



**SCOTT-MONCRIEFF**

EDINBURGH AND GLASGOW



## **Orkney Islands Council**

# **Annual Audit Report to Orkney Islands Council and the Controller of Audit 2007/08**



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# Executive Summary

## Introduction

This report summarises the findings from our 2007/08 audit of Orkney Islands Council. The report covers the audit of the financial statements and aspects of the Council's performance and governance arrangements.

## Key Messages from our 2007/08 audit

### *Use of Resources*

We are pleased to report that the 2007/08 accounts of the Council comply with the Code of Practice on Local Authority Accounting in the United Kingdom in all material aspects. Our audit certificate is unqualified.

The Council reported a general fund surplus of £1.514 million in 2007/08. The general fund balance brought forward of £15.884 million at 1 April 2007 increased to a cumulative net surplus of £17.398 million at 31 March 2008. In its accounts, the Council has earmarked reserves of £2.303 million which leaves the Council uncommitted balances of £15.095 million. The Council's policy is to maintain a general fund balance at a level not less than £8 million as a contingency for unforeseen events.

The Council reported an under spend of approximately £9.975 million on its combined capital programme of which approximately £8.5 million has been carried forward to 2008/09. With a challenging capital programme over the next couple of years, it is essential that slippage is minimised if the Council wishes to meet its objectives.

In 2007/08, the Council finalised a single status agreement which took effect from 1 April 2007. All Council employees signed up to the single status agreement and a £1.1m provision was included in the financial statements at 31 March 2008 to cover single status payments due from 1 April 2007. Most of the payments due were subsequently made in July 2008.

Due to retirements and senior staff leaving, there will soon be a number of vacancies at senior management level. Whilst the Council has introduced schemes to develop and grow future managers internally there is limited evidence of succession planning being in place for senior management posts.

The Council's asset management arrangements are underdeveloped. This however has been identified as an area of improvement in the Council's audit improvement plan. It is also envisaged that the recently appointed asset management surveyor will be responsible for co-ordinating the Council's asset management arrangements.

The Council has recognised that the existing records for common good are incomplete and inaccurate and has approved a seven point action plan to improve the record keeping and maintenance of the common good fund.

### *Performance*

During 2007/08, Audit Scotland undertook a Best Value and Community Planning review of Orkney Islands Council. The findings of the review were published in June 2008. The report acknowledged the strength of the Council's leadership, its performance in certain areas and the partnership and joint working arrangements with NHS Orkney and its community councils. It did however also identify areas with scope for improvement. Following the publication of the report, the Council has prepared an audit improvement plan. It is the intention that this plan will be incorporated into the Council's corporate and service improvement plans.

The Best Value audit identified the Council's performance management arrangements as an area which required particular improvement. Due to the absence of good performance information, scrutiny of service performance is underdeveloped. An updated performance management system has since been approved by the Council's Monitoring and Audit Committee.

### *Governance*

The political governance structure within the Council was reviewed prior to the 2007 local government elections. A committee based structure exists with seven committees covering all of the main services within the Council. Elected member training was provided following the elections. Ongoing work also continues to develop a training programme for elected members linked to individual needs.

The Best Value audit noted that the Council works well with its community planning partners. The partners recognise the importance of community planning and joint working in maintaining sustainable services for Orkney. The audit did however highlight that the Council was unable to demonstrate progress against objectives as much of its activity was not systematically measured and reported. The Council's Audit Improvement Plan states that this is currently being addressed through the development of a Community Planning Performance Management System which is being developed to support the Community Planning Partnership's Single Outcome Agreement for 2009-2010 (also being developed at present).

The Council has continued to make progress in implementing its risk management arrangements. Risk management is currently being embedded into departmental practices through the development of departmental risk registers and action plans, which are at varying stages of development. This activity is also being supported by Zurich Municipal

## **Future Outlook**

In 2007/08 Scottish local government faced significant changes as new council administrations became established and new multi-member ward arrangements evolved. The agreement of the Concordat between the Scottish Government and COSLA in November 2007 marked a potential watershed in the relationship between central and local government in Scotland with agreement being reached on a variety of initiatives including funding levels and the achievement of national outcomes over a three year period. Whilst there is potential stability in terms of structures, national funding and the articulation of national priorities there remain a number of initiatives that will impact significantly on the Council and will have implications on future audits of the Council.

Within Orkney, the Single Outcome Agreement (SOA) was developed as a council only agreement with the Scottish Government and covered the priorities set out in the Council's corporate strategic plan 2008-2013. Over the next year, a SOA incorporating the outcomes and relevant indicators of other stakeholders involved in the Orkney Community Planning Partnership will be developed. There will be a need to ensure appropriate mechanisms are in place to report consistently and effectively against the SOA. Again, the audit improvement plan indicates that plans are underway to develop these mechanisms.

In 2008, the Scottish Government approved the revised outline business case for the schools investment programme and the conditional award of grant. The project is to be delivered through a special purpose vehicle structured as a company jointly owned by the Council and NHS Orkney. Due to "vires" issues on the part of the Health Board, however, this model has yet to be established. The timetable indicates that construction will be completed by May 2012.

The Council and NHS Orkney are also currently exploring the formation of a special purpose vehicle in the form of a limited company to provide a wide range of support services for both organisations. A business plan is currently being prepared which explores some of the issues surrounding this proposal. The provisional timetable for progressing with this initiative is for the company to be formed in April 2009 and service redesigns to be carried out over the period 2009-11.

The 2008/09 NFI exercise is due to begin in October 2008. Orkney Islands Council has already taken steps to ensure that information is submitted within the deadlines and arrangements are in place to review the data once received.

## **Conclusion**

This report concludes the 2007/08 audit of Orkney Islands Council. We have performed our audit in accordance with the Code of Audit Practice published by Audit Scotland, International Standards on Auditing (UK and Ireland) and Ethical Standards.

This report has been discussed and agreed with the Chief Executive and members of the Council's Management Team. We would like to thank all members of Orkney Islands Council's management and staff who have been involved in our work for their co-operation and assistance during our audit visits.

**Scott-Moncrieff**  
**September 2008**

# Introduction

- 1 This report summarises the findings from our 2007/08 audit of Orkney Islands Council. The scope of the audit was set out in our External Audit Annual Plan, which was presented to the Monitoring and Audit Committee on 13 December 2007.
- 2 The main elements of our audit work in 2007/08 have been:
  - Audit of the financial statements, including a review of the Corporate Governance Statement
  - Review of corporate governance arrangements
  - Review of internal financial controls and financial systems
  - Review of the Council's following the public pound arrangements
- 3 In addition to this report, we have issued the following detailed reports during 2007/08:
  - Corporate Governance Arrangements
  - Following the Public Pound

The key issues arising from these reports are summarised in this annual report.
- 4 Our findings are drawn together within three sections:
  - **Use of Resources:** covers how Orkney Islands Council is managing its finances, workforce and assets.
  - **Performance:** covers the Council's recent audit of Best Value and Community Planning, performance management arrangements and statutory performance indicators.
  - **Governance:** covers a summary of Orkney Islands Council's corporate governance arrangements.
- 5 This report will be submitted to the Controller of Audit and will be published on Audit Scotland's website, [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

# Use of Resources

## Introduction

- 6 In this section we summarise key aspects of Orkney Islands Council's reported financial position and performance to 31 March 2008. We also consider and report on the Council's arrangements in place for workforce related issues, asset management and procurement.

## Annual Accounts and Audit Opinion

- 7 Our audit report included on pages 66 and 67 of the annual accounts is addressed to the Members of the Council and the Accounts Commission for Scotland. The report was issued on 26 September 2008 and is unqualified.
- 8 We are pleased to report that the quality of the financial statements prepared by the Council continues to improve and is a demonstration of the Council's finance officials' commitment to consistently improve the disclosure of Orkney Islands Council financial and accounting information to stakeholders.

## Accounts Timetable

- 9 Scottish local authorities are required under Regulation 4 of the Local Authority Accounts (Scotland) Regulation 1985 to submit a copy of an abstract of their accounts to the Controller of Audit by 30 June. We are pleased to confirm that the Council adhered to this requirement by lodging accounts with the Controller of Audit on 27 June 2008.

## Format of the Accounts

- 10 The financial statements have been prepared in accordance with the Code of Practice on Local Authority Accounting: A Statement of Recommended Practice in the United Kingdom 2007 (the SORP). The SORP specifies the principles and practices of accounting required to prepare a Statement of Accounts which 'presents fairly' the financial position and transactions of a local authority and to prepare group financial statements where they have material interests in subsidiaries, associates or joint ventures.
- 11 The SORP is reviewed and updated annually by the CIPFA/LASAAC Local Authority SORP Board and the 2007 version, applicable to 2007/08, was issued in July 2007. The 2007 SORP contains a number of substantive changes from the previous edition, including:
- **Financial Instruments** - A new chapter covering financial instruments has been added with requirements based on Financial Reporting Standard (FRS) 26 Financial instruments: Recognition and measurement, FRS 25 Financial instruments: Presentation and disclosures

and FRS 29 Financial instruments: Disclosures. Financial instruments cover both financial assets and financial liabilities and include straightforward items such as debtors and trade creditors and complex ones such as derivatives. The previous requirements were based on FRS 4 Capital instruments and only covered borrowing.

- **Revaluation Reserve and Capital Adjustment Account** - From 1 April 2007 the Fixed Asset Restatement Account and Capital Financing Account was replaced with a Revaluation Reserve and Capital Adjustment Account. The 2007 SORP required this change to be made prospectively and consequently the opening Revaluation Reserve is zero.

- 12 As part of our 2007/08 audit we considered the arrangements Orkney Islands Council had in place to ensure the appropriate changes were made to the financial statements. Overall we concluded that the Council had complied with the new requirements of the SORP. We did however note the following:
- 13 The 2007 SORP states that recharges to and from services should be excluded so that the recharged cost is reflected only in the accounts of the service receiving it. During our review we noted that such recharges have not been excluded from the Council's financial statements. Due to the Council's existing method for recording such transactions, it has not been possible to establish the value of these transactions and as a result no adjustment has been made to the financial statements.

*Action Plan Point 1*

## **Summary Financial Position**

### **General Fund**

- 14 Orkney Islands Council achieved a general fund surplus of £1.514 million in 2007/2008. The general fund balance brought forward of £15.884 million at 1 April 2007 increased to a cumulative net surplus balance of £17.398 million at 31 March 2008. An analysis of the Council's general fund reserve at 31 March 2008 is presented below:



<b>Analysis of General Fund Reserves as at 31 March</b>		
	<b>2008 £'000</b>	<b>2007 £'000</b>
General Fund surplus at end of year	17.398	15.884
<b>Less Earmarked Reserves</b>		
• Modernising Government Fund	(0.017)	(0.067)
• Corporate Development Fund	(0.076)	(0.152)
• Modernising Teachers Fund	(0.068)	(0.068)
• Community Council	(0.210)	(0.192)
• Devolved School Management Fund	(0.167)	(0.071)
• Orkney College	0.875	0.923
• Single Status Fund	(1.600)	(1.056)
• ALCO Development Fund	(0.131)	(0.250)
• Training Fund	(0.101)	(0.039)
• Efficiency & Reform Fund	(0.567)	0
• Energy Advice Centre Transitional Fund	(0.021)	0
• Masterplans Studies Fund	(0.140)	0
• Energy Efficiency Fund	(0.080)	0
<b>Total Earmarked Reserves</b>	<b>(2.303)</b>	<b>(0.972)</b>
<b>Uncommitted Surplus on General Fund</b>	<b>15.095</b>	<b>14.912</b>

- 15 The analysis above indicates that the Council has earmarked reserves of £2.303 million which leaves the Council with an uncommitted general fund balance of £15.095 million. The Council currently considers that a minimum balance of £8 million should be retained within the general fund to meet unforeseen contingencies.

### **Housing Revenue Account (HRA)**

- 16 The Council does not retain a housing revenue account reserve. Instead any surplus is used to finance capital expenditure. In 2007/08 capital expenditure funded by the HRA amounted to £0.499 million (2006/07 £0.724 million).

### **Harbour Authority Account**

- 17 The Orkney County Council Act of 1974 authorises Orkney Islands Council to exercise harbour jurisdiction as a Competent Harbour Authority. The Act also requires the Council to keep separate accounts in respect of the harbour authority account. The trading position from the harbour operations is reflected within the Council's cost of services.
- 18 The Council reported a net increase in the harbour authority account fund balance in the year of £6.795 million. As a result the fund balance brought forward of £174.090 million at 1 April 2007 increased to a cumulative net surplus balance of £180.885 million at 31 March 2008. The main contributing factor to the increase in the fund balance for the year was the gain on investments of £8.461 million.

## Financial Performance

- 19 In comparison with the budget, the Council reported a favourable outturn position of £0.183 million. This comprised an under spend against budget of £1.895 million (see below) offset with a deficit of £1.712 million on sources of funding. The sources of funding include a use of balances budget (£2.144 million) made up of contributions from the strategic reserve fund and general fund balances. Due to the underspend achieved against budget the contribution from the general fund balances (£1.984 million) was not required.

<b>Financial Performance Summary 2007/08</b>			
	<b>Actual Net Expenditure £million</b>	<b>Annual Net Budget £million</b>	<b>Over/(under) spend £million</b>
Community Social Services	12.073	12.242	(0.169)
Other Housing	0.303	0.386	(0.083)
Environmental Services	2.996	3.225	(0.229)
Planning	0.925	0.692	0.233
Education	23.766	24.348	(0.582)
Recreation & Cultural	3.238	3.252	(0.014)
Transportation	6.716	6.640	0.076
Roads	3.959	4.374	(0.415)
Economic Development	0.551	0.590	(0.039)
Central Administration	0	0	0
Law, Order & Protective Services	3.583	3.374	0.209
Other Services	8.258	9.140	(0.882)
<b>TOTAL</b>	<b>66.368</b>	<b>68.263</b>	<b>(1.895)</b>

- 20 In 2007/08, Roads Services reported an underspend of £0.415 million (9.5%). This was largely due to resources being diverted from works funded through the roads revenue budget to carry out capital works to secure grant funding.

## 2008/09 Financial Position

- 21 The Scottish Government indicated a desire for local authorities to freeze council tax at 2007/08 levels and had indicated that certain funding would be dependent on this. For Orkney Islands Council this amounted to an annual sum of £0.231 million. In setting its 2008/09 budget, the Council agreed to freeze council tax at 2007/08 levels.
- 22 The Council agreed that priority should continue to be given to spending on meeting statutory obligations, care of the elderly, transport and housing. To achieve this, the Council committed to:

- Seeking further efficiency gains/savings within existing services and adopting alternative service delivery methods
- Where possible, redirecting some of the specific grant or ring-fenced funding to the Council's higher priority areas of spending
- The interest earned on the strategic reserve fund becoming a source of funding

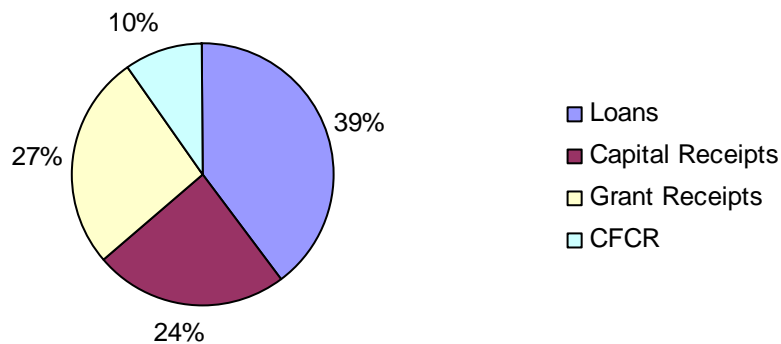
23 In 2007, the Council agreed to develop a medium term financial strategy to be implemented from the 2008/09 budget round. At the time of setting the 2008/09 budget however it was recognised that further work was required to develop the draft medium term financial strategy.

24 We noted in the Council's audit improvement plan the intention to develop the draft medium term financial strategy into a strategic resource management strategy. This will enable the Council to link overall strategic objectives to its revenue budget.

### Capital Expenditure

25 During the year the Council spent £10.700 million on capital expenditure. This was financed by borrowing, capital grants and capital receipts. (Note: The Council does not borrow externally but instead borrows from the harbour strategic reserve fund).

Sources of Funding



26 The Council reported an under spend of approximately £9.975 million on its combined capital programme of which approximately £8.5 million has been carried forward to 2008/09. In previous years, slippage on the capital programme was recognised by the Council as an inherent feature of the system of planning and progressing capital projects in the Council's capital programme. As a result, the Council revised their procedures for both appraising, profiling and controlling the capital programme. The revised capital project appraisal system has been applied to the programme since 2005/06. Significant levels of slippage however continue to be reported.

- 27 With a challenging capital programme over the next couple of years it is important that slippage of capital expenditure is minimised if the Council wishes to meet its objectives.

***Action Plan Point 2***

**Orkney College**

- 28 Orkney Islands Council provides further and higher education provision through the Orkney College using a devolved Board of Management arrangement. The Orkney College is funded by direct grant from the Scottish Funding Council (SFC).
- 29 During the financial year 2007/08 the College generated a surplus of £48k for the year, resulting in a decrease in the accumulated deficit position on the College to £875k as at 31 March 2008.
- 30 To ensure Orkney College is committed to managing its deficit position, the Council requires the College to budget for and realise an annual surplus on its activities on an ongoing basis. A working group has been established to explore options for improving the financial position of the College.

**Group Accounts**

- 31 Orkney Islands Council has classified its interests in four companies as subsidiaries with a further three company/trusts as an associates. The Council's interests in three of the Joint Boards are also being classified as associates. The Council's interests in the Valuation Joint Board have been classified as a joint venture. The Council has a number of other interests in companies which have not been consolidated into the group accounts as they do not meet the SORP definitions.
- 32 We have audited the group accounts prepared by the Council and the judgements made by the Council regarding those entities included or excluded from the group accounts. The audit report covers our audit opinion on the group accounts and is unqualified.
- 33 In 2006/07 we reported that a number of the Council's group bodies prepared financial statements using the Financial Reporting Standard for Smaller Entities (FRSSE). As a result certain disclosures, for example cash flow statements or FRS 17 disclosures, had not been prepared for these entities. Whilst this was immaterial to the group financial statements, we encouraged the Council to request that its subsidiaries prepare full financial statements and do not take advantage of any exemptions or reduced disclosure opportunities. We are disappointed to note that some of the Council's group organisations continue to prepare financial statements using FRSSE.

***Action Plan Point 3***

## **PPP**

- 34 Orkney Islands Council has joined the PPP building programme to create 21<sup>st</sup> Century Schools, with Scottish Government support for a £50 million project. The initial business case identified three projects, including Kirkwall Grammar School, a new primary school in Stromness and Halls of Residence at Kirkwall. Options also included plans for the future redevelopment of Kirkwall's Balfour Hospital. A revised outline business plan was submitted by Orkney Islands Council to the Scottish Government. The revised outline business case includes a fourth project; a new swimming pool at Pickaquoy Centre. The revised outline business case was approved at full Council in February 2008.
- 35 Following the submission of the revised outline business case the Scottish Government made a conditional offer of grant funding, capped at £3.58 million per annum over 30 years.
- 36 Discussions have been ongoing with the Scottish Government on how to deliver this project as a conventional PPP project is not considered appropriate. The initial delivery model set out in the revised outline business case proposed a Special Purpose Vehicle (SPV) structured as a Council owned limited liability partnership. This however did not meet the aspirations of the Scottish Government who wanted a separate legal entity jointly owned by the Council and NHS Orkney which would procure both schools and health projects and potentially other infrastructure projects in Orkney in the future.
- 37 NHS Orkney however cannot be brought into the original model due to "vires" issues on the part of the Health Board to participate in such a body. The Health Board does not currently have the power to participate in a limited liability partnership. It is also not clear whether the Health Board can participate in a company which provides facilities or services other than in the area of health. The Health Board is currently working with the Scottish Government to identify a way in which they can participate in the company. (Current indicators are that the issues set out above will be resolved in a positive manner).
- 38 Pending clarification of the above, "shadow" arrangements will be established. The revised timetable indicates that construction will be completed by May 2012.

## **Common Good**

- 39 Local authorities are required to administer common good funds under Section 15 of the Local Government (Scotland) Act 1994. The purpose of common good funds is to provide a benefit to the population of the area either through the financial disbursement of funds, securing assets for the ongoing use of the population or contributing to specific local projects/initiatives.
- 40 In April 2008, a joint report by the Chief Executive, Director of Finance and Housing and the Director of Technical Services was presented to the Council's Land and Property Sub-Committee. The report provided a summary of the current status of the common good fund. The report noted that the list of assets recorded within the common good register is incomplete,

existing descriptions within the register did not enable the Council to readily identify the asset being referred to and some of the properties recorded in the register no longer existed. It also recognised that at present there is no system for recording what documents are held in the Council's safe and no system for identifying the land to which the documents relate.

- 41 The report considered the options for taking forward the administration of common good. A seven point plan of action in respect of the common good fund has been approved:

<b>Orkney Islands Council – 7 point plan of action in respect of Common Good</b>
1. Remove properties which no longer exist from the common good fund;
2. Add properties historically omitted from common good fund on their transfer from Town Councils accounts in 1975
3. Revalue easily identifiable properties from the common good fund asset list for inclusion in the 2007/08 year end;
4. Ensure common good assets are treated in a manner consistent with the treatment of the other Council assets;
5. Seek to identify the other properties, from the common good asset list, for revaluation in future years;
6. Ensure from 1 April 2008, a reasonable income is returned to the common good fund for properties used by general fund services
7. Continue to attempt to identify common areas, from all sources, for inclusion in the Council's asset register
<b>Source:</b> Paper presented to Land and Property Sub-Committee April 2008

- 42 As part of our 2007/08 audit, we also noted the following in relation to the Council's administration of common good funds:

- St Magnus Cathedral was constructed approximately 300 years before the Royal Burgh of Kirkwall (predecessor of the common good) was established in the 1400s. The Council's balance sheet shows £2.2 million of capitalised expenditure in relation to St Magnus Cathedral. No sums are currently recorded in the common good balance sheet. As noted below, the Council are required to have a complete asset register in place by 31 March 2009 for all common good assets. It is essential that in meeting this deadline the ownership of St Magnus Cathedral is clarified and the accounting records reflect these findings. This may result in a change in the way asset expenditure on St Magnus Cathedral is reflected in the financial statements. It is essential that the respective responsibilities of the Council and common good in relation to St Magnus Cathedral are formalised.

**Action Plan Point 4**

- 43 In 2007 LASAAC issued a guidance note for practitioners on accounting for the common good fund. It is the intention that this guidance should be implemented by all local authorities in 2007/08. Transitional arrangements outlined in the guidance, however, suggest the introduction of an asset register by 31 March 2009 (see below).

<b>Accounting for Common Good – implementation of LASAAC guidance</b>	
<b>Action</b>	<b>Timescale</b>
Full application of Accounting Guidance	2007/08
Review of Asset Register Arrangements	April 2008 – March 2009
Introduction of Asset Register	31 March 2009

44 Orkney Islands Council has made reasonable progress in implementing this guidance. The Council has complied with the accounting guidance in 2007/08 and, as highlighted above, the Council has committed to reviewing and updating the common good asset register. Over the next year, we will continue to monitor progress made by the Council in implementing these arrangements.

### **Charitable Trusts**

45 Orkney Islands Council currently administers approximately 45 charitable trust funds covering the whole of Orkney Islands.

46 The Charity Accounts (Scotland) Regulations 2006 require charities registered with the Office of the Scottish Charity Regulator (OSCR) to prepare financial statements from 2006/07 and for them to be audited (subject to de minimis levels). Discussions have been ongoing between the CIPFA Directors of Finance Section and OSCR to agree a way forward for charities where a local authority is the sole trustee.

47 For 2007/08 reliance is placed on the local authority SORP, which requires authorities to disclose details of the nature and amount of trust funds where they are sole trustees. OSCR has also requested the following information, as a minimum:

- The differentiation between charitable and non-charitable bodies
- More governance information
- Outline of purpose and activities

48 We understand the Council has arrangements in place to prepare the minimum required information for OSCR in 2007/08. Going forward however we would encourage the Council to review and consider the provisions available to them within the appropriate regulations regarding reorganisation of its charitable trusts.

***Action Plan Point 5***

### **Efficiency**

49 The efficiencies included in the Council's 2007/08 Efficiency Statements are detailed in the table below:

<b>Efficiencies included in Orkney Islands Council's 2007/08 Efficiency Statement</b>			
	<b>Cashable (£'000)</b>	<b>Non Cashable (£'000)</b>	<b>Total (£'000)</b>
Procurement	22	0	22
Asset Management	320	18	338
Managing Absence	50	0	50
Other	0	770	770
<b>Total efficiencies</b>	<b>392</b>	<b>788</b>	<b>1180</b>

50 The Council's Finance Working Group, as a sub committee of the Policy and Resources Committee, oversees the development of the Council's budget strategy and the achievement of efficiency targets. The majority of the efficiency savings realised are achieved through the service planning process and led by the respective Heads of Service. Service committees have a responsibility to review these processes.

## **Joint Working**

51 Orkney Council is committed to working jointly with NHS Orkney and other partner organisations to deliver better and more efficient and sustainable services in Orkney. As part of this commitment the Council and NHS Orkney have been involved in some sharing of support services over a number of years. The benefits of such a sharing of services are that:

- economies of scale can be delivered
- sustainable services can be maintained and delivered within Orkney
- the recruitment and retention of public sector staff in Orkney should be easier

52 It has however been recognised that there would be further benefits in extending the fairly limited shared services working arrangements currently in place. An Orkney Public Sector Reform Programme Board has therefore been established which comprises the Council Convenor, NHS Board Chair and representatives from the Improvement Service and Scottish Government to take overall governance responsibility for a joint working programme. The joint working programme was funded by a Scottish Government revenue grant of £580,000 covering 2007/08 and 2008/09.

53 In June 2008 the Public Sector Reform Programme Board recommended to the Council and NHS Orkney that they explore the formation of a Special Purpose Vehicle (SPV) in the form of a limited company wholly owned by the Council and NHS Orkney to provide a wide range of support services for both organisations. They also requested that a business plan setting out proposals for the management, governance and operation of the SPV be drawn up. The Council and NHS Orkney agreed to these recommendations



- 54 The proposal currently being considered is that the SPV would include within its scope human resources, information services, hotel services, procurement, property management and maintenance, internal communications, public health, internal audit and committee administration. The preference of both the Council and NHS Orkney is that finance is also included within the scope of the company's activities.
- 55 A number of important issues have arisen in considering the viability of operating shared services through an SPV:
- Whether legal powers exist for NHS Boards to form an SPV
  - The extent to which exemptions from EU tendering requirements can be achieved on the transfer of services from public sector bodies to an SPV
  - The VAT status of an SPV. Whilst setting the SPV up as a limited partnership would have some tax advantages, NHS bodies do not appear to have the power to participate in such a limited partnership and therefore a limited company structure is the only option
  - Whether finance should be included within the scope of activities and if so what role would the section 95 officer of the Council take in relation to the activities of the SPV
  - Audit implications arising from such a structure being put in place
- 56 The business plan is currently being drawn up by the Council and NHS Board and this will address the issues raised above. Meetings have also been held recently with Scottish Ministers to agree an approach to some of these issues. These meetings have confirmed that shared financial services could be included within the scope of the SPV and that the principal of a shared post of Director of Finance between the Council and NHS Orkney may be reviewed in the future.
- 57 If following the submission of a business plan, the decision is taken by the Council to proceed with an SPV covering the services identified above there will be a period of staff consultation, service reviews, drafting service level agreements and set up of the SPV. The provisional timetable for progressing with this important initiative is for the SPV to start-up in April 2009 and service redesigns to be carried out during 2009-2011.
- 58 As auditors of the Council we will continue to monitor and report on the progress being made with this innovative approach to shared services.

## **Workforce Management**

### *Workforce Strategies*

- 59 Orkney Islands Council has recognised that it must improve the way it delivers its personnel services. The service has historically been focussed on the delivery of operational activities and has not sought to provide a strategic overview for the Council. The Council has sought to develop its workforce planning and management arrangements and is now beginning to roll this work out across the Council. The Council has recently appointed a joint head of personnel with NHS Orkney, with the aim of providing a joint personnel function. It is important that the Council

seeks to establish a strategic overview of personnel or the benefits of this joint post will not be fully realised.

**Action Plan Point 6**

- 60 As part of its review of workforce management arrangements the Council has committed to launch a staff appraisal project in late 2008 with all staff to have an appraisal and a personal development plan in place by 2010. A staff survey is also to be carried out in early 2009. In addition to these arrangements the Council has recognised the need to develop a systematic appraisal of its Corporate Management Team. Appraisal sessions of all CMT members have been carried out by the Chief Executive and the Council will use these meetings to identify individual and team development needs.
- 61 Due to retirements and senior staff leaving the Council there will soon be a number of vacancies at senior management level. The Council has historically struggled with recruiting to middle management posts and therefore the loss of senior posts may present difficulties for the Council. The Council has introduced schemes to develop and grow future managers from within internal staff but there is limited evidence of succession planning being in place for senior management posts.

**Action Plan Point 7**

*Absence Management*

- 62 The Council approved an absence management policy in 2005 but has not yet established a robust mechanism for providing absence data to line managers to allow them to effectively monitor absence. Previous SPI figures for sickness absence figures have been unreliable. For 2007/08 the SPI has now been assessed as reliable and absence figures for chief officers and local government employees were reported as 6.0% and 3.9% for teaching staff. Orkney Islands Council has yet to agree an improvement target for sickness absence levels but officer recommendation is a level of 4%. This therefore clearly indicates that there are savings which can be made by the Council through significantly reducing absence.

**Action Plan Point 8**

*Modernising Employment*

- 63 The single status agreement between local government employers and trade unions was introduced in 1997 and involves merging the pay and working arrangements for APT&C and manual employees. The agreement gives Orkney Islands Council the opportunity to review existing policies and employment arrangements to bring to an end outdated working practices, while complying with equal pay requirements.
- 64 In 2006/07 we reported that during the year the Council had made payment for all amounts due under equal pay legislation. These payments covered all liabilities due in the period to 31 March 2007. In 2007/08 the Council finalised a single status agreement which took effect from 1 April 2007. All Council employees signed up to the single status agreement and a £1.1m provision was included in the financial statements at 31 March 2008 to cover single status payments due from 1 April 2007. Most of the payments due were subsequently made in July 2008.

## **Asset Management**

- 65 The Council's asset management arrangements are underdeveloped. The Council has recognised that a considerable amount of work still needs to be done to actively ensure that all assets are properly documented and asset management plans are produced.
- 66 The Corporate Property Division, part of Technical Services, is responsible for strategic property management. Following a recent restructuring, an asset management surveyor has been appointed. It is the intention that this role will develop into an asset management co-ordinator for the Council.
- 67 The Council does not currently have a clear and overarching asset management strategy which links to asset plans for services. This has however been identified as a priority in the development of its audit improvement plan (following the Audit of Best Value and Community Planning).
- 68 The balance sheet shows that Orkney Islands Council's portfolio of tangible fixed assets was valued at over £213 million as at 31 March 2008. During the course of our audit we carried out detailed testing to determine whether the assets of the Council were fairly presented and accounted for in accordance with the SORP. We identified a number of weaknesses in Orkney Islands Council's approach to fixed asset accounting which we have incorporated into this report's action plan.

***Action Plan Point 9-12***

## **Procurement**

- 69 The Council's procurement arrangements do not currently meet any of the key points of good practice identified within the McClelland report. This weakness is acknowledged by the Council and the Council's joint bid with NHS Orkney to the Efficient Government Fund includes the proposal to buy central supplies and services through a joint procurement arrangement.
- 70 The Council has however recently appointed a procurement manager. This is considered to be the first step in developing the Council's overall procurement practices.

## **Future Outlook**

- 71 In 2008 the CIPFA/LASAAC local authority SORP board confirmed that from 2010/11 all local authority accounts will be prepared in accordance with International Financial Reporting Standards (IFRS). This change will bring local government into line with other UK public sector bodies. We recommend that the Council takes early steps to assess the financial implications of applying IFRS within its annual accounts together with the system and procedures changes that will be necessary to deal with the new accounting requirements.

***Action Plan Point 13***

- 72 At the same time as there are changes across the UK to financial reporting, in Scotland the establishment of a Scottish Futures Trust will potentially allow a greater opportunity for joined-up public sector action in infrastructure planning and the delivery and development of individual programmes in partnership with other public organisations. As one of its early tasks, the Scottish Futures Trust will be developing national strategies for the delivery and funding of schools, housing, waste and flood defences. It is important that Orkney Islands Council is ready to respond to the development of these strategies.

# Performance

## Introduction

73 Local authorities have a statutory duty to make arrangements to secure Best Value, which is defined as continuous improvement in the performance of functions. In securing Best Value, local authorities are required to maintain a balance of quality and cost considerations and must have regard, among other things, to economy, efficiency and effectiveness and the need to meet equal opportunity requirements and contribute to the achievement of sustainable development. Local authorities also have a duty to undertake effective community planning.

74 This section of the report summarises the Council's performance in the following areas:

- The Audit of Best Value and Community Planning
- Performance Management
- Statutory Performance Indicators
- National Audit Scotland reports

and also comments on the Concordat between the Scottish Government and COSLA.

## The Audit of Best Value and Community Planning

75 During 2007/08, Audit Scotland undertook a Best Value and Community Planning review of Orkney Islands Council. The review was undertaken on behalf of the Accounts Commission and was carried out to assess the extent to which the Council was meeting its duties under the Local Government (Scotland) Act 2003.

76 The findings from the review were published in June 2008. In general the Accounts Commission recognised the particular challenges facing the Council as a result of its remote and dispersed geography. The report acknowledged the strength of the Council's leadership, its performance in certain areas and the partnership and joint working arrangements operating with NHS Orkney and Orkney's community councils. The Commission were however critical of the inability of the Council to demonstrate that it was providing Best Value for the people of Orkney. In particular they commented that:

- The Council needs to adopt innovative approaches to building capacity, particularly to support corporate functions
- There is a need for effective corporate performance management arrangements
- Community and corporate plans needed to be supported by clear action plans with specific, measurable targets and milestone dates
- A number of the basic systems and processes to support the delivery and demonstration of Best Value were not in place

- The benchmarking of performance with other island councils should be extended to a wider range of councils to enable benefits to be achieved from best practice elsewhere in Scotland.

77 Following the publication of the report in July 2008 the Council authorised the preparation of an improvement plan in response to the Accounts Commission findings. The plan contains an improvement agenda with nine key areas

<b>Audit Improvement Plan – Key Areas</b>
1. Develop a detailed programme with targets and timescales to support the council's improvement agenda
2. Work with partners to develop a strategy to address skills gaps through a structured training and development programme and by identifying where additional temporary capacity would be appropriate
3. Ensure that the new corporate plan contains clear targets and measures of success and is supported by a detailed action plan to support the delivery of key objectives
4. Establish an effective corporate performance management system with measures of cost and quality across the range of council services, including measures of the cost and impact of sustaining fragile communities
5. Develop the role of elected members in leading Best Value, in particular through improving the scrutiny of performance
6. Develop the role of the CMT in providing strategic leadership and monitoring and driving performance improvement
7. Develop strategic resource management to ensure resources, including finance, assets, workforce and ICT are focused on delivering key priorities
8. Increase the level of challenge to existing ways of doing things to ensure that services provide best value and are designed around the needs of users
9. With Community Planning partners establish a corporate set of performance management arrangements to establish a monitoring framework for strategic objectives, ensuring that each partner's contribution is clearly specified and measured
<i>Source: Orkney Islands Council Audit of Best Value and Community Planning – audit improvement plan</i>

78 The improvement plan is supported by detailed action points. Lead officers and members have been identified as responsible for each action point and timescales have been assigned as have quantifiable improvement targets and monitoring arrangements.

79 The improvement plan which was submitted to the Policy and Resources Committee on 23 September 2008 and is to be made available to members of the Accounts Commission who visit the Council on 29 September 2008, is subject to final ratification at the general meeting of the Council on 2 October 2008. It is then the intention to incorporate improvement plan actions within Corporate and Service Improvement Plans.

80 Over the next three years of our audit appointment we will monitor the progress of the Council in addressing the Best Value review findings. The outcome of this monitoring will be reported in future annual audit reports.

### **Concordat between the Scottish Government and COSLA**

81 In November 2007 the Scottish Government and COSLA agreed a Concordat which set out a new relationship between the Scottish Government and local authorities. This new relationship was represented by a package of measures which was underpinned by an agreement on funding for local government over the period 2008/09 to 2010/11.

82 One of the critical measures outlined in the Concordat was the agreement to develop a Single Outcome Agreement which would be agreed between each Council and the Scottish Government, based on 15 key national outcomes.

83 Within Orkney the Single Outcome Agreement (SOA) was developed as a Council only agreement with the Scottish Government and covered the priorities set out in the Council's corporate strategic plan 2008 – 2013. The SOA for 2009/11 will include the outcomes and relevant indicators of other stakeholders involved in the Orkney Community Planning Partnership (OCP).

84 The 2008/11 Orkney SOA was submitted in draft to the Council's Policy and Resources Committee on 15 April 2008. In May the Council held meetings with Committee Chairs and Directors and also invited elected members to a seminar providing them with the opportunity to engage with the SOA in detail. These meetings provided input regarding clearer inclusion of the Council's priorities as outlined in the Council's corporate strategic plan. In addition to this the OCPP Steering Group also considered the Council's SOA and agreed in principle to the content. The Council delegated power to the Policy and Resources Committee to approve the SOA which it duly did on 24 June 2008.

85 The SOA identified local outcomes and relevant indicators for each of the 15 national outcomes contained within the Concordat. There are 74 relevant indicators included in Orkney's SOA covering all of the national outcomes. The extent of indicators supporting each outcome varies from 2 to 10. Orkney Islands Council will be looking to engage with the OCPP during 2008/09 to establish procedures regarding future governance and accountability arrangements so that future joint SOA's will be more robust and deliverable. We support this intention and would recommend that consideration is given to the following areas:

- Future performance reporting to members of progress against the SOA indicators should be consistent and complimentary to the performance management arrangements being put in place as part of the response to the Best Value and Community Planning Audit. These arrangements are set out in the audit improvement plan.

- In 2009/11 when the contribution from other community partners towards the achievement of the national outcomes is included, it will be important that the definition of indicators and the targets used are consistent across partners.
- It is important that future financial budgets are capable of being mapped against SOA priorities to show how funds are being used against particular outcomes.

**Action Plan Point 14**

- 86 Over the next year we will be reviewing the development of the Orkney SOA and assessing the extent to which it is contributing to improved performance reporting and accountability.

## **Performance Management**

- 87 The Best Value audit identified the Council's performance management arrangements as weak and an area where the Council should make significant changes to enable it to achieve continuous improvement. The Council did not have a structured performance management framework which measured and monitored progress against objectives. The Council has developed a balanced scorecard approach and is now embedding a consistent approach across all scorecards.
- 88 An updated performance management system was approved by the Council's Monitoring and Audit Committee in August 2008. Alongside this work updated balanced scorecards for Council departments are being prepared and should be presented to the elected members' seminar in September 2008. The CMT approved nine cross-Council generic indicators in May 2008. The Council has committed to embed these indicators in departmental balanced scorecards by March 2009.

## **Statutory Performance Indicators**

- 89 The Local Government Act 1992 set out the requirement for councils to prepare and publish performance indicators. In meeting this duty, Orkney Islands Council must ensure that it:
- establishes systems and procedures to ensure that the required information is gathered;
  - undertakes checks to ensure that, as far as practicable, the information gathered for publication is accurate and complete;
  - arranges to keep all working papers and any other sources which may be examined by appointed auditors, and is able to make these available on request; and
  - maintains a publicly available record of the reported information.
- 90 As external auditors we have a statutory duty to ensure that the Council has made such arrangements for collecting, recording and publishing statutory performance indicators by reviewing and examining evidence that is relevant to these arrangements in accordance with guidance issued by Audit Scotland.



- 91 Our audit of the performance indicators found that services were well organised and on the whole produced reasonable working papers within the requested timescales.
- 92 The table below summarises the results of our audit on Orkney Islands Council's Statutory Performance Indicators (SPI's) for 2007/08:

#### Summary of SPI Assessment

	Number of SPI's assessed	Rating of Assessed SPI's			
		Reliable	Unreliable	Failed to Report	No Service
<b>Orkney Islands Council</b>	56	54	0	1	1
No Service: relates to traffic light repairs.					

- 93 The Council failed to report on one of the roads and lighting indicators (the percentage of council bridges assessed that failed to meet the European standard of 40 tonnes). Orkney Islands Council provides data to enable an external consultant to carry out the assessment of bridges in the area. In accordance with the SPI guidance this measurement should take place at the end of the reporting year. In 2007/08, the Council failed to ensure that the process was complete prior to the end of the financial year.

#### **Action Plan Point 15**

- 94 One Adult Social Work indicator has also not been reported. This is because the Council is unable to report information on this indicator in line with other Scottish local authorities.
- 95 On an annual basis Audit Scotland provides a data compendium of all statutory performance indicators. For each indicator councils are ranked in order of performance. Based on the most recent national published information (2006/07), Orkney Islands Council was in the top quartile for 25 of the indicators and in the lower quartile for 21 of the indicators. Whilst there appears to be some improvements in the performance of certain indicators in 2007/08, the level of performance in others would suggest that for these indicators, Orkney Islands Council may still be positioned behind most local authorities. It is important that the appropriate committees challenge and manage the performance in these areas once national performance information is published.

#### **Action Plan Point 16**

### **Value for Money and other Inspection Reports**

#### *Social Work Inspection Agency*

- 96 In 2006 the Social Work Inspection Agency (SWIA) undertook an inspection of all social work and social care services provided by the Department of Community Social Services. A follow up inspection was carried out in March 2008. The follow up inspection noted that the Council has

made significant progress in most areas with many of the recommendations made having been fully addressed and evidence that others were being acted upon.

#### *Housing Benefit Review*

97 In previous years responsibility for inspecting housing benefits was the remit of the Benefit Fraud Inspectorate. On 1 April 2008 Audit Scotland took on these responsibilities which have been integrated with the current benefits audit that is undertaken by local auditors. The work that is now being undertaken by the Housing Benefit Review team considers whether local authorities are complying with their statutory responsibility to continuously improve their benefits service. This move is also reflected by the move from prescriptive DWP Performance Standards to the overarching 'Right Benefit, Right Time' indicators that have been in place since 1 April 2008.

98 Orkney Islands Council was one of the first local authorities to be reviewed under the new regime. The review took place in August 2008 and a final report is expected to be published soon. The emerging findings from the review were generally positive and note the excellent level of performance processing that is in place at the Council as well as the comprehensive quality checking regime. However, some areas with scope for improvement were noted including the following:

- Housing benefit information could be improved on the Council website
- Reporting of performance to service directors and members
- No SLA in place with debt recovery partner

99 We will continue to monitor the progress the council makes against the recommended actions in the Audit Scotland report.

#### *Audit Scotland Reports*

100 Throughout the year Audit Scotland has published reports and updates on issues across Scotland. The following table is a summary of the reports published during the year, when they were published, which Council committee they were presented to and when.

<b>Report</b>	<b>Date Published</b>	<b>Presented to</b>	<b>Date Presented</b>
National Fraud Initiative	May 2008	Monitoring and Audit Committee	19 June 2008
Improving the School Estate	March 2008	Monitoring and Audit Committee	8 May 2008
Sustainable Waste Management	September 2007	Monitoring and Audit Committee	11 October 2007
Dealing with Offending by Young People: Performance Update	August 2007	Dealt with internally by relevant Departments	September 2007
VFM in Public Sector Corporate Services	May 2007	Monitoring and Audit Committee - as annex to Crerar update	13 December 2007

## **Future Outlook**

101 Changes to the audit, inspection and regulatory arrangements are anticipated in future years and these will impact on the Council. The Crerar report on the independent review of regulation, audit, inspection and complaints handling of public services in Scotland was published in September 2007 and contained a series of recommendations designed to streamline the scrutiny landscape in Scotland. In their response to the Crerar report in June 2008, Scottish Ministers asked the Accounts Commission to put in place arrangements to reduce the burden of scrutiny for local authorities by establishing a single audit framework. A more co-ordinated approach to the audit and inspection regime is anticipated in the future.

# Governance

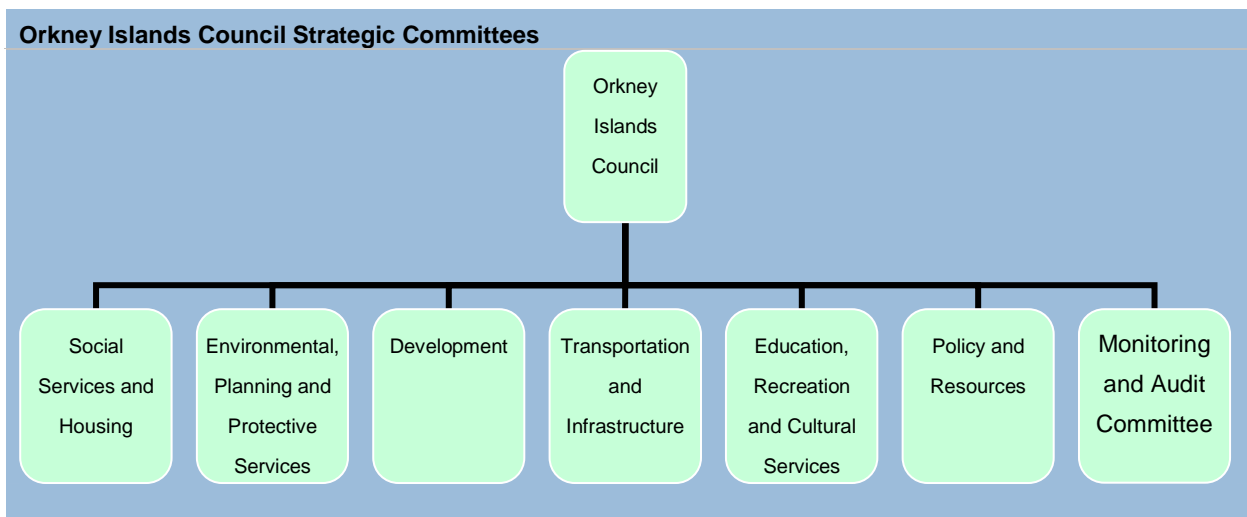
## Introduction

102 Corporate governance is concerned with the structures and processes for decision-making, accountability, control and behaviour at the higher levels of organisations. Through the chief executive and other statutory officers, Orkney Islands Council is responsible for ensuring the proper conduct of its affairs including compliance with relevant guidance, the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements.

103 This section sets out the main findings from our review of Orkney Islands Council's corporate governance arrangements.

## Political Governance

104 Orkney Islands Council recognised that the 2007 local government elections provided the Council with a clear opportunity to review its current structures and protocol arrangements. The political governance structure within the Council was reviewed in February 2007 prior to the elections. A committee based structure was retained with seven committees covering all the main services within the Council (see below). A cycle of meetings involving each of the committees takes place five times a year. Once a cycle has been completed, a meeting of the full council is held. All 21 councillors take part and make final decisions on the recommendations made by the committees.



## Multi-member ward arrangements

105 The 2007 local government elections saw the introduction of proportional representation and multi-member wards to local government. There was a high turnover of elected members within the Council with nearly 50% of councillors being new members. Orkney Islands Council has

seen very little change following the introduction of multi-member wards to local government. Members continue to work together for their local areas and the Council has received no indication from councillors or constituents that there have been any instances of work not being undertaken. Officers within the Council intend to carry out a survey of members to establish what, if any, impact the move to multi-member wards has had in respect of member workload or in the management of constituency business

- 106 The Council is currently reviewing its management structure with a view to reviewing the impact of this on the committee structure. The Council is keen to use the experiences of members working within the new multi-member wards to identify how the new structures can effectively support multi-member working.

### **Scrutiny arrangements**

- 107 A Council must be able to effectively scrutinise the actions of the leadership or Executive and hold it to account for its performance.
- 108 The Leadership Advisory Panel's Report on "Scottish Local Government's Political Management Structures" recognised that Council members enjoyed a strong culture of speaking out on issues in committee and challenging decisions or proposals. However, notwithstanding this they recommended taking scrutiny out of the committee structure and establishing a separate scrutiny group with its own corporate identity, formal work programme and remit. The report stressed that scrutiny should go wider than pure audit and Best Value. It should be about reviewing the performance of the Council in terms of service delivery; the processes by which policy decisions have been taken; the substance of a particular policy and how it fits with the overall objectives of the Council and the effectiveness of a policy in terms of implementation.
- 109 The recent Best Value report identified that whilst elected members at Orkney Islands Council are engaged in scrutinising strategic decisions and individual projects, scrutiny of service performance is significantly underdeveloped. This is partly attributable to the absence of good performance information (see paragraph 87). A key improvement area within the Council's audit improvement plan is the development of the role of elected members in Best Value and in particular improving scrutiny of performance. Targets for improvement have been established to be implemented during 2008/09, including the review of performance monitoring reports at committee and an overall review of the content of committee reports.

### **Elected Member Training**

- 110 Orkney Islands Council recognised that the 2007 local government elections would result in a significant turnover in elected members. In advance of the elections the Council began a work programme which would enable elected members to become equipped to effectively serve office.
- 111 Following the elections the Council held a series of structured training sessions on a range of issues. Specific training was provided for elected members in enhanced posts including

sessions for members of the Monitoring and Audit Committee and members of the Licensing Board.

- 112 A survey has since been held with elected members to identify training needs. A training programme is to be developed as a result. The Council is currently reviewing options for delivering a training programme including e-learning for those elected members on remote islands. The draft Chief Executive's service improvement plan includes a commitment to deliver a training programme for elected members.

### **Audit Committee Principles**

- 113 Audit Committees are increasingly viewed as a critical component in the overall corporate governance process. As part of our review of the Council's corporate governance arrangements we assessed the effectiveness of the audit committee arrangements in place within the Council. In doing this we considered the audit committee arrangements against publications which illustrate best practice. These included:

- Audit Committee Principles in Local Authorities in Scotland – a Guidance Note (CIPFA)
- Audit Committees – Practical Guidance for Local Authorities (CIPFA)
- The Smith Report

- 114 Overall we concluded that Orkney Islands Council's arrangements were largely able to deliver the audit committee principles set out in the CIPFA guidance and have had a positive impact on the Council's overall corporate governance framework. There were however a number of areas for scope for improvement. These included:

- **Terms of Reference:** The Monitoring and Audit Committee had yet to review its terms of reference against the model terms of reference published by CIPFA
- **Risk Management:** Due to the progress of the Council in implementing risk management arrangements, the Monitoring and Audit Committee had failed to provide sufficient challenge and/or review of the Council's risk management arrangements.
- **Annual Review:** Best practice recommends that an audit committee conduct an annual review of their work (*The Smith Report*). We recommended that the Monitoring and Audit Committee carry out an annual review.
- **Internal Audit:** The Monitoring and Audit Committee does not currently receive an annual report from Internal Audit. Whilst such a report is prepared it is only presented to the Director of Finance and Housing.

- 115 The Council has committed to implementing these recommendations over the coming year.

### **Statement on the System of Internal Financial Control**

- 116 Local authorities are required to include within their statement of accounts a statement on the system of internal financial control. This statement sets out the framework within which financial control is managed and reviewed and the main components of the system including the

arrangements for internal audit. Where the authority is in a group relationship with other entities and undertakes significant activities through the group these activities should be encompassed within the statement of internal financial control.

- 117 Orkney Islands Council has published a group statement on the system of internal financial control within the 2007/08 statement of accounts. The statement provides an overview of the key elements of the Council and its group governance arrangements and systems of internal financial control.
- 118 As part of our audit work we are required to review the information disclosed in the statement on the system of internal financial control and assess whether the Council's opinion on the effectiveness of its internal financial controls is consistent with our understanding of the Council's internal financial control framework. To inform our understanding of the Council's system of internal financial control we carried out a review of a number of specific areas during our 2007/2008 audit. Our assessment of the Council's corporate governance arrangements included consideration of the authority's risk management system and its mechanism for the prevention and detection of fraud. We also carried out systems reviews of the following systems at Orkney Islands Council:
- Housing and Council Tax Benefits
  - Members Allowances
  - Non Domestic Rates
  - Payroll
  - Purchases
- 119 Overall we found the systems of internal financial control reviewed to be of a good standard with controls operating at an adequate or effective level.
- 120 The Council's review of the effectiveness of the system of internal financial control procedures is informed by the views of the Chief Internal Auditor and the managers within the group entity. The results of this work allowed the Council to conclude that the system of internal financial control was largely effective.
- 121 Overall we concluded that the Council's statement on the system of internal financial control is consistent with our knowledge and understanding of the financial control framework operating at the Council.

## **Delivering good governance in Local Government**

- 122 In 2007 CIPFA/SOLACE published "Delivering Good Governance in Local Government: A Framework". This document revises the governance standards which were first established in 'Corporate Governance in Local Government: A keystone for Community Governance' and builds upon recent governance work, in particular The Good Governance Standard. The six

core principles from The Good Governance Standard have been tailored for local government purposes.

123 The principles and standards set out in the framework are expected to assist authorities in providing stronger leadership for communities. The framework is supported by detailed implementation and evaluation guidance. The guidance notes make a number of recommendations for councils to consider. These include the recommendations that council's should:

- Develop and update their local code to improve its effectiveness
- Review and show evidence of where improvements to the local code are required
- Consider the extent to which the authority complies with the principle elements of good governance set out in the framework

124 We understand that the Council intends to review its local code against this guidance over the coming year.

### **Codes of Conduct**

125 Propriety requires that public business is conducted with fairness and integrity. This includes avoiding personal gain from public business, being even-handed in the appointment of staff, letting contracts based on open competition and avoiding waste and extravagance. In 2007/08, we placed reliance on the work of internal audit in relation to this area. Overall they concluded that controls at Orkney Islands Council are satisfactory in relation to standards of conduct.

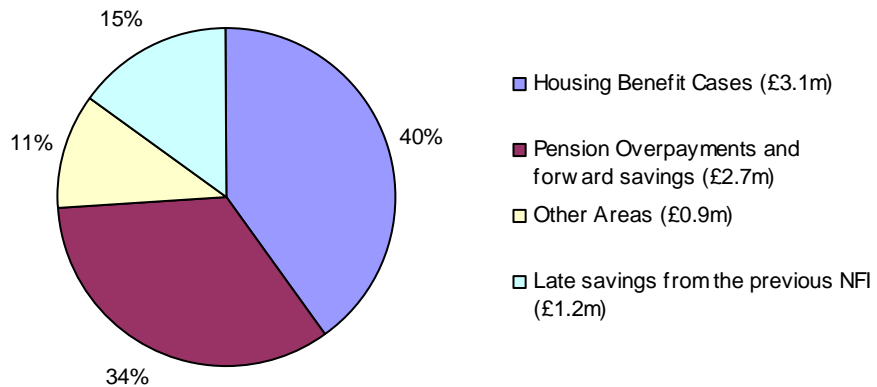
### **Fraud and Irregularity**

126 The integrity of public funds is at all times a matter of concern. As external auditors we are required to consider the arrangements made by management for the prevention and detection of fraud and irregularities. As part of our 2007/08 audit we have placed reliance on the work of internal audit in this area. Overall they concluded that controls at Orkney Islands Council were generally satisfactory to prevent and detect fraud and other irregularities.

### **National Fraud Initiative**

127 The National Fraud Initiative (NFI) in Scotland is an exercise that brings together data from councils, police and fire and rescue boards, health bodies and other agencies, to help identify and prevent a wide range of frauds against the public sector. This has been undertaken as part of the audits of the participating bodies and is completed on a two-yearly basis. During 2006/07 we reported on the outcomes of the NFI at Orkney Islands Council. The chart below shows the final outcomes recorded by Audit Scotland for all local authorities.





Source: Audit Scotland Data

128 The overall savings generated by local authorities as part of NFI totalled £7.9m, down from the £9.7m recorded in the 2004/05 exercise. The main results from NFI 2006/07 included:

- 186 pensions stopped after NFI identified that the pensioner was deceased
- 1,552 housing benefit cases involving public sector pensioners
- 672 housing benefit cases involving public sector employees
- 969 'blue badge' disabled parking permits cancelled after NFI identified that the holder was deceased

129 The totals for Orkney Islands Council in both exercises are as follows:

	Housing Benefit Cases £	Pension Overpayments and Forward Savings £	Other Areas £	Late savings from the previous NFI £	Total £
<b>NFI 2006/07</b>	0	0	0	0	<b>0</b>
<b>NFI 2004/05</b>	2,975	0	0	0	<b>2,975</b>

130 The total savings generated by both exercises are low, which should give assurances that the systems that are in place to prevent and detect fraudulent transactions are generally effective.

## NFI 2008/09

131 The 2008/09 NFI exercise is due to begin in October 2008. This will involve the capturing of data by all public sector bodies and uploading them to a secure website operated by the Audit Commission. We are pleased to note that the Council has taken appropriate steps to ensure that this deadline is met and that action points we have raised during the 2006/07 exercise are being considered. We will continue to monitor and report on the progress made by the Council during 2008/09.

## **Risk Management**

- 132 An important feature of a robust system of internal control is a developed and integrated approach to risk management. Effective risk management will deliver an appropriate balance between risk and control, more effective decision making, better use of limited resources and greater innovation. Overall we found that the Council has made progress in implementing risk management arrangements. In 2006/07 we raised a number of recommendations to assist the Council in developing its risk management arrangements. At the time of our review, the Council was seeking external advice to support the development of its risk management arrangements. It was agreed our recommendations would be implemented through the external support provided.
- 133 The Council subsequently appointed Zurich Municipal to assist in the development of a risk register. A series of workshops have been conducted with key strategic officers. These workshops have enabled the Council to identify the key issues and risks impacting on its work but also to identify the risks which are specific to a department and those which are of key strategic concern to the Council.
- 134 The Council has made steps in developing a risk register, and is currently embedding risk management into every day practices through corporate and departmental action planning. The corporate risk register will be presented to the Council's Policy and Resources Committee on 23<sup>rd</sup> September along with a sample of the action plans created to manage the identified risks.
- 135 As part of our corporate governance review we raised a number of recommendations to assist the Council in developing its risk management arrangements. We will monitor the Council's progress in implementing these recommendations over the coming year.

## **Internal Audit**

- 136 During the course of our audit we carry out an assessment of the internal audit function to assess its effectiveness and ascertain whether specific areas of internal audit work can be relied upon to inform the external audit of the Council's financial statements. As part of our review we also assess the Council's internal audit function against the standards set out in The Code of Practice for Internal Audit in Local Government in the United Kingdom.
- 137 Our review concluded that the Council maintains an effective internal audit function and is fully compliant across many of the Code's requirements. We were able to rely on the work of internal audit during 2007/08 in the following areas:
- Creditors
  - Payroll
  - Standards of Conduct
  - Fraud and Irregularity

- Housing Rents
- Council Tax
- Sundry Income
- Nominal Ledger
- Treasury Management
- Pensions

## **Community Planning and Partnership Working**

- 138 The Community Planning Partnership is led by a Steering Group with membership from Orkney's principal agencies; Orkney Islands Council, NHS Orkney, Highlands and Islands Enterprise, Northern Constabulary and Voluntary Action Orkney. The Council is represented on the Steering Group by the Convener, Vice Convener and the Chief Executive.
- 139 A wide range of other agencies, and community and voluntary sector organisations also belong to thematic partnership groups, each of which takes the lead in progressing relevant parts of the community plan. The chairs of these thematic groups meet as the Partnership Liaison Group (PLG) to provide a forum for liaison between different themes. The chair of the PLG also sits on the Steering Group, enabling a channel of communication between the thematic group and Steering Group.
- 140 The recent Audit of Best Value and Community Planning reported that the Council works well with its partners. The partnership published its second community plan in May 2007, covering the period 2007 to 2020. The partners recognise the importance of Community Planning and joint working in maintaining sustainable services for Orkney. The best value audit did however note that the Community Planning Partnership is unable to demonstrate progress against its objectives as much of its activity is not systematically measured and reported. The Council has committed to improving this within its audit improvement plan.
- 141 The SOA for 2009/11 will include the outcomes and relevant indicators of other stakeholders involved in the Orkney Community Planning Partnership. In the coming years there will therefore be a need to ensure that the partnership reports consistently and effectively against the new Single Outcome Agreement. It is essential that lines of reporting and monitoring are clear and transparent across the partnership given the additional reporting requirements needed for the outcome agreement.

*Action Plan Point 17*

## **Following the Public Pound**

- 142 Councils fund arms-length and external organisations (ALEOs) for a range of purposes related to council services and their broader objectives. These arrangements are often more complex than standard purchase contracts for goods or services and are usually designed to deliver wider public benefits. They involve the transfer of public funds from the direct control of a council to the control of an ALEO. In practice these can range from relatively small grants to voluntary organisations and small community organisations, to payments to trusts set up by councils to

manage all of their leisure facilities. A council may make a fixed payment to an ALEO, or the ALEO may have the power to commit council funds.

- 143 To ensure that public funds are used properly, to maintain accountability, and to ensure that value for money is secured, it must be possible to trace the funds from the point at which they leave the council to the point at which they are ultimately spent by the receiving organisation. In other words, it is important to be able to 'follow the public pound' across organisational boundaries.
- 144 During 2007/08 we carried out a review to establish the extent to which Orkney Islands Council has embraced the principles set of in the Code. In doing this we:
- Considered the work of internal audit in this area;
  - Reviewed the local procedures in place and obtained an overview of the following the public pound arrangements at Orkney Islands Council; and
  - Selected a sample of organisations in receipt of funding from the Council and reviewed the funding arrangements to ensure compliance with Council procedures and the Code in general.
- 145 An internal audit review carried out in 2006/07 found that whilst the Council had complied with, and implemented many of the requirements of the Code, improvements were necessary with respect to the monitoring arrangements of funding agreements. The findings of our review supported these conclusions.
- 146 Our review noted that at the time the Council received limited or no performance monitoring information from ALEOs other than through member or officer representation. In addition exit strategies had not been established for the sample of arrangements we reviewed.
- 147 We raised a number of recommendations during our review which have either been implemented or are to be implemented over the coming year.

# Action Plan

Our action plan details the significant weaknesses and opportunities for improvement that we have identified during our final audit visit. Significant weaknesses are defined as high risk, material observations which require immediate action.

It should be noted that the weaknesses identified in this report are only those that have come to our attention during the course of our normal audit work. The audit cannot be expected to detect all errors, weaknesses or opportunities for improvements in management arrangements that may exist.

<b>Action Plan Point</b>	<b>Paragraph Reference</b>	<b>Recommendation</b>	<b>Responsible Officer</b>	<b>Management Comments</b>	<b>Agreed Completion Date</b>
1	13	The Council should ensure arrangements are in place to ensure recharges to and from services are excluded from the financial statements.	Asst Director of Finance and Housing (Accountancy)	Procedures for raising internal recharges to be reviewed in light of the SORP accounting requirements.	June 2009
2	27	With a challenging capital programme over the coming years, the Council should ensure arrangements are in place to minimise slippage of capital expenditure.	Director of Finance and Housing	Commitment from CMT to review capital project appraisal process management and reporting arrangements	June 2009
3	33	We would encourage the Council to request that its subsidiaries prepare full financial statements and do not take advantage of any exemptions or reduced disclosure opportunities.	Asst Director of Finance and Housing (Accountancy)	A further reminder will be issued and followed up with a meeting if required	December 2008
4	42	In working towards the implementation of LASAAC guidance on Common Good, the Council should ensure ownership of St Magnus Cathedral is clarified and that the accounting records reflect these findings.  It is also essential that the respective responsibilities of the Council and common good in relation to St Magnus Cathedral are formalised.	Head of Legal Services/Director of Finance and Housing	Work in progress	March 2009

<b>Action Plan Point</b>	<b>Paragraph Reference</b>	<b>Recommendation</b>	<b>Responsible Officer</b>	<b>Management Comments</b>	<b>Agreed Completion Date</b>
<b>5</b>	<b>48</b>	We would encourage the Council to review and consider the provisions available to them within the appropriate regulations regarding reorganisation of its charitable trusts.	Head of Legal Services/ Director of Finance and Housing	Currently being reviewed	September 2009
<b>6</b>	<b>59</b>	We recommend the Council develops a personnel strategy which clearly outlines the strategic function of personnel services, defines the expectations of the personnel section and the duties it will perform.	Head of Personnel Services	Plans are in place to prepare a Personnel/HR Strategy. This action is included in the service's Improvement Plan for the year to come.	June 2009
<b>7</b>	<b>61</b>	We recommend that the Council develops succession planning arrangements for senior management posts across the Authority.	Head of Personnel Services	Workforce planning framework and process is to be developed as part of the revision of the personnel strategy outlined above with a specific focus during 09-10. The resultant workforce plan will include proposals for succession planning, increased usage of para -professionals, staffing new care facilities and the potential use of apprentice schemes.	April 2010
<b>8</b>	<b>62</b>	The Council should agree on a Council wide target for sickness absence and	Head of Personnel Services	Report on Sickness Absence Statistics presented to the Personnel Sub-Committee on 4th September confirmed	September 2009

<b>Action Plan Point</b>	<b>Paragraph Reference</b>	<b>Recommendation</b>	<b>Responsible Officer</b>	<b>Management Comments</b>	<b>Agreed Completion Date</b>
		<p>establish monitoring and scrutiny arrangements against this target.</p> <p>To improve absence management levels the Council should identify good practice within other local authorities and whether these can be applied to Orkney Islands Council.</p>		<p>the intention to prepare a strategy and provided members with robust and comprehensive data on current levels of absence.</p>	
<b>9</b>	<b>68</b>	<p>The Council should revisit its approach to accounting for subsequent expenditure on fixed assets to ensure compliance with generally accepted accounting principles.</p> <p>A formal decision should be recorded of any decision taken.</p>	<p>Asst Director of Finance and Housing (Accountancy)</p> <p>Head of Corporate Property</p>	<p>A review of spending plans to be undertaken in advance of capital programme being approved by Council</p>	<p>June 2009</p>
<b>10</b>	<b>68</b>	<p>We recommend that the Council consider implementing component accounting for future capital projects.</p>	<p>Asst Director of Finance and Housing (Accountancy)</p>	<p>To be progressed as part of CPA review</p>	<p>June 2009</p>
<b>11</b>	<b>68</b>	<p>We recommend that future valuations provided by Estates separate out land and building values.</p>	<p>Director of Technical Services</p>	<p>Part of ongoing asset management work</p>	<p>June 2009</p>
<b>12</b>	<b>68</b>	<p>We recommend that the Council make arrangements for locating title deeds and</p>	<p>Head of Legal Services</p>	<p>Plans are in place to address the need for a more managed approach to recording</p>	<p>Review progress September 2009</p>



Action Plan Point	Paragraph Reference	Recommendation	Responsible Officer	Management Comments	Agreed Completion Date
		updating records with regard to Council assets.		deeds against assets	
13	71	We recommend that the Council takes early steps to assess the financial implications of applying IFRS within its annual accounts together with the system and procedures changes that will be necessary to deal with the new accounting requirements.	Asst Director of Finance and Housing (Accountancy)	Detailed accounting requirements to be assessed with action plan prepared	December 2008
14	85	<p>We recommend that consideration is given to the following areas in relation to its SOA:</p> <ul style="list-style-type: none"> <li>• Future performance reporting to members of progress against the SOA indicators should be consistent and complimentary to the performance management arrangements being put in place as part of the response to the Best Value and Community Planning Audit. These arrangements are set out in the Audit Improvement Plan.</li> </ul>	Head of Policy	Performance reporting to members and to Orkney Community Planning Partnership will be consistent with the AIP but must also be consistent with the performance monitoring and reporting guidance due to be issued by the Scottish Government at the end of October 2008.	June 2009 (to be confirmed by Government)

Action Plan Point	Paragraph Reference	Recommendation	Responsible Officer	Management Comments	Agreed Completion Date
		<ul style="list-style-type: none"> <li>In 2009/11 when the contribution from other community partners towards the achievement of the national outcomes is included, it will be important that the definition of indicators and the targets used are consistent across partners.</li> <li>Future financial budgets are capable of being mapped against SOA priorities to show how funds are being used against particular outcomes.</li> </ul>	<p>Head of Policy</p> <p>Director of Finance and Housing</p>	<p>All indicators, data definitions and targets to be used in the joint SOA will be agreed in advance with the relevant partner agencies and thematic groups of Orkney Community Planning Partnership via the Partnership Liaison Group.</p> <p>We can and will do this for the Council but cannot undertake to provide information in this form on behalf of partner agencies.</p>	<p>April 2009</p> <p>April 2009</p>
15	93	The Council should ensure arrangements are in place to ensure all roads and lighting indicators are reported and the information reported in reliable.	Head of Roads	<p>Arrangements are in place to complete data transfer and assessment calculations required to provide previous SPI.</p> <p>Arrangements are also in place for measurements to take place prior to 31 March 2008/09 SPI</p>	<p>January 2009</p> <p>March 2009</p>
16	95	It is important that the appropriate Committees challenge and manage the performance of statutory performance indicators which are in the lower quartile.	Project Manager, Corporate Change and Development	There is an existing requirement through the Performance Management System that SPIs are reported quarterly to departmental management teams and six monthly to the Corporate Management	March 2009

Action Plan Point	Paragraph Reference	Recommendation	Responsible Officer	Management Comments	Agreed Completion Date
				<p>Team on an exception basis. Some SPIs are monitored through the departmental balanced scorecards and monitoring reports will be presented to service committees in Jan/Feb 09 (see Audit Improvement Plan 5.4). The remaining SPIs can also be presented to service committees as part of a broader performance report. This will allow further scrutiny by elected members.</p> <p>Please note that SPIs in the lower quartile are generally unit cost indicators or otherwise influenced by the high cost of providing certain services to island residents.</p>	

Action Plan Point	Paragraph Reference	Recommendation	Responsible Officer	Management Comments	Agreed Completion Date
17	141	We recommend that lines of reporting and monitoring are clear and transparent across the partnership to ensure the additional reporting requirements needed for the outcome agreement are achieved.	Head of Policy	Orkney Community Planning Partnership has a well established Partnership Liaison Group which has undertaken to assist with the collection and dissemination of performance information from/to all partner agencies and thematic groups.	August 2009



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