

Highland and Islands Fire Board

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



Contents

Introduction	2	Performance	9
Financial statements	3	Final Remarks	10
Governance	7	Appendix A: Action Plan	11



Introduction

1. This report summarises the findings from our 2006/07 audit of Highland and Islands Fire Board. The scope of the audit was set out in our audit fee letter issued on 1 February 2007.
2. The financial statements of the Joint Board are the means by which it accounts for its stewardship of the resources made available to it and its financial performance in the use of these resources. It is the responsibility of the Joint Board to prepare financial statements that present fairly its financial position and the income and expenditure for the year.
3. The members and officers of the Joint Board are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:
 - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed;
 - the Joint Board's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests;
 - the Joint Board has adequate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability;
 - the systems of internal control provide an appropriate means of preventing or detecting material misstatement, error, fraud or corruption;
 - the Joint Board has proper arrangements for securing best value in its use of resources.



Financial statements

Introduction

4. In this section we summarise key outcomes from our audit of the Joint Board's financial statements for 2006/07. We also summarise key aspects of the Joint Board's reported financial position and performance to 31 March 2007.
5. We audit the financial statements and give an opinion on:
 - whether they present fairly the financial position of the Joint Board and its expenditure and income for the year; and
 - whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.
6. We also review the Statement on the System of Internal Financial Control by considering the adequacy of the process put in place by the Joint Board 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 Joint Board.

Overall conclusion

7. We have given an **unqualified** opinion on the financial statements of Highland and Islands Fire Board for 2006/07.
8. The unaudited financial statements were submitted to the Controller of Audit by the deadline of 30 June. The Joint Board is required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP').
9. Overall, we were satisfied that the financial statements were prepared in accordance with the revised SORP. There were two significant adjustments made to the figures included in the un-audited financial statements provided for public inspection. Details of the adjustments are summarised below in paragraphs 17 and 18.



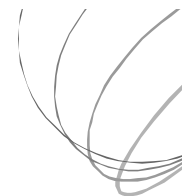
Financial position

Going concern

10. The Joint Board's balance sheet at 31 March 2007 shows net liabilities of £57.359 million. Auditing standards require auditors to consider an organisation's ability to continue as a going concern when forming an opinion on the financial statements. One of the indicators that may give rise to going concern considerations is an excess of liabilities over assets.
11. The net liability position is due to the requirements of Financial Reporting Standard 17 (retirement benefits) where there is an obligation to recognise the Joint Board's full pension obligations in the year they are earned. This technical accounting requirement has had no impact on the underlying basis for meeting current and ongoing pension liabilities which will be met, as they fall due, by contributions from constituent authorities in the normal way. In common with similar authorities, the Joint Board has considered it appropriate to adopt a going concern basis for the preparation of the financial statements.

Revenue performance 2006/07

12. The Joint Board's net operating expenditure for 2006/07 amounted to £20.885 million (after elimination of FRS 17 pension adjustments) and was met by constituent authorities' contributions of £21.302 million resulting in a small surplus for the year of £0.417 million. In his Report the Treasurer summarises performance against budget. The major factors contributing to the surplus were savings in staff costs; reduced activity in the retained part of the service and advantageous borrowing rates reducing capital charges in the year.
13. The Joint Board holds a general fund reserve as a contingency for unexpected events or emergencies. It is for the Joint Board to determine its strategy for managing such funds after taking account of local circumstances. At 31 March 2007 the Joint Board held a general fund reserve of £1.336 million. In our Report to Members on the 2005/06 Audit we highlighted that the Joint Board had yet to adopt a clear strategy for the use of these funds. A strategy was agreed by the Joint Board in November 2006 to retain approximately 3% of the contributions from constituent authorities for contingencies.
14. Capital expenditure totalled £3.685 million and was funded by government grant of £3.582 million and current revenue of £0.103 million.

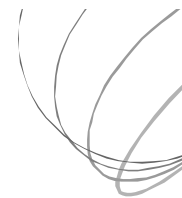


Issues arising from the audit of the financial statements

15. The financial statements are an essential means by which the Board accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources. The Board's unaudited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June. Final accounts preparation procedures and working papers were good and this enabled the audit to progress smoothly.
16. 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'). A number of adjustments were made to the figures included in the unaudited financial statements made available for public inspection.
17. The most significant change related to the construction of a fire station in the Western Isles whereby the Board paid £0.18 million to Comhairle Nan Eilean Siar before 30 March 2007. The agreement between the Joint Board and the Comhairle requires the Comhairle to make payments on behalf of the Joint Board on the basis of signed certificates issued by the contract administrators. The fire station is being built as part of a community project on land owned by the Comhairle. As the Joint Board was unable to provide a signed certificate at 31 March 2007 to substantiate the figure in the financial statements for the asset under construction the financial statements were adjusted to reduce assets under construction by £0.18 million and increase sundry debtors by £0.18 million. This adjustment had no impact on the income and expenditure account.

Action point 1

18. There were two other adjustments to the financial statements. The first adjustment increased the net pension liability and the pension reserve in the balance sheet by £1.184 million. The second adjustment related to an adjustment to debtors and creditors in the balance sheet. Neither adjustment had an effect on the income and expenditure account.

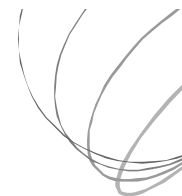


Financial outlook – pension liabilities

19. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long and the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions.
20. In accounting for pensions, FRS 17 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 large future liabilities being recognised in the financial statements.
21. The firefighters' pension scheme is unfunded and, therefore, has no assets to be valued. Note 9 to the Balance Sheet highlights that the present value of scheme liabilities at 31 March 2007 is £70.264 million. As the scheme is unfunded, the pension liability will fall to be met by serving firefighters' contributions and by taxpayers in the future (through constituent authorities' contributions).
22. The Board's estimated pension liabilities for support staff at 31 March 2007 exceeded its share of assets in the Highland Council Pension Fund by £1.462 million. The full triennial actuarial valuation of the Highland Council Pension Fund was reported in early 2006. Factors such as the volatile stock market and increasing life expectancy have resulted in the funding level, calculated as the ratio of fund assets to past service liabilities, falling from 105% as at March 2002 to 92% as at March 2005.
23. The 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 fund. The contribution levels are based on percentages of employee contributions, normally 6% of salary. This shows that budgeted contributions are expected to rise from 270% of employee contributions in 2006/07 to 290% in the 2008/09 financial year.

Legality

24. Each year we request written confirmation from the Treasurer that the Joint Board's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of other senior officers, the financial transactions of the Joint Board were in accordance with the relevant legislation and regulations governing its activities.
25. There are no additional legality issues arising from our audit which require to be brought to members' attention.



Governance

Introduction

26. In this section we comment on key aspects of the Joint Board's governance arrangements during 2006/07.

Overview of arrangements in 2006/07

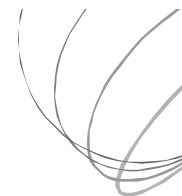
27. Corporate governance is concerned with structures and processes for decision making, accountability, control and behaviours at the upper levels of the organisation. The Joint Board has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.
28. A Statement on the System of Internal Financial Control is included within the annual financial statements, and highlights the Treasurer's view that reasonable assurance can be placed upon the adequacy and effectiveness of the Joint Board's internal financial control system. The statement highlighted the need to improve high level controls within the payroll and creditor systems. The Treasurer has indicated that appropriate arrangements will be in place by 31 March 2008.
29. The need to improve high level controls within the payroll and creditors systems was raised in our Report to Members on the 2005/06 Audit and the agreed date for implementation of our recommendation was March 2007. It is disappointing to note the timescale for implementation of this recommendation has slipped by one year.

Action point 2

30. The statement complies with accounting requirements and is consistent with the findings of our audit.

Systems of internal control

31. The Joint Board's financial transactions are processed through Highland Council's financial systems. It is the responsibility of the Council's management to maintain adequate financial systems and associated internal controls. The auditor evaluates significant financial systems and associated internal controls both for the purpose of giving an opinion on the financial statements and as part of a review of the adequacy of governance arrangements.
32. Our review of these systems was conducted as part of the audit of Highland Council, supplemented by specific audit work on the Joint Board's financial statements. Overall there are no material issues of concern in relation to the operation of the main financial systems.



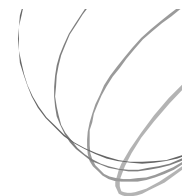
33. Internal audit plays a key role in the Joint Board's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. The Highland Council's Internal Audit section provided an internal audit service to the Joint Board during 2006/07.
34. Each year we undertake an overview of internal audit arrangements which includes an assessment of whether or not we can place reliance on internal audit work in order to reduce our own input. We concluded that internal audit work within the Board continues to be of a sufficient standard to allow us to rely on it.

Prevention and detection of fraud and irregularities

35. The Joint Board has appropriate arrangements for the prevention and detection of fraud and corruption. These arrangements include a strategy for the prevention and detection of fraud and corruption, written procedures for the investigation of suspected cases of fraud and corruption and a whistle blowing policy.

NFI in Scotland

36. In 2006/07 the Joint Board 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. The NFI has generated significant savings for Scottish public bodies (£27 million to 2005) but, if fraud or overpayments are not identified by a body, assurances may be taken about internal arrangements for preventing and detecting fraud.
37. The NFI 2006/07 results (data matches) were made available to audited bodies 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 Joint Board's involvement in NFI 2006/07 during the course of our audit.
38. The Joint Board is currently updating its records in respect of the work done in relation to NFI which produced sixty-eight data matches. A number of the matches (twelve) relate to benefit claimants and these have been referred to the Council for further investigation. To date no fraud or overpayments have been confirmed and we will continue to monitor progress in the clearance of the data matches by the Joint Board.



Performance

Introduction

39. In this section we summarise key aspects of the Board's reported performance and provide an outlook on future performance.

Statutory performance indicators

40. The Board has a statutory duty to collect, record and publish specified performance indicators and, so far as is practicable, ensure they are accurate and complete. The Accounts Commission issue a Direction each year detailing the statutory performance indicators (SPIs) that require to be published and external auditors review the Board's arrangements and return details of the indicators, including an opinion on their reliability, to Audit Scotland headquarters to enable compilation of national reports on performance.
41. We assessed all four of the Board's statutory performance indicators as reliable.

Community fire safety

42. SPIs show that the rate of incidents per 10,000 of the population resulting in casualties increased slightly in 2006/07 to 1.3 from 1.2 in 2005/06. This is lower than the 2005/06 Scottish average of 2.6. The rate of accidental dwelling fires per 10,000 of the population decreased slightly to 7 in 2006/07 from 7.1 in 2005/06. This is also lower than the 2005/06 Scottish average of 11.0.

Call response time

43. In 2006/07 the Joint Board was able to answer 95.6% of all calls within 2 minutes which is slightly below the figure of 96% in 2005/06.

Proportion of working time lost due to sickness absence

44. The level of absence for firefighters has reduced significantly since 2004/05 and was 3.6% for 2006/07 and is significantly below the 2005/06 national average of 6.4%. The level of absence for support officers has also decreased to 2.5% during 2006/07 which is significantly below the 2005/06 national average of 5.4%:



Final Remarks

45. 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 the Board. The action plan sets out management's response to the identified risks.
46. The members of Highland and Islands Fire Board are invited to note this report. We would be pleased to provide any additional information that members may require.
47. The co-operation and assistance given to us by officers of the Joint Board is gratefully acknowledged.

Audit Scotland
24 October 2007



Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Refer Para. No	Risk Identified	Planned Action	Responsible Officer	Target Date
1	17	Financial statements The Joint Board was unable to provide a signed certificate at 31 March 2007 to substantiate a figure in the financial statements for an asset under construction. <i>Risk: the financial statements do not accurately reflect the assets owned by the Joint Board.</i>	Valuation certificates will be obtained for all assets under construction at financial year ends.	Treasurer	April 2008
2	29	Governance The need to improve high level controls within the payroll and creditors systems was raised in our Report to Members on the 2005/06 Audit. The timescale for implementation has slipped by one year to March 2008. <i>Risk: there is a risk of failure of high level controls over the payroll and creditors systems.</i>	The exercise is now underway and the service will complete it soon.	Head of Corporate Services	October 2007