

# Lothian and Borders Fire and Rescue Board

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



October 2007







# Contents

<b>Introduction</b>	<b>2</b>
<b>Financial statements</b>	<b>3</b>
<b>Governance</b>	<b>7</b>
<b>Performance</b>	<b>10</b>
<b>Final Remarks</b>	<b>12</b>
<b>Appendix A: Action Plan</b>	<b>13</b>



# Introduction

1. This report summarises the findings from our 2006/07 audit of the Lothian and Borders Fire and Rescue Board. The scope of the audit was set out in our audit plan issued in March 2007.
2. The financial statements of the 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 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 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 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 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 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 board's financial statements for 2006/07. We also summarise key aspects of the 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 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 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 organisation.

## Overall conclusion

7. We have given an **unqualified** opinion on the financial statements of the Lothian and Borders Fire and Rescue Board for 2006/07.
8. The unaudited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June. The only amendment to the unaudited figures was a reduction in both debtors and creditors to remove an erroneous entry of £0.201 million. Final accounts preparation processes were generally satisfactory, but there is scope for improvement within working papers so that a stronger audit trail is provided.
9. The board is required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP'). A range of presentational changes were made to the unaudited accounts made available for public inspection to reflect the disclosure requirements set out in the SORP. As part of the closedown arrangements, we would suggest that the CIPFA disclosure checklist is completed to ensure that the unaudited accounts are presented in accordance with the requirements of the SORP. This will minimise the number of changes required as part of the audit process.



10. Audited accounts were finalised prior to the target date of 30 September 2007 and are now available for presentation to the board and publication.

## Financial position

11. The surplus or deficit on the income and expenditure account measures the board's financial result for the year, recognising the resources that have been consumed and generated in accordance with Generally Accepted Accounting Principles. The board's net operating expenditure in 2006/07 amounted to £63.334 million and was met by constituent authorities' contributions of £47.285 million, resulting in an income and expenditure deficit for the year of £16.049 million.
12. However, the movement on the general fund balance is an important aspect of the board's stewardship as the main budget reference point, the main differences being:
  - capital investment is accounted for as it is financed, rather than when fixed assets are consumed;
  - retirement benefits are charged as amounts become payable to pension funds and pensioners, rather than as future benefits are earned.
13. After adjusting for these items, the board achieved a general fund surplus of £0.439 million. During the year there was a transfer from earmarked to unallocated balances of £0.784 million. This, together with the general fund surplus for 2006/07 results in an increase of £1.223 million and represents an improvement of £0.116 million on the approved budget of £1.107 million. This arose from savings in a range of costs including reductions in overtime, retained fire activity and a lower than expected pay award.
14. The Police and Fire (Scotland) (Finance) Act 2001 limits the carry forward of unspent requisitions for the year to 3%, cumulative reserves are limited to 5%. Excluded from this carry forward limit are earmarked amounts held in respect of future commutation liabilities. At 31 March 2007, the service held a reserve of £4.722 million, of which £1.691 million has been earmarked for future pension commutations. While a further amount of £2.570 million has been earmarked for future capital expenditure this needs to be included with unallocated balances in determining whether the prescribed limits for the general fund have been exceeded. At 31 March 2007, unallocated balances totalled £3.031 million which is within the permitted limit.
15. Capital expenditure totalled £4.183 million and was funded through government grants of £2.906 million, revenue contribution of £1.197 and capital receipts of £0.080 million. This expenditure is in line with the service's capital plan for 2006/07.



## Accounting practice

16. The presentation of the 2006/07 financial statements has changed significantly from previous years to make them more consistent with the accounts of other public and private sector entities. They now include an income and expenditure account and a separate statement on the movement in general fund balance, replacing the revenue account. The latter statement reflects items that require to be taken into account when determining a board's budget requirement.
17. Overall, the board made a satisfactory attempt in preparing the accounts in accordance with the revised SORP. Several amendments were however agreed to improve the presentation of information contained within the accounts and provide the detail required by the SORP. For example:
  - including appropriate explanation for the reader of the accounts about the significant changes required by the 2006 SORP;
  - fuller disclosure on fixed assets, pension costs and the general fund.

## Equal pay

18. 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. Following cases pursued against English councils, the extent of exposure of Scottish councils and joint boards arising from individual pay claims began to emerge during 2005/06.
19. We have requested and received a specific representation from the Treasurer that actual and potential claims in relation to equal pay legislation have been reviewed and the amount of £0.308 million recognised as a provision is the best estimate of the expenditure likely to be required to settle the present obligation at the balance sheet date.

## Going concern

20. The board's balance sheet shows a net liability of £264.774 million. The negative balance reflects the pensions liabilities falling due in future years. Auditing standards require auditors to consider an organisation's ability to continue as a going concern when forming an opinion on financial statements. One of the indications that may give rise to going concern considerations is an excess of liabilities over assets.



21. The board's statement of accounting policies confirm that it has been considered appropriate to adopt a going concern basis for the preparation of the financial statements as the constituent councils have a legal obligation to fund the net expenses of the board. Future pension liabilities will therefore be met, as they fall due by contributions from constituent authorities and government grant in the normal way. We are satisfied that the process the board has undertaken to consider going concern is reasonable.

### **Pension liabilities**

22. 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. 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.
23. The board's estimated pension liabilities at 31 March 2007 were £289.964 million, reducing from £293.450 million in the previous year. This largely relates to the Firefighter Pension Scheme which is unfunded and therefore the pension liability will fall to be met by serving firefighters' contributions and by taxpayers in the future. In respect of non-uniformed and control staff, the actuary was required to make a three-year assessment of the contributions that should be paid by employing authorities from 1 April 2006 to maintain the solvency of the fund. In addition to employer's contributions of 14.1%, contributions of £109,000, £114,000 and £119,000 are required in the years 2006/07, 2007/08 and 2008/09 respectively.

### **Legality**

24. Each year we request written confirmation from the Treasurer that the board's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of the Chief Fire Officer and Senior Management Team, the financial transactions of the 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 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 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 board's internal financial control system, but that work is ongoing to embed the risk management process into the service's activities.

29. In accordance with good practice, the statement was reviewed by the board in September 2007 and is supported by a high level review of the adequacy and effectiveness of internal financial controls undertaken by Internal Audit. The statement complies with accounting requirements and is not inconsistent with the findings of our audit.

## Audit committee and internal audit

30. Effective scrutiny is central to good governance, with a significant role for board members to scrutinise performance and hold management to account. The board has an established Scrutiny Committee which receives reports from both internal and external audit. In addition, the Chief Internal Auditor provides an annual report, including a statement on the adequacy and effectiveness of the internal control system.

31. Recommendations made in previous years' audit reports are monitored by management and internal audit, with progress regularly reported to the Scrutiny Committee. A report submitted to the Scrutiny Committee in August highlighted that, overall, good progress had been made in implementing both internal and external audit recommendations.



32. Internal audit plays a key role in the board's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. An internal audit service is provided to the board by the City of Edinburgh Council's Chief Internal Auditor. From our review of the service, we found that the work is conducted in accordance with CIPFA's Code of Practice for Internal Audit in Local Government, that the audit plan was sufficient and that all work on which we planned to place reliance was completed and the relevant assurances obtained.
33. Arising from a review of the board's risk management activities, internal audit reported that the overall risk maturity assessment for the board was level 4 (of a 5 stage process) which is described as 'risk managed' i.e. the entity has firmly embedded risk management into its organisational culture and it is anticipated that it will continue to refine its risk management processes.

## Systems of internal control

34. The board's financial transactions are processed through the City of Edinburgh's financial systems. It is therefore 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.
35. Our review of these systems was conducted as part of the audit of City of Edinburgh Council, supplemented by specific audit work on the board's financial statements. Overall there are no material issues of concern in relation to the operation of the main financial systems.
36. We noted however that the board tracks movements in fixed assets through a series of spreadsheets. At 31 March 2007, we sought and received assurances from the Treasurer that these spreadsheets provided a complete record of fixed assets in the ownership of the board and that all were appropriately classified. We note that the service is still in the process of implementing its fixed asset module. Once in place, this will provide a more comprehensive asset register but will also assist in the development of asset management plans and provide better linkages with the capital plan.

### **Risk Area Action 1**



## Prevention and detection of fraud and irregularities

37. The board has arrangements in place to prevent and detect fraud, inappropriate conduct and corruption. These arrangements include standing orders and financial regulations, a whistle blowing policy, an anti-fraud and corruption policy and codes of conduct for elected members and staff. We are pleased to note that the board continues to have appropriate arrangements in place to minimise the risk of fraud and corruption.

## Looking ahead

38. In the coming years the board continues to face significant challenges which include:

- specific cost pressures arising from the requirement to absorb transitional funding and the need to fund increased pension costs. The service decided to separately account for transitional funding and efficiency savings so that it could determine whether savings will be sufficient to cover actual costs in 2007/08.
- implementation of the fixed asset module and development of a comprehensive asset register which will enable a robust asset management planning process to be developed that should be linked to capital expenditure strategies and plans thus ensuring best value in the use of the board's assets and that spending plans are affordable, prudent and sustainable.

39. These areas, and the controls put in place by management to address the issues, are likely to be subject to ongoing review during the 2007/08 audit



# Performance

## A performance audit of the Scottish fire and rescue authorities

40. The Fire (Scotland) Act 2005 established a statutory framework to enable Scottish fire and rescue authorities to modernise their services. The Act was accompanied by a statutory Fire and Rescue Framework for Scotland. With enabling legislation and a new statutory framework in place the Accounts Commission asked Audit Scotland to undertake a performance audit on the Scottish fire and rescue authorities during 2006 and to include a review of the overall outcomes of modernisation.
41. Consequently, the study was undertaken across Scotland over summer 2006 and focused on the extent to which fire and rescue authorities are achieving the objectives of modernisation and in particular whether the integrated risk management plans are effectively supporting the change in emphasis from intervention to prevention, and that the progress to modernisation is reflected in the culture of the organisation. Overall, the study covered the following areas:
  - strategic management ;
  - fire prevention and risk management;
  - financial management arrangements;
  - workforce management and development;
  - management of operational business;
  - communications.
42. Each joint fire and rescue service received a local report from Audit Scotland's Public Reporting Group and key messages were brought together for national reporting.
43. Lothian and Borders Fire and Rescue Service were considered to have a clear, long term vision for the future which reflected the aspirations in the Fire (Scotland) Act 2005 and the national framework. The service has a well established approach to service planning, supported by sound project and performance management arrangements.
44. Significant resources are invested in local partnership working but the service cannot yet assess the extent to which partnerships are contributing to its overall strategic objectives. Overall, however, good progress has been made since the 2004 Accounts Commission phase 2 verification audit. It has implemented the transition from rank to role, introduced the integrated personnel development system to wholetime and retained staff and agreed a range of flexible working options.



45. The service needed to focus on continuous improvement by implementing its service improvement plan, ensuring staff are fully engaged in the strategic direction of the service and taking a more strategic approach to working in partnership with other agencies. These issues form part of an agreed local action plan which will be followed up as part of the 2007/08 audit.

## **Performance indicators**

46. The service 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 indicators that require to be published and external auditors review the service's arrangements and return details of the indicators, including an opinion on their reliability, to enable compilation of national reports on performance. I am pleased to report that all indicators prescribed for 2006/07 were classified as reliable.



# Final Remarks

47. The members of the Lothian and Borders Fire and Rescue Board are invited to note this report. We would be pleased to provide any additional information that members may require.
  
48. The co-operation and assistance given to us by officers of the board and the City of Edinburgh Council is gratefully acknowledged.

**Audit Scotland**  
**October 2007**



# Appendix A: Action Plan

## Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1.	36	<p><b>Asset Register</b></p> <p>Fixed assets are tracked through a series of spreadsheets each year making it difficult to inspect a comprehensive list of assets.</p> <p><b><i>Risk: The asset register may not be complete leading to a loss of assets.</i></b></p>	<p>Comprehensive asset inventories are currently held by each Function within Lothian and Borders Fire and Rescue Service (LBFRS).</p> <p>LBFRS is implementing an Asset Management MIS (Miquest)</p> <p>Data loading to the system will be achieved in phases , starting with high value assets including Property and Appliances</p> <p>Remaining Assets will be added to the system in future phases.</p> <p>An Asset Management Strategy is being prepared.</p>	<p>Chief Fire Officer</p> <p>Chief Fire Officer</p> <p>Chief Fire Officer</p> <p>Chief Fire Officer</p> <p>Chief Fire Officer</p>	<p>March 2008</p> <p>March 2008</p> <p>March 2009</p> <p>December 2007</p>