



Fife Council

2015/16 Annual audit
report to Members and
the Controller of Audit

September 2016

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The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies (www.audit-scotland.gov.uk/about/ac/). Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General (www.audit-scotland.gov.uk/about/).

Gillian Woolman is the engagement lead for the audit of Fife Council for the period 2011/12 to 2015/16.

This report has been prepared for the use of Fife Council and no responsibility to any member or officer in their individual capacity or any third party is accepted.

The information in this report may be used for the Accounts Commission's annual overview report on local authority audits published on its website and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

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Key messages

Audit of financial statements

- We have issued an unqualified independent auditor's report on the 2015/16 council and group financial statements.
- We have issued an unqualified independent auditor's report on the Fife Council Charitable Trusts administered by the council.

Financial management and sustainability

- Overall, the council has sound financial management arrangements, although continued significant budget overspends have been incurred in Health and Social Care Services.
- Significant budget pressures have been identified over the years 2017 to 2020 with potential savings required of £141 million.
- There has been capital slippage of over £60 million or 22.4% of capital budget.
- The council acknowledges that transformation is required in delivering services. A change programme is to be developed to embrace a transformational approach.

Governance and transparency

- There are sound governance arrangements in place.
- Overall, the key controls within Fife Council's key financial systems are operating satisfactorily.
- The council has an effective internal audit function and sound anti-fraud arrangements.
- Overall, Fife Council is transparent in its decision making processes and in reporting performance.

Best Value

- There is a well established approach to best value with greater emphasis of reporting outcome performance through cross cutting Portfolio Boards.
- Public performance reporting is effective and is supported by effective performance management with performance measured against key themes.
- Benchmarking is used to monitor and improve performance.



Outlook

Councils are facing rising demands for services and continued funding pressures alongside managing major reforms in welfare and health and social care. Effective arrangements for Best Value will be essential for efficient use of available resources and strong governance and leadership will be needed to achieve continuous improvement.

Introduction

1. This report is a summary of our findings arising from the 2015/16 audit of Fife Council. The report is divided into sections which reflect our public sector audit model.
2. The management of Fife Council is responsible for:
 - Preparing financial statements which give a true and fair view
 - Implementing appropriate internal control systems
 - Putting in place proper arrangements for the conduct of its affairs
 - Ensuring that the financial position is soundly based.
3. Our responsibility, as the external auditor of Fife Council, is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.
4. An audit of financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements; this does not relieve management of their responsibility for the preparation of financial statements which give a true and fair view.
5. A number of reports, both local and national, have been issued by Audit Scotland during the course of the year. These reports,

summarised at [appendix II](#) and [appendix III](#), include recommendations for improvement.

6. [Appendix IV](#) is an action plan setting out our recommendations to address the high level risks we have identified during the course of the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "Management action/response". We recognise that not all risks can be eliminated or even minimised. What is important is that Fife Council understands its risks and has arrangements in place to manage these risks. The Council and the Council Executive Team should ensure that they are satisfied with the proposed action and have a mechanism in place to assess progress and monitor outcomes.
7. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures; consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.
8. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

Audit of the 2015/16 financial statements

Audit opinion	<ul style="list-style-type: none">• We have completed our audit of the council and its group and issued an unqualified independent auditor's report.
Going concern	<ul style="list-style-type: none">• The financial statements of the council, its group and the associated charitable trusts have been prepared on the going concern basis. We are unaware of any events or conditions that may cast significant doubt on the ability of the council, its group and the associated charitable trusts to continue as a going concern.
Other information	<ul style="list-style-type: none">• We review and report on other information published with the financial statements, including the management commentary, corporate governance statement and the remuneration report. We have nothing to report in respect of these statements.
Charitable trusts	<ul style="list-style-type: none">• We have completed our audit of the 2015/16 financial statements of the Section 106 Charitable Trusts administered by Fife Council and issued an unqualified independent auditor's report.
Group accounts	<ul style="list-style-type: none">• Fife Council has accounted for the financial results of seven companies, the common good and the charitable trusts as subsidiaries in its group accounts for 2015/16. The overall effect of consolidating these balances on the group balance sheet is to increase total reserves and net assets by £10.9 million..
Whole of government accounts	<ul style="list-style-type: none">• The council submitted a consolidation pack for audit by the deadline of 26 August 2016. This has been audited and the certified return submitted to the Scottish Government.

Submission of financial statements for audit

9. We received the unaudited financial statements on 30 June 2016, in accordance with the agreed timetable. The working papers were generally of a good standard although some deterioration was noted compared to last year due to finance staff having changed their areas of responsibilities. Council staff provided good support to the audit team, however, which assisted with the delivery of the audit to deadline.

Overview of the scope of the audit of the financial statements

10. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual Audit Plan presented to the Audit Committee on 14 April 2016.
11. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2015/16 agreed fee for the audit was set out in the Annual Audit Plan and, as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.
12. The concept of audit risk is of central importance to our audit approach. During the planning stage of our audit we identified a number of key audit risks which involved the highest level of judgement and impact on the financial statements and consequently had the greatest effect on the audit strategy, resources and effort.

We set out in our Annual Audit Plan the audit work we proposed to undertake to secure appropriate levels of assurance. [Appendix I](#) sets out the significant audit risks identified during the course of the audit and how we addressed each risk in arriving at our opinion on the financial statements.

13. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

Materiality

14. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other reasons (for example, an item contrary to law).
15. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
16. We summarised our approach to materiality in our Annual Audit Plan. Planning materiality was based on the results in the 2014/15 financial statements. We also set performance materiality to reduce

to an acceptable level the probability of uncorrected and undetected audit differences exceeding our planning materiality level.

17. On receipt of the 2015/16 financial statements and following completion of audit testing we reviewed our materiality levels and concluded that materiality should be amended to £12.6 million and performance materiality to £3.1 million (25% of performance materiality). All misstatements over £100,000 are reported.

Evaluation of misstatements

18. A number of presentational and monetary adjustments were identified within the financial statements during the course of our audit. These were discussed with relevant officers who agreed to amend the financial statements. The impact of the monetary adjustments has been to reduce the balance sheet figures for property, plant and equipment and reduce short term creditors by £5.2 million. This has no effect on the council's net assets. We have noted the details of the error giving rise to this adjustment in the 'significant findings from the audit' section below.

19. A number of misstatements were identified during the audit, which

have not been amended in the financial statements. These unadjusted errors are as follows:

- The council has a bad debt provision of £48.7 million as at 31 March 2016 to provide for the potential non-receipt of debt. The sum is netted against short term debtors to arrive at the short term debtors balance of £66.7 million. The provision includes £36.9 million for Council Tax income which is net of a

'negative provision' of £1.7 million which has been calculated for council tax income received in advance. A calculation of a bad debt provision sum for amounts received in advance is not prudent and therefore the overall bad debt provision is understated. The impact is that the short term debtors and the usable reserves in the balance sheet have been overstated by £1.7 million.

- A number of other over accruals totalling £1.1 million were identified in the short term creditors balance, £0.9 million of which was for capital expenditure and £0.2 million of which was for revenue expenditure. The impact is that the short term creditors balance has been overstated by £1.1 million, property, plant and equipment overstated by £0.9 million and the usable reserves understated by £0.2 million.
 - A number of under-accruals totalling £0.9 million were identified in the short term debtors. The impact is that the short term debtors and the usable reserves in the balance sheet have been understated by £0.9 million.
20. The total impact of the unadjusted misstatements is as follows:
- Property, plant and equipment overstated by £0.9 million
 - Short term debtors overstated by £0.8 million
 - Short term creditors overstated by £1.1 million
 - General fund/Usable reserves balance overstated by £0.6 million.

21. Management has chosen not to adjust for these misstatements on the grounds that they not material to the accounts.

Significant findings from the audit in accordance with ISA 260

22. International Standard on Auditing 260 requires us to communicate to you significant findings from the audit, including:
 - The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures.
 - Significant difficulties encountered during the audit.
 - Significant matters arising from the audit that were discussed, or subject to correspondence with management.
 - Written representations requested by the auditor.
 - Other matters which in the auditor's professional judgment, are significant to the oversight of the financial reporting process.
23. During the course of the audit we identified the following significant issues that, in our view, require to be communicated to those charged with governance in accordance with ISA 260.

Table 1: Significant findings from the audit

Significant findings from the audit
<p>Equal Pay</p> <p>The Equal Pay Act 1970 makes it unlawful for employers to discriminate between men and women in terms of their pay and conditions where they are doing the same or similar work, work rated as equivalent, or work of equal value. During 2015/16, Fife Council agreed to settle claims against the council in respect of equal pay compensation. A sum of £50.5 million was calculated for settlement with £43.8 million charged to the Comprehensive income and Expenditure Statement. The remaining £6.7 million was charged against the existing provision held for such claims. The total cost of £50.5 million has required £43.8 million of provisions to be made in year in addition to the opening provision of £6.7 million. £11.3 million was physically paid out in 2015/16 which resulted in a provision of £39.2 million to be carried forward for payment of the remaining claims in 2016/17. Note 26 on Provisions also includes an opening balance of £0.6 million for other employee allowances which was fully utilised in 2015/16.</p> <p>We have performed audit testing on the amounts disclosed and concluded that they are materially correct and disclosed appropriately within the council's financial statements.</p>
<p>Short Term Creditors</p> <p>A sundry creditor of £5.2 million was incorrectly accrued by the council for an affordable housing project. This was for the full purchase order cost of the project of £5.9 million less payments to 31 March 2016 of £0.7 million. The contract is a 'call off' contract with payments made as the contract progresses. The outstanding balance of the full contract cost should not have been accrued.</p> <p>Management agreed to amend the financial statements.</p>

Future accounting and auditing developments

Health and social care integration

24. Fife Integration Joint Board (IJB) was established on 3 October 2015 and from that date the financial results of the IJB required to be consolidated into the council's accounts. The 2015/16 financial results were not consolidated into the council's accounts on the grounds that they were immaterial. From 1 April 2016, when the IJB became fully operational, the financial results will become material and consolidation will be required.
25. The council will need to ensure that procedures are in place for the IJB to provide financial and non-financial information by a mutually agreed date to allow the council to prepare its 2016/17 financial statements. In addition, the council will need to consider what assurances are required from the IJB to support disclosures in its corporate governance statement.

Highways network assets

26. The council's highway assets are currently carried within infrastructure assets in the balance sheet at depreciated historic cost. The 2016/17 Code will require highways to be measured, for the first time, on a depreciated replacement cost basis. This is a major change in the valuation basis for highways and will require the availability of complete and accurate management information on highway assets. An initial overview has indicated that the council is well advanced in its preparations to value its highways network

asset with good collaborative working between finance and roads staff to develop processes for valuation, building on work through the SCOTS Asset Management Project.

Code of Audit Practice

27. A new Code of Audit Practice will apply to all audits from financial year 2016/17. There will be a focus on four areas:
 - Financial sustainability.
 - Financial management.
 - Governance and transparency.
 - Value for money.
28. The new Code increases the transparency of our work by making more audit outputs available on Audit Scotland's website. In addition, as well as the annual audit report, other significant outputs, such as the annual audit plan, will be published on Audit Scotland's website. This is irrespective of whether the body meets in public or makes documents such as Audit Committee papers routinely available on its own website.

Financial management and sustainability

Net service budget expenditure £760.0 million

Service outturn £763.0 million

Service budget overspend £3.0 million

Original planned capital expenditure £270.8 million

Capital outturn £210.2 million

Capital underspend £60.6 million

Closing usable reserves (including General Fund) £64.5 million

Opening usable reserves £100.5 million

Decrease in usable reserves £36.0 million

Closing General Fund balance £55.1million

Committed balances £30.2 million

Uncommitted balances £24.9 million

Financial management

29. In this section we comment on the council's financial outcomes and assess the council's financial management arrangements.
30. The council sets an annual budget to meet its service and other commitments for the forthcoming financial year. The setting of the annual budget impacts directly on residents as it determines council tax and other fees and charges. Regular monitoring of expenditure and income against agreed budgets is central to effective financial management.

Financial outcomes

31. The council reported an accounting deficit of £75.4 million on the provision of services in 2015/16. Adjusting this balance to remove the accounting entries required by the Code, resulted in a general fund balance £37.3 million less than the beginning of the year (1.4% of total revenue budget). The £37.3 million reduction is due to £20.4 million being applied in year to fund equal pay expenditure, use of balances brought forward of £33.2 million to fund expenditure, offset by a surplus on the provision of services of £16.3 million.
32. The surplus on the provision of services was £11.9 million more than had been budgeted for and was achieved despite an overspend of £4.5 million on the provision of Health and Social Care.
33. Positive variances were achieved in: Finance and Corporate Services (£1.0 million), increased council tax income (£2.4 million),

corporate savings from loan charges mainly due to re-phasing of the capital plan and changes to borrowing strategies (£8.1 million) and unused contingency budgets for extreme weather, inflation and the revenue consequences of capital spending (£2.4 million).

34. Although Education and Children's Services remained within its allocated annual budget, within the service, the Children and Families Services section overspent by £3.0 million, mainly due to overspends on purchased care placements. This was offset by underspends in the management of devolved school budgets arising from shortages in both permanent and supply teachers to take up vacancies and cover staff absences.
35. The overspend in Health and Social Care arose, in the main, due to unachieved income assumptions in the budget model. This will have a significant impact on the services transferred to the Fife Integration Joint Board and partner bodies going forward.
36. We note that £8.2m of the council's general fund reserves has been committed to support future expenditure on Health and Social Care and Children and Families Services.
37. The amounts available in 2015/16 to offset service overspends may not be sustainable in the long term and could impact on the longer term financial sustainability of the council.

Refer action plan, point 1

38. The council is required by legislation to maintain a separate housing revenue account and to ensure that rents are set to at least cover the costs of its social housing provision. Rent levels are therefore a

direct consequence of the budget set for the year. The HRA budget was set at £104.6 million with actual spend during the year of £104.3 million, which resulted in a small underspend of £0.3 million.

Financial management arrangements

39. As auditors, we need to consider whether councils have established adequate financial management arrangements. We do this by considering a number of factors, including whether:
- the proper officer has sufficient status within the council to be able to deliver good financial management
 - financial regulations are comprehensive, current and promoted within the council
 - reports monitoring performance against budgets are accurate and provided regularly to budget holders
 - monitoring reports do not just contain financial data but are linked to information about performance
 - members provide a good level of challenge and question budget holders on significant variances.
40. In February 2016 there was a change to the post of Executive Director Finance and Corporate Services, with the retirement and replacement of the Executive Director. We assessed the role and status of the proper officer against CIPFA's "Statement on the role of the Chief Financial Officer in Local Government" under both appointments and concluded that the council complies with the statement's five principles.

41. We reviewed the council's financial regulations, which are revised annually, and concluded that they are comprehensive and current. The council's financial regulations are available on the council's website.
42. Financial monitoring reports (both revenue and capital) are submitted to the Executive Committee on a quarterly basis. Broadly, the reports are comprehensive and clearly written.

Conclusion on financial management

43. Although the council has experienced significant budget overspends in both Health and Social Care and Children and Families Services, we have concluded that, overall, the council's financial management arrangements are satisfactory. However, continued effort should be made to address budget overspends incurred by services.

Financial sustainability

44. The council delivers a broad range of services, both statutory and discretionary, to its communities. Financial sustainability means that the council has the capacity to meet the current and future needs of its communities.
45. In assessing financial sustainability we are concerned with whether:
- There is an adequate level of reserves.
 - Spending is being balanced with income in the short term.
 - Long term financial pressures are understood and planned for.
 - Investment in services and assets is effective.

46. Effective long-term financial planning, asset management and workforce planning are crucial to sustainability.

Reserves

47. As shown in Exhibit 1, the overall level of usable reserves held by the council decreased by £36.0 million compared to the previous year and totalled £64.5 million.
48. £55.1 million is within the general fund, which has no restrictions on its use. The principal purpose of holding a general fund balance is to provide a contingency fund to meet unexpected events and as a working balance to help cushion the impact of uneven cash flows.

Exhibit 1: Usable reserves

Description	31 March 2015 £ million	31 March 2016 £ million
General fund	92.4	55.1
Housing revenue reserve	2.0	2.0
Capital grants unapplied	1.6	1.9
Insurance fund	4.5	5.5
Total usable reserves	100.5	64.5

Source: Fife Council 2015/16 financial statements

49. Planned commitments from the general fund balance amounted to £30.2 million, leaving an uncommitted general fund balance of £24.9

million. Planned commitments include the support to social work during transition (£8.2 million) and investment to support community projects in Fife (£4.8 million). This compares to earmarked balances of £60.0 million as at March 2015, with the reduction resulting from the requirement to use earmarked reserves for the purpose of funding equal pay claims.

50. The council estimates settlement of equal pay claims will exceed £50 million. A proposed funding strategy was agreed at the Executive Committee on 2 February 2016 which will see the reserves level falling to 0.75 per cent (of general fund expenditure) by 2017/18. The council's reserve policy is to hold a minimum of two per cent.
51. CIPFA best practice guidance recommends that councils should hold unallocated general fund balances of between 2% - 4% of revenue expenditure. The council's own policy is to hold a minimum of 2% of their annual turnover over the medium term. The council's unallocated general fund balance of £24.9 million (as at 31 March 2016) represents 3% of their revenue budget, which whilst exceeding the council's own policy is in the middle of the CIPFA best practice range.
52. However, over the next three years the Executive Director Finance and Corporate Services projects that reserves will fall to 0.75% by 2017/18, as a direct consequence of the £50 million settlement of equal pay. The Executive Director Finance and Corporate Services has recommended that "the council begins to restore balances

- within 2017/18 or decommit items already earmarked within balances".
53. We recognise that there remain significant financial challenges ahead which could significantly diminish the council's balances going forward, including, workforce change and increased demand for services. The Executive Director Finance and Corporate Services has exercised caution in recommending that the council restores its reserve balances.
- ### Financial planning
54. In August 2016 the Executive Director Finance and Corporate Services reported to the Executive Committee on financial scenario planning over the 2017-20 period. This report considered the implications from the March 2016 UK Government budget as well as possible implications of both the Scottish Government spending review and the EU Referendum. The report considers three possible scenarios: optimistic; midrange and pessimistic. The midrange scenario estimates a 'budget gap' of £25.2 million in 2017/18 which rises to £93.8 million in 2019/20. The most pessimistic scenario estimates that the 2019/20 budget gap could be as high as £141 million.
55. The report emphasises that the financial scene for Scottish local government in the next three years is likely to be at least as challenging as it has been since 2010 with an anticipated 5.6% reduction in revenue budgets between 2015/16 to 2019/20 for the Scottish public sector.
56. The report states that "it is important that the council develops a medium term financial plan in order to support the spending priorities going forward and to ensure that the council is financially sustainable. Audit Scotland stressed the importance of this in its report '*An Overview of Local Government in Scotland 2016*'. The report concludes with the Executive Director Finance and Corporate Services emphasising the council should take an approach to financial planning which is based upon sound principles and avoid "short term fixes".
57. In our 2014/15 Annual Audit Report, we stated that the realisation of savings will become progressively more challenging year on year and the council has recognised that further transformational change will be required. Management agreed to introduce an agreed Transformational Programme by March 2016.
58. We also commented in our Local Scrutiny Plan 2016/17 that "the council recognises that transformational change will be required across all services, but it is only in the last year that a focussed assessment has been taken forward and services tasked with identifying longer term transformation in the way they deliver services, from which the council's change programme is being established."
59. Overarching governance arrangements and principles on how best to implement the transformation programme were agreed by the Council Executive Team (CET) in February 2016 and the council is currently still working on developing its transformation programme.

Refer action plan, point 2

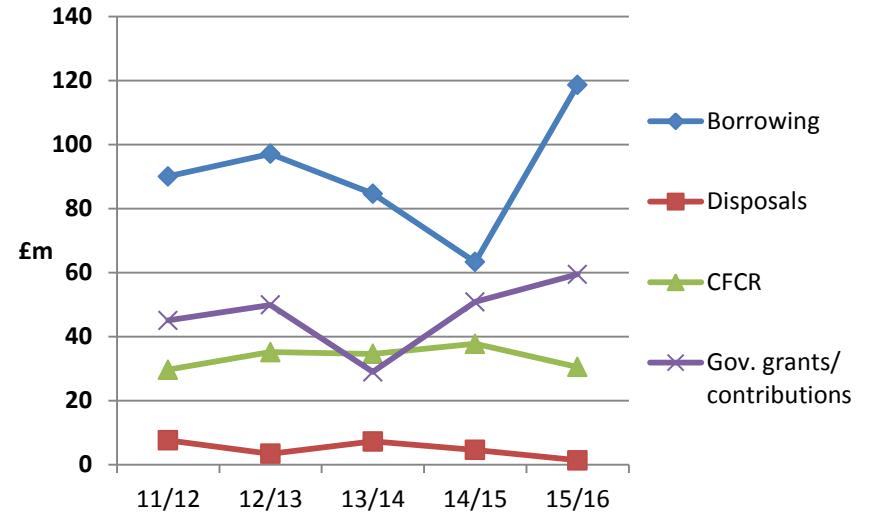
Capital programme 2015/16

60. The council spent £210.2 million on its 2015/16 capital programme (£105.0 million on the HRA programme and the remaining £105.2 million on other general fund services). This was £60.6 million less than planned expenditure of £270.8 million.
61. The underspend of £60.6 million (22.4% of capital budget) is an increase in the level of £39.5 million (20.1%) reported in 2014/15. Significant areas of underspend include additional income of £3.5 million for energy efficiency projects, reduced charging of £3.7 million for housing components replacement as well as slippage in capital works, mainly: £8.5 million due to the re-profiling of Affordable Housing expenditure; £6 million for delays to the building of two new care homes; £4.2 million for the lending of funds for the National Housing Trust Initiative).

Refer action plan, point 3

62. Capital expenditure was funded as shown at Exhibit 2:

Exhibit 2: Sources of finance for capital expenditure 2011/12–2015/16



Source: Fife Council Annual Accounts 2011/12 to 2015/16

63. The requirement to borrow has increased significantly, in part because of the impact of settlement of equal pay in 2015/16 (£13.9 million of direct borrowing for capital expenditure that would originally have been funded from capital funded from revenue (CFCR) (£10 million) and capital receipts (£3.9 million) which has meant that the council has had to incur additional borrowing for their capital programme. The remaining increase in borrowing is explained by the increase in overall capital expenditure in 2015/16 (£210.2 million) compared with 2014/15 (£156.6 million).

64. Going forward, the council plans to invest £899.9 million in capital projects during the period 2016-2025, with 55% of the planned expenditure due within the next three years. Significant capital investments will include £100.4 million within Education and Children's Services, £156.5 million within Assets, Transportation and Environment Service and £507.8 million on housing. The council considers the plan to be affordable based on their assessment of prudential indicators.

Asset management

65. In March 2015 we wrote a local follow up report to our national report on Major Capital Investments in Councils. The report found that the council demonstrates a number of elements of good practice in the financial stewardship of capital investments, including:

- Review of the long term capital plan which is then formally considered, scrutinised and approved by elected members.
- Sound governance arrangements including an Investment Strategy Group which acts as a corporate group on capital investment issues. It is comprised of capital investment experts from throughout the council and reports to the Corporate Improvement Board.
- The council's Fife Excellence Model Project Management Framework Guidance provides a good framework for the management of individual capital programmes and projects.

66. Our report also identified some areas for improvement and we included an action plan which included management responses and agreed actions. We are pleased to report that the council has set up a working group to consider our proposals in detail. This includes having designated officers and proposals for addressing each of our recommendations, as well as identified timescales for implementation.

Dunfermline flood prevention scheme

67. In our 2014/15 annual audit report we highlighted the significant overspend and completion delays in the Dunfermline flood prevention scheme (DFPS). The scheme was completed five and half years later than originally planned at a cost of £34.5 million, which was £20.3 million over budget.

68. In August 2015, the Executive Committee received a report by the Audit and Risk Management Services Manager setting out his findings from a review of the DFPS, which had been carried out at the request of the Committee.

69. The Audit and Risk Management Services Manager's report identified three main factors as contributing to the problems encountered with the scheme:

- Poor design work by the design consultants for the scheme (who also acted as site supervision agents), leaving it open to significant technical queries, variations and challenges during the course of the project.

- The construction contractor's vigorous pursuit of variations and additional costs, and a general 'unhelpful' approach to dealing with problems arising from the poor design work.
 - A form of construction contract, which was not effective for dealing with the problems encountered but which was standard practice at the time the construction contract, was let.
70. The council has now implemented a number of changes to how it manages major civil engineering projects, based on its review of the DFPS. These include:
- Using a new standard form of construction contract (the New Engineering Contract (NEC3)) for all new projects, intended to promote greater partnership working and collaboration between client and contractor.
 - Using a design and build style of NEC3 contract, where appropriate, to protect the council against risk in certain contracts.
 - Changing the form of contract for external scheme designers, which provides a more autonomous role for the project manager and site supervisor, and a more clearly defined process and timeline for decision-making.
 - Generally using its own staff to supervise the works where external consultants have carried out the design, providing that it has the necessary in-house skills and capacity.
71. Audit and Risk Management Services concluded that council staff acted appropriately at all stages of the project and that elected members and senior managers had been provided with appropriate information and updates on the progress of DFPS and the problems being encountered.
72. It is vitally important that the council learns lessons from its experience of the DFPS. To some extent this has already happened with the introduction of changes in the standard forms of contract used to manage major projects.
73. The council is currently engaged in legal action to attempt to recover a significant proportion of the additional costs associated with DFPS.

Refer action plan, point 4

Workforce management

74. Effective workforce management is essential to ensure that the council maximises the effectiveness of its employees. A workforce strategy is key to setting out how the council will ensure it has appropriately skilled people in place to deliver its services.
75. The council introduced a workforce change programme in 2011 as part of a council-wide programme of improvements and efficiencies to mitigate the impact of projected budget reductions. Since then, 2,139 full time equivalent posts have been released up to 2015/16, with 1,260 reductions funded through exit packages and the remaining 879 through what the council terms as 'mitigating factors' e.g. natural turnover. The scale of the financial challenge facing the council means that a further reduction in the workforce is probable as these reductions alone are not sufficient to close the projected budget gap over the period to 2019/20. The reduction in workforce

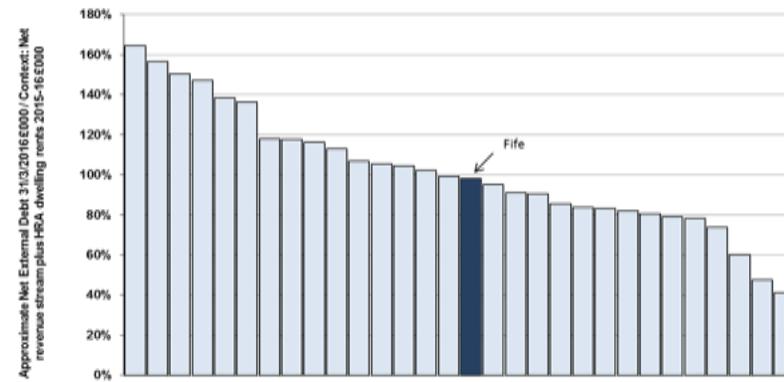
- should be coupled with an assessment of the key skills that will be required to continue to deliver services.
76. We identified workforce management as a key risk in our 2015/16 audit plan and as a result undertook a high-level review of the council's current workforce planning arrangements. We carried out the review using a questionnaire based on the main findings in the Audit Scotland Public Sector Workforce report (November 2013) as well as good practice guidance produced by Audit Scotland in March 2014.
77. Broadly, Fife Council meets many of the elements of good practice identified in the 2013 Audit Scotland report. In particular, the council's use of a principles based approach to workforce management, supported by a strategy document, comprehensive processes and financial modelling tools are commendable. However, there are some areas for improvement which particularly impact upon governance by elected members. These are:
- Elected members were not given an opportunity to scrutinise the council's workforce strategy.
 - Senior officers and elected members did not consider Audit Scotland's good practice guidance when scrutinising the workforce strategy to ensure it meets good practice.
 - The council's annual workforce report to elected members had limited focus on financial outcomes.

Refer action plan, point 5

Treasury management

78. High levels of debt may reduce a council's budget flexibility going forward as revenue resource has to be set-aside to service that debt. The impact that debt levels have on net revenue expenditure will be affected by interest rates and repayment periods.
79. At 31 March 2016 long term borrowing stood at £738.1 million, an increase of £62.4 million on the 2015 borrowing level of £675.7 million. During the same period, short term borrowing increased from £64.4 million to £97.4 million.
80. Analysing long term borrowing as a proportion of the net revenue stream gives an indication of the relative indebtedness of the council. Exhibit 3 shows net external debt as at 31 March 2016 as a proportion of the net revenue stream for the year (based on unaudited accounts information) for all mainland councils in Scotland. The graph demonstrates that the council sits just below the median for Scottish Local Authorities.

Exhibit 3: Scottish councils' net external debt as a percentage of net revenue streams



Source: Scottish councils' unaudited accounts 2015/16 (excluding Orkney and Shetland Island councils)

Pension liability

81. The net pension liability on the council's balance sheet has decreased from £862.4 million in 2014/15 to £700.7 million in 2015/16, a decrease of £161.7 million. A similar position is also reflected in the balance sheet for the group, with the group pension liability decreasing from £876.4 million to £708.3 million.
82. The pension liability represents the difference between expected future pension payments and the underlying value of pension fund assets available to meet this cost. Movements in the value of the real discount factor, used to estimate the current value of future

pensions, can have a significant impact on the value of the pension liability. The real discount factor has increased from 0.8% at March 2015 to 1.3% at March 2015. As a higher real discount rate results in a lower valuation for pension liabilities, this increased rate has had a positive impact on the net liability at 31 March 2016.

Conclusion on financial sustainability

83. Currently, the council has an adequate level of reserves, although this is projected to decline during the next two years, mainly as a result of the payment of equal pay claims. Overall, the council is containing its expenditure within annual budgets (albeit that this is only being achieved through corporate savings, which may not be sustainable). Rising demand for and costs of services will continue to place a strain on the council's capacity to deliver services at the current levels.
84. Overall we have concluded that significant transformational change is required if the council's financial position is to remain sustainable.

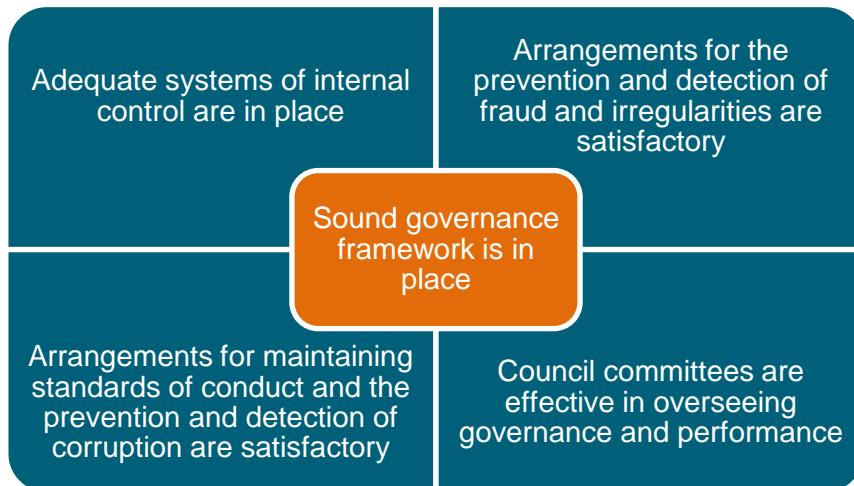
Outlook

85. Councils' revenue funding from the Scottish Government will reduce by five per cent in 2016/17, bringing the real terms reduction in revenue funding since 2010/11 to 11%. At the same time, they face additional financial pressures and greater demands on services. Fife Council has been effective in balancing their annual budgets until now but the council will face increasingly difficult decisions about

how best to spend their reducing budgets. This requires clear priorities and better long-term planning.

86. In common with many other councils, Fife Council is now reporting increasing gaps between income and the cost of providing services over the next few years. With further funding reductions expected, councils face tough decisions to balance their budgets. These decisions must be based on a clear understanding of the current financial position and the longer-term implications of decisions on services and finances.
87. For the council to meet its future budget requirements, further transformational change will be required as recognised in a report to the Executive Committee in August 2016 in which the Executive Director, Finance and Corporate Services stated that “It is clear that when faced with rising demand for public services coupled with a fall in resources in real terms, continuing to do what we currently do is not sustainable”.

Governance and transparency



88. Members and management of the council are responsible for establishing arrangements to ensure that its business is conducted in accordance with the law and proper standards, that public money is safeguarded and for monitoring the adequacy and effectiveness of these arrangements. Based on our observations and audit work our overall conclusion is that the governance arrangements within Fife Council are operating effectively.
89. Citizens should be able to hold the council to account about the services it provides. Transparency means that citizens have access to understandable, relevant and timely information about how the

council is taking decisions and how it is using its resources. The council demonstrates many of the characteristics of openness and transparency.

Corporate governance

90. The corporate governance framework within Fife Council is centred on the full Council which is supported by a number of standing committees, including the Executive Committee, two scrutiny committees, the Standards and Audit Committee and 7 geographically based Area Committees.
91. With the exception of the Executive Committee, committees are politically balanced, with the chairs of the committees being spread across the political parties within the Council.
92. As auditors we attend a number of council and committee meetings each year and have concluded that Members provide a good level of challenge and questioning at the meetings we attended.
93. In March 2016, we produced a report 'Best Value – Governance and Accountability' which was presented to the Standards and Audit Committee in April 2016. Our review used Audit Scotland's best value toolkit on governance and accountability, one of 18 best value toolkits produced by Audit Scotland to assist with the assessment of Best Value in the public sector.
94. Our report concluded that, overall, the council had demonstrated better practice in governance and accountability. We identified some areas for improvement including:

- A planned review of the Policy Advisory Groups (PAGS) had not taken place and there was no evidence to assess how well the PAGS are informing the Executive Committee in its policy development role.
 - We were unable to confirm that the members' register of interests is up to date.
 - There is scope for a more robust member development programme.
 - Minutes of committee meetings are often very brief and do not always capture the details of the discussions (without being too detailed).
 - Although the Standards and Audit Committee meets much of the good practice identified in CIPFA's '*Audit Committees - Practical Guidance for Local Authorities and Police*', some areas were noted for improvement.
95. In our report we encouraged management to develop an action plan, as appropriate, to address areas identified for improvement. This has not yet been developed.

Refer action plan, point 6

Local code of corporate governance

96. The council has a local code of corporate governance (in the form of a series of interlinked governance documents) setting out how the committee structures work and the roles and responsibilities of the members on the committees.

97. These documents reflect the key components as set out in the CIPFA/SOLACE Framework Corporate Governance in Local Government: A Keystone for Community Governance. The governance documentation is up to date and easily accessible to the public on the council's website, Fife Direct.

Internal control

98. As part of our audit we reviewed the high level controls in a number of systems fundamental to the preparation of the financial statements. Our objective was to obtain evidence to support our opinion on the council's financial statements.
99. We reported our findings from our review of the council's key internal controls to the Standards and Audit Committee in August 2016. Overall, no material weaknesses in the accounting and internal control systems were identified which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements. However, our findings included a number of recommendations to enhance the control system in operation, particularly around journals and the processing of some expenditure transactions.

Internal audit

100. Internal audit provides members and management of the council with independent assurance on risk management, internal control and corporate governance processes. We are required by

international auditing standards to make an assessment of internal audit to determine the extent to which we can place reliance on its work. To avoid duplication, we place reliance on internal audit work where possible.

- 101.** Internal audit services for Fife Council are provided by the council's Audit and Risk Management Services (ARMS). Our review of internal audit concluded that ARMS operates in accordance with the Public Sector Internal Audit Standards and has sound documentation standards and reporting procedures in place. We placed formal reliance on the work of ARMS for aspects of our review of the non-domestic rates billing and collection, trade receivables and housing rents financial systems.

ICT audit

Change management (Shared Support Services Programme) follow up

- 102.** Following our initial review of the Change management (Shared Support Services (3S) programme) in 2013/14, we undertook a second follow up review in 2015/16 reflecting on the action taken on the action plan included in our 2013/14 report. The follow up review considered progress with the ten actions that had been agreed in the 2013/14 action plan and highlighted that although five were considered to be completed, implementation of the actions to address the five remaining risks has continued to prove challenging.
- 103.** The high volume of process refinement and development that remains to be implemented indicates that additional resource

investment and time will be required to realise the benefits anticipated during the 2016-19 financial periods. In view of these uncertainties it remains an optimistic expectation that the anticipated benefits will be achieved within the timescale indicated.

ICT framework agreement - follow up

- 104.** In December 2012 the council awarded a four year framework agreement contract to Capgemini to deliver ICT project and business solutions, as part of its Business Change programme. In 2014/15 we carried out a review of the progress made by the council in relation to the framework agreement, in particular, whether it had achieved the stated objectives that contractor and council staff would work together to create selected products and services more rapidly, realising benefits sooner than could be delivered by council resources alone.
- 105.** We reported the findings from our review to the Standards and Audit Committee in January 2016. Our report contained an action plan which consisted of five action points with responsible officers identified for each action and an agreed date by which action would be taken.
- 106.** In 2015/16 we carried out a follow up review. Our report concluded that all five actions included in the 2014/15 action plan had now been completed. We also concluded that the council has made good progress in assessing the next steps to be taken in developing its ICT framework, including:

- Developing corporate-wide procurement support based on early identification of product requirements, together with identification of risks and gaps, enabling management to engage early with suppliers and utilise the variety of national frameworks that are now available.
- Strengthened governance arrangements to deliver the new ICT strategy and greater scrutiny by elected members on the adoption and implementation of major capital projects.
- Central recording of business impact assessments.

ERP application review

107. In December 2015 we submitted a report to management on our review of the phase 1 controls within the council's new financial management system, Oracle Enterprise Resource Planning (ERP), which had been introduced from 1 April 2014. Our December 2015 report focussed on the financial ledger and 'procure to pay' (procurement and accounts payable) modules of the system application and considered the level of management and operational control performed by the council.
108. In the report we concluded that the council experienced a number of difficulties when phase 1 of the ERP system was introduced in 2014/15. A high number of software changes were required which did not go through the council's formal change control procedures, significant staff resources were required to resolve issues pre and post implementation and the ERP system implementation requires further refinement to introduce more efficient controls at data entry

stage. An action plan was agreed by management to implement improvements.

109. As part of our 2015/16 audit we have undertaken a follow up review of the Enterprise Resource Planning application and the action taken by management. At this time we are in the process of drafting a report. The report will be agreed with management prior to issue and we plan to present the report to the Standards and Audit Committee in November 2016.

ICT cyber attacks

110. In recent years several Scottish public sector organisations have been affected by cyber attacks and related activities. Several attacks have attracted media coverage including City of Edinburgh Council, West Lothian Council and Scottish National Heritage. The increasing wider threat of cyber attacks and importance of ICT to the council's organisational capability led us to include this as a specific risk within our Annual Audit Plan for 2015/16.
111. Overall, we found that the council is aware of the risks associated with cyber attacks and is taking appropriate action to mitigate those risks. It is never possible for any organisation to completely eliminate the threat from a cyber attack, but the council demonstrates an awareness of good practice to minimise the risk.

Arrangements for the prevention and detection of fraud

112. The council's arrangements in relation to the prevention and detection of fraud and irregularities and maintaining standards of conduct overall were satisfactory.
113. Fife Council has a range of measures in place to prevent and detect fraud, inappropriate conduct and corruption including an anti-fraud and corruption policy and response plan, a whistleblowing policy and codes of conduct for members and staff. Standing Orders and Financial Regulations are also in place, which assist in the prevention of fraud and irregularities.

National Fraud Initiative in Scotland

114. The National Fraud Initiative (NFI) in Scotland brings together data from councils, police boards, fire and rescue boards, health bodies and other agencies, to help identify and prevent a wide range of frauds against the public sector. Matching data obtained from the systems of participating bodies allows the identification of potentially fraudulent claims on the public purse including housing benefit fraud, occupational pension fraud and payroll fraud. If fraud or overpayments are not identified in a body, and the NFI exercise has been undertaken properly, assurances may be taken about internal arrangements for preventing and detecting fraud.
115. The National Fraud Initiative has sufficient profile within the council with data matches investigated and findings reported to the Standards and Audit Committee. The May 2016 progress report to

the Committee noted that the current NFI exercise was essentially complete and had identified £253,351 of errors (£199,597 related to 3 duplicate payments; £39,904 related to benefit errors; £13,528 related to a private care home; and £322 related to an overpayment of VAT). Full recovery has either already been made or is in progress for the majority of the errors identified.

116. There are no issues of concern over the NFI process that we require to include in this report.

Arrangements for maintaining standards of conduct and the prevention and detection of corruption

117. We have concluded that the council has appropriate arrangements in place for the prevention and detection of corruption and we are not aware of any specific issues that we need to record in this report.

Transparency

118. Transparency means that residents have access to understandable, relevant and timely information about how the council is taking decisions and how it is using its resources.
119. Members of the public can attend meetings of the Council and its standing committees and have access to Council and committee papers on the website. The only exceptions are where there is a good reason for the session to be held in private, for example, discussion involving commercially sensitive information.

120. Information on council performance and the council's complaints system is also available to the public. The council has a structured approach to Public Performance Reporting (PPR) which provides a transparent assessment of the council's performance over the year.
121. A Councillors' register of interests is available to the public on Fife Direct. In our 2014/15 Annual Audit Report we noted that we were unable to confirm that the register was up to date and management agreed to review the process for updating the register of interests in 2015/16.
122. We note that officers in Democratic Services now issue twice yearly requests for members to provide information to update the register of interests or advise of no change. Despite these requests, from our review of the current register we are still unable to confirm that it is up to date. Some of the entries for members' interests date back to 2012. We would encourage members to provide regular update information or 'nil returns' to Democratic Services.

Freedom of Information requests

123. An annual report on freedom of information requests under the Freedom of Information (Scotland) Act 2002 is presented to the Standards and Audit Committee. The 2015/16 annual report states that the council received 3,353 information requests in 2015, of which the council responded to 90% within the statutory deadline. This is an improvement on 2014 when the council met 86% of requests within the statutory deadline. This improvement has been made despite an increase in the number of information requests,

which the council attributes to the council's establishment of a specialist Information Management and Request Team, which coordinates the response.

124. If an applicant is dissatisfied with the way the council has responded to a request they can refer to the Scottish Information Commissioner for a decision. In 2015 Fife Council had one application referred to the Scottish Information Commissioner and this was partially upheld against the council.
125. We have concluded that overall Fife Council has no significant issues of non compliance with the requirements of the legislation and has adequate procedures for processing information requests.

Integration of health and social care

126. Fife Integration Joint Board (IJB) was legally established on 3 October 2015 and became fully operational on 1 April 2016, when delegated services transferred to them. Fife Council (and NHS Fife) has provided support to help the IJB to develop its governance arrangements including internal audit arrangements, standing orders and financial regulations, performance arrangements and risk management arrangements. A report to the April 2016 meeting of the IJB recognised that ongoing work was required for the continued development of the IJB in line with the Act.
127. Membership of Fife IJB includes representatives from Fife Council and NHS Fife. The IJB also appointed a Chief Officer and a Chief Finance Officer (CFO), however both have since retired. A replacement Chief Officer has now been appointed, with an Acting

CFO also appointed for a period of six months. It is important that the changes are carefully managed to ensure there is no loss of direction and momentum for the IJB and its working relationship with Fife Council and NHS Fife.

128. The IJB has a Strategic Plan which was formally approved by the IJB in February 2016. The plan sets out how delegated services will be delivered over the next three years and sets out the financial framework for the IJB, including initial indicative budgets.
129. On 17 March 2016 the IJB considered a report by the CFO on due diligence work which examined the historical financial position of the delegated services and the revised proposed and indicative budgets. This report anticipated a £15 million shortfall in the sums required to deliver the delegated and managed services and that the development of investment and savings proposals are crucial to address this position. It also recognised the additional financial risks arising from the increased financial pressures in relation to 2016/17 budgets.
130. The IJB approved an indicative 2016/17 budget in March 2016. This identified a funding gap of £14.9 million. By June 2016, the gap had decreased to £11.6 million. Recovery plans have been put in place but arrangements will need to be agreed between Fife Council and NHS Fife for the funding of any deficit, should that be the outturn by the year end.
131. Little detailed information on the IJB financial position has been formally presented to the Council. It is important that Fife Council

members are provided with sufficient information to allow them to discharge their responsibilities as elected members of Fife Council.

Refer action plan, point 7

Housing and council tax benefits performance audit

132. Audit Scotland carries out risk assessments of the benefit services of all 32 Scottish councils. Fife Council was last assessed in 2013/14 when it was demonstrated that the council's benefits service had delivered continuous improvement across a number of areas but that further improvement could be made. An action plan was prepared to assist delivery of these improvements.
133. A follow up review is being undertaken in 2016/17, the results of which will be reported at the conclusion of the assessment.

Local scrutiny plan

134. The 2016/17 Local Scrutiny Plan (LSP), prepared by the Local Area Network of scrutiny partners for the council, has been published on Audit Scotland's website and was presented to the Education, Health and Social Care Scrutiny Committee in May 2016.
135. No risks were identified which require additional scrutiny or audit work in 2016/17. A range of nationally driven scrutiny activity was identified to be undertaken in 2016/17, with the outcome of this work reported in due course.

Outlook

136. Councils will continue to operate in a changing environment within continuing financial constraints. Under these circumstances councils will be obliged to consider the delivery of services by different means. Good governance will be particularly important where council resources and service delivery are devolved to third party organisations.
137. Partnership, joint working and arm's length organisations have become increasingly popular vehicles for planning and delivering council services and there is a sustained national focus on their use. Where council services are being delivered by third party organisations it will be crucial that the council implements robust assurance and governance arrangements to deliver best value while at the same time ensuring an appropriate level of accountability for public money. Community planning and health and social care integration will require an ongoing focus on governance and assurance to ensure that the council's priorities are being achieved.

Best Value



138. Best value is a key factor to consider when planning policies, programmes and projects and when taking any spending decisions. A council should have systems and processes to ensure that it can demonstrate that it is delivering best value by assessing and reporting on the economy, efficiency, effectiveness and equality in service provision.

Best Value audit

139. Overall the council has a well established approach to best value including clear strategic priorities and a strong focus on monitoring and reporting performance. In 2014, the council assessed itself as well placed in delivering best value.

140. The council uses a portfolio managed approach to planning and performance, aimed at cutting across the traditional structures of the council to focus on delivering better outcomes. The council believes that this approach will ensure that a balance is maintained between activities to achieve improvements and everyday service delivery. This approach has five portfolio boards as follows:

- Economy Theme Board.
- Environment Theme Board.
- Inclusion and Opportunities Theme Board.
- Organisational Development and Improvement Board.
- Quality of Life Board (including Area Management).

141. A Portfolio Board has been established to oversee the operation of the five portfolio boards. The Portfolio Board is made up of members of the CET. The council also believes that this approach better reflects the approach to community planning encouraged by the Community Empowerment Act 2015.

142. The council participates in the Local Government Benchmarking Framework (LGBF) and has good arrangements to report its performance in accordance with the requirements of the framework.

Self evaluation

143. In our 2013/14 and 2014/15 annual audit reports we commented on the council's decision to postpone conducting self evaluation exercises using the Fife Excellence Model (FEM), a self evaluation mechanism based on the Improvement Service's Public Service

Improvement. At present the council is re-evaluating the use of FEM as a self-assessment tool. This review is influenced by several factors which include:

- Recognition that the original FEM was too onerous and time-consuming for both the assessors and services and a more streamlined self-assessment process was needed.
 - An Improvement Service learning event on self assessment held in May 2016.
 - Awaiting forthcoming Audit Scotland direction on the revised approach to Best Value Audit.
144. As a result the council has not conducted any FEM based evaluations for a number of years. The Executive Director (Communities) presented a paper to the CET in June 2016 which provided background to the council's proposed revised approach along with a number of options which the council are currently considering.

Refer action plan, point 8

Procurement

145. The council has already recognised that transformational change is required in its procurement function if meaningful improvement is to be made and has included Procurement as a strand of its Shared Service Support Service (3S) Programme.
146. Recent activity includes a focus on identifying and maximise opportunities to generate procurement savings benefits including more effective supplier management, robust demand challenge,

improved compliance and the adoption of best procurement practice across the organisation. The council has implemented a revised organisational structure for the Procurement Service aimed at enabling it to operate as a strategic function across the whole council.

147. In 2015 the Scottish Government introduced a new annual evidence-based assessment, the Procurement and Commercial Improvement Programme (PCIP) to monitor public bodies' adoption of good purchasing practice and as a basis for sharing best practice. This replaces the previous assessment, the procurement capability assessment (PCA). Under PCIP organisations will be assessed every two years, with Fife Council scheduled for assessment during 2016/17.

Following the public pound

148. The Chair of the Accounts Commission wrote to all council Leaders and council Chief Executives in March 2015 highlighting the importance of holding to account arm's length external organisations (ALEOs) and fulfilling their statutory obligations in respect of compliance with the Code of Guidance on Funding External Bodies and Following the Public Pound. This code is based on the premise that to ensure public money is used properly and that Best Value is being secured, it must be possible to "follow the public pound" across organisational boundaries.
149. We were advised in September 2015 that the Chief Executive had tasked the ARMS Manager with undertaking assurance work in this

area in 2015/16 to ensure that the council is satisfying the requirements of the guidance. As a result internal audit produced two reports in June 2016: a report on the governance arrangements over ALEOs and another on governance over grants to voluntary bodies.

150. From these reports the ARMS Manager concluded that broadly, the council is complying with the requirements of the Following the Public Pound guidance. However, some areas were identified where improvements could be made including:

- A lack of documented checklists for the payment of non-recurring grants made to voluntary bodies
- Elected members serve on the board of the ALEOs but the council has no formal policy for determining the number, skills or experience of nominees, or for taking account of their other responsibilities
- Some of the ALEOs have officers on their boards. However, the council has no formal policy for whether or when officers should be placed on ALEO boards and, if so, the criteria for determining the number, skills or experience of nominees, or for taking account of their other responsibilities.

151. These points are being addressed through actions plans and will be followed up by internal audit to ensure that agreed action has been completed.

152. We also received correspondence from a member of the public in this area. The correspondent raised concerns over the relationship between the council and three Dunfermline based companies:

Dunfermline Delivers, Dunfermline First and First Dunfermline. Dunfermline Delivers is a Business Improvement Districts company set up to take forward projects which will benefit the local economy. Dunfermline First and First Dunfermline are limited companies, both of which have been set up for a variety of purposes including running a café, renting out office space and encouraging cultural events for the Dunfermline area

153. The concerns centred around the role of members and council employees on the Boards of these three bodies as well as the funding provided to them by the council. We understand that £250,000 of non-recurring funding was provided to Dunfermline First to fund the employment of an events manager, support the promotion and running costs of an events programme and to assist with capital works.

154. Our review did highlight some areas where there is scope for improvement in the council's processes, some of which are similar to areas identified by internal audit in their reviews of Grants to Voluntary Organisations and ALEOs:

- Initial assessments of prospective projects could be improved upon, with more robust evidence of the proposed activity against which the companies could be monitored by appropriate officers.
- The council uses link officers for monitoring other community grants projects funded by council grants. The introduction of a monitoring officer would improve the transparency of the council's involvement in bodies such as these.

- There was a lack of guidance on the role of Council Members who are on such organisations' boards. Members of the BID company board are appointed by the Council but members of the limited company boards are not. The council is of the view that the Council Members that sit on the limited company boards do so in an individual capacity and not as Council Members. This distinction, and the rationale for it, needs to be clearly documented.
 - An officer of the council sat on the boards of both Dunfermline First and First Dunfermline when they were initially set up in August 2013, without the knowledge of senior council officers. The Employee Code of Conduct requires an employee to declare such membership to their line manager. The officer subsequently resigned from both boards once senior council officers became aware of the membership in August 2014 in order to avoid any conflict of interest.
155. In the absence of a robust initial assessment of this project funding and monitoring by the council it is difficult for the council to evidence that the funds provided were used for the intended purpose.
156. Changes are currently being made to the grants monitoring and evaluation framework and it would be appropriate to incorporate improvement actions which address the findings noted above to strengthen governance arrangements and the control framework.

Refer action plan, point 9

Performance management

157. Following the move to a portfolio based approach, the council is moving away from a service orientated planning framework to one based more on managing outcomes over a longer time frame. The council has been developing a new monitoring and reporting structure based upon outcomes which the council believes will better reflect performance against the council's priorities.
158. The council has developed a timetable for taking new portfolio themed outcome performance monitoring reports to committee and has recently taken the first of these reports, 'Improving Quality of Life in Local Communities', to the August 2016 Environment, Finance and Communities Scrutiny Committee. As well as the portfolio themed reports, the council also reports progress against all outcomes in its Annual Performance Report which is scheduled to be presented to the full Fife Council in December 2016. This is an area of ongoing development.
159. As noted at paragraph 142, the council participates in the LGBF. A high level report on the council's performance against each LGBF benchmark for 2015/16 is scheduled to be made available to the public in 2017, through the council's website. The council also produces a more detailed benchmarking report for use internally by council officers, which includes detailed quartile and family group information on each indicator.
160. We are satisfied that appropriate performance management arrangements were in place within Fife Council for 2015/16, although it is of some concern that the 2015/16 annual performance

report information will not be publically available until December 2016.

Overview of performance targets in 2015/16

161. The council's Annual Public Performance Report which reports progress in delivering the outcomes and targets set out in the Fife Community Plan 2020 and the Fife Council Plan 2012 to 2017, will not be available until December 2016. We are unable, at this stage, to report an assessment of the council's performance against its targets for 2015/16.

Statutory performance indicators (SPIs)

162. The Accounts Commission places great emphasis on councils' responsibility for public performance reporting. The Commission does not prescribe how councils should report but expects councils to provide citizens with fair, balanced and engaging performance information reporting.

163. For 2015/16 three (SPIs) were prescribed:
- SPI 1: covering a range of information relating to areas of corporate management such as employees, assets and equalities and diversity.
 - SPI 2: covering a range of information relating to service performance.
 - SPI 3: relates to the reporting of performance information as required by the Local Government Benchmarking Framework.

164. Overall we have concluded that the council's arrangements were satisfactory, although the Annual Performance Report and the LGBF information will not be reported until late 2016 and 2017 respectively.

Local performance audit reports

National performance audit reports

165. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2015/16, a number of reports were issued which are of direct interest to the council. These are outlined in [appendix III](#). The council has processes in place to ensure that national reports and their impact on the council are considered by the CET and Members.

Equalities

166. The Equality Act 2010 introduced a new public sector 'general duty' which encourages equality to be mainstreamed into public bodies' core work. The Act requires, by no later than 30 April 2015 and every two years thereafter, public bodies to publish a report on the progress made to achieve the equality outcomes it has set.

167. In 2016, the council published an annual Equality and Diversity Review report which outlines how well the council is performing against the equality outcomes that are set out in its Equality and Diversity Scheme. The report also identifies areas for improvement to be addressed by the council.

168. As part of the move to a portfolio based approach to managing its business the council has created a reducing inequality and opportunities theme board which has overall responsibility for equalities and diversity.
169. The council is reviewing its equality and diversity scheme and intends to produce a new scheme using a revised set of equality outcomes by April 2017.

Outlook

170. In common with other councils, Fife Council faces the key challenges of reducing budgets, an aging population with higher levels of need and the public expectation of high quality services. Savings have been made in recent years largely by reductions in the workforce. However, as choices on how to address funding gaps become increasingly difficult, councils will have to focus on making the very best use of all available resources and to challenge existing ways of doing things. A strong and effective performance management framework will be critical to the success of the council in achieving its key priorities and achieving best value.

Appendix I: Significant audit risks

The table below sets out the audit risks we identified during the course of the audit and how we addressed each risk.

Audit Risk	Assurance procedure	Results and conclusions
Risk of material misstatement in the financial statements		
<p>Income recognition</p> <p>Auditing standard ISA 240: The auditor's responsibility to consider fraud in an audit of financial statements requires auditors to presume a risk of fraud where income streams are significant. Fife Council receives a material amount of income from sources other than the Scottish Government including council tax, non domestic rates and housing rents.</p> <p>Risk: The extent of income means there is an inherent risk that income could be materially misstated. ISA 240 requires auditors to evaluate which types of revenue transactions give rise to such risks.</p>	<ul style="list-style-type: none"> Internal controls for key revenue systems are subject to review by Audit and Risk Management Services. Effective budgetary control by management. A range of measures are in place to prevent and detect fraud, including Standing Financial Instructions, Standing Orders, a Code of Conduct for Staff, a Fraud Prevention and Detection Strategy and a Whistleblowing Guide. Audit and Risk Management Services have a lead role in co-ordinating anti-fraud activities, including investigating all allegations of fraud and where appropriate reporting their findings to the Standards and Audit Committee. 	<ul style="list-style-type: none"> Evaluated accounting policies for income and expenditure. Tested journal entries. Reviewed accounting estimates. Evaluated the effectiveness of systems of internal control for income recognition and recording including the analytical review of income streams and testing of controls. Substantive tested income transactions to confirm occurrence and accuracy of amounts in the financial statements. Considered the fraud investigation work conducted by Audit and Risk Management Services. <p>We did not identify any instances of income being materially misstated.</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>Management override of control</p> <p>ISA 240 also requires auditors to consider, on all audits, management's ability to manipulate accounting records and prepare fraudulent or biased financial statements by overriding controls that otherwise appear to be operating effectively.</p> <p>Risk: Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls.</p>	<ul style="list-style-type: none"> A sound system of budgetary control including regular budget monitoring. Audit and Risk Management Services review a range of financial systems and related controls and provide an opinion on the control environment. A range of measures are in place to prevent and detect fraud, including Standing Financial Instructions, Standing Orders, a Code of Conduct for Staff, a Fraud Prevention and Detection Strategy and a Whistleblowing Guide. 	<ul style="list-style-type: none"> Tested journal entries. Reviewed accounting estimates for bias. Tested a sample of transactions substantively to confirm they have been correctly accounted for. Evaluated significant transactions to identify any that are outside the normal course of business. Analytically reviewed income and expenditure. <p>No evidence of fraud from our detailed testing of journal entries and review of accounting estimates for bias.</p>
<p>Restructuring of Financial Services</p> <p>The council is in the process of restructuring its Financial Services. We understand that this exercise will result in a reduction of about one third of Financial Services staff.</p> <p>Risk: the loss of key financial personnel from the service may impact on the council's ability to produce its financial statements to a high standard and by the statutory deadline. Changes also pose a risk to the wider control environment.</p>	<ul style="list-style-type: none"> The restructuring is being phased over three years and takes cognisance of the requirement to retain appropriately skilled staff to maintain the sound financial management of the Council and the production of accounts. Senior Management will continue to monitor the position on a regular basis. 	<ul style="list-style-type: none"> Reviewed systems of control including impact of reductions in staff. Reviewed standard of working papers provided to support the financial statements <p>We did not find any significant issues with the wider financial control environment, however some deterioration was noted in the standard of working papers compared to last year due to finance staff having changed their areas of responsibilities.</p>

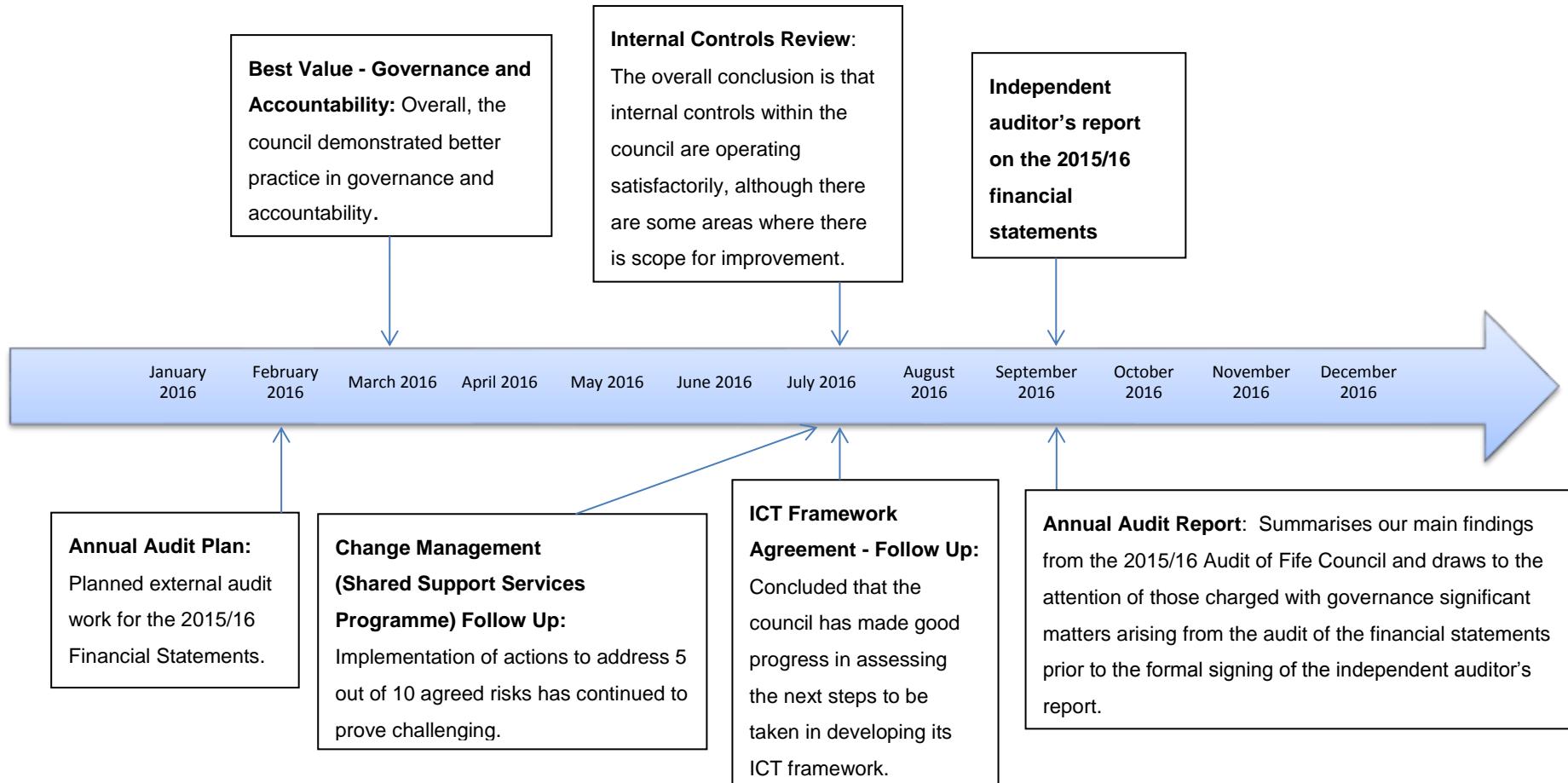
Audit Risk	Assurance procedure	Results and conclusions
<p>Accounting for the Fife Integration Joint Board (Fife IJB)</p> <p>The Fife IJB was established on 3 October 2015 (and will be required to prepare its own annual accounts for 2015/16). As a result, Fife Council will be required to include the IJB in its assessment of entities for inclusion in the group accounts and to consider relevant financial and governance disclosures regarding the IJB for 2015/16.</p> <p>Risk: Fife Council may not account for the IJB appropriately within its 2015/16 annual accounts.</p>	<ul style="list-style-type: none"> Liaison between Fife Council and the Chief Officer / Chief Finance Officer for the IJB to ensure that appropriate information is agreed and shared. Senior Management will continue to monitor the position on a regular basis. 	<ul style="list-style-type: none"> Considered the accounting treatment and disclosure in the annual accounts. <p>Fife IJB was correctly disclosed in the 2015/16 Fife Council accounts. The financial transactions of Fife IJB were not included in the council's group accounts as the amounts concerned in 2015/16 are not material.</p>
<p>Accounting for equal pay</p> <p>In light of the developments associated with the equal pay claims settlement, the council will be required to account for the expenditure, estimated at over £50 million, in the 2015/16 financial statements.</p> <p>Risk</p> <p>The council may not account for these appropriately in the financial statements and may not provide appropriate disclosure of the circumstances surrounding the expenditure.</p>	<ul style="list-style-type: none"> Management is aware of the accounting and disclosure requirements of the equal pay settlement and have plans in place to apply proper accounting practices. 	<ul style="list-style-type: none"> Considered the accounting treatment and disclosure in the annual accounts. <p>The 2015/16 expenditure and the associated year end provision are materially correct and disclosed appropriately within the council's financial statements.</p>

Audit Risk	Assurance procedure	Results and conclusions
Risks identified from the auditor's wider responsibility under the Code of Audit Practice		
<p>Health and social care integration</p> <p>The integration of health and social care services in Scotland requires to be implemented fully by 1 April 2016. Although the Fife IJB has been established and good progress has been made, significant aspects of health and social care integration still require to be progressed.</p> <p>Risk: Fife Council may not be fully prepared for the integration of health and social care. Financial pressures and political tensions could also adversely impact on the effectiveness of the move to full and effective implementation of health and social care integration.</p>	<ul style="list-style-type: none"> Regular reporting to the Integration Joint Board on progress on the integration of health and social care. 	<ul style="list-style-type: none"> Reviewed progress towards implementation by reviewing the reports presented to the Council. Reviewed internal audit report on health and social care integration financial assurance processes. <p>Good progress has been made but there remains much to do. We concluded that more information could be provided to Fife Council members on the Fife IJB financial position. This has been included in the action plan at Appendix IV (refer action plan, point 7).</p>
<p>Information technology – follow up review</p> <p>We reported last year on three areas of our IT work covering: the Enterprise Resource Planning (Financial Management) application review; the IT and Change Framework agreement; and a follow up audit of Change Management (Shared Support Services Programme). Action plans were agreed with the council.</p> <p>Risk: Actions may not be progressed or may not</p>	<ul style="list-style-type: none"> Action plans are being monitored by IT management. 	<ul style="list-style-type: none"> Undertook follow up reviews of actions agreed in the three 2014/15 IT reports. <p>Good progress has been made although some actions identified in 2014/15 remain to be completed.</p>

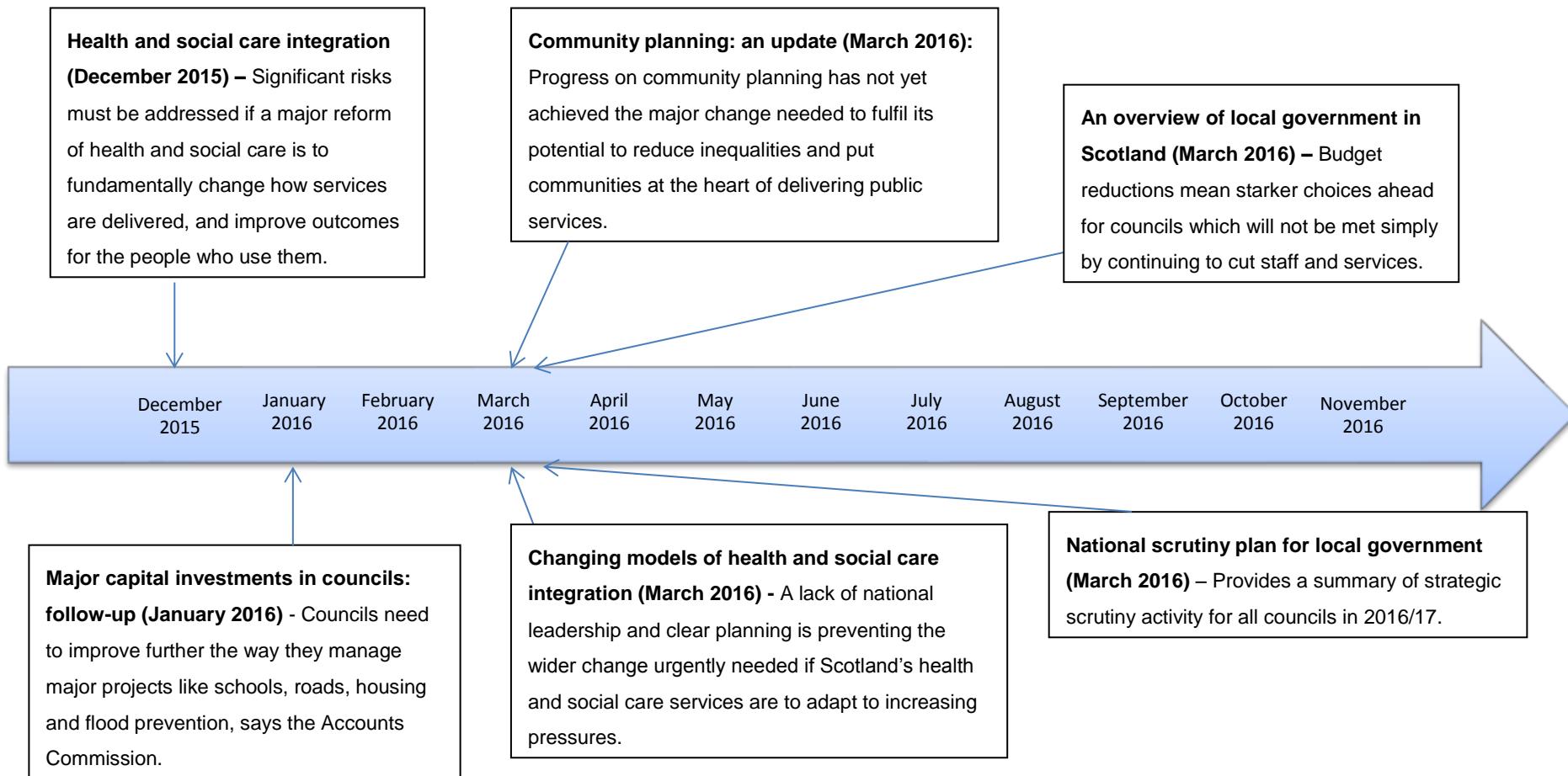
Audit Risk	Assurance procedure	Results and conclusions
be progressed timeously which would impact on the council successfully achieving improvements in its IT environment.		
<p>Information technology - cyber attacks</p> <p>Over the past 12 months several Scottish public organisations have been victims of cyber attacks and related activities. The threat from cyber attacks will continue to develop, potentially leading to reputational and financial harm.</p> <p>Risk: cyber attacks could disrupt the availability of the council's critical operational and financial systems.</p>	<ul style="list-style-type: none"> • Business continuity arrangements. 	<ul style="list-style-type: none"> • Undertook a high level, focused review of the council's arrangements to prevent and respond to cyber attacks. <p>Overall, we found that the council is aware of the risks associated with cyber attacks and is taking appropriate action to mitigate those risks.</p>
<p>Workforce planning</p> <p>In June 2015, a report to the Council Executive Team assessed the estimated workforce reduction over the period 2011 to 2018 at 2,375 full time equivalent (FTE) posts, of which 1,894 FTE posts have already been released up to 2014/15. The scale of the financial challenge facing the council means that further workforce change is probable. The council will need to consider different ways of delivering services including service re-design and increased joint</p>	<ul style="list-style-type: none"> • In December 2015, the Council Executive Team approved the Workforce Strategy 2016 – 2020. This set out the vision for the workforce and the strategic outcomes, and gives the Corporate Workforce Plan. • Priority actions are determined through stakeholder engagement on an annual basis, allowing emerging needs to be reflected in a dynamic way. • Actions within the Corporate Workforce Plan are progressed and evaluated over 	<ul style="list-style-type: none"> • Carried out a local follow up work based on the recommendations in Audit Scotland's report, <i>Scotland's Public Sector Workforce</i>. <p>Broadly, Fife Council meets many of the elements of good practice identified in the report. Some areas of improvement have been identified and have been included in the action plan at Appendix IV (refer action point 5).</p>

Audit Risk	Assurance procedure	Results and conclusions
<p>working and collaboration and will need be clear on the impact this has on the workforce requirements under any identified reforms.</p> <p>Risk: the council may be unable to deliver necessary service change in an increasingly challenging financial environment if its workforce requirements are not properly identified.</p>	<p>the course of each year, and reported in the Annual Workforce Report.</p> <ul style="list-style-type: none"> • The Annual Workforce Report is presented to Scrutiny Committee and Council Executive Team and is shared with the Trade Unions.. 	

Appendix II: Summary of local audit reports 2015/16



Appendix III: Summary of Audit Scotland national reports 2015/16



Appendix IV: Action plan

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
1. 13/ 37	<p>Overspend within services' revenue budgets</p> <p>Although the council achieved a net surplus of £11.9 million in 2015/16, service expenditure was overspent by £3.0 million. As in 2013/14 and 2014/15, the net surplus was only achieved as a result of underspends against budget on corporate activities.</p> <p>Risk: Continuing overspends on service delivery could impact on longer term financial sustainability. Savings on other corporate activities may not be sustainable in the long run.</p> <p>Recommendation: The council should review its service delivery to ensure that all services are put on a sound financial footing within reducing resources.</p>	<p>The Council is aware of the potential size of further reductions in income and planning is ongoing to deal with this. The Council Executive Team and individual Directorates have recently completed an exercise to redesign services within the likely medium term reduced resource which is intended to ensure that key services are delivered within the resources available. This information will form part of the ongoing budget strategy.</p>	Eileen Rowand (Executive Director Finance & Corporate Services) Ongoing

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
2. 16/ 59	<p>Financial management and sustainability</p> <p>The council faces budget cuts of up to £141 million by 2019/20. Transformational change will be required as recognised in the Executive Director Finance and Corporate Services report to the Executive Committee on 16 August 2016 which stated that “it is important that the council develops a medium term financial plan in order to support the spending priorities going forward and to ensure that the Council is financially sustainable”.</p> <p>Risk: The council may not be able to generate sufficient efficiencies and cost savings to bridge the funding gap and without effective transformation may find itself delivering reduced services.</p> <p>Recommendation: The council should ensure that it has robust medium to long term financial plans to address the anticipated budget gap. This will require an increased pace in the implementation of transformational change for service delivery.</p>	<p>The exercise to redesign services within the likely medium term reduced resource mentioned in Action Point 1 will form the basis of the Council’s budget strategy. It is accepted that an effective budget strategy must cover more than one financial year and that the pace of transformational change must increase. Plans currently being developed by the Council Executive Team will present the Council with options.</p>	Steve Grimmond (Chief Executive) Ongoing

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
3. 17/ 61	<p>Capital slippage</p> <p>The council has incurred significant slippage of £60.6 million in its capital programme in 2015/16.</p> <p>Risk: Capital programmes and associated service improvements may not be delivered in a timely manner.</p> <p>Recommendation: The council should consider the impact of the significant slippage on its capital programme.</p>	<p>The Council achieved a record level of Capital Expenditure in 2015-16 of £210m. The reality is that the Council has a reputation for delivering capital projects, however it is evident that there can be over optimism around the overall level of delivery. One of the outcomes from the ongoing review of the 10 Year Capital Plan will be approval of more realistic project spending profiles.</p>	Keith O'Donnell (Head of Finance / Chair of Investment Strategy Group) February 2017

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
4. 19/ 73	<p>Dunfermline flood prevention scheme</p> <p>The scheme was completed some five and half years later than originally planned at a cost £34.5 million, which was £20.3 million over budget. The council is currently engaged in legal action to attempt to recover a significant proportion of the additional costs associated with DFPS</p> <p>Risk: The council may be unsuccessful in its legal action if deficiencies are identified in their processes around the management of the scheme.</p> <p>Recommendation: Once the current legal cases are concluded, we recommend the council undertakes a final review of the legal decision on the DFPS project to see whether there are any additional lessons to be learned that should be incorporated into the council's standard procedures for managing and monitoring its capital programme and projects.</p>	<p>A final review will be carried out at the conclusion of the legal action.</p>	<p>Steve Grimmond (Chief Executive)</p> <p>At conclusion of legal action</p>

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
5. 20/ 77	<p>Workforce planning</p> <p>Our review of the council's arrangements over workforce planning found that there are some areas for improvement which particularly impact upon governance by elected members. These are:</p> <ul style="list-style-type: none"> • Elected members were not given an opportunity to scrutinise the council's workforce strategy. • Senior officers and members did not consider Audit Scotland's good practice guidance when scrutinising the workforce strategy to ensure it meets good practice. • The council's annual workforce report to elected members had limited focus on financial outcomes. <p>Risk: Elected members may not be given all of the information they require to properly scrutinise the workforce planning arrangements for the council.</p> <p>Recommendation: Management should ensure that relevant information on workforce planning is provided to enable elected members to reach informed decisions.</p>	<p>The Workforce Strategy Themes were outlined in the Annual Workforce Report 2014/15 which was scrutinised by members of the Environment, Finance & Corporate Services Scrutiny Committee on 10th November, 2015.</p> <p>Senior Officers were aware of Audit Scotland's good practice guidance when scrutinising the workforce strategy.</p> <p>The Annual Workforce Report 2015/16 refers to Audit Scotland's recommendations and good practice guidance. This report will be considered by the Environment, Finance & Corporate Services Scrutiny Committee on 1st November, 2016.</p> <p>We are in the first year of our new corporate workforce planning process. Further consideration will be given to how elected members are engaged in the scrutiny process.</p> <p>When drafting the annual workforce report for 2016/17, consideration will be given to the report having a focus on financial outcomes.</p>	Sharon McKenzie (Head of Human Resources) March 2017

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
6. 24/ 95	<p>Governance and accountability</p> <p>Our review of the council's arrangements for governance and accountability identified some areas for improvement and we recommended that an action plan be prepared by management to implement improvements. We note that work on producing an action plan has not yet commenced.</p> <p>Risk: The council may not achieve improved governance and accountability arrangements.</p> <p>Recommendation: An action plan should be prepared as soon as practicable addressing the improvement areas identified in our report to management.</p>	<p>A review of accountability and governance arrangements is being discussed to prepare options for discussion with the council. This will build on the work undertaken by external audit and also allow for developments to better meet the requirements of future public service change.</p> <p>Specific action to address the audit comments in relation to the Councillors' Register of Interests has already been taken and further work is ongoing in relation to looking at a more robust programme of elected member development opportunities. This will include re-establishing the Elected Member Development Focus Group and a review of previous practice in relation to elected member induction following Local Government Elections.</p>	Linda Bissett (Head of Democratic Services) / Paul Vaughan (Head of Community and Corporate Development) May 2017

No.	Issue/risk/Recommendation Page/Para.	Management action/response	Responsible officer / Target date
7. 29/ 131	<p>Fife IJB</p> <p>Very little detailed information on the financial and governance arrangements of the IJB has been presented to members of Fife Council.</p> <p>Risk: Members may not have sufficient information on the IJB to allow them to discharge their council responsibilities.</p> <p>Recommendation: Consideration should be given to the level of information provided to members in relation to the IJB.</p>	<p>Detailed financial information is provided to members of Fife Council on the funding provided from Fife Council to the Integrated Joint Board. Work is ongoing around how information on the wider IJB budget, including the contribution from NHS Fife, can be reported to members.</p>	Eileen Rowand (Executive Director Finance & Corporate Services) December 2016

Appendix IV: Action plan

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
8. 32/ 144	<p>Self evaluation and FEM</p> <p>We were advised in 2014/15 that the council had postponed the reintroduction of its self evaluation mechanism, the Fife Excellence Model (FEM), as a result of resources being diverted to implement new initiatives. Although we were advised that the council would recommence the FEM programme, as a less resource intensive but effective product in April 2016, currently the revised self evaluation model is still being developed.</p> <p>Risk: The council may not be able to evidence that it is achieving best value.</p> <p>Recommendation: Management should implement a revised self evaluation model as soon as practicable.</p>	<p>The Council has been working closely with the Improvement Service on the development of a less onerous approach to self-assessment using the Fife Excellence Model (FEM). A paper outlining a revised approach was endorsed by the Council Executive Team (CET) in June 2016 and a pilot self-assessment exercise is currently underway with the Economy, Planning & Environment Service (Sept/Oct 2016). Experience from this pilot will subsequently help inform the ongoing development and deployment of the new approach going forward.</p>	<p>Craig Waddell (Corporate Development Manager)</p> <p>October 2016</p>

No.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
Page/Para.			
9. 34/ 156	<p>Following the public pound</p> <p>Our review of the processes for non-recurring grant to a local company, Dunfermline First highlight some areas where there is scope for improvement in the council's non-recurring grant processes, including:</p> <ul style="list-style-type: none"> • Improving assessments of prospective projects. • Appointment of monitoring officers. • Providing clear guidance on the role of Council Members who are on such organisations' boards. • Reviewing the arrangements where employees intend to sit on such organisations' boards. <p>Risk: Governance arrangements and the control environment may not be effective in preventing conflicts of interest and improper use of public funds.</p> <p>Recommendation: The council should review its arrangements for non-recurring grants in line with the Following the public pound guidance.</p>	The council is reviewing the grants monitoring and evaluation framework and will incorporate changes to the monitoring of non-recurring grants and the role of monitoring officers within this guidance. As part of the briefing to councillors on their role in sitting on boards, the requirements of directorships for charities and companies will be reinforced.	Paul Vaughan (Head of Community and Corporate Development) December 2016