Dumfries and Galloway Council

Report to Members and the Controller of Audit on the 2006/07 Audit

October 2007

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Introduction

In 2006/07 we looked at the key strategic and financial risks being faced by the council. We audited the financial statements and we looked at aspects of performance management and governance. This report sets out our main findings, summarising key outcomes in 2006/07 and the outlook for the period ahead.

Key outcomes from 2006/07 audit

We have given an **unqualified** opinion on the financial statements of Dumfries and Galloway Council for 2006/07. We have, however, drawn attention to a failure to comply with the statutory requirement that all significant trading operations break even on a rolling three year basis as three of the council's four statutory trading operations returned cumulative deficits at 31 March 2007.

The council had corporate governance systems in place during 2006/07 that operated within a sound control environment. Immediate priority should however be given to improving risk management arrangements and introducing a business continuity plan for the council.

A general fund surplus of £ 0.989 million was achieved in 2006/07. At 31 March 2007 the council had a total general fund balance of £29.357 million, of which £7.912 million was unallocated. This is above the council's policy of retaining a minimum level of £6 million. A contribution from the general fund of £6.5 million was included in the 2006/07 budget. Due mainly to the receipt of higher than expected capital receipts, along with close budget monitoring throughout the year, the actual general fund contribution to expenditure in 2006/07 was £4.4 million and was below the initial budgeted contribution.

The financial difficulties experienced by Combined Services are a cause of concern, in particular the deficits experienced by the statutory trading operations and Homecare Services. Actions being taken by management to address these issues include the competitive tendering of Cleansing services and the formal review of options for the future delivery of care at home services.

For the third consecutive financial year, the council has underspent on the capital programme. Capital slippage in 2006/07 totalled £ 10.974 million, approximately 36% of the final capital budget for 2006/07. One factor contributing to the slippage was the late receipt of funding from the Schools Building Improvement Fund. Effective action has to be taken to reduce the level of slippage against the capital plan in 2007/08.

Asset management plans have still to be fully developed and approved by members. Progress is however continuing, with focus now being placed on the more challenging tasks of linking future asset plans and investment decisions to the council's vision and priorities.

The schools PPP project has reached the stage of securing the appointment of a preferred bidder. There has however been some slippage against the initial target date for financial close. This is now likely to be November 2007. It is important that the progress of negotiations to financial close are carefully managed to avoid any further slippage and any possible financial penalties to the council.

Progress in finalising the remainder of the council's schools estate maintenance plan has been slow. As decisions on possible school closures are still outstanding, it is not yet possible for a long term financial plan to be agreed to fund the repairs required to all schools not covered by the PPP.

It is clear that the council has dedicated resources over the year to the development of the Covalent performance management system and the wider Strategic Management Framework.   The initial set up stage of the Covalent system is now complete. The next key stages to complete are to fully populate the system with core performance data and to embed it into services' performance management processes.

Outlook for future audits

The council continues to face exceptionally challenging financial pressures. The council's budget strategy for the medium term continues to include contributions from general fund balances. This could result in balances being depleted to imprudent levels which represents a significant financial risk to the council.

There is a risk that elements of the savings secured to date by services cannot be sustained. Future budgets projections however continue to include demanding savings targets which may not be achievable without adversely impacting on levels of service provision.

Particular budget pressures are likely to continue within Social Work Services and Combined Services. The effect of the options review within Homecare Services in alleviating trading deficits will have to be carefully monitored. It is also essential that the council ensures improvement to the trading performance of the Catering and Cleaning and Cleansing and Grounds Maintenance statutory trading operations and can demonstrate the achievement of best value.

The recent loss by the Property Maintenance Service of the contracts with the Dumfries and Galloway Housing Partnership is a significant change and will have to be carefully managed.

In common with many other Scottish councils, the council has sought to limit its exposure to the financial risk associated with equal pay claims by making payments to specific groups of employees as part of a compensation package. A provision has also been recognised in the 2006/07 financial statements for the estimated cost of payments which may have to be made to additional groups of employees. While moves to agree compensation payments will help to reduce financial risk in this area to some extent, some risk remains while existing pay and reward structures are in place.

The council has still to implement a single status agreement. The implementation date will no longer be 1 April 2007 and a new date is to be jointly negotiated between the council and the trade unions. The delayed implementation of single status will go some way to alleviating the council's immediate financial difficulties. However the future affordability of single status will require savings from reductions in staff numbers. Priority should be given to the introduction of a structured programme for securing staff reductions. This will have to be closely managed to ensure the successful release of required savings.

The potential financial pressures facing the council over the medium term are exasperated by the current uncertainty over the impact the new Scottish Government will have on local government finance, in particular in relation to the local government settlement and council tax funding.

Decisions on the future of the council's schools estate need to be made and a long term financial plan is required to provide for the repair costs of all schools not covered by the PPP. It is important for the council to avoid any further delays in reaching financial close on the PPP and, in the light of the continuing need for budget cuts, the future affordability of the council's commitment to contribute to the Schools PPP sinking fund should be kept under review.

Work is ongoing to develop an updated Corporate Plan for the period 2008-2011. It is intended that improvements to the new plan will include more explicit objectives and outcomes derived from the council vision and more detailed performance information and targets.

To ensure an integrated approach to strategic and financial planning, full compliance with the Strategic Management Framework across the council will be essential. Close management and review of the Financial Efficiency Strategy will also be critical if the council is to deliver its strategic plans and improvements within such a challenging financial environment. It will be critical that the momentum achieved so far in the introduction of the Covalent system is maintained to ensure its effective use in supporting decision making and performance improvement.

The co-operation and assistance given to us by Dumfries and Galloway Council members and staff over our audit is gratefully acknowledged.

Audit Scotland

October 2007

Introduction

1. This report summarises the findings from our 2006/07 audit of Dumfries and Galloway Council. Findings are drawn together within four sections namely; performance, financial position, governance and financial statements. Within each of these sections we have also provided an outlook setting out key issues and concerns facing the council going forward.

2. The scope of the audit was set out in our Audit Risk Analysis and Plan (ARAP), which was submitted to the council's Governance and Audit Committee in August 2007. Under the following strategic themes, the ARAP set out our views on the key business risks facing the council and described the work we planned to carry out:

   - ensuring the future affordability and sustainability of services
   - securing the efficient use of resources
   - managing performance to achieve best value
   - effective partnership working
   - supporting governance and scrutiny.

3. Overall conclusions about the council's management of key risks are discussed throughout this report.

4. We also undertook a number of exercises which resulted in separate audit reports, for example, a review of the council's internal audit service, computer service review and an overview of the council's approach to best value service reviews. Within this report, we highlight key messages from those separate reports for the consideration of members. Appendix A of this report sets out the key risks highlighted in this report which we wish to draw to the attention of members and the action planned by management to address them.

5. We would like to take this opportunity to express our appreciation for the assistance and co-operation provided by officers and members during the course of our audit work.

Performance

Introduction

6. In this section we summarise key aspects of the council's reported performance during 2006/07 and provide an outlook on future performance, including our views on the current status of identified key risks. We also comment on the findings of national performance audit studies.

Corporate objectives and priorities

7. The Corporate Plan for 2003 – 2007 sets out the key goals and priorities for the council until 2007 and explains how it plans to achieve these. The plan sets out three themes which are in line with the themes of the Community Plan. These are:

- enterprising and learning communities
- safe and healthy communities
- inclusive communities.

8. The council has identified for the Corporate Plan the following strategic priority projects:

- Disability and Discrimination Act; Access to council buildings
- completion of the regional leisure complex, DG1
- broadband links
- schools PPP
- employee development
- waste management and recycling
- urban and area based regeneration
- improvement to infrastructure
- development of the Crichton Site
- public utilities
- commercial opportunities
- Southern Dumfries Access strategy
- achieving a balanced budget.

9. Progress so far against the milestones for each of these strategic projects was reported to the Business Review and Performance Committee in April 2007. The general picture given was one of making progress. The status of each project was reported in detailed and descriptive terms. Future progress reports would benefit from being more focused on specific output targets and by including clearer conclusions on whether projects were achieving strategic priorities. This should be facilitated by future reports being generated from the data held within the Covalent performance management system.

10. Following the May 2007 elections and the change of administration, work is ongoing to develop an updated Corporate Plan for 2008 – 2011 which incorporates the relevant manifesto commitments and council vision. It is intended that improvements to the new Corporate Plan will include explicit objectives and outcomes derived from the council vision and more detailed performance information and targets.

11. The five political group leaders and the council's management team have met and agreed a draft of the council vision, values, aims and objectives. These were considered by members of the council committees in August 2007. Following further consultation with council staff, planning partners and the wider public, the Corporate Plan is scheduled to be finalised by November 2007.

Overview of performance in 2006/07

Measuring Performance

12. The council's Strategic Management Framework is the overarching structure for managing performance. In brief this comprises a clear timetable for those key management activities required to support the council's business and guidance on strategic planning, service delivery, service review, performance reporting and budget planning. Critical to the council's Strategic Management Framework is the successful implementation and use of the Covalent performance management system. Once fully operational, this will provide the core performance data for many of the council's key activities and will generate monitoring information on the achievement of the council's priorities and objectives. Progress in implementing the Covalent system is detailed at paragraph 39.

13. Since October 2005 the council has also been working to a Financial Efficiency Strategy (FES). This is made up of the following components :

- controlling spend
- doing more with less / service review
- business transformation
- budget strategy.

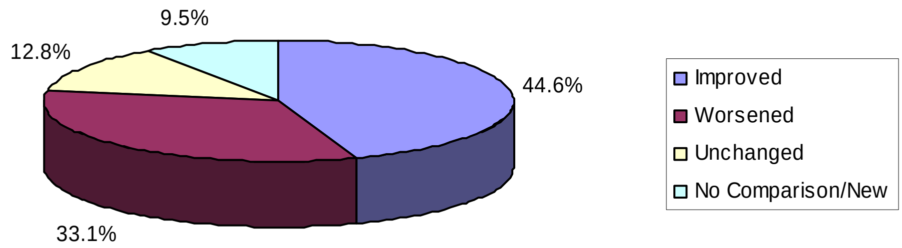
14. The FES was reviewed and updated by the Finance Sub-Committee in July 2007. Each component of the strategy was reviewed in the light of the council's continuing financial pressures and need to secure savings. Emphasis was given to making clearer the link between policies and budgets and to strengthen the influence of the service planning process on the budget. The FES has been the subject of a detailed risk assessment process and ten corporate risks were identified in relation to achieving the strategy. The CMT are to review each of these risks and report the progress to date to members.

15. The council has acknowledged the need for future changes in the management and delivery of council services. Under the business transformation component of the FES, a report was put to members in August 2007 covering the potential for new ways of delivering services. Options to be considered include partnership arrangements with the private sector and establishing trusts.

Statutory performance indicators

16. One of the ways of measuring council performance is through statutory performance indicators (SPIs). The council produces the full suite of SPIs which are reported to members, government and the public. However, we found that in a number of cases, the indicators are seen by some officers as an annual exercise and better integration with the overall performance management systems is required. The Covalent system will be populated with SPI data and it is the council's intention to make more use of this data for management purposes in conjunction with the development of local indicators to address local priorities.

17. Although the SPIs are not fully integrated into the management systems, the council does take note of the data produced. In past years, the council has tended towards average performance with a mix of improvements and deteriorations reported. In 2006/07, the council also reported some indicators that had improved and some that had worsened. While more have improved, the number that had worsened is a cause for concern. The following chart indicates the proportions:



18. Overall, substantial improvements have been made and maintained in:

- the new Environmental Standards Department who are responsible for the Protective Services indicators, most of which show improvement
- police clear up rates
- benefits administration.

19. However, examples of where performance indicators have declined include:

- road policing/safety where deaths and serious injuries have increased significantly
- phone call response times in fire and rescue where, however, more time spent answering calls has significantly reduced unnecessary attendances by fire tenders
- use of libraries.

20. Each year we review the reliability of the council's arrangements to prepare SPIs. Overall, the quality of working papers provided to support the SPIs this year had remained broadly consistent with previous years. While no indicators were classed as unreliable, which was an improvement on the previous year, too many working papers were difficult to follow. This was disappointing given the time spent by external audit during the year in assisting coordinators with their presentation. We have reported on the need to improve the standard of working papers in previous audit reports. Priority has to be given to ensuring the SPI working papers improve for next year.

Key risk area 1

Best Value audit

21. The Local Government in Scotland Act 2003 established best value and community planning as statutory duties for local authorities. In response the Accounts Commission introduced new arrangements for the audit of best value based on a full review by a specialist team once every three years. In the intervening years short follow-up reviews are carried out by the local auditor.

22. The council are scheduled to receive a best value audit in 2008/09.

Performance outlook – opportunities and risks

Introduction

23. In the course of our audit work we identified some of the strategic risks to Dumfries and Galloway Council delivering on its stated objectives and priorities in the years ahead. These risks were set out in our Audit Risk Analysis and Plan and grouped into five risk themes. In the following paragraphs, we comment on the progress made by the council during the year and the key risks yet to be fully addressed. Where appropriate, matters arising in a number of these areas are also reported in more detail elsewhere in this report. Risk exists in all organisations which are committed to continuous improvement and, inevitably, is higher in those undergoing significant change. The objective is to be "risk aware", and have sound processes of risk management, rather than "risk averse". Indeed, organisations that seek to avoid risk entirely are unlikely to achieve best value.

Ensuring the future affordability and sustainability of services

Ongoing financial pressures and budget cuts

24. The council is facing serious financial pressures. Services need to secure considerable ongoing budget cuts against in some cases, increasing demand for services. While the council was able to meet the 2006/07 budget there is the potential that savings achieved to date are non recurring and cannot be sustained. Future budgets continue to include substantial savings targets. At the time of setting the 2007/08 council tax, the revenue budgets for the year required savings of approximately £4 million. This excluded those savings which would be required to fund single status costs. Estimated savings required over the three years to 2010/11 significantly exceed the savings that the council has been able to achieve in previous years. There is a considerable risk that the council will be unable to secure budget cuts without adversely impacting on either the quality or levels of service. This situation is compounded by both the current uncertainty over future local government funding settlements and possible constraints on council tax levels.

Key risk area 2

25. Significant unavoidable cost pressures were identified as part of the budget setting process for 2007/08. An Officers Scrutiny Panel has reviewed the nature of these budget pressures put forward by services and has concluded that in the majority of cases the budget pressures were deemed unavoidable. Of the total of £5.3 million, it was concluded that £ 3.8 million were current pressures and in most cases services would have to come forward with options to fund their own budget pressures. These will have to be funded by services from compensating savings. An improved approach has been introduced for providing assurance on those budget pressures identified as part of future budget setting processes.

26. The assumptions made for future budgets include savings from cuts in staffing levels, in particular the savings required to finance the costs of single status. The council has yet to develop the single status natural wastage/redeployment and efficiency programme agreed by members in February 2007. Priority should be given to introducing such a programme to allow the overall affordability of single status to be closely monitored.

Key risk area 3

27. Future budgets include the ongoing depletion of general fund balances to levels which are below the council's policy of holding a minimum level of unallocated balances of £6 million. There is a risk that available general fund balances could reduce to imprudent levels leaving the council with inadequate reserves to fund any unforeseen costs.

Key risk area 4

28. Particular budget pressures are the increasing demand for social services and the trading difficulties experienced by the council's statutory trading operations. An outline of the pressures faced by the trading operations has been given at paragraphs 75 to 82. Homecare Services returned a deficit in 2006/07 of approximately £ 0.878 million or 12% of its annual expenditure budget. In response to these difficulties the council has approved a formal options appraisal review covering the future provision of the care at home services. It is expected that the results of the review will be reported in the Spring of 2008.

Key risk area 5

Single Status

29. In 1999 a single status agreement was reached between Scottish local authorities and trade unions to harmonise the terms and conditions of manual and administrative, professional, technical and clerical workers (covering pay, working hours, leave and negotiating mechanisms). There was a presumption that single status would be cost neutral with any increased costs being offset by savings arising from changes to other conditions of service or from efficiencies.

30. The original national single status agreement specified that implementation should take place by April 2002 but, following difficulties in establishing a model job evaluation scheme, was extended by agreement between local authorities and unions to April 2004.

31. The council has yet to reach agreement on a single status pay and grading structure. Discussions are ongoing with trade unions with the aim of reaching an agreement through a negotiated settlement. It is envisaged that by the end of October 2007 negotiations should be finalised and the trade unions will be in a position to ballot their members on the council's final offer for revised pay and grading and terms and conditions of service.

32. It has been agreed with trade unions that the implementation date for single status will no longer be 1 April 2007. A new date in 2008 is to be jointly negotiated. In postponing the implementation date, the council has agreed to award the outstanding pay increase and increments to staff and to back date this to April 2007. Further payments will also be made to those staff who have already received equal pay compensation. By postponing the implementation date, the costs of single status originally included in the council's 2007/08 budget will no longer be incurred. This will go some way to alleviating the immediate financial pressures currently facing the council.

33. However, until single status is implemented, the initial and continuing costs to the council cannot be reliably estimated. The current available estimates show that the costs of single status in 2008/09 will be £8.5 million rising to £9 million in 2010/11. Future single status costs represent a significant cost pressure to the council.

Key risk area 6

Smarter Schools PPP and Schools Estate Management Plan

34. The council is reaching the final stages of the Smarter Schools PPP project. A preferred bidder has now being appointed. There has been some slippage in the expected financial close date, which is now planned for 30 November 2007. It is important that progress in negotiations to financial close are closely managed to avoid any further delays and to minimise any possible financial penalties incurred by the council. The schools which are not being improved under the PPP have been included within the council's schools estate management plan. The council has prioritised the need for future repairs and improvements to these schools.

Key risk area 7

35. The council has established a sinking fund to finance both the affordability gap on the PPP and to contribute towards the improvement costs of those schools within the schools estate management plan. At the end of 2007/08 it is expected that the value of the fund will total £11.25 million. The council are committed to contributing £5 million each year to the fund, rising with inflation, over the remainder of the 30 years of the PPP. Capital funding is in place for the top priority schools (type 2a) and for part of the second highest priority group (type 2b). It is a cause of concern however that the council has yet to identify the funding for the remainder of the schools estate and that a long term financial plan has not been established. This will depend on the outcome of future decisions by members on the future of the schools estate and possible schools closure programmes.

Key risk area 8

Securing the efficient use of resources

Asset Management

36. The management of the council's portfolio of assets together with the loans that support them are the second highest revenue cost to the council after employee costs. In addition, increasing energy costs and property accessibility, place continuing pressures on expenditure. To allow the council to actively manage assets as part of fulfilling the council's priorities and objectives, asset management plans should be in place. Plans are also necessary to inform the planned programme of future asset sales built into the council's revenue budgets.

37. The council are continuing to develop their asset management plans. The corporate plan asset management plan will be drawn from the four separate plans covering the office, community, industrial and schools estates. Each of these plans are currently at different stages of completion and are being taken forward by the Strategic Property Group supported by separate working groups for each asset management plan. Work is currently taking place in identifying service visions, prioritising areas for future investment and drawing together asset plans to achieve service objectives. Once complete, the council will be in a position to approve each of the asset management plans and the overarching corporate asset management plan.

Key risk area 9

Service Review process

38. As part of our audit we reviewed the council's approach to date in carrying out service reviews. This identified that there was a need to improve procedures and that the council had in the past failed to apply a systematic approach to carrying out service reviews. In addition, the progress and outcome of reviews were not always reported to members. There were risks that some council activities would not be subject to reviews and that the council could not demonstrate best value. The council has recognised the need to improve these areas and has recently introduced arrangements, which if successfully followed, should strengthen procedures. Quarterly progress reports on service reviews are now to be submitted to the council's Scrutiny Committee. The overall review programme, which will now cover a five year period, is also to be approved on an annual basis. The committee is also to receive a report on the extent of compliance with the council's strategic management framework, which includes amongst other things, clear guidance on service reviews. These are positive developments in the council's approach to best value service reviews and it is important that the success of these arrangements is ensured. We will continue to monitor progress in this area in future audits.

Managing performance to achieve best value

Performance Management Framework

39. The council has made sound progress in introducing the Covalent performance management system. The core system is now up and running and staff are receiving training on its use. The next important steps are to complete the input of key targets and performance measures, to update performance data on an ongoing basis and to use the system to generate performance monitoring reports. The Covalent system will play a critical role in the future success of the council's performance management framework. Having completed the initial introduction stage, it is now essential that the system is successfully rolled out and fully utilised by all services throughout the council.

Key risk area 10

Social Work Inspection Agency Report

40. It is clear that the council has been proactive in responding to the critical report received in September 2006 from the Social Work Inspection Agency (SWIA) on the performance assessment of the council's social work services. Detailed proposals for addressing the SWIA inspection report on social work services, along with the separate report on criminal justice services were approved by members in December 2006. The 'Delivering Change' improvement agenda covers the years from 2007 to 2010 and sets out the council's vision for social work services. A revised management structure and processes have been approved for taking forward this vision and securing the required improvements. This includes the introduction of a quarterly business review process to provide a systematic structure for managing performance and the establishment of a dedicated frontline performance improvement and quality team.

41. Detailed action plans have been drawn up to address each of the SWIA recommendations. The achievement of these actions will be challenging and will require the commitment of both staff time and financial resources. Although comprehensive in other respects, the action plans have not yet quantified the resources that will be required to secure the necessary improvements. The success of the council's delivering change programme for social work services depends on the availability of resources and it is important that these are quantified to allow informed decisions by members. We will keep the progress made against the SWIA report action plan under review.

Risk Management and Business Continuity Arrangements

42. We identified as part of our audit risk analysis and plan (ARAP) for 2006/07 that there was a need for the council to further develop its arrangements for managing risk and to introduce a business continuity plan. There has been limited progress in taking forward these issues. We have concerns around the lack of risk management arrangements particularly at service levels and the delays in introducing business continuity plans for the provision of key council services. Immediate action should be taken to address these risks.

Key risk area 11

Effective partnership working

43. Increasingly the council is dependent on partnership working and the sharing of resources to deliver service improvements. During the year the council has refocused the work of the Community Planning Joint Board. The community planning manager has held strategic level discussions with key partners to identify the priorities and projects to be taken forward in improving community planning. A future work programme will be agreed including those areas to be further developed. This will cover a number of priorities including the development of an outcome focussed performance management system and a review of the community planning structures. While it will be challenging to deliver, the strategic priorities being taken forward are critical to the future success of community planning within Dumfries and Galloway.

44. A major development in strengthening partnership working between the council and NHS Dumfries and Galloway has been the approval to replace the Joint Future Executive Partnership Board with a Community Health and Social Care Partnership Board. This should ensure closer partnership working and improve the planning of health and social care services across Dumfries and Galloway. The immediate actions for the new Partnership Board will include the agreement of arrangements for joint governance and joint resourcing.

Supporting governance and scrutiny

45. In common with many councils, the elections have resulted in a new administration and a considerable number of new councillors. The council's former Scottish Labour Party administration has been replaced by a minority administration from the Scottish Conservative and Unionist Party. While the council's style of government remains the traditional committee-based model, changes have been made to the remits of the committees. The membership of committees is generally along proportionate lines related to the numbers of members in each political grouping.

46. New and continuing members received a comprehensive programme of training following the May 2007 elections and it is the intention to introduce personal development plans for each member. A new Code of Conduct has also been issued which includes a protocol for relations between members and employees. A protocol has also been included in the members handbook covering joint working between members in multi -member wards.

47. The council has a number of outside bodies (eg the Crichton Trust and Visit Scotland) where members sit on the management committee or board. Such representation is decided by an appropriate committee. A detailed Scheme for Representation on Outside Bodies is part of the current members handbook. A risk assessment is carried out in each case examining the status of the body and members remain bound by the Councillors Code of Conduct which implements the advice of the Standards Commission for Scotland.

National studies

48. Audit Scotland carries out a national study programme on behalf of both the Accounts Commission and the Auditor General for Scotland. Reports of direct interest to the council are set out in paragraphs 49 – 56 below. Further information on these studies and reports can be obtained from Audit Scotland's web page at www.audit-scotland.gov.uk

Sustainable waste management

49. There is an increasing awareness of the need to protect the environment and to promote the sustainable use of resources. As a result of UN conventions and EU Directives, the UK government introduced a landfill tax to discourage the disposal of waste in landfill sites and set a (non-statutory) target that Local Authorities should recycle 25% of household waste by 2000. This target was not achieved.

50. Further EU Directives required Member States to "take appropriate steps to encourage the prevention, recycling and processing of waste" and to set out details of measuring processes within waste management plans. Subsequently a series of targets was set over the period to 2020 to reduce the amount of biodegradable waste going to landfill. The EC can impose a fine on the UK of up to £350,000 per day if it fails to meet its targets.

51. The purpose of Audit Scotland's study was to examine the performance of local authorities, the Scottish Environmental Protection Agency (SEPA) and the Scottish Executive in reducing the amount of municipal waste being disposed of as landfill, including the impact and value for money achieved by the investment in this area.

52. The key findings from Audit Scotland's national report published in September 2007 highlighted that:

- while significant progress has been made in meeting interim recycling targets, the rate varies considerably between councils and the type of collection system employed
- there has been slow progress in developing facilities to treat residual waste. There is therefore a significant risk that EU directive targets may not be met
- increased recycling has led to increased costs
- all parties need to work more effectively together to make rapid progress in waste minimisation, recycling and waste treatment to achieve the landfill directive targets.

Dealing with offending by young people

53. Audit Scotland published reports on *Dealing with offending by young people* in December 2002 and November 2003. Audit Scotland undertook a follow-up study review to ascertain the improvements in performance since 2002 of agencies who deal with young people who offend in the context of a changing policy landscape.

54. The key findings from the study are that the Scottish Government has shown a consistent commitment to improving youth justice services and has increased funding for the service from £235 million in 2000/01 to £336 million in 2005/06 together with practical support and guidance to help improve performance. However, the impact of this on services and outcomes is not yet demonstrated. Limited outcome measures are available and there are weaknesses in performance management arrangements. Therefore, it is not possible to assess the effectiveness of the additional expenditure in reducing offending and improving the quality of life of local communities.

Scotland's School Estate

55. A national review is being carried out on how effective recent investments in the Scottish school estate have been in terms of improving the quality of the buildings in which learning and teaching take place. The performance of the Scottish Executive and local authorities in improving the schools estate within the context of the 2003 strategy 'Building our Future – Scotland's School Estate' will be considered. This work is currently in progress and due to be reported in the Spring of 2008.

Police call management

56. This study is the first in-depth review of how police forces in Scotland manage calls from the public. All Scottish police forces have recently centralised how they manage calls from the public. The key findings from the review were that more calls to the police are now being answered and members of the public are generally satisfied with the service when they call. However limited performance information means forces are unable to demonstrate whether the new arrangements are delivering value for money or fully achieving the anticipated benefits. The lack of a national strategy has resulted in wide variations in approach. The report includes specific recommendations to improve the effectiveness of police call management in Scotland, and provide a framework against which to measure future progress. The information on call management by Dumfries and Galloway included in the report should be of use to management in taking forward any planned improvements.

Financial position

Introduction

57. In this section we summarise key aspects of the council's reported financial position and performance to 31 March 2007, providing an outlook on future financial prospects, including our views on potential financial risks. Under the strategic theme of 'ensuring the future affordability and sustainability of services', our audit risk analysis and plan recognised the significant challenges being faced by the council with regard to managing ongoing financial pressures. Our findings and key messages are set out in this section.

Council tax and the general fund

Operating performance 2006/07

58. The presentation of the 2006/07 financial statements has changed significantly from the previous year, as a result of changes to the *Code of Practice on Local Authority Accounting in the United Kingdom 2006 (the SORP)*. In place of the previous consolidated revenue account, the financial statements now include an income and expenditure account and a statement on the movement of the general fund balance which reflects items that need to be included/ excluded when determining a local authority's budget requirement and the level of council tax.

59. The council's net operating expenditure in 2006/07 was £ 324.4 million. This was met by government grants and local taxation of £296.2 million, resulting in an income and expenditure deficit of £ 28.2 million. The statement of movement on the general fund balance shows that a general fund surplus of £ 0.989 million was achieved in the year. When this is added to the general fund balance brought forward from 2005/06, the council has a general fund balance of £29.357 million at 31 March 2007. This includes unallocated balances of £7.912 million.

60. The budget set for 2006/07 included a planned contribution from the unallocated general fund balances of £6.5 million. In his Foreword to the financial statements the Director of Finance highlights, that due to a favourable variance of £2.1 million against the initial budget, the actual contribution from the general fund balance was £4.4 million. This favourable variance was due mainly to the generation of higher than expected capital receipts. Within this overall favourable outturn there are the following areas of concern:

- The financial difficulties being experienced within Combined Services which returned an overall trading deficit of £2.330 million. The main elements of this balance include the net deficit on the significant trading operations and a year end deficit on Homecare Services. A contribution of £1.5 million was made to Combined Services from the general fund in 2006/07. The service is carrying forward a cumulative deficit of £0.874 million to 2007/08.

- Education, Social Work and Community Services had been projecting budget overspends throughout the year. However the final outturn for this service proved to be a small surplus of £0.699 million. This was due mainly to underspends within the schools service. Management has accepted the need to improve the accuracy of budget projections reported to members and the reporting of a clearer trail for proposed and approved budget virements.

Reserves and balances

61. At 31 March 2007 the council had total cash backed reserves and funds of £52 million, including an insurance fund that underpins the council's self-insurance arrangements and repair and renewal funds to finance expenditure incurred in repairing, maintaining, replacing and renewing fixed assets.

Reserves and Funds

Description	2006/07 £ Million	2005/06 £ Million
General Fund	29.357	28.368
Capital Fund	5.015	3.920
Useable Capital Receipts	13.705	13.705
Renewal and Repair Fund	1.779	0.620
Insurance Fund	2.242	1.999
	52.098	**48.612**

62. The council aims to maintain a minimum working balance of £6 million. At 31 March 2007, the majority of the general fund was earmarked for specific purposes. The unallocated balance on the general fund was £ 7.912 million. This has reduced from £12.3 million at the end of 2005/06 due to the transfer of £4.3 million from the fund during the year to fund general expenditure. The budget assumptions for future year's budgets continue to include contributions from balances which could deplete available balances to imprudent levels. The depletion of available balances is one of the financial risks facing the council.

63. Significant amounts earmarked from the total general fund balance include £5.734 million for the Schools PPP, £5.809 million for the Waste PFI, £3.225 million for regeneration and housing projects and £3.074 million of revenue support grant funding allocated to specific projects and to be spent in 2007/08.

Going Concern and Accounting for Pensions

64. The council participates in four pension schemes, namely the Local Government Superannuation (Scotland) Scheme, the Police Pensions Scheme, the Fire Pensions Scheme and the Teachers Pension Scheme (administered by the Scottish Executive) . In accounting for pensions, Financial Reporting Standard 17 (Retirement Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. This requirement results in very large future liabilities/ net pensions deficit, as assessed by actuaries, being recognised on the face of the annual accounts.

65. As at 31 March 2007 the combined deficit on the local government, police and fire pension scheme reflected in the council's balance sheet is £336.985 million. This has fallen from £377.777 million in 2005/06. The largest liability was on the police scheme at £197.658 million. The pension liability has a significant impact on the net worth of the council which is reported in the balance sheet at 31 March 2007 as a negative balance of £ 98.305 million. As noted in the explanatory foreward, the Director of Finance has considered the impact this has had on the ability of the council to continue to deliver services in the future and he concludes that the preparation of the accounts under the going concern basis remains appropriate.

Pension funds

66. Dumfries and Galloway Council in its capacity as trustee, administers the local government superannuation scheme (LGPS). This scheme covers the council employees and employees from another eleven bodies. The net assets of the fund at 31 March 2007 totalled £450.397 million, up from £412.429 at 31 March 2006.

67. The council employs external fund managers to manage the pension fund investment assets. The Pension Fund Investment Sub –Committee reviews the performance and considers the investment strategy of the pension fund on a quarterly basis. The council made a number of changes to the fund's management arrangements during 2006/07 to improve diversification by increasing the number of external fund managers responsible for managing the fund's investments.

68. As part of our audit of the pension fund accounts we have agreed a number of areas for improvement in 2007/08. These include a reduction in the value of pension investments held with the council's loans fund, an updated Statement of Investment Principles and Compliance Statement and improved disclosure in certain areas of the accounts.

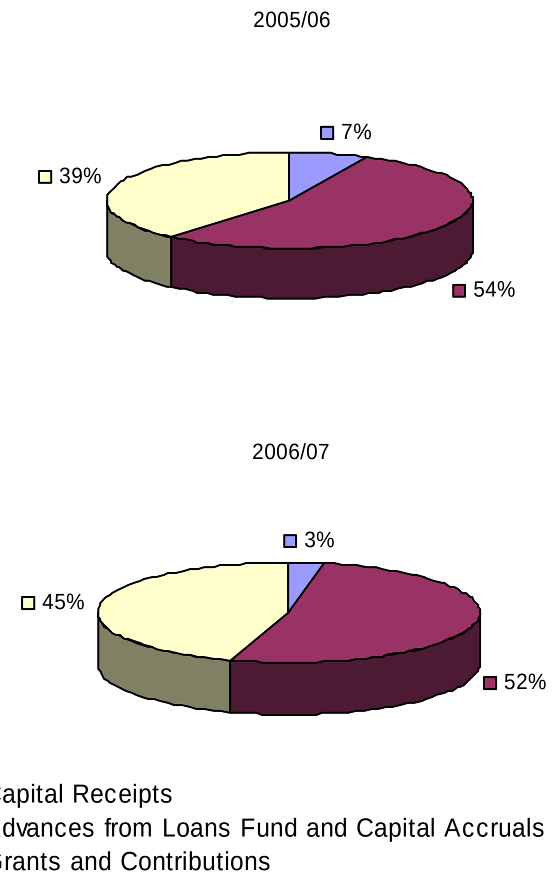
Spending on assets and long-term borrowing

Capital performance 2006/07

69. Following the introduction of the prudential code in April 2004 the council can decide locally on a capital investment strategy which must meet best value requirements as well as being affordable.

70. Capital expenditure in 2006/07 totalled £23.967 million. This has risen slightly from £21.405 million in 2005/06. The proportion of capital expenditure funded by borrowing is in line with the previous year. Capital investment in the last two years was funded as shown below.

Sources of finance for capital expenditure



Capital Slippage

71. The council continued to underspend on its capital programme in 2006/07. As shown in the following table, capital slippage has also occurred in the last two years and remains at a significant level.

Capital slippage in capital programmes

Year	Capital programme £ Million	Capital spend £ million	Underspend /Slippage £ million
2004/05	26.574	18.542	8.032 (30%)
2005/06	27.051	17.286	9.765 (36%)
2006/07	30.334	19.360	10.974 (36%)

72. The main areas of capital slippage in 2006/07 were in respect of :

- slippage of £2.085 million (38% of annual budget) on the Dumfries Leisure Complex. The contractor has produced a revised programme of work and it is currently expected that the facility will open 4 weeks late
- slippage of £ 1.142 million (78% of annual budget) on work to ensure compliance with the Disability Discrimination Act. The council has committed £6.5 million to 2009/10 to this project. Phase 2 is currently nearing completion and Phase 3 is being developed
- slippage of £2.177 million (57% of annual budget) on schools maintenance work. Late additional grant funding was received from the Schools Building Improvement Fund during the year which left insufficient time to fully develop projects. As the total Schools Fund has to be fully spent in 2007/08, this slippage is being carried forward to later years.

The council's capital working group has been tasked with addressing the ongoing slippage in the capital programme. Delays in capital spending can have a significant impact on meeting the council's priorities and objectives and it is essential that the council can reduce slippage on the 2007/08 capital programme.

Key risk area 12

Forward capital programme

73. The council's revised capital plan based on the final position to 31 March 2007 anticipates annual capital expenditure of £33.4 million in 2007/08 and £28.932 million in 2008/09. This is expected to be funded mainly from borrowing and grants. Future receipts from the sale of assets by the council have been earmarked to support revenue expenditure as part of the Financial Efficiency Strategy.

74. The council's loan charges budget for 2007/08 and the next two years has been set at £15 million. This is currently below the forecasted cost of borrowing required to fund future capital programmes (shortfalls varying between £5 million and £4 million across years). The council however expects that slippage on the programme is likely to reduce the level of loan charges to within the assumed level. However if slippage is addressed as planned by management then this would have material implications for future years revenue budgets and as such is being closely monitored.

Significant trading operations

75. The Local Government in Scotland Act 2003 replaced compulsory competitive tendering regulations with a duty to maintain and disclose trading accounts for significant trading operations (STOs), which are required to break even over a three year rolling period. The first three year period ended in 2005/06.

76. The Council has four STOs; Catering and Cleaning, Cleansing and Grounds Maintenance, Roads Maintenance and Property Maintenance. As shown in the following table three of the four STOs made deficits in 2006/07 and failed to achieve the statutory rolling break even target:

Surplus/ deficit on statutory trading operations

	2006/07 surplus/(deficit) £000	3 Year surplus/(deficit) £000
Catering and Cleaning service	(449)	(1,780)
Cleansing and Grounds Maintenance Service	(733)	(2,024)
Roads Maintenance Service	441	995
Property Maintenance Service	(1,171)	(2,168)
Total	(1,912)	(4,977)

77. Our review of the council's STOs found overall that services have been managed in accordance with very old contracts which include out of date specifications. Until recently, contracts had not been subject to market testing and services had not been bench marked on a regular basis to confirm that services were providing best value. The exception to this is the Roads Maintenance service which has been market tested on a more regular basis. In addition Grounds Maintenance has in the past been subject to benchmarking exercises. As noted in the following paragraphs, action is however being taken by management to address these issues.

78. **Catering and Cleaning service**: the trading performance of the catering and cleaning service has encountered exceptional additional costs over the last two financial years relating to equal pay compensation paid to staff. While removing these additional charges would have resulted in the service achieving a small surplus of £0.034 million in 2006/07, it still would have failed to achieve the

three year breakeven target. While there is to be a formal review of the building cleaning service in 2007/08, there are no immediate plans to market test catering services. This issue is currently being considered by management.

79. **Cleansing and Grounds Maintenance service**: the cleansing and grounds maintenance service has returned deficits in each of the last three financial years. To address these trading difficulties the council carried out a review of the cleansing service which recommended that the service should be subject to market testing. The council has approved subjecting the service to competitive tender on the basis of three bids covering refuse collection, street cleansing and combined. It is expected that the new contract will be awarded in July 2008. The competitive tendering process will provide the council with an opportunity to review the contract specification and charge out rates.

80. The competitiveness of the Grounds Maintenance Service was last formally tested around 10 years ago and there is a need for the council to take steps to ensure they can demonstrate best value in this service.

81. **Property Maintenance service**: the council's property maintenance service is also facing significant trading difficulties with 2006/07 being the third consecutive year in which the service has returned a deficit. The service however incurred one off additional staff costs during the year caused by reductions in the workforce through early retirements and redundancies. This, along with increased fuel and material costs and a reduction in the level of work required by the Dumfries and Galloway Housing Partnership (DGHP) contributed to the year end deficit.

82. The DGHP, which makes up 70% of property maintenance's workload, has retendered their contracts for responsive maintenance, heating servicing and maintenance and grounds maintenance. Both the council's property maintenance and grounds maintenance services submitted tenders for this work. The results of the tender process have recently been announced. The bids from both the property maintenance and grounds maintenance services were unsuccessful and they have not been re-awarded the contracts by the DGHP. We are advised that the relevant employees are to transfer under the terms of the TUPE regulations at the end of March 2008. The impact of losing this contract will have to be closely assessed and managed by management and members. We will keep this under review as part of the 2007/08 audit.

Key risk area 13

Financial outlook

Current budget

83. The council's revenue budget for 2007/08 was approved in February 2007. The 2007/08 budget required a contribution from general fund balances of £3.941 million. It was also dependent on

services continuing to achieve demanding savings at times when budgets are under pressure from increasing levels of demand. Containing expenditure within budget in 2007/08 will be challenging and there are particular concerns regarding the ability of Combined Services and Social Work to avoid budget overspends. Some pressure has however been reduced due to the decision to delay the implementation of the single status agreement.

84. As part of the budget setting process for 2008/09 the council has approved a budgeting assumption of a council tax freeze.   Future budget scenarios put to members will therefore include a zero council tax rise. Applying a council tax freeze to future budgets will obviously place even greater pressure on what is already an exceptionally challenging financial position.

Equal pay

85. The 1970 Equal Pay Act makes it unlawful for employers to discriminate between men and women in terms of their pay and conditions where they are doing the same or similar work, work rated as equivalent, or work of equal value. Employees who consider that they have been discriminated against in terms of pay can put forward claims to an Employment Tribunal.

86. As detailed in our 2005/06 report, estimated costs of £4.320 million were recognised in the financial statements for the total one-off cost of dealing with the equal pay legislation. The actual value of compensation paid by the council in 2006/07 totalled £4.504 million. The council's obligation to equal pay continues and a further provision of £ 5.550 million has been made in 2006/07. This relates mainly to claims made by new groups of employees who were not included in the original payments made by the council. These employees have lodged claims with the industrial tribunal. The provision for equal pay also includes the further payments due to employees as a result of delays in implementing single status. As recognised by the council, there is a risk however that the value of compensation due to employees could exceed that provided for and that groups of workers not included in current estimates may be successful in their claims for equal pay compensation.

Efficient government

87. As part of the continuing drive to improve the efficient use of resources committed to delivering public services, the Scottish Executive expect public sector organisations to apply the principles of the efficient government initiative in their day-to-day operations with an aspiration to achieve recurring efficiency gains of £1.5 billion by 2007/08. In the case of councils, efficiency savings have been incorporated into the annual financial settlement provided to councils by the Executive. The principles of the efficient government initiative encourage the delivery of services for lower unit cost without compromising the quality of the service provided.

88. During 2006, councils across Scotland recognised that as part of their partnership arrangement with the Scottish Executive, they had a responsibility to report efficiencies on the Executive's five key operational themes as set out in "Building a Better Scotland" (Procurement, Absence Management, Asset Management, Shared Services and Streamlining Bureaucracy) on a consistent basis. As a result, the Improvement Service was commissioned to devise a set of standard measures which would allow councils to publish unaudited efficiency statements on a common basis. Guidance was issued to all councils in May 2007.

89. The council has been progressing the efficient government agenda as part of its Financial Efficiency Strategy. The council's efficient government statement, which did not require to be audited, records that the council achieved cash efficiencies of £4.75 million against a total target of £3 million (made up from £1.8 m set by the Scottish Executive and £1.2 m set by the council).

90. The efficiencies reported by the council are summarised against the workstreams in the following table:

Efficiencies included in efficiency statement (unaudited):

Efficient Government Theme	Cash efficiency £m	Description of main efficiency
Procurement	0.900	Savings in energy costs through retendering.
Asset Management	0.720	Reduction in staff costs through vacancy and recruitment management.
Managing Absence	0.000	n/a
Shared Services	0.000	n/a
Streamlining Bureaucracy	1.445	Reduced staff costs through service restructuring and control of overtime charges.
Other	1.685	Absorption of inflationary rises in prices in existing budgets and increased income generation from services.
Total efficiencies	**4.75**	

91. Overall the council has complied with the improvement service guidance in preparing the annual efficiency statement. More focus however needs to be given in future statements to the challenging issue of reporting improvements in performance and performance measures. The statement claims that the identified efficiencies did not have an adverse impact on service delivery. This is mainly because all identified efficiencies were cash savings resulting from such actions as changes in procurement methods and cuts in staffing levels, overtime payments etc. The council are continuing to develop a benefits tracking system for assessing the impact of efficiencies on service provision as part of its performance management framework.

92. The Scottish Executive has set efficiency savings targets for the council of £ 3.5 million for 2007/08. The continuing need to secure these efficiencies along with the council's local targets will prove especially challenging for the council.

Future Pension liabilities

93. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions. A recent Audit Scotland report on public sector pension schemes highlighted that the combined funding shortfall and unfunded liabilities of the six local government pension schemes in Scotland may be as high as £53 billion. There are proposals to amend the Local Government Pension Scheme which are designed to reduce the ongoing cost, although these have not yet been implemented.

94. The council's actuary is required to make a three-year assessment of the contributions that should be paid by the employing authorities to maintain the solvency of the pension fund. The contribution levels are based on percentages of employee contributions. This shows that budgeted employer contributions are expected to rise from 290% of employee contributions in 2006/07 to 310% in 2007/08 and 325% in 2008/09. The council has made an allowance for increasing rates of employers pensions contributions in future budget estimates.

Governance

Introduction

95. In this section we comment on key aspects of the council's governance arrangements during 2006/07. We also provide an outlook on future governance issues, including our views on potential risks.

Overview of arrangements in 2006/07

96. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. Based on the work undertaken, we concluded that the council's main systems operated within a sound control environment.

97. A Corporate Governance Assurance Statement is included within the annual financial statements which provides a commentary by the Leader of the Council and the Chief Executive on progress made during the year in taking forward areas for improvement within the council's Code of Corporate Governance. Progress against the action plan has been monitored throughout the year by the Governance Team and this will continue to be reviewed by the council's new Governance and Audit Committee.

Governance and Audit Committee

98. Effective scrutiny is central to good governance, with a significant role for members to scrutinise performance, hold management to account on service delivery and support the reform and modernisation agenda. The success of a council's audit committee as part of the council's governance arrangements is very much dependent on the extent to which members understand the role of an audit committee and engage in providing effective scrutiny.

99. Prior to the elections in May 2007, our assessment of the council's former Audit Committee was that it adhered to CIPFA's guidance on Audit Committee Principles and made a sound contribution to the council's overall control environment. The council has now established a new Audit and Governance Committee. This has seen an increase to the committee's remit and an increase in membership.

100. Our initial impressions of the new Audit and Governance Committee have overall been encouraging. Given the degree of change from the previous structure and responsibilities of the former Audit Committee, the council should consider reviewing the effectiveness of the new Governance and Audit Committee against good practice guidance. In particular, consideration should be given to the extent to which the committee is operating apolitically and whether the number of members on the

committee is correct. Our past experiences have shown that the more effective audit committees operate with a smaller number of members than the current Governance and Audit Committee.

Internal Audit

101. In December 2006, CIPFA published a revised Code of Practice for Internal Audit in Local Government, which updated the previous 2003 Code. We carry out an annual review of the council's internal audit arrangements and found overall that during 2006/07, the internal audit service complied with the Code of Practice. This allowed us to take assurance from the work of internal audit in most of the main financial systems. There is scope however for internal audit to improve their approach to audit planning, documenting the work done and performance management. Actions have been agreed to address these areas and we will review progress as part of future audits.

Systems of internal control

102. In his annual report for 2006/07 the Chief Internal Auditor provided his opinion that based on the internal audit work undertaken during the year, reasonable assurance can be placed upon the adequacy and effectiveness of the council's internal control systems. The Corporate Governance Assurance Statement identified two key areas of the council's business where controls need to improve. These related to the:

- lack of risk management strategies at a service level
- lack of a council wide business continuity plan resulting in the risk that key services and functions cannot be provided in the event of computer systems failing.

103. It is essential that improvements are secured in the council's risk management and business continuity arrangements.

104. As part of our work to provide an opinion on the annual financial statements we assessed the extent to which we could gain assurance on a number of the council's main financial systems. We assessed the following central systems as having a satisfactory level of control for our purposes:

- payroll
- main accounting system
- budgetary control
- creditors payments
- debtors and income system
- council tax billing and collection
- non domestic rates billing and collection
- pensions administration
- housing and council tax benefits.

105. We have reported to management those areas in which controls could be further strengthened and an improvement action plan has been agreed.

Prevention and detection of fraud and irregularities

106. At the corporate level, the council has appropriate arrangements in place to prevent and detect fraud, inappropriate conduct and corruption. These arrangements include an anti-fraud and corruption policy, a whistle blowing policy, codes of conduct for elected members and staff, and defined remits for relevant regulatory committees.

NFI in Scotland

107. In 2006/07 the council again took part in the National Fraud Initiative (NFI) in Scotland. The exercise is undertaken as part of the audits of the participating bodies. NFI 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. These include housing benefit fraud, occupational pension fraud and payroll fraud. For 2006/07 the exercise was extended to include information about tenants and councils were asked to submit further specified datasets where the risks merited their inclusion. The NFI has generated significant savings for Scottish public bodies (£27million to 2005) and, if fraud or overpayments are not identified in a body, assurances may be taken about internal arrangements for preventing and detecting fraud.

108. The NFI 2006/07 results (data matches) were made available to councils on 29 January 2007 via a new secure web-based application. Participating bodies follow up the matches, as appropriate, and record the outcomes of their investigations in the application. We monitored the council's involvement in NFI 2006/07 during the course of our audit.

109. The council has taken a positive approach to NFI. While the exercise is still to be completed, progress is continuing. Attention should however be given to the referrals identified for Police services, where the review by officers has not yet been started.

110. In other areas matches have been prioritised and the council has concentrated on the high priority cases. Low priority risk-based matches, where the returns are likely to be small in relation to the effort required, have not yet been examined. A total of 1399 referrals were received for review in 2006/07. At the end of September, 716 referrals had been investigated with 27 in the process of being followed up. Total savings identified to date for 2006/07 are in the region of £0.039 million. At this stage, it would appear that savings will be down on those achieved in the previous exercise possibly due to the preventative effect of previous work.

111. Interim reports on progress have not yet been taken to Members but will be reported once the exercise is nearer completion. Monthly internal progress reports are maintained. Progress reports can also be accessed direct from the NFI web-based application by audit.

Future Outlook

112. CIPFA/SOLACE have recently produced Delivering Good Governance in Local Government – Framework which sets out principles and standards to help local authorities to develop and maintain their own codes of governance and discharge their accountability for the proper conduct of business. The council are aware of this new guidance. The publication of the Scottish guidance notes will aid any future reviews of the council's corporate governance structures against the framework.

Financial statements

Introduction

113. In this section we summarise key outcomes from our audit of the council's financial statements for 2006/07. We comment on the significant accounting issues faced and provide an outlook on future financial reporting issues. We audit the financial statements and give an opinion on:

- whether they present fairly the financial position of the council and its expenditure and income for the year
- whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.

114. We also review the Corporate Governance Assurance Statement by considering the adequacy of the process put in place by the council to obtain assurances on systems of governance and internal financial control and assessing whether disclosures in the statement are consistent with our knowledge of the council.

Overall conclusion

115. We have given an **unqualified** opinion on the financial statements of Dumfries and Galloway Council for 2006/07.

116. We have, however, drawn attention to a failure to comply with the statutory requirement that all significant trading operations breakeven on a rolling three year basis as three of the council's four statutory trading operations returned cumulative deficits at 31 March 2007. This does not impact on the fairness of the financial statements and, therefore, does not affect the opinion on the accounts.

117. The Local Government in Scotland Act 2003 requires councils to maintain and disclose trading accounts for significant trading operations, which are required to break-even over a three year rolling period. As highlighted in paragraph 76 of this report, three of the four significant trading operations made an aggregate loss of £5.97 million in the three years to 31 March 2007, with the result that the council has failed to meet this statutory requirement. As noted in the authority's financial statements, the Cleansing and Grounds maintenance and the Property Maintenance trading operations have encountered significant trading difficulties. The additional liability arising from equal pay compensation payments has had a negative impact on the financial performance of the Catering and Cleaning service.

118. The council's un-audited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June. While the package of final accounts working papers were available to audit in line with agreed timescales, there were some gaps in the papers provided, particularly in the level of detail given in some of the reconciliation statements. It has been agreed that further attention will be given to this area. Audited accounts were finalised prior to the target date of 30 September 2007 and are now available for presentation to the council and publication. The financial statements are an essential means by which the council accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources.

Accounting practice

119. Local authorities in Scotland are required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP'). The 2006 SORP required a number of significant changes to be made to the 2006/07 financial statements to make them more consistent with the accounts of other public and private sector entities. These included:

- replacement of the consolidated revenue account with a traditional income and expenditure account
- a new statement that reconciles the income and expenditure account surplus or deficit for the year to the general fund surplus or deficit
- replacement of the statement of total movement in reserves with a statement of total recognised gains and losses
- restatement of the 2005/06 comparative figures.

120. Overall, we were satisfied that the council had prepared the accounts in accordance with the revised SORP.

121. The council made a number of adjustments to reflect our findings from the audit. There were no unadjusted errors remaining. Details of significant issues arising in the course of the financial statements audit are summarised below.

Title Deeds Checks

122. We have reported for a number of years that the council is to complete an exercise to establish where all its heritable properties are, who holds title to them and what the value is. This is important to ensure that both the council's and common good assets are fairly stated. While progress has been made in this area during the year there still remains a considerable level of checks to be carried out. We will continue to monitor this issue in 2007/08.

Key risk area 14

Delays in spending Resource Transfer monies

123. The 2006/07 creditors include a balance of £ 2.6 million relating to resource transfer monies received from NHS Dumfries and Galloway and which had not been spent by the council at the year end. The level of this underspend has remained in the region of £2.5 million since 2004/05. We are advised that underspends have resulted from delays in setting up care projects and identifying appropriate care packages for individuals which could be funded in line with the terms of the resource transfer agreements. Action is continuing by officers to address this issue to ensure that resource transfer monies received by the council are fully utilised in the provision of appropriate services.

Key risk area 15

Legality

124. Each year we request written confirmation that the council's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes. The Director of Finance , the council's Proper Officer, has confirmed that to the best of his knowledge and belief and having made appropriate enquiries of the council's management team, the financial transactions of the council were in accordance with the relevant legislation and regulations governing its activities. Details of the legality issues arising from our audit are summarised below.

125. Local authorities with registered charitable bodies (ie registered trust funds) are required to comply with the requirements of the Charities Accounts (Scotland) Regulations 2006. In effect, this means a full set of financial statements is required for each trust fund. It has now been agreed with the Office of the Scottish Charities Regulator (OSCR) that as an interim measure in 2006/07, reliance can be placed on the existing disclosures for trust funds in the council's financial statements. Further discussions between OSCR and CIPFA will take place with respect to the requirements for 2007/08 onwards.

126. The council are required to comply with the provisions of the Disability Discrimination Act 1995. In order to meet the requirements of the Act the council will have to ensure that their public buildings are accessible by disabled people. The council's statutory performance indicator for 2006/07 shows that only 34% of public buildings are accessible. In addition, there was considerable slippage in capital expenditure on the adaptations of buildings capital programme in 2006/07. There is a need for the council to ensure fuller compliance with the Disability Discrimination Act in terms of

accessibility of public buildings. We are advised that the level of slippage in capital spending is reducing in 2007/08.

127. There are no additional legality issues arising from our audit which require to be brought to members' attention.

Financial reporting outlook

128. Overall the council is well placed to continue to prepare annual financial statements in accordance with accounting and statutory requirements. It has a record of responding positively to audit issues and to changing accounting rules. Challenges ahead include a number of changes that have been made to the 2007 SORP.

129. The main change is that the 2007 SORP requires authorities to comply with financial reporting standards (FRS) 25 and 26 in respect of loans, from 2007/08. This will result in large expenditure entries to the income and expenditure account as the SORP requires premiums on loans which have been rescheduled, to be written off in line with the FRSs. At present, councils are able to write off premiums over the period of the replacement loan, which can be up to 40 to 50 years. Regulations restrict the write off periods for new premiums incurred on LOBOs from 1 April 2007 to a maximum of 20 years. These changes do not impact on council tax levels.

130. Central government and NHS bodies are to move from UK Generally Accepted Accounting Principles to International Financial Reporting Standards (IFRS) with effect from 2008/09. The government also announced its intention to publish Whole of Government Accounts on an IFRS basis from 2008/09. It was recognised that there would need to be discussions with CIPFA/ LASAAC about the introduction of IFRS-based accounts for local government. Of particular note is that IFRS do not address PFI accounting in the public sector. The Treasury are therefore currently considering the most appropriate accounting treatment for PFI public sector transactions. If IFRS principles, or similar, were applied in the public sector then many PFI assets are likely be brought onto public sector balance sheets.

Final Remarks

131. We have made a number of recommendations in the various reports we have issued during the course of the year and have obtained assurances from officials that action will be taken as appropriate.

132. Attached to this report is an action plan setting out the key risks identified by the audit which we are highlighting for the attention of members. In response, officers have considered these issues and have agreed to take the specific steps set out in the column headed ‘planned management action’. On occasion, officers may choose to accept the risk and take no action. Alternatively, there may be no further action that can be taken to minimise the risk. Where appropriate, the action plan clearly sets out management’s response to the identified risks.

133. A mechanism should be considered and agreed by members for monitoring the effectiveness of planned action by officers. We will review the operation of the agreed mechanism as part of the 2007/08 audit.

134. The co-operation and assistance given to us by Dumfries and Galloway Council members and staff is gratefully acknowledged.

Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1	**Statutory performance indicators** The overall quality of the working papers to support the statutory performance indicators (SPIs) continue to be poor. ***Risk: the accuracy of the council's SPIs cannot be validated resulting in indicators being reported as unreliable.***	Background information provided by the Auditor will be used to prioritise the sequence by which services will be approached and supported in improving the procedures to meet the SPI Audit process. The objective for each service will be to identify the trail of necessary and sufficient information required to meet the Audit process and to implement the procedures to support and sign-off these requirements.	Group Manager – Policy & Performance	March 2008
2	**Financial pressures** The council are facing significant financial pressures. To achieve current and future budgets, services will have to achieve considerable savings. These exceed the level of savings that the council has been able to achieve in previous years. ***Risk: the savings made to date are non recurring and cannot be sustained. Future budget cuts cannot be achieved without adversely impacting on the quality or levels of services.***	All proposed savings measures to be subject to thorough scrutiny and review to ensure achievability/sustainability. The Corporate Financial Efficiency Strategy, and individual savings proposals, also to be subject to thorough risk appraisal to ensure that the quality and level of service is protected where possible.	Chief Executive / Director of Finance	January 2008 (for savings to be reflected in the 2008/09 budget)
3	**Workforce consolidation** The council has yet to develop a natural wastage/redeployment and efficiency programme to support the planned staff cuts necessary to fund future single status costs. ***Risk: the savings required from staff cuts are not released in time to fund single status costs.***	A revised policy on Redundancy/Redeployment was agreed by members on 26-10-07. A revised Recruitment Protocol is being introduced with more central involvement and monitoring of recruitment activity.	Group Manager (Human Resources)	October 2007 November 2007 December 2007

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
		Funding for the creation of a team of 6 officers to support the natural wastage/redeployment and efficiency programme has been agreed. However, it is recognised that clear management decisions on service change and staffing reductions, which would trigger redeployment or retraining, are still to be taken to direct the work of this team.		
4	**Depletion of available balances** Future budgets continue to rely on contributions from available general fund balances**.** ***Risk: general fund balances will fall below the council's target of £6 million to possible imprudent levels. There are inadequate reserves to fund any unforeseen costs.***	Full information to be provided to Members on the reasons for the retention of balances and the risks associated with the depletion of balances as part of the budget development process. A specific report on the appropriate level of balances will be presented to the Finance Sub Committee and all budget overview reports will outline the impact on balances of individual budget strategies.	Director of Finance	January 2008
5	**Statutory trading activities and Homecare Service within Combined Services** Particular budget pressures and trading difficulties are being experienced by the council's Statutory Trading Activities and the Homecare Service within Combined Services. Three out of four of the council's statutory trading activities have returned deficits and have failed to achieve the break even target over a three year period. ***Risk: the Homecare Service and the Statutory Trading Activities continue to return deficits and fail to achieve the statutory breakeven target.*** ***The council cannot demonstrate the achievement of best value by the statutory trading operations.***	The trading position of the Property Maintenance Unit will be reassessed taking into account the loss of the DGHP contracts. Refuse services out to tender July 2008. Street cleaning out to tender July 2008. Major review of council Home Care Service now in place – action plan early 2008.	Corporate Director of Combined Services	April 2008 July 2008 July 2008 Spring 2008

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
6	**Agreement of single status** The council has yet to reach an agreement on a single status pay and grading structure. ***Risk: until single status is implemented the costs to the council cannot be reliably estimated and continue to represent a financial risk***	A joint negotiation process between the council and the trade unions is continuing to ensure the implementation of single status as early as possible. Based on the best information currently available, single status costs have been estimated and these costs reflected within the council's financial plans. These estimates will be continually reviewed and updated as appropriate up to the date of implementation.	Chief Executive	March 2008
7	**Smarter Schools PPP** There has been some slippage in the expected financial close date for the schools PPP project. ***Risk: the target financial close date is not achieved resulting in delays in the start of the construction programme and possible financial penalties to the council.***	Progress against the agreed project plan is monitored/reported on a daily/weekly basis and an escalation process and fortnightly project board meetings have been implemented to ensure that slippage is minimised and effectively managed.	Project Director (Schools PPP)	December 2007
8	**Schools estate management plan** Decisions on the future of the schools estate and possible closure programme have not been made. A long term financial plan has not been established to finance the improvements required to the schools not covered by the PPP. The long term commitment to contribute to the PPP sinking fund is a considerable future cost pressure. ***Risk: the schools estate management plan cannot be progressed and the funding required for the necessary improvements is not identified and included in future financial plans. The council cannot afford to finance the PPP affordability gap.***	An updated School Estate Management Plan is currently being prepared and will be presented to Members before the end of the current financial year. Provision has been included within existing financial plans to address the projected costs of the Schools PPP project and the loan charges associated with the development of the 2A Schools project. The affordability of both projects, and the requirements associated with the remainder of the schools estate, will be continually reviewed on an ongoing basis as part of the annual budget process and at key stages (eg at PPP financial close).	Operations Manager (Property Services) / Director of Finance	March 2008

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
9	**Corporate asset management plan** The council has yet to finalise and approve the corporate asset management plan and the plans for the office, community, industrial and schools estates. ***Risk: assets are not effectively managed and do not contribute to achieving the council's objectives and priorities.***	The officers Strategic Property Group met in October 2007 and agreed a series of actions to complete the 4 Estate Management Plans which will form the Corporate AMP. An action plan and timetable is currently being prepared but the work is expected to be completed by the end of the financial year. One of the key actions is to hold a Member seminar to obtain member input into the development and finalisation of the estate management plans in particular the Office Estate Management Plan. The seminar is scheduled for 13 December 2007.	Group Manager – Policy & Performance	March 2008 December 2007
10	**Performance management framework** The council remains to fully populate the Covalent performance management system and to roll out implementation to services. ***Risk: the Covalent system is not fully implemented and used effectively across the council. It does not provide the information required by management and members to manage and improve performance.***	(1) The Officers Covalent Users Group will focus on the quality of information that has been used to populate Covalent. This work commenced in September 2007, with a programme of scrutiny to be completed by December 2007. (2) A report will be presented to Corporate Management Team in October 2007 to ensure that all directorates examine the information on Covalent to ensure that it is fit for purpose.	Group Manager – Policy & Performance	December 2007 October 2007

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
11	**Business continuity and risk management** The council does not have a corporate business continuity plan in place and there is a need to improve risk management arrangements, particularly at a service level. ***Risk: the council cannot continue to provide key services in the event of computer systems failing. Potential risks have not been identified and plans have not been identified for minimising their effect.***	Following a review to improve the Council's Civil Contingencies, Risk Management and BCM arrangements the Council recently appointed an Operations Manager Civil Protection, Resilience and Corporate Risk. A work plan is currently being prepared and will incorporate the Audit issues raised. A Report outlining where we stand at present and where we are going will be taken to the Governance and Audit Committee on 27 Nov. This report will outline a proposed overall strategy for FY 2008/09 and outline a timetable for delivery. It is also proposed to appoint a FT Officer to advise on Corporate Risk and Business Continuity.	Operations Manager – Civil Protection, Resilience and Corporate Risk	March 2008 November 2007
12	**Capital slippage** There has been capital slippage for the third consecutive year and the council continues to underspend against its capital plans. ***Risk: delays in the completion of capital projects will prevent the council from achieving its objectives and priorities.***	A report is being presented to the Finance Sub Committee on 22 November 2007 identifying reasons for slippage and measures to address them. These measures will include the requirement for a rigorous business case and accurate cash flow forecasting as part of the project bidding process to ensure that resultant financial plans are more realistic.	Operations Manager (Property Services) – as Chair of the Capital Officers Working Group	November 2007 March 2008

Action Point	Risk Identified	Planned Management Action	Responsible Officer	Target Date
13	**Loss of contracts with the Dumfries and Galloway Housing Partnership (DGHP)** The Property Maintenance and Grounds Maintenance Services have not been re-awarded the contracts for responsive repairs, heating maintenance and grounds maintenance with the DGHP. ***Risk: the continuity of the current services being carried out Property Maintenance and Grounds Maintenance is disrupted and the handover process is not closely managed.***	Ensure continuity and deliverability of existing contract to 31 March and ensure the smooth TUPE transfer of all affected staff.	Corporate Director of Combined Services	March 2008
14	**Confirmation of assets to title deeds** The council has yet to complete the exercise agreed in 2005/06 to confirm the fixed assets held by the council and the Common Good to title deeds. ***Risk: the council's and Common Good's fixed assets are not fairly reflected in the accounts.***	Complete exercise to identify known titles by end November 2007. Develop PMIS to provide direct links to electronic titles & GIS by end June 2008. Implement electronic links by end September 2008. Risk assess the identified deficiencies by end March 2009. Address high risk deficiencies April 2009 onwards.	Operations Manager (Property Services)	November 2007 June 2008 September 2008 March 2009
15	**Delays in spending resource transfer monies** The council has not fully utilised the resource transfer monies received from Dumfries and Galloway NHS. Underspends in the region of £2.5 million have continued since 2004/05. ***Risk: delays in setting up appropriate care projects continue despite the availability of funding. Services are not being provided to those in need.***	Following on from work done in 2006/07, a joint exercise is being undertaken with the NHS to ensure that appropriate care services are identified, agreed and funded through the resource transfer monies.	Chief Social Work Officer / SWIA Workstream 4 Lead Officer	March 2008