Falkirk Council

Annual Audit Report to Members and the Controller of Audit - year ended 31 March 2018

28 September 2018

Building a better working world

Contents

About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Falkirk Council (the Council) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

This report is for the benefit of the Council and is made available to the Accounts Commission, the Controller of Audit and Audit Scotland (together the Recipients). This report has not been designed to be of benefit to anyone except the Recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

Complaints

If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Diane McGiffen, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

1. Executive Summary

Purpose of this report

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as the external auditor of Falkirk Council (the Council) for the five year period 2016/17 to 2020/21.

We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Report is designed to summarise our key findings and conclusions from our audit work. It is addressed to both members of the Council and the Controller of Audit, and presented to both Council management and those charged with governance. After consideration by the Council, this report is provided to Audit Scotland and published on their website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the Council. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, our observations around where the Council employs best practice and where practices can be improved. We use these insights to form our audit recommendations to support the Council in improving its practices around financial management and control, as well as around key aspects of the wider scope dimensions of audit. These are highlighted throughout the report together with our judgements and conclusions regarding arrangements.

Scope and responsibilities

The Code sets out the responsibilities of both the Council and the auditor. We provided details of these in our Annual Audit Plan, which was presented to the Audit Committee on 9 April 2018. We summarise these responsibilities of the Council in Appendix A.

Our Annual Audit Plan set out an overview of our audit scope and approach for the audit of the 2017/18 financial statements. We carried out our audit in accordance with the plan. We applied the following level of materiality to our audit.

Materiality for our audit – no change to that reported in our Annual Audit Plan	£12.0 million
Tolerable Error is our materiality applied at an individual account balance – no change	£9.0 million
Reporting threshold, set in line with the requirements of the Code – no change	£0.25 million

Financial statement audit

We are responsible for conducting an audit of the financial statements of the Council. We provide an opinion on the financial statements as to:

- whether they give a true and fair view of the financial position of the Council and its group as at 31 March 2018 and its expenditure and income for the year then ended; and
- whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2017/18 Code of Practice on Local Authority Accounting in the United Kingdom.

We also review and report on the consistency of the other information prepared and published by the Council along with its financial statements.

Key contacts

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Independence

We confirm that we have undertaken client and engagement continuance procedures, included in which is our assessment of our continuing assessment of our independence to act as your external auditor.

Wider scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider-scope public audit. Our audit work over the wider scope audit dimensions compliments our financial statements audit.

Financial statements audit – key messages

We have issued unqualified audit opinions on the Council and group financial statements as well as in respect of the Falkirk Temperance Trust.

We have concluded satisfactorily in respect of each of the significant risks and audit focus areas identified in our Annual Audit Plan.

The Annual Accounts, Statement of Responsibilities, Annual Governance Statement and Remuneration Report were received at the start of the audit fieldwork. The Annual Accounts were generally of good quality, as were supporting working papers. We made a number of recommendations around areas for improvement around the presentation and disclosures within the financial statements, many of which were consistent with feedback we provided in 2016/17.

Management made the required amendments in response to audit comments to ensure the narrative (the Management Commentary and Annual Governance Statement) and presentational aspects of reporting met the requirements of the Code. We have outlined in the report where we believe there is scope for further improvement to the commentary to support users of the financial statements in understanding the Council's position and journey through the year.

We identified three audit adjustments to the financial statements during our audit work. These had a positive net impact of £0.9 million on the Council's General Fund position at the year end. We identified one audit difference which was unadjusted, which had no impact on the Council's General Fund position. We have outlined the audit differences identified at Appendix E to the report.

Progress against recommendations in the BVAR – key messages

In February 2018 the Accounts Commission published its follow up report on the Council's progress against its previous BVAR from 2016. In its findings the Accounts Commission reported positively on the progress made by the Council and the plans for further implementation of improvements, in particular around Council of the Future. It did however note the importance of transitioning from planning to implementation, and a need for an increase in the pace of change in improvements, to ensure the required savings and improvements are delivered.

As part of the 2017/18 audit we considered both the Council's approach to tracking progress against the recommendations and the progress around the required actions. We have outlined our specific findings in our wider scope work below and throughout the report, in particular in our reporting around financial sustainability and value for money.

Wider scope audit - key messages

We set out below our key messages in respect of each of the dimensions of public sector audit, along with our overall assessment in terms of red / amber / green. Our assessments reflect our overall judgements of the Council's arrangements and the degree of risk potentially facing the Council, based on the audit work completed during the year.

Financial management	► Overall, the Council has demonstrated good financial monitoring of the in-year revenue budget. There is scope for improvement in the monitoring and reporting of the capital budget. ► The importance of good financial control is clearly understood across the Council. In our view the Council currently has sufficient financial skills, capacity and capability, however this is an important area that needs to be kept under review.	Green
Financial sustainability	► The Council continues to experience financial pressures. Significant progress is required to deliver 2018/19 outturn in line with budget and to support approval of a robust 2019/20 budget. ► The Medium Term Financial Plan is being developed in conjunction with the objectives of the Council's Corporate Plan and is linked to the developments in the Council of the Future change programme. ► There are extensive funding gaps over the period to 2023/24, with the level of savings required over the next five years significantly greater than the identified savings. Difficult decisions will have to be taken to achieve financial balance. There is a need for an improvement in the pace of transformation to support the delivery of a robust Medium Term Financial Plan.	Red
Governance & transparency	► The Council has an established governance structure through Council and standing committees. The governance framework comprises Standing Orders, Scheme of Delegation and Financial Regulations. ► Progress in responding to recommendations to enhance governance arrangements has been mixed. There is scope to ensure the Audit Committee is better sighted on the status of implementation of recommendations in respect of audit and other scrutiny activity.	Green
Value for money	► From a delivery perspective, individual Council of the Future projects have progressed, and plans are in place to continue the delivery of existing projects, with the approval of new projects ongoing. ► In our view the overall status of the programme is one of being still in the earlier phases of implementation. Significant improvement is required over the pace of the programme and in moving from planning to implementation and delivery. ► There has been progress in enhancing the governance and management arrangements over the Council of the Future transformation programme. Further enhancements could be made to facilitate more effective transparency and scrutiny; enabling more timely identification and action on delivery risks.	Red

2. 2017/18 financial statements audit

2. Summary of 2017/18 audit opinion

The detailed form and content of our audit report, and the requirements underpinning the report, are set out in guidance issued by Audit Scotland. This covers our reporting requirements in accordance with International Standards on Auditing (UK), plus those matters prescribed by the Accounts Commission.

Element of Audit opinion	Nature of opinion and basis for that
Opinion on financial statements	**Unqualified opinion**
▸ Truth and fairness of the state of affairs of the Council and its group at 31 March 2018 and of the income and expenditure for the year then ended ▸ Preparation of the financial statements in accordance with the relevant financial reporting framework	▸ Performance of audit procedures to respond to our assessed risk of misstatement, including significant risks ▸ Accounting policies are appropriate and estimates are reasonable ▸ Completion of financial statement disclosure checklists / consideration of relevant guidance issued by CIPFA / Audit Scotland
Conclusions relating to the going concern basis of accounting	**No matters to report**
▸ The use of the going concern basis of accounting used in the preparation of the financial statements is not appropriate	▸ Supported by our core financial statements audit work, supplemented by our wider scope audit procedures in respect of financial sustainability
Other information in the annual accounts	***Appendix D – recommendation one***
▸ We are required to consider whether the other information in the annual accounts is materially inconsistent with the financial statements or our knowledge obtained in the audit.	▸ The Management Commentary and Annual Governance Statement met the core requirements as set out by the Code. There are a number of improvements that can be made to provide a more comprehensive view of the Council's developments and arrangements. ▸ Review of committee minutes and papers / discussions with management / understanding of the business / participation in shared risk assessment / review of the unaudited financial statements.
Opinions on matters prescribed by the Accounts Commission	**Unqualified opinions**
▸ The audited part of the Remuneration Report has been properly prepared in accordance with applicable regulations ▸ Information in the Management Commentary / Annual Governance Statement is consistent with the financial statements, and prepared in accordance with the relevant guidance	▸ We agreed the form of the report to the regulations and agreed the disclosures to underlying accounting records and supporting schedules ▸ We reviewed the content of the narrative statements to the information known to us in the audit, and against the requirements of the guidance
Matters on which we are required to report by exception	**No matters to report**
▸ Whether there has been a failure to achieve a prescribed financial objective ▸ Whether adequate accounting records have been kept ▸ Whether financial statements and the audited part of the Remuneration Report are not in agreement with the accounting records ▸ Whether we have not received the information we require for our audit	▸ We have not identified any failures to achieve a prescribed financial objective ▸ In respect of the other areas, we obtained the Council's accounting records by data download and agreed the financial statements and the audited part of the Remuneration Report to these. ▸ We were provided with all the information we required

2. 2017/18 financial statements audit

The Council's Annual Accounts enables the Council to demonstrate its accountability for the resources at its disposal, and its overall performance in the application of those resources during the year.

Financial Statements Preparation 2017/18

Compliance with requirements

The Local Authority Accounts (Scotland) Regulations 2014 (the Regulations) set out the statutory requirements on the Council in respect to the annual accounts, their availability for public inspection and the consideration and signing by the Council or a committee with an audit or governance remit.

The Council has complied with the relevant requirements.

In particular, the unaudited annual accounts were considered by the audit committee on 18 June, prior to their submission to us and well in advance of the deadline of 31 August. This demonstrates good practice.

Management ownership of recommendations for improvement

We made five recommendations in our 2016/17 Annual Audit Report in respect of financial statement preparation and the underlying financial processes and controls. These covered areas for improvement in the preparation of the core financial statements and Management Commentary, and arrangements to account for subsidiaries, fixed asset valuations and provisions at the yearend.

We have reported on the progress of individual recommendations throughout this report in the appropriate areas. A number of actions have been taken by management, however a number of the recommendations remain relevant as evidenced by consistent findings and audit adjustments identified during the 2017/18 audit.

Recommendations one, three, four

Audit logistics

We held a debrief with the finance team to learn lessons from the first year audit and to support efficiencies in the second year of audit. We advanced key elements of audit testing to earlier in the year, in particular around payroll costs throughout the year, to reduce the burden of the audit on the finance and audit team over the summer period.

Overall, in our view, the annual financial statements are prepared in a timely manner and there has been good cooperation provided across the finance team to support our audit work. We will complete a year two audit debrief with management shortly to identify further improvements to the management preparation and audit processes for the next audit cycle.

Other matters

We have not identified any circumstances to notify the Controller of Audit that a statutory report may be required under the Local Government (Scotland) Act 1973.

We did not receive any objections to the 2017/18 Annual Accounts from members of the public.

Audit differences

There was one unadjusted audit difference arising from our audit, a projected misstatement in relation to the valuation of the Council's share of the Falkirk Council Pension Fund's year end assets. This difference would have no impact on the Council's General Fund position at yearend. The difference, along with the adjusted differences, are outlined at Appendix E.

We discussed the Council's presentation of internal recharges and their interpretation of recent advisory guidance issued by LASAAC. As a result, management revised the presentation of items in the Comprehensive Income and Expenditure Account. There was no impact on the reported deficit on provision of services as a result of the adjustment.

2. Significant audit risks

Significant risk - risk of fraud in income and expenditure recognition: ISA (UK) 240 requires us to make a rebuttable presumption that the fraud risk from income recognition is a significant risk. In the public sector, we extend that to consider the risk of material misstatements by manipulation of expenditure.

Our overall approach

We rebutted the risk of improper recognition of income in respect of core grant funding from the Scottish Government, as well as in respect of council tax and non-domestic rate income. This was because we considered that there is no judgement in respect of the recognition of these income streams.

We undertook walkthroughs in respect of the processes management has established to account for key income and expenditure streams. We obtained data downloads of the Council's financial ledger in order that we could trace the key transactions through initiation to recording in the financial statements.

Key components of the Council's income	Significant risk	2017/18 (£m)
Council tax income	×	60.8
Non domestic rates distribution	×	66.8
Non ring-fenced government grants	×	205.4
Capital grants and contributions	✓	25.8
Service and other income	✓	319.6
Interest and investment income	×	22.2
Total income		**700.6**

Key components of the Council's expenditure	Significant risk	2017/18 (£m)
Employee Expenses	×	238.0
Other services expenditure	✓	366.4
Depreciation, amortisation & impairment	×	43.8
Interest payments and pensions	×	57.8
Gain on disposal of assets	×	-
Total Expenditure		**706.0**

What did we do in response to the significant risk over income and expenditure streams?

- Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias.
- Reviewed transaction listings for individually material transactions as well as unusual items (debits to income, credits to expenditure etc.) to agree to supporting documentation and third party evidence.
- Tested a representative sample of transactions across the remaining untested income and expenditure population to ensure coverage of testing across all balances.
- Reviewed and tested revenue cut-off around the year end through reviewing manual journals posted to revenue and reviewing material credit notes raised after year end.
- Performed a search for material receipts received after year end and ensured these had been accounted for in the correct period.

All audit procedures to address significant risks to the financial statements are performed at a lower materiality level than for other accounts.

Other audit procedures – non-significant risk areas:

Council tax / Non-domestic rates income: We established detailed expectations of income and expenditure and checked the reconciliation to the relevant feeder system.

Non ring-fenced grant income: Substantively tested these balances to grant confirmation letters.

Employee expenses: Bespoke data analysers provided an understanding of all payroll transactions in the year, which were reconciled to payroll system.

Depreciation, amortisation & impairment: We undertook testing of these balances in conjunction with our work on property, plant and equipment.

Interest income / payments: We agreed balances to bank and other loan confirmations.

What are our conclusions

- Our testing has not identified any material misstatements relating to revenue and expenditure recognition. We did not identify any areas of significant estimation or judgement as part of our audit work in these areas.

2. Significant audit risks (cont.)

EY

Significant risk – misstatement due to fraud or error: As identified in ISA 240, management is in a unique position to perpetrate fraud in its financial reporting because of its ability to manipulate accounting records directly or indirectly by overriding controls that otherwise appear to be operating effectively.

We respond to this risk on every engagement	
Audit procedures performed	**What did we find?**
We gave consideration to the risk of fraud, inquiring of management about their assessment of the risks of fraud and the controls put in place to address those risks. We also updated and developed our understanding of the oversight of those charged with governance over management's processes over fraud.	We have not identified any material weaknesses in controls or evidence of material management override.
Test the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements	We obtained a full list of journals posted to the general ledger during the year, and used our bespoke data analysers to identify any unusual journal types or amounts based on our identified risk areas for the audit. We then tested a sample of these journals, understood their purpose and agreed and corroborated them to supporting documentation.
Review accounting estimates for evidence of management bias, including management's retrospective consideration of prior year estimates.	We identified and considered the appropriateness of key accounting estimates, including provisions, and their susceptibility to bias. Management has disclosed their consideration of the critical accounting judgements and key estimates in the financial statements. We have reviewed these and materially agree with the detail of the assessment performed.
Evaluate the business rationale for any significant unusual transactions	We did not identify any significant unusual transactions outside the normal course of business.
Review capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised.	We reviewed expenditure on property, plant and equipment to ensure that expenditure items were not being inappropriately capitalised to defer costs to future years. Likewise we performed analytical procedures and transaction testing of Housing Revenue Account expenditure to ensure funds were not being utilised to meet General Fund expenditure. No issues were noted through testing performed.

What are our conclusions

- We are have not identified any material weaknesses in the design and implementation of controls around journal processing. We did not identify any instances of evidence of management override of controls.

We respond to this risk on every engagement	
Audit procedures performed	**What did we find?**
Consistency and application of accounting policies / overall presentation of financial information	We consider the accounting policies adopted by the Council to be appropriate. There are no significant accounting practices which materially depart from what is acceptable under IFRS or the Code. Following discussion with management on their interpretation of the LASAAC advisory guidance in respect of internal recharges, management revised the presentation in the Comprehensive Income and Expenditure Statement. The presentation is now compliant with the 2018/19 Code. Appropriate segmental reporting information has also been reported. There was no impact on the surplus / deficit position as a result of the revised presentation. We considered the presentation of the Expenditure and Funding Analysis in the financial statements and considered it met the core requirements of the Code but could be adjusted in future years to meet the most up to date best practice guidance from Audit Scotland. ***Recommendation two***

Revenue recognition – looking ahead

IFRS 15 – Revenue From Contracts With Customers

The applicable accounting framework is CIPFA's annual Code of Practice on Local Authority Accounting in the United Kingdom (which is IFRS based as adapted for Local Authorities). The 2018/19 Code will apply to accounting periods starting on or after 1 April 2018.

The 2018/19 Code will determine how IFRS 15 *Revenue from Customers with Contracts* will be adopted by local government bodies. It is our view, that IFRS 15 will not have a material impact on this Council's financial statements. The vast majority of the Council's income streams are taxation or grant based. The following income streams are within the scope of IFRS 15, but are not expected to result in major adjustments to the accounting treatment:

- fees and charges for services under statutory requirements;
- sale of goods provided by the authority; and
- charges for services provided by a local authority.

We look forward to working with management to ensure any relevant changes in requirements are considered and dealt with effectively.

2. Other inherent audit risk areas

Higher inherent risk – valuation of property, plant and equipment: The fair value of PPE represent significant balances in the Council's financial statements and are subject to valuation changes, impairment reviews and depreciation charges.

What judgements are we focused on?

The Council's property, plant and equipment portfolio is significant, totalling £1 billion of assets at the year end. In terms of the focus of our work, the main judgements are in respect of:

- Council dwellings – due to the materiality of the balance and the judgements in the methodology for social housing valuation.
- Other land and buildings – this is the most material grouping of assets, covering most of the Council's operational assets. Asset categories included here with a 2016/17 valuation of £56 million were re-valued in 2017/18.
- Infrastructure assets, assets under construction and vehicles, plant, furniture and equipment categories of assets are valued at historical cost. As such, we consider these as having a lower inherent risk as there is no material valuation judgement required.

Category of Property, Plant & Equipment	2017/18 (£m)	2016/17 (£m)
Council Dwellings	349.6	342.1
Other Land and Buildings	514.4	495.7
Vehicles, Plant, Furniture and Equipment	12.7	11.6
Infrastructure Assets	113.4	108.2
Community Assets	14.0	13.7
Assets under construction	9.7	18.7
Surplus assets, not yet held for disposal	2.3	2.3
Total Property, Plant & Equipment	**1,016.1**	**992.4**
Heritage assets	0.2	0.2

Source: Falkirk Council Audited Accounts 2017/18

What did we do?

- Consider the action taken by management to address the prior year recommendation.
- Review of the annual cycle of valuations to ensure that assets have been valued in accordance with the requirements of the Code, and whether any specific changes to asset use have been communicated.
- Consider the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work.
- Sample test key asset information used by the valuers in performing their valuation (e.g. floor plans to support valuations based on price per square metre).
- Review assets not subject to valuation in 2017/18 to confirm that the remaining asset base is not materially misstated.
- Consider changes to useful economic lives as a result of the most recent valuation.
- Test accounting entries have been correctly processed in the financial statements.

What did we find

We did not identify any material misstatements in relation to the valuation of land and buildings.

We also considered a selection of other property valuations and noted that there were no material changes in value from 2016/17. The audit team has considered the assumptions used in these valuations and are content that these valuations are materially accurate.

Through our discussions with management and review of the valuations impacting the 2017/18 financial statements, we identified that the valuation reports provided by the Council's appointed valuer are as at 1 April (beginning of the financial year). A valuation date of 31 March would be more appropriate to ensure the valuations of assets are as current as they can be for the balance sheet date.

In response management has taken steps to ensure all future valuations for fixed assets include a roll-forward exercise to the balance sheet date to ensure any material variations from 1 April are identified and accounted for in the correct financial year.

What are our conclusions

- We have not identified any material weaknesses in the valuation process or judgements used by the valuer.

Higher inherent risk – accounting for retirement benefits: extensive disclosures are required in respect of the Council's participation in the Local Government Pension Scheme (LGPS). Management involves specialists in the preparation of this material accounting estimate.

Accounting for retirement benefits

In line with accounting standards, the Council recognises the cost of retirement benefits provided to its staff in the reported cost of service when they are earned by the employee and not when the pension benefits are actually paid.

The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the Council. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

What did we do?

- We obtained responses to our enquiries of the auditor of the Falkirk Council Pension Fund, thus obtaining appropriate assurance over the information supplied to the actuary in relation to the Council's participation in the Fund.
- We have assessed the work of the Pension Fund actuary (Hymans) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by Public Sector Auditor Appointments for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team.
- We have reviewed and tested the accounting entries and disclosures made within the Council's financial statements in relation to IAS19.

What did we find

We concluded that we were able to rely on the work of management's specialists – the pension fund actuaries – and were satisfied that actuarial assumptions used in the preparation of the IAS 19 report were within an acceptable range based on our own actuaries' review of key assumptions.

The timing of production of actuarial reports means that actuaries produce their IAS 19 reports using estimated data for the final part of the year. As estimates require to reflect the latest available, reliable information, we identified a potential material adjustment due to estimated returns on investment assets; impacting employer assets. We requested management obtain an update from the actuaries.

A revised IAS 19 report was produced by the actuaries based on actual outturn to 31 March 2018. This showed a £3.6 million increase in actuarial gains, compared to that previously reported. The impact of this was to decrease the pension liability from £264 million to £260.6 million as at 31 March 2018.

We obtained relevant assurances from the pension fund auditor to support our conclusions. The fund auditor noted one audit difference following the completion of their audit procedures, being an understatement of fund assets by £8.5 million. The Council's share of this understatement would extrapolate to approximately £3.2 million.

These two matters resulted in an overall projected difference in the valuation of the Council's pension assets of £6.8 million. Management has chosen not to adjust the financial statements.

Recognising there is a risk of these differences re-occurring next year, given timing differences will always exist, we have agreed to discuss with management and the actuaries arrangements in advance of the financial yearend to seek to address this before the IAS 19 reports are drafted.

Recommendation three

What are our conclusions

- We identified one unadjusted audit difference of £6.8 million in relation to the asset valuation driving the Council's net pension liability. This was made up of differences due to the timing of the IAS 19 report received by the actuaries which resulted in a reduction of the pension liability by £3.6 million, and a difference identified by the Pension Fund auditor resulting in a difference of £3.2 million.

2. Other audit areas

With local authorities in general developing new and different ways of working in partnership with other entities in delivering services, the accounting code of practice requires the Council to prepare group financial statements setting out its interests in other entities and the impact these have on the Council.

Group financial statements

The Council has identified and accounted for the following interests in other entities within its group financial statements.

Falkirk Community Stadium Ltd - subsidiary

We reported in 2016/17 around the management arrangements at FCSL. These have been followed up in our governance and transparency reporting in this report.

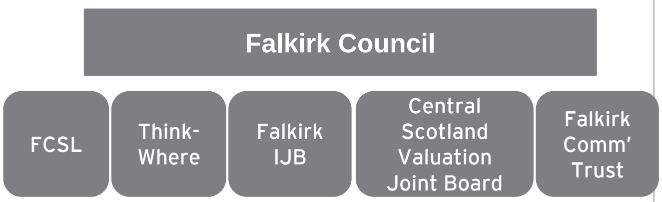
The Council's unaudited financial statements accounted for an investment valuation in FCSL of £5.8 million. On review of the financial position we noted that this was above the value of the net assets of the company with no forecast for improved financial performance going forward. We therefore identified an audit difference of £1.5 million to the investment valuation, which management has adjusted.

Falkirk Community Trust- subsidiary

We have noted through discussions with management that the arrangements at the Community Trust are currently under review by the Council with a paper due to go to the Council in September 2018 to determine the future management and control arrangements. No matters have been identified to date in respect of impacting the consolidation arrangements.

Central Scotland Valuation Joint Board - associate

Management has assessed that it exerts significant influence, but not control, over Central Scotland Joint Board. We have agreed with the assessment and the treatment therefore as an associate entity.



Falkirk Integration Joint Board (IJB) – joint venture

We agree with management's assessment of this entity as a joint venture.

We have been appointed as auditor to the Falkirk integration Joint Board and we report separately on our audit of that entity.

The only significant component by size is the Council, which accounts for 99% of consolidated gross expenditure. While the IJB accounts for approximately 10% of total expenditure, the joint venture accounting essentially leads to a gross-up of income and expenditure relating to the IJB, without additional third party spend outside of the Council/IJB relationship being incurred.

We did not identify any specific risks that may indicate a component is significant by risk, as the IJB does not affect the transactions as such, only the nominal funding agreement in and out of the IJB.

We are satisfied that management has conducted a suitable updated assessment in respect of other entities where the Council has a relationship, but it has been assessed that consolidation has not been required.

Impact on audit opinion: we are able to issue an unqualified opinion in respect of the Council's group financial statements

Statutory Trading Operations

Under the Local Government in Scotland Act 2003, the Council has to maintain statutory trading accounts for any 'significant trading operations' (STOs). The 2003 Act also prescribes that STOs have to break even over a three year rolling period.

The cumulative three-year result for the Council's statutory trading operations is a surplus of £0.7 million, meaning that the Council has met the core requirements of the Act.

Impact on audit opinion: we are able to issue an unqualified opinion in respect of the Council's compliance with statutory trading obligations.

Our overall audit approach is based upon developing a detailed understanding of your significant classes of transactions and account balances, and the internal controls established by the Council. We use our data analysers to understand and visualise the interaction of these transactions within your financial ledger.

Overall audit approach

Financial controls

It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

As part of our audit of the financial statements, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. As we have adopted a fully substantive approach, we have therefore not tested the operating effectiveness of controls.

Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control. We have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements of which you are not aware.

Use of data analytics

As the technology supporting audit develops, we increasingly utilise data analytics to support our audit conclusions over traditional sample testing arrangements. This is designed to provide a more thorough audit approach while simultaneously reducing the comparative burden of audit compliance on management.

We use our bespoke data analysers to enable us to capture entire populations of your financial data. We capture the data through our formal data requests and the data transfer takes place through secured EY sites. These are in line with our data protection policies which are designed to protect the confidentiality, integrity and availability of business and personal information.

In 2017/18, our analysers were used in the Council's audit to analyse and test journal entries, employee expenses and other income and expenditure.

Journal entry analysis

We obtained downloads of all financial ledger transactions posted in the year. We performed completeness analysis over the data, reconciling the sum of transactions to the movement from the opening to closing trial balances and financial statements to ensure we captured all data. Our analysers complete integrity checks over the data received, to identify possible indicators of incomplete or incorrect data, such as journals which do not balance to nil. Our analysers then review and sort transactions based on our identified risks, allowing us to more effectively identify and focus on journals that we consider to be higher risk, as identified in our audit planning report.

Payroll analysis

We also use our analysers for testing payroll expenditure. We obtain all payroll transactions posted in the year from the payroll system and perform completeness analysis over the data, including reconciling the total amount to the general ledger trial balance. We then analyse the data against a number of specifically designed procedures to address risks of misstatement in payroll. These include analysis of payroll costs by month to identify any variances from established expectations, as well as more detailed transactional interrogation, such as where new employees appear to have been paid before their start date.

We have no differences to report in respect of our audit procedures.

The narrative elements of a local authority's annual accounts form a key part of explaining the performance of the council during the year. They also enable the local authority to demonstrate openness and transparency in governance and remuneration provided to members and key officers.

Other reporting requirements

Management Commentary

Requirement: Regulation 8(2)(a) of the Local Authority Accounts (Scotland) Regulations 2014

Relevant statutory guidance: Scottish Government Local Government Finance Circular 5/2015

Audit responsibility: Audit Scotland requires us to read the Management Commentary and express an opinion on whether the information given is consistent with the financial statements and whether it has been prepared in accordance with the statutory guidance.

We read the Management Commentary and compared the content against the information in the financial statements and against the statutory requirements. We concluded that the content was consistent with the financial statements and prepared in accordance with the statutory guidance. We made a number of recommendations for changes to enhance certain aspects of the commentary. These were designed to ensure the commentary was:

- reflective of the progression of the Council in delivering its key objectives
- provided a good understanding of the financial performance of the business to be obtained
- demonstrated any progress made against BVAR / audit recommendations and the challenges facing the Council going forward

Management updated the commentary in a number of areas. Our view is that the commentary can still be enhanced further to provide a greater breadth of understanding for the reader, and bring it more in line with the standard we have noted elsewhere across the sector.

Recommendation one

Impact on audit opinion – unqualified opinion on Management Commentary

Remuneration Report

Requirement: Regulation 8(2)(d) of the Local Authority Accounts (Scotland) Regulations 2014

Audit responsibility: Auditors are required by the Code to audit the disclosures of remuneration and pension benefit, pay bands, and exit packages and express a separate opinion within their independent auditor's report on whether they have been properly prepared in accordance with the Regulations.

No amendments were required to the draft Remuneration Report to ensure its consistency with underlying records and presentation in accordance with the statutory requirements. The Council has disclosed appropriately exit packages provided to 2 staff totalling £0.04 million (*2016/17: 2 staff totalling £0.02 million*).

Impact on audit opinion – unqualified opinion on Remuneration Report

Annual Governance Statement

Requirement: Regulation 8(2)(c) of the Local Authority Accounts (Scotland) Regulations 2014

Audit responsibility: Auditors are required by the Code to report as to whether the statement is consistent with the financial statements and has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016)

We set out our detailed findings as part of our wider scope audit work on governance and transparency in section 3.3 of this report.

Impact on audit opinion – unqualified opinion on Annual Governance Statement

3. Wider scope audit & Best Value

Together the Accounts Commission and the Auditor General for Scotland agreed the four dimensions set out in the Code which comprise the wider scope audit for public sector in Scotland. These are: financial sustainability, financial management, governance and transparency, and value for money.

Wider scope audit

The Accounts Commission agreed the overall framework to auditing Best Value in June 2016. Best Value will be assessed over the five year audit appointment, as an integral part of the wider scope annual audit process. Every council will have a Best Value Assurance Report (BVAR) considered by the Accounts Commission in every 5-year cycle.

Our wider scope audit work, and the judgements and conclusions reached in these areas, therefore contribute to the overall assessment and assurance on the achievement of Best Value. We participate in the Local Area Network (LAN) for the Council, comprising representatives from different scrutiny bodies to agree the Council's local scrutiny plan (LSP).

The 2017/18 LSP was set in the context of the BVAR scheduled for the Council. No specific scrutiny risks were highlighted. The 2018/19 LSP was published in April 2018 and confirmed no scrutiny risks for 2018/19, consistent with the prior year. The LSPs formed the context for our audit and risk assessment.

Accounts Commission Strategic Audit Priorities

The Accounts Commission has set the following strategic audit priorities, which reflects their interest in:

A. The clarity of council priorities and quality of long-term planning to achieve these.

B. How effectively councils evaluate and implement options for significant changes in delivering services.

C. How councils are ensuring members and officers have the right knowledge, skills and support to design, develop and deliver effective services in the future.

D. How well councils are involving citizens in decisions about services and empowering local communities to identify and help deliver services they need.

E. The quality of councils' reporting of their performance to enhance accountability to citizens and communities.

The table below sets out our plan for our five year audit appointment, including coverage of the elements of Best Value statutory guidance as well as the Commission's strategic priorities, and how we will report these in accordance with the wider scope dimensions of public audit.

High level five year Best Value plan / audit coverage			
Element of Best Value, in accordance with the statutory guidance	**Reported under wider scope audit dimension**	**Linked to Strategic Audit Priority**	**Audit year**
Performance and outcomes	Value for money	B	Year 2
Improvement	Value for money	-	Year 2/5
Leadership, Governance and Scrutiny	Governance & transparency	A, C	Year 5
Equal Opportunities	Value for money	E	Year 3
Partnership Working and Empowering Communities	Governance & transparency	D	Year 4
Financial and service planning	Financial sustainability	A, C	Year 3
Financial governance and resource management	Financial management	-	Year 4
BVAR	All	All	TBD
Follow up of BVAR	All	All	Year 1 / 2

Year 1 = 2016/17 Year 2 = 2017/18 (this year) Year 3 = 2018/19 Year 4 = 2019/20 Year 5 = 2020/21

3. Wider scope – Best Value overview

Auditor considerations of the Council's arrangements to secure Best Value

In February 2018 the Accounts Commission published its follow up report on the Council's progress against its previous BVAR from 2016. In its findings the Accounts Commission reported positively on the progress made by the Council and the plans for further implementation of improvements, in particular around the Council of the Future transformation programme. It did however note the importance of transitioning from planning to implementation, and a need for an increase in the pace of change in improvements, to ensure the required savings and improvements are delivered. The Commission endorsed the recommendations set out in our Annual Audit Report for the 2016/17 financial year, in particular those relating to our work around the four dimensions of wider scope audit, expecting the Council to act on these as part of its ongoing implementation of improvements relating to Council of the Future and the Council's Corporate Plan.

As part of our 2017/18 annual audit we considered both the Council's approach to tracking progress against the recommendations and the actual progress around the required actions. Actions were agreed by management in the 2016/17 Annual Audit Report; we have followed up on the status of these actions through our work in 2017/18, as outlined in the relevant sections.

The main focus of our work in 2017/18 has therefore been the follow up of the Controller of Audit recommendations, our Annual Audit Report, as well as the Accounts Commission's findings. This has been undertaken in cooperation with the Audit Scotland team involved in the original Council BVAR and subsequent follow up work.

Management's assessment of progress showed varied results at the time of our onsite audit work in July 2018. Many elements of the recommendations will of course require ongoing work to deliver as they relate to longer term objectives around financial sustainability and value for money. Management's self-assessment formed the basis of our audit work as reported in the wider scope sections of this report. We have addressed the current status of recommendations through these sections of the report.

3.1 Financial management

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.	
Green	▶ Overall, the Council has demonstrated good financial monitoring of the in-year revenue budget. There is scope for improvement in the monitoring and reporting of the capital budget. ▶ The importance of good financial control is clearly understood across the Council. In our view the Council currently has sufficient financial skills, capacity and capability, however this is an important area that needs to be kept under review.

2017/18 financial statements and context around financial management

The Council incurred gross expenditure on the provision of services of £613.7 million (*2016/17: £602.4 million*), and incurred an accounting deficit of £6.4 million (*2016/17: £1.2 million surplus*) on those services. This is shown in the surplus / deficit on provision of services line within the Comprehensive Income and Expenditure Statement (CIES) which sets out the cost of providing Council services in accordance with generally accepted accounting practices.

The Expenditure and Funding Analysis (EFA) note to the financial statements provides an explanation of how this expenditure is used and funded by the Council. This is different from the accounting position shown in the CIES in accordance with the Code and, together with the Movement in Reserves Statement, demonstrates how the Council's statutory reserves, including the General Fund, have changed in the year. As shown in the EFA, the outturn for the financial year against the Council's General Fund was a surplus of £2.7 million (*2016/17: deficit of £0.12 million*). These results are within the context of a continuingly challenging financial environment, as we have outlined in our reporting on financial sustainability.

Financial statements results	2017/18 £000	2016/17 £000	Commentary	RAG rating
(Surplus) / deficit on provision of services	**6,430**	(1,220)	The accounting deficit includes capital and pension fund accounting items which are not directly controllable by the Council. While accounting surpluses are preferable the key focus is on the movement in the Council's useable funds.	G
(Surplus) / deficit on General Fund and HRA	**(2,672)**	119	This reflects a change from the budgeted position, which projected a draw on reserves of £3.3 million. This is mainly due to non recurring transactions, including a VAT refund of £0.7 million, additional RSG of £1 million, and an adjustment of £0.9 related to Council Tax bad debt provision.	G
Uncommitted general fund	**(13,077)**	(11,529)	This is consistent with the Council's reserves strategy, which requires a minimum of £6.6 million. The approved 2018/19 budget is projecting a decrease of £2.3 million.	A
Earmarked reserves	**(14,397)**	(13,545)	Earmarked reserves provide the Council with some flexibility around key initiatives. The increase comes from an increase in grants related to the Pupil Equity Fund, which was carried into 2018/19, offset by a decrease in the Devolved School Management reserve.	A
Net current liabilities	**(36,691)**	(43,956)	2017/18 has seen a decrease in net current liabilities, attributable to a rise in short term debtors and cash deposits. The net position could still potentially lead to an inability to meet liabilities as they fall due, however good cash flow management will ensure that this risk does not materialise.	G
Total Usable Reserves	**(44,354)**	(42,278)	The increase is due to an increase in General Fund, partially offset against a decrease in the Capital Receipts Reserve.	A
Total Unusable Reserves	**(357,291)**	(133,933)	The increase in unusable reserves has primarily arisen due to a £197.7 million actuarial gain in the accounting for pension liabilities in the year.	G
Net increase / (decrease) in cash	**5,423**	(10,798)	The increase in cash is primarily a result of a reduction in investments held as these are translated back into cash for use in the Council's activities.	G

Elements of financial management, and our assessment of the Council's arrangements

- The budget monitoring reports include both the full-year commitments entered during the reporting period, together with the forecast outturn position. Separate budget monitoring reports are presented to the Council Executive outlining the Housing Revenue Account (HRA) position. In line with prior year, the HRA achieved a small surplus during the financial year.
- The final expenditure outturn for the Council in 2017/18 was £330.5 million, a favourable variance of £2.8 million against the approved budget. The most significant variance between budget and actual was in Corporate & Housing Services, which had a favourable outturn from budget of £4.2 million, or 14.6% of its overall budget. This was mainly attributable to savings on staff cost (£2.3 million), a non-recurring VAT reclaim (£0.7 million), and additional government funding in the year (£1 million). From our review of in year monitoring reports these variances occurred through the year; the variances were reported in a timely manner and not indicative of poor financial budgeting at the start of the year. Children's Services outturn was only £0.1 million over its budgeted outturn, however through the year the reporting on projected outturn varied significantly. The improved outturn position from the month 9 projection reflects an underspend relating to the Pupil Equity Fund and Early Years Expansion Programme which has been carried forward into 2018/19.
- Table 2 sets out the capital programme for 2017/18 and delivery against budget. The budget set out below includes an additional £7.6 million expenditure approved for the year following slippage in the 2016/17 capital programme. The Council subsequently reported a significant underspend in general services capital expenditure in the year of £5.2 million. This underspend increases to £8.2 million when externally funded capital projects are taken into account. Only £5.2 million of slippage was reported to Council Executive in February 2018, with the additional £3 million reported in the final outturn report in August. While some of this slippage was due to the inclement weather experienced in March, in our view the majority of this slippage could have been identified and reported at an earlier stage in the financial year. The capital programme outturn has followed a similar pattern in recent years; brought forward spend through prior year slippage, then increasing slippage in the programme through the year resulting in significant underspends at year end. There is scope to improve the monitoring and reporting around the capital programme.

Recommendation four

Table 1 - Analysis of budget monitoring reports presented to the Council Executive during 2017/18	Variance v budget on monthly monitoring				Actual Net spend £000
Service area	Month 4 £000	Month 6 £000	Month 9 £000	Outturn £000	
Children's Services	740	1,169	986	110	184,057
Social Work Adult Services	(567)	(472)	(486)	(413)	5,196
Development Services	135	135	-	201	29,095
Corporate & Housing Services	(1,564)	(1,946)	(3,339)	(4,207)	24,830
Housing Revenue Account	-	-	-	-	(1,224)
Valuation Joint Board	-	-	-	-	1,215
Falkirk Community Trust	-	-	-	-	11,433
Integration Joint Board	-	-	-	-	58,723
Service expenditure	**(1,256)**	**(1,114)**	**(2,839)**	**(4,309)**	**313,999**
Non-service expenditure	(350)	(130)	584	1,447	16,549
Total Net expenditure	**(1,606)**	**(984)**	**(2,255)**	**(2,862)**	**330,548**

Table 2 - capital programme	2017/18 budget- £000	2017/18 actual - £000	Variance -£000
General Services	33,595	28,317	(5,278)
HRA	31,228	32,893	1,665
Total	**64,823**	**61,210**	**(3,613)**

3.1 Financial management (cont.)

Elements of financial management

- Can the body demonstrate the effectiveness of the budgetary control system in communicating accurate and timely financial performance?
- Do finance reports support effective scrutiny and challenge?

Budget monitoring reports are presented on a quarterly basis to the Council Executive. Monitoring reports provide an appropriate level of detail, split between General Fund, and the Housing Revenue Account, and analysed by service line. Narrative commentary highlights where variances have occurred and the drivers behind these.

Each monitoring report includes the projected outturn in a tabular format, displaying the budgeted position, the projected outturn, as well as any variance. This allows members to easily see where the variances are occurring, and then to investigate this further using the information provided - this supports members to exercise appropriate oversight.

- Are standing financial regulations comprehensive, current and promoted within the body?
- Does the body have arrangements to ensure systems of internal control are operating effectively?

Financial regulations are comprehensive, covering financial management and planning; risk management and control of resources; and systems and procedures. They are available publicly on the website and updated most recently in October 2015 with a review and update currently being undertaken by management. It is planned that these will be finalised before the end of 2018. The regulations appear to remain appropriate for the Council's requirements at this stage, however regular review and challenge is important to the robustness of the regulations.

Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control which we identify. We have not identified any such matters to report.

- Are there suitably qualified and experienced officials leading the body's finance team?
- Is there sufficient financial skills, capacity and capability in the body?

The Council's section 95 officer is the Chief Finance Officer. We considered the role and status of the section 95 officer and are satisfied that the Council adheres to the principles laid out within CIPFA's Statement on the role of the Chief Financial Officer in Local Government.

From our discussions with senior management, attendance at meetings, and review of papers and minutes, in our view there is evidence that the Council currently has sufficient financial skills, capacity and capability. However, management is conscious of the context of a significant reduction in finance resources in recent years, and has recently identified a permanent replacement for the senior corporate finance manager which was noted as vacant at the end of the 2016/17 audit.

While the preservation of front-line services is understandably of prime concern to members and officers, maintenance of strong financial control to support service transformation necessitates the retention of suitable financial and other corporate support services. Keeping this balance will be a challenge for all local authorities in the current environment but the importance of doing so cannot be understated. This is an important area that needs to be kept under review by management, with ongoing scrutiny from members, particularly in conjunction with the progress of recommendations around financial management.

Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.	
Red	► The Council continues to experience financial pressures. Significant progress is required to deliver 2018/19 outturn in line with budget and to support approval of a robust 2019/20 budget. ► The Medium Term Financial Plan is being developed in conjunction with the objectives of the Council's Corporate Plan and is linked to the developments in the Council of the Future change programme. ► There are extensive funding gaps over the period to 2023/24, with the level of savings required over the next five years significantly greater than the identified savings. Difficult decisions will have to be taken to achieve financial balance. There is a need for an improvement in the pace of transformation to support the delivery of a robust Medium Term Financial Plan.

The context for financial sustainability

Since we issued our Annual Audit Plan, the Accounts Commission issued the second part of their overview reporting for Local Government in Scotland: Challenges and performance 2018. This report recognised the complex and challenging environment facing local government, citing for example:

- the significant uncertainty around terms for the UK's withdrawal from the European Union (EU);
- revenue funding from the Scottish Government has fallen in real terms by 9.6% between 2010/11 and 2018/19; and
- Scotland's population is getting older, leading to increased demand for social care services and fewer working age people to fund public services.

Some national policies, however, combined with ongoing spending commitments such as pension and debt costs, mean there are limitations on where councils can make savings. Smaller service areas, which often include important regulatory functions, have seen the biggest budget reductions, while education and social care services take up a growing proportion of council spend.

Findings of the BVAR / prior year audit

In the prior year audit, we made a number of recommendations around financial sustainability, which were subsequently supported in the BVAR follow up report considered by the Accounts Commission in February 2018. We have reported on progress in respect of specific recommendations in this section, in particular around the level of useable reserves and Council borrowing, and achievement of the required future financial savings.

Focus on EU Withdrawal

Management has ensured the Council and Council Executive are sighted on the issue of Brexit and the possible implications for the Council's service delivery at a high level, through the inclusion of "uncertainty around Brexit" in the risk register which is reviewed routinely by Council Executive. The Council recognises the risk to the local economy as well to the Council specifically in terms of budgeting and staff resource pressures.

The uncertainty around Brexit is also highlighted as a significant uncertainty and sensitivity around financial planning for the Council. It is routinely referenced as such in budget monitoring reports and more recently in the Council's financial planning papers for its Medium Term Financial Plan. Management has noted the difficulty in quantifying the impact and addressing service delivery issues while there is the current degree of uncertainty, and continues to monitor developments.

EY view: Management is sighted on this issue. As the implications become clearer, there is scope for greater focus on the particular risks which could crystallise in respect of, for example, delivery of social care services, and the impact on specific services in receipt of EU funding.

3.3 Financial sustainability (cont.)

Aspects of financial sustainability, and our assessment of the Council's arrangements

- Does the Council have a medium term financial strategy / long-term financial strategy?
- How has the Council factored in the demographic impact of changes in population, demography and demand within its financial plans?

- As noted by the Accounts Commission in their 'Financial Overview 2016/17', an important element of financial sustainability is longer term financial strategies and planning. Formulating such plans and strategies, encourages councils to look beyond the current year, and seek efficiencies and savings which will facilitate sustainability over the longer term. One of the conclusions from the Best Value follow up report published in February 2018 was the expectation that the Council demonstrates its ability to meet the future financial challenges through financial strategies and savings plans, linked to and driven by its transformational improvement plans.
- Recognising the context of the increasing financial pressures facing the Council, management is continuing to work on the Council's Medium Term Financial Plan. This outlines the projected resource shortfall in the five year period to 31 March 2024. We have outlined the funding gap for the five year period in the table below, including management's assessment of possible variances between base; optimistic and pessimistic planning scenarios.
- There is a significant variance between each of the three projections, with the base funding gap being 50% of the pessimistic, and the optimistic being 44% of the base gap. While these represent more extreme outliers in possible future scenarios, they recognise the potential scale and degree of uncertainty the Council faces over the period of the MTFP. The key assumptions driving these variances are around future revenue support grant levels, which have yet to be confirmed by the Scottish Government beyond 2020, future forecasts for employee salary and pension costs and wider demographic movements impacting service needs across the Council. The base projection assumes 3% Council Tax increases for the period of the MTFP.

Forecast budget gaps / required savings	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Pessimistic	32.7	24.6	22.2	23	22.6	125.1
Base	**14.1**	**13.6**	**11.1**	**12**	**11.7**	**62.5**
Optimistic	8.3	6	3.8	4.7	4.9	27.7
Savings identified to date	**10.8**	**6.4**	**5.5**	**6.4**	**6.2**	**35.3**
Remaining budget gap	**3.3**	**7.2**	**5.6**	**5.6**	**5.5**	**27.2**

Source: Falkirk Council MTFP progression report – September 2018

Addressing the budget gap and delivery on savings

The Council is planning a multifaceted approach to addressing the required savings. The Medium Term Financial Plan is being developed in conjunction with the objectives of the Council's Corporate Plan and is linked to the developments in the Council of the Future change programme. We report on the progress around the Council of the Future change programme as part of our value for money considerations.

While there is alignment between the Council's financial planning arrangements and improvement plans, notably Council of the Future, the scope of savings required over the next five years continues to be significantly greater than the identified savings through CoTF over the same period. This means the Council will continue to be reliant on other approaches to achieving savings to balance budgets.

- Of the £14.1 million savings required for 2019/20, only £10.9 million has been identified to date. Of this, £1.7 million relates to existing Council of the Future projected savings. Other planned savings are forecast from health and social care integration, reduction in Trust costs and increasing fees and charges, which the Council forecasts could account for an additional £3.5 million of the budget gap. The £10.9 million total savings identified includes £4.6 million from savings options not taken up in prior year budget decisions by members. Even with all these savings components taken together, to achieve a balanced 2019/20 budget a further £3.2 million of savings still requires to be identified.
- Of the £62.5 million forecast savings required over the period 2019-2024, only £35.4 million has been identified to date, of which £5.5 million is currently from approved Council of the Future projects. Management forecasts these to increase as more projects are scoped, approved and implemented.
- While the anticipated savings to be achieved through health and social care integration are included in the Council's latest iteration of its Medium Term Financial Plan, these are not defined in detail and are more subject than most savings to the budget sensitivities outlined on the previous page, especially given changing demographics, with an expected 3% increase in population, and 25% increase in over 80s by 2025.
- Management has outlined a comprehensive approach to addressing the funding gap over the period to 2024. However, the timeline of the various work streams, combined with the current position of the Council of the Future programme means the Council will continue to be reliant on a traditional approach to balancing budgets for 2019/20 and possibly 2020/21. This approach, of identifying and selecting savings options from existing expenditure, will become more challenging. Additionally, the Council's reserves position going forward reduces the ability to draw on reserves.

A significant amount of planning is underway to address savings requirements through to 2024. However, the implementation of these plans does not align with the pace required to address budget gaps, in particular the £14 million gap in 2019/20 and the £62 million gap through to 2024. There will be significant challenges in identifying savings through the approaches the Council has traditionally relied upon. Difficult decisions will be need to be taken to achieve financial balance.

Recommendation eight

EY view – example of best practice

In our view best practice in medium term financial planning would be evidenced through the identification and approval of the required savings across the planning period. The later years in any MTFP are likely to require some refinement given sensitivities and developments in service requirements. Approval of a MTFP provides the agreed framework within which officers can plan and deliver the required levels of transformation to achieve the extent of service change to meet both users needs and the deliver the significant level of financial savings.

Use of reserves – does the Council have clear plans for its usable reserves?

The Account Commission previously highlighted its concern at local authorities' utilisation of General fund reserves. In our prior year report we emphasised the importance of the Council having sufficient reserves to call upon should they be required and recommended the Council ensure effective scrutiny of the use of reserves going forward.

As at 31 March 2018, the Council has uncommitted General Fund reserves, of approximately £13 million, this is in line with the Council's Reserves Strategy which provides for 2% of annual revenue expenditure to be held as uncommitted General Fund reserves. This represents an increase from 2016/17 of £1.5 million.

The Council plans to utilise £2.3 million of General Fund reserves to balance the 2018/19 revenue budget. In the 2018/19 period four revenue outturn report management reported a forecast negative variance against budget of £4.3 million, which if not addressed would result in a corresponding further call on reserves and forecast yearend reserves position of £8.1 million.

In the most recent outturn report, the Council's section 95 officer highlighted the pressure on the Council's reserves and the potential likely future requirements from unbudgeted costs around equal pay and other claims. In recent years the Council's budgeted use of reserves has often not materialised to the extent forecast, allowing reserves to be called in subsequent budgets. However, the increasingly acute financial position of the Council reduces scope to utilise this approach to balance budgets going forward.

Involvement of members in setting priorities, and approval of budgets

In the Accounts Commission's findings on the BVAR, they reported that it was crucial that elected members play a more prominent and leading role in responding to these challenges. In particular, it was recommended that members should identify earlier in the budgeting process the priorities which need to form the basis of engagement with communities.

The Council are proactive in involving members in the budget setting process, with regular forward looking reports being provided to both meetings of the Council Executive and full council. Members are also consulted on the key options and decisions faced by the Council in the delivery of the savings required. There is a member budget working group which meets regularly prior to the annual budget meeting to consider and respond to budget proposals. Members have also been involved with the production of the Medium Term Financial Plan.

As with many local authorities across Scotland, the Council will need to continue be proactive in its consultation with members to bridge the projected funding gap. Members will need to make difficult decisions and reconsider how services are delivered to achieve the required level of savings.

Capital investment – general services

The Council approved a three year, £84 million, capital investment plan in February 2018. Officers have recognised the revised Prudential Code and Treasury Management Code of Practice issued by CIPFA in December 2017. In response, officers are preparing a detailed Capital Strategy for integration into the Council's Medium Term Financial Plan. In 2019/20, the Council plans to produce a five year Capital Plan, aligning to the Medium Term Financial Plan period, supporting better forward planning.

The Council recognise that resources available for capital investment are likely to be constrained in light of the forecast revenue budget gaps. To ease pressure on the revenue budget, the Council has taken the decision to restrict the planned prudential borrowing (excluding Tax Incrementing Finance) to a nominal amount (£0.6 million) and focus on other sources of financing for capital investment. The overall projected resources to be utilised for the investment are summarised below.

We have reported in the financial management section of this report on the recurring slippage in delivery and issues with forecasting in respect of the Council's capital programme. Effective delivery and monitoring of annual capital plans will inherently have an impact on the Council's longer term capital plans and subsequent financing strategies.

Recommendation four

The most significant elements of the capital programme relate to roads and infrastructure, (approximately £27.5 million; 32% of forecast capital expenditure). Significant capital expenditure is planned on infrastructure projects under the Scottish Government's TIF initiative (£26.3 million; 31% of forecast capital expenditure), and £13.8 million; 16% of forecast capital expenditure on school improvements.

Projected resources	£ million
Scottish Government Grants	46.4
Capital Receipts	5.2
Prudential Borrowing	0.6
Prudential Borrowing / CFCR for TIF Projects	26.3
Other funding (Planning Obligations, CFCR etc.)	5.8
Total	**84.3**

Capital investment – housing

A three year housing capital investment programme was approved in January 2018, covering the period to 2020/2021. This totals £143 million, of which the main elements relate to £47 million for building new housing stock and £70 million for housing improvement work. Management estimate that approximately £27 million of revenue resources, £24 million of Scottish Government Affordable Housing Grant and borrowing of £92 million, will be needed to fund the expenditure over the next 3 years.

3.3 Governance and transparency

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information.	
Green	• The Council has an established governance structure through Council and standing committees. The governance framework comprises Standing Orders, Scheme of Delegation and Financial Regulations. • Progress in responding to recommendations to enhance governance arrangements has been mixed. There is scope to ensure the Audit Committee is better sighted on the status of implementation of recommendations in respect of audit and other scrutiny activity.

Leadership and corporate planning

Following the local elections in May 2017, the new administration continued to input into preparing of the Council's Corporate Plan, including the embedding of the Council of the Future transformation programme. Both the Corporate Plan and the Council of the Future was subject to consultation by a cross party group of members. The revised Corporate Plan, and the Council of the Future change programme, was subsequently approved by the Council at the end of 2017.

There have been significant developments in the leadership arrangements at the Council since the approval of the Corporate Plan. Following the local elections in May 2017, the Council maintained the executive and scrutiny model which gave the principal decision making roles to the Council Executive and Education Executive, both of which had an administration majority. This was balanced by two scrutiny committees, equally balanced between opposition and administration members, with the chair being an opposition member. The administration formed after the election comprised a minority of the Council's members. In April 2018, the Council voted to politically balance the Council Executive and Education Executive between the political groups represented on the Council. They also decoupled the chairing of these committees from the role of the Council Leader. This led in turn to further changes in the composition and chairing arrangements on the scrutiny committees. Both committees became politically balanced and the chairing is shared by the two groups not holding the chair of the Council Executive or Education Executive.

The Council's view is that the distinction between the decision making role of the Executive committee and the scrutiny and oversight role of the scrutiny committees has been maintained, and that members are working well together on scrutiny activity. Agreement was reached among members to share the convenorship of the Executives and Scrutiny Committees between the main political groups. It is recognised that these arrangements may need to revisited in the event that a majority administration is formed in the future.

Commitment to transparency

Audit Scotland issued auditors with supplementary guidance covering transparency in public sector bodies in Scotland. We have utilised this guidance as part of our audit work, and in particular the questions for auditors to consider.

We have identified the following relevant aspects of the Council's arrangements:

- Decisions are transparent as actions are documented within Council and committee minutes.
- There is a high level of transparency through the Council's website, which includes minutes and papers for all committee meetings.
- Corporate strategies and management plans are included on the website, and there are links to Council performance reports.

3.3 Governance and transparency (cont.)

Annual Governance Statement (AGS)

The AGS sets out the Council's governance framework. The Council supports its arrangements through its local code of corporate governance, and assessments are undertaken regularly of compliance against this. Other core support for the AGS is through the system of compliance statements which are obtained from key individuals in the Council's management team, relating to their areas of responsibility.

In the prior year we made suggestions to management on the form and content of the AGS and these were agreed to be considered for the 2017/18 financial statements. In our initial review of the current year unaudited financial statements we made a number of similar comments and identified a number of areas where we believed the AGS could be strengthened. In particular these were around:

- reflecting the developments of governance arrangements in the year, in particular with regards to changes in the structure of the Council's executive committees
- including a summary of the structure of the Council / executive administration and the arrangements for scrutiny, linking to the developments in the year
- inclusion of an assessment of progress against the Accounts Commission's and our own recommendations arising from the 2016/17 annual audit.

No significant weaknesses in corporate governance were identified in the AGS.

The annual report from the Internal Audit, Risk and Corporate Fraud Manager is a significant source of support for the AGS. This report for 2017/18 provided substantial assurance to the Audit Committee and concluded *"there were largely satisfactory risk, control and governance systems in place."*

Adding value to the Council	We made a number of recommendations to management around improvements to the AGS. We have also followed up on a number of recommendations and areas for improvement to governance and transparency arrangements we identified in our 2016/17 audit. We report on these matters further below.

Actions taken in response to the prior year annual audit report recommendations

The February 2018 BVAR follow up report made a number of observations around the governance arrangements for Council of the Future, which we have commented on within the value for money section of this report. We have reported on developments in respect of internal audit working arrangements on the following page. In our 2016/17 Annual Audit Report we made three further recommendations around governance and transparency of the Council for follow up in 2017/18.

Audit Committee work plan

The Council has agreed that following approval of the Committee's schedule and agenda for 2019 an underlying work plan will be prepared to supplement the core work plan set up with the committee's terms of reference a number of years ago.

Review of joint working arrangements by internal audit

Management has confirmed that the joint working arrangements for internal audit with Clackmannanshire Council have been subject to the review and the arrangement has been extended for another two years. We have not noted any delivery matters arising from the joint working arrangement during the year, with internal audit continuing to deliver its work programme in line with agreed timetables.

Falkirk Community Stadium Limited

Arrangements remain in place whereby Council officers act as Directors for FCSL. We reported in 2016/17 this was a potential conflict of interest. Management has confirmed a report on the company's financial and management arrangements would be provided to the Council before the end of the calendar year, and would include a review of the director appointments.

Recommendation six

Overall, progress in responding to recommendations to enhance governance arrangements has been mixed. In our view, implementation of recommendations would be supported by more robust and proactive monitoring and reporting on the status of audit recommendations, with scrutiny from the Audit Committee.

Internal audit / risk management

The Council's Internal audit, risk and Corporate Fraud team is responsible for ensuring that there is a corporate framework which enables the Council to effectively manage its risks. The unit also independently audits key risks and investigates allegations of fraud or irregularity. The team is comprised of full-time equivalent staffing of 7.8, including 3.8 in internal audit, 2 in corporate fraud and 1 in risk management in addition to the internal audit, risk and corporate fraud manager.

The Audit Committee approves an annual internal audit plan. The 2017/18 internal audit plan was completed and enabled the Audit, Risk and Corporate Fraud Manager to provide his annual opinion to the Audit Committee. The internal audit annual assurance report concluded that internal audit could provide substantial assurance on the Council's arrangements for risk management, governance, and control for the year ended 31 March 2018. The only individual report which resulted in "limited assurance" related to a review in Social Care and Education Transport, in particular around the compliance arrangements for volunteer drivers for the Council.

National Fraud Initiative

The Council's internal audit team coordinates the National Fraud Initiative (NFI) biennial data matching exercise. The 2016/17 matches were received in January 2017. The NFI exercise identified 8,366 matches, of which 2,896 were recommended matches. These are matches which, in the opinion of the NFI administrators, are more likely to result in fraud or error being identified. As at 31 March 2018, 3,354 of the identified matches have been processed and closed on the NFI system. While this represents 41% of the total matches, management estimates the majority of the recommended matches have been addressed. The data matching exercise has identified no frauds and 14 errors resulting in a total overpayment of approximately £18,000, which is currently being recovered.

In 2016/17 we recommended that NFI could be given a greater emphasis as a core element of counter fraud arrangements. The internal audit, risk and corporate fraud team has taken this recommendation into account in 2018/19 as part of its risk based approach to allocating resources around counter fraud. In 2017/18, the Council has made progress in related programmes, such as an exercise to identify wrongly claimed Council Tax discounts, with an estimated £142,000 in the process of being recovered.

Risk management

The Council's Risk Management Policy and Framework was updated during 2017/18, and Corporate Risk Management Group (CRMG) oversees the application of policy and framework. All 'high' risks are considered and reviewed on a cyclical basis by CRMG. CRMG reports to the Corporate Management Team, with periodic updates provided to the Audit Committee and Executive.

Adding value to the Council

In response to an audit recommendation from the 2016/17 annual audit, and subsequent peer review of internal audit which took place during 2017/18, internal audit is revising its audit work to better align with the Council's risk register, and including a grading system for its recommendations resulting from its work. These will support the Audit Committee and members in understanding both key priorities for implementation of audit recommendations, and how the work programme being delivered is supporting the Council's governance framework and addressing key risks.

We have agreed to review any proposed changes in advance of implementation to both agree the adequacy of changes and to provide our own insight into best practice from our experiences in the sector and beyond.

As part of these arrangements there is scope to ensure the Audit Committee is better sighted on the status of implementation of recommendations in respect of audit and other scrutiny activity.

Recommendation five

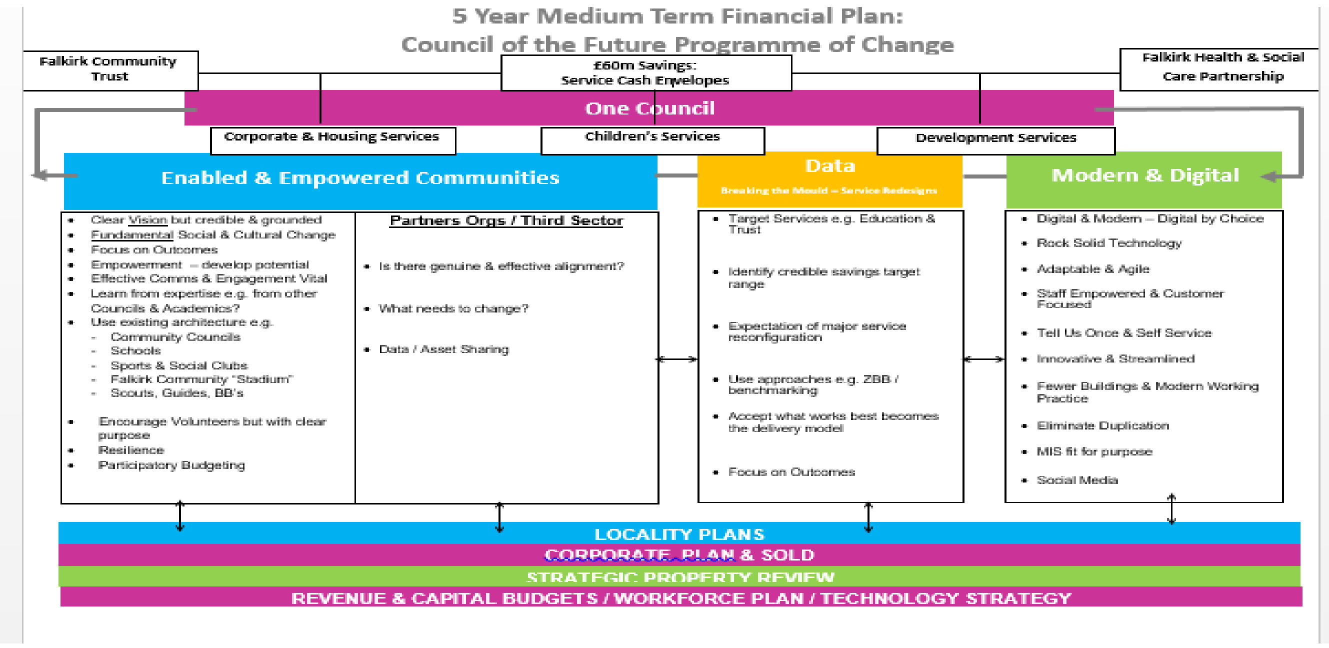
3.4 Value for money

Value for money is concerned with using resources effectively and continually improving services. A focus for our work in this area is the Council's progress in respect of its transformation programme.

Red	► From a delivery perspective, individual Council of the Future projects have progressed, and plans are in place to continue the delivery of existing projects, with the approval of new projects ongoing. ► In our view the overall status of the programme is one of being still in the earlier phases of implementation. Significant improvement is required over the pace of the programme and in moving from planning to implementation and delivery. ► There has been progress in enhancing the governance and management arrangements over the Council of the Future transformation programme. Further enhancements could be made to facilitate more effective transparency and scrutiny; enabling more timely identification and action on delivery risks.

The context for value for money

In September 2017 Council was updated on the progress of the Council of the Future change programme, and approved the programme in line with the Council's Corporate Plan through to 2022. This reflected the Council's vision of being a "responsive, innovative, trusted and ambitious organisation". The integration of the key work streams for Council of the Future into the Council's Corporate Plan and priorities is set out below. The alignment between Council of the Future and the Council's corporate plan and priorities are outlined in the diagram below.



Council of the Future is the Council's key transformational change programme to underpin the delivery of the Corporate Plan. There is a risk that any failure to deliver multi-year projects on time will lead to significant financial and operational difficulties for the Council. We have reported on the financial context for the Council in our financial sustainability section of this report.

In our 2016/17 Annual Audit Report, we noted that strong programme management should be in place around the Council of the Future, to enable:

- ► Dashboard reporting of the programme as a whole
- ► Clear deliverable milestones within individual projects
- ► Risk ratings against progress
- ► Timeline of savings / efficiencies expected over 5 years to meet budget gaps

These recommendations were supported by the Accounts Commission in its follow up report in February 2018, with an expectation of an update on the Council's progress in relation to both specific recommendations and the overall pace of change in this Annual Audit Report.

3.4 Value for money (cont.)

Elements of value for money, and our assessment of the Council's arrangements

Progress and key developments in Council of the Future

In its report in February 2018 the Accounts Commission noted "the council has demonstrated that it responded positively to the Accounts Commission's December 2016 findings. It has made satisfactory progress against the Accounts Commission's findings, given the relatively short time period since December 2016 and the impact of the local government elections in May 2017." In particular it noted the progress in taking forward Council of the Future as an ambitious and coordinated improvement programme, the successful period of engagement with staff, elected members and other stakeholders about the programme, and the development of its new corporate plan and supporting service plans. A significant level of employee and stakeholder engagement, including Elected Members, Partners and Trades Unions, is continuing to form the ongoing self-assessment process to shape the Council of the Future programme.

As a result of the engagement and consultation process, Council of the Future was designed and approved to deliver against four organisational capabilities:

- One Council
- Enabled and Empowered Communities
- Modern & Digital
- Data

The Council plans to continue its cycle of 'plan-do-check-act' to ensure that the priorities and delivery of projects are monitored in line with the Corporate Plan priorities and Medium Term Financial Plan, through continuous self-evaluation. We have outlined the scrutiny and governance arrangements for Council of the Future later in this report.

In 2017/18 Council of the Future progress included completion of a number of projects. Examples include a new contact centre, a "smart work smart travel" project to transform the way the Council does its business, re-design of day services, and an on-line system for health and social care. The Council's business support service has transitioned to a new way of working as part of the overall transition to how the Council delivers services. Completed projects resulted in savings for 2018/19 of around £5 million, in line with the forecast savings included in the approved 2018/19 budget.

Management intends that the focus on improvement will be built into the next cycle of Council of the Future projects which will emerge as part of the Medium Term Financial Plan, currently being worked up as 'Service Reviews' and 'Business Plan' initiatives. From all of this, management is expecting that the Council of the Future will be the principal delivery mechanism for the majority of the financial savings identified within the Medium Term Financial Plan from March 2019.

Elements of value for money, and our assessment of the Council's arrangements

Leadership, Governance and Reporting around Council of the Future

The Council remains committed to Council of the Future (CoTF), as its major change programme, as a diverse and ambitious programme of modernisation and cultural change across the organisation. In August 2018 a new Chief Executive was appointed and he is responsible for chairing the CoTF Board.

Following a review of the CoTF governance arrangements the Council has begun implementing a number of changes following approval by the CoTF Board. The review supports continued direction from members, the new Chief Executive, and service directors. The following changes were agreed:

- The main political groups to nominate two elected member representatives to attend CoTF Board, with a named substitute. The proposed named substitute measures should ensure more consistent attendance by members. Officer representation is to remain the same, with the Chief Executive and directors attending.
- Refreshed project management and reporting requirements. The Council intends to examine its arrangements for planning and reporting at service / project level over Autumn 2018. This is important to enable effective, consistent planning and management of CoTF projects, with clear lines of accountability.
- Improved communication and transparency by making CoTF Board papers available to all members and staff, including webinar communications.
- Project management training for project managers responsible for CoTF projects and for other staff involved in projects. It also recommended consideration of a simplified project methodology.

The Project Management Office (PMO) has been strengthened to include additional project managers and support and communication posts which are to be in place by the end of September 2018. The PMO is also providing more consistent support at service level by embedding a PMO representative into each service change group.

There is regular reporting of project progress to the Council Executive; the CoTF risk register and project update is reviewed at Audit Committee, and progress is reported to the CoTF Board at its monthly meetings. The Board also considers the programme risk register at each meeting to ensure it remains current and correctly graded, and completes a full review every six months.

In our view there is evidence of established reporting arrangements around CoTF across the Council, and the reporting does provide a reasonable level of detail to update management and members around progress. However, there are further enhancements that could be made to CoTF reporting arrangements to facilitate more effective transparency and scrutiny and to further support timely identification and action on risks around delivery of projects and the programme as a whole. We have outlined a number of possible areas for improvement below for management consideration and discussion going forward:

- Reporting around CoTF progress could be more clearly defined into detailed project updates and a more strategic summary of overall programme progress against the Council's Corporate Plan.
- Detailed reporting to the Executive Committee and CoTF Board could be further enhanced to more clearly articulate project progress against agreed milestones, savings made to date and forecast, and key project specific risks. This would help facilitate effective challenge and scrutiny on how specific projects are progressing.
- Reporting to the Audit Committee and members on the overall state of the programme could be enhanced to help show progress in the context of the "bigger picture" at the Council. This could include updates of financial savings to date and forecast against the MTFP and budget targets, the impact of completed projects against key corporate and service plan priorities, and the overall risk position of the programme, such as the possible impact of enabler projects on delivery of future work.

Recommendation seven

Elements of value for money, and our assessment of the Council's arrangements

Our assessment of the Council's progress, and pace of change in CoTF

The Accounts Commission report in February 2018 noted that "the Council is now moving into the implementation phase of CoTF, and that a focus needed to be on quantification of anticipated savings going forward and to further develop the detail of the CoTF projects and the savings that they are expected to deliver over the five-year period".

In our view there has been ongoing progress in the development and enhancement of the governance and management arrangements over the CoTF transformation programme since February 2018. From a delivery perspective, individual Council of the Future projects have progressed, and plans are in place to continue the delivery of existing projects, with the approval of new projects ongoing. We recognise the Council's view that CoTF should be subject to ongoing planning as new projects are approved to continue improvement and delivery of savings, especially those subject to other enabler projects currently underway. Our view is that the overall status of the programme is one of being still in the early phases of implementation. This is based on our assessment of the status of existing projects, and the expectation of the scale of CoTF work still be approved for future years. We have reported in our financial sustainability reporting that the scale and pace of delivery around CoTF from a financial savings perspective is currently insufficient to meet the level of savings required through to 2024.

Approximately half of the approved CoTF projects are in early stages and some projects are not yet clearly defined in terms of objectives and planned savings. The Council has attributed £5.5 million of savings from 2019/20 to 2023/24 to existing CoTF projects. However, given the stage of progress of a number of these projects there is an inherently higher risk that these will not be delivered. The Council has noted that the CoTF is a "live" programme and continues to grow and develop as new projects are identified and approved for implementation. This should support the growth of identified savings throughout the life of the programme and the Council's Corporate Plan.

The Council has recently been working to align future CoTF projects with the MTFP and corporate priorities, including the required savings for the next five years. While this is an important and necessary piece of work, it supports our view that key planning activity is still ongoing rather than the focus being on wider delivery and implementation. This work is targeted for completion in March 2019 in conjunction the approval of the next evolution of the Council's MTFP. Management is confident the underlying project management and governance arrangements will facilitate an efficient and timely transition into delivery of new projects in 2019/20.

Recommendation eight

Is there a flow from the corporate plan and improvement plans to performance reports?

In our 2016/17 Annual Audit Report, we recommended that, to drive continuous and ambitious transformation, longer term targets for key priorities should be set to assist in providing the framework to fully challenge how services are delivered, and what the key metrics and indicators are that matter to service users and communities.

The Council is continuing to review its performance indicators. Management has stated this will start through working with communities to understand the things that are important to them, and has been evidenced through the Council's revised approach to the budget consultation. Through this, and the locality planning, the Council will develop indicators that are more responsive to communities. The Council then intends to work with services to develop longer term targets taking into account the Medium Term Financial Plan and financial impact of budget reductions.

4. Other work; audit deliverables

4. Timing and deliverables

We deliver our audit in accordance with the timeline set by the Council, in accordance with guidance from Audit Scotland. Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2017/18.

JAN FEB MAR APR MAY JUN JUL AUG SEP OCT NOV DEC

Audit Activity	Deliverable	Timing
➢ Onsite fieldwork, documentation and walkthrough of key accounting processes ➢ Scoping of Best Value work for the year	Annual Audit Plan	9 April 2018
➢ Review of frauds reported to the audit committee.	Fraud Return Submission	Submitted – in line with frauds reported to audit committee
➢ Education Maintenance Allowance (EMA) grant claim testing	Certified EMA return	Issued 31 July 2018 – no matters to report
➢ Year-end substantive audit fieldwork on unaudited financial statements ➢ Conclude on results of audit procedures ➢ Issue opinion on the Council's financial statements ➢ Performance of Best Value fieldwork	Whole of Government Accounts assurance statement to NAO Certify Annual Financial Statements Issue Annual Audit Report Submit Best Value Data Return to Audit Scotland	28 September 2018 30 September 2018 1 October 2018
➢ Criminal Justice Social Work (CJSW) return testing	Certified CJSW claim	No longer required
➢ Completion of Non-domestic rates return testing	Certified Non-Domestic Rates return	On track for 6 October 2018
➢ Completion of housing benefits claim testing	Certified Housing benefit subsidy claim	On track for 30 November 2018

Appendices

In our Annual Audit Plan, we provided a summary of the responsibilities on audited bodies falling within the public sector audit framework, as set out in the Code of Audit Practice (the Code).

Responsibilities of audited bodies	
Corporate governance	Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.
Financial statements and related reports	Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for: ▸ preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. ▸ maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures. ▸ ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority. ▸ maintaining proper accounting records. ▸ preparing and publishing, along with their financial statements, an Annual Governance Statement, Management Commentary (or equivalent) and a Remuneration Report that are consistent with the disclosures made in the financial statements. Management Commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body. Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework. Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.
Standards of conduct / prevention and detection of fraud and error	Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.
Financial position	Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to: ▸ such financial monitoring and reporting arrangements as may be specified ▸ compliance with any statutory financial requirements and achievement of financial targets ▸ balances and reserves, including strategies about levels and their future use ▸ how they plan to deal with uncertainty in the medium and longer term ▸ the impact of planned future policies and foreseeable developments on their financial position.
Best Value	Local authority bodies have a statutory duty, under the Local Government (Scotland) Act 1973 and associated statutory guidance, to make arrangements to secure best value through the continuous improvement in the performance of their functions. Specified audited bodies also have to prepare and publish performance information in accordance with directions issued by the Accounts Commission.

Professional ethical standards, and the Terms of our Appointment, require us to communicate all significant facts and matters that have a bearing on EY's objectivity and independence as auditor of the Council.

What we are required to communicate

The FRC Ethical Standard requires that we provide details of all relationships between Ernst & Young (EY) and your Authority, and its directors and senior management and its affiliates, including all services provided by us and our network to your Authority, its directors and senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on the our integrity or objectivity, including those that could compromise independence and the related safeguards that are in place and why they address the threats.

There are no relationships from 1 April 2017 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.

Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan, dated 9 April 2018.

We complied with the Financial Reporting Council's Ethical Standards and the requirements of Audit Scotland's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that management and members of the Council consider the facts known collectively to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of Council on 25 September 2018.

Audit fees – payable to us in the respect of the year ended 31 March 2018

Component of fee:	**2017/18**	2016/17
Auditor remuneration – expected fee	£183,620	£181,800
Audit fee in respect of S106 Trust Funds	£550	£550
Audit Scotland fixed charges:		
Pooled costs	£16,320	£15,830
Performance audit and best value	£96,200	£98,110
Audit support costs	£11,660	£10,860
Total fee	**£308,350**	**£307,150**

B – Independence and audit quality (cont.)

Audit Quality
International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances. The EY 2017 UK Transparency Report, volumes one and two, can be accessed on our website at www.ey.com/uk/en/about-us/ey-uk-transparency-report-2017. This material is published to provide a timely and relevant source of information about EY in general, and our audit business in particular. The disclosures are extensive. For example, they explain our outlook and how we are structured and governed, including the role of our Independent Non-Executives and how we apply the requirements of the UK's Audit Firm Governance Code. We refer to the quality of our audits and our commitment to recruiting, developing and diversifying our people and talent pool. We also explain how we manage our risks and remain innovative and technologically advanced in what we do and how we do it. Maintaining high audit quality across all of our engagements is of paramount importance to us. Our transformational Audit Quality Programme continues and is a part of the global EY Sustainable Audit Quality Programme. Our Audit Quality Board (AQB) continues to oversee all matters relating to audit quality and sets the agenda for the Audit Quality programme. The AQB meets monthly and also holds an annual strategy session. The AQB reports to the EY UK Board. The AQB receives regular updates on regulatory matters, results of internal and external reviews, results of root cause analysis, resourcing, the SAQ programme and pursuit approvals, as well as a comprehensive dashboard on quality measures. Our Audit Quality Support Team (AQST), which started within the SAQ programme, reviews 40 to 50 audits each audit cycle providing challenge and guidance to the engagement teams. These are in-depth reviews carried out by experienced auditors independent of the audit team. AQST reviews enhance the quality of both the audit under review and other audits on which team members apply the lessons learned. The AQST has now become a business-as-usual function with a new leader.
Audit Scotland – Audit Quality Framework / Annual Audit Quality Report
Audit Scotland's Appointments and Assurance Team are responsible for applying the new Audit Quality Framework across all financial audits and performance and Best Value audits. This covers the quality of audit work undertaken by Audit Scotland staff and appointed firms. The team are independent of audit delivery and provide assurance on audit quality to the Auditor General and the Accounts Commission. We support Audit Scotland in their commitment to reporting on audit quality through responding to requests for information and providing the results of internal quality reviews undertaken in respect of relevant public sector audits in Scotland. The most recent audit quality report which covers our work at the Council since appointment can be found at: www.audit-scotland.gov.uk/uploads/docs/report/2018/as_audit_quality_1718.pdf.

Required communication	Our reporting to you
Terms of engagement / Our responsibilities Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties. Our responsibilities are as set out in our engagement letter.	Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice
Planning and audit approach Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Annual Audit Plan
Significant findings from the audit ▸ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▸ Significant difficulties, if any, encountered during the audit ▸ Significant matters, if any, arising from the audit that were discussed with management ▸ Written representations that we are seeking ▸ Expected modifications to the audit report ▸ Other matters if any, significant to the oversight of the financial reporting process	This Annual Audit Report We request written representation from you in respect of key matters arising during the course of our audit, and in accordance with auditing standards. A copy of this letter is provided for your consideration and signature at the time of approval of the financial statements.
Going concern Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: ▸ Whether the events or conditions constitute a material uncertainty ▸ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▸ The adequacy of related disclosures in the financial statements	No conditions or events were identified, either individually or together to raise any doubt about the Council's ability to continue for the 12 months from the date of our report.
Misstatements ▸ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation ▸ The effect of uncorrected misstatements related to prior periods ▸ A request that any uncorrected misstatement be corrected ▸ Corrected misstatements that are significant ▸ Material misstatements corrected by management	This Annual Audit Report
Fraud ▸ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity ▸ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ▸ A discussion of any other matters related to fraud	This Annual Audit Report
Consideration of laws and regulations ▸ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▸ Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	This Annual Audit Report We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations.

C - Required communications (cont.)

Required communication	Reference
Related parties Significant matters arising during the audit in connection with the entity's related parties including, when applicable: ▸ Non-disclosure by management ▸ Inappropriate authorisation and approval of transactions ▸ Disagreement over disclosures ▸ Non-compliance with laws and regulations ▸ Difficulty in identifying the party that ultimately controls the entity	No significant matters have been identified.
Independence Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: ▸ The principal threats ▸ Safeguards adopted and their effectiveness ▸ An overall assessment of threats and safeguards ▸ Information about the general policies and process within the firm to maintain objectivity and independence	Annual Audit Plan This Annual Audit Report – Appendix B
Internal controls Significant deficiencies in internal controls identified during the audit	This Annual Audit Report – no significant deficiencies reported
Group audits ▸ An overview of the type of work to be performed on the financial information of the components ▸ An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components ▸ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work ▸ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted ▸ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements	Annual Audit Plan This Annual Audit Report
Subsequent events ▸ Where appropriate, asking the audit committee whether any subsequent events have occurred that might affect the financial statements.	We have asked management and those charged with governance. We have no matters to report.
Material inconsistencies Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	This Annual Audit Report

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Council or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	**Findings and / or risk**	**Recommendation / grading**	**Management response / Implementation timeframe**
1	**Financial statement presentation – management commentary** We concluded that the content of the Management Commentary and Annual Governance Statement was consistent with the financial statements and prepared in accordance with the statutory guidance. In our view the commentary could be further enhanced to provide a greater breadth of understanding for the reader, and bring it more in line with the standard we have noted elsewhere across the sector.	As part of the year two audit debrief and year three planning arrangements, we will again discuss with management expectations and recommendations around enhancements that can be made to the Management Commentary and Annual Governance Statement. *Grade 2*	As part of the debrief of the final accounts process with the auditors we will reflect on further improvements and enhancements that can be made to the Management Commentary and Annual Governance Statement and incorporate into 2018/19 final accounts. **Responsible officer: Corporate Finance Manager** **Timeframe: 31 March 2019**
2	**Financial statement presentation – Expenditure and Funding Analysis** The draft financial statements were prepared with the EFA in advance of the primary financial statements without being listed as a primary statement. Audit Scotland guidance directs the EFA to be presented as a note to the financial statements.	Management should ensure the EFA is presented in the 2018/19 financial statements in line with available guidance, which currently recommends it is presented as a note to the financial statements. *Grade 3*	Having reviewed the Code of Practice, we have left the EFA adjacent to the CIES. We will give further consideration to its positioning in 2018/19, again with regard to the revised Code. **Responsible officer: Corporate Finance Manager** **Timeframe: 31 March 2019**

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Council or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	**Findings and / or risk**	**Recommendation / grading**	**Management response / Implementation timeframe**
3	**IAS 19 accounting for defined benefit pensions** We identified a projected audit difference in the accounting for pensions of £6.8 million, resulting from an understatement of the Council's share of the Falkirk Pension Fund's assets at 31 March.	Recognising there is a risk of these differences re-occurring next year, given the timing differences will always exist, we have agreed to discuss with management and the actuaries arrangements in advance of the financial yearend to seek to address this before the IAS 19 reports are drafted. *Grade 2*	Management notes that dialogue will be taking place between Audit firms and Actuaries to review the way in which pension fund asset valuations are determined. Management will liaise with the Falkirk Pension Fund actuary in relation to the 2018/19 IAS19 process and incorporate any recommendations emerging from the wider discussions, all with a view to minimising the risk of a material difference occurring in the future. **Responsible officer: Corporate Finance Manager** **Timeframe: 31 December 2018**
4	**Capital programme monitoring and reporting** The capital programme outturn has followed a similar pattern in recent years; brought forward spend through prior year slippage, then increasing slippage in the programme through the year resulting in significant underspends at year end. There is scope to improve the monitoring and reporting around the capital programme.	Management should ensure the capital programme is reviewed in conjunction with the related monitoring and reporting arrangements to support more accurate measurements and forecasting, which in turn facilitates delivery of the programme through identification and resolution of risks and issues. *Grade 2*	As noted in a report to the August Executive, discussions have taken place with Internal Audit and the 2018/19 Audit Plan includes a review of the General Fund Capital Programme. This work is currently underway and is focused on reviewing mechanisms for recording, reporting and monitoring expenditure relating to the General Capital Fund Programme, including arrangements for dealing with slippage. The main findings of this review will be reported to members in due course. **Responsible officer: Capital Manager** **Timeframe: 31 December 2018**

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Council or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	**Findings and / or risk**	**Recommendation / grading**	**Management response / Implementation timeframe**
5	**Governance and transparency – internal audit improvement actions** Actions are planned over improvements to be made to internal audit planning and reporting arrangements, but implementation remains outstanding at the time of reporting As part of these arrangements there is scope to ensure the Audit Committee is better sighted on the status of implementation of recommendations.	Management should ensure the Audit Committee is better sighted on the status of implementation of recommendations in respect of audit and other scrutiny activity to facilitate more effective scrutiny and challenge. *Grade 2*	The 2018/19 Internal Audit Plan agreed by Audit Committee in April 2018 linked planned assignments to the relevant corporate risks as per the Corporate Risk Register. It prioritised assignments by categorising as Annually Recurring Assignments, Committed Assignments (for first six months of the year), and Indicative Assignments (for second 6 months of the year). Internal Audit KPI's have been reviewed and proposed, revised indicators are set out in the Internal Audit Progress paper to 27 September Audit Committee. On grading of recommendations, we have canvassed the SLACIAG peer group and will consider the outputs of that exercise in devising any grading of our recommendations. In relation to Audit Committee being fully sighted on recommendations arising from audit and scrutiny activity, Internal Audit Recommendations form part (but not all) of this. We will commit to including IA Recommendation status twice yearly to Audit Committee (April and November meetings) – this will include recommendations outstanding beyond their agreed implementation date. This has been done in the past, but accept that there is a need to be timetabled regularity. **Responsible Officer – Internal Audit Manager** **Timeframe – November 2018**

D – Action plan (cont.)

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Council or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	**Findings and / or risk**	**Recommendation / grading**	**Management response / Implementation timeframe**
6	**Governance and transparency – prior year audit recommendations** Actions around previously identified areas for improvement around governance remain outstanding at the yearend.	Management should ensure the actions agreed previously around the Council's Audit Committee work plan and arrangements for Falkirk Community Stadium Limited governance are completed in a timely manner. Management should also ensure annual audit recommendations are subject to reporting to and scrutiny by the audit committee going forward. *Grade 2*	It is agreed that following approval of the Audit Committee's schedule and agenda for 2019 an underlying work plan will be prepared to supplement the core work plan that was set up with the Committee's terms of reference a number of years ago. A report on Falkirk Community Stadium's financial and governance arrangements will be provided to Members. **Responsible Officer - Chief Governance Officer/Corporate Finance Manager** **Timeframe – December 2018**
7	**Value for money - Council of the Future monitoring and reporting arrangements** In our view there are further enhancements that could be made to CoTF reporting arrangements to facilitate more effective transparency and scrutiny and to further support timely identification and action on risks around delivery of projects and the programme as a whole. We have outlined a number of possible areas for improvement below for management consideration and discussion going forward.	Management should review the reporting arrangements around Council of the Future with a view to supplementing existing reporting with the noted enhancements. *Grade 2*	A review of the Council of the Future reporting arrangement is underway. New arrangements will be reported to the Council of the Future Board and advised to the Executive. **Responsible Officer: Head of Human Resources & Business Transformation** **Timeframe: December 2018**

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Council or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		**Grade 2:** Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	**Grade 3:** Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	**Findings and / or risk**	**Recommendation / grading**	**Management response / Implementation timeframe**
8	**Financial sustainability / Value for money – Delivery of Council of the Future and MTFP** While there is alignment between the Council's financial planning arrangements and improvement plans, notably Council of the Future, the scope of savings required over the next five years continues to be significantly greater than the identified savings through CoTF over the same period. A significant amount of planning is underway to address savings requirements through to 2024. However, the implementation of these plans does not align with the pace required to address budget gaps, Our view is that the overall status of CoTF is one of being still in the early phases of implementation. Given the stage of progress of a number of these projects there is an inherently higher risk that these will not be delivered. The Council has recently been working to align future CoTF projects with the MTFP and corporate priorities, including the required savings for the next five years. This work is targeted for completion in March 2019 in conjunction the approval of the next evolution of the Council's MTFP. Management is confident the underlying project management and governance arrangements will facilitate an efficient and timely transition into delivery of new projects in 2019/20.	It is important that the planned actions outlined by management in the remainder of 2018/19 are delivered to provide a comprehensive MTFP with identified savings across its five year period to cover budget gaps. Inherently linked to this process is the confirmation of the next tranche of CoTF projects with planned outputs, including financial savings, over the term of the MTFP and objectives aligned to the Council's priorities set out in its corporate plan. *Grade 1*	Work is on-going to ensure business plans are in place across the Council, which support the finalisation of the MTFP, with the aim of completion by March 2019. The COTF programme of change will be adjusted to accommodate such developments and to ensure a refreshed programme which covers the 5 year period of the MTFP. **Responsible Officer – Head of Human Resources & Business Transformation** **Timeframe: March 2019.**

E – Summary of audit adjustments

This appendix sets out the significant adjustments processed in the financial statements prior to their finalisation. We also report on the unadjusted audit differences identified.

1. Adjustment to valuation of investment balance held for FCSL	Income and Expenditure impact / £	Balance sheet impact / £
Dr Revaluation Reserve	£1,500,000	
Cr Investments		(£1,500,000)
2. Adjustment in relation to council tax provision overstatement		
Dr Council tax debtor provision	£912,000	
Cr CIES council tax income		(£912,000)
3. Adjustment in relation to equal pay provision		
Dr CIES non-payroll expenditure	£300,000	
Cr Provisions		(£300,000)

We have outlined below all audit differences identified which remain unadjusted.

1. Project misstatement in relation to the Council's share of the Falkirk Pension Fund asset valuation understatement	Income and Expenditure impact / £	Balance sheet impact / £
Dr Net pension liability		£6,800,000
Cr Gain on pension assets	(£6,800,000)	

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