Shetland Islands Council

The Audit of Best Value and Community Planning

Progress report

Prepared for the Accounts Commission

January 2007

AUDIT SCOTLAND

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. It provides services to the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Executive and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

Commission findings

When the Commission made findings on the Best Value report on Shetland Islands Council in March 2005 we required a further report by the Controller of Audit on the progress made by the council during 2005/6 and on the extent to which the objectives of Shetland's Improvement Plan had been achieved, and we accept this report as fulfilling that requirement. The Commission recognises that the report gives a broad picture of the council's performance based on the work of Audit Scotland and does not attempt a comprehensive review of all service delivery. We acknowledge the cooperation and assistance given to the audit process by members and officers of the council.

The Commission accepts the conclusion of the report that Shetland Islands Council has made a start in addressing the issues raised in the Commission's previous findings. In particular we acknowledge:

- The introduction of a Corporate Improvement Plan and service planning and performance management frameworks.
- Moves towards achieving the longer term ambition of financial sustainability.

We remain concerned, however, about the pace and extent of change as a number of initiatives are relatively recent and are not yet fully established. We wish to place particular emphasis on the need for early improvement in the following areas:

- the development of Community Planning
- clarity of lines of accountability between the council and Trusts.

The Commission welcomes the steps that the council has taken in the direction of establishing better scrutiny processes. We believe, however, that it is essential to have an Audit Committee that is separate from other deliberative and decision-making bodies.

Accordingly we urge the council to increase the pace of change in delivering the Improvement Plan. Progress will be monitored through the annual audit process.

Introduction

The Local Government in Scotland Act 2003 introduced new statutory duties relating to Best Value and Community Planning. The report on the Audit of Best Value and Community Planning undertaken at Shetland Islands Council and the Accounts Commission's findings were published in March 2005.

The report described a council that had been slow to address its statutory duties on Best Value. After many years of economic prosperity, it was in the process of adjusting to changed circumstances. It was still an affluent council, with no loan debt and reserves of around £280 million. However, it recognised that, with income from North Sea oil in decline, it needed to ensure the long-term sustainability of the wide range of services that it provides.

While there was a clear vision of achieving financial sustainability, the council was struggling to translate this into a practical programme of action. A key factor was the high degree of dependency on council services and expectations of continued service growth from the local community. This meant that the necessary changes were likely to generate significant resistance. In turn, councillors showed a marked tendency to represent the interests of their individual wards, at the expense of their wider corporate role for the council and Shetland as a whole.

Furthermore, the lack of progress in establishing Best Value and sound management processes meant that the council was not well placed to meet this challenge. High level strategies were not prioritised and matched to resources. Service plans and targets were not properly established, and as a result, managers and councillors were unable to systematically monitor service performance and identify areas in need of improvement.

The Commission found that there was considerable scope for improvement in the management and leadership of the council and the internal arrangements for scrutiny. In particular, it highlighted:

- A lack of clear strategic plans with targets translating the broad vision of the council and its partners into practical programmes of action.
- Planned activity not prioritised and matched to planned resources.
- A lack of evidence and systems to allow managers and councillors to systematically monitor performance across all areas of activity or identify areas of under-performance.
- A lack of a corporate approach to procurement.
- The Executive Committee also trying to fulfil the role of an independent Audit Committee.
- The complexity of the service delivery arrangements in place between the council and various local trusts and the need to apply the principles of *Following the Public Pound*.
- The council's inability over the previous three years to agree a balanced budget without significant recourse to its reserves, and the unsustainability of this approach.

In concluding its findings the Commission said that it would continue to monitor the situation. It required a further report by the Controller of Audit on the progress made by the council during 2005/06 and on the extent to which the objectives of Shetland's improvement plan had been achieved.

Progress at Shetland Islands Council

Commitment and leadership

The council has made a start in addressing the issues raised in the 2005 audit report. Its Corporate Improvement Plan addresses the key issues and its progress is regularly monitored. There is evidence of an improved corporate approach in many areas, led by the chief executive and the Executive Committee. However, many of the changes have been made only recently and have yet to become fully established.

1. In response to the audit report, the council approved an updated Corporate Improvement Plan in June 2005. This addresses all of the key concerns raised in the audit report and progress has been regularly monitored by senior managers and members. This extensive range of reforms is challenging for the council, given the limited capacity available to it as a relatively small organisation. However, the council has sought to prioritise its efforts, by targeting its resources on the most important issues.
2. Steps have been taken to increase the capacity of the organisation. A programme of management development training has been established, and there has been an increase in corporate resources, with a secondment into the Organisational Development team, effectively doubling its capacity to provide guidance and support the introduction of service planning and performance management.
3. The council has also strengthened its corporate and partnership working arrangements. Membership of the Executive Management Team (EMT) has been expanded to include the newly-created post of assistant chief executive, with a remit to oversee cross-cutting initiatives. The EMT now also includes the general managers of the Shetland Charitable Trust and, when the post is filled, the Shetland Development Trust in an effort to improve the coordination of services provided by the council and the trusts.
4. At member level, there have been important developments, with the introduction of a Scrutiny Committee and quarterly 'performance review meetings'. The council has also started to show a willingness to make difficult decisions in its quest to achieve long-term financial sustainability; for example, it recently approved a programme of cuts in service budgets and rejected some capital proposals.
5. These measures suggest that a greater commitment to the principles of Best Value and Community Planning is emerging on the part of members and senior management. However, most of these changes have only been made recently, and some are still proposals which have yet to be implemented.

Strategic and service planning

The council has made some progress in translating its broad vision into practical programmes of action, particularly in terms of its Corporate Improvement Plan and the establishment of a service planning framework. Less progress has been made in community planning, although long-term indicators have been developed and an Efficient Government bid has been submitted to the Scottish Executive.

6. The council has made progress in strengthening the links between its high-level aims and priorities, as set out in its corporate and community plans, and its improvement plan. The council's Corporate Improvement Plan was established in 2005, with a series of specific targets. Many of these planned improvements relate to management processes, but around 20 per cent of them include specific targets for services, such as education, community safety, and waste management. Quarterly progress reports, setting out planned improvements, timescales, and achievements, are monitored by senior managers and councillors.

7. Progress has also been made in establishing a service planning framework. In 2005/06, a series of service plans, covering all areas of council activity, was established. The council's organisational development unit provided corporate guidance on the format of service plans and carried out some quality control checks, and training was undertaken for service managers.

8. Each service plan follows a standard corporate format, which includes details of the main service developments and issues expected to arise over the coming year, as well as a range of targets based on national and local performance indicators. Some developments are still needed, particularly in terms of aligning service planning with the budget setting process, but the current approach provides a sound base from which further improvements can be made.

9. Relatively little progress has been made in developing the community plan, although there is evidence of a more practical approach emerging. As a precursor to establishing specific targets, a series of long-term indicators have been developed to help measure Shetland's quality of life and sustainability. *Sustainable Shetland*, published in September 2006, sets out a series of specific measures, covering ten key areas such as population, health, education, and economy. Once targets are set for each of these indicators, this should help drive a more practical and focused approach to the work of the council and the community planning partnership.

10. In March 2006, the council and its community planning partners put forward an Efficient Government bid to the Scottish Executive. The council played a key role in leading and developing the bid which seeks to build on a common vision of community wide planning and resource sharing as central features. This vision is ambitious but seen as critical in an area as relatively isolated and distinct as Shetland. The bid includes proposals for the various public sector bodies in Shetland to share support services, such as estates management and ICT, and makes proposals for greater joint management of services, such as health and community care. Funding has been received from the Scottish Executive

to provide a more detailed business case. If Scottish Executive approval and funding is received to implement the proposals, it is projected that this could lead to annual savings of around £0.5 million. However, if approval is not received, it is not clear how community planning will be developed.

Matching of resources and priorities

Some progress has been made in prioritising targets and matching them with resources in terms of capital projects. The council now needs to align its budget setting and service planning processes to ensure that there is a better match between resources and council priorities.

11. In previous years, the council has not taken a structured approach to managing and prioritising its capital programme. As a result, this has become a long 'wish-list', currently valued at £197 million, which the council has estimated would take ten years to complete.

12. The council has recognised that this approach is not sustainable and has now introduced a more structured approach to the selection and prioritisation of its capital programme. A corporate approach has been established, with a capital programme management team created to develop, manage and monitor all capital projects. A prioritisation system has been developed by a joint officer and member working group. This is based on a series of criteria, such as the impact on revenue expenditure, the number of people that would benefit, the impact on employment, and links to the corporate plan. This scoring system is being used to screen new proposals, but it is also planned to prioritise projects already on the approved programme by the end of 2006.

13. There is also some evidence of a change in attitude by members to proposed capital projects. Recent decisions not to proceed with certain proposals, such as a refurbished library at Scalloway costing over £400,000, and various harbour improvements, demonstrate a willingness to make difficult decisions and prioritise the use of its capital funds. These decisions are seen as representing something of a 'turning point' by key officers and suggest that the council is now starting to move towards achieving a more sustainable capital programme.

14. The council also needs to introduce a more structured and corporate approach to setting revenue budgets. At present, the service planning and budget setting processes are not aligned. The council follows an essentially incremental approach to setting budgets, with departmental budgets reflecting historic levels and varying little in response to changing priorities. As a result, there are few clear links between resources and corporate priorities.

15. In turn, this creates difficulties in managing the overall budget. Rather than the corporate centre pro-actively setting the overall budget, based on available resources, the budget tends to be driven by services. As a result, a reactive approach has had to be taken by the corporate centre. The initial budget for 2006/07 envisaged a draw on reserves of £11.7 million. The council recognised that this needed to be addressed and this led to a series of budget cuts, with the aim of reducing the annual

budget by £4.9 million. Based on the experience of previous years, there is also evidence that services tend to hold on to resources in order to protect their budgets and offer up savings only towards the end of the financial year, rather than as part of a long-term financial strategy.

16. These deep-rooted attitudes need to be tackled. The council has recognised the issue and plans to begin to align its budget-setting process with service planning for 2007/08.

Performance management

The council has established a performance management system which links with its new service planning framework. This has improved the quality of performance information provided to officers and members, providing a firmer base from which to take decisions. More work is needed to ensure that the council's arrangements are consistently implemented within services, and to develop a corporate performance management culture.

17. The council has introduced a more systematic approach to corporate performance management, covering all departments and using a common corporate standard for the format of its monthly reports. This has led to an improvement in the quality of performance reporting to members and officers. There are clear links with the service planning framework and comprise a mix of national and local performance indicators. For example, environmental services has a wide range of local indicators, such as the proportion of waste used for heat recovery, the energy produced, and breaches in emission limits. Some services, such as ferries and environmental services, also include measures of customer satisfaction. Updates on key achievements and issues affecting performance are also reported by services.

18. Momentum has been provided by the establishment of a performance management coordinator within Organisational Development. This has provided central support and direction, with workshops held as part of a management development programme, and regular performance management bulletins issued to senior officers, setting out required activities and deadlines.

19. There are arrangements for monitoring performance within each department, but these are less consistent. Monitoring reports follow different formats and tend to be based on the performance information available, rather than service priorities.

20. The introduction of a corporate performance management system has led to noticeable improvements in the quality of information provided to members. Our survey of councillors, carried out as part of the audit, suggests that around 75 per cent now feel that they are able to clearly identify which service areas are in greatest need of improvement from the service performance information they are provided with.

21. A promising development, in terms of monitoring service performance, has been the establishment of quarterly 'performance review meetings'. These are based on the model of informal 'away days' used

within environmental services. These performance review meetings have been in place for a year and cover all services. They are based around joint meetings between members and managers. These meetings are viewed positively by both elected members and officers, and are helping to encourage frank discussions on performance and budget issues and leading to corrective action to address areas of concern. It will be important to ensure that this initiative is maintained and that elected members continue to be engaged with monitoring service performance.

22. The framework provides a more systematic means of monitoring and controlling budgets. The quarterly 'performance review' meetings have helped to promote a culture of controlling budgets. This helped the council to achieve a £3 million under spend on its budget in 2005/06, reducing its draw on reserves and helping it move towards financial sustainability. This development needs to be sustained if the council is to reduce its reliance on reserves and achieve financial sustainability in the future.

23. There is also scope for further improvement to be made to the council's budget monitoring system, particularly in terms of commitment accounting. During the current financial year, for example, the current system has not allowed managers to easily judge their progress in achieving actual savings against their predicted spend.

Procurement

The council has not yet established a corporate approach to procurement. A broad policy was approved in 2005, but practical steps have been taken only recently, with a series of pilot projects currently underway.

24. A Procurement Policy was approved by the council in 2005. This set out the key principles of a corporate approach, but it was a short, high-level document which offered little practical guidance to managers.

25. During 2006, a corporate procurement team was formed, with representation from each of the key departments, to develop a more practical approach. It is not expected that a revised procurement strategy will be fully in place until 2007, but a series of five pilot projects are underway with the aim of gaining quick savings in areas such as travel, food, consultancy, and stationery.

Audit and Scrutiny Committees

In response to the Accounts Commission's concerns, the council has established an independent Scrutiny Committee, although the role of audit committee is still carried out by the Executive Committee. This has been implemented relatively recently and it is, therefore, too soon to judge its effectiveness.

26. Shetland's councillors are largely Independent members, without strong party political allegiances. In 2003, the council established an Executive Committee in order to provide a better focus on corporate governance and take the lead on corporate priorities. Its remit also includes the role of an Audit

Committee, considering reports from the internal and external auditors. It has had nominal responsibility for the wider aspects of scrutiny, but this role has been underdeveloped. The Accounts Commission expressed concern at the lack of independence of an Executive Committee in carrying out this role.

27. The council has now separated its decision-making and scrutiny functions, although the Executive Committee still fulfils the role of an audit committee. In 2006 it piloted the use of a separate Scrutiny Committee. This consists of eight councillors who, apart from the vice-convener, are not members of the Executive Committee and are, therefore, in a position to provide a degree of independent challenge.

28. Steps have been taken to provide support for the committee to carry out its role effectively. A *Scrutiny Handbook* has been produced which sets out practical guidance for elected members. Staff from Organisational Development also carry out investigations on behalf of the committee, although it is not clear if this small team can sustain this role within its current resources.

29. While it will need more time to become fully established and broaden its role by, for example, looking at more cross-cutting issues or overseeing Best Value reviews, the Scrutiny Committee has initiated reviews into three areas of concern flagged up in performance review meetings: the council's underperforming planning service, the time taken to re-let council houses, and the gender imbalance among senior managers. As the role of the Scrutiny Committee develops, the council will need to keep the autonomy and effectiveness of the audit committee function under review to help ensure that it can demonstrate that there is an independent scrutiny of decision-making.

Joint working with trusts

Steps have been taken to improve the overall coordination of service delivery, with the general managers of the two largest trusts now included as part of the council's EMT. There has also been some rationalisation of the services provided by the council and trusts. However, there are continuing concerns about the lines of accountability between the council and the trusts. The principles of *Following the Public Pound* need to be embedded in the way the council funds external organisations. In the light of the European Commission's ruling on State Aid, the council also needs to ensure that all other existing and future transactions are soundly based and comply with Best Value guidance on competitiveness.

30. The delivery of public services in Shetland is characterised by a unique infrastructure of local trusts working alongside the council. The largest of these, the Shetland Charitable Trust, was set up to manage the income generated from the North Sea oil boom in 1970s and has clearly benefited the local economy. However this complex pattern of service delivery makes it more difficult to coordinate activity and ensure that resources are properly matched to the needs of the community. It can also blur lines of public accountability.

31. The council has moved to improve the overall coordination of service delivery between itself and the Shetland Charitable Trust and the Shetland Development Trust. Membership of the council's EMT has recently been expanded to include the general managers of both trusts.

32. Clearly, this has the potential to help coordinate activities and focus on the wider issues of community planning. However, it also has the potential to blur the distinctions between the council and the trusts. The council's annual accounts for 2005/06 have received a qualified audit certificate, due to a failure to comply with new regulations on Group Accounts and concerns by the external auditors that the activities of these trusts are not properly included in the council's annual accounts. Managers have indicated a willingness to comply with this ruling in future years, but the auditor's report has still to be agreed by the elected members.

33. The external auditor has also raised concerns about the controls in place over money transferred from the council to trusts. The principles of *Following the Public Pound* require clear objectives and monitoring arrangements to be attached to such funding and the council scored poorly in a national study carried out in 2005. The council has taken action to address these issues but the external auditor has noted that most of these relate to drafting a policy document, which was only approved in September 2006. New procedures have still to become embedded in the way the council funds external organisations.

34. By far the largest of the trusts is the Shetland Charitable Trust. This is independently funded from North Sea oil revenues and receives no income from the council. Through a range of funding arrangements with other trusts, this provides around £12 million per year supplementing the council's expenditure on areas such as sports and leisure centres. Significant progress has been made in rationalising the services provided by the trust and the council. The Shetland Welfare Trust, a subsidiary of the Shetland Charitable Trust, has provided funding of over £3 million per year for the provision of care homes, in addition to the service provided by the council. However, in April 2005, in a move to reduce administration costs and improve the coordination of services, the Shetland Welfare Trust was formally wound up and the provision of care homes was integrated into a single management structure within the council.

35. There have been concerns about the role of the Shetland Development Trust and the trust's use of council funding to support local commercial interests. This has attracted a great deal of public comment in recent years, particularly over the failure of investments and loss of £7 million in salmon farming and recent support for ferries.

36. A recent investigation by the European Commission has found that grants made in earlier years to local fish catching and processing businesses do not comply with a common market and should be regarded as state aid, rather than normal commercial investments. This also contravenes Best Value guidance on competitiveness. The European Commission has not required that these funds should be

recovered, but the council has taken action to prevent a recurrence of these issues. Concerns have also been raised about the Shetland Development Trust's funding of the Smyril Line ferry company, dating back to 2001, and the influence of the council on these decisions. Additional funding of approximately £700,000 to the Smyril Line is currently on hold as legal advice is sought on the State Aid ruling. A review is currently being undertaken by the council to ensure that no similar transactions exist and to introduce formal procedures to provide assurance that any future transactions are soundly and legally based.

37. Concern has also been expressed about the links between the trust and the council's economic development unit. The council is now seeking to resolve these with their merger into a new Shetland Community Development Trust.

Financial sustainability

The council has set a clear commitment to achieving financial sustainability, aiming to eliminate the use of reserves to fund revenue expenditure by 2012/13, and to maintain its reserves at £250 million or above. Despite some progress in approving a series of cuts in service budgets and prioritising the use of capital funds, the council has still to show that its use of reserves is falling compared with previous years.

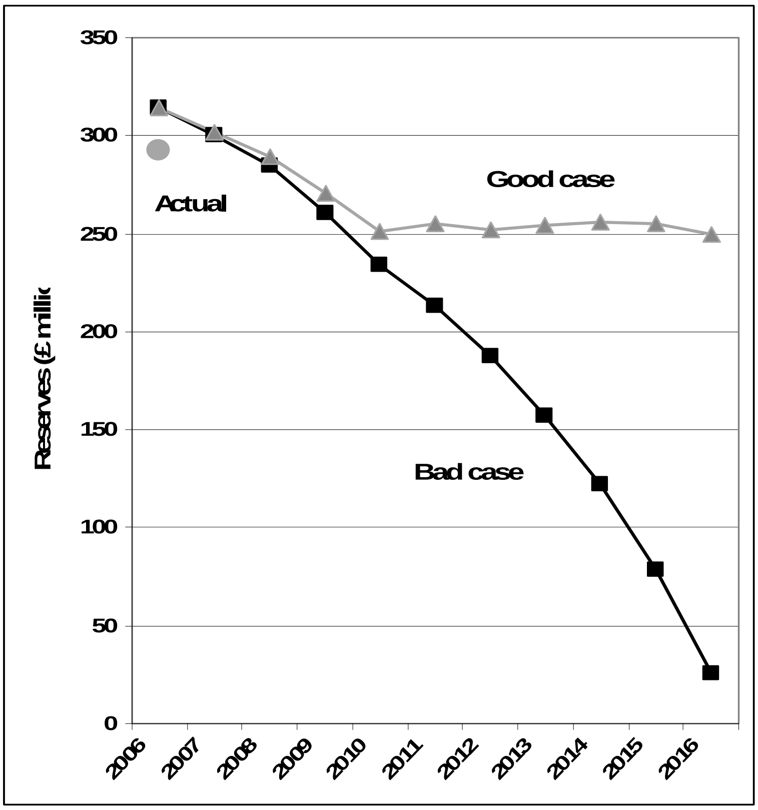
38. In recent years, the council has used its reserves to help fund revenue expenditure. The fall in the overall value of its reserves has been reversed during the past year or so, due to favourable market conditions.

39. Despite the value of its investments increasing from £286 million to £292 million over the past year, the council has recognised that its current approach is not sustainable in the long-term. As part of its long-term financial strategy, the council has determined that it needs to maintain its reserves at £250 million or more. In order to achieve this, it is aiming to eliminate its reliance on reserves to fund revenue expenditure by 2012/13, and to reduce its capital spending by around 39 per cent. Without these restrictions, the council has projected that its reserves would be exhausted by 2016 (see Exhibit 1) and the loss of investment income would result in severe cuts in frontline services.

Exhibit 1

Shetland Islands Council – projected reserves 2006 to 2016

The council aims to maintain the value of its reserves at around £250 million. However, unless it is successful in controlling the use of reserves for revenue expenditure, they are projected to disappear by 2016, forcing severe cuts in services. The ‘actual’ position is £20 million below projections due to the recent purchase of four ferries.



Source: Shetland Islands Council, ‘Long term Financial Planning’, 10 September 2006

40. At this stage, it is not clear that the council is reducing its reliance on its reserves. It has made some important changes and there is evidence of progress. For example, a series of planned savings initiatives have recently been approved by members, reducing the council’s budget for 2006/07 by £4.9 million and the planned contribution from reserves from £11.7 million to £6.8 million. However, even assuming that these forecasts are accurate, this compares with a contribution from reserves of only £4 million in 2005/06. Moreover, the council is facing growing pressures on its resources. A recent Budget Task Force review of social work, formed with the aim of identifying the scope for significant savings, found the need for additional resources to meet growing demands.

41. Similarly, there is mixed evidence that the council is successfully prioritising its capital programme and reducing its draw on reserves. As mentioned earlier in this report, it has recently approved a more structured approach for prioritising its capital programme and assessing future proposals. Moreover,

members have shown a greater willingness to turn down capital proposals, such as the Scalloway library project and the development of various piers, rather than simply add them to a capital 'wish-list'. However, the council's recent decision to purchase four ferries for £20 million, aimed at reducing annual leasing costs, has reduced its reserves below projected levels (see Exhibit 1).

Conclusion

42. Shetland Islands Council has made a start in addressing the issues raised by the Accounts Commission in March 2005. It has made improvements to its strategic planning arrangements with the introduction of a corporate improvement plan, and service planning and performance management frameworks. It has also introduced an independent Scrutiny Committee and made some moves towards achieving its longer term ambition of financial sustainability, although there is scope to further improve on this.

43. There remain, however, concerns about the pace and extent of change. A number of initiatives are relatively recent and consequently they are not yet fully embedded and have yet to have an impact in terms of improved service delivery or outcomes. In particular there has been limited progress in respect of community planning, the council’s Audit Committee remains within the remit of the Executive, and the council is yet to establish a corporate approach to procurement. The council has made some improvements in its joint working arrangements with trusts, but there are still concerns about the clarity of lines of accountability between the council and trusts. The council is also not yet able to demonstrate a tangible improvement in reducing its reliance on reserves.

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