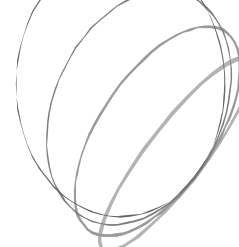


Tayside Contracts Joint Committee

**Report to Members and the Controller of Audit on the
2007/08 Audit**

Contents

Key Messages	1
Introduction	2
Financial statements & financial position	3
Auditor's report	3
Financial position	3
Issues arising	4
Legality	5
Statement on the system of internal financial control	6
Future outlook	6
Governance	8
Overview	8
Anti-fraud and corruption arrangements	8
Systems of internal control	9
Performance	10
Overview	10
Performance Management and Improvement	10
Future outlook	10



Key Messages

In 2007/08 we have audited the financial statements and looked at aspects of governance and performance within Tayside Contracts Joint Committee. This report sets out our main findings.

Overall, we found the financial stewardship of Tayside Contracts Joint Committee during the year to be satisfactory. The main conclusions and outcomes from the audit are highlighted below:

- An unqualified audit opinion has been issued on the financial statements for 2007/08;
- The Statement on the System of Internal Financial Control included in the accounts complies with accounting requirements and is not inconsistent with audit findings;
- Many aspects of a sound corporate governance framework are in place;
- A 5-year Business Plan for the period 2006 to 2011 had been developed in conjunction with members and constituent councils that identifies future opportunities and risks;
- An anti-fraud and corruption strategy is in place;
- There are weaknesses in the internal control environment as this function is not independent of management and no risk based audit methodology is used;
- The Committee is behind schedule in implementing a number of previous audit findings although revised implementation dates have now been agreed.

The annual report on the work carried out by the Internal Control & Audit function concluded that “The work carried out during the year continues to give confidence that the necessary controls are in place and where weaknesses have been identified appropriate remedial action is taken so that the Joint Committee have confidence in the underlying systems of financial control and the financial service provided”.

Ongoing key issues for the Joint Committee in the future include specific cost pressures which may arise from inflation and the need to fund increased pension costs, implementation of the Single Status Job Evaluation exercise and staff turnover.

**Audit Scotland
October 2008**

Introduction

1. The members and officers of the Joint Committee 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 Committee'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 Committee has adequate corporate 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 mis-statement, error, fraud or corruption;
 - the Joint Committee has proper arrangements for securing best value in its use of resources.

2. This report summarises the most significant issues arising from our work during 2007/08.

Financial statements & financial position

3. In this section we summarise key outcomes from our audit of the Joint Committee's financial statements for 2007/08, aspects of the Joint Committee's reported financial position and performance to 31 March 2008, and provide an outlook on future financial prospects and financial reporting issues.

Auditor's report

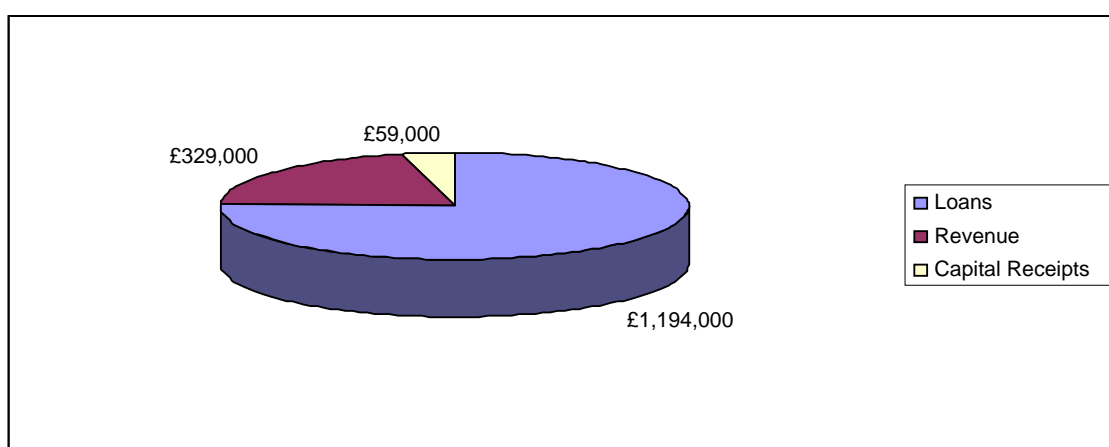
4. We have given an unqualified opinion on the financial statements of Tayside Contracts Joint Committee for 2007/08, concluding the financial statements:
 - present fairly, in accordance with relevant legal and regulatory requirements and the 2007 SORP, the financial position of the Joint Committee as at 31 March 2008 and its income and expenditure for the year then ended; and
 - have been properly prepared in accordance with the Local Government (Scotland) Act 1973.
5. The Joint Committee's balance sheet has an excess of liabilities over assets of £5.3 million due to the accrual of pension liabilities in accordance with accounting standards. 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.
6. The Joint Committee has considered it appropriate to adopt a going concern basis for the preparation of the financial statements as future actuarial valuations of the pension fund will consider the appropriate employer's contribution rate to meet the fund's commitments. The constituent authorities of the Joint Committee are also liable to fund the Joint Committee's liabilities as they fall due. We are satisfied that the process the Joint Committee has undertaken to consider going concern is reasonable.

Financial position

7. The Joint Committee's Income & Expenditure account shows a net surplus of £480,000 for the year. The net surplus figure measures the Board's financial results in the year under Generally Accepted Accounting Principles. The movement on the general reserve balance is also an important figure when considering the Board's financial stewardship. Adjustments are made to the net surplus figure to take account of expenditure that statute and non-statutory proper practice require to be charged to the general reserve. Following these adjustments, the surplus for the year increased to £659,000, £500,000 of which is to be distributed to the constituent


councils in accordance with the profit sharing percentages approved by the Joint Committee on 8 May 2006, and the general reserve balance carried forward at the year end was £299,000.

8. 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, which are required to break even over a three year rolling period. In the three years to 31 March 2008 the Construction Division Statutory Trading Account achieved an aggregate surplus of £534,000 and the Facilities Services Statutory Trading Account made an aggregate surplus of £885,000. Both Statutory Trading Accounts, therefore, met the statutory target.
9. Capital expenditure in the year totalled £1.582 million. The majority of this expenditure related to the addition of items of plant and vehicles for the Construction Division, including spreaders, tipping trucks, winter fleet and a crusher for the quarry. Capital was funded by:



Issues arising

10. The Joint Committee'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 significantly improved on prior years and this enabled the audit to progress smoothly.
11. 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 2007 SORP required a number of significant changes to be made to the 2007/08 financial statements to make them more consistent with the accounts of other public and private sector entities. The major changes include:
 - accounting for financial instruments based on FRS25, FRS 26 and FRS 29
 - replacement of the fixed asset restatement account and capital financing account by a revaluation reserve and capital adjustment account
12. Overall, we were satisfied that the Joint Committee had prepared the accounts in accordance with the revised SORP.

- 
13. Presentational adjustments were made to the unaudited accounts issued on 16 June 2008. These adjustments were in respect of past service costs and credits and the allocation of overheads to trading accounts. Past service costs and credits were previously included in service expenditure but are now correctly disclosed within Non Distributed Costs (NDC) on the face of the Income & Expenditure Account. In addition, adjustments were made to the trading accounts to include overheads previously omitted as they were included in NDC and Corporate and Democratic Core (CDC). Tayside Contracts receives no grant funding and has to meet 100% of its overheads from trading undertaken by its two trading operations. On that basis, it is reasonable that all overheads, including CDC and NDC, be taken into account in determining whether the breakeven target has been met. The effect of this change was to reduce the 2007/08 break-even position of the Construction division by £179,000 and Facilities Services by £43,000. The negative impact on the three year rolling breakeven target was £446,000 and £107,000 respectively. These adjustments had no impact on the overall surplus.
 14. Audited accounts were finalised prior to the target date of 30 September 2007 and are now available for presentation to the Joint Committee and for publication. The financial statements are an essential means by which the Joint Committee accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources.
 15. Further matters arising from the audit of the financial statements which requires to be brought to the attention of members are summarised below.

Legality

16. Each year we request written confirmation from the Proper Officer that the Joint Committee's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Proper Officer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of members and officials of Tayside Contracts Joint Committee, the financial transactions of the Joint Committee were in accordance with the relevant legislation and regulations governing its activities.
17. 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. The Joint Committee has recognised a liability in the financial statements in relation to the potential contravention of this Act. Until the single status agreement (see paragraph 22 below) is implemented, however, there remains the possibility that the Joint Committee could be judged to have contravened the 1970 Act.
18. There are no additional legality issues arising from our audit which require to be brought to members' attention.

Statement on the system of internal financial control

19. The 2007/08 financial statements include a Statement on the System of Internal Financial Control which highlights the Proper Officer's view that reasonable assurance can be placed upon the adequacy and effectiveness of the Joint Committee's internal financial control system.
20. The Statement is supported by a high level review of the adequacy and effectiveness of internal financial controls undertaken by Chief Officers.
21. The statement complies with accounting requirements and is not inconsistent with the findings of our audit.


Future outlook

Single Status

22. In 1999 a single status agreement was reached between Scottish local authorities and trades 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.
23. 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. Tayside Contracts has yet to implement the agreement. At 31 March 2008, the Joint Committee had not set aside any funds for the cost of single status. On-going costs associated with single status are largely confined to Facilities Services and will be separately recovered from constituent councils through billing mechanisms. Those associated with the Construction Division will be absorbed and recovered through the job costing and billing systems.
24. In securing a local agreement the Joint Committee needs to ensure it maximises the opportunity for service and job redesign to ensure that it achieves value for money from its investment in its staff.

Pension liabilities

25. 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. 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 being recognised on the face of annual accounts.

- 
26. The Joint Committee participates in the Local Government Superannuation Scheme (Tayside Superannuation Fund), a defined benefits scheme administered by Dundee City Council. Note 33 to the Core Financial Statements highlights that the Joint Committee's scheme net liabilities at 31 March 2008 are £7.245 million, a decrease of £3.2 million from the previous year largely as a result of changes in the interest rate.
 27. In 2006/07 we reported that changes to the pension regulations to the pension regulations allowing individuals to elect to receive a larger lump sum payment in return for a reduced annual pension had resulted in a reduction in the pension liability of £1.35 million. This was based on the assumption that 50% of retirees would opt to take the larger lump sum in return for a reduced annual pension and Dundee City Council, the administering authority for the pension fund, had agreed to have this assumption monitored over time against the actual take up of the higher lump sum. We noted that no monitoring had taken place in the year following the changes to the regulations. We have been advised that Committee officials consider that this assumption is a long term one and should be monitored at each triennial valuation rather than annually.
 28. The full actuarial valuation of the Tayside Superannuation 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 97% as at March 2002 to 91% as at March 2005. The actuary is required to make a 3-year assessment of the contributions that should be paid by the employing authorities as from April 2006 to maintain the solvency of the fund. The contribution levels are based on percentages of employee contributions normally 5% - 6% of salary. The current 3-year assessment shows that budgeted contributions are expected to rise from 275% of employee contributions to 315% by 2008/09.
 29. The next full actuarial valuation will assess the position at 31 March 2008. This will determine contribution rates for 2009-10 and the next two financial years. Recent changes to the Local Government Pension Scheme regulations are expected to release some future financial benefits, while providing additional flexibility to future pensioners.

Governance

30. In this section we comment on key aspects of the Joint Committee's governance arrangements during 2007/08.

Overview

31. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. In previous years we have concluded that the Joint Committee has many aspects of a sound corporate governance framework in place and have reached the same conclusion this year.

Internal Control Function

32. Internal audit should play a key role in the Joint Committee's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system.
33. In our 2006/07 report to members we highlighted concerns about the environment in which the internal control officer operates, for example:
- there is no central risk register in place and no risk-based audit methodology used
 - the internal control officer works alone and it is unclear to what extent his work is planned, supervised and reviewed
 - the internal control officer is not independent of management.
34. During 2007/08 we were advised that discussions had taken place with an independent firm of accountants with a view to conducting an Audit Needs Assessment but that this had stalled due to a lack of response from the accounting firm. Further discussions are planned during 2008/09. In the meantime, the internal control officer has developed an audit plan for 2008/09.

Anti-fraud and corruption arrangements

35. The Joint Committee has appropriate arrangements in place to prevent and detect fraud and corruption. These arrangements include the Councillors' Code of Conduct, Anti -Fraud and Corruption Strategy, which was approved by the Joint Committee in May 2006, along with supporting policies and guidelines and a whistle-blowing policy.

Systems of internal control

36. The Managing Director presented an annual report on the work carried out by the Internal Control & Audit function to the Joint Committee in June 2008 which concluded that "The work carried out during the year continues to give confidence that the necessary controls are in place and where weaknesses have been identified appropriate remedial action is taken so that the Joint Committee have confidence in the underlying systems of financial control and the financial service provided".
37. As part of our 2007/08 audit, we reviewed controls over key financial systems and corporate governance arrangements. We also assessed actions taken by officers to address our prior year recommendations. Together, these strands of work inform our assessment of the effectiveness of risk management within Tayside Contracts. In general, we found that risk was being managed effectively in the areas we reviewed. A number of areas for improvement to internal controls were agreed with management including:
- identifying the underlying causes for the overdraft position and considering and implementing solutions to address these;
 - developing a procurement strategy,
 - developing a new suite of payroll reports following implementation of single status,
 - more explicit reporting of affordability and sustainability measures underpinning the capital budget.
38. Eleven audit points were agreed with management during 2006/07 and during 2007/08 we noted that five of these had been implemented. Although overall, progress is being made on all of the audit points the implementation dates had not been met in most cases. Revised dates were agreed with management in the following areas and we will continue to monitor progress towards full implementation of these during 2008/09:
- Financial regulations to be updated to include a formal "de-minimus" level for capital expenditure,
 - Updating the risk assessment/Audit Needs Analysis (see paragraph 34 above),
 - Recruitment of a Financial Systems Administrator,
 - Implementing an Integra Job Costing archiving system,
 - Developing the Integra Job Costing system to enable direct input of WIP each month,
 - Improve reporting and review of profitability by activity type.

Performance

39. In this section we comment on key aspects of the Joint Committee's reported performance during 2007/08 and provide an outlook on future performance.

Overview

40. The delivery of high quality and cost effective public services is a cornerstone of current government policy. Performance management and improvement involves raising the standards and quality of performance, achieving greater efficiency in the use of public funds and becoming more responsive to the needs and aspirations of both individual service users and the communities served. Performance management systems will need to be robust to handle changing requirements.

Performance Management and Improvement

41. The 2006/11 Business Plan acknowledges the need to improve efficiency and productivity and to make best use of assets and people in order to minimise the impact of cost pressures in the next five years. The Joint Committee's progress in meeting the objectives of the Business Plan is subject to on-going review.
42. An income gap had been identified in the Business Plan and, to date, Tayside Contracts has been successful in bridging the annual income gap by generating sufficient additional income, making efficiency improvements and cost savings.
43. During 2007/08 we reported to members that, partly as a result of improved forward planning and information sharing with the three constituent councils, we had been advised that for 2008/09, sufficient work has been identified to cover the income gap. Whilst we welcomed this positive development, we noted that this outcome does not include any provision for potential costs which may arise from ongoing equal pay claims. As the timings and costs of these potential costs are uncertain, action may still be required to ensure additional income is generated to fund any successful claims. In addition, further income may need to be generated to fund any single status costs not directly funded by constituent authorities.

Future outlook

44. The Joint Committee continues to face operational pressures and this is more pressing within the construction division. Looking forward, this division will need to ensure it secures sufficient work to enable all of its costs to be recovered.