

# West Lothian Council

Year ended 31 March 2017

Annual Audit Report

29 September 2017



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Section	Appointed auditor responsibility	Pages
<b>Executive summary</b>		<b>1-3</b>
<b>Financial statements accounting and audit matters</b>	Provide an opinion on audited bodies' financial statements	<b>4-13</b>
	Notify the Controller of Audit when circumstances indicate that a statutory report may be required	<b>5</b>
	Review and report on, as appropriate, other information such as annual governance statements, management commentaries and remuneration reports	<b>13</b>
<b>Wider scope audit</b>	Demonstrate compliance with the wider public audit scope by reviewing and providing judgements and conclusions on the audited bodies:	
	▶ financial position and arrangements for securing financial sustainability	<b>16-22</b>
	▶ suitability and effectiveness of corporate governance arrangements	<b>23-28</b>
	▶ effectiveness of performance management arrangements in driving economy, efficiency and effectiveness in the use of public money and assets	<b>29-30</b>
<b>Other audit deliverables</b>	Other assurance work such as grant claim certification and information returns for Audit Scotland	<b>32</b>
<b>Appendices</b>	Undertake statutory duties, and comply with professional engagement and ethical standards:	
	Appendix A: audited bodies' responsibilities	<b>34</b>
	Appendix B: required auditor communications	<b>35-36</b>
	Appendix C: auditor independence	<b>37</b>
	Appendix D: accounting and regulatory update	<b>38</b>
	Appendix E: summary of audit differences	<b>39 - 41</b>
	Appendix F: action plan	<b>42-45</b>

## About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of West Lothian Council (the Council) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

This report is for the benefit of the Council and is made available to the Accounts Commission, the Controller of Audit and Audit Scotland (together the Recipients). This report has not been designed to be of benefit to anyone except the Recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

## Complaints

If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Russell Frith, Assistant Auditor General, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

## Purpose of this report

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as the external auditor of West Lothian Council (the Council) for the five year period 2016/17 to 2020/21. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Auditing Practices Board; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Report is designed to summarise our key findings and conclusions from our audit work. It is addressed to both the members of the Council and the Controller of Audit, and presented to both Council management and those charged with governance. It will be published on Audit Scotland's website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the Council. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

## Scope and responsibilities

The Code sets out the responsibilities of both the Council and the auditor. We provided details of these in our Annual Audit Plan, which was presented to the audit committee on 27 February 2017. We summarise the responsibilities of the Council in Appendix A.

Our Annual Audit Plan also provided you with an overview of how we intended to carry out our responsibilities as your auditor. We carried out our audit in accordance with this plan with the exception of the following key change:

- ▶ Valuation of property, plant and equipment was changed to a significant audit risk from an inherent audit risk, reflecting the significance of change in valuation of certain property assets within the unaudited financial statements.

We planned our procedures using a materiality of £12 million and a Tolerable Error of £9 million. We reassessed this using the actual year-end figures contained within the unaudited financial statements, to confirm that the materiality remained appropriate for the audit. No adjustment was made to materiality amounts communicated in our Annual Audit Plan. The threshold for reporting audit differences is £250,000, in accordance with the Code.

## Status of the audit

We have completed our audit of West Lothian Council's financial statements for the year ended 31 March 2017. We have issued an unqualified opinion on the Council's financial statements for the year.

## Key contacts

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## Acknowledgement

We would like to thank all members of the Council's management and staff who have been involved in our work for their co-operation and assistance during our audit work.

## Accounting and audit matters – our reporting on the Council's financial statements

### Preparation of financial statements

- ▶ The unaudited financial statements were prepared to a good standard.
- ▶ There were a number of audit differences identified which were adjusted by management. Included within these were errors identified in the opening balance sheet information which resulted in management correcting the prior year comparative figures. The overall impact of audit differences was to increase net assets as at 31 March 2016 by £476.6 million in the consolidated balance sheet, and increase net assets by £17.1 million as at 31 March 2017. There was an overall increase in general fund of £6.6 million (2015/16: £6.6 million), due to the correction of treatment of developer contributions from the HRA.

### Significant risks

#### *Risk of fraud in income and / or expenditure recognition*

- ▶ We have not identified any material weaknesses in the design and implementation of controls tested as part of our audit, or evidence of fraud in income and expenditure recognition during the financial year.

#### *Management override of controls*

- ▶ We have not identified any material weaknesses in the design and implementation of controls around journal processing. We did not identify any instances of evidence of management override of controls.
- ▶ We consider that management made good disclosure on the accounting judgements and estimates made, with some scope for further enhancement.

#### *Valuation of property, plant and equipment*

- ▶ We identified a prior year adjustment of £470 million on the carrying value of property, plant and equipment as at 31 March 2016. This comprised an increase in value of other land and buildings by £482.3 million, offset by a decrease in value of £12.3 million to council dwellings. In addition, an adjustment of £23.3 million was also required to the 31 March 2017 carrying values of council dwellings to ensure these reflected Existing Use Value – Social Housing.
- ▶ While underlying valuations are robust, the process for accounting for changes in value can be enhanced.

### Other inherent risks

#### *Retirement benefits*

- ▶ Defined benefit pension scheme liabilities have been estimated using actuarial assumptions which we consider to be reasonable. The required disclosures are provided in the financial statements, including those providing details of the sensitivity of the valuation to changes in the assumptions.
- ▶ We have undertaken appropriate testing of underlying data to support the calculation of the liability.

### Other matters and reporting requirements

- ▶ The new Expenditure and Funding Analysis has been presented appropriately and the Movement in Reserves Statement and Comprehensive Income and Expenditure Statement restated accordingly. We consider the disclosures provided to be appropriate to the Council's internal reporting during the year.
- ▶ We have obtained reasonable and appropriate audit evidence over the Council's group financial statements. Based on our group scoping we were not required to undertake detailed testing at components of the group. We are the appointed auditor to West Lothian Integration Joint Board.
- ▶ We undertook the audit of nine of the Council's registered charitable trusts. We have provided a unqualified audit opinions on the financial statements of the trusts.
- ▶ We have concluded that the Council has complied with the requirements of the Local Authority Accounts (Scotland) Regulations 2014. In respect of our 'Opinions on other prescribed matters', which includes the management commentary, the auditable part of the remuneration report, and the annual governance statement, our opinion is unqualified.
- ▶ We include a statement noting that the Council has failed to achieve its statutory responsibilities to ensure that its significant trading operations achieves a break even position over a three year rolling period. We have not identified any other matters on which we are required to report by exception.

## Wider scope audit dimensions – our judgements and conclusions on the Council's arrangements

### Financial management

- ▶ We have concluded that the Council has generally sound financial management arrangements. This has been based on identification and overall tracking of budget savings well in advance as part of two-year indicative annual budget setting.
- ▶ The Council is going through a period of significant capital investment, both in general fund services and council housing. While there has been some delay in the new build housing programme, there is good evidence of delivery and management of projects.

We have made one recommendation in the action plan (point 4) in respect of the Council's arrangements.

### Financial sustainability – area of audit focus

- ▶ We have concluded that the Council's financial position is generally sound. While significant investment is required in response to demographic pressures, it has a good basis to undertake this investment.
- ▶ The Council has an established process for aligning its financial strategy to its corporate plan priorities. As a result only a one-year budget was approved for 2017/18, as this was the final year of the existing five year corporate plan. The Policy Development and Scrutiny Panels will consider the results of the public consultation in respect of officers' savings proposals in December 2017, prior to Council approval of a new five year corporate plan and underlying financial strategy in February 2018. In our view, since difficult decisions are expected to be required, the timeline for involvement of members could leave the delivery of savings in the required timescales at risk.

We have made three recommendations (points 5, 6 and 7) , two of which are graded one, in respect of the Council's arrangements.

### Governance and transparency – area of audit focus

- ▶ The Council has a comprehensive framework of governance arrangements and shows clear commitment to the core principles. Internal audit is well respected, however, we have raised a number of recommendations for consideration to strengthen reporting and monitoring by the audit committee.
- ▶ We consider there is scope to strengthen the arrangements for scrutiny of corporate and service performance. The relationship between the new governance & risk and audit committees should be monitored. The Council needs to improve the controls and governance arrangements around Following the Public Pound.

We have made seven recommendations (points 8 to 14), two of which are graded one, in respect of the Council's arrangements.

### Value for Money

- ▶ We have concluded that the Council has a comprehensive performance improvement framework, founded on the well established West Lothian Assessment Model. This has provided a stable and consistent framework through which services undertake self-assessment and seek to improve their performance.
- ▶ The Council monitors a suite of performance indicators through the Covalent system. Performance information shows that the Council generally performs very well compared to other councils, although the Council recognises areas where performance can be improved.

We have not identified any recommendations in respect of the Council's arrangements.

## Appendices

We set out in the appendices a number of required communications we provide in accordance with auditing and ethical standards. In particular, we have confirmed our continuing independence to act as auditor of the Council. No non-audit services have been provided to the Council during the year.

We also provide a short accounting and regulatory update highlighting forthcoming changes and their potential impact on the Council.

# **1. Financial statements and accounting**

# 1. Financial statements and accounting



The Council's Annual Accounts enables the Council to demonstrate accountability for, and its performance in the use of its resources. They are prepared in accordance with proper accounting practice, which is represented by the 2016/17 Code of Practice on Local Authority Accounting in the United Kingdom.

## Audit opinion

In respect of the financial statements, we have issued an unqualified opinion on the truth and fairness of the state of affairs of the Council and its group at 31 March 2017 and of the deficit on provision of services for the year then ended, in accordance with applicable law and the 2016/17 Code of Practice.

The detailed form and content of our audit report, plus the requirements underpinning the report are contained in the Audit Scotland guidance at:

[http://www.audit-scotland.gov.uk/uploads/docs/um/tgn\\_2017\\_5\\_local\\_authorities.pdf](http://www.audit-scotland.gov.uk/uploads/docs/um/tgn_2017_5_local_authorities.pdf).

We have not identified any circumstances to notify the Controller of Audit that a statutory report may be required under the Local Government (Scotland) Act 1973.

## Financial statements preparation

As part of your oversight of the Council's financial reporting process, we report on our consideration of the quality of working papers and supporting documentation prepared predominantly by the finance team to support the audit.

The overall preparation of the financial statements appears to be a smooth process and the financial statements are, in our view, easily readable and appropriately concise in the presentation of material financial information. Based on the findings expressed later in this section, overall we believe there is scope to improve the financial reporting process further in respect of supporting evidence of key judgements. This includes clearly documented consideration and review of critical assumptions around the valuation of property, plant and equipment and consideration of the scope of group financial statements. We have agreed with the finance team to work together to continuously improve both the financial reporting and audit process.

**Action plan point – 1**

## Materiality

We planned our procedures using a materiality of £12 million. We reassessed this using the actual year-end figures contained within the unaudited financial statements, to ensure that our level of materiality remained appropriate. We did not change our assessment of materiality as a result. Our Tolerable Error for the audit was £9 million and the threshold for reporting audit differences is £250,000.

We also identified areas where misstatement at a lower level than materiality might influence the reader and developed a specific audit strategy for them. They include:

- ▶ Remuneration disclosures including any severance payments, exit packages and termination benefits - we applied a materiality of £1,000 based on the potential sensitivity of these disclosures.
- ▶ Related party transactions - we considered the nature of these disclosures individually.

## Audit differences

We identified one unadjusted audit differences in the draft financial statements which management has chosen not to adjust. We ask that the audit committee and Council note this and that this will be included in the Letter of Representation. The aggregated impact of unadjusted audit difference is a £3 million decrease in net assets. We agree with management's assessment that the impact is not material.

There were a number of audit differences identified which were adjusted by management. Included within these were errors identified in the opening balance sheet information which resulted in management correcting the prior year comparative figures. We provide details of the reasons behind these adjustments within the relevant section of the report. The overall impact of audit differences was to increase net assets as at 31 March 2016 by £476.6 million in the consolidated balance sheet, and increase net assets by £17.1 million as at 31 March 2017. There was an overall increase in general fund of £6.6 million (2015/16: £6.6 million) due to the correction of treatment of developer contributions from the HRA. Full details can be found in Appendix E – Summary of Audit Differences.

Our Audit Plan identified key areas of focus for our audit of the Council's financial statements, including significant risks. This report sets out the results of our audit procedures plus relevant observations, including our views on areas which might be conservative, and where there may be potential risk and/or exposure.

## Significant risk – risk of fraud in income and expenditure recognition

### What is the risk?

Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

We rebutted the risk of improper recognition of revenue in respect of core grant funding from the Scottish Government, as well as in respect of council tax and non-domestic rate income. This is because there is no judgement in respect of the recognition of these income streams.

### Results of audit procedures

In relation to income, predominantly fees and charges, and other operating expenses where we had identified a significant risk of material misstatement, we:

- ▶ Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias.
- ▶ Reviewed transaction listings for individually material transactions as well as unusual items (debits to income, credits to expenditure etc.) to agree to supporting documentation and third party evidence.
- ▶ Tested a representative sample of transactions across the remaining untested income and expenditure population to ensure coverage of testing across all balances.
- ▶ Reviewed and tested revenue cut-off around the year end through reviewing manual journals posted to revenue and reviewing material credit notes raised after year end.
- ▶ Performed a search for material receipts received after year end and ensured these had been accounted for in the correct period.

Where we are performing procedures to address significant risks to the financial statements we do so to a lower level of materiality than for standard accounts. All procedures outlined above were completed with no material reported audit differences or other matters noted.

### *Other income and expenditure areas*

The most significant area of revenues was taxation and non-specific grant income of £399 million. £249 million of this related to government grant income which we substantively tested to grant confirmation letters. The remainder is made up of £87.7 million of NDR redistributions and £62.2 million of Council Tax income. These were agreed either to funding correspondence, and / or through establishing detailed expectations of income and expenditure, agreeing underlying assumptions to supporting evidence, and comparison to actual income and expenditure recorded by the Council in the year.

For expenditure, £230 million relates to payroll costs. These have been subject to detailed analytical procedures and reconciliation to underlying payroll information. We have agreed PPP transaction costs to PFI contract and finance models. Depreciation and impairment charges have been subject to detailed audit testing, including reconciliation to fixed asset register.

### Risk of fraud in income and expenditure recognition – what have we concluded?

- ▶ We have not identified any material weaknesses in the design and implementation of controls tested as part of our audit, or evidence of fraud in income and expenditure recognition during the financial year.



## Significant risk – management override

### What is the risk?

As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

### Audit procedures performed and what did we find?

*Test the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements*

We obtained a full list of journals posted to the general ledger during the year, and used our bespoke data analysers to identify any unusual journal types or amounts based on our identified risk areas for the audit. We then tested a sample of these journals, understood their purpose and agreed and corroborated them to supporting documentation.

*Review accounting estimates for evidence of management bias, including management's retrospective consideration of prior year estimates.*

We identified and considered the appropriateness of key accounting estimates, including provisions, and their susceptibility to bias. Management have disclosed their consideration of the critical accounting judgements and key estimates in the financial statements. We have reviewed these and agree with the detail of the assessment performed.

*Evaluate the business rationale for any significant unusual transactions*

We did not identify any significant unusual transactions outside the normal course of business.

*Review capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised.*

We reviewed expenditure on property, plant and equipment to ensure that expenditure items were not being inappropriately capitalised to defer costs to future years. Likewise we performed analytical procedures and transaction testing of HRA expenditure to ensure HRA funds were not being utilised to meet general fund expenditure. No issues were noted through our testing performed.

### Risk of management override – what have we concluded?

- ▶ We have not identified any material weaknesses in the design and implementation of controls around journal processing. We did not identify any instances of evidence of management override of controls.
- ▶ We consider that management made good disclosure on the accounting judgements and estimates made, with some scope for further enhancement.

## Significant risk – valuation of property, plant and equipment

### What is the risk?

The Council's property portfolio totalled £1.3 billion as at 31 March 2016, with the major elements of this being in respect of council dwellings, other land and buildings and infrastructure assets. Given the size of this balance and the fact that a number of assumptions are made in the valuation, we initially assigned a higher inherent risk to the valuation of property, plant and equipment.

The unaudited financial statements included significant revaluations in respect of certain operational land and buildings, totalling over £400 million. As a result, we re-scoped this aspect of our work as a significant risk.

### Audit procedures performed and what did we find

Through analysis of the source data and enquiries of management, we considered the appropriateness as to the procedures used by management's specialist to establish whether the source data was complete and concluded this was satisfactory.

We assessed the reasonableness of the assumptions and methods used in the valuation of land and buildings, including compliance with the Code of Practice on Local Authority Accounting. In doing so, we also considered the appropriateness of the timing of when management's specialist carried out the work. The Council revalue assets as part of a five year rolling programme. The Code of Practice on Local Authority Accounting requires assets to be carried at fair value. The Council considers material changes in asset valuations through consideration of significant capital additions in the year, as well as discussions with in-house valuers around potential asset impairments. This does not necessarily consider the potential impact of market movements impacting on fair value.

In line with the Council's policy, some operational land and buildings were subject to revaluation as at 1 April 2016. From assessment of market data management confirmed that the material increase in the asset valuations was due to conditions that existed as at 31 March 2016. Given the material revaluation increases, we concluded that this change should have been reflected in the prior year financial statements and that the carrying value was materially understated. We also identified that the Council had historically carried PPP school assets at cost on the balance sheet rather than at fair value. Taken together, the total value of the prior year misstatement for these elements was to understate assets by £482.3 million.

In respect of the valuation of council dwellings, we identified that these were also not appropriately valued as at 31 March 2017 or 2016. Consequently an impairment of £23.3 million (2016: £12.3 million) was required to the carrying value of these assets to ensure these were carried at Existing Use Value – Social Housing.

In performing our work, we involved EY valuation specialists to ensure management's underlying valuation approach was appropriate and consistent with guidance. We concluded that the underlying valuation process is robust. We recommend that management enhance the existing valuation process to ensure that a full consideration of the appropriateness of asset valuations, and their recognition in the financial statements, is undertaken in a more timely manner.

**Action plan point – 2**

## Significant risk, valuation of property, plant and equipment – what have we concluded?

- ▶ We identified a prior year adjustment of £470 million on the carrying value of property, plant and equipment as at 31 March 2016. This comprised an increase in value of other land and buildings by £482.3 million, offset by a decrease value of £12.3 million to council dwellings. In addition, an adjustment of £23.3 million was also required to the 31 March 2017 carrying values of council dwellings to ensure these reflected Existing Use Value – Social Housing.
- ▶ While underlying valuations are robust, the process for accounting for changes in value can be enhanced.

## Other inherent risks – retirement benefits

### What is the risk?

The Code and IAS19 require the Council to make extensive disclosures within its financial statements regarding the Local Government Pension Scheme (LGPS). Accounting for the pension fund assets and liabilities involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

### Results of audit procedures

In planning our audit, we identified that pension liabilities at 31 March 2016 were £176.1 million. Following the result of the EU Referendum in June 2016, we saw significant changes in certain economic assumptions used in the valuation of pension liabilities leading to significant increases in reported net pension liabilities by entities with accounting year-ends after June 2016. At 31 March 2017, the Council's net pension liability had increased to £290.3 million, primarily as a result of changes in the discount rate used to value the pension obligations. Our audit procedures included:

- ▶ Analysis of the payroll and pensions source data and made inquiries as to the procedures used by management's specialist to establish whether the source data was relevant and reliable.
- ▶ Utilisation of EY pension specialists to challenge the appropriateness of the assumptions used in deriving the liabilities at 31 March 2017. As part of this work, our specialists considered the work undertaken by PWC on behalf of the public audit agencies to provide assurance over the major actuarial firms involved in preparing IAS 19 valuation reports. Assumptions used by the actuary and adopted by the Council are considered to be within our acceptable range.
- ▶ Testing of the journal entries for the pension transactions to ensure that they have been accurately processed and agreed the required disclosures in the financial statements to relevant information provided by the actuary.

## Other inherent risks, retirement benefits – what have we concluded?

- ▶ Defined benefit pension scheme liabilities have been estimated using actuarial assumptions which we consider to be reasonable and the required disclosures have been provided in the financial statements, including those providing details of the sensitivity of the valuation to changes in the assumptions.
- ▶ We have undertaken appropriate testing of underlying data to support calculation of the liability.

Our Audit Plan identified other audit matters and aspects of our work which arise either in accordance with International Standards on Auditing (UK & Ireland) or in accordance with the Code. These are set out below.

## Other audit matters

### Expenditure and funding analysis

In 2016/17 there were amendments to the Code as a result of the 'Telling the Story' review of the presentation of local authority financial statements. The Code no longer requires statements or notes to be prepared in accordance with SeRCOP. Instead the Code requires that the service analysis is based on the organisational structure under which the Council operates, reflecting internal financial reporting structures.

This change impacted the Consolidated Income and Expenditure Statement (CIES), the Movement in Reserves Statement (MiRS) and introduced the new expenditure and funding analysis (EFA), with full retrospective restatement of the CIES and MiRS. Our audit approach has focused on:

- ▶ Reviewing the expenditure and funding analysis, CIES and new notes to ensure disclosures are in line with the Code. Management initially presented the EFA as the first statement within the financial statements. Since it does not form one of the four primary statements, we requested that management make the narrative clear that the EFA, while displayed prominently, is a note to the financial statements.
- ▶ Reviewing the analysis of how these figures are derived, the re-mapping of the ledger system to reflect the Council's organisational structure and how overheads are apportioned across the service areas reported.
- ▶ Agreement of restated comparative figures back to the Council's segmental analysis and supporting working papers.

### Opening balances

International Standard on Auditing (UK and Ireland) 510: *Initial audit engagements – opening balances* requires auditors to obtain sufficient, appropriate audit evidence that opening balances do not contain misstatements that materially affect the financial statements. The standard also requires auditors to verify that appropriate accounting policies are reflected in the opening balances and that they have been consistently applied in the current period's financial statements.

In response, we:

- ▶ Held discussions with your former external auditor in respect of previous significant audit issues, corporate governance and general risk assessment.
- ▶ Reviewed prior year financial statements, annual audit reports and other reports issued by your former external auditor.
- ▶ Substantively tested opening balances to ensure that they agree both to the prior year audited financial statements and closing trial balance.
- ▶ Undertaken a range of testing on balances during 2016/17 which provide assurance on the judgements and estimates made as at 31 March 2016.

We have reported elsewhere on the requirement to undertake restatement of the prior period to correct errors in the valuation of property, plant and equipment. A separate adjustment was also required to correct £6.6 million of developer contributions which were accounted for in current liabilities, instead of being held in an earmarked reserve.

### Other audit matters – what have we concluded?

- ▶ The EFA has been presented in accordance with the Code and the MiRS and CIES restated accordingly. We consider the disclosures provided to be appropriate to the Council's internal reporting during the year.
- ▶ We concluded our work on the opening balances as part of the requirements for initial audit engagements. As reported elsewhere, a number of adjustments to prior period figures were required.

## Other audit matters (continued)

### Group financial statements

In 2015/16, the Council accounted for West Lothian Leisure Ltd and Lothian Valuation Joint Board as associates, due to an assessment of having significant influence but not outright control over these two entities. The Council also identified two joint ventures, West Lothian Recycling Ltd and West Lothian Integration Joint Board (WLIJB). A number of other entities were excluded from consolidation on the grounds of either materiality or lack of significant influence.

In scoping our audit work over the group, only WLIJB was scoped into our audit procedures on the grounds of materiality. We are the appointed auditor to the WLIJB and report separately on our audit of that entity. The accounting for the WLIJB was new in 2016/17. The relationship as a joint venture meant that in the Council CIES, a gross-up of expenditure funding made to WLIJB plus the expenditure on social care services should be shown, offset by the income receivable from WLIJB as part of its delegation of resources. The unaudited financial statements did not account for this correctly, leading to an adjustment in the financial statements.

The overall impact of preparing group financial statements was to reduce total reserves by £2.9 million (2015/16: £0.8 million).

During the year, West Lothian Leisure converted from a registered society to an incorporate company limited by guarantee with the Council as the sole member. An updated assessment of the control arrangements was not conducted by the finance team based on the change in circumstances during the year. We have concurred with management's assessment that there was no material impact on the group financial statements even had a change to the group relationship been made during the year. An unadjusted audit difference with a cumulative value of £3 million has been identified.

From 1 April 2017, the articles of association of West Lothian Leisure were changed again. In addition, the company took on additional leisure and culture assets of the Council. An updated assessment of the group relationship with West Lothian Leisure should be conducted by management in advance of preparation of the 2017/18 financial statements.

**Action plan point - 3**

### Qualitative aspects of the financial statements

With the exception of the matters discussed specifically elsewhere in this report:

- ▶ We have reviewed the significant accounting policies, which are disclosed in the annual financial statements. We consider these to be appropriate to the Council.
- ▶ There was no disagreement during the course of the audit over any accounting treatment or disclosure.
- ▶ There were no significant difficulties encountered in the audit.

## Other audit matters (continued) – what have we concluded?

- ▶ We have obtained reasonable and appropriate audit evidence over the Council's group financial statements. Based on our group scoping we were not required to undertake detailed testing at components of the group. We are the appointed auditor to West Lothian Integration Joint Board.
- ▶ Management should ensure they update their consideration of the group boundary for changes in circumstances at entities with which they have an interest.

## Other audit matters

### Charitable trusts

The Council acts as sole trustee for 40 trusts and mortifications, nine of which are registered charities. The Charities Accounts (Scotland) Regulations 2006 outline the accounting and auditing requirements for charitable bodies. The Regulations require an auditor to prepare a report to the charity trustees where an audit is required by any other enactment. The Council's charitable trust funds are covered by the requirements of section 106 of the Local Government (Scotland) Act 1973 and consequently require a full audit. We have audited the 2016/17 financial statements of the charitable trust funds. In summary:

- ▶ We have provided an unqualified audit opinion on the charitable trust funds financial statements, in accordance with applicable law and the relevant financial reporting framework.
- ▶ There were no audit adjustments impacting on the net assets or income and expenditure reported for the year.
- ▶ No numerical and presentational adjustments were required to the financial statements prepared for audit.
- ▶ We considered and confirmed our independence to act as auditors of the charitable trust funds, in line with the procedures set out in Appendix C for the Council audit, together with the objectivity of the audit partner and staff.
- ▶ Materiality for the audit was set in accordance with our audit methodology, at 2% of total income.
- ▶ We encountered no significant difficulties in undertaking our work and have no other significant matters to report to you.

### Significant trading operations

Under the Local Government in Scotland Act 2003, the Council has to maintain statutory trading accounts for any 'significant trading operations' (STOs). The 2003 Act also prescribes that STOs have to break even over a three year rolling period.

The Council reports one significant trading operation, Economic Development Properties. The cumulative three-year result is a deficit of £4.86 million, resulting in a failure to achieve the statutory financial requirement. During 2015/16 and 2016/17 impairment charges against assets within the property portfolio were £4.48 million and £0.64 million, respectively. These impairment charges represented the reason why the statutory breakeven position was not achieved.

In line with the position reported in the prior year by your former external auditor, without qualifying our audit opinion, we include an Emphasis of Matter paragraph in our audit report explaining the Council's failure to achieve a statutory objective.

## Other audit matters (continued) – what have we concluded?

- ▶ We undertook the audit of nine of the Council's registered charitable trusts. We provided an unqualified audit opinions on the financial statements of the trusts.
- ▶ Without qualifying our audit opinion, we include an Emphasis of Matter paragraph in our audit report due to the Council's failure to achieve a statutory objective in the operation of its statutory trading operation.

The Local Authority Accounts (Scotland) Regulations 2014 set out the statements which should be included in the Annual Report and Accounts in addition to the financial statements. These items are covered by our independent auditor's report as *Other prescribed matters*, in accordance with the requirements of the Code.

## Other reporting requirements

### The Local Authority Accounts (Scotland) Regulations 2014 (the Regulations)

Regulations 8 to 10 set out the statutory requirements on the Council in respect to the Annual Accounts, their availability for public inspection and the consideration and signing by the Council or a committee with an audit or governance remit. As required, we received the unaudited Annual Accounts by the 30 June. The audit committee considered the unaudited Annual Accounts on 30 June 2017, in advance of the 31 August deadline. No statutory objections were received on the unaudited financial statements.

While complying with the regulations, we consider that there is some potential inconsistency in the role and remit of the audit committee in the oversight of the financial statements which management should consider.

**Action plan point – 8**

### Management Commentary

The requirement for the Council to include a management commentary is included in Regulation 8(2)(a). Audit Scotland requires us to read the management commentary and express an opinion on whether the information given is consistent with the financial statements and whether it has been prepared in accordance with the statutory guidance.

Guidance on the content of the management commentary was issued by the Scottish Government within Local Government Finance Circular 5/2015. We considered whether the management commentary provided a fair and balanced review of the Council's business; a description of the principal risks and uncertainties; financial and non-financial key performance indicators; a description of the Council's strategy and business model and the main trends and factors likely to affect future developments; performance and position of the Council's business and explanation of the amounts in the financial statements.

We made suggestions to provide some more detailed and specific analysis within the management commentary. Management updated the commentary appropriately to reflect key elements of our review.

### Remuneration Report

Auditors are required by the Code to audit the disclosures of remuneration and pension benefit, pay bands, and exit packages and express a separate opinion within their independent auditor's report on whether they have been properly prepared in accordance with the Regulations.

No amendments were required to the draft remuneration report to ensure its consistency with underlying records and presentation in accordance with the statutory requirements. The Council has disclosed appropriately exit packages provided to 42 staff totalling £951,000 (2015/16: 46 staff totalling £1.1 million).

### Annual Governance Statement

Audit Scotland requires us to read the information in the annual governance statement and express an opinion on whether the information given in the annual governance statements is consistent with the financial statements and whether the statement has been prepared in accordance with *Delivering good governance in local government: framework 2016*. We set out the work undertaken in respect of the Council's annual governance statement as part of the Wider Scope – Governance & Transparency section of this Report.

## Other reporting requirements – what have we concluded?

- ▶ We have concluded that the Council has complied with the requirements of the Regulations.
- ▶ In respect of our 'Opinions on other prescribed matters', which includes the management commentary, the auditable part of the remuneration report, and the annual governance statement, our opinion is unqualified.
- ▶ We have not identified any other matters on which we are required to report by exception.

## **2. Wider scope audit**



## 2.1 Wider scope – Approach to Best Value



Together the Accounts Commission and the Auditor General for Scotland agreed the four dimensions set out in the Code which comprise the wider scope audit for public sector in Scotland. These are: financial sustainability, financial management, governance and transparency, and value for money.

### Wider scope audit

Our wider scope audit work, and the judgements and conclusions reached in these areas, contribute to the overall assessment and assurance on the achievement of Best Value. As your external auditor we also participate in the Local Area Network (LAN). The LAN brings together representatives from across different scrutiny bodies to agree a Shared Risk Assessment (SRA) for each local authority. The SRA informs the local scrutiny plan (LSP) ensuring that for any risks identified there is an appropriate scrutiny response.

The 2016/17 LSP reported that the LAN were of the view that the Council demonstrates its commitment to best value, with evidence of strong leadership, a clear vision and a focus on continuous improvement. The LAN did not identify any specific areas from the risk assessment where scrutiny was required. The 2017/18 LSP confirmed this position and taken together formed a context for our audit and risk assessment.

### Best Value auditing

Under the new approach to Best Value auditing in local government, the Controller of Audit will provide a Best Value Assurance Report (BVAR) for each council at least once in a five year period. The Council was selected as one of six councils to be subject to a BVAR report in the first year of the new arrangements. Joint work has been undertaken by ourselves and members of Audit Scotland's Performance Audit and Best Value team. The finalised BVAR will be heard by the Accounts Commission in November 2017.

The annual audit continues to focus on aspects of Best Value over our five year appointment. We have identified an indicative five year Best Value Plan in the table below. This will be subject to ongoing revision as priorities change or emerging risks arise.

The Accounts Commission has published its strategic audit priorities and these are mapped across, at a high level, to the Best Value audit work planned as shown below.

- The clarity of council priorities and quality of long-term planning to achieve these.
- How effectively councils evaluate and implement options for significant changes in delivering services.
- How effectively councils are ensuring members and officers have the right knowledge, skills and time to lead and manage delivery of the council priorities.
- How effectively councils are involving citizens in decisions about services.
- The quality of council public performance reporting to help citizens gauge improvement.

Indicative five year Best Value plan	2016/17	2017/18	2018/19	2019/20	2020/21	Mapping to Strategic Audit Priority
<b>Planned BVAR</b>	X					
<b>Follow up of BVAR</b>		X				
<b>Audit coverage:</b>						
Performance and outcomes		X				<b>B</b>
Improvement		X				-
Leadership, Governance and Scrutiny			X			<b>A</b>
Equal Opportunities			X			<b>E</b>
Partnership Working and Empowering Communities				X		<b>C, D</b>
Financial and service planning					X	<b>A, C</b>
Financial governance and resource management				X		-

## 2.2 Financial management

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

### Financial management

In undertaking our work on this audit dimension, at a high level we consider the following aspects:

- ▶ Is financial management effective?
- ▶ Are the budget setting and monitoring processes operating effectively?
- ▶ Is there sufficient financial capacity?

### 2016/17 financial outcomes

The 2016/17 Comprehensive Income and Expenditure Statement (CIES) shows that the Council incurred gross expenditure on the provision of services of £754.2 million (2015/16: £702.2 million), and incurred an accounting deficit of £95.2million (2015/16: £105.9 million) on those services.

The new Expenditure and Funding Analysis (EFA) note to the financial statements provides an explanation of how this expenditure is used and funded by the Council. This is different from the accounting position shown in the CIES in accordance with the Code and, together with the Movement in Reserves Statement, demonstrates how the Council's statutory reserves, including the General Fund, have changed in the year.

As shown in the EFA, the outturn for the financial year against the Council's general fund was a deficit of £0.35 million (2015/16: £0.26 million). In February 2016, the Council approved its 2016/17 revenue budget and provisionally approved its 2017/18 budget. Included within the budget for 2016/17 were budget reduction measures of £11.2 million to deliver a balanced budget. These were delivered.

Key financial statements movements and balances are considered below.

Focus on financial statements results	2016/17 £000	Restated 2015/16 £000	Commentary	RAG rating
(Surplus) / deficit on provision of services	95,215	105,892	The primary factor in the reduced deficit was the significant depreciation charged to the Housing Revenue Account in 2015/16 on revaluation of council dwellings.	G
(Surplus) / deficit on General Fund and HRA	347	260	No significant change. In general this result reflects on good in-year financial management and budgetary control	G
Uncommitted general fund	2,075	2,070	This equates to 0.5% of budgeted net expenditure and is one of the lowest levels held of any local authority in Scotland. This needs to be kept under close review.	R
Earmarked reserves	23,187	23,539	Earmarked reserves have broadly been maintained at the same level and provide the Council with flexibility around key initiatives.	G
Net current liabilities	(245)	(12,542)	Net current liabilities can reflect a potential inability to meet liabilities as they fall due. In practice, good cash flow management will ensure that this is not a risk.	A
Total Usable Reserves	103,550	128,464	Most of the reduction is due to utilisation of the capital fund in supporting the Council's investment in assets. However there are significant usable reserves available.	G
Total Unusable Reserves	803,687	979,422	Revaluation of operational land and buildings / Council's asset base remains strong.	G
Net (decrease) / increase in cash	(12,718)	2,561	The decrease in cash reflects the significant investment the Council is currently making in its assets and in line with plan.	G

### 2016/17 budget monitoring and outturn

A balanced budget was set for 2016/17. The projected outturn against budget was reported regularly to the Council Executive during the year. The outturn report in June 2017 which supported the preparation of the unaudited financial statements is summarised in the table.

Service area	Budget £000	Outturn £000	Over / (under) £000
Schools, Education Support	207,730	207,370	(360)
Planning, Economic Development and Regeneration	6,999	5,263	(1,736)
Operational Services	68,160	68,160	-
Housing, Customer and Building	10,796	11,456	660
Corporate Services	17,609	17,609	-
IJB – Adults and Elderly Services	60,584	60,584	-
Non-IJB – Children's Services	30,010	30,100	90
Chief Executive, Finance and Property	32,632	32,167	(465)
Joint Boards	1,214	1,214	-
<b>Service Expenditure - Total</b>	<b>435,734</b>	<b>433,923</b>	<b>(1,811)</b>

The significant variance item giving rise to the underspend was reported as due to receipt in March 2017 of additional funding of £1.74 million for investment linked to employability and economic regeneration. This has been earmarked for spend in 2017/18. The key overspend in Housing, Customer and Building Services related to homelessness.

In-year budget monitoring reports were provided to the Council Executive on a regular basis, which included forecast outturn. There were no major fluctuations in the outturn projections provided to members during the year, demonstrating good financial control and an understanding of the budget and in-year management of financial pressures. Action to address service pressures were included in monitoring reports, enabling members to have appropriate oversight.

#### *Reporting on budget reduction measures*

Monitoring reports also included in-year analysis against the budget reduction measures. For 2016/17, these totalled £11.2 million and reports included red, amber, green assessment of their achievement. By Period 6, £9.4 million (78%) had been assessed as green with the remainder as amber. This included £2.1 million of staff performance savings, to be met through management of staffing vacancies during the year.

As the budget approved in February 2016 also included indicative figures for 2017/18. At mid-year in 2016/17 management were able to report that 59% of the £8.4 million reduction measures were already green with the remainder amber. This results in a position whereby at the time of the budget approval for 2017/18, the majority of savings are all identified and understood and so can deliver full in-year savings.

#### **Action plan point - 4**

#### **Housing Revenue Account**

The HRA delivered break-even performance in the year. There were no significant movements in any of rent arrears, losses on void properties or the bad debt provision from the prior year.

### 2016/17 financial outcomes – capital expenditure

Capital expenditure	Budget £000	Outturn £000	Over / (under) £000
<b>General services capital programme</b>	<b>63,304</b>	<b>69,616</b>	<b>6,312</b>
In line with prior year, the Council delivered accelerated spend on its general services capital programme. Compared with our experience elsewhere, where slippage on capital programmes can be a regular occurrence this demonstrates appropriate management of capital projects and ability to accelerate spend where circumstances allow.			
<b>Housing capital programme</b>	<b>62,450</b>	<b>49,787</b>	<b>(12,663)</b>
The housing programme under-delivered against the plan, due primarily on slippage due to the 1,000 Houses New Build programme. This accounted for slippage of £17 million against budget, although £27 million of expenditure was still invested in this programme during the year.			

Overall financing of the capital programme was supported by £67.1 million of capital receipts, grants from government and contributions from third parties and/or existing capital funds; £9.3 million of capital expenditure funded by revenue with the remaining £42.9 million funded by borrowing.

#### Capacity of finance and standing in the organisation

The Council's section 95 officer is the head of finance and property services. We considered the role and status of the section 95 officer and are satisfied that the Council adheres to the principles laid out within CIPFA's *Statement on the role of the Chief Financial Officer in Local Government*.

We have reviewed the Council's financial regulations and are satisfied that these are comprehensive and subject to regular update. They are available through the Council's website.

#### Internal control

It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

As part of our audit of the financial statements, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Our first year audit has been predominantly substantive in nature, and therefore we have not tested the operation of key controls.

Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control. We have not identified any such matters to report to you.

#### Financial management – what have we concluded?

- ▶ We have concluded that the Council has generally sound financial management arrangements. This has been based on identification and overall tracking of budget savings well in advance as part of two-year indicative annual budget setting.
- ▶ The Council is going through a period of significant capital investment, both in general fund services and council housing. While there has been some delay in the new build housing programme, there is good evidence of delivery and management of projects.

Financial sustainability interprets auditors' requirements under ISA 570 *Going concern* and looks forward to the medium (two to five years) and longer term (longer than five years) to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

### Financial sustainability

The Accounts Commission's overview report on Local Government in Scotland: Performance and Challenges 2017 sets out the increasingly demanding environment facing local authorities. In particular an overall reduction of 9.2% in Scottish Government total revenue funding since 2010/11 and demographic changes in particular in respect of aging populations. Additionally, there are a broad range of legislative and policy changes, including for example integration of health and social care, community empowerment provision and education reform.

Scottish Government funding is distributed to councils using a formula based on factors such as population, deprivation and rurality. This means that not all councils have experienced the same level of reductions in funding. Audit Scotland figures show that the Council's reduction in funding overall has been the lowest of all councils, at less than 5%. This is in the context, however, of a demographic which also shows that the Council is expected to experience the most significant increase in population over 75 years old, by over 120% in the period 2014 to 2039.

Education and social work increasingly make up a greater majority of expenditure in local government. Within the Expenditure and Funding Analysis, in terms of the amount chargeable to the general fund and HRA, 67% of spend was in respect of these areas, within a range nationally of 60 – 80%.

### Level of reserves

As shown in the table below, the Council's level of usable revenue reserves as a percentage of net expenditure on cost of services has decreased over the last five years. While reserves are broadly at a similar level, the overall net expenditure of the Council has increased. Within earmarked reserves, the Council's modernisation fund has been assisting in funding potential termination costs for staff, as service delivery has been modernised.

Analysis of reserves	2012/13 £000	2013/14 £000	2014/15 £000	2015/16 £000	2016/17 £000	%age change
Earmarked general fund	23,212	20,571	23,869*	23,539*	23,187	(28)
Uncommitted general fund	2,000	2,000	2,000	2,070	2,075	4
HRA fund	926	926	926	926	926	-
Insurance fund	12,269	12,193	13,570	13,715	11,835	(4)
<b>Total Usable Revenue Reserves</b>	<b>38,407</b>	<b>35,690</b>	<b>40,365*</b>	<b>40,250*</b>	<b>38,023</b>	<b>(1)</b>
<b>As a % of net expenditure on cost of services</b>	<b>9.9%</b>	<b>9.1%</b>	<b>10.4%</b>	<b>8.5%</b>	<b>8.2%</b>	
Capital fund	74,338	79,008	84,765	88,214	65,527	(12)
<b>Total Usable Reserves</b>	<b>112,745</b>	<b>114,698</b>	<b>125,130*</b>	<b>128,464*</b>	<b>103,550</b>	<b>(14)</b>

\* Restated following prior year adjustment processed in 2016/17

The Council has maintained an uncommitted general fund balance at around £2 million, representing approximately 0.5% of net expenditure. This remains one of the lowest balances of all local authorities in Scotland and while the use of earmarked balances should also be considered when reviewing the available flexibility to the Council in making budget decisions, we believe this level of uncommitted reserves represents a risk to the Council.

### Action plan point - 5

The significant capital fund means that reserves in total for the Council are strong. A significant proportion of this fund has been allocated, and is being utilised, to support the significant capital investment currently being made by the Council in both housing and general fund services, thus reducing the amount of additional borrowing required at this time.

### Forward financial planning

The Accounts Commission has stressed the need for long-term financial strategies, supported by medium-term financial planning, to provide councils with the ability to respond to the acknowledged demographic and fiscal pressures. The Council has traditionally aligned its financial strategy with its corporate plan, which was approved for 2012-17 in line with the timing of local elections. There is strong evidence of delivery of this financial strategy over the last five years, drawing on major public consultation exercises in 2012 and 2014.

During this period, the Council set multi-year indicative budgets, for example in January 2015 for the three year period 2015/16 to 2017/18 i.e. including the current financial year. This represents good practice. In January 2016 and January 2017 this was reduced to two-year and then just a one-year budget.

In February 2017, the Council approved the process to prepare a priority based revenue financial plan for 2018/19 to 2022/23 and to set out how the Corporate Plan priorities will be delivered over this period.

In setting the 2017/18 budget, the Council received an overview of the challenging economic outlook over the next five years. However, no detailed financial information was provided to members outlining the likely profile of the medium-term financial position. To our knowledge, this puts the Council in a minority of local authorities by not providing such information to members in advance of what was known to be a highly challenging period. The 2017/18 budget committed £2.179 million of non-recurring resources to meet the budget.

As part of the 2017/18 budget process, members agreed to the development of a financial and corporate plan for the period 2018/19 to 2022/23.

#### **Action plan point - 6**

In June 2017, management submitted a Revenue Budget Strategy 2018/19 to 2022/23 to the new Council Executive outlining the forecast budget gaps for the period.

Forecast budget gaps	2018/19 £m	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	Total £m
Gross expenditure	17.5	16.4	16.8	15.3	15.7	81.7
Gross Income	2.5	0.4	(7.0)	(5.9)	(6.0)	(16.0)
<b>Forecast Budget Gap</b>	<b>20.0</b>	<b>16.8</b>	<b>9.8</b>	<b>9.4</b>	<b>9.7</b>	<b>65.7</b>

Expenditure pressures on staffing comprised £19.8 million of the forecasts, based on a 1.25% pay rise assumption in the first two years and 1% thereafter. This is a key assumption and the paper notes that a 0.5% increase on this assumption would add a further £6 million in cost pressures. Given recent public announcements by the Scottish Government, in our view it is likely that will be a need to revisit these assumptions.

Demographic and demand led pressures account for £28.4 million, or 35% of the expenditure budget pressures. This is heavily weighted to social care costs, and the Council's demographic of an increasing elderly population.

Income assumptions are based on a 3% annual Council tax increase which, coupled with the house building programme in the area, results in the majority of the increase in gross income. The Local Government finance settlement is assumed to show further reductions in 2018/19 and 2019/20, before increasing again thereafter. Taken together, this results in the front loading of the budget gap, with 56% of savings in the first two years.

### Closing the gap

Following consideration of the Revenue Budget Strategy 2018/19 to 2022/23 report, in line with the officer recommendations in the report, Council Executive agreed that officers should report back to them in late summer / early autumn on proposals for a public consultation, including proposed priorities, future spending plans and savings options, and proposed council tax levels.

The Corporate Management Team has been working through officer savings proposals to meet the forecast budget gaps. In September 2017, the Council Executive considered an update from officers which set out a revised estimated budget gap of £66.1 million. This report set out the public consultation details as follows:

- ▶ Priorities for the next five years, drawing on the existing eight priorities of the Corporate Plan 2012/17 to ask respondents to comment on their ongoing suitability for West Lothian and again asking respondents to rank the priorities in order of importance.
- ▶ Seek views on the outline officer proposals for reductions and / or changes to services provided by the Council in seeking to balance the Council's financial position over the next five years.
- ▶ Seek views on the annual Council Tax increase of 3% which had been assumed in the budget model.

The consultation period will run from 16 October to 12 November 2017, with officers reporting on the results of the consultation to the relevant Policy Development and Scrutiny Panels for consideration in December 2017.

The development of the Council's new five year corporate plan and supporting corporate strategies, including the financial strategy resulting from the public consultation and subsequent consideration by members, are due to be approved in February 2018.

At the current time, therefore, the budget proposals are not public although we understand that management categorises these by prioritisation savings and efficiency savings, essentially considering how savings can be made in what the Council does, and secondly by how it does it. The required savings are expected to be found by an approximate 50:50 split between these two aspects.

Overall, we have assessed that the Council fully recognises the need for medium-term financial planning, linked to delivery of the corporate plan priorities. However, members have not yet been involved in determining the proposed areas of transformation and targeted savings. These are expected to include difficult decisions and so in our view this could leave the delivery of savings in the required timescales at risk.

***Action plan point - 7***

### Long-term capital programme

2017/18 represented the final year of the current capital programmes for both general and housing services.

Capital investment of £49.8 million on general fund services was approved in the budget although £21.9 million of investment already committed in 2018/19 and beyond was highlighted. By completion of the financial year 2017/18, this will bring £257 million of investment over the previous five years.

The Council is in the process of developing a 10-year capital plan to be approved along with the next round of the Corporate Plan and underpinning strategies. This will be phased for years 1-5 individually and then years 6-10 as one phase.

The Accounts Commission's 2015/16 financial overview report provided comparison levels of borrowing across councils. While the Council has a relatively high level of borrowing, in terms of affordability, it was the 11<sup>th</sup> lowest in terms of percentage of income used to service debt. The Council has accelerated elements of borrowing to fund the 2017/18 programme as interest rates continue to be low, leaving more of the Capital Fund available to fund the longer-term programme.

A housing capital budget of £77.2 million was approved for 2017/18, comprising £60.7 million on the new build housing programme and £16.5 million on other works including planned refurbishments. This is an ambitious programme, and reflects partly the under-delivery in the new build programme to date.

Funding of the housing capital programme is predominantly through borrowing of £53.5 million, with right to buy sales generating £5.6 million through completion of final sales before the legislative change which brought an end to tenants' right to buy. The retention of council housing will significantly impact on HRA rental income in the future, supporting the increased borrowing levels.

### Other long-term liabilities

#### *Retirement benefits*

We reported earlier on the significant increase in the liability assessed at the balance sheet in respect of the Council's obligations for pensions. Individual council obligations, and their corresponding affordability, reflects on a number of factors:

- ▶ performance of the pension funds of which they are members
- ▶ assumptions made by actuaries of the various funds
- ▶ the maturity of the council's membership (average age of pension scheme members)
- ▶ decisions made by councils to award discretionary benefits to staff retiring early.

In the Accounts Commission's 2015/16 financial overview report, at approximately 40%, the Council had the sixth lowest ratio of pension liability to net revenue. While this ratio has increased substantially to closer to 79%, similar movements will have affected all councils and so this remains one of the lower percentages.

#### *PPP liabilities*

The Council has two PPP contracts for schools, both over 31-year periods, one of which expires in 2032 and the second in 2039. The outstanding principal on these contracts totals £65.5 million at 31 March 2017. In line with other long-term leasing obligations, the Council also makes annual payments in respect of interest, lifecycle capital costs and operating costs.

### Integration of Health and Social Care

The Public Bodies (Joint Working) (Scotland) Act 2014 established the legal framework for integrating health and social care in Scotland. The West Lothian Integration Joint Board (the WLIJB) was legally established on 21 September 2015 and from 1 April 2016 took on the relevant functions and resources delegated to it from both the Council and NHS Lothian. The Council committed £60.6 million of expenditure to the WLIJB in 2016/17 and received direction from the WLIJB in respect of use of these resources in the year. The Council's 2017/18 budget approved resource of £69.4 million, representing the growth in resources required in this area.

### Edinburgh and South East Scotland City Region Deal

The Council is one of six local authorities within the Edinburgh and South East Scotland City Region Deal. The City Region Deal was approved in July 2017, with commitment from the Scottish and UK Governments to provide significant investment, along with additional investment from the councils as well as universities within the region. This provides opportunity for the Council to work with its partners to use this investment to improve economic performance in the region, deliver services more effectively and tackle inequality and deprivation.

### Financial sustainability – what have we concluded?

- ▶ We have concluded that the Council's financial position is generally sound. While significant investment is required in response to demographic pressures, it has a good basis to undertake this investment.
- ▶ The Council has an established process for aligning its financial strategy to its corporate plan priorities. As a result only a one-year budget was approved for 2017/18, as this was the final year of the existing five year corporate plan. The Policy Development and Scrutiny Panels will consider the results of the public consultation in respect of officers' savings proposals in December 2017, prior to Council approval of a new five year corporate plan and underlying financial strategy in February 2018. In our view, since difficult decisions are expected to be required, the timeline for involvement of members could leave the delivery of savings in the required timescales at risk.



Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information.

### Governance arrangements

During our audit, and in conjunction with the BVAR work, we have reviewed the Council's overall governance arrangements. In line with responsibilities of the Council, this has considered the Council's arrangements as they relate to standards of conduct including for the prevention and detection of fraud and error.

The Council has a set of Standing Orders which regulate the way it goes about its business, supported by the Scheme of Administration which sets out the membership, powers and responsibilities for full council, all its committees, sub-committees, working groups, Policy Development and Scrutiny Panels and Local Area committees. The Financial Regulations contain the Council's arrangements for the proper administration of its financial affairs. In line with good practice, all documents are kept up to date to reflect changes.

The full Council of 33 Members meets approximately every six weeks, with most of the Council's important decisions and policies made by the Council Executive or the Education Executive. The Council Executive meets twice between meetings of full Council, and the Education Executive once.

During 2016/17, the Council was led by a minority Labour administration. Following the May 2017 elections, which returned 13 Scottish National Party, 12 Scottish Labour Party, seven Scottish Conservative and Unionist and one Independent members of Council. The remains a minority Labour administration.

### Member training

The Council offers training to elected members through the year, and make available on its website details of the 19 events hosted during 2016/17 and the number of members who attended this. The content of training was broad and covered a range of subject matters corresponding to the breadth of responsibilities held by elected members.

Following the May 2017 elections, induction training was provided for new and returning members. Discussions with members as part of the ongoing Best Value work found that members were positive about the nature and extent of training provided.

We understand that Human Resources are in the process of developing and progressing individual training plans for members and records of training undertaken. While senior officers respond to and provide informal briefings to members when they have queries, given the increasing challenges facing local government, we would encourage individual tailored plans to be developed for elected members to support them in discharging their roles in ensuring Best Value in provision of services at the Council over the coming term in office.

### Annual Governance Statement (AGS)

The AGS sets out the Council's governance framework. The Council supports its arrangements through its local code of corporate governance, and assessments are undertaken regularly of compliance against this. Other core support for the AGS is through the system of compliance statements which are obtained from key individuals in the Council's management team, relating to their areas of responsibility.

The annual report from the Audit, Risk and Counter Fraud Manager is a further source of support for the AGS. This report concluded "*that the council's framework of governance, risk management and control is generally sound.*" We observed that of the 19 reviews for which an audit conclusion was provided, two obtained an '*unsound*' conclusion and nine '*required improvement*'. With over half of the reviews receiving one of the bottom two gradings produced by internal audit; we considered whether the overall support for the AGS was appropriate. We judged that since areas requiring improvement were included within the AGS then there was appropriate transparency and disclosure of the underlying control framework. The Audit, Risk and Counter Fraud Manager has further advised that in reaching his conclusion, he considers other sources of assurance than that of the individual audit reviews.

### Focus on Audit and Governance and Risk Committee arrangements

Prior to the local elections in May 2017, the audit and governance committee had primary responsibility for matters relating to internal and external audit, and the governance arrangements of the Council. During 2016/17 this committee continued to be chaired by a member of the administration, which as also reported by the Council's former auditor, does not accord with our own, or the Accounts Commission's, views on best practice for independence of audit committee chairs.

The main change to the Council's committee structure following the elections was to split the remit of the audit and governance committee into two, replacing it with an audit committee and a governance and risk committee. Both of these committees have a membership of five (two Labour, two Conservative and 1 SNP), with in addition one lay member currently appointed to the audit committee, and a lay member due to be appointed to the governance and risk committee. At the current time, three of the five members of each committee are the same, while the SNP members are not taking up their one position on each committee.

The remits of the two new committees contain some significant overlap, for example in June 2017 both committees considered the Internal Audit Annual Report. There are a number of occasions where it is likely that the same reports from officers may need to be considered by both committees in order to fully discharge their responsibilities.

Management have explained that the reason for the split is to allow members to have a greater focus in particular on risk within the Council. We agree with this principle as there has been limited consideration or review of the corporate risk register at any committee of the Council during the year, as this was performed at the Governance & Risk Board during the year.

While the chairs of both new committees are not currently members of the minority administration, best practice would suggest formalising the arrangement within the Scheme of Administration such that the chair, or vice-chair, of these important committees should not be drawn from the administration.

Given the new arrangements, and the potential overlap in remit, we believe it will be important for officers and members to keep the operation of the committees under review during their first cycles of operation.

**Action plan point - 8**

### Focus on performance and scrutiny arrangements

The scrutiny of performance by members is carried out in different places in the decision-making structure. There are two committees, Performance committee and Education (Quality Assurance) committee (EQAC) and nine Policy Development and Scrutiny Panels (PDSPs).

The Council operates a series of PDSPs. These are small groups of councillors (four Labour administration, three opposition) and up to six invited third party representatives, who develop new policies for the Council, or scrutinise the workings of existing policies to consider where changes are needed. They do not have the power to actually make decisions, but they make recommendations to the Council Executive or Education Executive for them to make decisions which are binding on the Council.

Since they report through either the Council Executive or the Education Executive, the current membership of the PDSPs is such that most have a majority of elected members who are also members of either executive committee.

The PDSPs therefore play an important role in the development and scrutiny of policy decisions. In undertaking this role, in accordance with the Scheme of Administration their remit also includes the review of periodic service performance reports. This enables them to make recommendations to officers for improvements or actions to be taken.

This is an important part of the scrutiny of policy, although in our view we do not consider this alone would represent sufficient scrutiny of service performance by elected members.

The main committees in the structure for consideration of performance are the Performance committee, and for education services, the EQAC.

The Performance committee comprises five members. In practice, it has been and is currently chaired by a non-administration member, although the Scheme of Administration does not require this, nor does it set out whether members of the Executive(s) may or may not be on the committee. According to its remit, the purpose of the committee is consideration of the Council's corporate performance, including ensuring that performance management arrangements cover Best Value considerations.

The EQAC has since its inception been chaired by a non-administration member. Its membership includes religious and parent members and parent council representatives are invited to attend for each school under review. It considers reports from external and internal school inspections and reviews and the action plans that have been developed in response. There is evidence of member involvement in scrutiny and a willingness to follow up reports at future meetings to monitor progress. Of its 13 elected member representation, 11 of these members are also on the Education Executive.

In our view, there is scope to review and potentially enhance the arrangements in the Scheme of Administration for review of performance within the committee structure, to ensure that this provides for sufficient involvement from elected members drawn from outside the decision-making committees of the Council.

#### **Action plan point – 9**

The Performance committee sets a work-plan for the year and receives an annual report on the Council's performance within the Local Government Benchmarking Framework. From our review of committee business, there has tended to be more focus on service performance reports than overall corporate performance reporting. Further, from our review of minutes there is limited evidence of challenge and oversight of corporate performance of the Council, as the minutes often record that members noted the content of reports without recording any challenge or scrutiny which may have occurred.

Robust challenge and involvement from elected members in driving improvement of Council performance at a corporate level is a key element of a commitment to delivering Best Value.

#### **Action plan point – 10**

### Focus on Internal Audit

The Council has an in-house internal audit function which is designed to provide members and management of the Council with independent assurance on risk management, internal control and corporate governance processes. As part of our first year appointment, we considered aspects of internal audit's performance with relevance to their compliance with Public Sector Internal Audit Standards (PSIAS). Our work in this area was assisted by Internal Audit's own self-assessment against PSIAS, and an independent peer review of this self-assessment by the Chief Internal Auditor from Moray Council. Broad compliance with the PSIAS was noted.

Overall, the Council's Internal Audit team demonstrates a number of areas of good practice, including clear access and reporting to the leadership team and the audit committee. Review of internal audit reports and observation of audit committee meetings evidenced that management is subject to challenge.

The Audit, Risk and Counter-Fraud section consists of 7 FTE of skilled and experienced personnel, with access to more specialised IT technology support through its partnership relationship with Falkirk Council. The internal audit complement is 3 FTE. The relatively small size of the team, which is reflected in the cost of the function being benchmarked as the second lowest in Scotland, increases the inherent risk around the dependency and reliance on key individuals within the team. Our review of Internal Audit working papers found that while there was a structured quality review process, there were opportunities to enhance aspects of assignment working paper review and sign-off to be aligned with good practice which we have discussed with management.

The PSIAS assessment identified that planned audit reviews are not prioritised in the internal audit plan for the year. The Audit, Risk and Counter Fraud Manager provided the mitigation that this is due to the intention to complete the annual internal audit plan each year, giving every review the same high priority. We have observed that experience shows that this is not the case, with reviews being rescheduled into future years or removed from the plan as other pressures on resource arise.

#### **Action plan point - 11**

In line with the Council's performance management framework, Internal Audit reports against a series of performance indicators. Notable is the highly positive feedback which is consistently received from services which have been subject to audit. However, in our view, there is scope to improve the indicators identified and / or the targets for assessment of performance. For example, the 12-week target as the average time to issue draft reports on completion of assignments is not sufficiently challenging and provides a risk that control weaknesses can continue un-addressed while draft reports are being prepared. Management have advised that in practice, any significant risk or issue would be escalated out with formal reporting cycles.

#### **Action plan point – 12**

### Focus on Internal Audit's role in the organisation

The Audit, Risk and Counter Fraud Manager fulfils a role both as Head of Internal Audit and also Risk Manager. The risk associated with internal audit self-review is mitigated by management ensuring that audit of the Council's risk management process is conducted independently from the in-house internal audit team. Nonetheless, our view is that this combined Risk Manager and Head of Internal Audit role creates a potential conflict of interest.

The delivery of the Council's new corporate plan is likely to bring a period of significant change as the Council works to deliver and enhance services for users, while responding to changing demographics and ongoing budgetary and funding constraints. In our view, at such times, a Risk Manager should be utilising their specialist risk experience and knowledge to provide advice and support to management across the Council in identifying and managing risks, supporting effective internal control, the risk management framework and overall good governance. This allows Internal Audit to be free from any actual or perceived conflict of interest to challenge and scrutinise management on delivery of transformation of Council working practices.

#### **Action plan point - 13**

### Following the public pound

Auditors are required to consider the Council's arrangements for compliance with the Code of Guidance on Funding External Bodies and Following the Public Pound (the FtPP Code). The audit and governance committee received and considered the Accounts Commission's report "*Roles and working relationships in councils - Are you still getting it right?*" Part of this report considered the relationship of working with Arms Length External Organisations (ALEOs). The committee agreed that the contents of the report would be progressed through the Governance and Risk Board and a further report considered if any recommendations arose from that consideration.

Internal audit undertook a review of the monitoring processes in respect of grants to voluntary and not-for-profit organisations. At the time of the review, this covered payments totalling £22.8 million during 2015/16 of which approximately £20.3 million were related to social policy and £2.5 million to other areas. Internal audit concluded that controls were effective where grants were made in respect of social policy, although it highlighted that there was a risk of a lack of effective oversight by members as required information on contract performance had not been properly reported to the Social Policy PDSP.

In respect of funding of other areas, controls were found to be unsound with four 'high' graded recommendations and four 'medium' graded recommendations made by internal audit.

### Focus on West Lothian Leisure

The Council has an interest in one ALEO, West Lothian Leisure Limited (WLL). West Lothian Leisure was established in 1998 but during 2016 converted, from a registered society, to a company limited by guarantee with the council as the sole member. The Council provides a management fee, which for 2016/17 amounted to £1.9 million, being approximately 20% of WLL's income. From 1 April 2017, additional leisure and cultural services were transferred from the Council to WLL.

One consequence of using more complex structures involving ALEOs in delivering services is that the public may be less clear about who is responsible for services. Maintaining transparency by having arrangements that are easy for people to get access to and understand is a key objective of good governance. This is detailed in the Accounts Commission's *How councils work: Arm's-length external organisations (ALEOs): are you getting it right?* 2011 report.

It is good practice that councils should monitor how ALEOs perform against both financial and service expectations. Internal audit undertook a review of financial monitoring and reporting in relation to WLL and concluded that the control framework required improvement. A number of recommendations were made in respect of improving the governance and control environment, which were accepted and management have advised that these have been implemented.

The West Lothian Leisure Advisory Committee is the committee responsible for oversight of the Council's relationship with WLL. As a result of the internal audit report, financial and performance reporting was separated into different reports. However, all papers considered by this committee have up until now been done so in private.

During 2016/17 three members of the advisory committee were also directors of WLL. The Accounts Commission's 2011 report identifies that such roles are incompatible or pose a real risk to governance and accountability, stating that "*the councillor or officer who scrutinises an ALEO on behalf of the council, or makes funding decisions affecting an ALEO, should not be a board member of the ALEO.*"

On 28 February 2017, the Council Executive was given explicit advice about appointment of members to ALEOs based on Standards Commission advice. Since the May elections, no member on the advisory committee is also a director of WLL. However, the Council Scheme of Administration does not set out that this should not occur. In addition to the actions identified by internal audit, therefore, the Council should review its governance arrangements to ensure they provide for a relationship with WLL that is clear and complies with best practice and relevant guidance, thus reducing the risk of conflicts of interest arising.

**Action plan point – 14**

### Fraud and irregularity

In line with our responsibilities under the Code, we have considered the Council's high level arrangements as they relate to the prevention and detection of fraud and error. Overall we consider the Council's arrangements to be appropriate.

#### *National Fraud Initiative*

The National Fraud Initiative (NFI) is a counter-fraud exercise co-ordinated by Audit Scotland working together with a range of Scottish public bodies, external auditors and overseen by the Cabinet Office for the UK as a whole to identify fraud and error. These exercises are undertaken every two years as part of the statutory audit of the participating bodies. Local authorities were required to submit datasets in autumn 2016 and matches for investigation and follow-up were released early in 2017.

We reviewed the Council's arrangements for participation in the NFI in support of preparation of a return to Audit Scotland. We were satisfied that the Council had appropriate arrangements to respond to the NFI and had initiated their response to the most recent exercise.

### Standards of conduct

Through consideration of the Council's financial regulations, standing orders and scheme of administration, supplemented by consideration of the Code of Conduct for elected members, we are satisfied that the Council has established appropriate arrangements. The Standards Commission for Scotland did consider two cases in respect of councillors during the period and in both cases found against them for relatively minor breaches in respect of disclosure of interests.

### Governance and transparency – what have we concluded?

- ▶ The Council has a comprehensive framework of governance arrangements and shows clear commitment to the core principles. Internal audit is well respected, however, we have raised a number of recommendations for consideration to strengthen the reporting and monitoring by the audit committee.
- ▶ We consider there is scope to strengthen the arrangements for scrutiny of corporate and service performance. The relationship between the new governance & risk and audit committees should be monitored. The Council needs to improve the controls and governance arrangements around Following the Public Pound.

Value for money is concerned with using resources effectively and continually improving services. This includes consideration of whether resources are being used effectively; services are improving and the Council has appropriate arrangements to demonstrate Best Value.

### Performance and improvement

#### *Framework for improvement*

The Council uses the Covalent performance management software as their central performance management system. Covalent supports management and reporting of performance and includes functionality for setting and reviewing targets and thresholds to trigger intervention or action from the service.

The Council has an improvement strategy which guides how continuous improvement is pursued throughout the organisation. The strategy is well rounded in that it considers the different stages of the improvement cycle, from engagement, to planning, performance management and self-assessment. Services carry out self-assessment of their performance through the West Lothian Assessment Model (WLAM). There are two elements to the WLAM, looking at what has been done (enablers) and what has been achieved (results).

Information on the enablers is provided by the service's assessment team. Results information is lifted from the relevant performance indicators on the Covalent system by the Council's Performance and Improvement Service and analysed jointly along with the assessment team. These performance indicators are related to both processes and activities. A final score is then agreed based on both parts of the assessment.

WLAM cycles run for three years, with each WLAM unit required to carry out one assessment per cycle with the aim of achieving continuous improvement. Assessments are presented to a WLAM Review Panel, which is made up of the Chief Executive and two other senior managers (not from the service subject to review). The Review Panel is set up to provide high level scrutiny and peer review, and ensure a consistent approach to self-assessment.

The Council produced an end of programme report for the WLAM cycle 2014-17. This showed that the average score across the Council had improved from the previous cycle and all services (where comparable information was available) had improved performance in their assessment. The Council did acknowledge that the pace of improvement varied between services and that some services could benefit from swiftly addressing the recommendations from their Review Panel.

The Council is currently considering the refresh of the WLAM programme for 2017-20.

#### **Statutory performance indicators**

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. The 2015 Direction set out a streamlined and more flexible set of performance information for the 2016/17 financial year that the Commission required councils to collect and report in public. Councils are required to publish the required information from the financial year ended 31 March 2017 each year through to the financial year ending 31 March 2019. The schedule within the 2015 Direction sets out the required information as:

##### *Achievement of Best Value*

SP 1: Each council will report a range of information setting out its performance in:

- ▶ improving local public services (including with partners)
- ▶ improving local outcomes (including with partners)
- ▶ engaging with communities and service users, and responding to their views and concerns
- ▶ achieving Best Value, including its use of performance benchmarking; options appraisal; and use of resources

##### *Local Government Benchmarking Framework*

SP 2: Each council will report its performance in accordance with the requirements of the Local Government Benchmarking Framework (LGBF)

### Performance and improvement (continued)

The Council utilises four categories of performance indicator in its performance management framework:

- ▶ Public Performance Reporting (PPR): A small number of key indicators – linked to the key processes / activities and / or outcomes that are reported externally, for example to meet the Accounts Commission's requirements.
- ▶ High Level: Key indicators – linked to the key processes / activities and / or outcomes that are reported to senior officers and elected members.
- ▶ WLAM: Indicators of local service performance – linked to the key processes / activities that are reported within the service.
- ▶ Management: Indicators that provide management information for use in the service to plan or forecast provision

Service plans, approved through the PDSPs at the start of the financial year, set out the performance targets for the year ahead as well as reporting on the trend performance against the indicator for the previous three years.

The Council reports annually to its performance committee on comparative performance through the LGBF. The most recent report covered the 2015/16 performance year. This shows that the Council generally performs well against its peers. Using data from the Local Government Benchmarking Framework, the Council calculates an average ranking against other Scottish Local Authorities to measure performance. Under the most recent reported figures it came fifth overall in 2015/16, down from second in 2014/15. The report identified a number of areas where performance had declined, particularly around cost pressures in adult social work.

The BVAR will report in more detail on the Council's performance, focussing in particular on trend performance and the linkage between indicators and improvements in outcomes.

### Options appraisal and decision making

In advance of approving the transfer of management of facilities and functions to a modernised West Lothian Leisure, the Council Executive received a series of papers outlining the options appraisal exercise undertaken in advance of the recommended option. The move to a shared service delivery was driven by the need to generate additional savings of £0.5 million, but the appraisal decision was based on criteria which would indicate the likelihood that the option would support the Council's priorities of people living longer, healthier lives through increased participation in sport, leisure and cultural activities.

In line with the revised arrangements for Best Value, and the Accounts Commission's strategic priorities, our approach to which we set out in our indicative five year plan, we will undertake further detailed work on options appraisal and decision making in future years following the adoption and implementation of the new Corporate Plan.

### Value for money – what have we concluded?

- ▶ We have concluded that the Council has a comprehensive performance improvement framework, founded on the well established West Lothian Assessment Model. This has provided a stable and consistent framework through which services undertake self-assessment and seek to improve their performance.
- ▶ The Council monitors a suite of performance indicators through the Covalent system. Performance information shows that the Council generally performs very well compared to other councils, although the Council recognises areas where performance can be improved.



### **3. Other audit deliverables**

### 3. Other audit deliverables

Under the terms of our appointment, we provide other assurance activities such as the certification of certain grant claims and the Council's Whole of Government Accounts return, as well as information returns to Audit Scotland.

Other audit deliverables			
Aspect of work	What we did and what we found	Expected completion / submission date	Submitted on time
Annual Audit Plan	Reported to audit committee on 27 February 2017	31 March 2017	Yes
Audit Scotland Fraud Return submission	We submitted fraud returns summarising the reporting to audit and governance committee during the year.	26 May 2017	Yes
Submit NFI return to Audit Scotland	Reviewed the Council's arrangements and completed an information return – see conclusion elsewhere in this report	30 June 2017	No – submitted July 2017 due to EY staff illness
Submit Audit Scotland EU Funding questionnaire return	<p>The purpose of this questionnaire was to support the development of an understanding of Scotland's reliance on EU structural funding arrangements and in particular the extent to which public bodies have been preparing themselves for the consequences of not having access to EU funds in the future.</p> <p>We identified that the Council is managing £5.95 million of EU funds through 2016/17 and 2017/18, with 39 staff members involved in associated projects. Updates on the risk facing the Council are reported to the Partnership and Resources PDSP.</p>	30 June 2017	Yes
Submit certified Education Maintenance Allowance return	The return was not received by the Council submission deadline. When testing was undertaken during July, specific supporting evidence was not available for key elements of the claim, with evidence held offsite at schools. Our opinion was qualified as a result.	31 July 2017	No, due to the delays as a result of lack of evidence available from the Council
Submit certified Criminal Justice Social Work claim	Audit work has been undertaken with no significant findings arising.	29 September 2017	Complete
Whole of Government Accounts assurance statement to NAO	Audit work will be undertaken on updated WGA pack, following audit adjustments made to the financial statements.	29 September 2017	Complete
Certify Annual Accounts and submit Annual Audit Report	Pending formal approval of the financial statements	30 September 2017	On target
Submit Best Value Data Return to Audit Scotland	N/A for the Council due to BVAR in 2017	2 October 2017	N/A
Submit certified Non-Domestic Rates return	Audit work has been undertaken with no significant findings arising.	6 October 2017	On target
Submit certified Housing benefit subsidies claim to DWP	Work is in progress and we will discuss findings with the relevant officers prior to submission of our certification report.	30 November 2017	On target

# Appendices

- A – The Council’s responsibilities**
- B – Required communications with the audit committee**
- C – Auditor independence**
- D – Accounting and regulatory update**
- E – Summary of audit differences**
- F – Action plan**

# A. The Council's responsibilities



The Code of Audit Practice (the Code) summarises the responsibilities on all audited bodies falling within the public sector audit framework. We summarise these on this page.

<b>Responsibilities of audited bodies</b>	
<b>Corporate governance</b>	<p>Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.</p>
<b>Financial statements and related reports</b>	<p>Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:</p> <ul style="list-style-type: none"> <li>▶ preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation.</li> <li>▶ maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures.</li> <li>▶ ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority.</li> <li>▶ maintaining proper accounting records.</li> <li>▶ preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body.</li> </ul> <p>Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.</p> <p>Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.</p>
<b>Standards of conduct / prevention and detection of fraud and error</b>	<p>Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.</p>
<b>Financial position</b>	<p>Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> <li>▶ such financial monitoring and reporting arrangements as may be specified</li> <li>▶ compliance with any statutory financial requirements and achievement of financial targets</li> <li>▶ balances and reserves, including strategies about levels and their future use</li> <li>▶ how they plan to deal with uncertainty in the medium and longer term</li> <li>▶ the impact of planned future policies and foreseeable developments on their financial position.</li> </ul>
<b>Best Value</b>	<p>Local authority bodies have a statutory duty, under the Local Government (Scotland) Act 1973 and associated statutory guidance, to make arrangements to secure best value through the continuous improvement in the performance of their functions.</p> <p>Specified audited bodies also have to prepare and publish performance information in accordance with directions issued by the Accounts Commission.</p>

## B. Required communications



There are certain additional communications that we must provide to the Audit Committee, in accordance with ISA 260 and other auditing standards. These are set out below.

Required communication - what is reported?	Our reporting to you
<p><b>Terms of engagement</b></p> <p>Confirmation by the audit committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.</p>	<p>Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice</p>
<p><b>Planning and audit approach</b></p> <p>Communication of the planned scope and timing of the audit, including any limitations.</p>	<p>Annual Audit Plan – 27 February 2017</p>
<p><b>Significant findings from the audit</b></p> <ul style="list-style-type: none"> <li>▶ Our view of the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Any significant difficulties encountered during the audit</li> <li>▶ Any significant matters arising from the audit that were discussed with management</li> <li>▶ Written representations we have requested</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Any other matters significant to overseeing the financial reporting process</li> <li>▶ Findings and issues around the opening balance on initial audits</li> </ul>	<p>This Annual Audit Report</p> <p>We request written representation from you in respect of key matters arising during the course of our audit, and in accordance with auditing standards. A copy of this letter is provided for your consideration and signature at the time of approval of the financial statements.</p>
<p><b>Going concern</b></p> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	<p>No conditions or events were identified, either individually or together to raise any doubt about the Council's ability to continue for the 12 months from the date of our report.</p>
<p><b>Misstatements</b></p> <ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ Significant corrected misstatements, in writing</li> </ul>	<p>This Annual Audit Report</p>
<p><b>Fraud</b></p> <ul style="list-style-type: none"> <li>▶ Asking the audit committee whether they have knowledge of any actual, suspected or alleged fraud affecting the Council</li> <li>▶ Unless all those charged with governance are involved in managing the entity, any fraud identified or information obtained indicating that a fraud may exist involving: <ul style="list-style-type: none"> <li>(a) management;</li> <li>(b) employees with significant roles in internal control; or</li> <li>(c) others where the fraud results in a material misstatement in the financial statements.</li> </ul> </li> <li>▶ A discussion of any other matters related to fraud, relevant to audit committee responsibility.</li> </ul>	<p>This Annual Audit Report</p>

Required communication - What is reported?	Our reporting to you
<p><b>Significant deficiencies in internal controls identified during the audit</b></p> <ul style="list-style-type: none"> <li>▶ Significant deficiencies in internal controls identified during the audit.</li> </ul>	This Annual Audit Report
<p><b>Related parties</b></p> <p>Significant matters arising during the audit in connection with the Council's related parties including, where applicable:</p> <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and/or regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the entity</li> </ul>	We have no matters to report.
<p><b>Subsequent events</b></p> <ul style="list-style-type: none"> <li>▶ Where appropriate, asking the audit committee whether any subsequent events have occurred that might affect the financial statements.</li> </ul>	We have asked management and those charged with governance. We have no matters to report.
<p><b>Other information</b></p> <ul style="list-style-type: none"> <li>▶ Where material inconsistencies are identified in other information included in the document containing the financial statements, but management refuses to make the revision.</li> </ul>	We have no matters to report.
<p><b>External confirmations</b></p> <ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ We were unable to obtain relevant and reliable audit evidence from other procedures.</li> </ul>	We have received all requested confirmations.
<p><b>Consideration of laws and / or regulations</b></p> <ul style="list-style-type: none"> <li>▶ Audit findings of non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on "tipping off"</li> <li>▶ Asking the audit committee about possible instances of non-compliance with laws and/or regulations that may have a material effect on the financial statements, and known to the audit committee.</li> </ul>	We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations.
<p><b>Group Audits</b></p> <ul style="list-style-type: none"> <li>▶ An overview of the type of work to be performed on the financial information of the components</li> <li>▶ An overview of the group audit team's planned involvement in the component auditor's work on the financial information of significant components</li> <li>▶ Instances where the group audit team's evaluation of a component auditor's work of gave rise to a concern about its quality. Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted</li> <li>▶ Fraud or suspected fraud involving group or component management, employees with significant roles in group-wide controls, or others where the fraud resulted in a material misstatement of the group financial statements.</li> </ul>	<p>Annual Audit Plan – 27 February 2017</p> <p>This Annual Audit Report</p>
<p><b>Independence</b></p> <ul style="list-style-type: none"> <li>▶ Communication of all significant facts and matters that have a bearing on EY's objectivity and independence.</li> </ul>	This Annual Audit Report – Appendix C

Professional ethical standards, and the Terms of our Appointment, require us to communicate all significant facts and matters that have a bearing on EY's objectivity and independence as auditor of the Council.

## What we are required to communicate

Communicating key elements of the audit engagement partner's consideration of independence and objectivity such as:

- ▶ The principal threats.
- ▶ Safeguards adopted and their effectiveness.
- ▶ An overall assessment of threats and safeguards.
- ▶ Information on the firm's general policies and processes for maintaining objectivity and independence.
- ▶ Communications whenever significant judgments are made about threats to objectivity or independence and the appropriateness of safeguards.

## Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan, dated 27 February 2017.

We complied with the APB Ethical Standards and the requirements of Audit Scotland's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that you and your audit committee consider the facts known to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the audit committee on 25 September 2017.

## Summary of fees

As part of our reporting on our independence, we set out below a summary of the fees initially agreed for the year ended 31 March 2017.

We confirm that we have not undertaken non-audit work outside the Code requirements.

Additional auditor remuneration of £4,000 was agreed with management in respect of the audit of the Council's nine charitable trust funds.

Auditor remuneration per Annual Audit Plan	£201,333
Audit Scotland central costs	£130,480
<b>Total fee per Annual Audit Plan</b>	<b>£331,813</b>
Additional auditor remuneration	£4,000
Non-audit service fees	-
<b>Total fees</b>	<b>£335,813</b>

# D. Accounting and regulatory update



There are a number of new accounting standards and interpretations which will impact on the local authority accounting code of practice in the next two or three years. The following table provides a high level summary of those that have the potential to have the most significant impact on you.

Area	Summary	Potential impact
<i>IFRS 9 – Financial Instruments</i>	<p>Applicable for local authority accounts from the 2018/19 financial year. This new standard will change:</p> <ul style="list-style-type: none"> <li>▶ How financial assets are classified and measured</li> <li>▶ How the impairment of financial assets are calculated</li> <li>▶ Financial hedge accounting</li> <li>▶ The disclosure requirements for financial assets.</li> </ul> <p>Transitional arrangements are included within the accounting standard, however as the 2018/19 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be and whether any accounting statutory overrides will be introduced to mitigate any impact.</p>	<p>Although some initial thoughts on the approach to adopting IFRS 9 have been issued by CIPFA, until the Code is issued and any statutory overrides are confirmed there remains uncertainty. The Council will, however, have to:</p> <ul style="list-style-type: none"> <li>▶ Reclassify existing financial instrument assets</li> <li>▶ Remeasure and recalculate potential impairments of those assets; and</li> <li>▶ Prepare additional disclosure notes for material items</li> </ul>
<i>IFRS 15 Revenue from Contracts with Customers</i>	<p>Applicable for local authority accounts from the 2018/19 financial year. This new standard deals with accounting for all contracts with customers except:</p> <ul style="list-style-type: none"> <li>▶ Leases;</li> <li>▶ Financial instruments;</li> <li>▶ Insurance contracts; and</li> <li>▶ for local authorities, Council Tax and NDR income.</li> </ul> <p>The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations.</p> <p>There are transitional arrangements within the standard, however as the 2018/19 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be.</p>	<p>Again CIPFA have issued initial thoughts on the approach to adopting IFRS 15, although uncertainty remains until the Code is issued. For all material income sources from customers the Council will have to:</p> <ul style="list-style-type: none"> <li>▶ Disaggregate revenue into appropriate categories</li> <li>▶ Identify relevant performance obligations and allocate income to each</li> <li>▶ Summarise significant judgements</li> </ul>
<i>IFRS 16 Leases</i>	<p>IFRS 16 will be applicable for local authority accounts from the 2019/20 financial year.</p> <p>Whilst the definition of a lease remains similar to the current leasing standard, IAS 17, for local authorities who lease in a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet.</p> <p>There are transitional arrangements within the standard, although as the 2019/20 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be or whether any statutory overrides will be introduced.</p>	<p>Until the 2019/20 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area.</p> <p>However, what is clear is that the Council will need to undertake a detailed exercise to classify all of its leases and therefore must ensure that all lease arrangements are fully documented.</p>



# E. Summary of Audit Differences



There were a number of significant adjustments processed to the unaudited financial statements as a result of our audit work. The impact of these is summarised below.

## Summary of audit differences – prior period adjustments

No.	Account	Comprehensive income and expenditure statement (Increase) / Decrease	Balance sheet (Decrease) / Increase
<b>1</b>	<b>Revaluation adjustment to correct increase in value of other land and buildings in prior year</b>		
	Property, plant & equipment – land & buildings		£426.2 million
	Revaluation reserve		£(426.2) million
<b>2</b>	<b>Recognition of revaluation of schools PPP assets</b>		
	Property, plant & equipment – schools PPP assets		£56.0 million
	Revaluation reserve		£(56.0)million
<b>3</b>	<b>Impairment to carrying value of Council Dwelling additions in the period to hold at Existing Use Value – Social Housing in accordance with the Code of Practice on Local Authority Accounting</b>		
	Property, plant and equipment – Council Dwellings		(£12.2 million)
	Impairment recognised in cost of services	£12.2 million	
<b>4</b>	<b>Adjustment to remove HRA developer contributions from creditors and reflect these as a transfer between HRA fund and General Fund.</b>		
	Short Term Creditors		£6.6 million
	Housing Revenue Account Expenditure	(£6.6 million)	
	Housing Revenue Account Fund		£(6.6) million
	General Fund – earmarked reserves		£6.6 million

## E. Summary of Audit Differences (cont.)



There were a number of significant adjustments processed to the unaudited financial statements as a result of our audit work. The impact of these is summarised below.

### Summary of audit differences – current year adjustments

No.	Account	Comprehensive income and expenditure statement (Increase) / Decrease	Balance sheet (Decrease) / Increase
<b>1</b>	<b>Revaluation adjustment to correct increase in value of other land and buildings in prior year</b>		
	Property, plant & equipment – land & buildings		£(426.2) million
	Revaluation reserve		£426.2 million
<b>2</b>	<b>Impairment to carrying value of Council Dwelling additions in the period to hold at Existing Use Value – Social Housing in accordance with the Code of Practice on Local Authority Accounting</b>		
	Property, plant and equipment – Council Dwellings		(£20.6 million)
	Impairment recognised in cost of services	£20.6 million	
<b>3</b>	<b>Adjustment to depreciation in year to reflect depreciation on PPP assets</b>		
	Property, plant and equipment - depreciation		£(12.8) million
	Depreciation charged to cost of services	£12.8 million	
<b>4</b>	<b>Recognition of initial contribution to West Lothian Integration Joint Board and subsequent income received to deliver services.</b>		
	CIES – Service gross income	£(60.6) million	
	CIES – Service gross expenditure	£60.6 million	
<b>5</b>	<b>Adjustment to remove incorrect recognition of an accrual and prepaid income within the draft financial statements.</b>		
	Short-term creditors		£0.5 million
	Short-term debtors		£(0.5) million

## E. Summary of Audit Differences (cont.)



There were a number of significant adjustments processed to the unaudited financial statements as a result of our audit work. One difference remains unadjusted as set out below.

### Summary of audit differences – unadjusted differences

No.	Account	Comprehensive income and expenditure statement (Increase) / Decrease	Balance sheet (Decrease) / Increase
1	<b>Net estimated impact of recognising West Lothian Leisure as a subsidiary in the group financial statements instead of as an associate</b>		
	Group net assets		£(3.0) million
	Group reserves		£3.0 million

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Council or management to action.

<b>Classification of recommendations</b>			
<b>Grade 1:</b> Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		<b>Grade 2:</b> Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	
<b>Grade 3:</b> Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.			
<b>No.</b>	<b>Findings and / or risk</b>	<b>Recommendation / grading</b>	<b>Management response / Implementation timeframe</b>
<b>1</b>	<p><b>Financial reporting process</b></p> <p>Overall the financial reporting process is well established within the Council.</p> <p>However, particularly in relation to non-transactional items, we have identified that there are examples where judgements made in the financial statements process are not fully and appropriately documented and approved.</p>	<p>Where key judgements on items within the financial statements are being made, these should be fully documented and subject to approval by the Head of Finance and Property Services, and retained to support current and future year financial statements.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Key judgements will be fully documented and approved by the Head of Finance and Property Services for the 2017/18 financial statements onwards.</p>
<b>2</b>	<p><b>PPE Valuations</b></p> <p>Our audit work identified significant movements in operational building valuations which were not being taken into account when assessing whether, in line with Code requirements, the year end values of assets could be materially different from the carrying value recorded in the financial statements.</p>	<p>Management requires to consider and agree an appropriate process to ensure the valuation cycle is appropriate to take into account potential material movements in key assets, as well as a means to ensure that where a 1 April valuation is undertaken, that the valuation remains appropriate as at the 31 March balance sheet.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>A review will be undertaken by the end of December 2017 to agree an appropriate process.</p>
<b>3</b>	<p><b>Group financial statements</b></p> <p>From 1 April 2017, the articles of association of West Lothian Leisure were changed again. In addition, the company took on additional leisure and culture assets of the Council.</p>	<p>An updated assessment of the group relationship with West Lothian Leisure should be conducted in advance of preparation of the 2017/18 financial statements.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>An assessment has been completed. West Lothian Leisure will be accounted for as a subsidiary in the 2017/18 financial statements.</p>
<b>4</b>	<p><b>Financial management – risk assessment of savings</b></p> <p>Management has an established process of risk assessing the delivering of savings within the in-year budget monitoring. Savings will, however, become increasingly difficult to deliver.</p>	<p>We have discussed with management the means to identify within budget papers the risk assessment associated with individual savings proposals. We recommend that an overall red/amber/green rating is provided to members on savings proposals allowing them to focus on the area of greatest financial risk.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Savings proposals going forward will be assessed on a red/amber/green basis by officers. This information will be included in the revenue budget papers reported to elected members.</p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
5	<p><b>Level of uncommitted general fund reserves</b></p> <p>The Council has one of the lowest levels of uncommitted general fund reserves of all Scottish local authorities. While the Council exhibits good in-year financial management, as financial savings become harder to delivery, this low level of reserves reduces the Council's flexibility around budget decisions.</p>	<p>Management should consider whether the target level of uncommitted reserves remains appropriate in the context of approval of the forthcoming medium-term financial strategy.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Management has considered if the level of uncommitted reserves remains appropriate. Taking account of clear financial planning arrangements, sound financial management and the level of other reserves, the Head of Finance and Property Services believes the level of uncommitted reserves is appropriate.</p> <p>The level of uncommitted reserves will continue to be reviewed as part of the revenue budget setting process and will continue to be subject to a specific recommendation in the annual revenue budget report.</p>
6	<p><b>Approval of 2017/18 budget</b></p> <p>As the final year of the existing five year financial plan, the Council set a one-year budget for 2017/18. While an overview of the economic outlook was provided to members, there was no detailed information provided on the financial challenges facing the Council over the medium-term.</p>	<p>While we understand that the Council links the financial strategy to the corporate plan, we recommend that in setting budgets, the Council should always have a multi-year budget strategy in place so that savings are being considered in the context of a medium-term plan.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>Updates on the economic context at UK, Scottish and West Lothian level and an update on the council's future budget model are now being presented quarterly to the Partnership and Resources PDSP. In future, these updates will include information for at least three years in advance on the anticipated financial position of the council. This information will also be included in any reports on future financial planning.</p>
7	<p><b>Engagement of members in long-term financial planning</b></p> <p>In advance of public consultation, the corporate management team has been developing proposals to meet the significant forecast budget gaps. While members have approved the overall process, their detailed consideration of officer savings proposals will commence in December 2017. These are expected to include difficult decisions and could leave the delivery of savings in the required timescales at risk.</p>	<p>With significant challenges facing the Council over the coming years, in our view it is important that members take an early lead in shaping the direction of future priorities and service delivery.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>Council, in February 2017 agreed objectives, a process and a timetable for corporate and financial planning. In accordance with the agreed process and timetable a consultation is to take place from mid October to mid November and provides all stakeholders in West Lothian with the opportunity to comment on proposed priorities, officer savings proposals and future council tax levels.</p> <p>Reports on all responses to the consultation will be presented to PDSPs in December 2017 providing the opportunity for elected members to share the direction of future priorities and service delivery.</p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
8	<p><b>Operation of audit and governance &amp; risk committees</b></p> <p>With the remit of the audit and governance committee split across these two new committees, to introduce a greater focus on risk, there is the potential for unnecessary duplication in the work of the committees, together with a lack of clarity in respect of where reports and business are considered.</p> <p>In addition, while the audit committee received the unaudited accounts on 30 June 2017, its remit does not formally include the annual accounts and so there is a risk of uncertainty arising around the audit committee's role in considering the external audit report on the annual accounts.</p>	<p>It is recommended that, in line with best practice, these committees undertake annual self-assessments of effectiveness, including with a focus on how they have interacted with each other over a full cycle of reporting. The role of the audit committee with the annual accounts should also be clarified.</p> <p>In addition, best practice would suggest that the scheme of administration sets out that the chairs of these committees should not be drawn from the Council administration.</p>	<p>It is intended to include a self assessment in the work-plan for both committees.</p> <p>In accordance with the agreed procedures, Council will consider for approval the auditor's annual report and audited annual accounts. Following approval, the auditor's report and the audited annual accounts will be referred to audit committee for information.</p> <p>Changes to the scheme of administration are a matter for elected members of the council to consider. The covering report by the Head of Finance and Property Services on the auditor's annual report will highlight these recommendations to elected members for consideration.</p>
9	<p><b>Scrutiny of performance</b></p> <p>The Performance committee and the Education (Quality Assurance) committee are the main committees within the scheme of administration for consideration of performance.</p> <p>At the current time, the scheme of administration does not set out the membership of these committees in relation to roles elected members may have on other committees.</p>	<p>In our view, there is scope to review and potentially enhance the arrangements in the Scheme of Administration for review of performance within the committee structure, to ensure that this provides for sufficient involvement from elected members drawn from outside the decision-making committees of the Council.</p>	<p>Changes to the scheme of administration are a matter for elected members of the Council to consider. The covering report by the Head of Finance and Property Services on the auditor's annual report will highlight these recommendations to elected members for consideration.</p>

No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
10	<p><b>Performance committee reporting</b></p> <p>The performance committee is the key committee for independent scrutiny of overall corporate performance. Improvements could, however, be made to the information and reports received on corporate performance.</p> <p>Review of committee minutes, and attendance at the committee, also found that there is scope to improve evidence of member involvement in providing robust challenge and scrutiny to drive forward improvement at the Council.</p>	<p>As the key committee for driving improvement at a corporate level, including oversight of the key Council priorities against which the Council reports in its public performance reporting, the performance committee should receive appropriate information on corporate performance and record evidence of effective and robust challenge and scrutiny provided by the committee in respect of achievement of corporate performance targets should be recorded.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>A officer review will be undertaken by the end of October 2017 to consider how reporting and scrutiny on corporate performance can be improved. The documented minutes of performance committee will provide more details of questions and discussion at the committee.</p>
11	<p><b>Prioritisation of internal audit reviews</b></p> <p>Experience has shown that the original annual audit plan is not always delivered with reviews either rescheduled into future years or removed from the plan as other pressures on resource arise. For example, in 2016/17 four reviews were rescheduled to 2017/18 and three removed, totalling 125 days out of the original 370 day plan.</p>	<p>While the audit committee is asked to review a revised plan, in our judgement, prioritisation of reviews in the original plan is important to support members in discharging their oversight role on the appropriate delivery of the internal audit plan for the year.</p> <p>Good practice would also show the audit plan productive days as an element of total resources available.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>In future the audit reviews included in the annual audit plan, and presented to the audit committee for approval, will be prioritised and the productive days as an element of total resources will also be included in the plan.</p>
12	<p><b>Internal audit performance indicators</b></p> <p>In our view, certain targets set for measurement of the performance of internal audit are not sufficiently stretching, with for example 12 weeks to deliver a draft report providing a risk that control weaknesses continue un-addressed while the report is being prepared.</p> <p>Key performance indicators also indicate that 100% of the annual audit plan has been delivered, but this does not relate to a measurement of the original plan set at the start of the year.</p>	<p>A review of internal audit performance indicators should be undertaken to ensure that these are appropriately challenging, relevant to business needs and take account of changes in annual audit plans in the year.</p> <p>In addition, while internal audit reports appear to be suitably challenging of the control environment, a key indicator of the challenge provided is the percentage of recommendations which are accepted and implemented by management.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>Internal audit performance indicators are currently subject to ongoing review, however a further review will be undertaken by the end of December 2017.</p>

No.	Findings and risk	Recommendation / grading	Management response / Implementation timeframe
13	<p><b>Role of internal audit</b></p> <p>The Audit, Risk and Counter Fraud Manager fulfils a role both as Head of Internal Audit and also Risk Manager. This creates, in our view, a potential for conflict of interest to arise.</p>	<p>During a forthcoming period of potentially significant change, senior officers should consider the potential for this risk to arise and to ensure there is appropriate mitigation, such that the risk manager is not involved in activities which could subsequently affect their independence in conducting internal audit reviews in certain areas.</p> <p style="text-align: right;"><i>Grade 2</i></p>	<p>The view of the council's Corporate Management Team is that the arrangements in the council have improved significantly since responsibility for risk management was combined with Internal Audit.</p> <p>A review will be undertaken by the end of December 2017 to identify any potential conflicts of interest to ensure mitigating actions are implemented.</p>
14	<p><b>FtPP Compliance / Governance</b></p> <p>Scrutiny of the performance of West Lothian Leisure has been undertaken in private throughout 2016/17. In addition, two members of the committee charged with scrutinising performance have also been directors of the Company. This is not in line with the Accounts Commission's guidance on working with arms-length external bodies.</p>	<p>In addition to addressing the weaknesses identified through an internal audit review, the Council should review the overall governance and scrutiny arrangements in respect of West Lothian Leisure to ensure these accord with best practice.</p> <p style="text-align: right;"><i>Grade 1</i></p>	<p>A review will be undertaken by the end of February 2018 of governance and scrutiny arrangements in respect of West Lothian Leisure.</p>



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