarching and supporting governance arrangements which provide a framework for organisational decision-making. The Council operates a cabinet structure, with a cabinet and two statutory committees; education and planning. The 2012 review of chief officers resulted in a reduction in the number of heads of service and a shift in this role to a more strategic position. A further change in the management structure occurred with effect from 1 April 2013, with three directors being reduced to two deputy chief executives. VERS also contributed to further staffing changes during 2013-14.
	Councillors are subject to a Code of Conduct instituted by the Ethical Standards in Public Life etc. (Scotland) Act 2000 and enforced by the Standards Commission for Scotland. A briefing session on the Code of Conduct was held during 2013-14 to ensure councillors are aware of their responsibilities. The Code of Conduct is documented within the Standing Orders, which are publically available. The Standing Orders were revised in June 2013 and updated in June 2014 to include a revised scheme of delegation and new procurement procedures. Commitment to the training and development of Councillors is evident through targets outlined in the 2014-15 improvement plan.
	As part of the Code of Corporate Good Governance a task group comprising senior officers of the Council was given responsibility for developing, monitoring and reviewing corporate governance. An annual corporate governance self evaluation has been implemented as a result of this. The results of the 2014 self evaluation were reported to the audit and governance committee in May 2014 and noted four improvement points, a decrease from the 13 points noted in 2013. This annual review of corporate governance demonstrates good practice and commitment to continuous improvement.
Risk management	Management is continuing to review risk management arrangements to provide assurance to elected members over the mitigation of identified risks. The risk management strategy and supporting documentation demonstrate a commitment to good practice and were initially implemented in December 2009. A corporate risk register is in place and is supported by departmental risk registers. The corporate risk register was updated in May 2014, following a review by the corporate risk management group. This was approved by cabinet in June 2014. Risk registers are currently maintained on spreadsheets, but are being transferred to the Aspireview system going forward.
	Risk appetite is referred to in the risk management strategy, although the Council's overall risk appetite is not defined. The risk management strategy was last updated in 2012 and is due to be updated again in October 2014; it would be beneficial to users of the strategy to include further information on the Council's risk appetite.
	The Council has a corporate risk management group, which is responsible for developing and monitoring the risk register, as well as identifying mitigating controls.

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Our reporting through the year identified improvements in the governance and controls framework from the prior year.

Annual governance statement	The annual 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 and identifies areas for improvements to be focussed on in the future. The statement also highlights the annual self-evaluation exercise carried out by the Council, which is based on the SOLACE/CIPFA good governance framework. Improvement points from this exercise are included within the statement and in the corporate improvement plan. The statement references the declarations of assurance completed by the Chief Officers to confirm that internal controls are operating effectively within their service or highlight any exceptions. Declarations of assurance were not completed by all officers in line with the Council's timetable. Due to long term absences, two of the declarations were signed by other people on behalf of the officers. The governance statement has been amended to reflect this.
Remuneration report	Since 2011-12, regulations place a 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 for the preparation of the remuneration report. The guidance states 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 is included before the annual governance statement. There were initially incorrect figures stated in the draft remuneration report and presentational changes required to ensure that it complied with guidance. In addition to these errors, the guidance requires the disclosure of the Chief Executive or most senior officer of any subsidiary bodies. There was no such disclosure for the Council's subsidiary body, the Musselburgh Racecourse. This disclosure is required by the guidance, in a tabular format showing any remuneration received from the subsidiary body. Some employees were missing from the salary bandings disclosure, meaning these figures were incorrect. Furthermore, we identified an instance where an exit package was calculated incorrectly as the payroll department had not been made aware of a change in leaving date. The incorrect disclosures have been updated in the report; management should review the report more thoroughly prior to finalisation to identify any errors or inconsistencies. *Recommendation seven* The remuneration report is required to disclose details of any exit packages awarded during the year. Due to the VERS and other redundancies, 101 people received exit packages in 2013-14. We tested a sample of exit packages, verifying they were awarded in line with the Council's policy on early retirement and the correct amounts were disclosed. We reviewed exit package disclosures against Audit Scotland guidance. We did not identify any issues arising from this testing.

While management have demonstrated a commitment to continuous improvement, the area of procurement would benefit from further attention.

Procurement	A new procurement policy and related procedures were drafted in 2013. The corporate procurement procedures were updated during the year and approved by Council on 24 June 2014. The procedures are included in the Standing Orders as an appendix and training has been provided to employees. As part of the update to procurement procedures, tendering limits were reduced and the approval process for new suppliers tightened. However, there is still a large volume of new suppliers and there has been limited progress in increasing the use of PECOS within the Council. We placed reliance on internal audit for review of procurement controls; internal audit identified weaknesses within procurement procedures. Cases were identified where the procurement process had not been initiated by an officer with the appropriate delegated authority. The procedures for ensuring all documentation is completed and the guidance to officers on reporting procurement activity to members require review. Internal audit also noted that various versions of procurement procedures were made available to staff. The 2012-13 public performance report from Audit Scotland identified that the Council does not report fully on a range of information, sufficient to demonstrate that it is securing Best Value in relation to procurement. 10 Councils in Scotland also received a similar outcome in the analysis. Management is considering the improvements to be implemented. The 2012 procurement capabilities assessment rated the Council as 'conformance', with a score of 44% (2011: 28%), the increasing score demonstrates management focus on improving procurement. As part of organisational change, the procurement team now sits alongside the legal team, instead of previously within the finance function.
Prevention and detection of fraud	A key mechanism in the allocation of authority, accountability and responsibility and the prevention and detection of fraud is the existence and maintenance of strategic and financial documentation. The Council has appropriate policies and codes of conduct for staff and councillors including a whistle blowing policy. The whistle blowing policy was updated in June 2014, to reflect the staffing restructure. Management identified no significant fraud or irregularities, other than issues that were already brought to our attention by internal audit.
Maintaining standards of conduct and the prevention and detection of corruption	The Council has recently reviewed and updated its Standing Orders and supporting Schemes of Administration and Delegation and procurement procedures. Role descriptors for councillors were approved by Council in October 2013, in line with best practice guidance from The Scottish Local Authorities Remuneration Committee. New councillors and new employees are required to agree to their respective Codes of Conduct on commencement of office or employment, and management is required to communicate any changes in the Code of Conduct to employees. This reinforcement of values will contribute to the effective prevention and detection of corruption at the Council. Internal audit reviewed the updated procurement procedures, and highlighted some weaknesses which require addressing.

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| National fraud initiative | The National Fraud Initiative ('NFI') is a data matching exercise which compares electronic data within and between participating bodies in Scotland to prevent and detect fraud. This exercise runs every two years and provides a secure website for bodies and auditors to use for uploading data and monitoring matches.

We prepared a short return to Audit Scotland in December 2013 assessing management's participation in the NFI exercise. Management's progress against a number of controls was graded on a traffic light basis, and an overall green rating was awarded. The Council has established a process for investigated cases of potential fraud highlighted by NFI, which is primarily undertaken by internal audit. Internal audit reported to the audit and governance committee in January 2014 on their findings from the recent NFI exercise. Internal audit show commitment to NFI and it is embedded within their annual plan, however some areas for improvement were identified. |
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We noted improvements in the internal control environment, and the implementation of recommendations raised in the prior year.

In particular we welcome the timely completion of the year-end bank reconciliation.

We are able to place reliance, where relevant, on the work of internal audit.

Systems of internal control	We have noted considerable improvements in the governance and controls framework over the three years of our appointment. Changes to policies and procedures have been made against a backdrop of senior staff restructuring and ongoing efficiency rationalisation. While management has acted on a number of the recommendations made in previous audit reports, there are opportunities to further enhance the control environment, particularly in relation to journals processing. Our interim management report made five recommendations; three grade two (material) and two grade three (minor).
	Our substantive testing of bank reconciliations identified two bank accounts which were not being managed centrally, and therefore had not been included within the bank balances presented by management. These related to the social work department and held £52,000; we do not consider these to be material. Management has begun investigating these accounts, including looking at the position with regard homes for older people.
	Recommendation eight
	Overall, our testing of the design and operation of financial controls over significant risk points confirms that generally controls relating to financial systems and procedures are designed appropriately and operating effectively.
Internal audit	As set out in our audit plan and strategy, we have evaluated the work of internal audit. In 2013-14 we relied on:
	■ journals processing;
	■ procurement scheme of delegation;
	■ trading operations;
	■ creditors;
	■ housing revenue account; and
	■ national fraud initiative.
	We had also planned to use internal audit's work on statutory performance indicators, however this has not yet been completed. This is due to be completed in September 2014, working jointly with Midlothian Council.
	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 2014.' The most significant areas where internal audit identified weaknesses in the design or operation of internal controls included procurement arrangements, journals processes, guidance for creditor payments, new suppliers, approval of payments, checking rent increases and homeless rent charges and retention of supporting documentation.
	The IASAB produced a common set of public sector internal audit standards ('PSIAS'), which were effective from 1 April 2013. Internal audit considered these standards when setting the 2013-14 and 2014-15 audit plans. Internal audit intend to complete an assessment against these new standards and implement an internal audit charter as part of the internal audit plan for 2014-15.

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Performance management

Our perspective on the performance management arrangements, including follow up work on Audit Scotland reports

Our work has identified that the Council's Best Value and performance management arrangements are good practice.

Best Value	Best Value places a statutory requirement on local authorities to ensure they have procedures in place for 'continuous improvement'. To achieve this, the Council developed an improvement framework, approved on 27 March 2012. Implementing an improvement framework demonstrates good practice in assessing whether the Council is achieving Best Value. The framework was reviewed in March 2014, and it was determined that no revision was required. That has not yet been reported to the Council.
	The Director of Performance and Best Value reported to the Accounts Commission on public performance reporting in June 2014, to consider whether councils reported on a range of information sufficient to demonstrate Best Value in a range of areas. East Lothian Council achieved a 'yes' score in 14 areas, a 'partial' score in six areas and a 'no' score in the area of procurement. This has prompted a review of KPIs in this area. The Council was highlighted as good practice in a range of areas, particularly around effective use of customer satisfaction information and a structured approach to public performance reporting. The performance website is well structured to the range of services and performance in each of these. The annual performance report is also well presented and contains information to show how customer feedback has been taken on board.
Performance management arrangements	A new Single Outcome Agreement ('SOA') has been developed by the Council and related partners. The SOA is an agreement between the East Lothian Partnership and the Scottish Government, setting out how each party will work to improve outcomes and reduce inequalities for East Lothian residents.
	The Council continues to use a well established approach to self-evaluation through the use of the How Good is our Council ('HGIOC') model, which is completed by all Council departments on an annual basis. The 2013-14 HGIOC process is substantially complete, but the results are yet to be compiled as some departments did not return their data on time. The results of the HGIOC exercise will be used to inform the service plans. Three year service plans are to be developed in order to align the plans with the three year budgets and provide continuity in each years' plan going forward.
	Together with the focus on self-evaluation, the main element of performance management takes place through monitoring service performance against agreed performance indicators. Performance indicators are listed on the Council website and progress is updated on a quarterly basis. 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.
	A review of performance indicators is underway to ensure each single outcome agreement outcome, council plan objective and Audit Scotland indicator category is linked to a specific KPI. KPIs are reviewed on an annual basis to ensure they are still appropriate, demonstrating commitment to continuous improvement.
	A Council improvement plan is developed annually. This identifies actions from a range of sources, including the HGIOC reviews, corporate governance self-evaluation, audit reports, Audit Scotland's *Overview of Local Government in Scotland* and any outstanding actions carried over from the prior year improvement plan. Management reviews progress against the improvement plan during the year in order to identify any points which require carrying forward.

The AIP states that overall the Council continues to perform well in most areas, and no areas have been selected for further scrutiny.

During 2013-14 we have prepared returns to Audit Scotland on health inequalities, ALEOs and major capital investment.

Shared risk assessment	The Council considered the updated assurance and improvement plan on 24 June 2014. This is used as a source of action points for the Council improvement plan, which was discussed and approved by members on the same date. The Local Area Network (LAN) recognises the Council's ongoing commitment to continuous improvement and self-evaluation. It recognises areas of strong performance, and a number of improvement activities. This plan contains no areas identified for further scrutiny, where two areas were selected in the previous year.
Local response to national studies	The Council's response to the following national reports was considered: ▪ Health inequalities in Scotland The report was published on 1 December 2012 and was considered by the audit and governance committee and senior management team together with an assessment of East Lothian Council's position. The report prompted the East Lothian Partnership to begin developing a health inequalities strategy. We prepared a short return to Audit Scotland in relation to the report.
Major capital investment in councils	The council management team considered the March 2013 Audit Scotland report '*Major capital investment in councils'* in May 2013. The audit and governance committee considered this report in June 2013. This provided background to the publication and the action plan prepared in response to this. The Council has made good progress against their action plan and has developed a comprehensive asset management strategy. However, the development of a formal capital investment strategy setting out a clear link between investment, performance and outcomes should be considered. We prepared a report to Audit Scotland on our findings from this review. These findings were documented in full in the 2013-14 interim management report.
Arms length external organisations (ALEO): Are you getting it right?	The Accounts Commission published a report in 2011, *'Arm's-Length External Organisations: Are you getting it right?',* as part of its 'How Councils Work' series of improvement reports. The aim of this was to provide the Accounts Commission a position statement on the councils' use of ALEOs. Management presented the report on ALEOs to the audit and governance committee on 27 September 2011. This was discussed by the audit and governance committee but no action plan was developed. The committee requested a clearer paper on ALEOs to be prepared, however this has not yet been completed. Our full findings from the targeted follow up are outlined in a separate report. These have been reported to Audit Scotland.

Performance against statutory performance indicators and other local government bodies is measured by the Council and our responsibilities as external auditor extend to understanding the arrangements and systems.

Statutory performance indicators	As part of our review of performance management, Audit Scotland require specific consideration of SPIs. The aim of this work is to assess how authorities are compiling and reporting data and ensuring it is complete and accurate. Local authorities have a statutory duty to ensure appropriate arrangements are in place for collecting, recording and publishing performance information. Auditors have a statutory duty to be satisfied that the council has made adequate arrangements for collecting and recording information, and for publishing it, as are required for the performance of their duties. Consideration has been given to the Council's procedures for collecting and reporting information on SPIs, in line with Audit Scotland requirements.

The audit of SPIs is a two stage process. Our results of the stage one assessment have been reported to Audit Scotland and our responses are outlined in a separate report. The results of the second stage, assessing the quality of PPR, will be reported to the Accounts Commission by May 2015.

In 2013-14, Statutory Performance Indicators were not specified and were drafted by the Council based on categories provided by Audit Scotland. The specified indicators have been replaced by the Scottish Local Government Benchmarking Framework. The 2013-14 SPIs were developed in consultation with the policy and performance review committee, and are linked to the Audit Scotland categories as well as council plan and single outcome agreement objectives.

The Council uses the Aspireview system to input, manage, interrogate and present data. For each indicator a performance indicator verification certificate is produced, requiring confirmation from two individuals. Management consider that there are adequate checks and controls to provide comfort over the completeness and accuracy of data. Internal audit are working jointly with Midlothian Council to perform sample testing on the SPI data at both councils. This is due to be performed in September 2014.

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 2013-14 report is due to be published in October 2014. |
| **Benchmarking** | The Local Government Benchmarking Framework has been developed to help councils compare their performance using a standard set of indicators. The indicators in the framework replace the specified Statutory Performance Indicators ('SPI's') from 2013-14 onwards. Results are analysed in 'family groups' to ensure comparison is between authorities with similar characteristics.

Management reviewed the available 2012-13 results, and reported these to the policy and performance review committee in April 2014. Indicators where there was a significant change from the prior period or a variance from the rest of the family group were analysed. Management has reviewed the five indicators where performance was poorest in the 2011-12 results, and has also reported the results of this. The Council is also participating in two pilot benchmarking exercises in road maintenance and school leaver destinations, the results of which will be reported to the policy and performance review committee later in the year. This shows commitment to continuous improvement.

The framework also contains indicators based on customer satisfaction. These results show high levels of satisfaction for residents of East Lothian in a range of services, including a first place ranking for satisfaction with parks and open spaces across 32 councils. |

Appendices

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There was one adjusted audit difference and one unadjusted audit difference.

Area	Key content	Reference
Adjusted audit differences Adjustments made as a result of our audit	There is one adjusted audit difference in relation to the changes to IAS19 which removed the £5.1 million return on plan assets from other comprehensive income and expenditure and correctly recognised this amount within financing and investment income and expenditure (net interest on the net defined benefit liability). The balance on general fund reserves is not effected.	Appendix 2
Unadjusted audit differences	We are required by ISA (UK and Ireland) 260 to communicate all uncorrected misstatements, other than those which are trivial. There is one unadjusted audit difference for the under recognition of depreciation on enhancements to existing assets. If recognised, net assets and total reserves would decrease by £0.6 million to £251.7 million.	Appendix 2
Confirmation of Independence Letter issued by KPMG LLP to the Audit Committee	We have considered and confirmed our independence as auditor and our quality procedures, together with the objectivity of our Audit Director and audit staff. There are no non-audit fees for the year.	Appendix 3
Draft management representation letter Proposed draft of letter to be issued by the Company to KPMG prior to audit sign-off	There are no changes to the representations required for our audit from last year.	-

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There is one adjusted audited differences and one unadjusted audit difference to the financial statements.

Adjusted and unadjusted audit differences

We are required by ISA (UK and Ireland) 260 to communicate all corrected and uncorrected misstatements, other than those which are trivial, to you. There is one adjusted audit differences and one unadjusted audit difference.

Adjusted caption	Nature of difference	Deficit on provision of services (£'000)	Other comprehensive income and expenditure (£'000)
Comprehensive income and expenditure statement – financing and investment income and expenditure	The recognition of the net return on assets within the deficit on provision of services.	5,122	
Comprehensive income and expenditure statement – other comprehensive income and expenditure			5,122
Net impact		**5,122**	**5,122**

Unadjusted caption	Nature of difference	Net assets	Total reserves
Balance sheet – property, plant and equipment – Council dwellings	The recognition of depreciation on enhancements to existing assets council dwellings and other property, plant and equipment	(1,567)	
Balance sheet – property, plant and equipment revaluation		1,567	
Balance sheet – property, plant and equipment – other			
Balance sheet – unusable reserves		(551)	551
Net impact		**(551)**	**551**

A number of numerical and presentational adjustments were required to some of the financial statements notes, to add extra disclosures or to include additional information to aid the reader of the financial statements. The most significant of which were:

■ remuneration report – inclusion of the most senior manager of the Council's subsidiaries and changes to the amounts disclosed to accurately reflect officer and councillor remuneration.

■ pension note – correction of prior year comparatives, reordering the disclosure note and extra narrative disclosure.

■ segmental and subjective analysis – represented disclosure note in line with the Code's guidance.

Auditing standards require us to consider and confirm formally our independence and related matters in our dealings with the Council.

We have appropriate procedures and safeguards in place to enable us to make the formal confirmation in our letter included opposite.

Auditor independence

Professional ethical standards require us to provide to you at the conclusion of an audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed. This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence.

We have considered the fees paid to us by the Council and its related entities for professional services provided by us during the reporting period. We are satisfied that our general procedures support our independence and objectivity.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the APB Ethical Standards. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Regular communications
- Internal accountability
- Risk management
- Independent reviews

Please inform us if you would like to discuss any of these aspects of our procedures in more detail.

There are no other matters that, in our professional judgement, bear on our independence which need to be disclosed to the Council.

Confirmation of audit independence

We confirm that as of 1 September 2014, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This report is intended solely for the information of the audit and governance committee and should not be used for any other purpose.

Yours faithfully

KPMG LLP

In respect of employee benefits, each of the assumptions used to value the Council's net pension deficit are within an acceptable range of KPMG's expectations.

We are of the view that this therefore represents a reasonable and balanced approach, in accordance with the requirements of IAS 19R.

Defined benefit pension liability		
2014 £000	**2013 £000**	**KPMG comment**
(128,785)	(110,842)	In line with our established practice and in advance of the audit fieldwork, our actuarial specialists reviewed the approach and methodology of the actuarial assumptions used in the IAS19R pension scheme valuation. Details of key actuarial assumptions are included in the table, along with our commentary.

Assumption	Council	KPMG central	Comment
Discount rate (duration dependent)	4.30%	4.30%	Acceptable. The actuarial assumption has been calculated using a different approach from the prior year. It is KPMG's view that this represents an enhancement in methodology.
CPI inflation	RPI - 0.8%	RPI – 1%	Acceptable – the Council's assumption is more prudent (higher liability) than KPMG's central rate, but is within the acceptable range.
Net discount rate (discount rate – CPI)	1.50%	1.65% - 1.75%	Acceptable – the Council's assumption is more prudent (higher liability) than KPMG's central rate, but is within the acceptable range.
Salary growth	1% pa until 31 March 2015. 1.5% above RPI	0% - 1.5% above RPI/CPI inflation	Acceptable – the Council's assumption reflects 1% salary increases until 31 March 2015.

The overall assumptions applied by management are considered to be reasonably balanced for a scheme with a liability duration of between 17 and 23 years. The closing deficit increased by £17.9 million compared to 2012-13, primarily due to the application of an updated discount rate. A reconciliation from opening to closing deficit is included in appendix four.

The Council has appropriately applied IAS 19 *(revised)* in the financial statements. If the standard had been adopted early in 2012-13, the estimated change to finance costs would be £2.9 million. We do not consider this to be a material amount and therefore agree with management's decision not to restate the prior year comparatives. There would be no impact on the prior year net assets position if the Council had restated the prior year comparatives. An audit adjustment of £5.1 million was processed to correct the accounting for the return on plan assets, which had been incorrectly recognised in other comprehensive income and expenditure instead of financing and investment income and expenditure.

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The table opposite shows the reconciliation of the movement in the statement of financial position.

Increases to the pension scheme deficit in the year have been driven by changes to the financial assumptions, particularly in respect of the discount rate.

	£000	Deficit/loss	Surplus/gain	Impact	Commentary
	Opening pension scheme deficit			**(110,842)**	The opening IAS 19 deficit for the Scheme at 1 April 2013 was £110.8 million, consisting of assets of £346.4 million and defined benefit obligation of £457.2 million.
I & E	Service cost			(13,899)	The scheme remains open to accrual. The employees' share of the cost of benefits accruing over the year is £13.9 million.
I & E	Past service cost			(1,165)	A past service cost of £1.2 million is recognised, relating to early retirement over the year.
I & E	Net interest			(4,993)	This is the interest on the opening deficit of £110.8 million adjusted for contributions paid during the period.
Cash	Contributions			14,834	The Council made contributions of £14.8 million, broadly in line with contributions made last year, allowing for salary increases.
OCI	Actuarial gain/(loss) – demographic assumptions			-	There was no change to the demographic assumptions since 31 March 2014, and so there is no gain or loss.
OCI	Actuarial loss – financial assumptions			(18,010)	There was an actuarial loss of £18.0 million, driven by a 0.2% decrease in the discount rate assumption. This is in line with the size and duration of the scheme.
OCI	Other experience			168	
OCI	Return on assets			5,122	The actual return on assets is lower than the interest on assets of £5.1 million.
	Closing pension scheme deficit			**(128,785)**	The closing IAS19 deficit on the scheme at 31 March 2014 is £128.8 million (consisting of assets of £370 million and defined benefit obligation of £498.8 million).

I&E – impacts on surplus /(deficit) within statement of comprehensive net expenditure
Cash – cash-flow impact
OCI – charged through other comprehensive income

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The action plan summarises specific recommendations arising from our work, 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 auditor. 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 Fixed asset register		**Grade two**
As in previous years Council dwellings are recognised as a single line item by road or area in the fixed asset register with total annual enhancements recognised as separate assets. It was not possible for management to specifically allocate the valuation based on this recognition in the fixed asset register. As at 31 March 2014, management elected to recognise all council dwellings as a single line item in the fixed asset register, and all additions and enhancements to council dwellings will be recognised on this one line. This does not allow for componentisation of assets. There is a further risk to the depreciation calculation as individual assets and components useful lives cannot efficiently be applied to accurately calculate the depreciation amount for 2014-15.	Management should continue with its review of the fixed asset register to ensure appropriate data is held on individual council dwelling assets. This should cover methods to componentise council dwellings, the allocation useful lives and the calculation of depreciation of individual components.	**Responsible officer:** **Implementation date:**

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

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
2 Impairment review		**Grade three**
There is opportunity to further enhance the impairment review by tracking all manager reviews, potential impairments identified and conclusions in one document. We suggested to management that the review could be performed as at 28 February thereby providing greater time for consideration and implementation of impairments. There is a risk that the value of assets is overstated due to potential impairments conditions not being considered.	A stronger audit trail of impairment reviews tracking manager reviews, potential impairments identified and conclusions, summarised in one document, would help to support impairments recognised in the financial statements or consideration of impairment triggers. To support the formalisation of the impairment review, management could implement year end departmental surveys which would require managers to disclosure pertinent information.	**Responsible officer:** **Implementation date:**
3 Depreciation		**Grade three**
We consider that management has an unique method of calculating depreciation on enhancements to existing assets, which gave rise to an immaterial depreciation error in the year. There is a risk that the audit adjustment could become material.	We recommend management reviews the current depreciation policy and considers revising the current methodology. This should take account of how enhancements to council dwellings are recognised in the fixed asset register as there is a risk that the audit adjustment could become material in value.	**Responsible officer:** **Implementation date:**

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

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
4 Bad debt provision		**Grade three**
The bad debt provision is calculated separately for council tax, housing rents, housing benefit and general bad debt. The council tax, housing rents and housing benefit provisions are calculated on a historic basis, meaning they may not accurately reflect the bad debt the Council will face. Overall, the Council provides for 73.5% (2012-13: 66.29%) of its debtors. We have reviewed this compared to other authorities and consider that council tax, rents and housing benefit provisions are prudent or that gross debtors can be written off.	We recommend that management reviews the calculation methods for bad debt provisions and write-offs. This should include analysis of debtor payment profiles to update and refresh the bad debt and write off policies.	**Responsible officer:** **Implementation date:**
5 Sites with rectification obligations		**Grade two**
Whilst the Council do not operate any landfill sites, coal mines or other sites which carry significant liabilities to restore, there is one Council owned former landfill site and one present private operation. Management monitors the environmental impact of the former landfill site. There is sector-wide consideration of operations with obligations to restore and potential financial stability of operators. There is a risk that there is a financial obligation on the Council or out-of-date knowledge of rectification, coupled with risks	We recommend management performs further analysis is required by management to identify any potential liability and ensure they have appropriate monitoring procedures in place. Management needs to review any site (including wind farms and quarries) with a decommissioning or rectification obligation.	**Responsible officer:** **Implementation date:**

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

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
6 Accounts timetable		**Grade three**
The Local Authority Accounts (Scotland) Regulations 2014 will come into force on 10 October 2014. The regulations contain provision for the unaudited annual accounts as submitted to the auditor to be considered by the audit and governance committee no later than 31 August, and the audited accounts to be presented to the audit and governance committee for consideration and approval prior to auditor signature before 30 September. There is further opportunity for continuous improvement in the financial statement preparation. For example in the use and preparation of the CIPFA pro-forma financial statements in advance of the year end and in determining the approach to key judgements prior to the year end.	Whilst the audit and governance committee already consider the unaudited accounts, management should review the accounts timetable to ensure the audited accounts are also considered by the audit and governance committee.	**Responsible officer:** **Implementation date:**
7 Remuneration report		**Grade three**
A number of corrections and presentational adjustments were required to ensure that the remuneration report was accurate and complied with guidance. There is a risk that remuneration report is inaccurate or is not in line with guidance. We identified a miscalculation of an exit package, as the payroll department had not been made aware of a change in leaving date. There is a risk that exit packages are calculated incorrectly, and overpayments are made to employees leaving the council.	We recommend that the report should be reviewed more thoroughly prior to its inclusion in the financial statements to identify errors and inconsistencies. Furthermore, information for calculating and awarding exit packages should be passed to payroll in a timely manner to ensure overpayments are not made.	**Responsible officer:** **Implementation date:**

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

Finding(s) and risk(s)	Recommendation(s)	Agreed management actions
8 Bank accounts		**Grade three**
Substantive testing of bank reconciliations identified two previously unidentified bank accounts held with the Bank of Scotland. These related to the social work department and held £52,000; we do not consider these to be material. Management has begun investigating these accounts, including looking at the position with regard homes for older people.	We recommend that management should continue its investigation into other potential unidentified bank accounts. To ensure that the central finance team has all relevant information concerning bank accounts, management could implement year end departmental surveys which would require managers to disclose pertinent information.	**Responsible officer:** **Implementation date:**
There is a risk that other previously unidentified bank accounts exist that could hold significant bank balances or overdrafts.		

KPMG

cutting through complexity

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East Lothian Council

Targeted follow-up report

Arm's-Length External Organisations – Are you getting it right?

7 July 2014

Contents

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 ("Council") and is made available to Audit Scotland and the Accounts Commission (together "the beneficiaries"), and 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 required to complete the questionnaire.

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 (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary's Publication Scheme or otherwise) 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.

The purpose of this report is to report our findings from a targeted follow-up on the Council's arrangements as they relate to the Accounts Commission report '*Arms-Length External Organisations: Are you getting it right?',* which was published as part of the Commission's 'How Councils Work' series of improvement reports for councillors and officers.

Background

Arm's-length external organisations ("ALEOs") provide recognised 'council services' e.g. leisure services, but they can also manage commercial operations e.g. exhibition facilities and commercial properties. While the ALEO is responsible for services, the council remains responsible for the public money it gives to the ALEO and the quality of services the ALEO provides.

The Accounts Commission's interest in ALEOs goes back to the 1996 'Following the public pound' Code produced with COSLA. In 2011, the Commission published *'Arm's-Length External Organisations: Are you getting it right?'* as part of its 'How Councils Work' series of improvement reports for councillors and officers.

The aim of this targeted follow-up work is to:

- provide the Accounts Commission with a position statement on councils' use of ALEOs and, in particular, on progress since the How Councils Work report on ALEOs was published in 2011; and

- inform the Accounts Commission's consideration of ALEOs in the context of the public audit model.

This follow-up work is being undertaken in accordance with the local government planning guidance issued by Audit Scotland to local auditors.

Approach

The governance of ALEOs is a major element of the targeted follow-up audit. To this end, and to support judgements on the effectiveness of governance arrangements, the guidance issued to local auditors was to apply the 'Toolkit for improving the governance of ALEOs' set out at the end of the How Councils Work report on ALEOs. This identifies the key issues and includes a list of prompts which might indicate 'basic practice, basic and better practice and advanced practice'.

Our audit approach has therefore involved a review of policies and procedures in operation at the Council, as well as information gathering in respect of certain arrangements.

To support reporting to the Accounts Commission, we have provided in our report judgements on the effectiveness of the governance arrangements within the Council.

It is recognised that there is of course no single definition of what an ALEO is, and therefore, for the purposes of this follow-up work, the starting point has been to use the information in the Council's group accounts, supplemented by our local knowledge of the Council and its activities. In appendix one we set out the Council's ALEO, and subsidiary entities as noted in the Council's group accounts.

This report is structured to answer the five questions identified in the checklist provided by Audit Scotland to inform the follow-up work:

1. Has the council formally considered the Commission's How Councils Work report on ALEOs. If so did it develop an action plan and have also actions been addressed?

2. How clear is the council about its reasons for delivering services through ALEOs?

3. How well does the council understand the financial commitment and risk to which it is exposed through ALEOs?

4. How effective are the council's arrangements for monitoring the financial and service performance of ALEOs, maintaining accountability and for ensuring audit access?

5. Where members or senior officers are appointed to the board or equivalent of ALEOs, how clear are they about their role?

Our consideration of the overall arrangements for governance and accountability has focused on Enjoy East Lothian Limited. Management have identified this to be the sole ALEO of the Council.

Question	Evidence	Conclusion*
Has the council formally considered the Commission's How Councils Work report on ALEOs. If so did it develop an action plan and have also actions been addressed?	Management presented the Commission's report on ALEOs to the audit and governance committee on 27 September 2011. This was discussed by the audit and governance committee however an action plan was not developed. The committee requested a clearer paper on ALEOs to be prepared, however this has not yet been completed.	Basic
How clear is the council about its reasons for delivering services through ALEOs?	An options appraisal was prepared by external advisers, exploring the rationale and risks for a number of scenarios for delivery of sport and leisure services. This was considered by the Council before it committed to progress a transfer to an ALEO, being Enjoy East Lothian Limited ('Enjoy'). The specification for leisure services document sets out the minimum service provision required. This does not set out the circumstances in which the agreement would be terminated. Management do not formally review whether the services provided by the ALEO remain aligned with the Council's wider objectives, although recently the Enjoy Board was encouraged to recruit a health care professional to provide expertise in light of the evolving Council objectives in relation to community health partnerships. There are no formally documented circumstances which would trigger a review of the Council's involvement in the ALEO, although management discussed three situations (under performance of service delivery, not meeting the wider Council objectives and significant financial difficulties) whereby they would consider a review. Ongoing regular contract management helps mitigate the associated risks.	Basic

* Our conclusion is based the three levels of practice (basic, basic and better, advanced) as defined in *appendix two: toolkit for improving governance of ALEOs* in the Audit Scotland report.

Governance and accountability – overall arrangements

Question	Evidence	Conclusion*
How well does the council understand the financial commitment and risk to which it is exposed through ALEOs?	Financial commitment and risk were two elements of the option appraisal considered by Council prior to transferring services and staff to the ALEO. During the transfer process, the Council was advised by external legal and financial advisers who were considered to be specialists in the field. A project board and project group were constituted and explored issues raised in respect of funding and risk. Reports to Council were prepared and considered at appropriate milestones in the process to ensure elected members were content with progress and with the direction of travel.

There is a management contract between East Lothian Council and Enjoy East Lothian Limited and there are a number of service level agreements for IT, HR, payroll and property maintenance, which set out the summary of charges in relation to these services provided to Enjoy.

The services to be delivered by Enjoy are specified in the contract between the parties and the effects of failure to perform are also set out. Further improvements in accountability and performance measurement are being explored by Council officers and the Enjoy Board at this time.

The Council has not set specific governance, finance and performance indicators for Enjoy and there are no documented contingency plans to ensure continuous service delivery if the agreement were to end. Financial statements are prepared and audited annually, with a summary presented to the audit and governance committee of the Council each year, together with a management report, enabling consideration of performance and related financial risks. | Basic and better |

* Our conclusion is based the three levels of practice (basic, basic and better, advanced) as defined in *appendix two: toolkit for improving governance of ALEOs* in the Audit Scotland report.

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Question	Evidence	Conclusion*
How effective are the council's arrangements for monitoring the financial and service performance of ALEOs, maintaining accountability and for ensuring audit access?	The initial specification for leisure services identified that the Company would liaise at regular intervals. The specification also sets out the expected standards of service and ways in which the Company would work with stakeholders.	Basic and better
	Enjoy presents its annual accounts to the Council; the audit and governance committee meeting in September 2013 included a management report on the performance, which covered financial performance, user statistics, future developments and an extract of the audited financial statements. This enabled members to scrutinise performance of the ALEO.	
	There are quarterly contract meetings between senior officers of the Council and Enjoy. The quarterly meetings are attended by the depute chief executive (support services) and finance manager. The head of infrastructure and senior manager for sport, countryside and leisure attend all Enjoy Board Meetings as observers.	
	The council receives forward plans and scrutinises the contents; Enjoy is developing the business plan and this will be presented to the Council in 2014,	
	We understand that there are no significant performance or financial concerns about the ALEO and there are no other public organisations directly involved in Enjoy activities.	
	The Council expects Enjoy to develop and monitor its own targets and methods of measurement for monitoring performance; these are not stipulated by the Council. Management of Enjoy report internally within the entity on employment practices, equality requirements, purchasing policies and sustainability, although there is no requirement for the Council to monitor these elements.	
	The access rights for internal and external audit are not covered in the management contract. Enjoy appoints its own independent auditor, currently Scott Moncrieff.	

* Our conclusion is based the three levels of practice (basic, basic and better, advanced) as defined in *appendix two: toolkit for improving governance of ALEOs* in the Audit Scotland report.

Question	Evidence	Conclusion*
Where members or senior officers are appointed to the board or equivalent of ALEOs, how clear are they about their role?	One third of the Enjoy Board is appointed from elected members of the Council, the appointments are determined at the start of each term. A paper was put to the 12 May 2012 Council meeting which set out the proposed appointments to the Enjoy Board. This did not set out the reasons behind its decisions to select the individual members. Following the last local election, all elected members (including those that had previously been members of the Council) were offered a package of induction training that included a session on potential conflicts of interest arising from their positions on external bodies. Although not all members attended training, management consider that those that did appeared to understand the issues that might arise. There are disclosure policies to be followed and management consider that members appropriately declare interests at Council and committee meetings and seek advice from the monitoring officer / legal advisers if uncertain. On the formation of the Enjoy Board, the external legal advisors provided an induction to Board members and there is subsequently an induction for all new Enjoy Board members.	Basic and better

* Our conclusion is based the three levels of practice (basic, basic and better, advanced) as defined in *appendix two: toolkit for improving governance of ALEOs* in the Audit Scotland report.

Appendix

cutting through complexity

Appendix one – data collection

The table opposite provides the required collection of quantitative data for each of the entities identified by the Audit Scotland in its paper *Arm's Length External Organisations: Powers of the Commission* presented to the Accounts Commission in October 2013.

Name of ALEO	Legal status	Services delivered	Turnover (£)	Net assets (£)	Workforce	Source of data e.g. 12/13 accounts, developments in 13/14 etc.	Status
Enjoy East Lothian Limited	Company limited by guarantee	The activities of the company are to provide recreational facilities for the people of and visitors to East Lothian, organise recreational activities, which are available to members of the public at large with the objective of improving their conditions of life, contribute to advancing the wellbeing of the inhabitants of, and visitors to the area.	5,784,103	5,262,379	298	2012-13 accounts	ALEO

The following entities are identified within *Arm's Length External Organisations: Powers of the Commission* as subsidiaries and are not considered to be ALEOs.

Name of entity	Legal status	Services delivered	Turnover (£)	Net assets (£)	Workforce	Source of data e.g. 12/13 accounts, developments in 13/14 etc.	Status
East Lothian Land Limited	Private company limited by shares	The principal activity of the company continued to be that of trading in land for development.	9,511	606,702	None	2012-13 accounts	Sub committee
East Lothian Investments	Private company, without share capital	The principal activity of the company continued to be that of granting interest free loans to businesses in East Lothian with the aim of encouraging commercial activity and enterprise in the area.	14,610	552,726	None	2012-13 accounts	Sub committee
Brunton Theatre Trust	Registered Charity	Provision of arts services	1,016,268	386,274	None*	2012-13 accounts	Associated committee
Musselburgh Joint Racing Committee	Joint Racing Committee	The remit of the committee is to organise and develop horse racing at Musselburgh Links. The council nominates four of the seven Committee members.	1,370,241	212,645	Not disclosed	2012-13 accounts	Associated committee

* Brunton Theatre Trust does not have any employees, however there are 11.5 FTE members of staff employed by the Council who work at the Theatre.

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East Lothian Council

Statutory Performance Indicators

28 August 2014

![KPMG logo]

The contacts at KPMG in connection with this report are:

Andy Shaw
Director, KPMG LLP

Tel: 0131 527 6673
Fax: 0131 527 6666
andrew.shaw@kpmg.co.uk

Michael Wilkie
Senior Manager, KPMG LLP

Tel: 0141 300 5890
Fax: 0141 204 1584
michael.wilkie@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

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This report a is presented in connection with our audit for the year ended 31 March 2014 under the terms of our appointment by the Accounts Commission for Scotland.

This report outlines our findings from a review of East Lothian Council's ("the Council") approach to Statutory Performance Indicators (SPIs).

Background

Under the Local Government Act 1991, local authorities have a statutory duty to ensure appropriate arrangements are in place for collecting, recording and publishing performance information. Auditors have a statutory duty to be satisfied that the council has made adequate arrangements for collecting and recording information, and for publishing it, as are required for the performance of their duties.

The Accounts Commission has a statutory power to define the performance information that local authorities must publish. From 2013-14, performance indicators are no longer specified but criteria is provided to guide local authorities in the performance indicators they should develop and report.

Audit Scotland provides auditors with a pro forma template to review the Council's SPIs. The aim of this template is to assess whether adequate arrangements are in place for collection and publication of accurate and complete information in relation to the SPI categories, and report our findings to Audit Scotland.

Approach

Our audit approach has therefore involved a review of policies and procedures in operation at the Council as well as information gathering in respect of SPI monitoring and reporting. To support reporting to the Accounts Commission, we have included judgements on the effectiveness of performance management arrangements within the Council.

This report is structured to answer the specific questions identified in the stage one pro forma provided by Audit Scotland. This focuses on two key areas:

■ planning arrangements

■ systems assessment

The audit of SPIs is a two stage process. Our findings from the initial stage are outlined within the summary of findings. The results of the second stage, assessing the quality of PPR, will be reported to the Accounts Commission by May 2015.

Summary of findings

As part of our review of performance management, Audit Scotland require consideration of the process for collecting and reporting data on Statutory Performance Indicators (SPIs).

We performed the stage one work over SPIs using the Audit Scotland template.

Statutory Performance Indicators

As part of our review of performance management, Audit Scotland require specific consideration of SPIs. The aim of this work is to assess how authorities are compiling and reporting data and ensuring it is complete and accurate. Local authorities have a statutory duty to ensure appropriate arrangements are in place for collecting, recording and publishing performance information. Auditors have a statutory duty to be satisfied that the council has made adequate arrangements for collecting and recording information, and for publishing it, as are required for the performance of their duties.

1. To ascertain and appraise the council's overall approach to Scottish Local Government Benchmarking Framework indicators and Public Performance Reporting		
Area	**Procedures**	**KPMG comment**
Planning arrangements	Inspect and assess the council's overall plans for collecting performance information.	Each KPI is assigned a responsible officer, or a collator, who is responsible for the collection of data. Each KPI also has a verifier to confirm the data is complete and accurate. The collator is then responsible for uploading the information to Aspireview, or passing it to the policy officer.

The KPI data is due to be collected by the end of August, to link with the deadline for reporting the Local Government Benchmarking Framework data.

Data is collected from a variety of sources and is maintained in the performance monitoring system, Aspireview. The requirements for quality data, as well as the processes for the collection of data, are outlined in the performance data quality policy. |
| | Confirm the work the council has done to identify the information its communities want to see and how this has impacted on the council's arrangements. | A survey of residents was last conducted in 2011, where questions were asked to identify the issues that were most important to the community. This informed the planning process and helped to prioritise KPIs.

Due to high costs and a low response rate of the surveys, the Council is moving to a citizens' panel approach for consultation of residents. The panel has recently been established and contains approximately 1600 consultees, who have agreed to answer questions sent by the Council on a quarterly basis. The members of the panel have been recruited to be representative of the wider population of East Lothian. However, as this has recently been established, the first consultation has not yet taken place. |

1. To ascertain and appraise the council's overall approach to Scottish Local Government Benchmarking Framework indicators and Public Performance Reporting (continued)		
Area	**Procedures**	**KPMG comment**
Planning arrangements (continued)	Confirm the work the council has done to identify the information its communities want to see and how this has impacted on the council's arrangements.	KPIs are developed with feedback from the policy and performance review committee to ensure the key issues are appropriately addressed. This process was last performed in April 2013, but the KPIs are currently in review and will be taken to the policy and performance review committee once they have been redrafted. Elected members are asked for feedback on performance related matters, as they are seen as intrinsically linked to their communities.
	Inspect and assess the alignment of performance measures to key priorities and outcomes.	Performance indicators are developed using the council plan objectives, Single Outcome Agreement outcomes and SPI categories. Each objective, outcome and category is linked to at least one indicator during the development process. This was most recently performed in April 2013, when the most recent indicators were reviewed. A report was presented to the policy and performance review committee on 30 April 2013 showing how these are aligned. This process is currently ongoing as the indicators are being redeveloped for 2014-15. The SPI categories and SOA outcomes have been sent to heads of departments in a spreadsheet format to ensure there is a clear indicator for each one. This is also in response to Audit Scotland feedback that some indicators were not explicitly aligned.
	For the indicators listed in SPI 1 and 2 inspect and assess the council's plans for collection and reporting.	In the 30 April 2013 report to the policy and performance review committee each indicator listed in SPI1 and 2 were linked to at least one KPI. However, some weaknesses were noted by Audit Scotland in this linking, particularly in the area of procurement. A review is currently being performed to ensure each indicator from SPI1 and 2 is explicitly linked to a Council KPI. This is being completed by each service for the KPIs for which they are responsible, and will then go to the policy and performance review committee and the CMT for scrutiny before being implemented. The data is collected in Aspireview and reported in the annual performance report, as well as through updates on the performance website.

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1. To ascertain and appraise the council's overall approach to Scottish Local Government Benchmarking Framework indicators and Public Performance Reporting (continued)		
Area	**Procedures**	**KPMG comment**
Planning arrangements (continued)	Confirm the council's plans for internal verification of the indicators listed in SPI 1 and 2.	Each service must fill out a verification sheet for their KPIs. Performance against the KPI is reported by the collator and verified by both the assigned verifier and the head of service.
		Internal audit also verify a sample of performance indicators, using a risk based approach to. Going forward, this will be performed jointly with Midlothian Council. The councils will work together to indentify the performance indicators that are most important to each council, and test these in both councils. This is due to be completed by September 2014.
	Inspect and assess the council's plans for publishing indicators and performance information.	The East Lothian Council Annual Performance Report is completed on an annual basis and is due to be published October 2014. However, updates against indicators are reported on the performance website more frequently. The website is automatically updated when Aspireview is updated. Some indicators can be measured quarterly. Progress against these reported to the policy and performance review committee on a quarterly basis, and this is published on the website. The quarterly reports focus on areas of challenge and how performance can be improved. The annual report shows both achievements and challenges.
		The Scottish Local Government Benchmarking Framework indicators are due to be published by December 2014, once the collation exercise is complete. The completion deadline is the end of August and the process is running on schedule. These indicators will be published on the performance website, and also referenced in the annual report. The full SLGBF for all authorities will be published at a later date. Once these results are available, there will be a separate report to the policy and performance review committee and published on the website to show how East Lothian Council's results compare with other local authorities.
		The majority of comparative data comes from the SLGBF on an annual basis. If there is a comparative available for an indicator, it will be shown on alongside the East Lothian Council position on a graph linked to the indicator on the performance website. The website also shows whether the position of the indicator has increased or decreased since they were last reported. Prior period results are also shown on the graph.

2. To ascertain and appraise the council's systems for Scottish Local Government Benchmarking Framework indicators and Public Performance Reporting		
Area	**Procedures**	**KPMG comment**
Planning arrangements (continued)	Inspect and assess the council's plans for publishing indicators and performance information	The overall reporting contains varying levels of quantitative and qualitative information. There are links in the annual performance report to guide users to the performance website for further information on the indicators.
System Assessment	Inspect the council's progress against their planned timetable for collecting and publishing performance information. Consider the impact of any delays.	The council is on track with the timetable for the Scottish Local Government Benchmarking Framework reporting, due to be completed at the end of August 2014, as the majority of the information required for this has been received. However, the progress has been slower than anticipated on SPI reporting due to a change in process in 2013-14. As the specific indicators are no longer specified, the Council has implemented new indicators in 2013-14 and employees are not used to reporting these. There have also been various staffing changes in the year. However, although the Council is behind in collecting verification sheets, the annual performance report is not due for publication until October and they are still on track for this deadline.
	Confirm the internal verification that has taken place. Review the results and action taken.	Internal verification takes place on the verification checklist completed for each indicator. An example was reviewed and had been verified by the verifier and the head of service. However, not all checklists have been completed to date. Internal audit are also due to perform further verification checks, however as the process is still ongoing, this has not yet taken place.

2. To ascertain and appraise the council's systems for Scottish Local Government Benchmarking Framework indicators and Public Performance Reporting

Area	Procedures	KPMG comment
Planning arrangements (continued)	Confirm that arrangements for collection, verification and reporting are communicated to all staff involved and understood.	The arrangements for the collection, verification and reporting of data is outlined in the Performance Data Quality Policy, which is available to all staff. This is followed up with emails from policy officer responsible for the SPI process to the collators. One-to-one meetings are available for staff who may not be clear on the process, however there is no formal training. To update indicators in Aspireview, collators can do this directly and upload their supporting documentation, or pass on the information to the policy officer to upload for them.

REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Chief Executive

SUBJECT: Corporate Risk Register

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1   PURPOSE

1.1   In keeping with the Council's risk management strategy, the Corporate Risk Register has been updated following a review by the Corporate Risk Management Group on behalf of and in consultation with the Council Management Team.

1.2   The Corporate Risk Register was approved by Cabinet on 12th June and is now presented to the Audit and Governance Committee for discussion, comment and noting.

2   RECOMMENDATIONS

2.1   It is recommended that the Audit and Governance Committee notes the Corporate Risk Register for 2014.

2.2   In doing so, the Audit and Governance Committee is asked to:

- note that the relevant risks have been identified;
- note that the significance of each risk is appropriate to the current nature of the risk;
- note that the total profile of corporate risk can be borne by the Council at this time in relation to the Council's appetite[1] for risk; and,
- recognise that, although the risks presented are those requiring close monitoring and scrutiny throughout 2014, many are in fact longer term corporate risks for the Council that are likely to be a feature of the risk register over a number of years.
- note that the Council Management Team will review risks in the Corporate Risk Register on a regular basis.

3   BACKGROUND

3.1   In presenting the proposed Corporate Risk Register 2014 to the Committee for discussion, comment and noting, the Council Management Team would wish to draw the Committee's attention to one specific matter. All risks have been

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[1] How much risk the council can bear, or could be willing to take in pursuit of an opportunity (if it were judged to be (1) worthwhile pursuing and (2) the council was confident in its ability to achieve the benefits and justify the risk).

evaluated using the standard (5x5) risk matrix which involves multiplying the likelihood of occurrence of a risk (scored 1-5) by its potential impact (scored 1-5). This produces an evaluation of risk as either 'low (1-4)', 'medium' (5-9), 'high' (10-19) or 'very high' (20-25).

3.2   The Council's response in relation to adverse risk or its risk appetite is such that:

- Very High risk is unacceptable and measures should be taken to reduce, transfer or treat the risk to a more tolerable position;
- High risk may be tolerable providing the Council is assured that adequate and effective control measures are in place;
- Medium risk is tolerable with control measures that are cost effective;
- Low risk is broadly acceptable without any further action to prevent or mitigate risk.

3.3   The 2014 Corporate Risk Register includes one Very High risk, eight High risks and five Medium risks.

3.4   In accordance with the Risk Management Strategy 'Very High' and 'High Risks' identified in the Corporate Risk Register will be subject to closer scrutiny by the Council Management Team, the Cabinet and the Audit and Governance Committee.

4   POLICY IMPLICATIONS

4.1   In noting this report the Council will be ensuring that risk management principles, as detailed in the Corporate Risk Management Strategy are embedded across the Council.

5   EQUALITIES IMPACT ASSESSMENT

5.1   This report is not applicable to the well being of equalities groups and an Equalities Impact Assessment is not required.

6   RESOURCE IMPLICATIONS

6.1   Financial – The recurring costs associated with the measures in place for each risk are proportionate to the level of risk. The financial requirements to support the Corporate Risk Register for 2014 should be met within the proposed budget allocations. Any unplanned and unbudgeted costs that arise in relation to any of the corporate risks identified will be subject to review by the Corporate Management Team.

6.2   Personnel – There are no immediate implications.

6.3   Other – Effective implementation of this register will require the support and commitment of the Risk Owners identified within the register.

7   BACKGROUND PAPERS

7.1   Appendix 1 – Corporate Risk Register

AUTHOR'S NAME	Scott Kennedy	
	Paolo Vestri	
DESIGNATION	Emergency Planning and Risk Officer	
	Service Manager - Corporate Policy and Improvement	
CONTACT INFO	skennedy@eastlothian.gov.uk	01620 827900
	pvestri@eastlothian.gov.uk	01620 827320
DATE	28th August 2014	

East Lothian Council Corporate Risk Register (V16: 27th May 2014)

Risk Ref.	Risk Description	Existing Risk Control Measures	Assessment of Current Residual Risk			Planned Additional Risk Control Measures	Assessment of Predictive Risk			Risk Owner	Timescale for Completion / Review Frequency
			Likelihood	Impact	Total		Likelihood	Impact	Total		
			L	I	L x I		L	I	L x I		
ELC CR 1	Resourcing The Council is facing considerable financial pressures arising from the extended period of public finance constraint , at best "flat cash" revenue support grant awards and the freeze in Council Tax. Therefore, over the medium term it is highly likely that the Council's main funding income will remain static. At the same time it will have specific cost pressures to deal with. These include: (1) demographic change and social-economic pressures - increasing pupil and elderly numbers; (2) general inflationary pressures; (3) specific cost pressures such as the affordability of the increasing number of high-cost individual care packages; and (4) potential financial costs associated with legislative changes such as a number of environmental issues. Efficient Workforce Management, VERS, restructuring and budget restrictions could result in the services not being able to maintain a level of staff to allow the service currently provided to continue in its present form. Staff morale could be adversely affected because of increasing workload and unreaslistic expectations. The shape of the work force will continue to change as greater efficiency, productivity and more streamlined ways of working are embedded. If the council's financial pressures were not to be successfully planned for and managed effectively over the medium to longer term (i.e. the next 3 and possibly up to 7 years), there would be a serious risk of unplanned/ reactive budget realignments with significant adverse impact on availability and quality of both front-line services and required investment in the Council's infrastructure and asset base.	The Council has well developed short to medium term financial planning arrangements. These include: • Three year General Services revenue budgets; • Seven year General Services capital plan budgets; • Ten year Housing Revenue Account revenue and capital budgets. In addition, it has cost control and financial management arrangements for managing in year budget performance. Both of which provide mitigating controls in terms of the immediate financial risk and pressures the Council is faced with. Partnership working with Midlothian Council and other partners is being developed to increase capacity to provide services within existing resources. Longer-term modelling is deemed to be of limited value as the public sector financial environment is unlikely to be stable in other than the short and medium term. The focus is on creating a programme of short and medium term organisational change that can be adapted to match the Councils position as that emerges. The Chief Social Work Officer also has a role to play in overall performance improvement and the identification and management of corporate risk in so far as they relate to social work services. Communication between CMT and all employees regarding the impact of change. All VERS decisions were made following business impact assessments, with support given only to those applications with minimum business impact. The impact of VERS and Efficient Workforce Management was reported to Audit & Goernance Committee, 20th May CMT is working with Service Managers on service reviews to redesign services within resources.	4	5	20	CMT/Managers continue to follow the financial strategy i.e. cost control/ cost minimisation to ensure delivery of agreed savings. This is also being monitored closely through the Chief Executive's new Budget Review Group. Through the Corporate Asset Group, the Council implement will implement the approved Asset Management Strategy and related action plan. CMT will continue to monitor the impact of council restructuring and service re-design Further consideration will be given to increasing income where possible Staff communications is being reviewed to ensure that staff engagement improves The Workforce Development Plan is a key part of the Council's response to increasing financial pressures. It aims to support transformational change, build and sustain leadership and management capacity, sustain a skilled, flexible and motivated workforce and develop the workforce for the future.	3	4	12	Chief Executive Depute Chief Executive – Resources and People Services Head of Council Resources Council Management Team	Financial Pressures and VERS/restructuring risks combined to create this new risk in April 2014. Risk further reviewed by CMT in May 2014 and current score increased from 15 to 20. Further review planned throughout 2014.

Risk Ref.	Risk Description	Existing Risk Control Measures	Assessment of Current Residual Risk			Planned Additional Risk Control Measures	Assessment of Predictive Risk			Risk Owner	Timescale for Completion / Review Frequency
			Likelihood	Impact	Total		Likelihood	Impact	Total		
			L	**I**	**L x I**		**L**	**I**	**L x I**		
ELC CR 2	Duty of Care The Council has a responsibility to provide care and support for the people of East Lothian. Any breach of this duty of care may compromise health, safety and wellbeing, impacting on, for example, the protection of children and adults. Failure to fulfil the duty of care could also result in serious harm/death to an individual/s, prosecution, having to pay compensation and have a negative impact on the reputation of the Council. The duty of Care is at the heart of the Council's approach to risk management. The likelihood of this risk occurring is influenced by a range of factors including for example: (1) Complexity of partnership arrangements in the care sector; (2) Number of vulnerable people in East Lothian; (3) Levels of deprivation in East Lothian; (4) Increased population and more complex service demands presented by an increasing number of service users whilst resources have reduced. The introduction of Self Directed Care and the increased uptake of Direct Payments may present new challenges in relation to the service user choice and the application of PVG checks. **Adult Wellbeing**: More than half of the care provided is purchased from private and voluntary sector agencies. The risks associated with purchased care are well understood and monitored through contract compliance and monitoring of care providers in association with the Care Inspectorate. **Children's Wellbeing:** Duty of care operates in individual agency and partnership working with other universal and specialist agencies, some of which operate under contractual/service level agreements, all of which operate under defined professional standards of practice, policies and procedures and directly with families and carers all of which is monitored in association with Care Inspectorate and other inspection agencies.	**Corporately** There is an HR policy in place on procedures laid down by Disclosure Scotland and the Protecting Vulnerable Groups scheme and training sessions are in place for all managers and staff to make them aware of the policy and processes to be followed to comply with the PVG scheme. For Social Work and Health Services the Council follows safe recruitment procedures as described by the Care Inspectorate. Details of the posts which are subject to the Disclosure process are published on the Council intranet. Risk assessments and risk management are central to the care planning process. Frameworki and service specific systems are used to identify and record risk factors in a structured and consistent manner. E-Learning for all employees: GIRFEC, Child Protection and Adult Protection. Adult Wellbeing and Children's Wellbeing also have control measures in place	4	4	16	Implementation of Action Plans following on from Child Protection (single and multi-agency) and SWIA/Care Inspectorate inspections. Staged Assessment and Intervention practices continue to embed in multi-agency working practices. New obligations of the Children & Young People Bill introducing the 'Named Person' role will be further implemented during 2014/15. East and Midlothian Public Protection Committee (EMPPC) is being established (June 2014) There will be one standing sub-group which will focus on Performance and Quality across all areas and both partnerships and will have responsibility for developing and implementing a consistent framework for self evaluation, audit and scrutiny. Systems are being developed to take forward an integrated, "lifespan" approach to all aspects of public protection. This approach will provide innovative opportunities for a cohesive response and will support operational staff in partner agencies to safeguard and improve outcomes for the most vulnerable children and adults at risk of harm. Inspection of Services for Children took place in November 2013 and the Care Inspectorate's report on such was published on 10 April 2014. A multi-agency improvement plan will be developed by June 2014 and this will be reflected in the work of the Critical Services Oversight Group (CSOG), the ELP/RPP and also in the review of the Integrated Children's Services Plan.	3	4	12	Depute Chief Executive – Partnerships and Community Services Depute Chief Executive – Resources and People Services Director of East Lothian Health and Social Care Partnership Critical Services Oversight Group	Risk reviewed and updated April/May 2014 with further review planned throughout 2014/15.

Risk Ref.	Risk Description	Existing Risk Control Measures	Assessment of Current Residual Risk			Planned Additional Risk Control Measures	Assessment of Predictive Risk			Risk Owner	Timescale for Completion / Review Frequency
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			L	**I**	**L x I**		**L**	**I**	**L x I**		
ELC CR 3	Information Security and Data Protection Failure to have comprehensive council wide Information Security Management measures in place will put at risk the availability, integrity and confidentiality of the councils information and may cause a Council wide failure of central I.T. systems (incl. Telephony) caused by a malicious attack by hackers, virus, trojan, disclosure of information or Fire/Flood event. The Cabinet Office has introduced zero tolerance for all LA's connected to the PSN network. All Scottish LA's use the PSN to register Births, Marriages & Deaths and connection to DWP for benefit provision. We have to re-accredit to this network every year and must meet stringent requirements. Failure to do so would mean disconnection from the PSN. Breach of the Data Protection Act, other confidentiality requirements, any relevant laws or duty of care through the loss or wrongful transmission of information (including information stored electronically) could result in - harm to individuals; - legal action; - fines of up to £500,000. - requirement to pay compensation; - adverse publicity; - damage to reputation.	ISO 27001:2013 is the international standard for management of Information and I.T. Security. East Lothian Council uses this standard as the framework for its Information & I.T. Security Management system. This includes objectives, overall policy framework, internal audit, organisation and management support and treatment, training and awareness, risk assessment, measurement of effectiveness, management review, non-conformity management and continual improvement. As part of the security controls required by the standard to mitigate risks, several control areas are set out : Information security policy; Information security organisation; Human resources security; Asset management; Access controls and managing user access; Physical & Environmental security of all sites/equipment Secure communications, Data handling and Data Protection (including paper documents etc); Secure acquisition, development, and support of information systems; Security for suppliers and third parties; Information Security Incident management; Business continuity/disaster recovery (to the extent that it affects information security) – I.T. disaster recovery plan in place; Compliance - ELC takes measures to avoid breaches of law, statutory, regulatory or contractual obligations (incl. DP Act and Public Records Act). There is a Council IS Forum hosted by the IT Security Officer. IS, DP and Records Management Awareness training now forms part of our induction process for new employees. Data Protection and Information Security awareness training is mandatory for all employees and must be renewed every two years.	4	4	16	Information Security and Data Protection training now mandatorily part of induction completed August 2013 while existing employee roll out is to start July 2014 for IS training. Online system is being updated and allows for reporting on who has completed training and when. Regular IT health checks of PSN requirements on the existing infrastructure will be carried out quarterly commencing June 2014. New systems being introduced to our infrastructure will be risk assessed and security checked before introduction to ensure they meet criteria. The Data Protection Officer has started an ongoing series of "health checks"/audits with various Council departments to ensure compliance and to improve practice. The Council's Records Management Plan is to be adopted later in 2014 and will be a 5 year plan covering how the Council manages its records and will include links to our existing information security and data protection policies.	3	4	12	Depute Chief Executive – Resources and People Services Head of Council Resources	Information Security and Data Protection risks combined to create this new risk in April 2014. Risk to be reviewed in November 2014 following commencement of employee training roll out, PSN checks and adoption of Council Record Management plan.
ELC CR 4	Climate Change As the incidence of flooding and coastal erosion increases as an impact of Climate Change, there is an increased risk of disruption to road and path networks, impact on public safety, damage to roads, property, harbours and natural heritage sites and an associated increase in claims against the Council.	Flooding and drainage issues are considered when processing planning applications. Inspection regimes and good housekeeping measures in place and working effectively. The Severe Weather Response Plan has been developed over the past few years and ensures a co-ordinated and consistent multi-agency response across the county. Emergency surface water, coastal and river flood procedures in place and have proven effective. Shoreline Management Plan has been produced and Flood Risk Management Strategy and Plans are being prepared to meet the requirements of the Flood Risk Management (Scotland) Act 2009.	4	4	16	The Council is working with the Community Councils to promote and progress "Resilient Communities" as per the Scottish Government initiative "Ready Scotland". Improved communication with vulnerable groups regarding access and assistance during severe weather events. ELC have commissioned Flood Studies for Haddington and Musselburgh and are to engage a consultant to further develop Flood Protection works on the River Tyne	3	3	9	Depute Chief Executive – Partnerships and Community Services Depute Chief Executive – Resources and People Services	Risk reviewed March 2014

Risk Ref.	Risk Description	Existing Risk Control Measures	Assessment of Current Residual Risk			Planned Additional Risk Control Measures	Assessment of Predictive Risk			Risk Owner	Timescale for Completion / Review Frequency
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			L	**I**	**L x I**		**L**	**I**	**L x I**		
		Flooding advice is given on the Council website and directs people to the relevant pages on the SEPA website.				and Esk, The implementation of Flood Protection Works is reliant on funding availability.					
ELC CR 5	Duty of Care to Council Staff (Health & Safety) East Lothian Council has a duty of care to all its employees across the full range of services and those who can be affected by the Council's activities. Any breach of this duty of care may affect the health, safety and wellbeing of the Council's employees leading to increased sickness absence, pressures on service delivery with the added potential for claims against the Council for incidents involving employees or non-employees. Lone Working Failure of the Council to provide employees with an effective Lone Working Policy & Practice and the appropriate training could result in injury or death to those employees resulting in H&S prosecution, civil insurance liability, reputational risk, increased sickness absence, pressures on service delivery and also potential claims against the Council. Safe Driving at Work "Health and Safety Law applies to on the road work activities as to all work related activities and the risks should be managed within a health and safety management system". Failure to implement a Safe Driving at Work (SDAW) Policy and Guidance to ensure that the Council meets current Health & Safety guidelines and the Corporate Manslaughter and Corporate Homicide Act 2007 could result in the Council facing a significant fine and/or legal action if a serious road accident were to take place involving any driving operation undertaken by employees or Elected Members using personal, Council or hired vehicles, as well as any volunteers, agency workers or other authorised parties driving Council fleet vehicles, in connection with Council business.	Quarterly Joint Health and Safety Committees oversee the Health and Safety Agenda of Council. This is supported by Departmental committees examining health and safety at a department level. All Health and Safety Training needs identified from project plans and Risk Assessment Findings. Safety Management System is in place and is supported by audit and inspection programme across all areas of the Council. Managing attendance and Managing sickness Absence Policies in place. Training for managers in managing attendance and sickness absence in place. Quarterly reviews of Occupational Health Service referral levels take place. Monthly Occupational health contract and work level review takes place along with a review of service need and demands. Lone Working Information on Lone Working Policy is part of the Service Level Induction process. All employees have received training on the use of the ELC lone working system. Specific procedures are in place in services with a high level of lone working such as Children's Wellbeing and Revenues, including risk assessments and electronic diaries and signing in/out books. Safe Driving at Work A Safe Driving at Work policy and a Guidance Manual has been drafted by the SDAW Group to ensure that safe driving principles are embedded across the Council. The draft policy will be issued for consultation and once approved will be publicised to all staff and implemented. Arrangements in place to ensure the reporting and recording of all accidents and incidents arising from work related driving as well as identifying and implementing remedial actions following road traffic accidents. Council vehicles used in the course of Council activities properly maintained and fit-for-purpose. All Council vehicles to be maintained in accordance with VOSA publication "Guide to Maintaining Roadworthiness".	3	5	15	Duty of Care towards Council staff (including Health & Safety) H&S Policy, Management Arrangements, Approved Guidance and Training Suite being created which builds into a H&S competency framework which will then be audited. Training will be identified from Risk Assessments and delivered timeously and built into H&S competency framework. Children's Wellbeing Lone Working policy and procedures continue to embed within Children's Wellbeing managers and admin staff ensuring that front line employees adhere to Lone Working controls. Senior Management Group will take over functions of Lone Working Group in monitoring use and reviewing current procedures. Revenues Re-introduce mobile technology with GPS tracking. All The Council is working towards creating a Potentially Violent Clients Register which will enable the sharing of information relating to potentially violent clients across customer facing teams which in turn allows managers to identify and implement appropriate control measures protecting employees from harm. Safe Driving at Work Implement and continually review Policy and Guidance through the Safe Driving at Work Group.	2	5	10	Head of Children's Wellbeing Head of Adult Wellbeing Service Manager – Revenues SDAW Group Depute Chief Executive – Partnerships and Community Services	Risks on Lone Working, Safe Driving at Work and Duty of Care amalgamated into one Duty of Care (H&S of employees) Risk in May 2014 at the request of CMT. To be fully reviewed December 2014 following implementation of SDAW Policy and Guidance during 2014.

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			L	I	L x I		L	I	L x I		
ELC CR 6	Development Plan Failure to maintain an up-to-date Local Development Plan could lead to a shortfall in the effective 5 year housing land supply to meet the needs of our growing population and a lack of control over planning decisions due to planning by appeal. This could lead to unplanned development at odds with the Council's planning strategy for East Lothian, and consequent reputational damage. It could also contribute towards the Council not being able to achieve its Council Plan objectives – Growing our Economy and Growing our Communities – and related Single Outcome Agreement objectives. The Local Development Plan is also required to support and guide the provision of infrastructure required to meet the needs of our growing population and growing economy.	Staffing levels and other resources are stretched in fulfilling the task. Preparation of Main Issues Report and Local Development Plan is a Policy & Projects Business Plan objective (ongoing review). Details are set out in the Local Development Plan Scheme with timescales. ELC and SESplan Development Plan Schemes commit to a programme of Development Plan review (reviewed annually). SESplan Joint Committee, Project Board and Steering Group guide joint authority preparation of Strategic Development Plan for Edinburgh and SE Scotland. Community Planning Partnership liaison and involvement through East Lothian Strategic Land Use Planning Group.	5	3	15	Delay to the MIR will be contained by maintaining existing LDP timescale, achieved by shortening consultation timescales from 12 weeks to 6 (statutory minimum) Detailed timeline being drawn up for MIR/consultation/LDP key stages, including internal consultation and allocation of tasks to staff	2	3	6	Planning Manager	Monthly Fortnightly
ELC CR 7	Public Sector Reform Major elements of public sector reform have been or are being implemented including: • The creation of a national police force and a national fire service; • Integration of Health and Social Care and creation of a new H&SC Partnership; • Review of Community Planning; • New legislative duties in relation to procurement, community empowerment, regulation, and children and young people. These reforms create uncertainty, additional workload for senior staff, a requirement to restructure services and create new accountability, governance and partnership arrangements. There is continuing uncertainty about the future governance of Scotland, the future structure and governance of local government and the public sector and continuing pressure on public finances. The cost of implementing changes arising from legislation is not always fully reflected in Scottish Government funding. Whilst these risks are dealt with in detail in service risk registers there is a corporate level risk that the Council will not have the resources to fund these changes or the capacity to prepare for all these reforms simultaneously.	Effective working relations with key partners including Lothian & Borders Police, Lothian & Borders Fire and Rescue Service, East Lothian CHP and the voluntary sector are being further developed through regular meetings to prepare for public sector reform. The Council Management Team and Council / Cabinet receive regular reports on the implications of the reform proposals and on the Council's preparations. Planning processes are led by the Chief Executive. Responses to the Scottish Government on consultations around public sector reform are prepared and submitted as required. Financial and resource scoping is carried out as required. Systems for operational, performance and financial management and scrutiny are being prepared. The new Community Planning Partnership structure established in September 2013 provides a more strategic focus for the CPP. The Single Outcome Agreement Development Plan prioritises early intervention, tackling inequalities, joint resourcing, and joint asset management. The scrutiny and accountability arrangements for Police and Fire services, shared between Council and the Safe and vibrant Communities Partnership were established in April 2013. The Shadow Health and Social Care Partnership was established in April 2013 and work is progressing on developing the Integration Plan and Commissioning Strategy for the Partnership in line with the guidance and timetable. The milestones will be closely monitored by the HSCP Board and Officers of East Lothian Partnership on a	4	3	12	Continue to monitor developments in the Public Sector Reform agenda and Scottish Government's legislative programme and develop responses to exploit potential benefits from, or mitigate potential negative impacts of, different future scenarios CMT and elected members will work together to ensure that the Council is prepared for future public sector reform and the differing scenarios for future governance arrangements.	3	3	9	Chief Executive	Risk reviewed and refreshed April/May 2014. Ongoing action. Risk to be reviewed Feb 2015.

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			L	I	L x I		L	I	L x I		
		monthly basis and effective action will be agreed to ensure any misalignment from the agreed milestone is addressed. This will be evidenced by the minutes of meetings which will include an action plan that identifies who is responsible, a timeframe for completion and details of remedial actions.									
ELC CR 8	Welfare Reform

The UK Government is introducing a range of measures to reform the welfare system and reduce the budget for welfare benefits by at least £11 billion annually. It has been estimated (Scottish Local Government Forum Against Poverty, Sept 2010) that the changes could result in the loss of £8m - £9.5m annually from welfare benefits paid to East Lothian residents.

The changes could lead to:

• Increase in rent arrears from reduced Housing Benefits and possible increase in evictions

• increased pressures on tenancy support and rent collection teams

• increase in homeless presentations, placing even more pressure on already stretched resources for temporary accommodation

• increase in Council Tax arrears and non-payment of Council Tax

• increase in caseload for Adult Wellbeing and Children's Wellbeing staff dealing with vulnerable people affected by cuts in benefits

• increase in caseload and demand for services from the Welfare Rights Service

• loss of income the Council currently receives for administering Housing Benefits | The Council has received several update reports and will continue to be updated.

The Council has established a Welfare Reform Task Group to plan for changes to the welfare system. The Task Group has a detailed action plan to ensure that the Council takes the necessary measures to prepare for welfare system changes.

The work of the group has been based around communications; data sharing; training; and migration to the new benefits system such as the establishment of the Scottish Welfare Fund.

The Task Group and workstreams are meeting regularly and will continue to report back to the Council Management Team and to the Council. Key actions that have been completed include:

• establishing processes and procedures for distributing the Scottish Welfare Fund

• revising the Discretionary Housing Payments policy and distributing the additional allocation to tenants affected by the new single occupancy rules

• providing training for Council staff on welfare reforms

• providing information about welfare reforms to the general public through the Council website (e.g. the welfare reform videos), Living newspaper and Homefront magazine

• successfully applying for funding from the Scottish Legal Aid Board for Tenancy Support Officers. | 4 | 3 | 12 | The Council's Welfare Reform Task Group is revising and updating its Action Plan and will continue to implement the plan to mitigate the impact of welfare reform.

An action to mitigate the impact of welfare reform on rent arrears will be developed and progress will be monitored by a senior level task group chaired by the Depute Chief Executive – Partnerships and Community Services | 3 | 3 | 9 | Depute Chief Executive – Resources and People Services

Welfare Reform Task Group | Risk reviewed April 2014. Current score reduced from 16 to 12 and predicted score reduced from 12 to 9.

Risk is under constant review by the group. |

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			L	I	L x I		L	I	L x I		
ELC CR 9	Public Protection East and Midlothian Public Protection Committee (EMPPC) is being established with effect from June 2014 to replace the current Adult Protection Committee, Child Protection Committee, Offender Management Committee and Violence Against Women Partnership and to ensure robust links with Midlothian and East Lothian Drug and Alcohol Partnership (MELDAP). A failure in this new committee or any problem caused by the increased complexity of its work or it being unable to fulfil its statutory duties/duty of care could result in a service user suffering harm or detriment. This would result in reputational damage to and increased scrutiny of the Social Work service. If a service area is given higher priority than another area then people may be left at risk of harm.	Policies and procedures are in place. Governance and scrutiny arrangements in place through Critical Services Oversight Group (CSOG). Established performance monitoring and reporting mechanisms.	3	4	12	Review all policies, procedures and governance arrangements in light of integrated Public Protection model. Develop co-ordinated approach across all areas, Implementation of revised Public Protection structure will strengthen governance and scrutiny.	2	4	8	Public Protection Team Manager Senior Manager Operations Head of Adult Wellbeing East and Midlothian Public Protection Committee	Risk created May 2014 and to be reviewed following establishment of committee.
ELC CR 10	Severe Weather There is a risk that an extended period of very cold weather or snow such as that which occurred in November to December 2010, will lead to a demand for gritting and clearing of footpaths in all areas which exceeds normal capacity and supplies of salt. This could result in travel disruption, difficulties for people in accessing services, failure to maintain refuse collection timetable and school closures at short notice as well as a possible increase in insurance claims related to pothole damage.	The Infrastructure Winter Maintenance Plan has been in place for some time and ensures that main transport routes are treated as priority. The Council Severe Weather Response Plan has been developed over the past few years and ensures a co-ordinated and consistent multi-agency response across the county. There is a claims protocol in place within the Insurance section. Council's Salt Barn has a capacity of 8,000 tonnes to meet demand arising from severe cold weather. Snow clearing equipment has been supplied to Primary Schools and Community Councils on request. A number of grit bins are provided to enable self-help gritting of adopted roads and footways. Winter Maintenance Duty officers trained as Winter Service Supervisors to City and Guilds level.	3	3	9	Training and awareness sessions for staff. The Council is working with the Community Councils to promote and progress "Resilient Communities" as per the Scottish Government initiative "Ready Scotland". Several Community Councils have started to create their own emergency response plans. A workshop, hosted by East Lothian Council, to further progress Resilient Communities, for the benefit of Community Councils, will take place in October 2014.	3	3	9	Depute Chief Executive – Partnerships and Community Services	Risk reviewed March 2014

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			L	I	L x I		L	I	L x I		
ELC CR 11	Energy and Carbon Management There is a risk of reputational harm (in terms of corporate social responsibility) and the potential for significant unbudgeted costs and financial penalties if the Council does not meet Climate Change (Scotland) Act 2009 (CC(S)A 2009) statutory obligations (increasing cost of Carbon Credits). Examples of this risk include: • More expensive travel due to increase fuel costs and taxes • Rising energy costs due to oil and gas price increases and Carbon Reduction Commitment (CRC) • Less energy security due to potential UK and worldwide resource constraints for fuel and electricity.	A Carbon Management Plan (2009-14, extended to 2015) is in place, which aims to achieve emissions and cost reductions set out by the Scottish Government and the Council. Progress is reported annually, and includes a number of energy efficiency and management projects. The current carbon management plan covers the period 2009-14. It was agreed at the Carbon Management Board meeting in December 2012 that the current CMP would be extended to 2014/15. The Council is on target to meeting the 25% reduction target. However, the Climate Change (Scotland) Act interim carbon target is 42% reduction by 2020. It will become increasingly harder and more costly to meet the target, as the easy wins have been identified and implemented.	3	3	9	Review and update the Carbon Management Plan 2016-2020	3	3	9	Depute Chief Executive – Partnerships and Community Services	Risk reviewed March 2014
ELC CR 12	Standards in Public Life Failure of corporate governance or to meet standards in public life. Failure of the Council's corporate governance or of officer or members to meet standards in public life could result in reputational damage.	The main internal controls are the Council's Code of Corporate Governance, the Annual Governance Statement, Standing Orders, Scheme of Administration and Financial Regulations. Standing Orders (the Schemes of Administration and Scheme of Delegation) were extensively revised and approved by Council in August 2013. Other changes include the role of statutory officers and job outlines for senior officers. The conduct of elected members and employees is governed by Codes of Conduct. The Audit and Governance Committee also has a role in promoting good governance. The Council's Monitoring Officer and legal advisers provide advice as required. A programme of briefings for Elected Members has been established during 2013 with an event scheduled at least once every two months during the current committee session (2013/14). Briefing topics include: Code of Conduct, Health Inequalities and Suicide in East Lothian. The Council is developing its links with the Local Area Network of audit and inspection agencies and with its Auditors.	3	3	9	Dates have already been earmarked for briefings to Elected Members to continue during the session 2014/15. The majority of the briefings will be delivered by external professionals such as Audit Scotland and the Standards Commission. Elected Members will have a further opportunity to participate in the Improvement Service's CPD programme.	2	3	6	Depute Chief Executive – Resources and People Services	Risk reviewed March 2014. Actions ongoing through 2014/15. Risk to be reviewed March 2015.
ELC CR 13	Business Continuity Non availability of: • premises, through fire, flood or other incident; • key staff or significant numbers of front-line staff for any reason including a Pandemic; and/ or • systems (IT, telephony, power failure etc)	Business Continuity Framework Plan in place and regularly reviewed. This corporate document reflects information from each service continuity plan and contains information required to prioritise relocation of council services and restoration of critical services. Business Continuity Plans are produced by all service areas, giving details of minimum levels of staff, alternate locations, exercise and review dates and version control.	2	4	8	An IT Disaster Recovery Plan to be written which will cover Disaster Recovery arrangements for the Council's main data centres (JMH & Penston House). Management Information software has been purchased and will assist in the maintenance and review process of all plans once fully	2	3	6	Depute Chief Executive – Partnerships and Community Services Depute Chief Executive – Resources	Fuel shortages risk included within Business Continuity risk in April 2014 and new risk reviewed and updated with amended planned measures reducing predicted score

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			L	I	L x I		L	I	L x I		
	• any form of transportation due to a fuel shortage The occurrence of any of these will have an adverse effect on the Council to function fully and to carry out our statutory requirements.	IT –specific disaster recovery arrangements in place for the critical systems – e-mail and social care. These have duplicate services in place off site which can be brought into action if we lost the main data centre at JMH. For single server failure - there are over 100 systems now running on virtual servers which automatically fall over to another server if there are hardware issues. Controls that are in place to prevent and limit the effects of IT system unavailability including firewalls, anti-virus software, system/ data backup routines, and resilience in the form of a back-up generator for the main data centre at JMH. The Council has a Fuel Plan in place and is able to call a Fuel Group at anytime. Fuel supply held at our depots and can be sourced externally from local fuel service stations and through shared services with other Local Authorities.				operational. Regular monitoring of current fuel stock and assessment of any weather predictions, political developments or industrial action etc that may affect fuel availability.				and People Services	from 8 to 6.
ELC CR 14	Equality Failure to meet duties and legislative requirements of the Single Equality Act 2010 The Single Equality Act 2010 and related guidance places a general duty on public authorities to be active in promoting equality, eliminating unlawful conduct and fostering good relations. It also places specific duties on public authorities to • report on mainstreaming the equality duty • publish equality outcomes and report progress • assess and review policies and practices • gather and use employee information • publish gender pay gap information • publish statements on equal pay • consider award criteria and conditions in relation to public procurement • publish in a manner that is accessible. There is a risk that the Council may not be able to meet its general or specific duties and in particular at a time when difficult budget decisions are having to be made that there will be cuts in services or increases in charges that have a disproportionate impact on people who may need those services most because of their equality background. The Council would be open to legal challenge of not meeting its duties and in particular of not carrying out adequate assessment of impact of policies and budget decisions.	ELC Equality Plan in place and available online A new Combined Impact Assessment Process has been developed with Midlothian Council and NHS Lothian to support the Council to meet its legal duties. HR is capturing the employment monitoring information required under the Act and reporting it appropriately. E Learning equalities modules are available on Learn Pro and 'Get in on the Act' guides to the Council's legal responsibilities are available for all employees and Elected members.	2	4	8	Embedding of new Combined Impact Assessment procedure across all Council services, including new online learning modules and face to face briefings. Equality Impact Assessment carried out as part of the budget preparation process. Equality indicators included as part of the Performance Framework and SOA indicator set	1	4	4	Depute Chief Executive – Partnerships and Community Services	Risk reviewed and refreshed March 2014, to be further reviewed December 2014.

Original date produced (Version 1)	13 April 2011		
File Name	East Lothian Council Corporate Risk Register		
Original Author(s)	Scott Kennedy, Risk Officer		
Current Revision Author(s)	Scott Kennedy, Risk Officer		
Version	Date	Author(s)	Notes on Revisions
1	13/04//2011	S Kennedy	Original Version
2	05/12/2011	S Kennedy	2nd version made available to BoD for review
3	23/08/2012	S Kennedy	Draft version updated
4	15/11/2012	S Kennedy	Updated following BoD meeting and Strategy update
5	07/12/2012	S Kennedy	Updates received from services following BoD recommendations
6	18/12/2012	S Kennedy	Updated with additional risks.
7	04/01/2013	S Kennedy	Updated following consideration by CMT
8	09/05/2013	S Kennedy	EP &BC Risks updated
9	31/07/2013	S Kennedy	Data Protection Risk Added
10	01/11/2013	S Kennedy	Welfare Reform Risk updated (no change to score)
11	04/03/2014	S Kennedy	New Corporate Risks added on Safe Driving at Work, VERS, Fuel Shortages and Lone Working
12	March/April 2014	S Kennedy	All risks reviewed, refreshed and scores updated where required.
13	11/04/2014	S Kennedy	New Corporate Risk on Integration of Health &Social Care and Adult Wellbeing added.
14	25/04/2014	S Kennedy	Amendments following consultation with CMT and Risk Authors
15	01/05/2014	P Vestri	Amendments following review of latest draft by Chief Executive and Depute Chief Executives.
16	27/05/2014	S Kennedy	Final amendments following consultation with CMT and Risk Authors including addition of Development Plan and Public Protection risks

Risk Score	Overall Rating
20-25	Very High
10-19	High
5-9	Medium
1-4	Low

East Lothian Council

REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Depute Chief Executive (Partnership and Services for Communities)

SUBJECT: An Overview of Local Government in Scotland 2014 (Accounts Commission, March 2014)

6

1 PURPOSE

1.1 To review East Lothian Council's position in relation to the findings of the Accounts Commission report, *'An overview of local government in Scotland 2014'*

2 RECOMMENDATIONS

2.1 The Committee should note the position of East Lothian Council in regard to the findings and recommendations of the Overview of Local Government in Scotland 2014, as detailed in the Appendix and identify any further information or scrutiny activity it would wish to have reported back to future meetings of the Audit and Governance Committee.

3 BACKGROUND

3.1 Each year the Accounts Commission produces an overview of issues that have arisen from the local authority audits conducted by Audit Scotland. The Overview assists councils in identifying and planning for pressures that they may face in the coming year.

3.2 The Overview highlights priorities for 2014 that have been identified through the work of Audit Scotland, in particular:

- Understanding the changing context and the crucial role of councillors

- Meeting user demands and the financial challenges, and

- Providing strong leadership and governance to support change

3.3 Each priority is supported by a number of specific recommendations. The key findings and recommendations of the report are outlined in the

Appendix to this report. A summary of the position of East Lothian Council in regard to each recommendation, including relevant actions points that have been included in the 2014/15 Council Improvement Plan, is also provided in the Appendix.

4 POLICY IMPLICATIONS

4.1 Councils are required under the Local Government in Scotland Act 2003 to achieve Best Value in regard to economy, efficiency, effectiveness, equal opportunities and sustainable development. The 'Overview of Local Government in Scotland 2014' will assist the Council in recognising the challenges that it faces in achieving Best Value in the future.

5 EQUALITIES IMPACT ASSESSMENT

5.1 This report is not applicable to the well being of equalities groups and an Equalities Impact Assessment is not required.

6 RESOURCE IMPLICATIONS

6.1 Financial – none.

6.2 Personnel – none.

6.3 Other – none.

7 BACKGROUND PAPERS

7.1 Appendix: Findings and East Lothian Position and Actions

7.2 'An Overview of Local Government in Scotland 2014', Accounts Commission, March 2014

AUTHOR'S NAME	Andrew Strickland
DESIGNATION	Policy Officer
CONTACT INFO	astrickland@eastlothian.gov.uk
DATE	15th August 2014

Appendix: Overview of Scottish Local Government Findings and East Lothian Position and Actions

1. Understanding the changing context and the crucial role of councillors

Maintaining a clear understanding of the financial position	
Audit Scotland findings	*East Lothian Council position and actions*
Audit Scotland found that spending by local government broadly matches its current income from government grants, council tax, charges for services and the application of reserves. However, the Overview report goes on to note that 'Upward pressures on the costs involved in providing services, including energy costs, waste disposal and maintenance, are continuing and need to be managed alongside increasing expectations and demands for services'.	The Council's Financial Strategy 2014/15 to 2016/17 notes that:
	As far as possible, the Council is seeking to contain costs by becoming more efficient, which would minimise the effect on services provided. However, the size of the medium-term deficit suggests that more significant changes in how services are managed and delivered will be required as the means of containing costs whilst maintaining and where possible improving services in accordance with the Council Plan and SOA.
The report states that: 'Local government's share of the Scottish budget has remained fairly constant but, for revenue funding, translates to a real terms reduction, ie after factoring the effects of inflation.'	The Strategy includes commitments to:
The report provides examples of increasing demand for services:	• Develop a sustainable General Services budget avoiding the use of reserves in 2016/17
Older People: Demand is increasing because people are living longer with more complex needs. Resources need to be targeted at preventing illness and helping people to live at home.	• Deliver a Change Programme that will achieve significant efficiency savings across all areas and all inputs such as staffing and supplies;
Housing: Housing faces increasing demand for supported living as a result of the ageing population, an increase in number of single person households, and demand resulting from welfare reform.	• Constrain cost growth through effective demand management, good financial control and by effective negotiation with suppliers.
Equal pay: Two thirds of councils anticipate further equal pay costs that cannot yet be quantified.	The 2013/14 Council Improvement Plan included an action to 'Review and further strengthen the Council's financial management process'. In accordance with agreed actions arising from the annual audit process, a number of improvements have now been implemented e.g. introduction of a new Efficiency Progress Rating that supplements the existing Financial Risk Rating.
Roads: Increasing maintenance costs for roads and other assets, increasing demands from flooding and winter maintenance.	The 2013/14 financial outturn shows that fewer reserves were required than planned and the 2014/15 to 2016/17 budgets are balanced using fewer reserves than previous budgets.

Understanding the public reform agenda, including the impact of welfare reform (Public service reform provides challenges and opportunities for new approaches to services)	
Audit Scotland findings	*East Lothian Council position and actions*
'Alongside demand and resource pressures in services, councils are at the centre of wider public service reforms introduced by the Scottish Parliament and by the UK Parliament. The Scottish Government's approach is founded on 'four pillars' for change: shifting resources towards prevention; integrated local services through better partnership working; workforce development; and transparent and improving performance.'	**Establishment of single Police & Fire services:** The Council has put in place arrangements for scrutiny and engagement with the national Police and Fire services. Council received a report in April 2013 entitled 'Police and Fire and Rescue Services: Arrangements for Public Scrutiny and Engagement'. The report described the role of Council in the scrutiny of the Police and Fire services. The report also outlined the role of the Safe and Vibrant Communities Strategic Partnership in monitoring progress towards the achievement of outcomes from the Single Outcome Agreement.
The report highlights a number of public sector reforms that impact upon local government:	
Establishment of single Police & Fire services: Councils are working with their local commanders (police) and local senior officers (fire and rescue) to develop approaches to local scrutiny and engagement, including links to community safety partnerships and CPPs.	**Welfare Reform Act 2012:** The Council has established a Welfare Reform Task Group that includes representatives from a variety of Council services. The Task Group has developed an action plan to address the implications of Welfare Reform. Cabinet has also received regular updates on Welfare Reform, including the impact of cuts in Housing Benefit on rent arrears. The Council has successfully taken responsibility for the Scottish Welfare Fund in East Lothian and has disbursed the additional allocation for Discretionary Housing Payment to mitigate the impact of the reduction of Housing Benefits.
Welfare Reform Act 2012: Uncertainties remain that make it difficult for councils to plan ahead, particularly in relation to the shift from housing benefits to universal credit and the level of support they are expected to provide to customers in future. Scottish Parliament estimates suggest that £1.6bn will be taken out of the Scottish economy as a result of welfare reform, with the most deprived areas facing the largest impact.	
	The Council has established a Welfare Reform Reference Group with key partners. Members of this group include; Housing Associations, Health, East Lothian, DWP, and advice agencies. Quarterly meetings of the group provide the opportunity for welfare reform updates and information sharing.
Community Empowerment Bill: The proposals highlight the important role that communities can play in participating in new models of service delivery and developing models of 'co-production' that draw upon the knowledge, skills and experience of local people in ways that maximise the impact and value of public assets.	**Community Empowerment Bill:** East Lothian Council has established a model of local community planning based on the establishment of Area Partnerships in each of the Council Wards. The Council has transferred Community Centres to volunteer management committees and is supporting the establishment of community based Social Enterprises.

Preparing for changes in health and social care	
Audit Scotland findings	**_East Lothian Council position and actions_**
Audit Scotland highlight the need for barriers to partnership working between health and social care services to be addressed. Audit Scotland stress the importance of a joint vision and clear priorities for the use of shared resources.	Council received a report in April 2013 outlining the development of a Shadow Integrated Health & Social Care Partnership and Board (Integration of Health and Social Care: Proposed Shadow Partnership Arrangements), including the appointment of a Joint Director. The report noted that:
	'_The Shadow Partnership will focus on rethinking the model of health and social care services in East Lothian taking account of the changing demographic profile of the area, financial restraint on the Council, the NHS and our partners, and opportunities to improve the health and wellbeing of our communities._'
	A further report on Health and Social Care Integration was considered by Council in June 2014 and Council agreed to adopt the body corporate model for the Partnership.
	A project board is preparing the Integration Scheme and draft Strategic Plan to be published within the timescales set by the government.
Keeping up to date through training and development	
Audit Scotland findings	**_East Lothian Council position and actions_**
Audit Scotland found that there is a demand and need for more training for councillors. The report highlights that councillors have 'a complex and demanding role, made more so in the current context where reduced budgets mean that choices and decisions are more difficult.'	Five elected members have signed up for the Continuous Professional Development (CPD) programme. In 2013 members of the Audit & Governance Committee were provided with CIPFA training on the role of the Audit Committee.
	The 2014/15 Council Improvement Plan includes actions to provide 'Scrutiny training for members of the Policy and performance Review Committee' and to 'Review and develop elected members' training and briefings based on Councillors' responses to a survey based on Audit Scotland Overview of Scottish Local Government Councillors' Checklist.'

2. Meeting user demands and the financial challenges

Appraising the options for delivering services and charging for services	
__Audit Scotland findings__	*__East Lothian position and actions__*
Audit Scotland note that councils should make greater use of options appraisal. While options appraisal is used in some circumstances it has the potential to be used much more consistently as part of the decision-making process. Audit Scotland also investigated councils' approaches to charging for services. Councils need to ensure that they have a clear policy for charging, which is regularly reviewed in consultation with communities and service users.	The Council has recently reviewed its approach to Best Value Reviews. A framework for undertaking Best Value Reviews has been developed, which includes an element of options appraisal. The 2014/15 Council Improvement Plan includes an action to: 'Review and revise the Improvement Framework and make more effective use of benchmarking, develop guidance and training on the use of benchmarking, Best Value reviews and options appraisal.' Audit Scotland's report 'Charging for services: are you getting it right?' suggested that East Lothian Council raised a relatively low proportion of its income from charging when compared to other councils in Scotland. The Council has embarked upon a benchmarking exercise to compare its charges and fees against those set by other councils.
Requiring good-quality cost and performance information for decisions and scrutiny, & **Making better use of benchmarking to support service improvement and public reporting**	
__Audit Scotland findings__	*__East Lothian position and actions__*
'Councils are working to review and refine performance arrangements. However, more needs to be done to ensure the quality of performance information and that there is clear read-across between the information which is collected and councils' objectives, so that progress can be measured.' Priorities include providing more information on costs alongside service performance information to help assess value for money. Performance reports should also identify and prioritise areas for improvement. Audit Scotland suggest that reports should	Members of the Council's Policy and Performance Review Committee have reviewed the Council's Key Performance Indicators (see reports to PPRC January 2013 and April 2013). The aim of this review was to ensure that the indicators related to the Council's priorities and outcomes. The review also allowed members to provide feedback on the presentation of the data to the public and the Committee. The Council's approach to reporting performance information is outlined in the Improvement Framework. The Council's Key Performance Indicators are reported publically via the Council website. Data is shared between the

evaluate the impact of improvement activity, including the impact of self-evaluation.	Council's performance management software and the main Council website, which means that the data reported on the website is always as up-to-date as possible. The performance website displays trend data, targets, comments and (where available) comparative data for each indicator. Further improvements to the presentation of performance data will be considered including the increased use of narrative, contextual and comparative information.
Improvements required on public performance reporting include: • More narrative and contextual information • More use of targets, trends, progress with initiatives or actions being taken to address underperformance	
Audit Scotland suggests that 'A key element of Public Performance Reporting is comparing performance with other councils. Consistent with the improvements in Public Performance Reporting generally, more councils are including this as part of their reports. However, fewer than half of councils include information showing how they are performing relative to other councils.'	A recent report to the Accounts commission showed that the Council fully met the requirements for performance reporting in 14 out of 18 criteria, placing fifth amongst 32 councils. The report went on to cite the council's Annual Performance report as an example of good practice in four areas.
The report also highlights that 'the Local Government Benchmarking Framework will facilitate comparisons on spend and performance between similar councils so that councils can identify strengths and weaknesses, learn from councils that seem to be doing better and improve their performance.'	The introduction of the Local Government Benchmarking Framework has provided additional information regarding service costs. The results for the indicators contained within the Framework have been reported to the Policy & Performance Review Committee. The Council is participating in two pilot benchmarking exercises that are being co-ordinated by the Improvement Service.
	The 2014/15 Council Improvement Plan includes an action to: 'Review and revise the Improvement Framework and make more effective use of benchmarking, develop guidance and training on the use of benchmarking, Best Value reviews and options appraisal.'

3. Providing strong leadership and governance to support change

Maintaining good professional working relationships and providing strong political leadership	
Audit Scotland findings	***East Lothian position and actions***
The report highlights that: 'The best performing councils are able to identify when to set aside political differences and work on a constructive basis to support the council as a whole. In these councils, councillors from all political groups generally agree on	The Council uses the Corporate Governance Self-Evaluation to assess the strength of its governance and control arrangements. The Corporate Governance Self-Evaluation is based upon the 'CIPFA/ SOLACE Guidance on Delivering Good Governance in Local Government'. Member-

the overall priorities for the area, with debate focusing on how best to deliver them.'

Audit Scotland has found that: 'There is increasing evidence of political tensions and instability which is leading to strained working relationships or where working relationships have broken down and present risks to the council's ability to do business effectively and achieve Best Value.'

officer relations are considered as part of the self-evaluation.

The results of the last self-evaluation were reported to the Audit & Governance Committee in June 2014. The self-evaluation identified that the Council has adequate arrangements in place to determine the roles and responsibilities of officers and members. The Council's Standing Orders and Scheme of Delegation were reviewed recently the Council has approved new Roles and Responsibilities for elected members.

The annual Corporate Governance Self-Evaluation will continue to be used to assess whether further action may be required to ensure that East Lothian Council maintains good professional working relationships and strong political leadership.

Getting assurance that governance is sound, including where arm's-length external organisations (ALEOs) are in place

Audit Scotland findings	*East Lothian position and actions*
The Audit Scotland report states that: 'ALEOs offer an alternative to more traditional 'in-house' or contract-based service delivery and usually take the form of companies or trusts. ALEOs provide recognised 'council services', such as leisure services, but they can also deliver commercial operations such as exhibition facilities. While the ALEO takes on responsibility for services, the council remains responsible for both the public money it gives to the ALEO and for the quality of services the ALEO delivers.'	East Lothian Council only has one Arms Length Organisation – Enjoyeisure.
	The 2012/13 Council Improvement Plan contained the following action: '*Review governance of arms length services, commissioned services and partnerships including: development of a greater understanding of exposure to risk relating to arms length /outsourced / commissioned services; and incorporate monitoring of commissioned / outsourced services into performance indicators.*'
'For those councils that have not done so already, the time is right for a systematic review of their involvement in ALEOs and underlying agreements….In the current financial circumstances, the principles of good governance are more important than ever. This means providing clear direction and strong control, regardless of how services are provided, i.e. by in-house services, through contracts and, as set out in the previous section of this report, through other options including ALEOs.'	The following update was provided for this action: '*The Council's relationship with arms length services, commissioned services and partnerships is reviewed as service level agreements and partnership funding is considered. The revised guidance on service planning will include reference to the need to consider exposure to risk from arms length/ outsourced/ commissioned services. The revision of the Council's performance indicators will include consideration of performance monitoring for commissioned/ outsourced services*'

Providing stronger leadership of Community Planning Partnerships and working with partners to make the best use of the overall public resources available in the area	
Audit Scotland findings	*East Lothian position and actions*
The Scottish Government and COSLA reviewed community planning and Single Outcome Agreements (SOAs) in 2012. They then published a joint Statement of Ambition. This sets out high expectations for community planning:'	The East Lothian Plan (Single Outcome Agreement 2013-23) outlines three strategic objectives (sustainable economy; resilient people; and safe and vibrant communities) and 10 high-level outcomes that provide a clear vision for East Lothian. The overarching priority of The Plan is to reduce the inequalities across and within our communities.
To implement the Statement of Ambition successfully Audit Scotland concluded that CPPs need to:	The development of the Plan was preceded by a review of the governance arrangements of the East Lothian Community Planning Partnership. The outcome of the review was reported to Council in April 2013. One of the aims of the review was to 'consider the impact of the review of Community Planning being undertaken at a national level'.
- focus more clearly on where they can make the greatest difference in meeting the complex challenges facing their communities - ensure that all partners align their service and financial planning arrangements with community planning priorities - significantly improve their governance and accountability, and planning and performance management arrangements.	The governance review led to the 'East Lothian Community Planning Partnership' becoming the 'East Lothian Partnership'. New structures were also implemented that aim to:
The national Community Planning Group agreed that it should focus on getting partners to deploy their resources jointly towards partnership objectives.	- Lead a culture of collaboration and co-production across sectors - Ensure effective community involvement - Monitor and scrutinise progress on the SOA - Ensure transparency and accountability through public reporting and information sharing across partners.
	The functioning of the new arrangements will be reviewed using the Improvement Service Community Planning Partnership self-evaluation toolkit. East Lothian Partnership will undertake a self-evaluation supported by the Improvement Service in autumn 2014.
	A chief Finance Officers Group has bee established to develop approaches to Joint Resourcing and a multi-agency group is to develop a Joint Asset Management Plan.

An overview of local government in Scotland 2014

ACCOUNTS COMMISSION

The Accounts Commission

The Accounts Commission is the public spending watchdog for local government. We hold councils in Scotland to account and help them improve. We operate impartially and independently of councils and of the Scottish Government, and we meet and report in public.

We expect councils to achieve the highest standards of governance and financial stewardship, and value for money in how they use their resources and provide their services.

Our work includes:

- securing and acting upon the external audit of Scotland's councils and various joint boards and committees
- assessing the performance of councils in relation to Best Value and community planning
- carrying out national performance audits to help councils improve their services
- requiring councils to publish information to help the public assess their performance.

You can find out more about the work of the Accounts Commission on our website: **www.audit-scotland.gov.uk/about/ac**

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Exhibit data

When viewing this report online, you can access background data by clicking on the graph icon. The data file will open in a new window.

Summary

Key facts

Revenue spend

£18.5 billion

£18.6 billion — Income

Value of assets — **£38** billion

£1.86 billion — Useable reserves[1]

Capital spend — **£2.3** billion

Staff employed — **204,500**
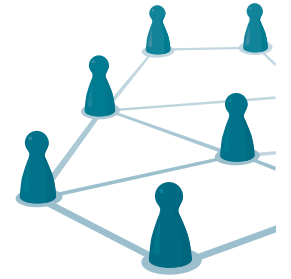
1,223 — Councillors
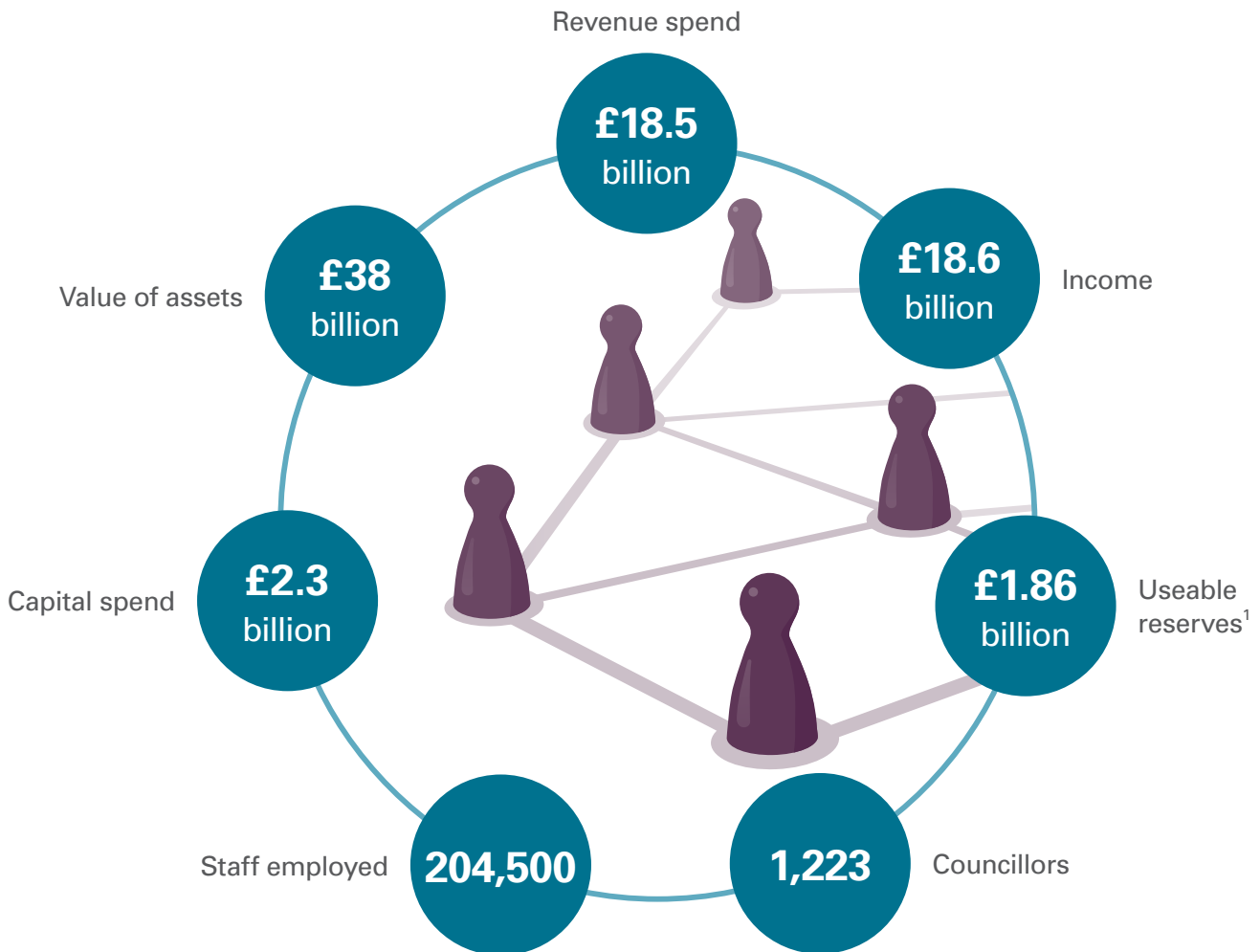
Note: 1. Excludes Orkney and Shetland Islands councils which hold large reserves and balances arising mainly from harbour and oil-related activities.

Chair's introduction

1. Scotland's 32 councils provide vital public services from the cradle to the grave. Delivered directly or in partnership with others, these services involve substantial resources. In 2013 councils spent nearly £21 billion, employed 204,500 staff and used buildings and other assets with a value of around £38 billion. Councils face reducing budgets and increasing demand. Finances remain tight and councils anticipate further budget reductions. To date they have balanced budgets mainly by reducing staff numbers but this alone is not sustainable in the longer term. Increasing numbers of older people, who typically need more public services – notably health and social care, as well as the public's rising expectations of service quality are among a range of factors contributing to increased demands on services.

2. Thus councils face increasingly difficult choices. To help make these decisions they need to make better and consistent use of options appraisal so that they can deliver the best possible value-for-money services to their communities. Councils need to ask the question, 'What works best and can we prove it?' The Commission recognises that options appraisal is challenging for councils, councillors, managers and staff. Loyalties run deep in councils, strong political beliefs are held and balancing competing interests is always difficult but the duty of Best Value – making best use of public resources – must always be paramount. Potential cuts require rigorous appraisal of alternatives so that decisions are transparent and based on solid information. Over and above these internal challenges, councils are having to deal with the impact of welfare reform, to plan with their partners for changes in health and social care and to deepen and strengthen the effectiveness of community planning.

3. In this complexity of change, the foundation stones of good governance and accountability remain constant. A fundamental principle of good governance is councillors and officers operating in clearly defined and understood roles. The role of the councillor can best be described as being at the start and the end of the process; at the start deciding policy, and at the end holding officers to account for their performance in implementing the policy. The part in the middle, the management of the council, is the responsibility of officers. Our audits have consistently shown that where roles are clear and respected and where Best Value is at the heart of its business, a council will be best placed to meet the challenges of 2014 and beyond. In contrast, bad governance is debilitating, time-consuming and expensive.

4. Strong political and managerial leadership is also more important than ever. While political coalitions have worked well in recent years there is evidence of heightened tensions in council chambers. Of course there will always be different views and approaches across political parties; that is the essence of local democracy. However, the Commission has expressed its consistent view that it is unacceptable if political tensions become so extreme that they compromise a council's ability to ensure effective leadership, demonstrate good governance and, as a result, weaken the public's trust and confidence in the integrity of the council and its councillors to conduct public business.

5. The Commission's messages and recommendations are not new; they reflect recommendations and messages in previous overview reports. The fact they are similar serves to underline their continuing relevance and importance.

Douglas Sinclair
Chair of the Accounts Commission

About the report

6. The Accounts Commission's overview report is based on the local government audit work in 2013. We use this to provide a high-level, independent view on the progress councils are making in managing their finances and in achieving Best Value, and to help councillors identify priorities in 2014.

7. The report focuses on what more needs to be done. First, we set out the context for local government and the key role of councillors within that. We then consider what more councillors need to know about current services and the options for providing services. We conclude by focusing on key elements needed to deliver Best Value, ie leadership and governance, and how more can be achieved through partnership working.

8. The report is supported by two appendices:

- Appendix 1 summarises how councils used resources in 2013.

- Appendix 2 contains a checklist and links to other material which is available to support improvement in 2014.

9. The report is primarily for councillors, as a source of information to support them in their role. However, councillors will need to work closely with officers to identify the position in their councils and to address the priorities we identify. We also expect councils to discuss the report with their community planning partners.

Key messages
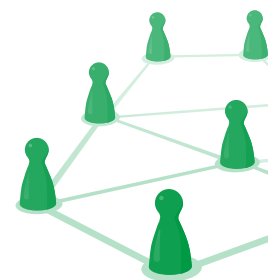
1 Councillors need to maintain a good understanding of the rapidly changing economic, social and political context. Demands on services and resources continue to increase and need to be managed alongside public service reforms, including changes in the welfare system and in health and social care.

2 Achieving Best Value requires good information about the cost and performance of current services and robust analysis of the options and the related risks associated with alternative ways of delivering services.

3 Governance is more important than ever. Councillors need to scrutinise reports from officers on the financial position and service performance: get the right information; ask the right questions; and ensure issues are resolved. They also need to scrutinise reports from auditors and get assurances from officers that weaknesses in financial systems are addressed. Councillors should assure themselves that the officer responsible for the council's finances retains appropriate access and influence within management structures.

4 The total level of reserves has increased but the level of 'free' reserves has fallen, with councils predicting future funding gaps. More work is needed to develop longer-term resource plans that show connections between savings, staff changes and how assets, such as land and buildings, are used to best effect in providing services.

5 Councils are working with their partners to meet the challenges of significant service reforms. Achieving more from Community Planning Partnership (CPP) working requires strong shared leadership, more effective governance and making the most of the combined public sector resources in the area.

6 There is increased evidence of political tensions and instability which is leading to strained working relationships. This comes at a time when decisions on services are becoming increasingly difficult and require strong political and managerial leadership. There will be additional demands on councillors in the run-up to the independence referendum. This will require a balance between their council responsibilities and their wider political activities.

Key recommendations

Councils continue to face significant challenges. They need to review how services are currently delivered and consider options as to how services might be delivered in future. They also need to increase the focus on partnership working and longer-term resource planning. Councils that place Best Value at the heart of all they do are best placed to deal with the challenges in 2014 and beyond.

Key priorities for councillors in 2014

- Understanding the changing context and the crucial role of councillors
  - Maintaining a clear understanding of the financial position.
  - Understanding the public reform agenda, including the impact of welfare reform.
  - Preparing for changes in health and social care.
  - Keeping up to date through training and development.

- Meeting user demands and the financial challenges
  - Appraising the options for delivering services and charging for services.
  - Requiring good-quality cost and performance information for decisions and scrutiny.
  - Making better use of benchmarking to support service improvement and public reporting.

- Providing strong leadership and governance to support change
  - Maintaining good professional working relationships and providing strong political leadership.
  - Getting assurance that governance is sound, including where arm's-length external organisations (ALEOs) are in place.
  - Providing stronger leadership of CPPs and working with partners to make the best use of the overall public resources available in the area.

Priorities in 2014
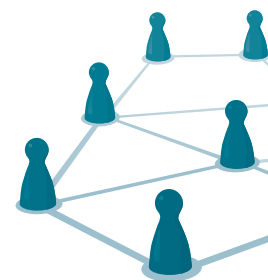
Understanding the changing context and the crucial role of councillors

10. Councils are continuing to operate in challenging financial circumstances and against a backdrop of increasing expectations and demands on services. To achieve success for their local communities, councillors need to maintain a good understanding of the rapidly changing economic, social and political context within which their council operates.

11. In this section of the report we set out the context for services in 2014 and review the councillor's role, which is crucial to success.

There are continuing pressures on finances and services

12. Pressures on resources in local government are not new. Councils, as with other parts of the public sector, have always faced difficult choices in allocating limited money, staff and other assets such as buildings across competing priorities. However, against a backdrop of savings and staff reductions to date, these decisions are increasingly difficult.

13. Local government's share of the Scottish budget has remained fairly constant but, for revenue funding, translates to a real terms reduction, ie after factoring in the effects of inflation. The funding settlement to councils for 2014/15 is £10.6 billion, an increase of about 2.9 per cent in cash terms or 0.8 per cent in real terms. Revenue funding has remained constant at £9.8 billion which represents a decrease of 1.2 per cent in real terms. Capital funding has increased to £0.8 billion in 2014/15, an increase of 40 per cent in cash terms or 37.1 per cent in real terms. The majority of this increase is due to the reprofiling of capital funding which resulted in £120 million moving from 2012/13 to 2014/15 and £100 million moving from 2013/14 to 2015/16.

14. Key information about council finances is included in Appendix 1 (page 33). This shows that spending on services is around £21 billion, ie £18.5 billion on the day to day business of providing services and £2.3 billion on buildings and other assets used to provide services over time. The day-to-day costs are matched broadly by income from government grants, council tax, charges for services and the application of reserves. Upward pressures on the costs involved in providing services, including energy costs, waste disposal and maintenance, are continuing and need to be managed alongside increasing expectations and demands for services Exhibit 1 (page 10).

15. The public sector faces significant challenges in reshaping care for older people. This involves changing the way services are delivered while continuing to meet current need. People are living longer with more complex care needs and

the councillor role is crucial in meeting the challenges in 2014 and beyond

Exhibit 1
Demand and resource pressures in 2014 and beyond

Demand pressures

Population growth and changes:
- demand for social care services
- demand on school places

Economic pressures:
- increasing benefits claimants/pressures on welfare benefits and advice services
- social housing demand
- demand on economic regeneration and business advice services

Impact of welfare reform

Implementing national and local priorities

Local pressures:
- increasing maintenance costs for roads and other assets
- flooding/winter maintenance demands

Council services

Resource pressures

Reducing revenue budgets

Salary, equal pay and pension commitments

Reducing staff numbers and increasing span of control

Borrowing commitments

Capital programme slippage

Economic pressures:
- council tax freeze
- council tax arrears
- rent arrears
- reducing income from sale of buildings/assets
- reducing income from cash deposits/investments
- reducing income from planning and building control fees
- inflation and rising costs, eg fuel
- opencast mining and landfill site obligations
- waste disposal

Source: Audit Scotland

this has implications for councils and other organisations that provide services for older people. Our report *Reshaping care for older people* (PDF) found that the programme has brought together the different bodies involved in these services, which cost £4.5 billion a year. These organisations now need to better target resources at preventing or delaying illness and at helping people to keep living at home.

16. There are also substantial pressures within individual services. In housing, for example, councils have a long-standing role and wide-ranging responsibilities, including specific legal requirements to tackle sub-standard housing and homelessness. Our report *Housing in Scotland* (PDF) highlighted significant challenges from population and policy changes in the next few years. For example, the ageing population is likely to increase demand for supported living, the number of single-person households is set to rise and welfare reform will further increase pressures on housing services.

17. Dealing with equal pay claims and the associated costs remains a significant issue. Councils continue to settle equal pay claims and make provision for those cases not yet settled. Cumulatively, councils had paid out £507 million by March 2013, including payments of over £32 million in 2012/13. A further £73.2 million is set aside to meet expected future amounts. In addition, around two-thirds of councils anticipate future costs which cannot yet be quantified.

18. The costs of settlements are significant but there are also unquantified workforce resources and associated costs, particularly for legal and human resource departments. It is in councils' interests to resolve these cases as quickly as possible, not least to eliminate the continuing uncertainties this issue presents in terms of their overall financial position.

19. Councils' experience of dealing with equal pay claims has identified the ongoing need to deliver pay equality. The Convention of Scottish Local Authorities (COSLA) has been working with the Society of Personnel Directors in Scotland and unions to review the terms and conditions of service for local government employees. This review will reflect the developing legislative environment and best employment practices. These changes are not anticipated to raise difficult matters for negotiation, but will ensure that the employment schemes are compliant with the latest legal position at European and UK levels.

Public service reform provides challenges and opportunities for new approaches to services

20. Alongside demand and resource pressures in services, councils are at the centre of wider public service reforms introduced by the Scottish Parliament and by the UK Parliament. The Scottish Government's approach is founded on 'four pillars' for change: shifting resources towards prevention; integrated local services through better partnership working; workforce development; and transparent and improving performance.

21. Responding to public service reform is challenging but it can also help councils deal with demand and resource pressures, address inequality and better meet the expectations of people and communities. The increasing emphasis on partnership working and community empowerment, while challenging, also provides opportunities for new approaches to services.

22. Single police and fire and rescue services came into effect in April 2013. This was one of the largest and most complex restructuring reforms in the public sector for many years, involving services with annual expenditure of the order of £1.4 billion.

23. Councils retain an important role in helping to strengthen connections between the police and fire and rescue services and local communities and are responsible for monitoring services in their areas. They are working with their local commanders (police) and local senior officers (fire and rescue) to develop approaches to local scrutiny and engagement, including links to community safety partnerships and CPPs.

24. The Welfare Reform Act 2012 aims to improve work incentives, simplify the benefits system and deliver savings. This is the biggest reform of the UK welfare system for 60 years and has significant implications for households, and for councils and the services they provide.

25. We have been monitoring the position and our survey in 2013 indicated that councils have carried out a significant amount of work to plan for and to mitigate the impact of the reforms. They are working closely with partners such as COSLA, the Scottish Government and the UK's Department for Work and Pensions to deliver the changes. However, uncertainties remain that make it difficult for councils to plan ahead, particularly in relation to the shift from housing benefits to universal credit and the level of support they are expected to provide to customers in future.

26. It will be some time before the full impact of welfare reform is clear. However, surveys by the Scottish Housing Regulator[1] and COSLA[2] indicate that the removal of the spare room subsidy may be contributing to increasing levels of rent arrears. More widely, a report commissioned by the Scottish Parliament in April 2013 estimated that, when fully implemented, welfare reform will take more than £1.6 billion out of the Scottish economy each year. Councils with higher levels of deprivation are likely to be hardest hit and, over time, the reforms could have a substantial impact on local economies.

27. The integration of health and social care services affects major parts of the public services and, potentially, represent the biggest change in local government since reorganisation in 1996. The aim is to improve the quality and consistency of care for adults, and to shift resources away from institutional to community care.

28. Councils are at various stages in preparing for health and social care integration. We support the principle that public services should be designed around the needs of the service user, and that public bodies should seek to overcome the organisational barriers that get in the way of delivering seamless integrated health and social care. It is essential that services are able to work well together to respond to needs while making the best use of existing resources and delivering high-quality services. We have highlighted in several reports the need for barriers to partnership working to be addressed and the importance of a joint vision and clear priorities for the use of shared resources.

29. Looking further ahead, the Scottish Government has brought forward proposals in the Community Empowerment Bill.[3] These highlight the important role that communities can play in participating in new models of service delivery and developing models of 'co-production' that draw upon the knowledge, skills and experience of local people in ways that maximise the impact and value of public assets, eg people, buildings and local knowledge. This may lead to changes in the relationship between councils and communities.

30. We provided a response to the Bill covering areas such as common good, community planning, scrutiny and the possible accounting implications of the transfer of assets to communities. Our response reflects on our experience in the scrutiny of community planning and of our responsibilities in holding councils to account and encouraging improvement. We welcome the increased emphasis for CPPs on delivering outcomes and the opportunity for clarity on responsibilities, accountability and governance.

Councillors have a complex and demanding role, which is crucial to the success of their councils

31. Councillors represent their constituents, provide leadership and direction and scrutinise service performance and how resources are used. The effectiveness of councillors has a strong bearing on the achievement of Best Value and the overall success of councils.

32. As we state in our 'how councils work' report *Roles and working relationships: are you getting it right?* (PDF) this is a complex and demanding role, made more so in the current context where reduced budgets mean that choices and decisions are more difficult. Councillors are involved at the start of the process (getting views from people and communities and setting policies) and at the end (holding officers to account for the implementation of policies and keeping people and communities informed about services changes and performance), Exhibit 2 (page 14). The part in the middle, the management of services, is the responsibility of council officers.

33. The political context in 2014 is particularly challenging with local, national and international interest in the referendum on Scottish independence. This is likely to mean additional demands on councillors, requiring a careful balance between their crucial role in councils and their political interest in the referendum.

34. Whatever the outcome of the independence referendum, further discussions are likely on local services, governance and accountability. In October 2013, COSLA established a commission on Strengthening Local Democracy to consider how local democracy and accountability might be improved and to provide advice on what is needed for that to happen. Discussions are also ongoing on the the joint initiative 'Our Islands Our Future' which seeks greater powers for the islands councils. More recently the Scottish Parliament's Local government and Regeneration Committee launched an inquiry into the flexibility and autonomy of local government.

35. In this quickly changing context it is more important than ever that councillors are supported in their role. We are of the firm view that effective democratic decision-making can only take place when councillors have the right skills, information and support to carry out their roles. It is essential that officers provide councillors with sufficient, well-researched and presented information to enable them to carry out this role. Other key requirements are awareness and understanding of governance processes; our audits confirm that there is a continuing demand and need for more training and development.

36. There is already a wide range of material and resources available to councillors. For example, the Continuous Professional Development (CPD) framework established by the Improvement Service in consultation with local government provides professional and personal development opportunities in a wide range of important skills.

Exhibit 2
The councillor role
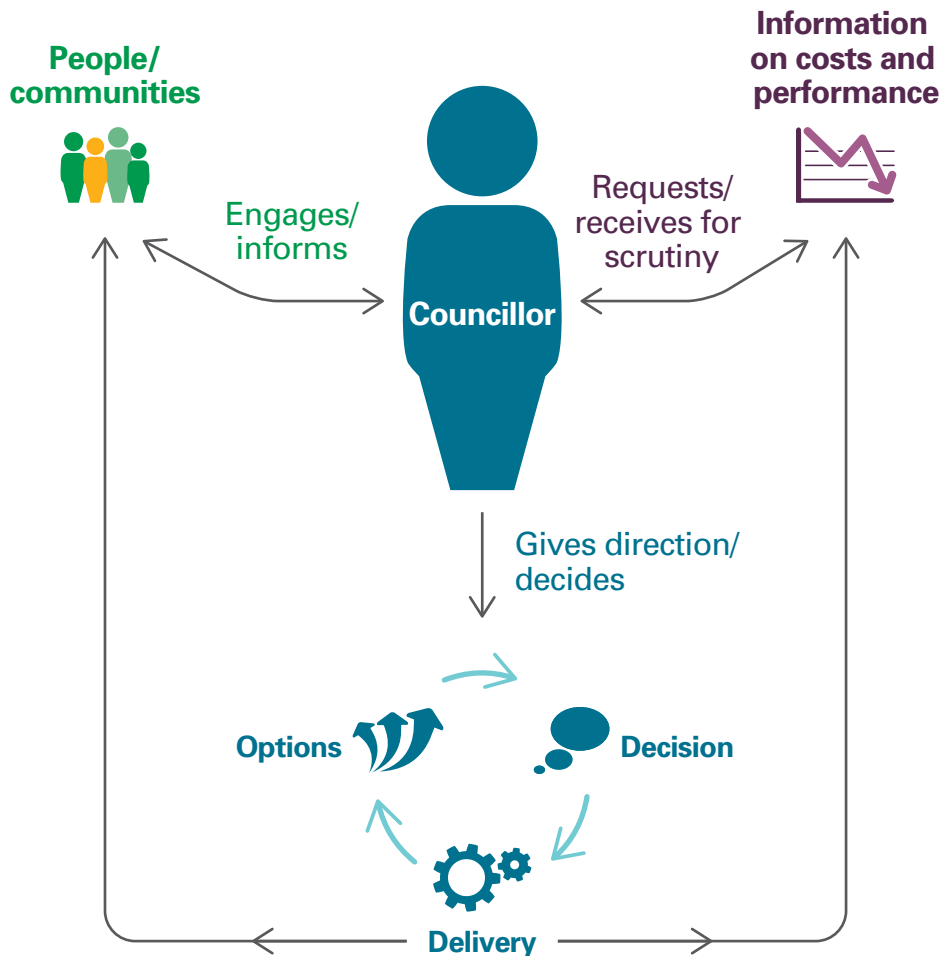
Source: Audit Scotland

37. However, the onus is on councillors to ensure that they regularly review personal development plans and discuss training needs. A recent Improvement Service survey of councillors showed that, of those who responded, around 80 per cent said that local induction programmes addressed their needs.[4] Around two-thirds felt that they had been given adequate training to carry out their scrutiny role effectively. This is encouraging but also suggests that there is still a long way to go before all councillors have the support they feel they need.

Summary and points for action in 2014

- Maintaining a clear understanding of the financial position.

- Understanding the public reform agenda, including the impact of welfare reform.

- Preparing for changes in health and social care.

- Keeping up to date through training and development.

Meeting user demands and the financial challenges

38. Councils need to consider options to decide which services best meet the needs of the people and communities they serve. In so doing, they must comply with their statutory duty to provide Best Value. This requires continuous improvement while maintaining a balance between quality and cost and having regard to value for money, equal opportunities and sustainability.

39. Faced with reducing finance and increasing demands and expectations of services, councils are reviewing the way they deliver services. Pressures are building and councils need to identify innovative and ambitious approaches to services and then make consistent use of options appraisal to decide the way forward. Changes always carry some degree of risk; our expectation is that councils should be risk aware, not risk averse.

40. In this section of the report, we consider what more councillors need to know about current services and about options for future services.

Councillors need good information to support decision-making and accountability, consistent with Best Value responsibilities

41. To scrutinise and assess services, councillors need good information on performance and costs of current service activities. This is crucial information which highlights what is working well and where there may be emerging problems, where improvement may be needed and whether value for money is being achieved.

42. Our 'how councils work' report *Managing performance: Are you getting it right?* (PDF) sets out the key aspects of performance management, including the key characteristics for managing performance and improvement. The report emphasises that everyone in the council has a role in managing performance and that, together, council officers and councillors are responsible for ensuring their council meets the Best Value duty.

43. Councils are working to review and refine performance arrangements. However, more needs to be done to ensure the quality of performance information and that there is clear read-across between the information which is collected and councils' objectives, so that progress can be measured. The evidence indicates, in particular, that the priorities in 2014 are to:

- Include more information on costs, outcomes and service users' views.

- Use performance information alongside cost information to assess value for money.

- Identify and prioritise areas for improvement.

- Evaluate the impact of improvement activity, including the impact of self-evaluation using approaches such as the Public Service Improvement Framework (PSIF).

44. Managing performance based on the 'plan-do-review-revise' cycle provides a systematic framework for performance management. Within that, councillors need to focus on the crucial contribution they make in this process Exhibit 3 (page 16). In summary, councillors:

- Need to be clear about what the council is wanting to achieve and how they will monitor and review performance.

- Need to be prepared and equipped to challenge officers on service performance and to ensure that priorities are delivered and that the needs of local communities are being met.

- Can support improvement by showing they are actively interested in performance management and taking action based on what performance information is telling them.

Exhibit 3
Councillors' role in managing performance: the 'plan-do-review-revise' cycle

Plan

- Set out the objectives or targets
- Identify what needs to be done to achieve these
- Identify how this will be done and what resources will be needed
- Identify who is responsible
- Set clear measures

Do

- Ensure the necessary systems and processes are in place
- Take action
- Identify and manage risks
- Support staff to achieve their objectives

Revise

- Incorporate improvements into future planning
- Revise objectives and targets
- Update resource planning

Review

- Monitor progress regularly
- Identify what worked well and what could be improved
- Speak to service users and stakeholders about their experience
- Scrutinise performance and hold those responsible to account

Plan   Do

Revise   Review

Source: Audit Scotland

45. As part of their Best Value responsibilities, councils have a duty to report their performance publicly so that local people and other stakeholders know what quality of service is being delivered and what they can expect in the future. Public Performance Reporting (PPR) has significantly improved over the last three years, with improvement across all corporate themes and service areas. However, there is still room for improvement .

46. We are encouraged by developments in local government benchmarking. SOLACE, COSLA and the Improvement Service have been leading work in

Exhibit 4
Public Performance Reporting

Improvements achieved in 2013:

- More information on comparisons over time.

- Improved coverage of the statutory performance indicators.

Improvements required in 2014:

- More narrative and contextual information to help the reader understand the indicators and performance information provided.

- More use of targets, trends, progress with initiatives or actions being taken to address underperformance, to help the reader understand how well the council is performing.

Source: Audit Scotland

this area through the Local Government Benchmarking Framework (LGBF). This provides comparative benchmarking covering all major service areas, with a strong emphasis on costs. Data for 2012/13 was recently released accompanied by an overview[5] covering broad trends and variations. The benchmarking website has interactive capabilities to extract data sets both on a council basis and for individual indicators, allowing councils to undertake their own detailed analysis.

47. A key element of PPR is comparing performance with other councils. Consistent with the improvements in PPR generally, more councils are including this as part of their reports. However, fewer than half of councils include information showing how they are performing relative to other councils. With the increasing availability and refinement of LGBF data we expect there will be opportunities for greater use of comparisons with other councils in PPR material in 2014 and that this will result in better information for the public.

48. More generally, the LGBF will facilitate comparisons on spend and performance between similar councils so that councils can identify strengths and weaknesses, learn from councils that seem to be doing better and improve their performance. The data covers 60 per cent of the total spend of local government and provides the opportunity for services to use the data to determine why disparities exist between services in different councils and to support change and accountability for service performance.

Councils need to consider options for new ways of working and changes in the way services are delivered and paid for

49. Everything councils do has its roots in legislation. Some services are more prescribed in legislation than others, for example collection of council tax and business rates; for other services councils have discretion on the level of service provided. Even for those services where there is some prescription it is normally relatively limited and councils have substantial discretion on how services are delivered and by whom.

50. An options appraisal is all about making well-informed decisions; the basic stages are shown in Exhibit 5. The '*Best Value: Making Choices*'[6] guidance published by the Scottish Government in 2001 noted that, as with any decision-making tool, options appraisal provides support to the process, it does not provide the answers. The value of decision-making tools is that they take people through the process stage by stage, and assist in making sure that everything relevant is taken into account.

Exhibit 5
Basic stages of options appraisal
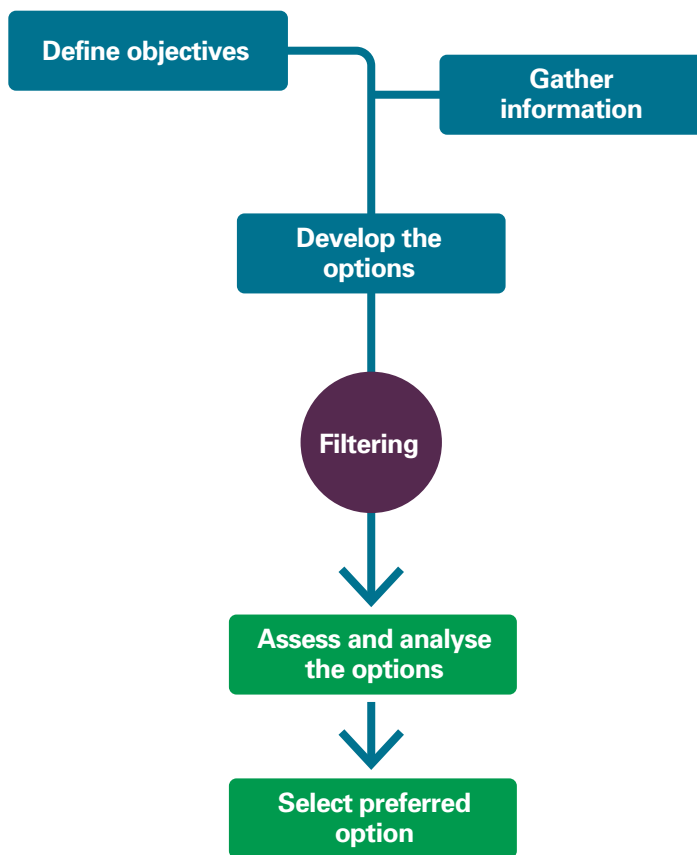
Source: *Capital Planning and Option Appraisal – A Best Practice Guide for Councils*, CIPFA Local Government Directors of Finance, October 2006

51. Our expectation is that options appraisal is a standard part of decision-making involving changes in how services are delivered and involving major capital projects. We recently published a further report in the 'how councils work' series, *Options appraisal: Are you getting it right?* (PDF) 🖥.

52. Cost information is important in assessing performance and value for money in existing services over time. Looking at service performance alone is not sufficient - what it costs to provide the services is an important factor in forming overall judgements. Cost information is also crucial in reviewing options for new ways of delivering services. Our 'how councils work' report *Using cost information to improve performance: are you getting it right?* (PDF) 🖥 identified what cost information involves and how it can be used more effectively.

53. In redesigning services, councils need to ensure they are designed around the needs and expectations of the people who use that service. A decision to pursue an alternative method of service delivery can change long-standing arrangements and can have far-reaching consequences for service users, services, systems and staff. Successful engagement with the public and staff can help manage expectations about what can be achieved in the context of reducing budgets.

54. Options for the delivery of council services include the use of arm's-length external organisations (ALEOs). ALEOs offer an alternative to more traditional 'in-house' or contract-based service delivery and usually take the form of companies or trusts. ALEOs provide recognised 'council services', such as leisure services, but they can also deliver commercial operations such as exhibition facilities. While the ALEO takes on responsibility for services, the council remains responsible for both the public money it gives to the ALEO and for the quality of services the ALEO delivers.

55. We have an ongoing interest in ALEOs. With COSLA, we published a *Code of Guidance on Funding External Bodies and Following the Public Pound*[7] which set out the principles of best practice for councils when establishing funding relationships of this type. While the context has changed since the Code was published in 1996, the principles remain valid Exhibit 6.

Exhibit 6
The 'following the public pound' code principles

The principles of openness, integrity and accountability apply equally to funds or other resources which are transferred to ALEOs. The code sets out six principles that require councils to:

1. have a clear purpose in funding an ALEO

2. set out a suitable financial regime

3. monitor the ALEO's financial and service performance

4. carefully consider representation on the ALEO board

5. establish limits to involvement in the ALEO

6. maintain audit access to support accountability.

Source: Audit Scotland

56. Our 'how councils work' report *Arm's-length external organisations: Are you getting it right?* (PDF) pointed out that delivering projects or services through ALEOs is likely to make governance complex but that the same principles of good governance apply. For those councils that have not done so already, the time is right for a systematic review of their involvement in ALEOs and underlying agreements.

57. Our report *The Highland Council: Caithness Heat and Power: Follow-up statutory report* (PDF) demonstrated the serious consequences of weak governance in dealings with ALEOs. This case provides useful learning points

for all councils, particularly the need for robust governance and accountability in which roles and responsibilities are clear, particularly those of councillors. We have shared our findings with all councils.

58. Options not only include changing who provides the service; there will be opportunities to simplify, standardise or adjust existing approaches to achieve better value for money, eg by reviewing existing systems for paying for goods and for collecting money.

59. Intelligent purchasing may help public bodies to improve the quality of services they provide and help them to reduce costs. Public bodies need to have well-trained staff and effective systems to provide the procurement capability to achieve good results. While some bodies perform well in these areas others have a significant amount of work to do to demonstrate value for money in procurement. We will shortly publish a report on procurement in local government.

60. We welcome the Scottish Government's proposals to set a new general duty on public bodies to conduct procurement in a transparent and proportionate manner. The requirement on authorities with significant procurement expenditure to produce a procurement strategy and annual procurement reports will support this duty.

61. Also, within existing service arrangements, charges can be a means to sustain and improve services. They can also be used to bring in new sources of income or help a council to improve the services it offers.

62. Our 'how councils work' report *Charging for services: Are you getting it right?* (PDF) 🖥 looked at the contribution charges make to budgets and how charges can influence how people choose to use services (Exhibit 7, page 21). The report also contains examples of good practice, including understanding costs and getting the views of people who use services, and a guide to managing charges.

63. Our report found councils can make more effective charging decisions when they consult with service users, community planning partners, residents and other stakeholders over proposed charges. Councils need to provide leadership in ensuring that these decisions do not adversely impact on particular groups of people. Equalities-impact assessments should be considered as part of any significant charging decision or service change.

64. We concluded that councils should have clear policies in place for charges and concessions and that they should regularly review charges to ensure that they are appropriate and meet their intended objectives. The report also recognised the important role of councillors in determining charging policies, participating in the design of charges and concessions and understanding the contribution charges make to their council's overall financial position.

Summary and points for action in 2014

- Appraising the options for delivering services and charging for services.

- Requiring good-quality cost and performance information for decisions and scrutiny.

- Making better use of benchmarking to support service improvement and public reporting.

Exhibit 7
Income from sales, fees and charges compared to income from council tax (shown in 2011/12 prices)
Income from charges is increasing, while income from council tax has declined in real terms.
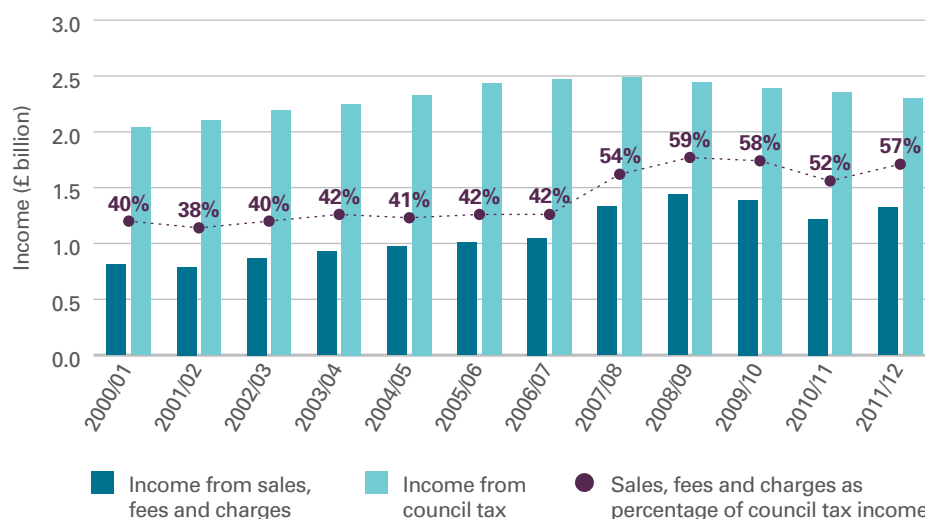
Note: Figures adjusted in real terms to 2012.

Source: Audit Scotland and Scottish Government Local Financial Returns

Providing strong leadership and governance to support change

65. In previous reports we highlighted the significant changes in the make-up of the people leading, managing and working in councils. Over a third of councillors elected in May 2012 were new to local government. There have also been substantial changes in council senior management teams in recent years, including changes in the chief executive in nearly half of all councils.

66. Working together, councillors and officers lead and manage their councils to provide vital services for the people and the communities they serve. Trust, confidence and good conduct between councillors, and between councillors and officers, are essential for good working relationships. Against a background of changes in the people leading and managing councils, we have highlighted the need to build and maintain strong working relationships, and the potential risks to leadership and Best Value where problems emerge.

67. We have also emphasised the importance of good governance, including the structures which provide the basis for good financial governance, and the role and behaviours of councillors and officers in ensuring effective governance in practice.

68. In this section of the report we focus on leadership and governance, and how to make more from community planning.

There is evidence of increasing political tensions and instability which is leading to strained working relationships

69. Our 'how councils work' report *Roles and working relationships: are you getting it right?* (PDF) acknowledges that politics is an integral and important part of local government decision-making and that tensions are inevitable given the differing policy objectives of political parties and individuals. The best performing councils are able to identify when to set aside political differences and work on a constructive basis to support the council as a whole. In these councils, councillors from all political groups generally agree on the overall priorities for the area, with debate focusing on how best to deliver them.

70. There is increasing evidence of political tensions and instability which is leading to strained working relationships or where working relationships have broken down and present risks to the council's ability to do business effectively and achieve Best Value.

71. For example, in Argyll and Bute Council the auditors concluded that political instability meant that there was a lack of collective strategic leadership by councillors. They also found that the council's political management arrangements were contributing to the problems rather than helping the council do business effectively. Working relationships between councillors and between a few councillors and officers were strained and the challenges facing the council were affecting the capacity of senior managers.

72. While the problems were not yet affecting frontline services, they were beginning to inhibit progress with strategic planning and there was a risk that services may suffer in the future if the difficulties were not addressed. We expressed concerns in our findings and requested a report on progress within six months (Exhibit 8, page 23).

73. In Falkirk Council auditors reported that not all councillors were participating in new decision-making structures. Some councillors were not attending executive and scrutiny committee meetings and scrutiny and policy development panels because of their concerns about the lack of effective scrutiny. The auditors noted significant risk to the effectiveness of the council's governance arrangements.

74. At Aberdeen City Council the auditors highlighted the importance of setting aside politics to support the constructive working of the council. They had observed political tensions among councillors in several meetings which affected the effectiveness of decision-making. Behaviour in the council chamber was regularly disrespectful and it had been necessary for councillors to be reminded of the requirements of the councillors' Code of Conduct. A number of local issues had been particularly challenging and had added to the political tensions.

75. Helping to improve working relationships can absorb a large amount of councillor and senior manager time when there are already pressures on senior managers to deliver the changes required to address existing service and financial issues.

76. Looking ahead, further pressures and tensions are likely. Locally, the political make-up of councils is closely balanced, with half of councils run by coalitions, and reduced budgets mean that choices and decisions on services are harder. Nationally, the referendum on independence is the main political issue in Scotland in 2014, with heightened political activity for all parties and elected representatives, including councillors.

Exhibit 8
Argyll and Bute Council: extract from the Accounts Commission's findings

'…the Commission is seriously concerned about substantial risks to the council caused by the instability of leadership by elected members since the last council election. The council's ability to set and maintain a clear strategic direction is at risk of being compromised and the Commission is concerned that this will, in time, negatively affect the services that the council provides for the people of Argyll and Bute. We are also concerned about the negative effect that this is having on the council's reputation.

The quality of leadership of the council has been inadequate. We urge the elected members and the corporate management team to work together to provide stronger and effective leadership of the council. Effective working relationships between elected members, and between members and officers, need to be based upon mutual trust, respect and transparency. Elected members need to achieve a more effective balance between focusing on local issues and priorities and the longer term strategic objectives of the council and the best interests of the whole community of Argyll and Bute…'

Source: Accounts Commission's findings, Argyll & Bute Council Statutory report, October 2013

77. Councils are also changing the way services are managed. Management restructuring and significant changes in the role of officers need to be handled carefully to ensure consistency and continuity of leadership and governance. This can provide opportunities to review and develop the senior management arrangements. For example, our report *The City of Edinburgh Council: the Audit of Best Value and Community Planning* (PDF) highlighted significant changes at managerial level and that good relationships and strong leadership resulted in a more corporate and strategic approach.

78. Building and maintaining good working relationships are vital to the success of all organisations. In local government, good working relationships are a key component in the conditions necessary to achieve Best Value (Exhibit 9, page 24).

Decisions on services are becoming increasingly difficult and require strong leadership and governance

79. So far, tighter budgets have been met by reducing staff numbers (Appendix 1, page 33). Our report *Scotland's public sector workforce* (PDF) identified that councils have managed workforce costs and numbers in a number of ways including pay restrictions/freezes, managing vacancies and redeploying staff to new areas of work. All councils have used voluntary departures to reduce staff costs. As part of a wider review across the public sector in Scotland, we considered the use of voluntary departures in local government.[8] In view of the likelihood of further early departures to reduce costs we took the opportunity to emphasise good practice standards including the need for clear policies, to consider all costs and potential savings, and to check that savings are delivered (Exhibit 10, page 25).

80. More work is needed to monitor the impact of staff reductions on front-line services but also on the capacity and resilience of support functions, including

Exhibit 9
Governance, working relationships and Best Value
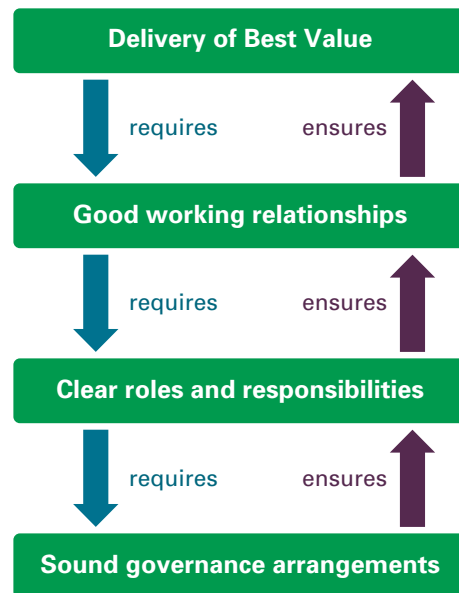
Source: Audit Scotland

finance departments, ICT and people management. This may be apparent from routine performance information but may also require connections to be made with other information, including audit reports. For example, councillors should consider whether delays in performing key, routine accounting controls or delays in receiving up-to-date information on the financial position are indicative of under-staffing or reduced skills and capacity in finance departments.

81. More widely, increasing levels of staff overtime may be indicative of pressures in services which in time may affect service performance and diminish the savings anticipated from decisions to reduce the size of the workforce.

82. While councils have relied mainly on staff reductions, this is not sustainable in the longer term and they face having to consider policy options which they may have previously rejected because they are politically unacceptable or unpopular. There is emerging evidence that councils are considering options to reduce or stop services by, for example, removing subsidies for bus services, closing libraries or reducing support for arts development. As indicated earlier, good decision-making requires good-quality information on costs and performance and rigorous options appraisal.

83. Having taken difficult decisions, strong leadership is required to see them through. Councillors need to explain the rationale to local people and to monitor the impact. Officers need to implement the changes agreed by the council and ensure systems are in place to provide information on the consequences of the changes in terms of cost, performance and value for money. Our report *Maintaining Scotland's Roads: An audit update on councils' progress* (PDF) ⬇, for example, highlighted the need for councils to continue to monitor the impact of changing levels of maintenance expenditure on the condition of their roads.

Exhibit 10
Early departures – principles of good governance
The Accounts Commission's report on voluntary departures re-emphasised key principles in the governance of early retirements.

Framework for decision-making

- Early retirement policies should be approved by councillors and reviewed regularly.

Informing members

- Councillors should receive a report at least annually that details the number of early retiral decisions, along with information on the associated costs and savings.

Decision-making

- Councils should rigorously appraise individual cases to ensure the expected savings associated with a retiral outweigh the costs.

- To improve accountability and assist in monitoring, the costs of early retirement should be charged to the appropriate service budget.

- Councillors should be involved in approving early retirement decisions for senior staff.

Source: Audit Scotland

Effective governance of finances is more important than ever

84. In the current financial circumstances, the principles of good governance are more important then ever. This means providing clear direction and strong control, regardless of how services are provided, ie by in-house services, through contracts and, as set out in the previous section of this report, through other options including ALEOs.

85. Audit committees provide a focus on financial control and risk and enhance public trust and confidence. We remain strongly of the view that audit committees should be separate from the executive and chaired by someone who is not a member of the political administration. We are pleased to note that this has been achieved in councils where that was previously not the case. Elsewhere, councils need to monitor their approach to ensure transparency and that the actual and perceived independence of the Audit Committee is not compromised.

86. The effectiveness of the Audit Committee depends on the committee members and their approach. They need to know how services and resource management work and be prepared to ask challenging questions. Particular areas for focus include cases where weaknesses in basic accounting systems and controls, under-resourcing of internal audit (generally, and in relation to pension funds) and under-developed risk management are reported to the Audit Committee. If basic financial information is compromised so are decisions based on that information.

87. Councillors need to be firmer in asking what officers are doing to address these problems and to follow through to obtain assurances that effective action is

implemented within acceptable timescales. This in itself requires particular skills, and there is evidence that councillors see the need for more training to support their scrutiny activities.

88. The chief officer for finance (also known as the statutory officer for finance or the section 95 officer) has a crucial role in providing professional advice to colleagues and councillors on all aspects of the council's finances and is central to effective financial governance. CIPFA's guidance[9] develops the requirements of the role.

89. The focus on finances means that the chief financial officer role is increasingly important. The role carries overall responsibility for financial management and reporting, contributing to the strategic management of resources and advising on the financial aspects of what are often complex options for new ways of delivering services. However, management restructuring and the shift to smaller management teams means that in about half of councils the chief financial officer is not now a member of the senior management team.

90. There is a risk, therefore, that the statutory role is less visible and that financial governance is affected. Where the chief financial officer is not a member of the senior management team, we re-emphasise that councillors need to understand why that is the case and satisfy themselves that the officer has appropriate access and influence to perform this crucial role.

91. Councillors also need to be aware of the important contributions provided by the other statutory officers who, like the proper officer for finance, act independently to promote and enforce good governance. The monitoring officer, for example, is responsible for advising councillors on the legal position on proposals and ensuring that the council follows proper procedures. More details about the statutory officers can be found in our 'how councils work' report *Roles and working relationships: are you getting it right?* (PDF) 🖥.

Reserves have increased but the level of 'free' reserves has fallen, partly because they have been applied to reduce funding gaps
92. Annual audited accounts show a council's financial performance and position and are important in demonstrating the proper stewardship of public money. The accounts should be published as soon as possible after the end of the financial year, along with an opinion from the independent, external auditor stating whether the accounts present a 'true and fair' view. This provides important assurance on financial reporting.

93. For financial year 2012/13, accounts for all councils and other local authority organisations, including the 11 local authority-administered pension funds, were presented for audit on time and signed off by auditors without qualification. We welcome this achievement and the assurance it provides to the public and other stakeholders.

94. Despite the financial pressures that they face, all councils managed to balance finances and most identified underspends at the end of 2012/13. Reduced staff numbers and the corresponding reduction in costs was the main reason for under-spending but the reasons varied. Some councils used 'free' or unearmarked reserves to ease financial pressures.

95. Councils hold cash-backed reserves (useable cash funds as opposed to reserves which are the product of accounting practice) which are available to

finance service expenditure, to ensure stability in cash flow, to build up funds for predicted costs pressures, and as a contingency for unforeseen expenditure. The overall level of reserves increased by £174 million to £1.86 billion at 31 March 2013.

96. Within the overall figure, general fund balances totalled £1.05 billion. Councils earmark these reserves for reasons including devolved school management, workforce change or voluntary redundancy and corporate improvement programmes. Earmarked reserves increased by £170 million to £743 million at 31 March 2013. The remaining reserves are deemed unearmarked or 'free'. The level of 'free' reserves has fallen for the first time in recent years, from £334 million at 31 March 2012 to £312 million at 31 March 2013, a reduction of 6.7 per cent.

97. The amounts in cash-backed reserves are substantial and we remain of the view that more needs to be done to provide more information on why reserves are held, how this fits with the council's overall financial strategy and how they will be used. Councillors in particular need good information about movements in earmarked funds, to assist their full understanding of their council's overall financial position.

98. While the short-term (this year and next) financial position is relatively stable, councils are identifying medium-term funding gaps and need to make substantial savings, at least over the next four years. Few councils have longer-term financial plans, beyond a four-year period, which identify gaps and how these will be addressed, with full explanations of the assumptions and risks under-pinning projections.

99. More work is also needed in these longer-term financial plans to show the links between finances, workforce and assets, to build a complete picture of how the overall resource will be applied and the connections between resources.

100. As indicated, there is some evidence that reserves are being used in the short term to narrow funding gaps. However, this is not sustainable because reserves can only be used once and can not support recurring expenditure.

101. In terms of annual budgets, we are encouraged by the extent to which councils are engaging with the public, employees and other key stakeholders, sometimes with the assistance of external researchers. This helps build a better understanding of the council's financial position and the choices that have to be made within available budgets. Particularly, within councils, it helps further reinforce awareness of costs and the need to make the most of available resources.

102. There is also evidence of councils developing a priority-based approach to budgets, which is an alternative to the traditional, incremental approach to budget-setting. It involves a clear understanding of how services contribute to the council's strategic priorities, developing options for services and agreeing options which are prioritised to achieve particular outcomes.

103. Following our previous reports on *Scotland's public finances*[10] we have collected further information on how councils are addressing the financial pressures in budgets. We will summarise key issues in a report later this year, in advance of the next budget cycle. This will include materials for councillors to assist their consideration of 2015/16 budgets.

104. We will continue our focus on other key aspects of councils' finances. In our previous overview report we noted that councils determine programmes for capital investment in accordance with the prudential code, which supports local authorities' capital investment decisions.

105. In the period since the code was introduced in 2004, the overall level of net indebtedness increased by around 45 per cent, from £9.1 billion to £13.3 billion. Bearing in mind local circumstances, there is wide variation across councils in the change in net indebtedness in the years since the prudential code came into effect. We will review the position, including the use of the code, as part of our audit of council treasury management and borrowing.

Achieving more from partnership working requires strong shared leadership supported by more effective governance

106. Community planning is the process by which councils and other public bodies work together, with local communities, businesses and voluntary groups, to plan and deliver better services and improve the lives of people who live in Scotland. It was given a statutory basis by the Local Government in Scotland Act 2003 (the Act). That Act, and the statutory guidance supporting it, sought to establish community planning as the key means of leading and coordinating partnership working at the regional, local and neighbourhood level.

107. The Scottish Government and COSLA reviewed community planning and Single Outcome Agreements (SOAs) in 2012. They then published a joint Statement of Ambition. This sets out high expectations for community planning and puts the community planning process at the heart of public service reform Exhibit 11. It also emphasises that all partners are collectively accountable for delivering services.

108. The Statement of Ambition is clear that significant changes to improve community planning are needed to respond to the challenges of reducing public finances while demand for services increases. CPPs also need to be equipped to reduce the stark variations in outcomes experienced by different communities.

Exhibit 11
Expectations of community planning:

- taking the lead role in securing integrated public services

- focusing more on potential problems and identifying ways to prevent them happening

- ensuring public bodies continue to improve the ways in which they manage and provide services

- achieving better outcomes for communities, such as better health and lower crime

- providing the foundation for effective partnership working, within which wider reform initiatives will happen.

Source: Audit Scotland

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109. There is now a renewed focus on community planning which provides a clear opportunity to deliver a step change in performance. This will require strong and sustained shared leadership from CPP boards.

110. Partnership working is now generally well established and many examples of joint working are making a difference for specific communities and groups across Scotland. But overall, and ten years after community planning was introduced, CPPs are not able to show that they have had a significant impact in delivering improved outcomes across Scotland.

111. *Improving community planning in Scotland* (PDF) 🔲 identified key issues from the CPP audits carried out in 2013. To implement the Statement of Ambition successfully we concluded that CPPs need to:

- focus more clearly on where they can make the greatest difference in meeting the complex challenges facing their communities

- ensure that all partners align their service and financial planning arrangements with community planning priorities

- significantly improve their governance and accountability, and planning and performance management arrangements.

112. Community planning is at a crossroads. This offers a significant opportunity to establish a system of leadership, governance and performance that ensures continuous improvement in community planning (Exhibit 12, page 30). This will not be easy. Barriers stand in the way, and this virtuous cycle will only be achieved through a level of sustained leadership that is significantly stronger than we have seen to date.

113. Our other national report work supports our key findings. For example, our report *Housing in Scotland* (PDF) 🖥 recognises that planning arrangements are complicated and have many partners. Councils must demonstrate leadership and work to influence partners. Our report *Maintaining Scotland's Roads: An audit update on councils' progress* (PDF) 🖥 recommends that councils need to work with partners to produce a strategy for developing the best service and structural models to deliver roads maintenance.

Partnerships need to identify and make better use of the overall resources available in their area

114. CPPs need to focus more clearly on where they can make the greatest difference in meeting the complex challenges facing their communities. They need to make their SOAs a true plan for the communities that they serve. They need to show how they are directing the significant public money and other resources available to CPP partners to target inequalities and improve outcomes. SOAs need to specify what will improve, how it will be done, by whom, and when.

115. CPPs also need to ensure that partners align their service and financial planning arrangements with community planning priorities. This means ensuring that budget setting and business planning decisions by CPP partners such as councils and NHS boards take full account of community planning priorities and SOA commitments.

116. The national Community Planning Group agreed that it should focus on getting partners to deploy their resources jointly towards partnership objectives.

As a result an Agreement on Joint Working on Community Planning and Resourcing was published in September 2013 (Exhibit 13, page 31). We will review progress during our CPP audits.

Summary and points for action in 2014

- Maintaining good professional working relationships and providing strong political leadership.

- Getting assurance that governance is sound, including where ALEOs are in place.

- Providing stronger leadership of CPPs and working with partners to make the best use of the overall public resources available in the area.

Exhibit 12
A virtuous cycle of continuous improvement in community planning

- Meaningful community consultation
- Working with, and for, communities
- Locality-based planning and service delivery

Effective community consultation and engagement

- SOA as true 'plan for place'
- Improvement targets focused on equalities outcomes
- Shared vision for public service reform driven by the CPP

Ambitious shared improvement priorities

Strong shared leadership supported by effective governance

- Critical review of partnership working and its effectiveness
- Robust self-evaluation by CPPs

Review of outcomes and culture of self-evaluation

Robust planning and alignment of resources to agreed goals

- Partnership prevention plans
- Shared workforce development strategies
- Joint asset planning
- Partner resources directed to agreed improvement areas

- Meaningful, relevant performance data
- Robust challenge and holding to account by CPP boards
- Effective external scrutiny of CPPs

Effective performance management, scrutiny and challenge

Improved outcomes for communities and demonstrable impact of community planning

Source: Audit Scotland

Exhibit 13
Resourcing CPPs – Agreement on joint working

Individually and collectively the relevant partners in each CPP will:

- ensure the SOA is the focal point for the planning and deployment of resources locally

- share budget, investment and resource planning information through the CPP, at an early stage in the decision-making process, including setting out the broad financial parameters they are working to, key milestones, and how resources are already utilised and can further support SOA delivery

- agree how total resources can most effectively be deployed and aligned between partners to achieve the outcomes set out in the agreed SOA and ensure that deployment and alignment in practice

- demonstrate commitment and adherence to this agreement through their engagement with CPPs and in relevant governance and budget-making processes, including final budget documents, delivery plans and subsequent accountability arrangements.

Source: National Community Planning Group

Endnotes
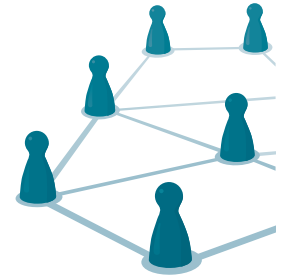
◀ 1   *Early Impacts of Welfare Reform on Rent Arrears - Research Report*, Scottish Housing Regulator, October 2013.

◀ 2   *Housing Impacts of Welfare Reform - Survey of Councils*, COSLA, July 2013.

◀ 3   Community Empowerment (Scotland) Bill, November 2013.

◀ 4   *Scotland's Councillors 2013, Research Report*, Improvement Service, December 2013.

◀ 5   *2014 Scottish Local Government Benchmarking Overview report*, Improvement Service, March 2014.

◀ 6   *Making Choices: Volume 2: A Practice Guide to Best Value, Procurement and Competitiveness*, Scottish Government, December 2001.

◀ 7   *Code of Guidance on Funding External Bodies and Following the Public Pound*, Accounts Commission/COSLA, 1996.

◀ 8   *Managing early departures from the Scottish public sector* (PDF) 🖥 Audit Scotland, May 2013.

◀ 9   CIPFA statement on the role of the chief finance officer, CIPFA.

◀ 10 *Scotland's public finances: Preparing for the future* (PDF) 🖥 Audit Scotland, November 2009 and *Scotland's public finances: Addressing the challenges* (PDF) 🖥 Audit Scotland, August 2011.

Appendix 1

Resource use in 2013 – summary
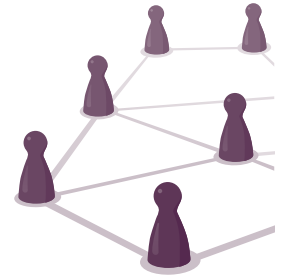
Finance

- Total income was £18.6 billion (Exhibit 14), the same as in 2011/12. The Scottish Government provided around 80 per cent of total income through revenue and capital funding and the redistribution of non-domestic rates.

- Councils spent £20.8 billion, £18.5 billion on services and £2.3 billion on capital.

- Spending on services was £18.5 billion (Exhibit 14), a one per cent reduction on 2011/12 (£18.7 billion). The proportion of spend on individual services was broadly the same as 2011/12.

Exhibit 14
Council income and expenditure 2012/13

General revenue funding from government

£7.8bn

Service fees, charges, other revenue government grants and housing rents
£5.5bn

Council tax **£2.3bn**

Non-domestic rates **£2.3bn**

Capital grants & contributions **£0.7 bn**

Income £18.6 billion

Expenditure £18.5 billion

£5.4bn Education

£3.9bn Social work

£3.4bn Housing

£3.3bn Roads, environment, culture and planning

£1.7 bn Other services and operating expenditure

£0.8 bn Police and fire & rescue services

Source: Audit Scotland

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- **Spending on capital assets was around £2.3 billion**, three per cent less than 2011/12 (£2.4 billion) and around ten per cent less than planned (£2.6 billion). Three-quarters of councils spent less than they planned.

- **Useable cash-backed reserves increased by £174 million (over ten per cent)**, they totalled £1.86 billion at 31 March 2013. Within that **General Fund balances increased by £147 million to £1.05 billion** at 31 March 2013. The amounts earmarked for specific purposes increased significantly by £170 million to £743 million at 31 March 2013.

- **The unearmarked portion of council General Fund balances reduced by £22 million**, around seven per cent, to £312 million (Exhibit 15). This is the first time in recent years that there has been a reduction in unearmarked balances.

- **Net indebtedness has increased**. From a level of £9.1 billion in 2003/04 net indebtedness has increased by around 45 per cent to £13.3 billion at 31 March 2013 (£12.9 billion at 31 March 2012).

Exhibit 15
Earmarked and unearmarked General Fund balances
Percentage increase or decrease on previous year
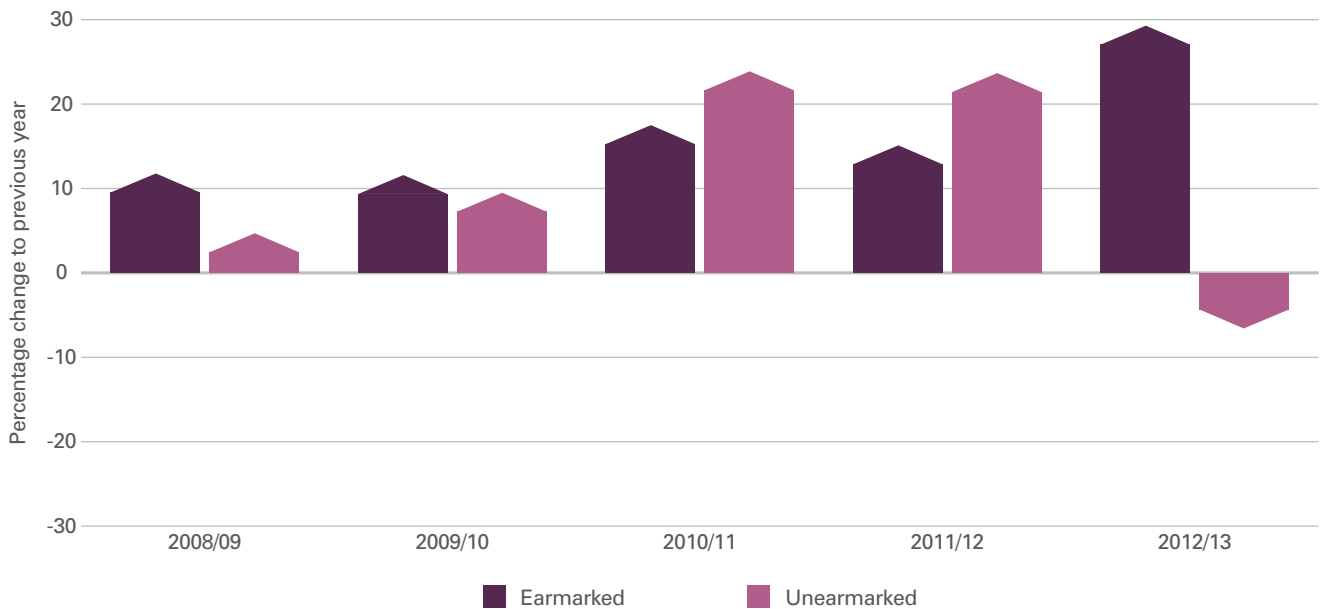
Source: Audit Scotland

Assets

- **Councils held assets worth £38 billion at 31 March 2013**. This is a slight increase in the balance sheet value of assets of £37.4 billion at 31 March 2012 and reflects changes in valuation and accounting adjustments, in addition to spend on assets.

- **Major capital projects generally cost significantly more than councils estimate**. An audit of major capital projects reported that only two-fifths of projects were completed within initial cost estimates. Estimating improved significantly as projects advanced, plans became clearer and contracts were awarded.

Procurement

- **Councils spend over £5 billion annually in procuring goods** to deliver public services, around half of the total for the whole Scottish public sector.

- **Most spending is on social care (23 per cent) and construction/ construction materials (30 per cent)**, spending on goods and services is diverse.

- **Four councils have still to achieve the 50 per cent target level of procurement capability** that the Public Procurement Reform Board set for all public bodies. This is based on the results of the 2013 Procurement Capability Assessment.

Workforce

- **Workforce numbers are falling**. In March 2013 there were 204,500 whole-time equivalent staff employed by councils. In 2009 there were 228,300 whole-time equivalent staff but numbers have fallen by an average of 2.6 per cent each year. This is in part due to the transfer of staff to ALEOs. In the four year period since March 2009, around 9,000 staff transferred to ALEOs. Councils forecast that numbers will continue to fall over the next two years.

- **Staff costs are at least £6 billion**, one-third of the £18.5 billion spent on providing services.

- **Councils paid out £32 million on equal pay claims** in 2012/13. Council balance sheets identify future payments of £73.2 million. Twenty-three from 32 councils have identified the need for potential future payments but their uncertainty means they can not yet be quantified.

- **Sickness absence increased in over two-thirds of councils** in 2012/13. Overall sickness absence rates were 6.6 days for teachers (6.2 the previous year) and 10.9 days for other council staff (10.4 the previous year). These increases go against the trend of recent years.

Appendix 2
Checklist and resources
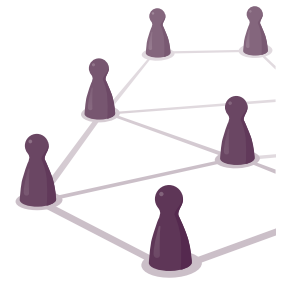
Checklist to support the local government overview report

Do I have a good understanding of the changing context in my council around:		
• financial and service pressures?	Y	N
• the impact of police and fire reforms?	Y	N
• the impact of welfare reform?	Y	N
• the integration of health and social care?	Y	N
Do I understand my role and responsibilities and those of officers?	Y	N
Am I supported in my role?	Y	N
Do I have access to, and take up, appropriate development opportunities?	Y	N
Do officers provide me with performance information which is clear and concise and enables me to judge how well we are doing?	Y	N
Does the information I receive cover:		
• service performance?	Y	N
• service costs?	Y	N
• customer satisfaction?	Y	N
• trend data?	Y	N
• benchmarking data?	Y	N
• targets and outcomes?	Y	N

Question	Assessment	
Do I have good understanding of performance and value for money across the council?	Y	N
Do we, as a council, provide clear information to the public on our performance?	Y	N
Am I provided with options and supporting information to support the decisions on services and capital projects that I have to take?	Y	N
Do I receive cost information that helps me make decisions?	Y	N
Does the way our services are designed and delivered meet people's needs?	Y	N
Am I clear on our objectives, purpose and role when involved with ALEOs?	Y	N
Do I give direction over aims and priorities for charges (in areas where the council has discretion)?	Y	N
Do I understand the non-financial contribution of charges, eg to behaviours and service uptake?	Y	N
Providing strong leadership and governance to support change (paragraphs 65 – 116)		
Is my relationship with other councillors, and with officers, professional and constructive?	Y	N
How effective am I in contributing to constructive challenge and debate at meetings?		
How well do we work together as councillors, and with officers, to deliver the best outcomes for our communities?		
Do I receive information on early retirals along with associated costs and savings?	Y	N
How effective is the Audit Committee (or equivalent)? Is it challenging to officers?		
Do I know who the council's statutory officers are and what they do?	Y	N
How well is the council working with the leaders of community planning partners to deliver better outcomes for communities?		
Are we working with community planning partners to deploy resources jointly in our partnership objectives?	Y	N

Useful resources

Councillors may find the following publications in our 'how councils work' series, along with their checklists useful. These publications explore some of the issues highlighted throughout this report in more detail.

Roles and working relationships: are you getting it right? (PDF)

Arm's-length external organisations (ALEOs): are you getting it right? (PDF)

Using cost information to improve performance: are you getting it right? (PDF)

Managing performance: are you getting it right? (PDF)

Major capital investment in councils: good practice guide (PDF)

Charging for services: are you getting it right? (PDF)

Options appraisal: are you getting it right? (PDF)

An overview of local government in Scotland 2014

This report is available in PDF and RTF formats, along with a podcast summary at:
www.audit-scotland.gov.uk

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REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Depute Chief Executive (Partnership and Services for Communities)

SUBJECT: Options Appraisal: are you getting it right? (Audit Scotland, March 2014)

1 PURPOSE

1.1 To provide Audit and Governance Committee with a summary of the Audit Scotland report, *'Options Appraisal: are you getting it right?'* and the actions being taken by the Council in response to the report's recommendations.

2 RECOMMENDATIONS

2.1 Committee notes the Audit Scotland report and the actions that East Lothian Council is taking to develop the use of options appraisal.

3 BACKGROUND

3.1 *Options Appraisal: are you getting it right?'* (March 2014) is the latest in the Audit Scotland series of 'How Councils Work' reports for councillors and officers. The report is in two parts:

Part 1 looks at the roles that councillors have in options appraisal.

Part 2 provides detail of the options appraisal process.

3.2 This covering report provides a summary of the report's key messages and key issues raised in Parts 1 and 2 and the current position with regards to options appraisal in East Lothian Council.

3.3 The report's key messages are:

- As demand and resource pressures continue to build, councils should *'ensure rigorous and challenging appraisal of options for delivering services'*

- Even for services which are prescribed in legislation and where there is some prescription in what services are provided *'councils*

1

retain substantial discretion on how services are delivered and by whom'

- '*Councils need to consider a wide range of options when considering what services to provide and how to provide them,*' ensuring themselves that they are '*value for money, efficient and effective and demonstrate Best Value'*

- A robust options appraisal helps councils make the important decisions about how services are provided. *'It also helps to ensure that decisions are transparent and based on solid information'*

- The objectives of any options appraisal must be clearly defined and be consistent with the council's strategic policy objectives. *'This might be about providing services in a different say to better meet the needs of residents, it might be about making existing services more effective or it may be about making savings to provide resources for other higher priority areas'.*

Part 1: Councillors have a crucial role in options appraisal

3.4 The Accounts Commission has previously reported that savings made by councils to date have mainly been achieved by reducing workforces, but that this is not sustainable in the longer term. Therefore councils must critically examine current arrangements for service delivery through rigorous options appraisal.

3.5 As councillors face increasingly difficult decisions about where to focus resources it is even more important that they are confident that the council is providing the right services in the right way. The report highlights that *'A robust options appraisal process helps provide assurance to councillors and the public that these decisions are being made on a sound basis and by considering all of the relevant information.'*

3.6 In its 'Overview of Scottish Local Government in Scotland 2013' Audit Scotland had recommended that *'councillors need to ensure rigorous and challenging appraisal of options is undertaken for delivering services.'*

3.7 Audit Scotland suggests that councillors could be involved in:

- agreeing the council's options appraisal framework

- determining the need for an options appraisal

- setting the criteria which will be used to assess which options best fit the council's objectives; e.g. improving performance or achieving savings

- making the decision on which option to implement

2

- scrutinising the implementation of the decision and the impact it has on service delivery.

3.8 The report highlights that some of the factors that might be barriers to effective options appraisal including: unclear objectives, the 'Aye Bin' principle, and, a short-term perspective. In order to counter the perceived barriers councils need to invest the time, effort, staff and money required to undertake rigorous options appraisal with clear governance arrangements

3.9 Appendix 2 of the report provides a checklist of prompt questions designed to help councillors evaluate their role in options appraisal and assess how effective current arrangements in their council are.

Part 2: The options appraisal process

3.10 Options appraisal is a tool that helps to inform decision-making. It does not provide the decision itself. Options appraisal typically includes the following key stages:

- defining the objectives

- gathering information

- identifying, filtering and challenging the options

- assessing and analysing the options

- selecting the preferred option

- implementing the option

- monitoring performance and delivery against objectives.

3.11 The report includes a useful diagram illustrating and providing additional detail on these stages, including consultation with stakeholders at key stages (Exhibit 2, page 16). The report goes on to provide further details on the key stages and key requirements for rigorous options appraisal.

3.12 The report makes the important point that councils have choices about the size and scale of the options appraisal processes they use to ensure that it is proportionate to the significance of the decisions to be made. There are a number of potential triggers for options appraisals:

- Service reviews

- Budget planning or budget imperatives

- Self-assessment

- The outcome of an external inspection or evaluation exercise

- New administration

3

- Poor performance.

3.13   Finally, the report highlights that there is a range of possible outcomes from an options appraisal. Exhibit 3, page 20, illustrates some of the key features of four broad options:

- Retaining service in house

- Delivering services in partnership

- Outsourcing services

- Choosing not to deliver a service.

Options appraisal in East Lothian Council

3.14   The Assurance and Improvement Plan 2014-2017 prepared by the Local Area Network, including Audit Scotland and the Council's auditors as highlighted that the Council's Improvement Framework and work around performance management shows that: "*There continues to be a very strong commitment from officers and members to improving the work of the council.*"

3.15   The Corporate Governance Self Evaluation and How Good is Our Council? self-evaluation carried out in 2012 identified the need to develop a 'more effective use of benchmarking, and guidance and training on the use of benchmarking, Best Value reviews and options appraisal'.   This was included in the Council Improvement Plans for 2012/13 and 2013/14.

3.16   The Council is participating in several national benchmarking exercises being undertaken under the auspices of the Improvement Service based on priorities identified from the Local Government Benchmarking Framework.

3.17   A template for undertaking Best Value Reviews, incorporating options appraisal has been prepared to assist services to undertake Best Value exercises. The options appraisal element of the Best Value Review framework follows the template outlined in the Audit Scotland report.

4   POLICY IMPLICATIONS

4.1   The Audit Scotland report has highlighted the need to develop a systematic approach to options appraisal and to ensure that the role of elected members in options appraisal is recognised.

5   EQUALITIES IMPACT ASSESSMENT

5.1   This report is not applicable to the well being of equalities groups and an Equalities Impact Assessment is not required. However, it is recognised

that whenever options appraisals are carried out by the Council they will be subject to consultation and Impact Assessments.

6   RESOURCE IMPLICATIONS

6.1   Financial – none.

6.2   Personnel – none.

6.3   Other – none.

7   BACKGROUND PAPERS

7.1   *Options Appraisal: are you getting it right*? Audit Scotland, March 2014

AUTHOR'S NAME	Paolo Vestri
DESIGNATION	Service Manger (Corporate Policy and Improvement)
CONTACT INFO	pvestri@eastlothian.gov.uk 01620 827320
DATE	28th August 2014

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How councils work:
an improvement series for councillors and officers

Options appraisal:
are you getting it right?

ACCOUNTS COMMISSION

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The Accounts Commission is the public spending watchdog for local government. We hold councils in Scotland to account and help them improve. We operate impartially and independently of councils and of the Scottish Government, and we meet and report in public.

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- securing and acting upon the external audit of Scotland's councils and various joint boards and committees
- assessing the performance of councils in relation to Best Value and community planning
- carrying out national performance audits to help councils improve their services
- requiring councils to publish information to help the public assess their performance.

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Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Background

Who is this report for?

1. This report is for:

- Councillors – who are responsible for setting strategic direction, taking policy decisions and scrutinising performance. Part 1 (page 9) focuses on the crucial role that councillors have in ensuring that a wide range of options are considered when deciding what services their council should provide and how they are delivered. Councillors also have a leadership role in the options appraisal process itself. Councillors must have the information and support they need to enable them to do this. Appendix 2 (page 31) offers a set of prompt questions which councillors should use to critically appraise arrangements in their council.

- **Chief executives and corporate management teams** – who are responsible for delivering the council's objectives and ensuring that councillors receive the information they need to make informed decisions.

- **Managers** – who are responsible for managing a robust options appraisal process.

2. Part 2 (page 15) is of a more technical nature. Both councillors and managers are encouraged to read it, but its principal target is practitioners engaged in the preparation, implementation and review of options appraisals.

3. We want this report to stimulate discussion among councillors and managers and to support change and improvement. This is critical given the current financial climate and the need to challenge existing ways of doing things. The report supports councillors and officers by signposting sources of information and guidance. We have also included checklists that we hope councillors and officers will find helpful.

4. This report covers:

- The leadership role that councillors have in the options appraisal process.

- Identifying the main options for delivering services and critically assessing them.

- Implementing the decision and monitoring performance.

- Managing an options appraisal process.

What do auditors say?

These boxes appear throughout this report. They have been drawn from Accounts Commission and Audit Scotland audit reports.

Want to know more?

There is a wide range of guidance material available on options appraisal. We reference this material in the report where appropriate.

About our 'how councils work' series

5. The Accounts Commission seeks to support developments in Best Value and how to manage resources such as people and finance. We recognise these as two components vital to successfully delivering council services.

6. Our 'how councils work' series of reports aims to stimulate change and improve performance. We select topics based on the recurring themes and issues from our Best Value audit work, the work of local auditors and our annual overview report.

7. This is the seventh report in the series. Previous reports have examined:

- The roles, responsibilities and working relationships of councillors and council officers in achieving best value (PDF) (August 2010).

- The relationships between councils and their ALEOs (arm's-length external organisations) (PDF) (June 2011).

- The importance of good-quality cost information in policy decision-making and scrutinising performance (PDF) (May 2012).

- The importance of effective performance-management systems (PDF) (October 2012).

- Good practice guide for councils in managing major capital investment (PDF) (March 2013).

- Charging for services (PDF) (October 2013).

8. All reports are available on Audit Scotland's website, www.audit-scotland.gov.uk.

9. This report highlights the importance of councils using rigorous options appraisals to:

- deliver efficient and effective services to local communities

- show they are achieving Best Value.

10. We have worked with the Improvement Service in developing this report and we are grateful for their contribution. We also shared the draft report with some councillors from a number of councils and thank them for their comments.

11. This report is intended as the first of two reports on options appraisal. A follow-up report will consider existing practice in councils on how they undertake options appraisals.

Key messages

1 There are many challenges facing councils, the most pressing being the need to manage financial pressures and the increasing demands on services. The Accounts Commission report *Responding to challenges and change: An overview of local government in Scotland 2013* (PDF) highlighted that demand and resource pressures continue to build for councils. One of our key recommendations was that councils should 'ensure rigorous and challenging appraisal of options for delivering services.'

2 Everything a council does has its roots in legislation. Some services are more prescribed in legislation than others, for example the collection of council tax and business rates. For other services, councils have a lot of discretion on the level of service provided. Even for those services where there is some prescription, it is relatively limited and councils retain substantial discretion on how services are delivered and by whom.

3 Councils need to consider a wide range of options when considering what services to provide and how to deliver them. They must assure themselves that the services they are providing are value for money, efficient and effective and demonstrate Best Value through continuous improvement. They can do this by critically assessing the current arrangements and by looking at how services are provided by other councils and other organisations.

4 Councillors and officers need to be open to considering a broad range of options for delivering services. This might involve providing services in a different way, or even not providing some services at all. These are difficult decisions to make as they affect residents and customers, partner organisations and council staff. A robust options appraisal helps councils make these important decisions and provides assurance that all the relevant issues, including quality, cost and risk have been considered. It also helps to ensure that decisions are transparent and based on solid information.

5 It is vital that councils clearly define the objectives of any options appraisal process. This might be about providing services in a different way to better meet the needs of residents, it might be about making existing services more effective or it may be about making savings to provide resources for other higher-priority areas. When deciding on the objectives, a council needs to ensure that the possible outcomes of any options appraisal are consistent with its strategic policy objectives.

6 As with any process, options appraisal needs to be resourced properly to ensure that it works well. This involves devoting the appropriate time, money, skills and experience to ensure that sound decisions are made. The process needs to be proportionate to the significance of the decision to be made.

Part 1
Councillors have a crucial role in options appraisal
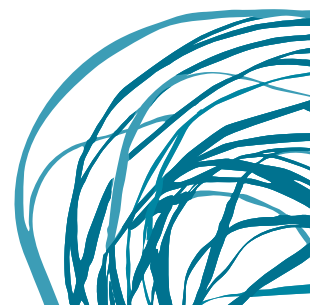
Why is options appraisal important?

12. The Local Government (Scotland) Act 2003 introduced the statutory duty of Best Value in local government. The duty of Best Value requires councils to deliver continuous improvement. The public are entitled to services which are efficient, effective and represent the best possible value for money.

13. Councillors have to make difficult decisions about where to focus the council's resources. In the current financial climate it is even more important that councillors are confident that the council is providing the right services in the right way. They can do this by critically assessing the current arrangements and by looking at how services are provided by other councils and other organisations. They should then consider a wide range of options for delivering services and assess the relative merits of the options. A robust options appraisal process helps provide assurance to councillors and the public that these decisions are being made on a sound basis and by considering all of the relevant information.

14. In addition to the widely accepted benefits of robust options appraisal process there are also significant consequences of not conducting a proper appraisal:

- Services may not be as efficient and effective as they could be.

- Services may not be achieving value for money.

- Resources may not be directed to priority areas, such as preventative expenditure, and the council's strategic objectives may not be achieved.

- The council may face criticism from residents and customers.

- The council may face criticism from the Accounts Commission, auditors and other scrutiny agencies.

- The council will not be able to demonstrate that it is achieving Best Value.

What is options appraisal?

15. An options appraisal is all about making well-informed decisions. The *Best Value – Making Choices, Volume One: A Manager's Guide to the Strategic Framework for Best Value, Procurement and Competitiveness* published by the Scottish Government in 2001 noted that, as with any decision-making tool, options appraisal provides support to the process, it does not provide the answers. The value of decision-making tools is that they take people through the process stage by stage, and they assist in making sure that everything relevant is taken into account.

am I considering all of the options on how services might be delivered?

16. The basic stages of an options appraisal process (Exhibit 1) were set out in our report *Arm's-length external organisations (ALEOs): are you getting it right?* (PDF) published in 2011.

Exhibit 1
Basic stages of an options appraisal process
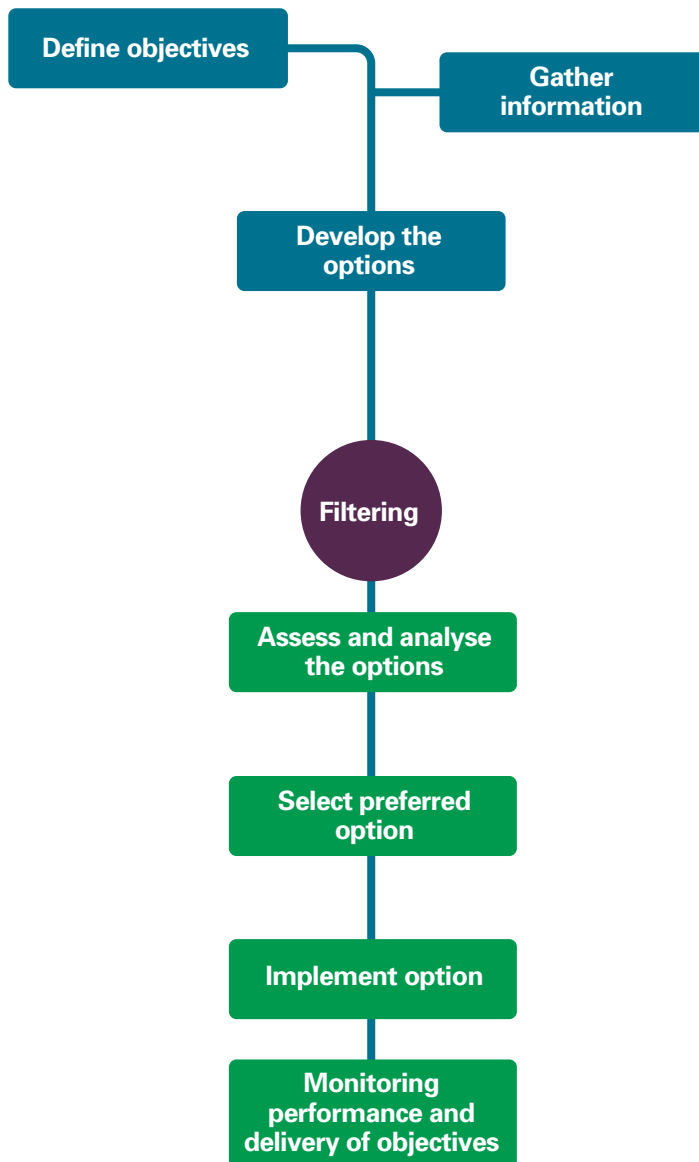
Source: *Capital Planning and Option Appraisal – A Best Practice Guide for Councils*, CIPFA Local Government Directors of Finance, October 2006, adapted by Audit Scotland

17. We have developed this further to highlight the role of councillors, the key reporting stages and the importance of consultation with stakeholders. This more detailed process map is shown in Exhibit 2 (page 16).

18. There is a wide range of possible outcomes from an options appraisal process. These include:

- delivering services in partnership (with other councils, with other public or voluntary organisations or with the private sector)

- setting-up an arm's-length organisation like a charitable trust

- outsourcing services to a private sector supplier

- retaining services in-house

- setting-up an employee-owned cooperative or mutual company

- deciding not to deliver a service at all.

19. In 2011, the National Audit Office published *Options Appraisal: Making informed decisions in government*. The report found that the quality of options appraisal varied within and between departments across government. It is reasonable to assume that this is also the case in the public sector in Scotland.

What role does a councillor play in options appraisal?

20. Councillors have a crucial role in options appraisal. The Accounts Commission report *Responding to challenges and change: An overview of local government in Scotland 2013* (PDF) recommended that councillors need to ensure rigorous and challenging appraisal of options is undertaken for delivering services.

What do auditors say?

Councillors need to oversee options appraisals that involve potential major shifts in how services are provided. They have a key role, for example in agreeing the broad objectives of the options appraisal, in the appraisal process itself or in scrutinising the process and emerging proposals.

Source: *Arm's-length external organisations (ALEOs): are you getting it right?* (PDF)
Accounts Commission, June 2011

21. Councils that involve councillors in determining the need for an options appraisal to be carried out have often been more successful in obtaining a good outcome. At the outset, councillors should consider the significance of the options being considered and assure themselves that the options appraisal process being used to help them make the decision is robust and proportionate.

22. Councillors have an important role in ensuring strong corporate ownership of options appraisal. Councillors need to be involved in agreeing the framework, in effect they are agreeing 'the rules of the game' to ensure that they have confidence in the options being presented to them. This also helps to ensure a consistent and systematic approach to options appraisal is used across the council.

23. Weighing up the relative merits of the options is an important part of the process. Councillors may therefore have a role in setting the criteria which will be used to assess which options best fit the council's objectives. For example, if the priority is improving performance, this will feature strongly in the assessment criteria. In other cases achieving savings might be the priority, so that will feature more prominently. In any options appraisal, however, the criteria should include both quality and cost. The council also needs to consider the impact on equalities and sustainability.

24. The most important part of any councillor's role in an options appraisal is the decision on which option to implement. This can have far-reaching consequences on the services the council delivers, how it delivers them and ultimately on the users of those services.

25. Following the decision, councillors also have an important role in scrutinising the implementation of the decision and the impact it has on service delivery. This can be achieved by monitoring performance and the delivery of service objectives on a regular basis.

Important considerations

26. In our 2010 report *Roles and working relationships: are you getting it right?* (PDF) we highlighted that councillors need to be open to considering a wide range of options for providing services and that decisions must be transparent and evidence based, taking cost and quality into account.

27. It is essential that councillors have the appropriate skills to scrutinise options appraisals. Councillors have an important role in asking officers challenging questions to assure themselves that the appraisal is robust and that all of the relevant issues are being considered.

28. Careful consideration also needs to be given to resourcing options appraisal as the outcome may have far-reaching consequences for residents, customers and the council. Councils also need to consider whether or not the council has the necessary skills and expertise in-house to carry out the appraisal. Some of the options being considered may be innovative or complex and it may be that specialist external support is required.

29. The council also needs to consider the timing of options appraisals. Wherever possible the process should align with a council's planning and budgeting timetables, so that any important decision on service delivery can inform and be informed by these processes. Councils also need to consider the timing in relation to the political cycle, including local and national elections. Experience indicates that difficult decisions become far more problematic politically in the run-up to an election.

30. Appendix 2 (page 31) to this report includes a checklist of prompt questions designed to help councillors evaluate their role in options appraisal and assess how effective current arrangements in their council are.

Potential barriers to an effective options appraisal

31. Options appraisal can be extremely challenging for councils, for councillors, for managers and for staff. Loyalties run deep in councils, councillors hold strong political beliefs and balancing competing interests is always difficult. But the duty of Best Value on making best use of public resources must always be paramount.

32. Councillors should be aware of things that might get in the way of an effective options appraisal. These include:

- **Unclear objectives:** a council needs to take the time and be clear about the reasons why services are provided in-house. There may be good reasons for this; it may be due to the specialist nature of the service, the vulnerability of the client group, the absence of an alternative provider or issues of equality and fairness. They need equally to be clear which services are open to alternative forms of service delivery through a rigorous options appraisal. We have seen examples, however, where councils have spent time and public money pursuing alternative service delivery options, only to withdraw late in the process.

- **The 'Aye Bin' principle:** change is never easy, it can be challenging for officers and for councillors to radically change the way a council has provided a service often over a lengthy period of time. Councillors might believe that options appraisal would be too difficult and fear that the alternatives seem too radical. Councillors may also be uncomfortable with alternatives given their personal and political sympathies and aspirations.

- **A short-term perspective:** focusing too much on the 'here and now' or on the short term can mean that the longer-term benefits are not fully considered.

What do others say?

Options should be appraised on their costs and benefits, not on personal preferences of key stakeholders or individuals.

Source: *Options Appraisal Workbook: Planning Advisory Service pilot projects*, Local Partnerships (jointly owned by HM Treasury and Local Government Association), 2012

33. The Accounts Commission has previously reported that the savings made to date have mainly been achieved by reducing workforces, but that this is not sustainable in the longer term. Councils must therefore critically examine their current arrangements for service delivery through rigorous options appraisal. But to gain acceptance of the need for options appraisal, councils need to invest the time, effort, staff and money. This would help councillors, managers, employees and other key stakeholders understand the importance of options appraisal and the use it can have to deliver the council's overall objectives. Councillors have a crucial role in ensuring that local communities understand this as well.

34. Councils can address some of the perceived barriers by making sure that for any options appraisal, it has the right people involved, that those people have the right skills and that everyone has clear roles and responsibilities. Furthermore by putting in place clear governance structures at the outset of the options appraisal, this will ensure that the decisions on selecting the preferred options are transparent.

What do we mean by governance?

Governance is about how local government bodies ensure that they are doing the right things, in the right way, for the right people, in a timely, inclusive, open, honest and accountable manner.

It comprises the systems and processes, and cultures and values, by which local government bodies are directed and controlled and through which they account to, engage with and, where appropriate, lead their communities.

Source: *Delivering Good Governance in Local Government*, SOLACE/CIPFA, 2007

Part 2

The options appraisal process
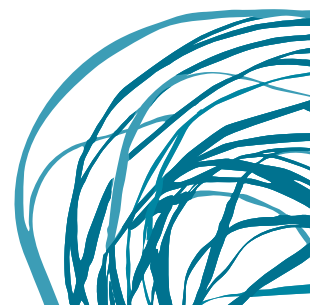
An options appraisal process is all about making well-informed decisions

35. Options appraisal is a tool that helps to inform decision-making. As with any decision-making tool it provides support to the process – it does not provide the decision itself. Best Value review teams, senior managers and elected members still have to make judgements and it may be necessary to explain those judgements to others. The value of decision-making tools is that they take people through the process stage by stage and they assist in making sure that all the relevant factors are taken into account. A decision that has been carefully considered in discussion with others and informed by a robust process is more likely to be successful.

36. Options appraisal typically includes a number of key stages:

- defining the objectives

- gathering information

- identifying, filtering and challenging the options

- assessing and analysing the options

- selecting the preferred option

- implementing the option

- monitoring performance and delivery against objectives.

37. These stages are illustrated in Exhibit 2 (page 16) and we say more about each of them in the sections that follow.

38. The key stages of options appraisal can be used to help make decisions at a number of different levels, from strategic decisions about services to more specific decisions about projects or operational matters. Councils have choices about the size and scale of the options appraisal processes they use to ensure that it is proportionate to the significance of the decision to be made.

a decision that has been carefully considered in discussion with others and informed by a robust process is more likely to be successful

Exhibit 2
Stages of an options appraisal

Triggers for an options appraisal

For example:
• Service reviews
• Budget planning
• Self-assessment
• New administration
• Poor performance

Define objectives

Gather information

Consult with stakeholders to establish objectives and constraints

Report initial business case to council

Develop the options

Consultation on selection and weighting of criteria

Regular reporting to council on the progress of the options appraisal

Filtering

Assess and analyse the options

Further options appraisal required if preferred option involves an external provider

Report to council outlining available options and business case

Select preferred option

Communicate decision made to stakeholders

Develop and report full business case

Implement option

Service user satisfaction information

Monitoring performance and delivery of objectives

Regular performance reports to relevant committee(s)

Further triggers for options appraisal

• Poor performance
• Non-compliance of contract
• Not meeting agreed objectives

Source: *Capital Planning and Option Appraisal – A Best Practice Guide for Councils*, CIPFA Local Government Directors of Finance, October 2006, adapted by Audit Scotland

Everyone involved needs to have clear roles and responsibilities

39. It is important to be clear about who is accountable for the options appraisal and who will be involved in the work. It is also important that those involved keep an open mind and remain objective. A range of people may be involved in the appraisal depending on the significance of the decision being taken and at different stages in the process. These might include:

- Councillors – to agree the overall approach to options appraisal and indicate a willingness to consider a wide range of options.

- Senior officers – to oversee the process, critically appraise the options, make recommendations and implement the chosen option.

- Council officers within the service areas being appraised – to provide service-specific knowledge and expertise.

- Chief financial officers and other finance officers – to provide specialist financial skills to the appraisal team.

- Trade union representatives – to represent any staff who may be affected by the decisions taken.

- External advisers – to provide specialist advice and an independent perspective.

40. Councils may also consider involving staff from other service areas or organisations in an appraisal team to provide fresh perspectives and insights from their own experiences.

41. Council officers need to ensure training is made available to councillors and other staff involved in the options appraisal process so that they can each fulfil their respective roles effectively.

Defining clear objectives is critical for success

42. The need to carry out an options appraisal process may come from a variety of sources. These 'triggers' might include:

- a strategic review of service delivery, for example as part of a council's transformation programme or improvement plan

- the outcome of a self-evaluation exercise

- the outcome of an external evaluation exercise

- poor service performance – highlighted by performance indicators and through benchmarking comparisons

- a new administration is formed

- budget imperatives

- policy direction.

43. It is vital that councils clearly define the objectives of any options appraisal process. When deciding on the objectives, a council needs to ensure that the possible outcomes are consistent with its policy objectives. In a practical sense this means checking the objectives with key strategic documents including the Single Outcome Agreement, the Corporate Plan and service plans.

Good-quality information informs good decisions

44. Good decisions are made when they are based on good information. The information should provide decision-makers with what they need to fulfil their role effectively.

45. How much information is needed will depend on the significance of the decision being made. The information requirements are likely to become more detailed at each stage of the options appraisal process. For example, the final stages of a process involving competitive bidding will require detailed financial and quality information, and may require legal advice in some cases.

46. At various stages of the process those involved are likely to need information about:

- The current position
  - the context – the demands facing the service and the environment within which it operates
  - current performance and costs.

- The options
  - 'strategic fit' with the council's policy objectives
  - impact on the quality of service for the customer
  - financial implications (both costs and savings) and value for money
  - legal implications
  - risk assessment
  - impact on other council services and partner organisations.

47. Councils should invest sufficient time to gather the relevant information. This leads to a more constructive challenge from the outset, provides for a more rigorous options appraisal process overall and therefore a well informed decision.

Consulting with stakeholders is a key to success

48. The size, nature and subject of the options appraisal will determine who the key stakeholders are. At the outset it is useful to do a stakeholder analysis to identify:

- who the stakeholders are

- what their interest and contribution to the process might be

- how and when to consult with them.

49. In our report *Major capital investment in councils* (PDF) published in March 2013, we highlighted that engagement with a wide range of stakeholders is an important part of any project. While this related to major capital projects, it is equally applicable to the options appraisal process.

What do auditors say?

Every project has stakeholders. These can cover a range of different groups including local residents, businesses, employees, service users, suppliers and public sector bodies such as health boards. Engaging and consulting with stakeholders is essential in achieving a successful project outcome. Stakeholders' interest in a project can have both positive and negative effects on its progress. Their concerns may also create additional risks to a project's outcomes. Engaging with stakeholders effectively is therefore important and should be a vital part of project planning from the start. Consulting with stakeholders can often be a lengthy process. But it can shape the project at an early stage and help ensure a more successful outcome.

Source: Major capital investment in councils: Accounts Commission March 2013

Critically appraising a wide range of options ensures the process is robust

50. At an early stage of the process, councils should develop a 'long list' of options. This long list should include those which might be considered radical, for example ceasing to provide a service. This is to ensure that all options are considered, so that, even if they are then ruled out, this is done by design rather than oversight.

51. Those involved in the options identification stage need to be open-minded and creative in thinking what the options might be. The 1999 Accounts Commission report *Better together? Making improvements by reconfiguring services (PDF)* highlighted the importance of 'thinking radically about options'. It suggested this be done right at the beginning of the process, generating ideas by, for example, benchmarking and looking beyond current boundaries and practices. This might include looking at good practice elsewhere in the public sector, the private sector and what happens more widely in the UK and internationally.

52. There is a range of possible outcomes from an options appraisal process and many different ways to deliver services. These include retaining services in-house, delivering services in partnership, outsourcing services or even choosing not to deliver a service at all. Some of the key features of these broad options are illustrated in Exhibit 3 (page 20). The exhibit is designed to be illustrative rather than comprehensive as there is a huge range of options a council can consider.

Filtering options

53. The next stage is filtering the 'long list' of options into a shorter list which will be the subject of more detailed analysis and assessment. To do this, councils need to agree a set of criteria. The criteria and the decision made to 'rule in' or 'rule out' options at this stage should be recorded. This is important for accountability and transparency.

54. This stage of the process shares many of the characteristics of the later, more detailed stages of assessment of the options (Exhibit 4, page 21).

Exhibit 3
Possible outcomes from an options appraisal

In-house

🔍 **Key features**

- The in-house team
  - is delivering economy, efficiency and effectiveness
  - has capacity/capability to sustain good performance
  - can generate sufficient funds
- No market for service or activity
- High risk of failure, so better managed in-house
- Not delivering activity directly would question authority's ability to function as an organisation
- Benefits of other options outweighed by costs of implementation

Status quo by retaining current arrangements

In-house services: Reconfigured, re-engineered services (including service merger, one-stop-shops, online)

Bring services back in-house

Outsourcing

🔍 **Key features**

- Economies of scope
- Economies of scale
- Innovation and investment
- Increased productivity
- Effective management of risk
- Access to investment
- An opportunity to stimulate or influence market development

Contract out to external supplier

Service transferred to trust or arm's-length external organisation

Partnership

🔍 **Key features**

- Opportunities to develop an effective 'mixed economy' of approaches for achieving the authority's objectives
- Risks and benefits are shared between the council and the partner organisation

Shared services with other councils

Service provided in collaboration with other public sector agencies/ voluntary sector

Mutualisation, services run with service users or employees

Cessation

🔍 **Key features**

- Little or no demand for the service
- Costs of provision outweigh any benefits
- There are alternative providers of the service – and individuals using those providers would not be disadvantaged
- The activity does not contribute to the council's objectives
- No statutory or strategic requirement to make provision

Stop delivering the services, the council no longer provides or funds the service

Note: Economics scope – as commercial and not-for-profit organisations concentrate on their specialisms or areas of expertise. An organisation specialising in the care of elderly people may be able to deliver better value than one that delivers services to a range of client groups. Economies of scope may also come from the development of a team of specialists working with a number of different clients.
Best Value – Making Choices, Volume Two: A Practice Guide to Best Value, Procurement and Competitiveness, Scottish Government, 2001
Source: Audit Scotland, 2014

Exhibit 4

The options appraisal process becomes more detailed as it progresses

At each stage the process of options appraisal can become more detailed and more focused on comprehensive, specially collected, data. In the early stages the process for options appraisal will be the guarantee of consistency of approach. At the final stages it will be both process and data that are important. If that final stage is one of tender evaluation in a competitive bidding process it will be possible to undertake sophisticated analysis of financial and quality data that simply did not exist at the early stages.

Source: *Best Value – Making Choices, Volume One: A Manager's Guide to the Strategic Framework for Best Value, Procurement and Competitiveness,* Scottish Government, 2001

55. Having developed a 'shortlist' the next stage is to carry out a detailed assessment. There is a range of ways to go about this.

56. At this stage, councils should refine the assessment criteria to help decide on the preferred option. The criteria will depend on what service or project is being considered, but will typically include three main areas:

- Performance appraisal.

- Financial appraisal.

- Risk appraisal.

Performance appraisal

57. In assessing the relative merits of options, decision-makers will need to consider what effect each of the options will have on service performance. This should include an assessment of current performance (to provide a 'baseline') and what the anticipated effect each option would have on future performance. The performance appraisal should include a mix of both quantitative and qualitative measures. These might include an assessment of:

- customer experience and satisfaction

- contribution to the council's policy objectives and outcomes, including equalities and sustainability

- changes to the services, including when they are available and what services are offered.

58. This kind of appraisal is most effective when it uses a broad range of performance criteria and where data and projections include comparisons:

- over time

- against targets

- with other organisations.

What do auditors say?

The characteristics of good performance information is that it is:

- accurate
- timely
- meaningful (but not overly detailed)
- relevant
- high quality
- well presented.

Source: *Managing performance: are you getting it right?* (PDF) Accounts Commission, October 2012

Financial appraisal

59. A robust financial appraisal is another important part of an options appraisal process. In developing a financial appraisal of the options, councils will need to consider:

- initial set-up/transfer costs associated with each option
- operational costs/savings
- staff costs/savings
- tax and non-domestic rates implications
- central/recharge costs/savings.

What do auditors say?

As with other performance measures, it is important that councils understand the key assumptions on which any unit costs are based to ensure that any comparisons are relevant and that any differences are understood. For example, when comparing costs, councils must be clear about what overheads are included in the make-up of a unit cost. If this is not clear there is a risk that councils are not comparing like with like. This is particularly important when councils are using cost information to inform an options appraisal process. For example, if comparing the costs of an external supplier with an 'in-house bid', councils must ensure that the cost information is comparable to ensure that the bids are being assessed consistently.

Source: *Using cost information to improve performance: are you getting it right?* (PDF) Accounts Commission, May 2012

60. The assessments of costs and benefits should also include adjustments for 'optimism bias' and assess risks and uncertainties. Optimism bias is the tendency for appraisers to be over-optimistic about estimates of costs, timescales and benefits. As a result councils should build in appropriate allowances to estimates to take account of this, for example by increasing the cost estimates, decreasing the projected benefits or extending the timescales over which costs and benefits are being considered. *The Green Book – Appraisal and Evaluation in Central Government* by HM Treasury (2003) has further guidance on addressing optimism bias and provides an adjustment procedure to help address 'systematic optimism that historically has afflicted the appraisal process.'

Risk assessment

61. Carrying out a robust risk assessment is also an important part of an options appraisal process. This is even more important when the options being considered are very different to the way things are currently done. However, even the status quo has associated risks which decision-makers need to take into account.

62. Those responsible for carrying out the options appraisal should identify any risks and uncertainties associated with each of the options. It is important that councillors are made aware of and fully understand the nature and degree to which any risks identified influence the appraisal results.

63. There are a variety of tools to support risk assessment processes, though these typically include an assessment of risk in terms of:

- strategic/commercial risks

- economic/financial/market risks

- legal/regulatory risks

- organisational/management/human resource risks

- political risks

- environmental risks

- technical/operational/infrastructure risks.

The decision on selecting the preferred option needs to be transparent

Scoring and weighting systems

64. Some of the costs and benefits cannot be valued in monetary terms, but they still need to be taken into account. These include environmental, social, political or legal considerations. It is important that these considerations are recorded and, where possible, quantified.

65. Scoring and weighting systems offer a way of systematically assessing a range of factors to assess the relative merits of the options. There is a range of guidance available on using scoring and weighting systems (Want to know more?, page 29).

66. Exhibit 5 illustrates a scoring and weighting approach, using a simplified worked example.

Exhibit 5
Key stages in the weighting and scoring method

- Identify the various objectives/criteria/factors against which the options are going to be scored. These should relate closely to the project objectives.

- Give each of these objectives a weighting (a value within a certain range) to reflect relative importance. Good practice would be to consult or involve stakeholders in identifying the criteria and weighting their relative importance.

- Each option is then allocated a score to reflect how closely it meets the identified objectives.

- Multiply the weight of each factor by the relevant score and sum to find the total weighted score for each option. Generally the highest score against the criteria would be the best option.

Criteria	Weight	Option 1		Option 2		Option 3	
		Score	Weighted score	Score	Weighted score	Score	Weighted score
Criteria 1 – performance	40	2	80	4	160	3	120
Criteria 2 – cost/savings	30	5	150	1	30	3	90
Criteria 3 – policy fit	15	1	15	3	45	5	75
Criteria 4 – risk	15	2	30	1	15	3	45
	100						
Total weighted score			**275**		**250**		**330**

Source: Audit Scotland, 2014

Having a good business case supports effective decision-making and accountability

67. Having a robust business case is vital for good decision-making, accountability and transparency. A clear business case will include a summary of the analysis done so far and set out the relative merits of the options clearly. The business case is a key document in an options appraisal process. Exhibit 6 (page 25) outlines what a good business case might include.

68. In our recent report *Managing Capital Projects* (PDF) we found that business cases were not being used effectively enough.

Exhibit 6
The options appraisal process becomes more detailed as it progresses

A business case should:

- provide an assessment of whether spend/save proposal is worthwhile
- clearly communicate conclusions and recommendations.

An effective business case should help you answer three questions

- Have you taken into account all relevant factors in deciding what the project should be?
- Should you go ahead with the project?
- What is the best way to carry out the project?

Source: Options Appraisal training material, CIPFA, 2013

What do auditors say?

Many councils do not have established processes for developing and using business cases. Where available, business cases are often short and highly summarised and do not all reflect good practice. Without good-quality and realistic business cases, particularly at the initial approval stage, key performance information on aims, cost, time, scope and risk may not be clearly defined. This may make it more difficult to hold decision-makers to account if problems arise on a project.

Source: *Major capital investment in councils* (PDF) Accounts Commission, March 2013

69. HM Treasury and the Improvement Service make reference to three types of business case:

- The preliminary or initial business case, which establishes the case for change and defines the strategic objectives of the options appraisal work.

- The outline business case, which sets out the options being considered, draws together the main findings of the appraisal and recommends a preferred option.

- The full business case will follow the selection of the preferred option and may lead to the selection of a preferred provider or procurement of a service.

Good governance arrangements underpin good decisions

70. For an options appraisal process to be effective there needs to be strong governance arrangements in place. Any significant decision arising from an options appraisal is likely to be made within the council's existing governance arrangements, through its committees and full council.

What do auditors say?

Good Practice – managing capital programmes (options appraisal)

Put a clear and effective governance structure in place and ensure responsibilities are clearly defined, allocated and understood. The structure should provide scope for constructive challenge and effective scrutiny at all stages of the programme.

Source: *Major capital investment in councils* (PDF) Accounts Commission, March 2013

71. It is good practice to set out a clear reporting framework at the start of an options appraisal. Regular reporting on progress should be built into the process, so that senior officers and elected members are kept informed.

72. Reports should be clear and contain the most relevant information. They should be detailed enough, but avoid being unnecessarily long and overly complicated, as this risks diluting important messages. Reports should also avoid using technical jargon.

73. When considering difficult and potentially controversial options, it is important that the decision-making process is – *and is seen to be* – robust. The decisions must be open to public scrutiny, although there will be stages in the process where some information is managed carefully to respect commercial confidentiality.

Implementing the chosen option and monitoring performance

74. Councils need to monitor the implementation of the decision and what difference this is making to services. The 1999 Accounts Commission report Better together? Making improvements by reconfiguring services (PDF) highlighted the key factors to consider when implementing a chosen option. These factors are just as relevant today and focus on people, planning and performance (Exhibit 7, page 27).

75. The Scottish Government 'Making choices' guidance highlights that 'implementation must be properly managed and planned so the benefits of the proposed option can be achieved. Authorities should have a clear plan for implementing the changes proposed, with clear milestones for the completion of key stages.' This involves the careful consideration of transition arrangements including communicating with service users, resource management (budgets, staff and assets) and performance monitoring.

Exhibit 7
Success factors for implementing a decision

Attention needs to be paid to people, planning and performance management to implement change successfully.

People

Who will manage the project?

Who else needs to be involved in running the project?

Is a project sponsor needed - a councillor and/or member of the management team?

Who will be affected by the change?

How will we communicate with them?

What training will be required?

Planning

What budget approvals are required?

What is the timetable for the work?

What are the milestones?

What needs to happen, and when, to meet the milestones?

Performance

What are the objectives of change?

What are the performance targets?

What monitoring arrangements are there?

What are the reporting arrangements?

Source: *Better together? Making improvements by reconfiguring services* (PDF) 🖥 Accounts Commission, May 1999

76. Where a council has chosen to go into partnership or externalise a service it is important that this is supported by an appropriate contract or service level agreement (SLA). This should set out the services to be provided, the level of service required and the standards to be maintained throughout the duration of the agreement. The performance of the service provider should be monitored on a regular basis to ensure compliance with these conditions. Service level agreements should include:

- defined objectives

- roles and responsibilities (for both the council and the service provider)

- clear performance targets

- clear monitoring arrangements (including what information is to be supplied and when)

- escalation arrangements (which may be required if the service provider is not meeting the requirements of the agreement).

What do auditors say?

…the council remains accountable for the funds used to deliver public services, regardless of the means by which the service is delivered. Consequently, it is important for the council to be able to 'follow the public pound' to the point where it is spent. This requires well-thought-through governance arrangements from the outset and action to ensure those arrangements are applied effectively in practice.

Source: *Arm's-length external organisations (ALEOs): are you getting it right?* (PDF)
Accounts Commission June 2011

Reviewing the process can help decisions in the future

77. In addition to monitoring the effectiveness of the new service delivery arrangements, councils should also review the options appraisal process itself. It should consider:

- How effective was the options appraisal process in delivering the stated objectives?

- Was the appraisal process itself delivered on time and on budget?

- What lessons have been learned which should inform future options appraisals?

Further work

78. This report is intended as the first of two reports on options appraisal. A further report will include a study of existing practice in councils in how they undertake options appraisals.

Want to know more?

There is a wide range of guidance material available on options appraisal. Some of this is general in nature and some is more specific to particular circumstances or projects.

- *The Local Government in Scotland Act 2003: Best Value guidance* (PDF), Scottish Government, 2003, Chapter 5

- *Best Value – Making Choices, Volume One: A Manager's Guide to the Strategic Framework for Best Value, Procurement and Competitiveness* (PDF), Scottish Government, 2001

- *Best Value – Making Choices, Volume Two: A Practice Guide to Best Value, Procurement and Competitiveness* (PDF), Scottish Government, 2001

- *Better together? Making improvements by reconfiguring services* (PDF), Accounts Commission, 1999

- *The Green Book – Appraisal and Evaluation in Central Government* (PDF), HM Treasury, 2003

- *Options appraisal: Making informed decisions in Government* (PDF), NAO, 2011

- *Scottish Transport Appraisal Guidance – Best practice transport appraisal guidance*, Transport Scotland, 2008

- *Building Our Future: Scotland's School Estate* (PDF), Scottish Government, 2004

- *Healthy Competition: How councils can use competition and contestability to improve services* (PDF), Audit Commission, 2007

- *Capital Planning and Options appraisal – A best practice guide for councils*, CIPFA Local Government Directors of Finance, 2006

- *Options Appraisal: A Practical Guide for Public Service Organisations*, CIPFA, 2011

Appendix 1
What an effective council looks like
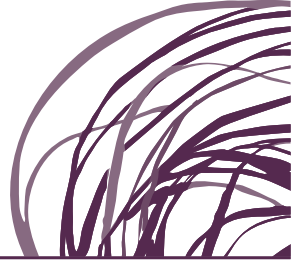
An effective council will:

- Consider a wide range of options for services:
  – what services it wants to deliver
  – how services are delivered (in-house, in partnership, by others).

- Have a robust process in place to:
  – define the objectives of any options appraisal process
  – identify options
  – analyse the options.

- Make clear and transparent decisions based on good-quality information.

- Implement the decision it has taken effectively.

- Have robust performance management arrangements in place to monitor service performance (regardless of whether the service is being delivered in-house, in partnership, or by another service provider).

- Review the effectiveness of its decision – to check that objectives are being delivered.

Appendix 2
Questions for councillors

References found within the councillor part of the report.

References to more detailed information which can be found elsewhere in the report.

Reference	Questions for councillors	Yes/No	Action
On the options for delivering services			
Key messages 2-3	Are there any restrictions, for example legal or financial, to providing this service in a different way?		

Paragraphs 18 and 23
 	
Paragraphs 50-52 and Exhibit 3
	Am I considering all of the options on how services might be delivered?
	
	• Does the current service provider:
	  – deliver economy, efficiency and effectiveness?
	  – have the capacity and capability to sustain good performance?
	  – generate sufficient funds or make the required savings?
	
	• Does the service directly contribute to the council's objectives?
	
	• Am I clear about what the full range of alternatives are for providing this service?
	  – Are there alternative providers for the service?
	
	• Is the risk of failure so high that risks are better managed in-house?
	
	• Are the potential benefits of other options outweighed by the costs of implementation?
	
	• Are there opportunities to:
	  – develop an effective 'mixed economy' of approaches for achieving the council's objectives?
	  – share the risks and benefits with partner organisations?		

Cont.

Reference	Questions for councillors	Yes/No	Action

On the options for delivering services (continued)

Reference	Questions for councillors	Yes/No	Action

Paragraphs 18 and 23
 	
Paragraphs 50-52 and Exhibit 3
	• Would the service benefit from:
	  – economies of scope (by providing a more specialised service)?
	  – economies of scale (by being bigger)?
	  – innovation and investment?
	  – increased productivity?
	  – access to investment?
	  – an opportunity to stimulate or influence market development?
	• Is there a demand for the service?		

On the options appraisal process

Reference	Questions for councillors	Yes/No	Action
Paragraph 23 Paragraphs 42-43	Am I clear about what the options appraisal is trying to achieve?		
Exhibit 2	Does my council have a robust process in place to help me decide on the options?		
	At the start of the process:		
Paragraph 43	• Have we set clear objectives?		
Paragraph 42	• Am I clear about why we are considering the options?		
	• Are those objectives consistent with the council's strategic objectives and policies?		
Paragraphs 39-41	• Have we set out clear roles and responsibilities?		
Paragraphs 70-73	• Have we agreed a clear plan which identifies what decisions need to be made and by whom?		
Paragraphs 48-49	• Have we identified the key stakeholders who need to be consulted?		
Exhibit 2	During the process:		
	• Am I getting regular updates on progress?		
	• Am I involved at the appropriate decision points?		
	• Is the process progressing to plan?		
Paragraph 27	• Am I getting the support I need from officers?		

Cont.

Reference	Questions for councillors	Yes/No	Action
On making sound decisions			
Paragraphs 44-47	Am I getting the information I need to make the decision?		
Paragraphs 57-58	• On the performance implications?		
Paragraphs 59-60	• On the financial implications?		
Paragraphs 61-63	• On the risks?		
Paragraphs 67-68	• Is there a clear business case?		
Paragraph 43	• Is the decision consistent with the council's strategic objectives?		
Paragraphs 48-49	• Have stakeholders contributed to the options appraisal process and what are their views?		
Paragraph 31	• Am I clear about how I balance my personal and political views with my statutory duty of Best Value?		
On implementing the decision			
Paragraphs 74-76	Am I getting the information I need to be assured that:		
	• the decision is being implemented effectively?		
	• it is having the desired effect?		

Appendix 3
Questions for officers

References found within the councillor part of the report.

References to more detailed information which can be found elsewhere in the report.

Reference	Questions for officers	Yes/No	Action
Defining the objectives			
Paragraphs 42-43	• Are the main reasons/drivers for considering other delivery arrangements clear? – performance – financial – risk – strategic priorities. • Am I clear about how the options relate to the council's corporate priorities?		
Agreeing the process			
Paragraph 21	• Have the elected members approved a robust options appraisal process?		
Paragraphs 39-41	• Is everyone aware of the roles and their responsibilities in the options appraisal framework being used? • Have I developed a clear plan for the process and identified: – timescales? – resource implications? – roles and responsibilities? – skills and expertise? – governance arrangements?		
Identifying and filtering options			
Paragraph 18	• Am I confident that I am identifying the full range of options? – Do I know how similar services are delivered by other councils in Scotland and in the UK? – Do I know how similar services are delivered in the private sector?		
Paragraphs 42-52			

Cont.

Reference	Questions for officers	Yes/No	Action
Identifying and filtering options (continued)			
Paragraph 18 Paragraphs 42-52	• Am I clear about the relative merits of the options? – 'Strategic fit' with the council's policy objectives – Impact on the quality of service for the customer – Financial implications (both costs and savings) – Legal implications – Risk assessment – Impact on other council services.		
Assessing and analysing options			
Paragraphs 53-69	• For the 'shortlist' of options have I considered: – all of the current and future costs and benefits? – legal and financial implications? – risks? – practical implications of delivering the option? • Is there a robust process in place to help members take the decisions? • Have I clearly presented all of the information members will need to make the decision? – On current and projected costs, performance and risks – Business case(s) including assumptions.		
Implementing the option			
Paragraphs 74-77	• Have I developed a clear action plan to implement the decision? – Timetable – Resources – Managing the risks. • Have I ensured that there are robust arrangements in place to monitor and report performance, regardless of the option chosen? – Contract – Service level agreement – Performance and financial reporting – Escalation arrangements if things go wrong. • Have I carried out a 'lessons learned review' to inform future options appraisals?		

Options appraisal:
are you getting it right?

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along with a podcast summary at:
www.audit-scotland.gov.uk

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Audit and Governance Committee Annual Work Plan 2014/15

Date	Internal Audit Reports	External Audit Reports	Accounts Commission/ Audit Scotland reports	Governance	Risk
9/09/14	Mobile Payment Devices Residential Units for Young People Fostering and Kinship Care Allowances National Fraud Initiative Housing Allocations Investigation Internal Audit Plan Progress Report	Draft Annual Report to Members ALEOs – Are you getting it right? Statutory Performance Indicators	Overview of Local Government in Scotland How Councils Work: Options Appraisal		Corporate Risk Register
18/11/14	Modernisation Programme Bathroom Adaptations Internal Audit Plan Progress Report		Managing Procurement in Councils Re-shaping Care for older People	2014/15 Council Improvement Plan Monitoring Report	Children's Wellbeing Service Risk Registers Adult Wellbeing Service Risk Register Education Service Risk Register
20/01/15	Internal Audit Plan Progress Report		Self Directed Support Scotland's Public Finances		Council Resources Service Risk Register Communities and Partnerships Service

				Borrowing and Treasury Management in Local Government		Risk Register
						Infrastructure Service Risk Register
						Development Service Risk Register
						Risk Strategy Update
17/03/15	Audit Plan 2015/16					
19/05/15	Controls Assurance Statement 2013/14 Internal Audit Plan Progress Report				2015 Corporate Governance Self-evaluation/ Annual Governance Statement	
14/07/15					Draft 2014/15 Annual Accounts	

East Lothian Council

REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Depute Chief Executive – Resources & People Services

9

SUBJECT: Internal Audit Report – Mobile Payment Devices

1   PURPOSE

1.1   To inform the Audit and Governance Committee of the recently issued audit report on Mobile Payment Devices.

2   RECOMMENDATION

2.1   That the Audit and Governance Committee note the contents of the Executive Summary and Action Plan for Mobile Payment Devices.

3   BACKGROUND

3.1   A review of Mobile Payment Devices was undertaken as part of the audit plan for 2013/14.

3.2   The Council offers a range of methods for tenants to pay their rent arrears. In 2013 the Council introduced Mobile Payment Devices as an additional method of collecting payments – the devices are currently used by Officers making home visits to tenants with rent arrears.

3.3   The main objective of the audit was to ensure that the internal controls in place for Mobile Payment Devices were operating effectively.

3.4   The main findings from our audit work are outlined in the attached report.

4   POLICY IMPLICATIONS

4.1   None

5   EQUALITIES IMPACT ASSESSMENT

5.1   This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.

6   RESOURCE IMPLICATIONS

6.1   Financial - None

6.2   Personnel - None

6.3   Other - None

7   BACKGROUND PAPERS

7.1   None

AUTHOR'S NAME	Mala Garden
DESIGNATION	Internal Audit Manager
CONTACT INFO	01620 827326
DATE	28 August 2014

EAST LOTHIAN COUNCIL – INTERNAL AUDIT
MOBILE PAYMENT DEVICES

1. EXECUTIVE SUMMARY

1.1 Introduction

As part of the Audit Plan for 2013/14 a review was undertaken of the mobile chip and PIN payment devices introduced by the Council's Revenues Section. A summary of our main findings is outlined below.

1.2 Areas where Expected Controls were Met

- The mobile payment devices introduced for the collection of rent arrears comply with the Payment Card Industry Data Security Standard (PCI DSS).
- Income received via mobile payment devices is fully integrated into the Council's Income Management system.
- Each of the mobile payment devices has been configured to accept payments of Housing Rent, Council Tax and Business Rates.
- Rent arrears payments collected via the mobile payment devices had been properly recorded in the tenant's housing rent account and the Council's general ledger.
- Regular reconciliations are performed between the Income Management system and the banking records.

1.3 Areas with Scope for Improvement

- For staff dealing with card payments, no corporate policy or procedures are in place to ensure compliance with the PCI DSS. *Risk – non-compliance with the PCI DSS.*
- The mobile payment devices in use have not been set up to record the operator's ID – the current configuration does not identify individual members of staff using the devices. *Risk – errors and irregularities may occur and remain undetected.*
- The use of mobile payment devices for the collection of rent arrears requires review – the annual support costs for operating the mobile devices are currently in excess of the total income being collected. The devices may be better suited for the collection of income for other chargeable services, which would enable customers to make card payments for services provided. *Risk – failure to make effective use of the Council's mobile payment devices.*
- The procedures for handling rent arrears payments received by cash require review – at present the receipts issued to tenants paying their rent arrears by cash fail to provide a clear audit trail. *Risk – errors and irregularities may occur and remain undetected.*

1.4 Summary

Our review of Mobile Payment Devices identified a number of areas with scope for improvement. Detailed recommendations and opportunities for improvement are contained in our main audit report.

Mala Garden
Internal Audit Manager   **August 2014**

ACTION PLAN

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.1.1	Detailed corporate procedures should be drawn up to ensure that all staff dealing with card payments comply with the Payment Card Industry Data Security Standard.	Medium	Head of Council Resources/ Service Manager - Revenues	Agreed		December 2014
3.2.1	Management should ensure that members of staff using the mobile payment devices are set up with an individual Operator ID number.	Medium	Service Manager - Revenues	Will investigate whether device functionality will allow such a set up and will explore alternatives if not.		October 2014
3.5.1	Management should ensure that the storage, retention and destruction of cardholders' data complies with both PCI DSS requirements and Council procedures.	Medium	Service Manager - Revenues	Agreed Records (receipts) now stored in locked drawer and will be destroyed after 18 months, in line with ELC Retention Policy.		In place

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.6.1	Management should review the current usage of the mobile payment devices – a detailed action plan should be drawn up outlining how the use of the devices can be rolled out to ensure that the Council obtains maximum benefit from them. Consideration should be given to redeploying some of the devices to other areas within the Council where a chargeable service is being offered.	Medium	Service Manager - Revenues	Agreed Will review usage to ensure maximum benefit to the Council.		December 2014
3.7.1	Management should ensure that a clear audit trail is maintained for all cash payments received – a duplicate receipt book should be used for recording cash received and a copy of the receipt given to the tenant.	Medium	Service Manager - Revenues	Agreed Investigating option to reconfigure mobile devices to produce receipt for cash payments, but if this is not possible duplicate receipt books will be ordered for use.		September 2014

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.7.2	The procedures for handling cash payments received should be formalised and issued to all relevant members of staff.	Medium	Service Manager - Revenues	Agreed Formal cash handling procedures to be developed and training session to be held for staff.		September 2014
3.8.1	Management should ensure that adequate documentation is maintained to evidence training provided on the use of the mobile payment devices.	Medium	Service Manager - Revenues	Agreed Refresher training to be provided for staff and training records to be held and maintained by Team Leader.		September 2014

Grading of Recommendations

In order to assist Management in using our reports, we categorise our recommendations according to their level of priority as follows:

Level	Definition
High	Recommendations which are fundamental to the system and upon which Management should take immediate action.
Medium	Recommendations which will improve the efficiency and effectiveness of the existing controls.
Low	Recommendations concerning minor issues that are not critical, but which may prevent attainment of best practice and/or operational efficiency.

REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Depute Chief Executive – Resources & People Services

SUBJECT: Internal Audit Report – Residential Units for Young People

10

1 PURPOSE

1.1 To inform the Audit and Governance Committee of the recently issued audit report on Residential Units for Young People.

2 RECOMMENDATION

2.1 That the Audit and Governance Committee note the contents of the Executive Summary and Action Plan for Residential Units for Young People.

3 BACKGROUND

3.1 A review of the IT arrangements operating at the Council's Residential Units for Young People was undertaken as part of the audit plan for 2013/14.

3.2 The main objective of the audit was to ensure that the IT arrangements in place at the Council's Residential Units for Young People were operating effectively.

3.3 The main findings from our audit work are outlined in the attached report.

4 POLICY IMPLICATIONS

4.1 None

5   EQUALITIES IMPACT ASSESSMENT

5.1   This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.

6   RESOURCE IMPLICATIONS

6.1   Financial - None

6.2   Personnel - None

6.3   Other - None

7   BACKGROUND PAPERS

7.1   None

AUTHOR'S NAME	Mala Garden
DESIGNATION	Internal Audit Manager
CONTACT INFO	01620 827326
DATE	28 August 2014

EAST LOTHIAN COUNCIL – INTERNAL AUDIT
RESIDENTIAL UNITS FOR YOUNG PEOPLE

1. EXECUTIVE SUMMARY

1.1 Introduction

As part of the Audit Plan for 2013/14 a review was undertaken of the IT arrangements in place at the Council's Residential Units for Young People. A summary of our main findings is outlined below.

1.2 Areas where Expected Controls were Met

- A Policy on the Acceptable Use of the Council's Information & IT Infrastructure (Acceptable Use Policy) is in place and provides guidance to all staff members using the corporate network.
- A separate PC/Internet Policy is in place, which provides guidance to the young people at the residential units with access to computers that are not part of the corporate network.
- Adequate arrangements are in place for monitoring the internet usage of young people at the residential units.
- Antivirus software has been installed on the computers used by the young people that are not part of the corporate network.

1.3 Areas with Scope for Improvement

- User access controls in place require review – staff members and aftercare clients can access the non-network computers with a generic login and password. *Risk – lack of an audit trail.*
- There was a failure to retain the weekly internet activity reports for both staff and young people as evidence of the monitoring carried out by the Administrator. *Risk – lack of evidence of checks carried out.*
- The Council's Acceptable Use Policy requires review – the existing policy fails to clearly outline the procedures that should be followed by users of non-network computers. *Risk – failure to provide clear guidance.*
- The existing arrangements for recording details of software installed and licences held require review. *Risk – failure to comply with legislation.*
- There was a lack of a detailed inventory of all IT assets held at the residential units. *Risk – loss or theft may occur and remain undetected.*
- The current arrangements for the destruction of IT hardware require review. *Risk – data held may not be properly erased.*

1.4 Summary

Our review of the IT arrangements operating at the Council's Residential Units for Young People identified a number of areas with scope for improvement. Detailed findings and recommendations are contained in our main Audit Report.

Mala Garden
Internal Audit Manager   **August 2014**

ACTION PLAN

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.1.2	Management should ensure that the existing Policy in place for young people using the computers is reviewed and updated. Management should ensure that the updated policy is issued to all young people at the residential units.	Low	Residential Services Manager	To be confirmed		
3.2.1	Management should ensure that all staff members and aftercare clients using the computers are set up with individual user accounts and passwords – under no circumstances should generic logins and passwords be used.	Medium	Residential Services Manager	To be confirmed		
3.3.2	Management should ensure that internet activity reports and email alerts received by the Administrator are sent to an ELC email account. Management should ensure that a clear audit trail exists to evidence the monitoring arrangements in place – the weekly internet activity reports should be retained and held securely in line with the Council's existing IT arrangements.	Medium	Residential Services Manager	To be confirmed		

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.3.2 (cont)	Management should ensure that a record is maintained of all restricted internet sites unblocked by the Administrators.					
3.3.3	Management should ensure that the activity reports of staff members, including the activity reports relating to the Administrators are reviewed by an independent person. Evidence of this check should be retained.	Medium	Residential Services Manager	To be confirmed		
3.4.1	Management should maintain a register of all software installed together with details of licences held.	Medium	Residential Services Manager	To be confirmed		
3.4.2	The IT Acceptable Use Policy should be reviewed to ensure that it clearly outlines the procedures that should be followed by users who are currently responsible for the administration of non-network computers.	Medium	Service Manager IT Infrastructure	To be confirmed		
3.5.1	Management should ensure that a detailed inventory is maintained of all IT assets held by the Unit.	Medium	Residential Services Manager	To be confirmed		

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.6.1	**Management should ensure that all IT software/hardware is disposed of in accordance with the Council's IT Acceptable Use Policy.**	**Medium**	**Residential Services Manager**	**To be confirmed**		
3.7.1	**Management should ensure that the Council's IT division provides support and advice to local administrators with responsibility for non-network computers – reviews should be undertaken to ensure compliance with Council Policy.**	**Medium**	**Service Manager IT Infrastructure**	**To be confirmed**		

Grading of Recommendations

In order to assist Management in using our reports, we categorise our recommendations according to their level of priority as follows:

Level	Definition
High	Recommendations which are fundamental to the system and upon which Management should take immediate action.
Medium	Recommendations which will improve the efficiency and effectiveness of the existing controls.
Low	Recommendations concerning minor issues that are not critical, but which may prevent attainment of best practice and/or operational efficiency.

East Lothian Council

REPORT TO:	Audit and Governance Committee
MEETING DATE:	9 September 2014
BY:	Depute Chief Executive – Resources & People Services
SUBJECT:	Internal Audit Report – Fostering and Kinship Care Allowances

11

1 PURPOSE

1.1 To inform the Audit and Governance Committee of the recently issued audit report on Fostering and Kinship Care Allowances.

2 RECOMMENDATION

2.1 That the Audit and Governance Committee note the contents of the Executive Summary and Action Plan for Fostering and Kinship Care Allowances.

3 BACKGROUND

3.1 A review of Fostering and Kinship Care Allowances was undertaken as part of the audit plan for 2014/15.

3.2 The main objective of the audit was to ensure that the internal controls in place for Fostering and Kinship Care Allowances were operating effectively.

3.3 The main findings from our audit work are outlined in the attached report.

4 POLICY IMPLICATIONS

4.1 None

5   EQUALITIES IMPACT ASSESSMENT

5.1   This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.

6   RESOURCE IMPLICATIONS

6.1   Financial - None

6.2   Personnel - None

6.3   Other - None

7   BACKGROUND PAPERS

7.1   None

AUTHOR'S NAME	Mala Garden
DESIGNATION	Internal Audit Manager
CONTACT INFO	01620 827326
DATE	28 August 2014

EAST LOTHIAN COUNCIL – INTERNAL AUDIT
FOSTERING AND KINSHIP CARE ALLOWANCES

1. EXECUTIVE SUMMARY

1.1 Introduction

As part of the Audit Plan for 2014/15 a review was undertaken of the internal controls in place for the payment of Fostering and Kinship Care Allowances. A summary of our main findings is outlined below.

1.2 Areas where Expected Controls were Met

- The Council has in place a 'Children's Wellbeing Kinship Care and Fostering Strategy: Payments to Foster Carers and Kinship Carers' – the Strategy was approved by Cabinet in April 2013.
- For the sample of foster carers reviewed we found that a placement agreement was in place.
- All fees and allowances for both foster care and kinship care payments had been correctly updated on the Frameworki System.
- All payments made for both foster care and kinship care were in accordance with the approved rates.

1.3 Areas with Scope for Improvement

- The draft Kinship Care Policy and Guidance in place requires to be finalised and issued to relevant members of staff with responsibility for administering kinship care allowances. *Risk – lack of a consistent approach.*
- There was a lack of formal agreements in place for kinship carers clearly outlining the roles and responsibilities of both the carers and the Council. *Risk – failure to fully undertake roles and responsibilities.*
- There was a lack of adequate documentation in place for initiating kinship care payments to both formal and informal carers. *Risk – unauthorised payments may be made.*
- In some cases, the Foster Carer Payment Fee Form had not been appropriately authorised. *Risk – unauthorised payments may be made.*
- For kinship care payments there was a lack of adequate monitoring arrangements in place to ensure that payments are stopped on a timely basis. *Risk – overpayments may occur.*
- In some cases, increases to foster carers' fee levels had not been approved by the Fostering and Adoption Panel. *Risk – inappropriate payments may be made.*

1.4 Summary

Our review of Fostering and Kinship Care Allowances has identified a number of areas with scope for improvement. Detailed findings and recommendations are contained in our main Audit Report.

Mala Garden
Internal Audit Manager   **August 2014**

ACTION PLAN

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.1.1	Management should ensure that the draft Kinship Care Policy and Guidance in place is finalised and issued to relevant staff members with responsibility for administering kinship care allowances.	Low	Group Service Manager – Children's Wellbeing Protection and Family Support	Kinship Care Policy and Guidance remained draft awaiting outcome of significant Scottish Government decision making around kinship carer finance. SG have extended the reporting time of short life working group to look at this over last two years. The Kinship Care Steering Group signed off current document on 23rd July. All staff will be issued with a copy of the draft document, including those administering kinship care allowances.		September 2014
3.4.2	For all kinship carers approved by the Kinship Care Panel, Management should ensure that a formal Agreement is in place and is retained on Frameworki.	Medium	Group Service Manager – Children's Wellbeing Protection and Family Support	Children's Wellbeing Senior Managers Group (SMG) have agreed a refresher session to all Children's Wellbeing staff, including administrative support, to ensure all staff aware of processes and documentation to be used.		October 2014

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.4.2 (cont)	Management should ensure that appropriate documentation is in place for informal kinship carers supported by the Council.					
3.5.1	Management should ensure that for all new placements the Foster Care Fee Payment Form is properly authorised by a designated officer.	Medium	Group Service Manager – Children's Wellbeing Long Term Care and Support	Workflow system to initiate Foster Carer Fee payments has been developed by Frameworki Team in consultation with Community Resources. Rollout has been delayed due to demands on lead Systems Development Officer and difficulties confirming training dates for relevant staff over summer period.	Since the implementation of a gatekeeping process (2006) to discuss all children on the cusp of care or requiring to be accommodated by the local authority, agreement that social workers and senior practitioners can sign off fee forms which initiates payment to carers. With reduced number of managers in Community Resources ensures no delay in payment. Gatekeeping process-Internal Provisions panel now multi-agency.	November 2014

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.5.1 (cont)					As foster carer payment made up of two payments – allowance for child and FC fee already checks built into system and Internal panel endorses decision to accommodate child. This is relevant until the new FWi system is in place.	
3.5.2	Management should ensure that the existing arrangements for payments to Kinship Carers are formalised – appropriate documentation should be in place and authorised by a designated officer.	Medium	Group Service Manager – Children's Wellbeing Protection and Family Support	See 3.4.2 above Payment documentation and authorisation will be managed through Frameworki.		October 2014

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.6.1	Management should ensure that all increases to foster carers' fee levels are approved by the Fostering and Adoption Panel. Management should ensure that carers' approved fee levels are detailed on the Panel minutes and the annual review letters sent to carers.	Medium	Group Service Manager – Children's Wellbeing Long Term Care and Support	Foster Carers apply to become Level 2 or Level 3 carers and demonstrate they meet criteria. The Fostering Panel makes recommendation to the Agency Decision Maker. With current budget constraints as per report to Cabinet (April 2013) Community Resources as team agree number of Level 1 carers eligible to apply for Level 2 (4 for 2014-2015). There are time limited changes to fee covered in Foster Carer Handbook. Agree these decisions should be endorsed by next available Fostering Panel. Community Resources recently updated the format of Supervising Social Worker's report for foster carer review and this ensures more detail regarding Level of skill i.e. Level 1, 2 or 3. Agree there has been inconsistency in recording the skill level in Foster Carer		September 2014

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.6.1 (cont)				Approval and review minutes and subsequent Foster carer approval letters will now record this.		
3.6.2	Management should ensure that regular reports are produced of all payments where manual adjustments have been made, to ensure that carers are being paid at the correct rates.	Medium	Group Service Manager – Children's Wellbeing Long Term Care and Support	Agreed. Regular reports will be produced as recommended.		September 2014
3.6.3	Management should ensure that annual reviews are carried out for children placed with both Formal and Informal Kinship Carers to ensure that payments being made are still valid.	Medium	Group Service Manager – Children's Wellbeing Protection and Family Support	Children placed in formal kinship care are LAC and statutory review processes in place. Finance will be added to checklist for discussion at statutory reviews.		September 2014

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.6.3 (cont)	Management should explore the facilities within Frameworki to establish if a system prompt is available to alert staff when a young person reaches the age of 16.			A system has recently been developed to annually review informal kinship care payments, beginning this September.		September 2014
	Management should investigate all potential overpayments identified and ensure that appropriate action is taken to recover the overpayments.			Group Service Manager Protection and Family Support will investigate overpayments identified.		September 2014
3.6.4	Management should review the current practice whereby level 3 carers who do not have a current placement are paid retainer fees beyond the 12 week period.	Medium	Group Service Manager – Children's Wellbeing Long Term Care and Support		Group Service manager alerted to these situations – rare as level 3 carers skills are in demand. Payment of an ongoing retainer to Level 3 Foster Carers has been established practice since the Level 3 Foster Carer Scheme introduced (Feb 2000). The	Awaiting Scottish Government Working group report regarding Foster carer Allowances.

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
3.6.4 (cont)					**scheme has been regularly best value reviewed and evidences positive outcomes for the young people placed with them. Awaiting outcome of Scottish Government short life working group on Foster Carer Payments, before reviewing terms and conditions of foster carers. It is the favourable terms and conditions we offer our foster carers that enables us to retain our foster carer community despite independent fostering agencies offering more favourable financial payments.**	

Grading of Recommendations

In order to assist Management in using our reports, we categorise our recommendations according to their level of priority as follows:

Level	Definition
High	Recommendations which are fundamental to the system and upon which Management should take immediate action.
Medium	Recommendations which will improve the efficiency and effectiveness of the existing controls.
Low	Recommendations concerning minor issues that are not critical, but which may prevent attainment of best practice and/or operational efficiency.

REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Depute Chief Executive – Resources & People Services

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SUBJECT: Audit Scotland Report – The National Fraud Initiative in Scotland (June 2014)

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1 PURPOSE

1.1 To inform the Audit and Governance Committee of the Audit Scotland report on 'The National Fraud Initiative in Scotland' issued in June 2014.

2 RECOMMENDATION

2.1 That the Audit and Governance Committee note the key messages contained in Audit Scotland's report, 'The National Fraud Initiative in Scotland'.

3 BACKGROUND

3.1 The National Fraud Initiative (NFI) is a data matching exercise, which is led by Audit Scotland and runs every two years. The purpose of the exercise is to match electronic data, both within and between participating bodies. NFI seeks to help participating bodies identify cases of fraud and detect and correct any over or under payments. The data for NFI in Scotland is processed by the Audit Commission on behalf of Audit Scotland.

3.2 The Audit Scotland report outlines the key messages and outcomes from the 2012/13 NFI exercise. In 2012/13, 127 bodies took part from the local government, central government, health and further education sectors and the total outcomes amounted to £16 million. Of the £16 million, £10.5 million was identified as a direct result of the 2012/13 NFI investigations.

The most successful matches in terms of financial outcomes, accounting for 78% of the total outcomes, were:

- pensions – 36%

- housing benefits – 29%

- blue badges – 13%

3.3 The Audit Scotland report concluded that 81% of participating bodies had managed their role satisfactorily. However, concerns were highlighted in the following areas:

- Bodies are slow to follow up matches.
- There is limited or no Internal Audit monitoring of the NFI approach and outcomes to ensure identified weaknesses are addressed.
- Fraud and error policies and strategy did not integrate the NFI arrangements.
- Reporting the NFI progress and outcomes to senior management and board/members is limited or does not happen.

3.4 In an East Lothian context, Internal Audit has played a key role in the 2012/13 NFI exercise. The findings from the NFI investigations were initially reported to the Audit and Governance Committee in January 2014. A summary of the outcomes of the investigations is outlined below:

- Number of matches processed – 826

- Errors identified – 86

- Frauds identified – 3

- Total outcomes – £44,053

3.5 The data collection for the 2014/15 NFI exercise will be undertaken in October 2014 and the matches should be available early in 2015. The results of the data matching exercise for 2014/15 will be reported to the Audit and Governance Committee as part of the audit plan for 2015/16.

4   POLICY IMPLICATIONS

4.1 None

5   EQUALITIES IMPACT ASSESSMENT

5.1 This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.

6   RESOURCE IMPLICATIONS

6.1   Financial - None

6.2   Personnel - None

6.3   Other - None

7   BACKGROUND PAPERS

7.1   Audit and Governance Committee, 21 January 2014, Internal Audit Report – National Fraud Initiative

AUTHOR'S NAME	Mala Garden
DESIGNATION	Internal Audit Manager
CONTACT INFO	01620 827326
DATE	28 August 2014

The National Fraud Initiative in Scotland

Contents

Summary

Key facts

£16 million — Overall outcomes[1,2]

127 — Public bodies took part

832 — Housing benefit frauds identified

3,851 — Overpayments are being recovered

81 per cent — Bodies managed their NFI roles satisfactorily

1   For national reporting purposes, outcomes are collated as at 31 March 2014. Outcomes recorded by participants after this date are included in subsequent reports.

2   Outcome figures referred to cover detected fraud, overpayments and error and include those already delivered as well as those that have been estimated where this is appropriate.

Key messages

1 Public bodies spend billions of pounds of taxpayers' money on the Scottish population, providing services and financial assistance to all citizens including those that need them the most. Systems underpinning public spending can be complex and errors can happen. Unfortunately, there are also some individuals who seek to exploit the systems and fraudulently obtain services and benefits to which they are not entitled.

2 Fraud does not recognise organisational or geographic boundaries. Data sharing enables bodies to match data internally and externally. Technology provides an efficient way to connect discrete data sets and therefore can limit gaps available for fraudsters to manipulate and help identify those that have. It also helps bodies to identify process improvements that can reduce future errors and the costs of correcting these errors.

3 Audit Scotland, working closely with public bodies, external auditors and the Audit Commission, has completed another major data sharing and matching exercise. The National Fraud Initiative (NFI) exercises make a significant contribution to the security and transparency of public sector finances by confirming that services are provided to the correct people and by reducing fraud and error.

4 Since we last reported on *The National Fraud Initiative in Scotland (PDF)* in May 2012, outcomes valued at £16 million have been recorded and the cumulative outcomes from the NFI in Scotland are now at £94 million. These outcomes are a significant return to the public finances of Scotland at a time when public finances continue to be under pressure. Across the UK the cumulative total is now £1.17 billion. What cannot be measured, but is important, is the deterrent effect that undertaking regular data sharing and matching exercises has, such as the NFI.

5 The NFI 2012/13 involved 127 Scottish bodies across four sectors making this the largest and most diverse data sharing exercise since the NFI began. Scottish bodies submitted 599 data sets and these generated 382,137 data matches for further investigation.

6 There are 4,447 investigations still in progress and action is being taken to recover £4.5 million of overpayments.

7 The benefits of data sharing and matching enabled bodies external to those who submitted the data to identify outcomes of £1.5 million.

8 Most organisations take advantage of the opportunities provided by the NFI but some could act more promptly to investigate matches and therefore stop frauds and correct errors more quickly.

9 The introduction of the Single Fraud Investigation Service (SFIS) has major implications for the resourcing of non housing benefits counter-fraud work. Councils should review their counter-fraud resources in light of this change and whether they are sufficient to deal with corporate fraud.

10 The Cabinet Office will take over responsibility for the NFI team and web application from April 2015. Audit Scotland expects no impact of this change for the NFI 2014/15 exercise which is due to start in summer 2014.

Recommendations

All participants

- Audit Committees, or equivalent, should review the self-appraisal checklist at Appendix 2, Part A to ensure that they are fully informed of the planning and the progress being made by their officers investigating the NFI 2014/15 exercise.

- All public audited bodies participating in the NFI should ensure that they maximise the benefits of their participation in the NFI. In particular, they should consider:
  – whether it is possible to work smarter on the NFI matches; reviewing the suggestions at Appendix 3 should help
  – using the NFI matches in conjunction with alternative matching services from other providers.

Local authorities

- Local authorities should take steps to retain or invest in sufficient capability, in the short and long term, to investigate non housing benefit fraud or corporate fraud, including relevant NFI matches, after the SFIS is introduced.

- Local authorities that administer pension schemes and are not already using more regular data matching to deceased records should consider doing this.

Part 1

Background

Key messages

1 The NFI is linked to the statutory audit of participating bodies and the results are reported every two years by Audit Scotland.

2 Data matching is an effective and efficient method to identify areas for further investigation by connecting discrepancies between different data sets. The powers to undertake data matching given to Audit Scotland enable it to cross entity boundaries and national borders.

3 The success of the NFI comes primarily from the public servants who investigate the data matches and the external auditors who review their arrangements.

1. Audit Scotland has coordinated another major counter-fraud exercise working together with a range of Scottish public bodies, external auditors and the Audit Commission to identify fraud and error. These exercises, known as the NFI, are undertaken every two years and are linked to the statutory audits of the participating bodies. The latest exercise (the NFI 2012/13) started in October 2012 and is now nearing completion.

2. The success of the NFI comes primarily from the public servants who:

- investigate the NFI data matches

- identify and stop frauds and errors

- recover overpayments

- hold fraudsters accountable
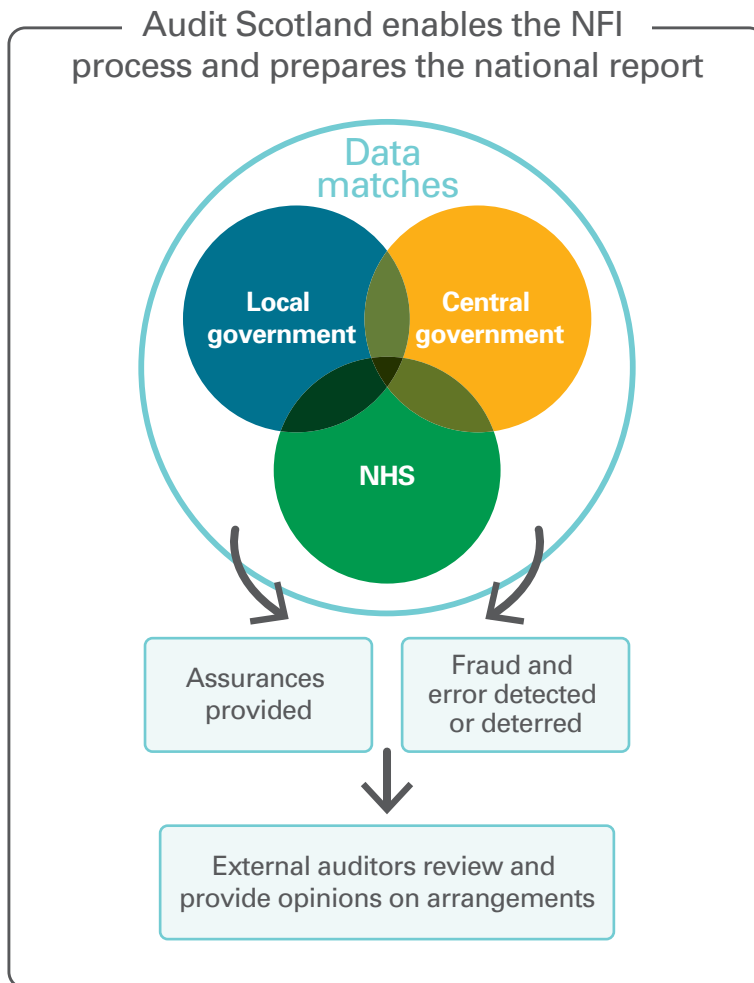
- improve their systems.

3. The role of external auditors in the NFI is vital. They review and conclude on the effectiveness of local arrangements in terms of how well the NFI is integrated into counter-fraud polices. They also provide assurance on the progress being made on the NFI investigations. Auditor conclusions provide the evidence for Part 3. Helping to improve, holding to account (page 28).

the NFI supports the public sector in taking action to prevent and detect fraud and error

4. Exhibit 1 summarises the relationships and responsibilities within the NFI in Scotland.

Exhibit 1
Relationships and responsibilities within the NFI in Scotland

Audit Scotland enables the NFI process and prepares the national report

Data matches

Local government

Central government

NHS

Assurances provided

Fraud and error detected or deterred

External auditors review and provide opinions on arrangements

Source: Audit Scotland

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5. The NFI in Scotland is now well established and has been operating for over a decade since it was first piloted. The NFI enables public bodies to take advantage of computer data matching techniques to detect fraud and error. The NFI remains the largest national fraud detection and prevention scheme that can provide data matches within and between public bodies. Its key features are that it:

- acts as a deterrent to potential fraudsters

- identifies errors and fraud thus enabling appropriate action to recover money and/or press criminal charges

- can provide assurances, similar to a regular health check, that systems are operating well and can also identify where improvements are required

- operates across boundaries between public bodies in different sectors and countries

- represents value for money in terms of the efficiencies deliverable through centralised data processing and identifying targeted high-priority matches.

6. The NFI works by using data matching to compare a range of information held on bodies' systems to identify potential inconsistencies or circumstances that could indicate fraud or error which are called 'matches'. A match does not automatically mean that there is a fraud or error and investigations are required to enable the correct conclusion to be drawn for each match. Bodies investigate these and record appropriate outcomes on a secure web application based on their investigations.

7. For the NFI 2012/13 exercise Audit Scotland increased the number of bodies involved to 127, including a large further education college and a greater number of central government bodies. All data sets were mandated.

8. Audit Scotland also includes data about its own employees and those of audit firms carrying out external audit work for the Auditor General for Scotland and the Accounts Commission.

9. In total 599 data sets were submitted for data matching. These returned 382,137 matches and of these, 62,172 were identified as recommended matches, being matches with a higher risk of fraud or error. It is up to individual bodies to determine which and how many matches to investigate. Exhibit 2 provides some examples of the types of data set matches undertaken.

Exhibit 2
Examples of the types of data set matches undertaken

	Type of data match	Potential fraud or error
	Housing benefit claimants to employees and public sector occupational pensions	Employees or occupational pensioners may claim benefit without declaring their income or by under-declaring the amounts.
	Employees to employees	An employee may be on long-term sick leave while working at another body.
	Public sector pensions to deceased persons' records	A pensioner's death may not have been reported to the pension authority. The pension continues to be paid to a bank account or may be collected by a relative.
	Blue badges to deceased persons' records	The permit holder's death may not have been reported to the council. The permit may continue to be used fraudulently or be sold for improper use.
	Employees to immigration records[1]	It is unlawful for someone to obtain employment if they are not entitled to reside or work in the UK.

Note: 1. This includes data about refused and expired visas, visas where there is no right to work and failed asylum applications.
Source: Audit Scotland

10. In addition to the main matching exercise, a separate exercise has been undertaken to match electoral registers against those households where council tax single person discounts are being claimed. The data uploads took place in October 2011 and the results were provided to councils in January 2012 to investigate.

11. Across the UK only two councils, Angus and Perth and Kinross, decided not to upload data for this particular data match. The NFI is one of the proven ways by which councils can address fraud and error in this area. A number of councils also employ credit reference agencies to match single-person details against a wider range of data sets such as credit and utility records.

12. Audit Scotland carries out the NFI process under powers in the Criminal Justice and Licensing (Scotland) Act 2010. It is important for all parties involved that this exercise is properly controlled and data handled in accordance with the law. The governance arrangements for the NFI are summarised at Appendix 1 (page 35).

13. The NFI is important in the context of the economic climate and fiscal projections for future public sector expenditure. The NFI exercises make a significant contribution to the security and transparency of public sector finances by ensuring that services and benefits are paid only to the correct people and by identifying and reducing fraud and error.

Part 2
Impact and outcomes

Key messages

1 Outcomes from the NFI 2012/13 are £16 million.

2 £10.5 million have been identified directly from the NFI 2012/13 investigations.

3 £5.5 million are further savings from the NFI 2010/11.

4 4,447 investigations are still in progress.

5 66 per cent (£4.5 million) of overpayments are being recovered.

6 Cumulative NFI outcomes are now at £94 million.

7 Across the UK £1.17 billion of NFI outcomes have now been recorded.

Outcomes

14. Since we last reported on *The National Fraud Initiative in Scotland* (PDF) in May 2012 outcomes valued at £16 million have been recorded. Cumulative outcomes from the NFI in Scotland are now at £94 million and represent a significant return to the public finances of Scotland.

15. The 2012/13 outcomes are split:

- £10.5 million of outcomes from the NFI 2012/13 matches

- £5.5 million of outcomes from further follow-up work on the NFI 2010/11 matches.
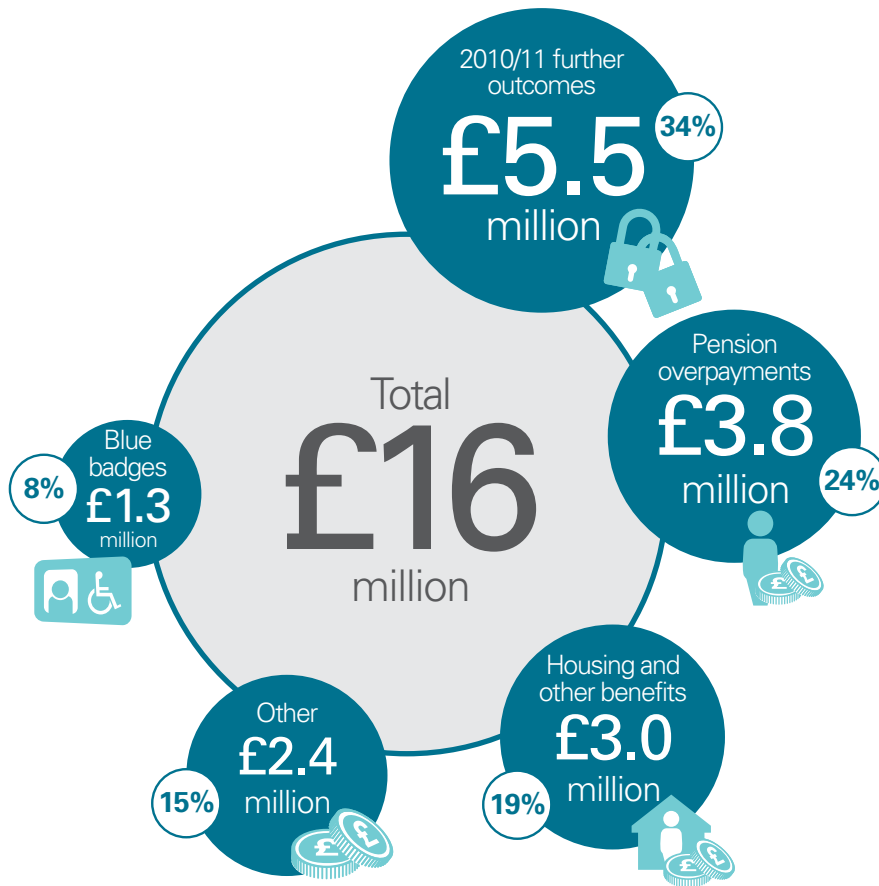
16. Exhibit 3 (page 12) provides more detail of key outcome areas recorded by bodies as at 31 March 2014.

17. Investigations from the NFI 2012/13 are ongoing. As at 31 March 2014, there were 4,447 investigations for this exercise still in progress. The evidence from previous exercises is that between reports, significant outcomes continue to be delivered. The last two NFI reports showed that:

- 39 per cent of 2010/11 outcomes arose after March 2012

- 30 per cent of 2008/09 outcomes arose after March 2010

- 45 per cent of 2006/07 outcomes arose after March 2008.

Exhibit 3
Analysis of NFI outcome from April 2012 to March 2014

2010/11 further outcomes
£5.5 million
34%

Pension overpayments
£3.8 million
24%

Blue badges
£1.3 million
8%

Total
£16 million

Other
£2.4 million
15%

Housing and other benefits
£3.0 million
19%

Source: Audit Commission NFI secure web application

18. If this pattern is continued we could expect to see further outcomes in the region of £3 to £4.5 million from the NFI 2012/13.

19. Importantly, once overpayments have been identified, recovery action can be taken. As at 31 March 2014 there was £4.5 million of recovery action being taken in 3,851 cases.

20. The NFI is more than the value of the financial outcomes recorded. Exhibit 4 (page 13) sets out the main results from the 2012/13 matches.
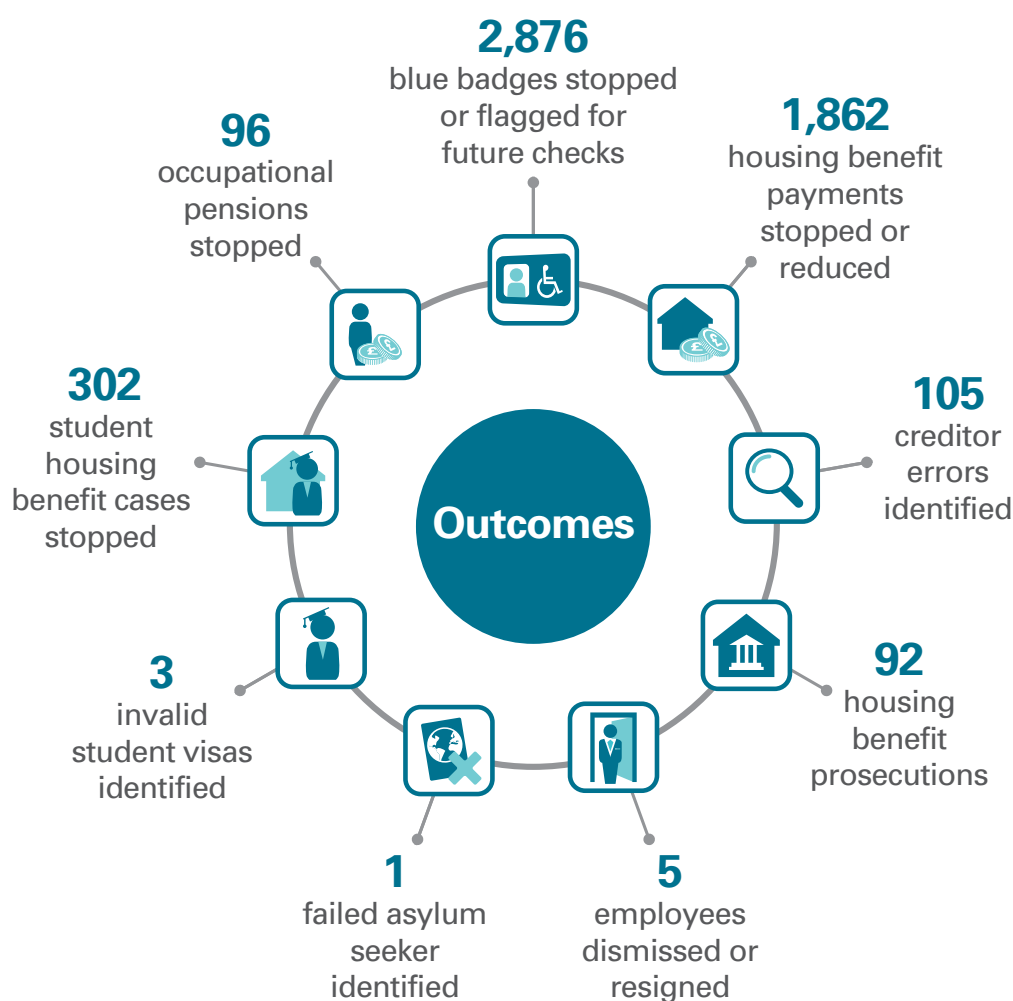
21. What cannot be measured directly is the value of the deterrent effect that the planned biennial NFI data matching has on potential fraudsters. Its significance should not be overlooked and is a key benefit to the Scottish public and taxpayers.

22. Overall outcomes are down on the last NFI exercise by 19 per cent in Scotland and 17 per cent across the UK. Late savings are consistent between exercises at £5.7 million for 2010/11 and £5.5 million for 2012/13. However, no obvious national trend can be assumed from the results of the last five NFI exercises because of changes in the scope of the NFI exercises, the number and variety of bodies participating and in the approach taken by bodies to tackling fraud and error.

Exhibit 4
Main results from the 2012/13 matches

2,876 blue badges stopped or flagged for future checks

1,862 housing benefit payments stopped or reduced

96 occupational pensions stopped

302 student housing benefit cases stopped

105 creditor errors identified

Outcomes

3 invalid student visas identified

92 housing benefit prosecutions

1 failed asylum seeker identified

5 employees dismissed or resigned

Source: Audit Commission the NFI secure web application

23. The most successful matches from the current exercise, excluding late savings, in terms of financial outcomes accounting for 78 per cent (£8.1 million) of the total (£10.5 million), are:

- pensions – 36 per cent

- housing benefits – 29 per cent

- blue badges – 13 per cent.

24. For this exercise Audit Scotland mandated creditor data from all participants which were previously optional. This has resulted in 105 creditor outcomes of £1.1 million for this exercise compared to 13 outcomes worth £15,000 in 2010/11. Recovery action is taking place for 54 of these overpayments. In other cases overpayments have already been returned or credit notes provided.

25. The largest drop is in the area of pension outcomes which are discussed in paragraphs 48–54.

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Matches benefiting other bodies

26. One of the key benefits in undertaking a UK-wide data matching exercise is that it enables matches to be made between bodies and across national borders. Exhibit 5 summarises these for the NFI 2012/13 exercise for Scottish data submitted.

Exhibit 5
Matches benefiting other bodies

Sector source data	Other bodies' outcomes (£)	Number of benefiting bodies
Central government	670,983	5
Local government	636,681	29
NHS	195,998	11
Further education	1,811	1
Total	**1,505,473**	**46**

Source: Audit Commission the NFI secure web application

27. The cross-sector scope of the NFI enabled 46 bodies to identify and take action on 717 outcomes worth £1.5 million. The majority are from cross-body housing benefits to other data sources such as student funding, payroll or pensions.

28. In the main these related to other Scottish bodies but there were also 26 English councils and the Northern Ireland Housing Executive able to identify outcomes from Scottish data. For example, one London borough removed six housing applications from their waiting lists as they were found to be in receipt of housing benefit at five Scottish councils.

29. For those participating bodies or sectors taking part in the NFI who may not always identify significant outcomes from their own matches, it is important to appreciate that other bodies and sectors may. If we look at the payroll and pension data submitted by central government and the NHS we see:

- central government bodies recorded direct outcomes of £1.7 million but also enabled £670,983 of outcomes to be identified at other bodies

- the NHS has recorded direct outcomes of £211,865 but also enabled £195,999 of outcomes to be identified at other bodies.
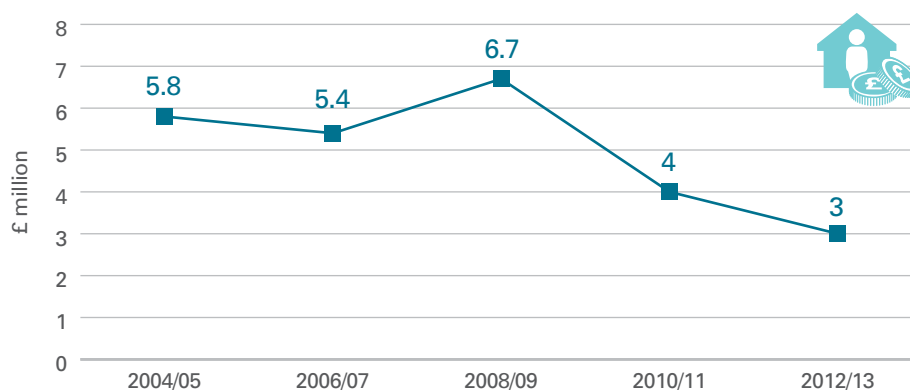
Benefit outcomes

30. The NFI provides councils with the opportunity to identify a wide range of benefit frauds and errors. The most common are caused by undeclared occupational pensions and undeclared earnings from public sector employment.

31. Where other benefits such as income support and jobseeker's allowance are also in payment, councils liaise with the Department for Work and Pensions (DWP) and joint investigations may be carried out. The amounts in this report include these other benefits, where relevant.

32. Exhibit 6 summarises the benefit outcomes from all the NFI exercises to date.

Exhibit 6
Housing and other benefit outcomes

Source: Audit Commission the NFI secure web application

33. This would indicate that there has been a decline in benefit outcomes in the last exercise. The possible reasons are:

- previous NFI exercises have detected the most significant and longest-running frauds and errors

- the trend may demonstrate the exercise's impact and local measures in deterring fraud

- the efforts of bodies to continuously improve their systems

- that less resources are being used to follow up the NFI matches in councils.

34. However, £2 million of the 2010/11 figure were recorded after the last NFI report in May 2012. If this trend is repeated then we would expect to see benefit outcomes at similar levels to the last exercise.

35. What is interesting is that the number of cases recorded with overpayments at 1,862 is slightly up on the previous exercise of 1,792. The individual value of overpayments has fallen from £3,303 to £2,694. This would indicate that resources are still being applied in line with previous NFI exercises and that it is the other three bullets outlined in paragraph 33 (page 15) that are impacting on outcome levels.

36. Despite expected reductions, the continuing high levels of benefit outcomes are best explained by the increased number of bodies participating and supplying data in the 2012/13 NFI and the impact of the economic recession resulting in increased numbers of benefit claims.

Case study 1

An individual was sentenced to nine months in jail after being convicted for £70,000 benefit fraud. This fraud was identified from a NFI 2010/11 match between housing benefits and payroll.

Investigators identified that the person had failed to inform the council and the DWP (as required by law) about earnings from a partner who moved in with them in 2005. For seven years, until March 2012, over £10,000 was stolen annually from public funds by this individual.

This type of outcome demonstrates the effectiveness and efficiency of using data matching to identify potential frauds. By linking benefits payments with payroll income to the same address it could be established that there was undeclared income requiring further investigation. Trained fraud officers can be used effectively to investigate and build cases before referral to procurator fiscal for prosecution.

Without data matching it would have been very difficult and expensive to identify this undeclared change of circumstance.

Source: Local Authority

Student funding to housing benefit claims
37. One of the most successful matches in terms of numbers and coverage is student funding to housing benefits. With a few exceptions, mainly lone parents and disabled students, students are not eligible for housing benefits. This match takes council data and matches against the Student Awards Agency for Scotland (SAAS) student funding data.

38. The match enabled 25 councils to stop 302 housing benefits payments worth £0.7 million to ineligible students. Given the prevalence of this, it is hoped that councils make use of the more regular NFI data matching available for this area.

Public sector workers and pensioners to housing benefit claims
39. It is critical that the public has trust in its public servants. This match identifies errors and frauds that have taken place between public sector payrolls and pensions. By the end of March 2014 councils had identified benefit overpayments from their NFI 2012/13 matches relating to (2010/11 figures are in brackets):

- 1,089 (997) public sector pensioners

- 290 (322) local government employees

- 131 (100) persons working in the NHS in Scotland

- 8 central government employees.

40. While no overpayments are desirable, Exhibit 7 puts some of these figures into context in relation to the populations involved and it does provide some overall assurance that these areas do not have high levels of fraud and error.

Exhibit 7
The NFI benefits outcomes compared to source populations

Sector	Number	Overpayments identified	Overpayment value (£ million)
Public sector pensioners	305,000	1,089	1.78
Local government employees	247,000	290	0.73
NHS employees	157,400	131	0.39
Civil servants	44,300	8	0.01

Source: Office for National Statistics, Scottish Government and the Scottish Public Pensions Agency

41. This exercise also included a further education college for the first time. While no outcomes were identified by the college there were five housing benefit overpayment outcomes identified by a council following up matches of their housing benefit (HB) data to the college payroll.

42. In terms of value, Glasgow City Council and East Dunbartonshire have so far achieved the highest levels of outcomes from their NFI 2012/13 benefits investigations (£454,256 and £299,610 respectively). A further eight councils recorded benefits outcomes in excess of £100,000. Only Shetland Islands Council recorded no benefit outcomes.

43. Another measure of success is the yield in terms of benefit outcomes to total housing benefit expenditure. Exhibit 8 (page 18) provides details of the top three councils in terms of yield ranking.

44. East Dunbartonshire Council consistently performs well by this measure across all of the NFI exercises that have been undertaken. The DWP estimates that for HB payments made in 2012/13, 5.1 per cent was overpaid in 2012/13.

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Exhibit 8
Housing benefit (HB) yield by outcomes

Council	Total HB expenditure	Rank by total HB expenditure (out of 32)	NFI 2012/13 HB outcomes	Rank by HB yield
East Dunbartonshire Council	£24,367,289	26	£299,610	1
Comhairle nan Eilean Siar	£6,957,240	30	£69,502.02	2
Clackmannanshire Council	£23,933,823	27	£91,727.11	3

Source: Department for Work and Pensions (DWP) and the Audit Commission NFI secure web application

45. However, care must be taken when analysing these yield rankings as there are a number of factors that can influence movement. These factors are discussed later in this section. Generally councils need to consider whether finding significant outcomes indicate effective detection of fraud and error or whether improvements to controls within systems could be made to reduce errors.

Housing benefits to licences
46. These matches compare housing benefits data to council-approved licences granted to individuals to identify potential undeclared income. This has again proved to be a successful area for the NFI. Exhibit 9 summarises the results from this exercise.

Exhibit 9
Housing benefit to licences results

Licence type	Number	Outcome	Average outcome per case
Personal alcohol	8	£242,764	£30,345
Taxi drivers	19	£75,641	£3,981
Market traders	2	£6,493	£3,247

Source: Department for Work & Pensions (DWP) and the Audit Commission NFI secure web application

47. In our 2010/11 *The National Fraud Initiative in Scotland* (PDF) 🖱 report, the personal alcohol match generated the largest outcome, estimated at £536,995. Case study 2 further demonstrates how important cross-body data matching is in identifying the full extent of frauds being committed. The investigation was again initiated based on a match between personal alcohol licence and housing benefits payments.

Case study 2

The NFI outcome for this case is £164,850.

An individual had a housing tenancy from Council A for which they also received housing and council tax benefit. The NFI data matches identified that they were also in receipt of a personal alcohol licence from Council B. This indicated that they were potentially working in the Council B area but not declaring any income.

Following up this match the investigators confirmed that the individual was working but not declaring income and had also been living in the Council B area since 2006 but their daughter and grandchild were living in the Council A tenancy.

The subject cancelled the tenancy and has since been reported to the Procurator Fiscal Service for benefit fraud totalling £38,850.78. The remaining element of the outcome is based on seven years' tenancy fraud at £18,000 per annum.[1]

Note: 1. Based on the average cost of housing a family in temporary accommodation for a year (*Protecting the Public Purse 2012,* Audit Commission, November 2012).
Source: Local Authority

Pension outcomes

48. The NFI provides pensions administering councils and the Scottish Public Pensions Agency (SPPA) with an efficient and effective means of checking that payments are only being made to living persons. The NFI 2012/13 helped these bodies identify 96 pensioners whose deaths had not been reported to them. Including other pension-related outcomes (for example, cases where early retirees have returned to work but not reported circumstances that require their pension to be reduced) and forward savings, the amounts for the NFI 2012/13 total £3.8 million.

Scottish Public Pensions Agency
49. The SPPA recorded outcomes of £0.85 million from its 2012/13 matches where 23 outcomes were identified which is a drop from 2010/11 outcomes of £4.4 million. In 22 of these cases recovery is in progress. Exhibit 10 (page 20) summarises SPPA pension outcomes since the NFI started.

50. Obtaining up-to-date information on pensioners returning to work is a very difficult area, particularly on deceased data when one considers that the SPPA has members living in over 50 countries around the world.

Exhibit 10
Pension outcomes
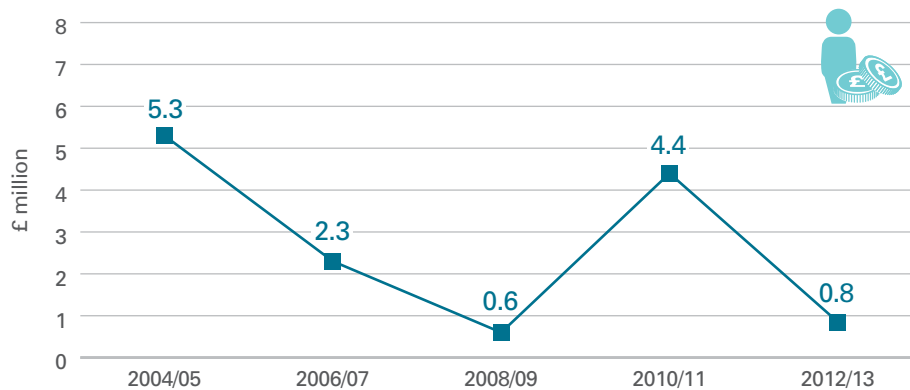
Source: Audit Commission the NFI secure web application

51. However, the SPPA is to be commended for embracing more regular data matching opportunities that have almost certainly led to a reduction in overpayments. It continues to work closely with the National Records of Scotland to reduce the number and in particular the length of pension overpayments through quarterly checks. It has also made use of the additional mortality screening available from the NFI outside the two-yearly cycles to identify further matches.

Local government
52. While SPPA outcomes are down, there has been an increase in local government-run pension scheme outcomes and these account for £2.9 million pension outcomes across 73 cases.

53. There are 11 local government-administered pension bodies in Scotland and five returned outcomes. As in previous NFI exercises the majority of the outcomes from local government are in the:

- Strathclyde Pension Fund (SPF) administered by Glasgow City Council which has a membership of over 197,000 and which recorded outcomes of £2.2 million. SPF administers about 42 per cent of all the local government pensions in Scotland. These outcomes were from 52 cases of which recovery action is taking place in 45.

- Lothian Pension Fund administered by City of Edinburgh Council with over 65,000 members and which achieved outcomes of £0.3 million from three cases all of which are being recovered.

54. Given the success in reducing outcomes that the SPPA has demonstrated, there is an opportunity for local government pension schemes to undertake more regular data matching either through the NFI and/or the National Records of Scotland.

Blue badges

55. The 'blue badge' scheme allows individuals with mobility problems, and who may have difficulty using public transport, to park free at on-street parking meters and pay-and-display machines. Holders are also allowed to park in designated blue badge spaces and may also be permitted to park on single or double yellow lines in certain circumstances.

56. Badges are sometimes used or renewed improperly by people after the death of the badge holder. The use of a blue badge by an unauthorised person is an offence. Importantly, by using a blue badge to park without need, the space is denied to people with real mobility issues. This is the true social cost of this type of fraud.

57. Councils do not always attempt to recover a badge relating to a deceased person to avoid causing distress but, by 'flagging' the relevant records, they can at least ensure that badges are not improperly renewed in the future. By sharing information with other departments, councils can also recover valuable equipment and aids if they have not been informed of a person's death.

58. Scottish councils have reported correcting 2,876 (4,403 in 2010/11) blue badge records where the NFI helped them to identify that the holder was deceased. Edinburgh (992) and Scottish Borders Councils (338) collectively corrected over 1,328 records. Seventeen councils did not record any blue badge corrections compared to only ten in the 2010/11 exercise.

59. The Audit Commission first identified the problem of blue badge fraud in a report published in September 2009 and also in their subsequent annual *Protecting the Public Purse* reports. They identified how criminals falsify blue badges or steal genuine ones from cars, and how a blue badge can be sold on the black market for as much as £500.

60. On 1 January 2012, the new Blue Badge Improvement Scheme (BBIS), procured by the Department of Transport as part of the Blue Badge Reform Programme, was made available to local authorities. The BBIS, which is being phased in over the next three years, is designed to help to prevent fraud and enable more effective monitoring of cancelled, lost or stolen badges.

61. These new arrangements are welcomed and the NFI will continue to undertake the deceased data matching to assist in identifying potential abuse of the badge scheme until these are fully in place.

Council tax single person discounts

62. People living on their own or with no countable[1] adults in the household are eligible for a 25 per cent Single Person Discount (SPD) off their annual council tax bill. The National Records of Scotland estimates that just under 38 per cent of households are entitled to a single person discount.[2]

63. Exhibit 11 (page 22) provides an indicator of the scale of the discount value across Scotland when applied to average band D charge. This demonstrates that this discount is of considerable value and therefore it is of particular importance to ensure that awards are properly made.

Exhibit 11
Council tax SPD estimate

823,314
Single person households

£1,149
Scottish band D average charge (2012/13)

£287.25
Average 25% discount

£236,496,947
Estimated annual discount value

Source: Audit Scotland

64. This NFI match is very simple in that it matches council tax records to the electoral register and a match is returned where a single person discount has been awarded but the electoral register indicates that another countable adult is living there. A letter can then be issued by council staff seeking clarification of household composition and initiate further investigations if required.

65. There were 48,089 matches returned to the 30 Scottish councils that submitted data. Of these, 20 councils have processed 15,813 matches and recorded £2.5 million outcomes with 573 still being investigated. Some councils use additional data matching options to undertake this review and some do not record results on the NFI system. The average return of the 15,813 matches processed is £158 per match.

Other matches

Payroll
66. The NFI matches data to identify cases of potential payroll fraud. But investigations can also lead, for example, to the discovery that employees are in breach of conditions of service or EU working time limits. Apart from other consequences, excessive working hours may pose public safety risks.

67. The NFI also matches payroll data to Home Office immigration data. It is unlawful to seek employment if you are not entitled to reside or work in the UK and the NFI provides bodies with a means of supplementing their recruitment checks.

68. As a result of the 2012/13 matches, three public sector employees in Scotland have so far been dismissed or resigned after bodies confirmed that they did not have permission to reside or work in the UK.

Case study 3

An overseas worker continued working after the expiry of their right to work visa in 2009 (they had been working at the health board legally since 2007). The value of the employee's salary since 2009 was £77,290. Their contract was terminated in 2013.

Source: NHS

Student immigration checks

69. Since the NFI 2006/07 the SAAS has been provided with its own matches, identifying cases where students may not hold valid permissions to reside or study in the UK.

70. SAAS has recorded ten cases of students that were found, after investigating the NFI matches with the Home Office, not to be entitled to receive support. This was because either these individuals were not entitled to be in the UK or they had lied about their personal circumstances. These students had received student support amounting to about £163,451.

Case study 4

A student applied for funding to undertake a Diploma in Nursing. In their application, they stated that they had been born in South Africa and that their nationality was South African. They stated that they had been ordinarily resident in the UK for three years and had indefinite leave to enter or remain in the UK.

The SAAS received a copy of the student's residence permit showing that there was no time limit on their stay in the UK and processed the award accordingly.

The student's data was matched against Home Office data as part of the NFI 2012/13 exercise. A full visa history from the Home Office stated that the student had no legal status in the UK. It also confirmed that the United Kingdom resident permit provided to SAAS to support their eligibility for funding was a false document (a photocopy).

The student has been paid a total of £8,832 to date. However, had the fraud not been picked up through the NFI, the total funding package would have been £26,372.

As part of the investigation into this student, it was discovered that the student's partner had also provided false documentation to support their own application for student support. They had received a total of £17,138 to date.

SAAS officers interviewed both individuals under caution and submitted a case to the procurator fiscal. A trial date has been set for later this year.

The Home Office is currently taking separate action against both parties.

Source: Audit Commission NFI secure web application and SAAS

Case study 5

A student's data was matched against Home Office data as part of the NFI 2012/13 exercise. A full visa history was received from the Home Office stating that they had a valid student visa between 1998–2002 but have had no legal status in the UK since 2002. This student has received a total of £53,806 student funding.

SAAS officers interviewed the individual under caution and submitted a case to the procurator fiscal. A trial date has been set for later this year.

Source: Audit Commission NFI secure web application and SAAS

Payments to private residential care homes

71. The NFI matches information about private residential care home payments to data about deceased persons. This can identify where payments may be continuing for people who have died.

72. The NFI helped councils identify 120 cases from these data matches and overpayments worth £22,150. The majority (99 per cent) of these overpayments are being recovered.

Right to Buy

73. The NFI matches data relating to tenants that have bought, or are in the process of buying, their council property at a discount as part of the Right to Buy (RTB) scheme. The match, to housing benefit and other tenancy records, enables councils to identify potential cases where they may have been acting on false information provided in support of the RTB application. It also identifies change of circumstances such as the former tenant selling the property within the discount period. This means that some, or all, of the discount amount could be owed to the council.

74. The Audit Commission *Protecting the Public Purse 2013* report identified a 168 per cent increase in detected RTB cases in England. In Scotland two councils have identified three RTB cases, for the first time, where applications for RTB have been withdrawn following investigations following the NFI matches. Had these ineligible applications been successful these valuable social housing lets would have been unavailable to eligible tenants and councils might have incurred considerable additional housing costs to rehouse these people.

75. The Housing (Scotland) Bill currently going through the Scottish Parliament intends to end RTB in Scotland. Until this happens, the NFI RTB matches will continue to highlight potential cases where ineligible applications are being made.

What bodies actually save or recover because of the NFI

76. The estimated value of the NFI to the public purse since we last reported in May 2012 is £16 million. However, some of this represents overpayments that will never be recovered and estimated values that have been attached, for example, to cancelling a blue badge. These amounts may not translate into cash savings, but they are valuable outcomes nonetheless.

Case study 6

A Right to Buy to housing tenancy match highlighted a case where a person had lodged a Right to Buy application with one council despite them also holding a tenancy in a different council. The investigation confirmed that the tenant was also claiming housing benefit at the second address.

The tenancy fraud officer confirmed with the tenant that they did indeed hold two tenancies. The tenant had not felt they had done anything wrong providing they paid the rent. They have since ended their tenancy with the council where they were not actually residing but their son was. The Right to Buy application has also been revoked and the council is preparing the case for prosecution.

Source: Audit Commission

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77. Audit Scotland previously canvassed bodies and established from those that responded that the NFI overpayments are usually subject to the same recovery processes that apply to other debt. Most bodies do not keep separate records of the NFI recoveries. Indeed, Audit Scotland would prefer that bodies devoted their resources to investigation work, rather than require them to record the NFI amounts that are often recovered by frequent small payments over long periods of time.

78. Based on the current NFI exercise the recovery rate is 66 per cent, excluding estimates. If we add the estimated forward savings from areas such as benefits and pensions, being public money which has been prevented from being paid out in fraud or error following investigations, we can reasonably estimate that the actual cash savings or recoveries for the public purse are at least half of the total outcomes of £16 million.

79. This then is an identified direct cost to public bodies and taxpayers where fraud and errors have taken place. There are also other costs that are incurred where frauds and errors are identified. These include:
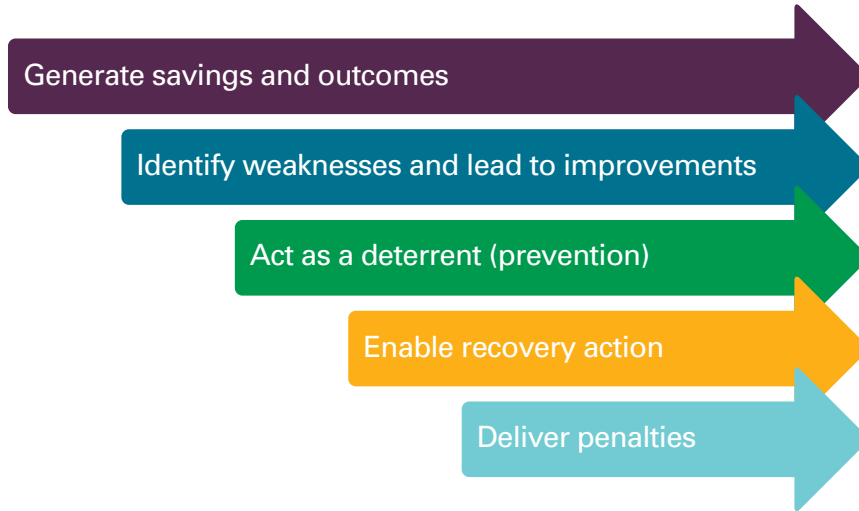
- the cost of investigating, correcting and recovering frauds and errors

- the opportunity cost of investigating, correcting and recovering frauds and errors instead of providing services

- the social cost of awarding incorrect benefits or proving ineligible services

- the reputational cost of failing to prevent frauds or in making errors.

What does the level of outcomes tell us?

80. The NFI impacts on a number of levels and across a number of bodies. These levels are summarised in .

Exhibit 12
The NFI impacts on a number of levels and across a number of bodies

Generate savings and outcomes

Identify weaknesses and lead to improvements

Act as a deterrent (prevention)

Enable recovery action

Deliver penalties

Source: Audit Scotland

81. A key benefit of the NFI is the fact that by identifying fraud and error the opportunity is provided to bodies to establish why they occurred and then improve their systems. This can be done by:

- simplifying system processes

- reviewing and strengthening the internal controls that failed to stop or capture errors or fraud.

82. While it would be difficult to eliminate all errors and prevent all frauds the NFI can provide the focus for such reviews to take place. Exhibit 13 summarises the circumstances where fraud and error are most likely to be found.

Exhibit 13
Circumstances that increase the risk of error and fraud

System complexity + Weak internal controls = → Increased risk of errors and fraud
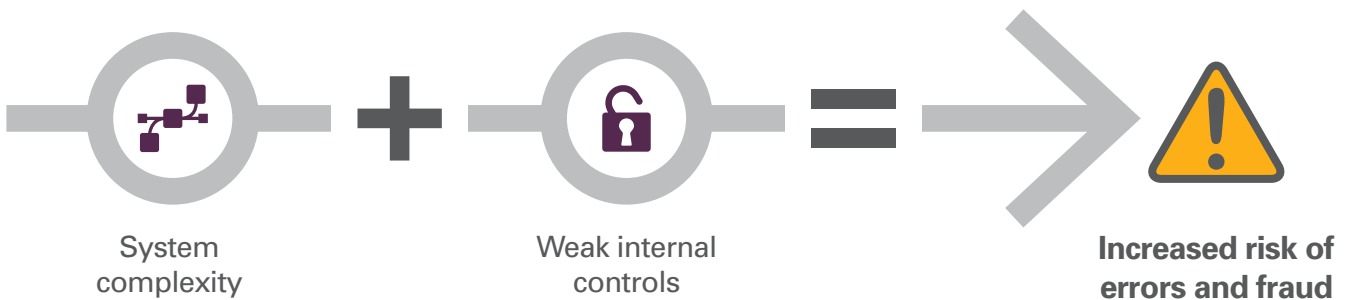
Source: Audit Scotland

83. System complexity can result in errors made by either the individual wishing to obtain a service or by the public servant processing the data. Where an individual knowingly exploits systems and controls by providing incorrect information, this is fraud.

84. The most effective approach to reduce the overall cost of fraud and error is to prevent it occurring in the first place. Both fraud and error can be reduced by public bodies establishing and maintaining sound systems of internal controls.

85. Audit Scotland does not take a view on whether high levels of the NFI outcomes are a good result or not. High levels of outcomes could be due to increased fraud and error in the system or to poor internal controls in operation.

86. Equally important is the assurance given to these bodies with few matches that in the areas covered by the NFI, there do not appear to be significant problems and the deterrent effect created by the NFI exercise taking place and being communicated to those whose data is included.

Part 3
Helping to improve, holding to account

Key messages

1 81 per cent of participating bodies managed their roles in the NFI 2012/13 exercise satisfactorily.

2 29 per cent of bodies need to follow up their matches more promptly.

3 Over a third of participating bodies need to integrate the NFI into their corporate policies and strategies for preventing and detecting fraud and error.

4 17 per cent of bodies reviewed were considered not to have deployed sufficient resources for managing the NFI.

Overall findings

87. Local auditors concluded that 81 per cent of participating bodies had managed their role in the NFI 2012/13 exercise satisfactorily. However, a few showed scope for significant improvement.

88. Appendix 2 (page 37) includes a two-part checklist that we encourage all bodies to use to self-appraise their involvement in the NFI prior to and during the NFI 2014/15 exercise. Part A (page 37) is designed to assist audit committee members when reviewing, seeking assurance over or challenging the effectiveness of their body's participation in the NFI. Part B (page 38) is for officers involved in planning and managing the NFI exercise.

89. Auditors also provided up-to-date information about each body's NFI performance and progress at the end of December 2013. In reaching their conclusions, auditors do not attach significant weight to the value of the NFI outcomes achieved by bodies but do look to see that bodies have approached the exercise proportionately and effectively.

90. While 81 per cent is slightly down on the 2010/11 exercise ratings, it continues to indicate a high degree of commitment to the NFI. Local auditors are providing strong assurance that all sectors are taking the NFI seriously by putting adequate arrangements in place.

91. The biggest change from the last exercise is that central government bodies have, overall, weakened arrangements in comparison with NHS (improved) and local government (stayed the same) sectors (Exhibit 14, page 29).

Exhibit 14

External auditor review of the NFI arrangements
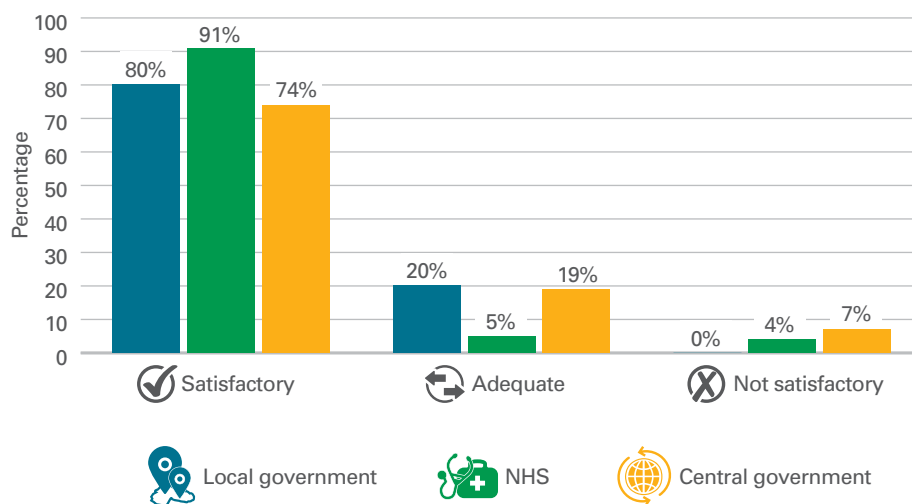
Source: External auditors

92. The central government sector had the greatest number of new bodies participating in the NFI 2012/13 and this, together with the diversity and size of new bodies, perhaps explains the weaker results and opportunity for improvement.

93. Local government has the largest range of data sets and number of matches returned. It is not entirely unexpected, therefore, that they have been identified as having some scope to improve.

94. The NHS has improved its arrangements based on auditor returns and this is to be commended.

95. The majority of the officers directly involved in preparing for the NFI and following up matches demonstrate commitment, while 90 per cent of the officers nominated to coordinate the exercise were considered suitable for the role.

Other key aspects of auditor reviews:

- 89 per cent of bodies submitted their data on time

- 91 per cent of bodies gave priority to following up recommended matches

- 15 bodies were considered not to have deployed sufficient or appropriate resources for managing the NFI exercise.

Areas that need improvement

96. Exhibit 15 summarises the key areas where local auditors indicated that there was room for improvement.

Exhibit 15
Areas of concern

Areas of concern	Percentage of bodies needing to improve
Bodies are slow to follow up matches	29%
There is limited or no internal audit monitoring of the NFI approach and outcomes to ensure identified weaknesses are addressed	39%
Fraud and error polices and strategy did not integrate the NFI arrangements	38%
Reporting the NFI progress and outcomes to senior management and board/members is limited or does not happen	24%

Source: External auditors

97. Auditors will follow up these findings in those bodies where improvements were required as part of the 2014/15 NFI exercise.

98. Auditors confirmed that appropriate arrangements had been made for issuing fair processing notices to those individuals whose data was submitted for the exercise.

99. Auditors reported that 11 per cent of bodies submitted data for the NFI 2012/13 after the specified processing deadline. This creates a need for another processing run at a future date, and thereby unnecessarily increases the cost of processing data. These bodies fell several months behind the other participants while waiting for their matches as well as causing other bodies to receive further matches.

100. Auditors reported that 21 per cent of bodies did not record their outcomes fully on the NFI secure website. Many could also improve the way they record their investigations and conclusions on the NFI application. Audit Scotland will work with colleagues in the Audit Commission to improve the clarity of recording requirements. Appendix 3 (page 41) provides some help in this area. However, the likely effect is that the value of the outcomes referred to in this report is understated in some areas.

Part 4
Future of the NFI

Key messages

1 The Cabinet Office is the new home of the NFI from 2015 and regards the use of data matching as an important tool in the prevention and detection of fraud.

2 The 2014/15 NFI exercise is due to start in June 2014 and Audit Scotland expects a smooth transition.

3 The next exercise will again look to expand the range of participating bodies and data sets.

4 The NFI is increasing its opportunities for flexible and real time data matching options aimed at fraud prevention.

5 The introduction of the Single Fraud Investigation Service (SFIS) has major implications for resourcing of council counter-fraud work.

Cabinet Office

101. Following the abolition of the Audit Commission it was recognised that certain key activities and services needed to be maintained. The NFI was recognised as one of these key areas and the Local Audit and Accountability Act (England) 2014 will transfer data matching powers and the Audit Commission's NFI team to the Cabinet Office on 1 April 2015.

102. These changes should have no direct impact in Scotland. Audit Scotland expects the same continuity of service for those taking part based on:

- Audit Scotland having its own data matching powers conferred to it by the Scottish Parliament (Appendix 1, page 35)

- the core NFI team with all its experience and support is being transferred

- the third party contract for running the NFI web application will also transfer to the Cabinet Office

- the positive talks held with the Cabinet Office and other national audit agencies on the future of the NFI.

Participating bodies and data sets

103. Audit Scotland will continue to look at which bodies should be asked to submit data and which data sets. This exercise mandated the majority of data sets for the first time and expanded the number of bodies participating so it is unlikely that the number of bodies will increase significantly. It also brought in the further education sector for the first time and, given the housing benefit outcomes identified based on the payroll data from this one college, the participation for this sector may be expanded.

104. In terms of data sets the direct payments made to eligible people for long-term social care support have been successfully piloted by the Audit Commission in England and will be considered for inclusion in the 2014/15 NFI exercise in Scotland for Scottish councils.

105. The draft data specifications are available on the Audit Commission's website and key contacts have been notified of these.

106. There are some very large registered social landlords' tenancy databases that Audit Scotland would like to work with to ensure the eligible and most vulnerable are being housed. This would have to be provided on a voluntary basis but Audit Scotland sees it as an area where a positive impact can be made.

Single Fraud Investigation Service (SFIS)

107. The introduction of the SFIS has major implications for resourcing of council counter-fraud work. In the near future many experienced and trained counter-fraud experts will move to the SFIS who will then investigate all welfare benefits.

108. The risk for local government bodies is that they do not adequately address this resource loss to ensure that sufficient capacity remains to counter other types of corporate frauds.

The NFI 2014/15 aims

109. The overall aims of the NFI are to serve the public interest by:

- safeguarding public money against losses from fraud or misappropriation

- contributing effectively to the fight against fraud.

110. To meet these aims the NFI 2014/15, which will be launched in June 2014, will involve work under three broad themes:

- Continuing with successful batch data matches and developing the service to offer more flexibility and meet new risks.

- Putting more emphasis on fraud prevention through the development of real time data matching services.

- Extending data matching for fraud purposes to a broader range of organisations and sectors.

111. Audit Scotland looks forward to the next NFI exercise and continuing to work with the Audit Commission and Cabinet Office, other UK audit agencies and participating bodies to successfully deliver these aims.

112. In the longer term the roll-out of Universal Credit is expected to have an impact on the data sets contributing to the NFI. The future direction of the exercise will be assessed at that time.

Endnotes

◄ 1 For NFI data matching, individuals recorded as qualifying for council tax single person discount on the basis that they live with other disregarded adults are excluded.

◄ 2 *Estimates of Households and Dwellings in Scotland*, National Records of Scotland, 2012.

Appendix 1

Governance arrangements

Background

The following summarises the key legislation and controls governing the NFI data matching exercise.

Legislation

The NFI 2012/13 exercise was carried out under powers given to Audit Scotland for data matching included in the Criminal Justice and Licensing (Scotland) Act 2010 passed by the Scottish Parliament. Under this legislation:

- Audit Scotland may carry out data matching exercises for the purpose of assisting in the prevention and detection of fraud or other crime and in the apprehension and prosecution of offenders

- Audit Scotland may require specified persons to provide data for data matching exercises. These include all the bodies to which the Auditor General for Scotland or the Accounts Commission appoints auditors, licensing boards, and officers, office holders and members of these bodies or boards

- other persons or bodies may participate in Audit Scotland's data matching exercises on a voluntary basis. Where they do so, the statute states that there is no breach of confidentiality and generally removes other restrictions in providing the data to Audit Scotland

- the requirements of the Data Protection Act 1998 continue to apply

- Audit Scotland may disclose the results of data matching exercises where this assists the purpose of the matching, including disclosure to bodies that have provided the data and to the auditors appointed by the Auditor General for Scotland and the Accounts Commission

- Audit Scotland may disclose both data provided for data matching and the results of data matching to the Auditor General for Scotland, the Accounts Commission, the Audit Commission, or any of the other UK public sector audit agencies specified in Section 26D of the Public Finance and Accountability (Scotland) Act 2000, for the purposes described above

- wrongful disclosure of data obtained for the purposes of data matching by any person is a criminal offence

- Audit Scotland must prepare and publish a Code of Practice with respect to data matching exercises. All bodies conducting or participating in its data matching exercises, including Audit Scotland itself, must have regard to this code

- Audit Scotland may report publicly on its data matching activities.

Code of data matching practice

The Criminal Justice and Licensing (Scotland) Act 2010 includes important data-protection safeguards such as a requirement for Audit Scotland to prepare a Code of data matching practice, and to consult with the UK Information Commissioner and others before publication. Our code, The Code of data matching practice 2010 (PDF) ⬐, was updated in November 2010 to reflect the new legislation and to ensure that the NFI exercises continue to comply with data protection requirements and best practice in notifying individuals about the use of their information for the NFI purposes.

The NFI web application

Bodies access the application via the internet using password access and encryption controls similar to internet banking. The secure website is the safest method of providing the data matches to bodies. The Audit Commission regularly reviews the application and implements developments to improve its functionality, ease of use, and security.

Interactive training was available to participating bodies and auditors via the web application to support the Audit Commission and Audit Scotland Guidance.

Security review and accreditation

The Audit Commission's NFI system is accredited to government standards[1] and is subjected to regular stringent security review. This covers infrastructure, information storage, handling and processing when under the control of the Audit Commission's data processing contractor and the NFI team. The review was undertaken by a consultant from the National Computing Centre (NCC) who confirmed compliance with government information standards.

This accreditation involved demonstrating to key government departments that the NFI is suitably secured and that information risks are managed to government standards. The NCC also undertook independent penetration testing of the NFI systems and concluded that the NFI was '…well implemented and robust from a security perspective'.

As well as regular internal reviews by the Audit Commission, the other UK audit agencies (ie, Audit Scotland, the Wales Audit Office, the Northern Ireland Audit Office and the National Audit Office) now also share a programme of independent audits of the different aspects of the NFI data security. The Information Commissioner's Office has also conducted an NFI data security audit at the invitation of the Audit Commission.

All of these measures provide current and future NFI participants with assurances that data is processed according to rigorous government security standards.

1   The National Fraud Initiative (NFI) system has undergone accreditation against HMG Information Assurance Standard No.1&2.

Appendix 2

Self-appraisal checklist

Part A: for those charged with governance	Yes/No/Partly	Is action required?	Who by and when?
Leadership, commitment and communication			
1 Are we committed to NFI? Has the council/board, audit committee and senior management expressed support for the exercise and has this been communicated to relevant staff?			
2 Is the NFI an integral part of our corporate policies and strategies for preventing and detecting fraud and error?			
3 Are the NFI progress and outcomes reported regularly to senior management and elected/board members (eg, the audit committee or equivalent)?			
4 Where we have not submitted data or used the matches returned to us, eg council tax single person discounts, are we satisfied that alternative fraud detection arrangements are in place and that we know how successful they are?			
5 Does internal audit, or equivalent, monitor our approach to NFI and our main outcomes, ensuring that any weaknesses are addressed in relevant cases?			
6 Do we review how frauds and errors arose and use this information to improve our internal controls?			
7 Do we publish, as a deterrent, internally and externally the achievements of our fraud investigators (eg, successful prosecutions)?			

Part B: for the NFI key contacts and users	Yes/No/Partly	Is action required?	Who by and when?
Planning and preparation			
1 Are we investing sufficient resources in the NFI exercise?			
2 Do we plan properly for NFI exercises, both before submitting data and prior to matches becoming available? This includes considering the quality of data.			
3 Is our NFI key contact (KC) the appropriate officer for that role and do they oversee the exercise properly?			
4 Do KCs have the time to devote to the exercise and sufficient authority to seek action across the organisation?			
5 Where NFI outcomes have been low in the past, do we recognise that this may not be the case the next time, that NFI can deter fraud and that there is value in the assurances that we can take from low outcomes?			
6 Do we confirm promptly (using the online facility on the secure website) that we have met the fair processing notice requirements?			
7 Do we plan to provide all NFI data on time using the secure data file upload facility properly?			
8 Do we adequately consider the submission of any 'risk-based' data-sets in conjunction with our auditors?			
9 Have we considered using the real-time matching (Flexible Matching Service) facility offered by the NFI team to enhance assurances over internal controls and improve our approach to risk management?			
			Cont.

Part B: for the NFI key contacts and users	Yes/No/Partly	Is action required?	Who by and when?
Effective follow up of matches			
10 Do all departments involved in NFI start the follow-up of matches promptly after they become available?			
11 Do we give priority to following up recommended matches, high-quality matches, those that become quickly out of date and those that could cause reputational damage if a fraud is not stopped quickly?			
12 Do we recognise that NFI is no longer predominantly about preventing and detecting benefit fraud? Have we recognised the wider scope of NFI and are we ensuring that all types of matches are followed up?			
13 Are we investigating the circumstances of matches adequately before reaching a 'no issue' outcome, in particular?			
14 (In health bodies) are we drawing appropriately on the help and expertise available from NHS Scotland Counter Fraud Services?			
15 Are we taking appropriate action in cases where fraud is alleged (whether disciplinary action, penalties/cautions or reporting to the procurator fiscal)? Are we recovering funds effectively?			
16 Do we avoid deploying excessive resources on match reports where early work (eg, on recommended matches) has not found any fraud or error?			
17 Where the number of recommended matches is very low, are we adequately considering the related 'all matches' report before we cease our follow-up work?			
18 Overall, are we deploying appropriate resources on managing the NFI exercise?			
			Cont.

Part B: for the NFI key contacts and users	Yes/No/Partly	Is action required?	Who by and when?
Recording and reporting			
19 Are we recording outcomes properly in the secure website and keeping it up to date?			
20 Do staff use the online training modules and guidance on the secure website and do they consult the NFI team if they are unsure about how to record outcomes (to be encouraged)?			
21 If, out of preference, we record some or all outcomes outside the secure website have we made arrangements to inform the NFI team about these outcomes?			
Part B: for the NFI key contacts and users		Is action	Who by

Appendix 3
How to work more efficiently

Concerns	How to work more efficiently
Many participants are not using the latest time-saving enhancements to the NFI software.	Ensure staff within the organisations that take part in the NFI keep up to date with new features of the web application and good practice by reading the guidance notes and watching the online training modules before they begin work on the matches.
Matches that are time critical and could identify an overpayment are not acted on first.	Key contacts should schedule staff resources so that time-critical matches, such as housing benefit to students and payroll to immigration, can be dealt with as soon as they are received.
Investigations across internal departments are not coordinated resulting in duplication of effort or delays in identifying overpayments.	Key contacts should coordinate investigations across internal departments and, for example, organise joint investigation of single person discount matches involving housing benefit, to ensure all relevant issues are actioned.
Disproportionate time is spent looking into every match in every report.	Use the tools within the web application, such as the filter and sort options or data analysis software, to help prioritise matches that are the highest risk. This will save time and free up staff for the most important investigations.
Enquiries from other organisations that take part in the NFI are not always responded to promptly.	Prioritise responses to enquiries from other organisations so investigations can be progressed.
Data quality issues that are highlighted within the web application are not addressed before the next NFI exercise.	Review the quality of the data supplied before the next exercise as external providers normally have to phase in changes to extraction processes. Better data quality will improve the quality of resulting matches.

Source: Audit Commission NFI team

The National Fraud Initiative in Scotland

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REPORT TO: Audit and Governance Committee

MEETING DATE: 9 September 2014

BY: Depute Chief Executive – Resources & People Services

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SUBJECT: Internal Audit Progress Report 2014/15

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1 PURPOSE

1.1 To inform the Audit and Governance Committee of Internal Audit's progress against the annual audit plan for 2014/15.

2 RECOMMENDATION

2.1 That the Audit and Governance Committee note the contents of the Internal Audit Progress Report 2014/15.

3 BACKGROUND

3.1 This report is prepared to assist the Committee in their remit to evaluate Internal Audit's work and measure progress against the annual audit plan.

3.2 The progress made to date is outlined in the attached report.

4 POLICY IMPLICATIONS

4.1 None

5 EQUALITIES IMPACT ASSESSMENT

5.1 This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.

6   RESOURCE IMPLICATIONS

6.1   Financial - None

6.2   Personnel - None

6.3   Other - None

7   BACKGROUND PAPERS

7.1   None

AUTHOR'S NAME	Mala Garden
DESIGNATION	Internal Audit Manager
CONTACT INFO	01620 827326
DATE	28 August 2014

INTERNAL AUDIT PROGRESS REPORT 2014/15

AUDITABLE AREAS	SCOPE OF THE AUDIT	TARGET COMPLETION DATE	STATUS
Fostering and Kinship Care Allowances	We will review the arrangements in place for the payment of fostering and kinship care allowances and fees.	August 2014	Completed
Bathroom Adaptations	We will examine the adequacy and effectiveness of the Council's Framework Agreement for bathroom adaptations.	August 2014	Completed
National Fraud Initiative	Internal Audit participates in the National Fraud Initiative, which is coordinated for Scottish Local Authorities by Audit Scotland. This initiative seeks to identify potential frauds and overpayments by matching data held within the Council to that held by other bodies.	August 2014	Completed
Public Records (Scotland) Act 2011	We will examine the adequacy of the existing arrangements in place within the Council for meeting the requirements of the Public Records (Scotland) Act 2011 – the audit will focus on how the Council uses, stores, makes secure, shares and destroys information.	October 2014	
Residential Homes for Older People	A review of the financial arrangements operating at the Council's residential homes for older people will be undertaken.	October 2014	
Fleet Management	We will review the adequacy and effectiveness of the Council's fleet management.	October 2014	

AUDITABLE AREAS	SCOPE OF THE AUDIT	TARGET COMPLETION DATE	STATUS
Review of Performance Indicators	Internal Audit will review the systems in place for the preparation and reporting of Performance Indicators.	October 2014	
IT Disaster Recovery	We will review the IT disaster recovery arrangements for the Council's main data centres (John Muir House and Penston House).	October 2014	
Tyne Esk LEADER Programme	We will examine the adequacy and effectiveness of the internal controls in place for the Tyne Esk LEADER Programme.	December 2014	
Standards and Policies	Internal Audit will report to the Audit and Governance Committee on the following: • The outcome of Internal Audit's assessment against Public Sector Internal Audit Standards (PSIAS) • The updated Internal Audit Charter • The Council's updated Whistleblowing Policy • The policies and procedures in place within the Council for the prevention and detection of fraud and corruption.	December 2014	
Cash Handling and Banking	We will examine the cash handling and banking arrangements in operation throughout the Council.	December 2014	
Self Directed Support	We will report on the progress being made by the Council in implementing Self Directed Support.	December 2014	

AUDITABLE AREAS	SCOPE OF THE AUDIT	TARGET COMPLETION DATE	STATUS
Partnership Funding	We will examine the arrangements in place for partnership funding provided by the Council.	December 2014	
Schools Audit	We will examine the internal controls operating within one secondary school and one primary school in East Lothian.	December 2014	
Gifts and Hospitality – Members	We will review the arrangements in place for the recording and acceptance of offers of gifts and hospitality by Members.	February 2015	
Contracts Audit	We will examine payments made to suppliers in respect of specific contracts.	February 2015	
Mandatory and Discretionary Financial Assistance	We will review the adequacy and effectiveness of the arrangements in place for the processing of mandatory and discretionary housing grants.	February 2015	
Frameworki – Payments on Schedule	We will examine the adequacy and effectiveness of the internal controls in place for payments made to suppliers via Frameworki.	February 2015	
Fees and Charges	For a range of Council services we will review the arrangements in place for the setting up, reviewing and updating of fees and charges.	February 2015	

AUDITABLE AREAS	SCOPE OF THE AUDIT	TARGET COMPLETION DATE	STATUS
Review of Previous Years' Work	Internal Audit will review the outcome of our previous years' work to ensure recommendations have been actioned as agreed and that risks accepted by management have been properly managed.	February 2015	
Non-Domestic Rates	We will examine the internal controls surrounding the administration of Non-Domestic Rates.	April 2015	
Payroll Overtime	A review of the internal controls in place for the authorisation, processing and monitoring of Payroll Overtime will be carried out.	April 2015	
Borrowings	We will examine the systems and controls in place in respect of borrowings – the audit will focus on the draw down and repayment of loans and the associated authorisation and monitoring procedures in place.	April 2015	
Pensions	We will review the systems and controls in place in respect of pensions – the audit will focus on the accuracy and completeness of pension data sent to the Lothian Pension Fund.	April 2015	