Perth & Kinross Council

2015/16 Annual audit report to Members and the Controller of Audit

September 2016

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The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies (www.audit-scotland.gov.uk/about/ac/). Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General (www.audit-scotland.gov.uk/about/).

The Accounts Commission has appointed Stephen Boyle as the engagement lead for the audit of Perth & Kinross Council for the period 2012/13 to 2015/16.

This report has been prepared for the use of Perth & Kinross Council and no responsibility to any member or officer in their individual capacity or any third party is accepted.

The information in this report may be used for the Accounts Commission's annual overview report on local authority audits published on its website and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

Contents

Key messages

Audit of financial statements	• Unqualified auditor's report on the 2015/16 Perth and Kinross Council financial statements. • Unqualified auditor's report on the Perth and Kinross Council Charitable Funds financial statements administered by the council.
Financial management and sustainability	• The council has a strong financial position with £85.8m usable reserves. Its reserves have increased by 60% over the last five years, primarily as a result of a planned approach to meeting both the anticipated future financial constraints in the public sector and for the delivery of large infrastructure projects. Unplanned underspends in service departments have also contributed to the growth in reserves. • In 2015/16 the council planned to use £13.8m of its usable reserves, but the final outturn reported sizeable underspends in the three main services along with additional income which resulted in an increase to reserves of £2.2m. Many of the underspends were anticipated early in the financial year and the council employs budget flexibility to allow for activities spanning more than one financial year. There is however, scope to increase this flexibility during the year to enable it to adjust planned expenditure for anticipated underspends. • The council has previously estimated that it needs to make £39 million of savings over the next three years and identifies the delivery of its transformation programme as being key to its future financial sustainability. The size of required savings could be higher in the event of changes in underlying assumptions.
Governance and transparency	• The council has effective overarching and supporting governance arrangements which provide an appropriate framework for organisational decision making, • It is currently reviewing its governance arrangements to ensure they remain appropriate following changes to its group structure • Systems of internal control operated effectively during the year. • The council's arrangements in relation to the prevention and detection of fraud and corruption and for investigating and reporting data matches identified by the NFI are satisfactory.

Best Value	• The council has a strong track record of partnership working • There is a strong focus on performance management and a sound framework for monitoring and reporting performance against the council's priorities. • Appropriate SPI arrangements were in place within the council for 2015/16. • The council has a robust approach to public performance reporting and the website provides links to further details on specific performance at a service-level.
Outlook	• In common with other councils, Perth & Kinross Council faces rising demand for services and continued funding pressures alongside managing major reforms in welfare and health and social care. Effective arrangements for best value will be essential for efficient use of available resources. Strong governance and leadership will be needed to achieve continuous improvement. The arrangements in place with the PKC IJB will be key to delivering the integrated health and social care agenda

Introduction

1. This report is a summary of our findings arising from the 2015/16 audit of Perth and Kinross Council (the council). The report is divided into sections which reflect our public sector audit model.

2. The management of the council is responsible for:
   - preparing financial statements which give a true and fair view
   - implementing appropriate internal control systems
   - putting in place proper arrangements for the conduct of its affairs
   - ensuring that the financial position is soundly based.

3. Our responsibility, as the external auditor of the council, is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.

4. An audit of financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements; this does not relieve management of their responsibility for the preparation of financial statements which give a true and fair view.

5. A number of reports, both local and national, have been issued by Audit Scotland during the course of the year. These reports, summarised at appendix II and appendix III, include recommendations for improvements.

6. Appendix IV is an action plan setting out our recommendations to address the high level risks we have identified during the course of the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "Management action/response". We recognise that not all risks can be eliminated or even minimised. What is important is that the council understands its risks and has arrangements in place to manage these risks. The council and management should ensure that they are satisfied with proposed action and have a mechanism in place to assess progress and monitor outcomes.

7. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures; consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

8. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

9. This is the final year of the current five year audit appointment. From 2016/17 the auditor of the council will be KPMG. In accordance with agreed protocols and International Standards on Auditing we will be liaising with the incoming auditors as part of this transition.

10. A new Code of Audit Practice was published in May 2016 and will apply to all audits from financial year 2016/17. This will focus the audit on four key areas:

- Financial sustainability
- Financial management
- Governance and transparency; and
- Value for money

11. In addition from 2016/17, as well as the annual audit report, other significant outputs, such as the annual audit plan, will be published on Audit Scotland's website.

Audit of the 2015/16 financial statements

Audit opinion	• We have completed our audit and issued an unqualified independent auditor's report on the council's accounts.
Going concern	• The financial statements of the council, its group and the associated charitable trusts have been prepared on the going concern basis. We are unaware of any events or conditions that may cast significant doubt on the council, its group and associated charitable trusts ability to continue as a going concern.
Other information	• We review and report on other information published with the financial statements, including the management commentary, annual governance statement and the remuneration report. A new approach to compiling the AGS was introduced for the 2015/16 financial statements however this has still to be fully embedded. We have nothing further to report in respect of these statements.
Charitable trusts	• We have completed our audit of the 2015/16 financial statements of the charitable funds administered by Perth & Kinross Council and issued an unqualified independent auditor's report.
Group accounts	• Perth & Kinross Council has accounted for the financial results of two subsidiaries, two associates, the common good funds and sundry trusts in its group accounts for 2015/16. The overall effect of consolidating these balances on the group balance sheet is to increase total reserves and net assets by £13.034 million.
Whole of government accounts	• The council submitted a consolidation pack for audit and the certified return was submitted to the National Audit Office by the 30 September deadline.

Submission of financial statements for audit

12. We received the unaudited financial statements on 23 June 2016, in accordance with the agreed timetable. The working papers were of a good standard and council staff provided good support to the audit team which assisted the delivery of the audit to deadline.

13. In 2015/16, for the first time, local government group accounts are required to include the financial results of Integration Joint Boards (IJBs) in their area, where material. The Perth & Kinross IJB was established on 3 October 2015 but was not operational until 1 April 2016 (see paragraphs 121-128). Consequently, as the amounts concerned in 2015/16 are not material, they have not been consolidated into the group accounts.

Overview of the scope of the audit of the financial statements

14. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual Audit Plan presented to the Audit Committee in March 2016.

15. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2015/16 agreed fee for the audit was set out in the Annual Audit Plan. We undertook additional audit work relating to the Bellwin Grant which resulted in an additional fee of £2,500. Our overall fee for the year was therefore £283,500.

16. The concept of audit risk is of central importance to our audit approach. During the planning stage of our audit we identified a number of key audit risks which involved the highest level of judgement and impact on the financial statements and consequently had the greatest effect on the audit strategy, resources and effort. We set out in our Annual Audit Plan the audit work we proposed to undertake to secure appropriate levels of assurance. Appendix I sets out the significant audit risks identified during the course of the audit and how we addressed each risk in arriving at our opinion on the financial statements.

17. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

Materiality

18. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other reasons (for example, an item contrary to law).

19. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial

statements, we assess the materiality of uncorrected misstatements, both individually and collectively.

20. We summarised our approach to materiality in our Annual Audit Plan. Based on our knowledge and understanding of the council we set our planning materiality for 2015/16 at £4.1 million (1% of gross expenditure). We report all misstatements greater than £0.1 million. Performance materiality was calculated at £2 million, to reduce to an acceptable level the probability of uncorrected and undetected audit differences exceeding our planning materiality level.

21. For the audit of the council's charitable trusts materiality has been set at £657 (1% of gross expenditure). Due to the size and nature of the investments held by the charitable trusts a separate materiality is appropriate for this area and has been set at £20,800 (1% of gross assets).

22. On receipt of the financial statements and following completion of audit testing we reviewed our materiality levels and concluded that our original calculation remained appropriate.

Evaluation of misstatements

23. All misstatements identified during the audit, which exceeded our misstatement threshold, have been amended in the financial statements.

24. A number of presentational and monetary adjustments were identified within the financial statements during the course of our audit. These were discussed with relevant officers who agreed to amend the unaudited financial statements. The effect of these adjustments none of which had an impact on the overall position, is to:

- increase both income and expenditure on the group comprehensive income and expenditure statement (CIES) by £1.3 million with £0.9 million of this also being reflected in the council CIES
- reclassify grant income of £0.4 million from services to taxation and non specific grant income
- reduce debtors by £0.23 million, decrease provisions by £0.56 million and increase creditors by £0.33 million on the council balance sheet
- reduce dwelling rent and increase other income on the Housing Revenue Account by £0.7 million.
- increase by £3 million the gross rate levied and reliefs for 2015/16 on the Non Domestic Rate Income Account (NDRI)
- reduce the previous years gross rates and reliefs by £0.1 million on the NDRI
- reduce prior year impairment of bad debt on the NDRI by £0.4 million and increase the contribution to the National Non-Domestic Poll by the same amount.

Significant findings from the audit

25. International Standard on Auditing 260 requires us to communicate to you significant findings from the audit, including:

- the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures
- significant difficulties encountered during the audit
- significant matters arising from the audit that were discussed, or subject to correspondence with management
- written representations requested by the auditor
- other matters which in the auditor's professional judgment, are significant to the oversight of the financial reporting process

26. The following table details those issues or audit judgements that, in our view, require to be communicated to those charged with governance in accordance with ISA 260.

Table 1: Significant findings from the audit

Significant findings from the audit in accordance with ISA260
Perth & Kinross Council
Annual governance statement (AGS): A new approach to compiling the AGS was introduced for the 2015/16 financial statements. It was however difficult to evaluate how effective the new approach was as there was not a full audit trail to evidence the process applied. For example it was not clear: • who completed returns/assurance statements as these were not always signed • what challenge process was undertaken by the Policy & Governance Group and service management teams • how the improvements areas fed in to the AGS. During our audit work we were subsequently provided with signed returns/assurance statements (although these were not dated), the minutes of the Policy and Governance meeting of 30 May 2016were expanded to better reflect the process and updates were made to the unaudited AGS to highlight improvement areas. Whilst the revised process introduced this year takes a more robust approach to compiling the AGS it is important that this is completed and evidenced prior to the statement being approved by Scrutiny Committee to ensure the statement fully reflects all strands of the governance process. ***Appendix IV – Action plan no. 1***

Significant findings from the audit in accordance with ISA260
Tayside Contracts – Minute of Agreement: In 2011/12 it was agreed that the Minute of Agreement would be reviewed by March 2013 to ensure it reflected the actual operation and governance of Tayside Contracts. Legal representatives from the three councils have met at various points over the years however, a revised Minute of Agreement has yet to be agreed. The council had anticipated a signed agreement in 2015/16 however this target was not achieved as all three constituent councils had been unable to reach a consensus. The council is hopeful of a conclusion being reached in a matter of weeks.
Perth & Kinross Charitable Funds
Charitable Trusts Governance documentation: As reported in 2014/15 governance documentation for several trusts could not be located as a consequence of the age of the trust, in some cases dating back over 100 years. As a result, classification of these funds between restricted, unrestricted and endowment funds can not readily be established and is it not possible to verify whether spend in these areas was in line with the original stated purpose for these individual trusts. Disclosures in the charities accounts identified the trusts for which governance documentation is not held and on what basis the trustees account for and use these funds. All funds are treated as endowments and where there is an absence of governance documentation the council rely on custom and practice to inform any decisions by the trustees in respect of the trusts expenditure and use of assets. The process of amalgamating smaller charities with a view to streamlining the administrative requirements and establishing clearer governance arrangements is continuing. We are not aware of any matters which would materially impact the financial statements.

Future accounting developments

Group Accounts

27. From 1 April 2016 IJBs are accountable for the provision of health and social care. IJBs will be required to produce financial statements in compliance with the Code of Practice on Local Authority Accounting in the United Kingdom. Where material the financial results of the local IJBs will need to be reflected in the council's group accounts in 2016/17. The council will need to include the IJB in its plans for the preparation and audit of the 2016/17 group accounts, including consideration of assurance arrangements relating to the annual governance statement.

28. A new cultural trust (Culture Perth & Kinross) was established in April 2016 with responsibility for delivery and development of museums and galleries, libraries, archives, arts development and some creative learning services. The total value of services being delivered by arms-length organisations following the establishment of this new trust will almost double to approximately £10 million in 2016/17.

29. The inclusion of the cultural trust and the IJB will increase the complexity of the council's group accounts

Highways network assets

30. The 2016/17 local government accounting Code will adopt a new measurement requirement for the valuation of the highways network assets. The highway network assets will be measured on a depreciated replacement cost basis. This will have a significant impact on the value of local authority balance sheets. The council is actively working on this and has identified the increase in its assets will be around £2.5 *billion.*

Financial management and sustainability

Net service budget expenditure £335.9m

Service Outturn £322m

Service Budget Underspend £13.9m

Original planned capital expenditure £78.9m

Outturn Capital spend £66.4m

Underspend against capital budget £12.5m

Planned use of reserves £13.8m

Actual increase in usable reserves £5.9m

Outturn usable reserves £85.8m

Financial management

31. In this section we comment on the council's financial outcomes and assess the council's financial management arrangements.

Financial outcomes

32. In cash terms, funding through taxation and grant income has increased in 2015/16 by 6.5% (£21.7 million) to £357.7 million. Of this increase £16 million related to capital grants and contributions. The council's financial statements reported £321.9 million expenditure on the cost of services with an overall surplus of £12.7 million after funding and financing activity are deducted.

33. The council sets an annual budget to meet its service and other commitments for the forthcoming financial year. The 2015/16 budget was agreed at the council meeting on 12 February 2015. The setting of the annual budget impacts directly on residents as it determines council tax and other fees and charges. Regular monitoring of expenditure and income against agreed budgets is central to effective financial management. These reports are prepared on a different basis to the accounting policies used in the financial statements.

34. The council had planned to use £13.8 million of its reserves during 2015/16, but the final position was an increase to reserves of £2.2 million. This resulted in an underspend against budget of £16 million which represents 3.9% of budgeted net expenditure. This was largely due to underspends across a number of its service departments as outlined below. Underspends were generally achieved on employee costs, property costs and supplies and services and extra income was also received in the year. Key variations in performance against budget are detailed in the management commentary within the financial statements and include:

- Education and Children's Services underspent by £5.5 million (£1.3 million from devolved school management).
- Housing and Community Care underspent by £3.3 million.
- The Environment Service underspent by £4.4 million.
- additional council tax income of £2.5 million through both an increase in the number of new properties across the council and improvements in the collection rates achieved
- other budgets delivered savings of £0.3 million primarily as a result of a higher than expected share of Tayside Contract's surplus for the year

35. The council is required by legislation to maintain a separate housing revenue account (HRA) and to ensure that rents are set to at least cover the costs of its social housing provision. Rent levels are therefore a direct consequence of the budget set for the year. The Housing and Health Committee set a break even budget for 2015/16 in January 2015.

36. The annual accounts reported an overall HRA deficit of £2.35 million. Adjusting this deficit to remove the accounting entries required by the Code, the HRA balance decreased by £0.678 million before transfers from reserves. The council has previously agreed to reduce the level of council tax discounts on second homes and long term unoccupied dwellings to create funding to support the development of affordable housing. Approval to use £0.82 million of the affordable housing earmarked reserve within the general fund was agreed in September 2015 with only £0.66m used in the year. The closing earmarked HRA balance within the general fund was £0.782 million (prior year £0.8 million) which is broadly in line with the level the council aims to maintain of £0.8 million.

Financial management arrangements

37. As auditors, we need to consider whether councils have established adequate financial management arrangements. We do this by considering a number of factors, including whether:

- the proper officer has sufficient status within the council to be able to deliver good financial management
- financial regulations are comprehensive, current and promoted within the council
- reports monitoring performance against budgets are accurate and provided regularly to budget holders
- monitoring reports do not just contain financial data but are linked to information about performance
- members provide a good level of challenge and question budget holders on significant variances.

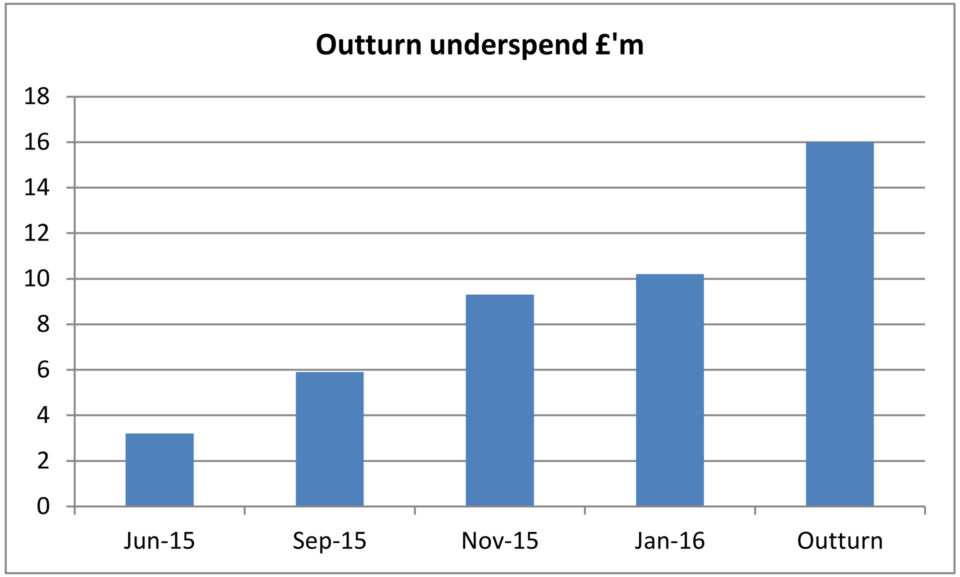
38. We assessed the role and status of the proper officer against CIPFA's "Statement on the role of the Chief Financial Officer in Local Government" and concluded that the council complies with the statement's five principles.

39. We reviewed the council's financial regulations, which are revised biennially, and concluded that they are comprehensive and current. The financial regulations are available on the council's intranet site. The scheme of administration was updated in October 2015, however this does not contain reference to the Public Bodies (Joint Working) (Scotland) Act. We have been advised by officers that a further update to the scheme of administration which is to be taken to the December 2016 council meeting will include reference to this Act.

40. Financial monitoring reports (revenue and capital) are submitted to both the executive officers team (EOT) and the Strategic Policy & Resources Committee every second month from September to April. Revenue reports are comprehensive but are wholly focussed on the forecasting outturn and do not show the actual spend to date against budget. The reports provide explanations for how the budget variances (both over- and underspends) occurred but currently only formally consider how any net underspends will be utilised in February in conjunction with the budget setting process and reserves strategy. Proposals to manage resources between financial years are considered under the council's approved revenue budget flexibility scheme in February each year. From 2016/17 each monitoring report will include reference to the council's approach to managing any net underspends achieved.

41. The size of the projected underspends (which also include additional income) reported to members for 2015/16 are summarised in Exhibit 1. The outturn position of £16 million includes year end factors which are not included in the in-year monitoring reports. For 2015/16 these were a post year end review of council tax provision (£1.3 million), increased share of surplus from Tayside Contracts (£0.4 million), movements on earmarked reserves (£1.7 million) and additional government grants received late in the year (£0.5 million).

Exhibit 1: Revenue monitoring 2015/16 – underspends (£million)



Source: Perth & Kinross Council's committee papers

42. The council has consistently underspent against its approved budget for a number of years as shown in Exhibit 2. Given this trend, there is scope to better align agreed budgets by challenging services on the timing of savings. The revenue monitoring report presented to the Strategic Policy and Resources Committee on 21 September 2016 is projecting an underspend of £0.94 million in 2016/17.

Exhibit 2: Underspends against budgeted expenditure 2012-2016

	2012	2013	2014	2015	2016
Budget £m	408.3	379.1	388.2	393.6	409.5
Underspend £m	7.4	10.2	11.1	12.9	16.0
%age underspend	1.7%	2.7%	2.9%	3.3%	3.9%

Source: Perth & Kinross Council financial statements and revenue budgets

43. In previous years it was highlighted that the business improvement team was working towards integrating service performance reporting and budget monitoring. This has yet to be implemented. This integration of reporting would allow members to more readily evaluate whether the underspend were having a detrimental impact on service delivery on a timeous basis.

Appendix IV – Action plan no. 2

44. The Audit Scotland report *Financial Reporting and Scrutiny: Why the Accounts Matter* was considered by the Audit Committee in March 2016 and members agreed to use the appendix to this report in scrutinising the annual accounts. As part of this decision members requested training on the financial statements which was delivered by CIPFA on 27th June 2016.

Conclusion on financial management

45. We have concluded that there is scope for the council to review aspects of its financial management arrangements. Services are routinely under spending against approved budgets which has contributed to unplanned increases in the size of the council's reserves (refer paragraph 50 below). There is scope to refine the in year financial management arrangements to consider the impact of underspends on service performance.

Financial sustainability

46. The council delivers a broad range of services, both statutory and discretionary, to its communities. Financial sustainability means that the council has the capacity to meet the current and future needs of its communities.

47. In assessing financial sustainability we are concerned with whether:

- there is an adequate level of reserves
- spending is being balanced with income in the short term
- long term financial pressures are understood and planned for
- investment in services and assets is effective.

48. Effective long-term financial planning, asset management and workforce planning are crucial to sustainability.

Reserves

49. The council approves the strategy for managing reserves annually in February. The reserves position at 31 March 2016 is in line with that strategy.

50. The council budgeted to use £13.8 million of useable reserves during 2015/16, however the final position was an increase to the general fund of £2.2 million.

51. There has been a significant strengthening of the council's financial position over the past four years, achieved during a sustained downturn in public sector funding. Overall the level of usable reserves held by the council has continued to increase with a rise of £5.9 million in 2015/16. As demonstrated in Exhibit 3, usable reserves have increased by £32.4 million (60.7%) since 2011/12. The main increases related to the general fund (£18.2 million) and the capital fund (£13.5 million).

52. As part of its approach to managing the impact of the reduction in public finances, £16 million of the general fund is held as an earmarked reserve for the transformation programme (including workforce management) (see paragraph 59).

53. The majority of the balance of £23.9 million in the capital fund as at March 2016 (£21 million) relates to revenue contributions and savings on loans charges applied to the fund in accordance with the council's approved policy to secure funding for the capital programmes in the medium to long term. This balance will be utilised in future years (see paragraph 72).

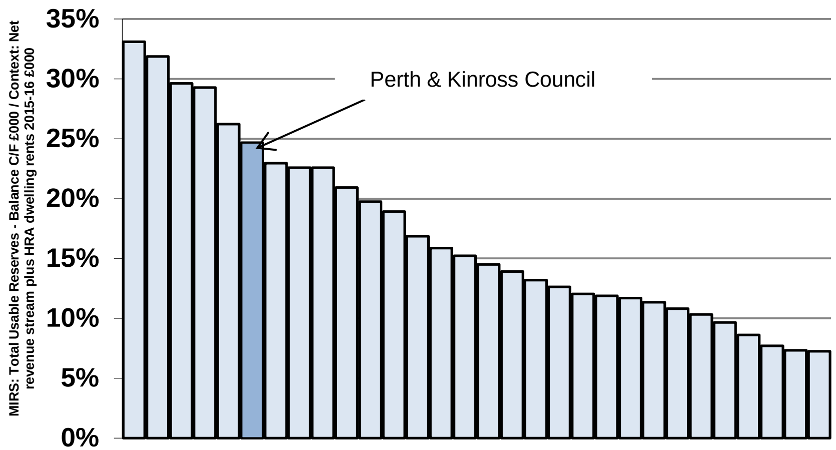
Exhibit 3: Usable reserves

Description	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m
General fund	36.7	41.7	48.0	52.7	54.9
Housing revenue	0.8	0.8	0.9	0.8	0.8
Capital fund	10.4	12.8	15.8	19.3	23.9
Capital grants unapplied	1.0	0.7	0.1	0.1	0.1
Capital receipt reserve	2.9	2.1	1.8	1.8	1.8
Repair & renewal fund	0.5	0.5	0.5	1.4	1.2
Insurance fund	1.1	2.0	3.4	3.8	3.1
Total Usable Reserves	**53.4**	**60.6**	**70.5**	**79.9**	**85.8**

Source: Perth & Kinross Council financial statements

54. Exhibit 4 below presents the council's usable reserves position in relation to net revenue stream for 2015/16 in comparison to other Scottish councils, excluding Orkney and Shetland (net revenue stream being presented as general revenue grant, council tax, non domestic rates and dwelling rents). The Scottish average usable reserves as a proportion of net revenue% (excluding Orkney and Shetland) is 16.8%. Perth and Kinross Council has the sixth highest percentage across Scotland at 24.7%.

Exhibit 4: Usable Reserves as a proportion of net revenue



Source: Scottish councils' unaudited accounts 2015/16 (excluding Orkney/Shetland)

55. By definition the useable reserves detailed at Exhibit 3, with the exception of part of the general fund, are earmarked for specific purposes. The principal purposes of holding a general fund reserve are to provide a contingency fund to meet unexpected events; as a working balance to help cushion the impact of uneven cash flows and a means of building up funds, referred to as earmarked portion of the general fund.

56. The council's planned commitments from the general fund balance amounts to £41.4 million covering 33 separate areas including the transformation programme (including workforce management), revenue budget flexibility, affordable housing strategy and devolved school management budgets.

57. The council agreed as part of its reserves strategy in February 2016 that any amount of uncommitted reserves in excess of 4% of the net revenue budget is earmarked for future costs in relation to its transformation programme. The earmarked portion for the transformation programme increased by £3.1 million to £16 million (2014/15 increased by £4.1 million to £12.9 million). This represents the main reason for the continuing increase in earmarked reserves during 2015/16. The council plans to use its reserves to transform its services and invest in large infrastructure projects in future years, while sustaining its financial sustainability.

Financial planning

58. The Scottish Government notified councils of the provisional financial settlement for 2016/17 in December 2015 with an update given on the figures in January 2016. The council agreed the 2016/17 budget of £323.1 million and provisional budgets for the following two years in February 2016. The settlement represented a significant decrease in the funding expected and the council has agreed savings of approximately £39 million and council tax income assumptions of £6 million over the next three years to support its financial position (£22 million and £1 million respectively in 2016/17). Anticipated reductions in the local government settlement are captured as scenarios in the council's medium term financial plan. Updated figures are to be reported to council in October 2016 and are expected to increase the savings required following a review of the underlying assumptions. The council's transformation programme will be key to achieving the required savings.

Transformation programme

59. The *Building Ambition: The Council's Transformation Strategy 2015-2020* was approved in July 2015. This strategy now identifies forty one wide ranging review areas which the council will consider in terms of its seven transformation themes:

- **Efficiency** – embedding efficiency and productivity into the fabric of the organisation to make the best use of human, financial and other resources
- **Redesign** – generating innovative ideas to transform services, to deliver different ways of working, and to keep the council at the forefront of modern councils
- **Targeted savings/Increased income** – making the best use of financial resources, to prioritise services to areas of greatest need, avoid additional future costs and proactively pursue commercial opportunities as a means of generating income, to offset the need to make savings
- **Partnerships** – participating in effective place-based partnership and integrated service provision between public services, to deliver services which best meet customer needs

- **Tackling Inequality** – pursuing preventative approaches to tackle disadvantage, prejudice and discrimination.
- **Community co-production** - engaging with the energy, wisdom, experience, knowledge, skills and other assets of communities. Recognising the vital role that people have in shaping and improving their own areas – making a difference to the places that they know best
- **Technology** – maximise the opportunities for transforming customer services, and improving efficiency through technological advancements

60. Progress on the transformation projects is regularly monitored by members and officers. The latest update to the Strategic Policy & Resources Committee in June 2016 highlighted that projects were mostly on target with slippage in only a few areas.

61. The transformation programme is underpinned by a medium term financial plan, the latest update to which was approved by the council in July 2015. The plan sets out the likely savings targets over 5 years to 2020/21 using three scenarios low, mid-range and high level changes in the assumptions used (e.g. pay award, demographics, government settlements, council tax increases, fees and charges). It is subject to on-going review and amendments were approved by the Strategic Policy and Resources Committee in September 2015. It was also considered by members as part of the 2016/17 revenue budget setting process in December 2015 and February 2016 and a further update is expected to be considered at the October 2016 council meeting.

62. Whilst many of the more readily achievable savings have already been made, services are required to continue to identify recurring savings going forward through the transformation programme and the budget process.

Capital programme 2015/16

63. The council in February 2015 approved its 2015/16 general services and housing capital programmes for £64.4 million and £21.1 million respectively (refer Exhibit 5). Actual capital expenditure was £44.8 million and £21.6 million respectively. This represents an underspend of 30.4% on the general services programme although the council has been able to fully deliver on its housing capital programme this year.

64. The capital programme's main expenditure in the year is detailed in the management commentary in the council's financial statements and is outlined in Exhibit 5 below. The other capital programmes included environmental improvements, community care projects, property upgrades and efficiency schemes as well as flood mitigation schemes.

Exhibit 5: Capital programme expenditure 2015/16 (£'m)

Expenditure area	Budget	Actual
School upgrades	16.8	9.9
Roads & transport projects	10.1	11.4
Other capital programmes (e.g. flood mitigation)	37.5	23.5
Affordable housing	8.2	6.1
Housing heating, rewiring and energy efficiency	5.5	3.8
Housing external works including double glazing	3.8	2.6
Other housing improvements	3.6	9.1
Total	**85.5**	**66.4**

Source: Perth & Kinross Council audited financial statements

65. In previous years we have reported on significant underspends against the council's total capital programme as highlighted in Exhibit 6. Capital expenditure has consistently been below budget with the exception of 2014/15. Actions were undertaken by the council to improve delivery of the capital programmes against budget however this trend of underspend has continued in 2015/16.

Appendix IV – Action plan no. 2

Exhibit 6: Total capital spend against original budget

Description	2012	2013	2014	2015	2016
Original budget	53.4	65.4	71.5	71.3	85.5
Under-(over-) spend £'m	13.0	23.2	13.5	(1.7)	19.1
Under-(over) spend %age	24.3%	35.5%	18.9%	(2.4%)	22.3%

Source: Perth & Kinross Council committee papers

66. Capital expenditure in 2015/16 was £66.4 million with the sources of funding, other than borrowing, totalling £63.5 million resulting in an increase of £2.9 million in the council's capital financing requirement (CFR). The CFR represents the council's need to borrow to finance capital expenditure.

67. The Prudential Code is a professional code of practice designed to support local authorities in taking capital investment decisions. The Code's objectives aim to ensure that, within a clear framework, the capital investment plans of local authorities are prudent and sustainable. The Head of Finance reviews the capital financing requirement on an annual basis and reports to the council on a series of prudential indicators as recommended by the Prudential Code. Performance against these indicators is reported to council regularly and this helps the council to plan its capital investment.

Treasury Management

68. High levels of debt may reduce a council's budget flexibility going forward as revenue resource has to be set aside to service that debt. The impact that debt levels have on net revenue expenditure will be affected by interest rates and repayment periods.

69. The council's capital financing requirement (CFR) at 31 March 2016 was £411.1 million (March 2015 £408.2 million) while the gross external debt was £37.7 million lower at £373.4 million (2014/15: £375.1 million).

70. The treasury management strategy agreed in February 2015 anticipated the need for further long term borrowing of £108 million over the six years to 2020/21 with £7 million expected in 2015/16. During the year the council borrowed £20 million but also repaid £19.7 million of its debt.

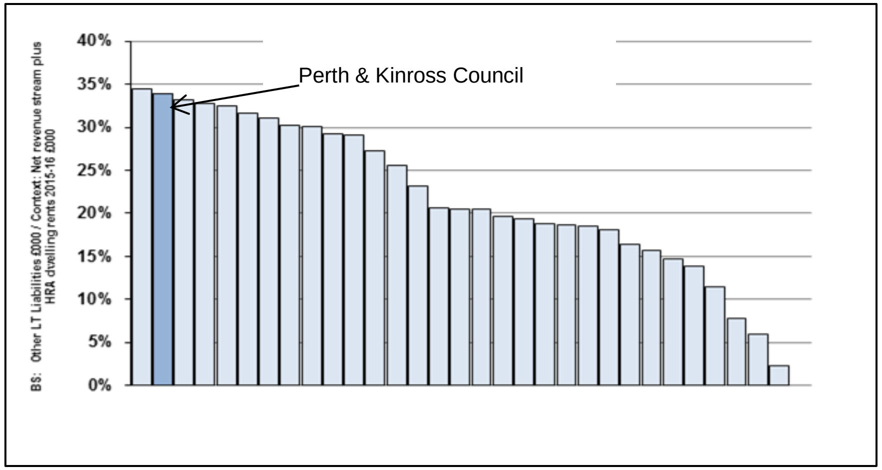
71. The council's net external debt of £316.2 million as at 31 March 2016 comprises three main areas:

- borrowing of £251.7 million (2014/15: £249.7 million), 80% of which is at fixed rate and is a repayable over the long term
- Public Finance Initiative (PFI) liability of £121.7 million (2014/15: £125.4 million) continues to paid over the life time of the agreements
- deposits and investments held of £57.2 million (2014/15: £56.7 million) represent 17.9% of the council's net revenue stream

72. The council's capital budget in February 2015 recognised the increasing pressure on its external debt over the longer term and approved setting aside a further £1 million per annum to the capital fund. The council's current projections estimate that the capital fund will be fully utilised by 2024/25 and it is working towards a solution to the projected deficit on servicing the debt in the following years.

73. Whilst the council's net external debt as a proportion of net revenue spend is comparable with other Scottish councils it has a high exposure to other long term liabilities as a proportion of total debt as shown in Exhibit 7. This represents the council's three PFI projects (a schools project to deliver six school campuses, an office accommodation project and a car park project). Accounting requirements mean that the council must recognise both the asset acquired under the PFI scheme and the related liability in its balance sheet.

Exhibit 7: Other long term liabilities as a proportion of total debt



Source: Scottish councils' unaudited accounts 2015/16 (excluding Orkney/Shetland)

74. Exposure to PFI debt is of interest as many local authorities have also incurred high contingent rental increases in recent years making servicing this debt more expensive.

75. The council's contingent rental to service the PFI debt as at 31 March 2016 is projected to be £112.4 million over the remainder of the contracts (2014/15: £117.8 million). PFI obligations of this degree reduce the council's flexibility in dealing with future funding challenges that are likely to present themselves across the public sector.

Asset Management

76. The council's transformation programme identifies several areas for review covering asset management. The council is currently reviewing its corporate property assets and its schools estate to:

- provide a property estate which is fit for purpose, integrated with partner organisations' asset management plans, maximising collaborative opportunities, and is in appropriate geographical locations. A project board has been established and meetings with other public sector organisations have discussed property collaboration opportunities.
- make the most effective and efficient use of buildings, and staff across the schools estate. The scope and criteria of this project is to be established in August 2016 with option appraisal on the estate thereafter.

77. An outline business case is being developed for the council vehicle fleet utilisation and optimisation review scheduled to commence in 2016/17.

Workforce Management

78. Effective workforce management is essential to ensure that the council maximises the effectiveness of its employees. Refer paragraphs 149 – 155 below for details of a local follow-up audit undertaken this year.

Pension liability

79. The council is a member of the Tayside Pension Fund which is a multi employer defined benefit scheme. In accordance with pension accounting standard IAS19 'Retirement Benefits' the council has recognised its share of the net liabilities for the pension fund in the balance sheet. The pension liability represents the difference between expected future pension payments and the underlying value of pension fund assets available to meet this cost.

80. The valuation as at 31 March 2016 provided by the scheme's actuaries decreased the council's share of the deficit from £178 million last year to £161.8 million this year.

81. A small change to the actuarial assumptions applied can have a significant impact on the liability. The scale of the movements in the council's pension liability over the last 5 years, arising from the annual valuation, can be seen in Exhibit 8 below.

Exhibit 8: Movement in Net Pension liability 2011 to 2016

	2011/12	2012/13	2013/14	2014/15	2015/16
Assets	418.8	492.5	531.6	593.8	588.7
Liabilities	(618.5)	(681.6)	(797.6)	(771.8)	(750.5)
Net	**(199.7)**	**(189.1)**	**(266.0)**	**(178.0)**	**(161.8)**

Source: Perth & Kinross Council audited financial statements

82. Officers have confirmed that the assumptions used by the actuary were reasonable and have explained in Note 4 to the financial statement the impact of small changes in these assumptions. We have examined the assumption used in 2015/16 and these are all within expected parameters. We are satisfied, therefore, that the pension liability as at 31 March 2016 is reasonable.

83. The Tayside Pension Fund was 99.8% funded and had assets of £2,396 million at the 2014 triennial valuation. The next valuation will take place in 2017. The last triennial valuation reduced the actual rate of contributions payable by the council for the period April 2015 to March 2018 to 17.0% of pensionable payroll.

Conclusion on financial sustainability

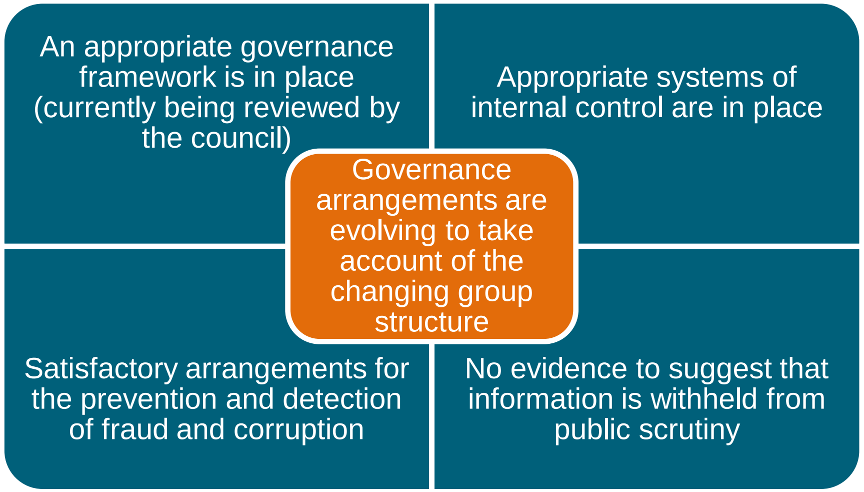
84. We have concluded that the council has considerable reserves to support its service priorities, but it is consistently underspending its annual budgets. Medium term financial plans are in place to support the council's financial sustainability. Overall we conclude that the financial position is sustainable currently and in the foreseeable future, however the council need to ensure that if the ongoing underspends in revenue and capital continue that they are not reducing the quality and range of its services.

Outlook

85. Councils face increasingly difficult financial challenges. Public sector budgets are reducing and demand for council services is increasing. With further funding reductions expected, councils face tough decisions to balance their budgets. These decisions must be based on a clear understanding of the current financial position and the longer-term implications of decisions on services and finances.

86. In common with many other councils, Perth & Kinross Council is now reporting gaps between income and the cost of providing services over the next few years and a significant savings programme has been developed to mitigate this risk.

Governance and transparency



88. Members and management of the council are responsible for establishing arrangements to ensure that its business is conducted in accordance with the law and proper standards, that public money is safeguarded and for monitoring the adequacy and effectiveness of these arrangements.

Corporate governance

89. The current governance framework is centred around Perth & Kinross Council which is supported by a number of standing committees including:

- Strategic Policy and Resources Committee which determines the strategic policy of the council and monitors the financial position
- Scrutiny Committee responsible for monitoring overall performance at a council and service level and considering national reports from scrutiny bodies
- Audit Committee responsible for ensuring action is taken to improve controls and address concerns raised by both internal and external auditors

90. There are also a number of theme related committees in place including, Lifelong Learning Committee, Housing & Health Committee, Enterprise & Infrastructure Committee and Environment Committee. The committee structure reflects the themes of the Perth & Kinross Community Plan and the council's Corporate Plan.

91. This structure allows members to scrutinise performance and hold officers to account. In previous years we have commented that committee structure can result in duplication of effort and inefficient use of member and officer time as the same reports are considered by several committees. The council agreed that a review of the entire decision-making structure will be undertaken in preparation for the local government elections in May 2017.

92. The Head of Legal and Governance is currently undertaking a review of the governance framework. This is expected to address changes required as a result of integration of health and social care services (e.g. updates to the Scheme of Administration to reflect the

Public Bodies (Joint Working) (Scotland) Act 2014) – refer paragraph 39.

93. The council's standing orders took effect from January 2013. The Scheme of Administration which sets out the membership, powers and responsibilities of the council's committees, sub-committees and working groups and lists the areas where the council has delegated decision-making to officers was updated in October 2015. The council also reviews its financial regulations every two years. The last review was in October 2014.

94. The standing orders, scheme of administration and financial regulations taken together address principal risk areas and are in line with our expectations.

95. A review of the senior management structure was approved in June 2015 with a view to increasing capacity, introducing more flexible arrangements and moving toward new models of management and delivery over the next two years. Implementation of the new structures began in October 2015.

96. We concluded that the council has effective overarching and supporting governance arrangements which provide an appropriate framework for organisational decision making.

Risk management

97. An internal audit report of the council's risk management processes in March 2016 highlighted several improvement areas. Officers are currently reviewing risk management arrangements and have agreed to implement these improvements to further embed risk management within its business planning process. This includes redefining the council's risk appetite, revising the risk management strategy and outlining clearer responsibilities for reporting and monitoring risks. The council expect to have a more robust approach to risk management once these changes are implemented.

Local code of corporate governance

98. The council developed and adopted a local code of corporate governance in 2012 which reflects the key components as set out in the CIPFA/SOLACE Framework Corporate Governance in Local Government: A Keystone for Community Governance. The local code has not been subject to review since its introduction and this is to be addressed through the next phase of the on-going review of the governance framework. It is anticipated a revised code will be in place by following the local government elections in May 2017.

Internal control

99. As part of our audit we reviewed the high level controls in a number of systems fundamental to the preparation of the financial statements. Our objective was to obtain evidence to support our opinion on the council's financial statements.

100. We reported our findings to the Audit Committee in June 2016. No material weaknesses in the accounting and internal control systems were identified which could adversely affect the ability to record,

process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements. Our findings included a number of recommendations to further enhance the control system in operation.

Internal audit

101. Internal audit provides members and management of the council with independent assurance on risk management, internal control and corporate governance processes. To avoid duplication, we place reliance on internal audit work where possible. We are required by international auditing standards to make an assessment of internal audit to determine the extent to which we can place reliance on its work.

102. As part of our 2015/16 audit we undertook a review of internal audit and concluded that it generally operates in accordance with the Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place. An external quality assessment is planned for 2016/17. We placed formal reliance on the work of internal audit on payroll this year.

ICT audit

103. Scottish public bodies continue to be the target of cyber attacks and related activities. The council has previously experienced degradation in its internet connection as an indirect consequence of a targeted hacking attack elsewhere and has been subjected to increasingly sophisticated threats. We reviewed the council's preparedness to deal with cyber attacks and found that it is well aware of the cyber risks it is subjected to. The challenges faced with regard to information security have been identified and will be reported upon annually. However, growing challenges around cyber security are putting increasing pressure on both information security and ICT resources to deliver technical measures and increase awareness among staff.

104. At the time of our review, the council had not experienced any cyber-attacks which led to system outages, such as a ransomware attack or a distributed denial of service (DDOS) attack. On a daily basis, however, any number of electronic threats are fielded, from virus and spam emails to malicious connection attempts.

105. The council's awareness of the cyber attacks and the actions taken to address the risks identified should help it to minimise the impact. Our report to the June Audit Committee highlighted further actions that could be taken to strengthen the council's existing controls including preparing an action plan to prioritise and deal with the challenges identified, testing incident management plans, ensuring appropriate staff training is completed and appropriate edge security is in place.

Arrangements for maintaining standards of conduct and the prevention and detection of fraud and corruption

106. The Strategic Policy & Resources Committee approved a Counter Fraud and Corruption Strategy in February 2015. This update

addressed the requirements of both the 2010 Bribery Act and the CIPFA Code of Practice on Managing the Risk of Fraud issued in October 2014.

107. An internal audit report to the March 2016 Audit Committee highlighted that not all staff dealing with planning applications were aware of the council's bribery and corruption policy. Officers have indicated that a review is currently being undertaken to ensure all services are aware of the policy.

108. The council has employee and Councillor codes of conduct in place and the 'Achieving and Maintaining Standards' policy sets out the action to be taken in the event of expected standards not being achieved.

109. Overall, we concluded that the council has satisfactory arrangements in place for maintaining standards of conduct and the prevention and detection of fraud and corruption.

National Fraud Initiative in Scotland

110. The National Fraud Initiative (NFI) in Scotland brings together data from councils, police boards, fire and rescue boards, health bodies and other agencies, to help identify and prevent a wide range of frauds against the public sector. Matching data obtained from the systems of participating bodies allows the identification of potentially fraudulent claims on the public purse including housing benefit fraud, occupational pension fraud and payroll fraud. If fraud or overpayments are not identified in a body, and the NFI exercise has been undertaken properly, assurances may be taken about internal arrangements for preventing and detecting fraud.

111. The NFI exercise identified 4,547 matches, of which 1,038 cases were recommended for investigation. In addition to the recommended cases a proportion of the remaining cases were considered using a risk based approach. Of the 1,682 cases investigated the total monies recovered or being pursued so far of £27,713 related to one duplicate payment (£10,605) and ten housing benefit claims (£17,108). No frauds were identified.

112. The council is one of only two Scottish councils that do not submit the electoral register as part of the National Fraud Initiative submission. To ensure that the risk of fraud relating to council tax single occupancy discounts is minimised the council procured a data matching exercise.

113. A report to the March 2016 Audit Committee highlighted that 218 of the 2,162 matches identified for investigation were found to have claimed this discount incorrectly (total £108,798). Of this £84,243 has been collected with arrangements in place to recover the balance.

114. Overall, we concluded that the council has satisfactory arrangements in place for investigating and reporting data matches identified by the NFI.

Transparency

115. Local residents should be able to hold the council to account for the services it provides. Transparency means that residents have access to understandable, relevant and timely information about how the council is taking decisions and how it is using its resources. We have considered this under various headings including:

- clarity and presentation of financial statements – a copy of the council's unaudited accounts was made available on the website. The format of the accounts complies with the Code and the narrative sections are written, as far as possible, in plain English to provide the reader with an understanding of the council's business
- budget monitoring reports – refer paragraphs 40 - 43
- performance reporting - refer paragraphs 139 - 141
- registers of interest – these are available on the website

116. Overall we have concluded that the council is open and transparent and we have not encountered any evidence to suggest that information is routinely and unjustifiably withheld from public scrutiny although improvements in budget monitoring reports could be made (refer paragraph 45).

Freedom of Information requests

117. The Freedom of Information (Scotland) Act 2002 (FOI) established a general public right of access to all information held by Scottish public authorities. The council's performance in relation to FOI requests is reported annually to the executive officer team and the Scrutiny Committee.

118. The report to the June 2016 committee confirmed that 1,368 FOI requests had been received in 2015. This was a slight decrease of 1.2% on the 2014 figure of 1,385. Requests from individuals remain the largest category (42%) followed by requests from the media (22%) and businesses (17%).

119. The committee was advised that the statutory requirement to respond within 20 working days was met for 96.9% of requests and 83% of cases received at least some of the information requested. 43 requests for a review of the decision were received which equated to 3.1% of the total requests received. Two requestors subsequently withdrew and the council's decision on 24 of the remaining requests was upheld.

120. Overall the council's approach to managing the FOI requests it receives is effective.

Integration of health and social care

121. The Public Bodies (Joint Working) (Scotland) Act received royal assent on 1 April 2014. The Act provides the framework for the integration of health and social care services in Scotland.

122. In the council, a Pathfinder Board was set up to lead on and oversee the transition to integrated services. The Board submitted the integration scheme which was passed by the Scottish Parliament on 3 October 2015 at which point the Pathfinder Board

became the Perth and Kinross Integration Joint Board for Health and Social Care (IJB) with responsibility for delivering services that meet local and national outcomes.

123. The integration scheme between Perth & Kinross Council and NHS Tayside sets out the key governance arrangements. It also sets out the requirement to identify and collate a core set of indicators and measures which relate to integrated functions to enable the reporting of performance targets and improvement measures.

124. The IJB board comprises a wide range of service users and partners including four elected councillors nominated by the council and four Directors nominated by NHS Tayside. It is supported by a chief officer who provides overall strategic and operational advice and is directly accountable to the IJB board and the chief executives of both the council and NHS Tayside. The chief officer provides regular reports to the council and the NHS board and is a member of the council's executive officer team.

125. The integration scheme sets out the approach to dealing with any overspends in the year. In the first two years responsibility for meeting overspends lies with the partner delivering the service. Thereafter the overspend could be allocated based on each partners proportionate contribution to the IJB budget.

126. In May 2016 the IJB considered two Audit Scotland reports – Health and Social Care Integration published in December 2015 and Changing Models of Health and Social Care published in March 2016. Officers have developed an action plan to address the risk identified in the reports and members noted the progress being made.

127. The IJB is in the process of developing a transformation programme to support the case for change set out in the Clinical Strategy for Scotland and the Strategic Plan for Scotland. This recognises the on-going challenges faced in relation to demand for health and social care services, issues with recruiting to certain medical disciplines and the financial pressures across the public sector.

128. The programme will be based on the triple aims of improving the experience of care; improving the health of the population and reducing per capital costs of health care and will be addressed through 5 workstreams:

- prevention and early intervention
- person centred care
- working with communities
- reducing inequalities and promoting healthy living and
- making best use of resources

Housing benefits performance audit

129. Separate from the audit of the council's housing benefit subsidy claim, Audit Scotland carries out a programme of housing benefit risk assessments.

130. In December 2013 Audit Scotland reported that the council needed to do more to improve its accuracy performance and to ensure that its intervention activity was effectively targeted with nine risks to

continuous improvement highlighted. The risk assessment in December 2015 found that seven of these risks had been addressed, one was no longer relevant and that further work requires to be undertaken to ensure the accuracy of processing. The council's improvement action plan highlighted officers are to scrutinise individual's performance statistics and use this information to aid in enhancing the accuracy of processing.

Local scrutiny plan

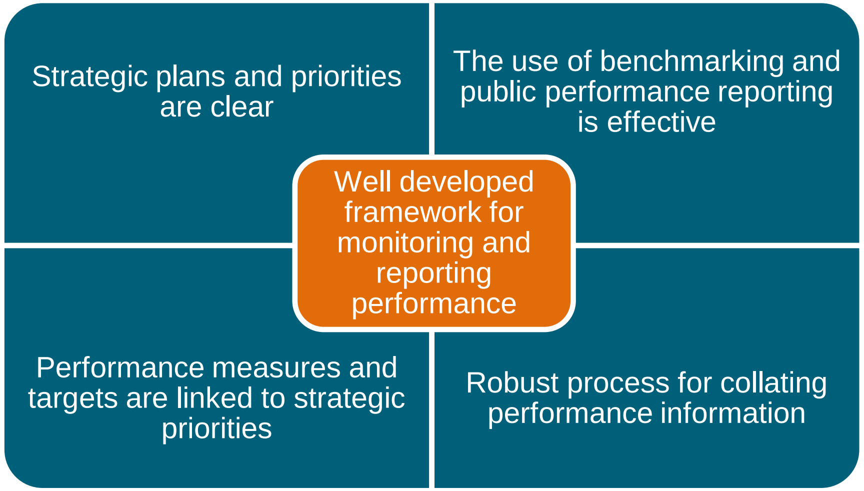
131. The 2016/17 Local Scrutiny Plan (LSP) prepared by the Local Area Network (LAN) of scrutiny partners was considered by the council in May 2016. The LAN's view was that further improvement could be made in relation to housing and specific scrutiny covering housing rent arrears would benefit the council. The Scottish Housing Regulator has scheduled this review for January 2017. The LAN did not identify any other specific additional scrutiny for 2016/17.

Outlook

132. Councils will continue to operate in a changing environment within continuing financial constraints. Under these circumstances councils will be obliged to consider the delivery of services by different means. Good governance will be particularly important where council resources and service delivery are devolved to third party organisations.

133. Partnership, joint working and arm's length organisations have become increasingly popular vehicles for planning and delivering council services and there is a sustained national focus on their use. Where council services are being delivered by third party organisations it will be crucial that the council implements robust assurance and governance arrangements to deliver best value while at the same time ensuring an appropriate level of accountability for public money (refer paragraph 28 re new cultural trust). Community planning and health and social care integration will require an ongoing focus on governance and assurance to ensure that the council's priorities are being achieved.

Best Value



134. Best value is a key factor to consider when planning policies, programmes and projects and when taking any spending decisions. The council should have systems and processes to ensure that it can demonstrate that it is delivering best value by assessing and reporting on the economy, efficiency, effectiveness and equality in service provision.

135. The council has a strong track record of partnership working and the Community Plan/Single Outcome Agreement (SOA) 2013-2023 outlines a vision for the area centred around the five strategic objectives:

- giving every child the best start in life
- developing educated, responsible and informed citizens
- promoting a prosperous, inclusive and sustainable economy
- supporting people to lead independent, healthy and active lives
- creating a safe and sustainable place for future generations.

136. The Corporate Plan 2013-2018 sets out how the council will support the Community Plan and identifies the high-level strategic objectives the council is working towards to meet local needs.

137. In June 2016 a three year Business Plan was agreed to sit alongside the Corporate Plan. This considers the significant changes being undertaken, for example, IJB, new Trust models for culture and sport, transformation programme, Community Empowerment Act and draw together corporate strands from the services BMIPs. This is an internally facing document covering the same period as the medium term financial plan. It outlines how the council plans to address the challenges of public service reform, increasing demand and reducing budgets as well as its approach to managing new models of service delivery, locality planning, collaborative working and strategic partnerships such as the City Deal.

138. Discussions with officers highlighted the main risks to the medium term budget strategy include: savings based on reshaping the teachers workforce; implementation of the living wage; borrowing costs; health and social care integration given the council area's demographics; and the potential impact of Britain leaving the European Union.

Performance management

139. The council has a strong focus on performance management and has a sound framework for monitoring and reporting performance against the council's priorities.

140. There is good alignment between the Community Plan/SOA 2013-2023 and the council's corporate plan. The Corporate Plan 2013-2018 is supported by services' Business Management and Improvement Plans (BMIPs). This is a well established approach to planning and performance management within the council with further improvements envisaged through the corporate business plan.

141. Annual guidance is produced giving all officers involved in corporate data collection information about the process and their roles and responsibilities. It outlines the process and timetable for collection (at corporate and service level). The Strategic Planning, Improvement and Risk Team collects data against each of the corporate performance indicators and produces an annual performance report. The council's website also provides links to further details on specific performance at a service-level. The 2015/16 annual performance report is expected to be considered by the council in October 2016.

Overview of performance targets in 2015/16

142. The annual performance report 2015/16 summarises the council performance against the Community Plan/SOA 2013/23 and the council's corporate plan 2013-18. The report showed performance improvements in 52 (71%) of the local outcome areas with 11 (15%) demonstrating consistent performance and 10 (14%) highlighted as needing attention. The report identifies the areas the council and community planning partners will be focussing on in 2016/17. These cover seven key themes:

- inclusive economic growth
- developing the approach to locality planning
- developing the approach to health and social care
- supporting vulnerable families
- helping older people stay at home longer
- targeted intervention to reduce inequalities
- protecting, reforming and improving public services.

143. The council participates in the Local Government Benchmarking Framework (LGBF). It includes a checklist of these within its corporate guidance for BMIPs. The council provides comparison over time and against targets within its services annual performance reports, SOA performance reports and LGBF

144. In April 2016 the council considered its performance against the 2014/15 LGBF indicators published by the Improvement Service in January 2016. Its performance, when compared to Scotland, showed:

- 10 indicators (30%) are in the upper quartile (2013/14: 29%)

- 15 indicators (46%) are in the upper middle quartile (2013/14: 45%)
- 5 indicators are (15%) in the lower middle quartile (2013/14: 19%)
- 3 indicators are (9%) in the lower quartile (2013/14: 12%)

145. The three areas where the council was classified in the lower quartile were:

- the percentage of A class roads that should be considered for maintenance treatment;
- people aged 65 or over with intensive needs receiving care at home; and
- the percentage of young people entering positive destinations.

Statutory performance indicators (SPIs)

146. The Accounts Commission places great emphasis on councils' responsibility for public performance reporting. The Commission does not prescribe how councils should report but expects councils to provide citizens with fair, balanced and engaging performance information reporting.

147. For 2015/16 three (SPIs) were prescribed:

- SPI 1: covering a range of information relating to areas of corporate management such as employees, assets and equalities and diversity
- SPI 2: covering a range of information relating to service performance
- SPI 3: relates to the reporting of performance information as required by the Local Government Benchmarking Framework.

148. Overall we concluded that the council's arrangements for publication were satisfactory. BMIPs report progress against indicators on a six-monthly basis and further details are available on the pkperforms page of the website.

Local performance audit work

149. In November 2013 the Accounts Commission and Auditor General published a report on Scotland's public sector workforce. The report highlighted a number of key messages on workforce changes across Scotland in the public sector and made a number of recommendations to the Scottish Government, central government bodies, the NHS, COSLA and local authorities. Local follow up work was undertaken during 2015/16 on the 2013 report to determine the extent to which audited bodies were implementing the recommendations. The findings from this work is likely to be reflected in sector specific overview reports

150. The council's executive officer team considered the 2013 report at a meeting in August 2014 and concluded that whilst the council had arrangements in place which satisfy many of the requirements identified in the Audit Scotland good practice guide, there was scope to further develop and enhance existing arrangements for both workforce planning and workforce change programmes.

151. A new organisational development framework was approved in June 2015 based around the "Learn Innovate Grow" principles. An

update to the 2010 framework for managing workforce change in was agreed in June 2016 designed to support the implementation of the council's transformation strategy.

152. The recently agreed corporate business plan highlighted further improvements including implementing a more systematic approach to workforce planning across services and implementing a number of workforce projects such as job families, recruit within and job and organisation design.

153. The business plan also recognises the challenges of recruiting and retaining staff and the need to ensure appropriate succession planning is in place to avoid losing essential skills and knowledge, particularly when considering further changes in staffing numbers.

154. A voluntary severance scheme has been in place for a number of years (Exhibit 9). Although there is no overarching forecast of expected staff numbers, skill needs and cost on a rolling basis over the entire council, requirements are considered under the transformation programmes and the workforce change framework.

Exhibit 9: Exit packages 2010 to 2016

Year	No. of exit packages	Cost of exit packages (£'m)
2010/11	118	3.6
2011/12	31	0.7
2012/13	40	1.1
2013/14	135	2.0
2014/15	24	0.2
2015/16	150	3.4
Total	**498**	**11.0**

Source: Perth & Kinross Council audited financial statements

155. Overall we concluded that the council has a range of workforce measures in place that are working effectively to promote a culture of change to address the changing public sector landscape

National performance audit reports

156. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2015/16, a number of reports were issued which are of direct interest to the council. These are outlined in appendix III. Perth & Kinross Council has processes in place to ensure that all national reports and their impact on the council are considered by Members.

Procurement

157. In 2009 the Scottish Government introduced an annual evidence-based assessment, the procurement capability assessment (PCA), to monitor public bodies' adoption of good purchasing practice and as a basis for sharing best practice.

158. Due to legislative changes around procurement the assessment is in need of updating and a new assessment regime – the Procurement & Commercial Improvement Plan (PCIP) – replaced the PCA in 2015. PCIP focuses on policies and procedures driving procurement performance and the results delivered. As this approach adopts new assessment methods and scoring the results will not be comparable to the previous PCA. The council's first assessment under PCIP is scheduled for September 2016.

159. A transformation project highlights achieving further savings from procurement activities through closer management of suppliers, maximizing use of collaborative procurement consortia, development of professional procurement skills for staff, improved monitoring and reporting systems, and managing demand through re-specifying products and services. As part of this project the council participated in a mock assessment under the national Procurement and Commercial Improvement Programme (PCIP) at the end of October 2015 and plans to use the findings from this to implement improvements prior to the formal assessment being undertaken..

Following the public pound

160. The Council has a local Code of Guidance based on the Code of Guidance on Funding External Bodies and Following the Public Pound issued by the Accounts Commission in co-operation with COSLA. A review of the local Code and other relevant documents is presently being carried out by officers of the Following the Public Pound Group to ensure that they are fit for purpose and relevant to the current operational requirements. A review of existing funding arrangements will be undertaken once the new Code of Guidance has been adopted to ensure they comply with the Code and all relevant statutory requirements

161. The Strategic Policy & Resources Committee was advised in February 2016 that a Following the Public Pound Toolkit would be produced and this is expected to be in place by the end of the year.

Equalities

162. The Equality Act 2010 introduced a new public sector 'general duty' which encourages equality to be mainstreamed into public bodies' core work. The Act requires that by no later than 30 April 2015 and every two years thereafter, public bodies must publish a report on the progress made to achieve the quality of outcomes it has set. The council's 2015 report is available on its website.

Outlook

163. In common with other councils, Perth & Kinross Council faces the key challenges of reducing budgets, an aging population with higher levels of need and the public expectation of high quality services. Savings have been made in recent years largely through a net reduction in workforce expenditure as a result of changes in the workforce composition. As choices on how to address funding gaps become increasingly difficult, councils will have to focus on making the very best use of all available resources and to challenge existing ways of doing things. A strong and effective performance management framework will be critical to the success of the council achieving its key priorities and achieving best value.

Appendix I: Significant audit risks

The table below sets out the audit risks we identified during the course of the audit and how we addressed each risk in arriving at our opinion.

Audit Risk	Assurance procedure	Results and conclusions
Risk of material misstatement		
Internal financial controls A robust system of internal financial controls is essential to reduce the risk of material error in the financial statements. In times of economic challenge, the council's financial systems may be exposed to increased risk of fraud or manipulation. Auditing standards (ISA 240 The auditor's responsibility to consider fraud in an audit of financial statements) require auditors to presume a risk of fraud where income streams are significant. The council receive a significant amount of income in addition to Scottish Government funding. The extent and complexity of these income streams introduces an increased risk of fraud. *Risk: The council's financial position is exposed to error. Fraud and manipulation may not be detected.*	Testing of key internal financial controls. Review of internal audits work in specific areas (i.e. payroll). Targeted testing of risk areas and report to members as appropriate. Review the council's involvement in the National Fraud Initiative.	No significant issues were found in relation to controls in place across the key financial systems Audit testing also confirmed that income was properly accounted for in the financial year.

Audit Risk	Assurance procedure	Results and conclusions
Management override of controls Management has the ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. *Risk: The accounts are material misstated.*	Detailed testing of journal entries. Review of accounting estimates for bias. Evaluating significant transactions that are outside the normal course of business.	Satisfactory explanations for variances between income and expenditure were provided by officers. No outstanding issues. Journal adjustments were tested and no indications of management override of controls were found. Judgements and estimations applied were tested to confirm they were appropriate and reasonable. No issues highlighted with the judgements and estimates applied.
Performance and governance disclosures The Local Authority Accounts (Scotland) Regulations 2014 require the financial statements to include: • a management commentary which includes details of the council's strategic performance during the year • an annual governance statement providing assurance that the governance framework is operating effectively In previous years the performance information has not been available to inform the completion of the unaudited accounts. Similarly all self assessments to inform the	Review the management commentary and the annual governance statement. Consider the process/evidence supporting these statements. Review of internal audit findings for corporate governance and corporate risk management.	As in previous years the annual performance report was not produced in time to inform the management commentary although a link to where this can be accessed is included in the accounts. A new approach to compiling the AGS was put in place this year but the effectiveness of the new approach was diluted as there was not a full audit trail to evidence the process had been appropriately applied. Refer action plan point 1 Appendix IV.

Audit Risk	Assurance procedure	Results and conclusions
council's view on its governance arrangements had not been completed prior to consideration of the unaudited accounts. *Risk: The unaudited accounts available to members and the public do not reflect a complete picture of the council's activities during the year.*		
Charities governance documentation The governance documentation for several trusts could not be located as a consequence of the age of the trusts, in some cases dating back over 100 years. To address this, in previous years, the council has treated all funds as endowments and where there was an absence of governance documentation it relied on custom and practice to inform any decisions by the trustees in respect of the trusts' expenditure and use of assets. *Risk: The funds are not accounted for accurately or used for the appropriate purpose.*	Audit of the charities financial statements to ensure compliance with requirements. On-going monitoring and inclusion in annual audit report as appropriate.	The 2015/16 accounts reflected which trusts have/do not have governance documentation and that all trusts are treated as endowments. A further eight trusts were amalgamated into the Welfare Trust in 2015/16 and a further trust was transferred to an external charity.
Risks identified from the auditor's wider responsibility under the Code of Audit Practice		
Financial position Along with all other public bodies in Scotland, the council is facing the prospect of having to make significant budget savings. At the same time as the council aims to support the local economy and maintain service provision, it is	On-going monitoring and inclusion in annual audit report as appropriate. Submit information on the council's workforce management arrangements to inform a national study follow up.	Refer financial management and sustainability section paragraphs 58 to 62 and Best Value section paragraphs 149 to 155 The council is anticipating savings in excess

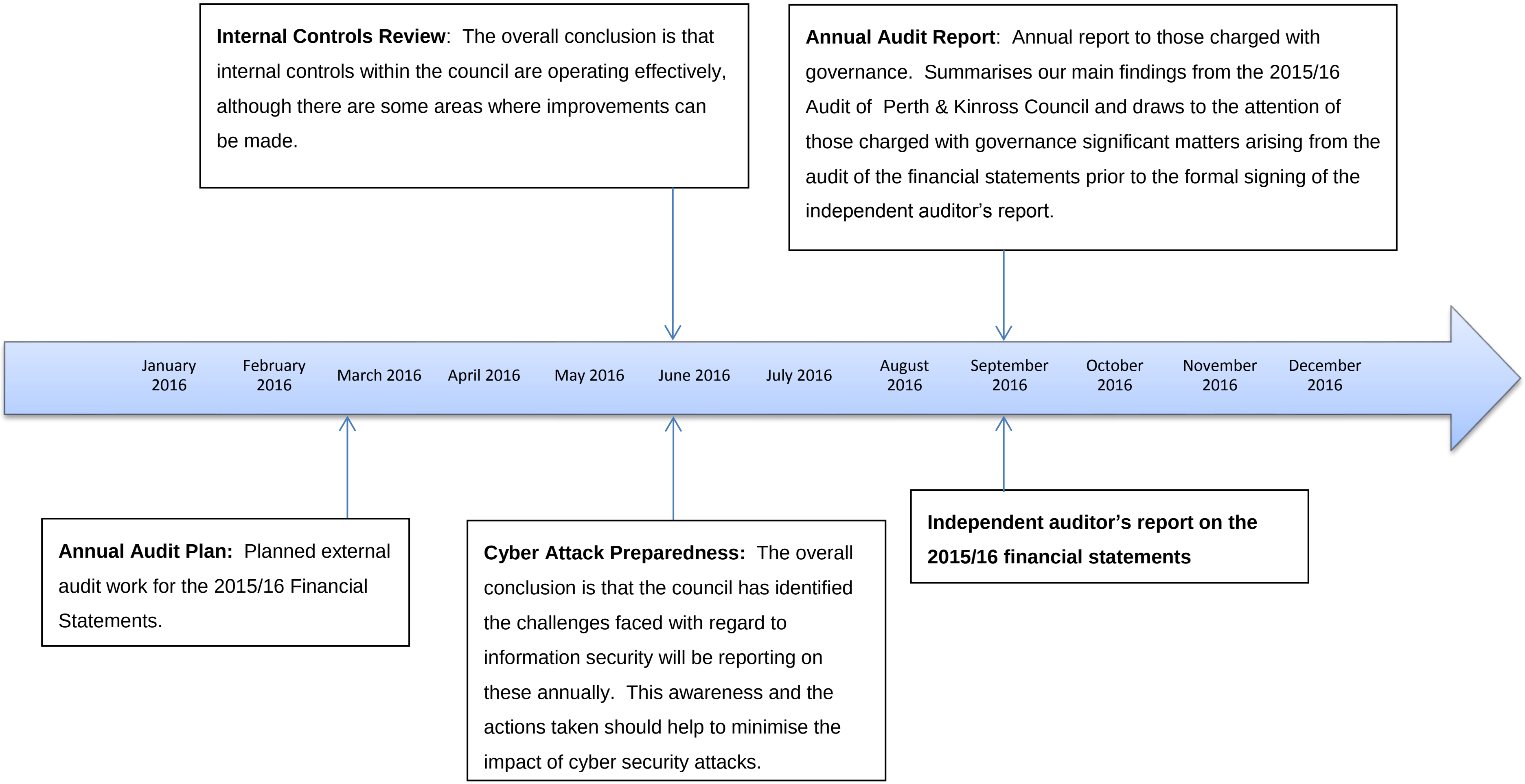
Audit Risk	Assurance procedure	Results and conclusions
likely to face a reduction in resources. *Risk: The council is unable to secure the efficiencies required without impacting on services.*	Review of internal audit findings for reserves strategy.	of the £39 million previously identified will be needed and the transformation programme will be key to delivering on these. Internal Audit report on reserves strategy confirmed there are effective arrangements in place and internal controls were strong
Capital expenditure In previous years we have reported on significant underspends against the council's capital programme. The outturn for 2014/15 represented progress in delivering the original programme with a 2.4% overspend, although we highlighted that the council was again unable to deliver fully on its housing capital programme. In 2015/16 gross capital expenditure is projected to be underspent against the original budget by £17.1 million (20%). This comprises a general fund capital programme underspend of £17.6 million and a housing investment programme overspend of £0.5 million. *Risk: The council is unable to deliver efficient and effective services and contribute to a prosperous, sustainable and inclusive economy for its area due to delays in investment or improvements to the asset base.*	On-going monitoring of capital budget, plans and monitoring reports and inclusion in annual audit report as appropriate. Review of internal audit findings for the housing investment programme.	The final outturn position for 2015/16 was an underspend of 30.4 % on the general services programme although the council was able to fully deliver on its housing capital programme in the year. Refer financial management and sustainability section paragraphs 63 to 67. On-going issue refer Action Plan point 2 Appendix IV.

Audit Risk	Assurance procedure	Results and conclusions
Performance management The council's performance indicates a relatively positive picture overall with only a few areas of performance declining. However, effectively managing performance will remain a key challenge as financial pressures increase. The council will need to use its performance information to understand and manage the impact of spending decisions. *Risk: The council's resources are not directed at priority areas and outcomes are not demonstrated.*	Review of processes to collate statutory performance indicators On-going monitoring of the performance management framework and inclusion in annual audit report as appropriate.	The 2015/16 annual performance report provides a balanced view of the council's performance against key indicators in the year and highlights areas in need of attention along with priorities to be addressed in 2016/17. The annual accounts include a reference to the pkperforms webpage which includes a link to the latest performance report. Annual guidance on compiling and reporting performance indicators is issued to officers and an internal verification process to ensure information is accurately reported is in place.
Locality planning The Community Empowerment (Scotland) Act 2015 places a new statutory duty to tackle inequalities and specifically creates a statutory duty on community planning partnerships to develop, publish and implement local outcome improvement plans setting out how partners will tackle stubborn inequalities across the area. *Risk: The council fail to tackle inequalities within its locality areas.*	On-going monitoring and inclusion in annual audit report as appropriate.	Community Planning Partnership aims to have locality outcome improvement plans in place by Summer 2017. No impact on the 2015/16 audit.

Audit Risk	Assurance procedure	Results and conclusions
Health & social care integration The Public Bodies (Joint Working) (Scotland) Act received royal assent on 1 April 2014. The Act provides the framework for the integration of health and social care services in Scotland. In the council, a Pathfinder Board was set up to lead on and oversee the transition to integrated services. The Board submitted the integration scheme which was passed by the Scottish Parliament on 3 October 2015 at which point the Pathfinder Board became the Perth and Kinross Integration Joint Board for Health and Social Care (IJB) with responsibility for delivering services that meet local and national outcomes. *Risk: Integration does not deliver the intended outcomes.*	On-going monitoring and inclusion in annual audit report as appropriate.	Refer governance and transparency section – paragraphs 121 to 128. This remains an ongoing issue for the council.
Cultural trust A cultural trust is to be established in April 2016. The total value of services being delivered by arms-length organisations will double to approximately £10 million. The council has a statutory requirement to follow the public pound in respect of commissioned services. *Risk: Governance and monitoring arrangements are ineffective for the new arms length organisation.*	On-going monitoring and include in report to members as appropriate. Review of internal audit findings for following the public pound.	Service level agreements are in place between the council and Culture Perth & Kinross which adequately cover the governance and monitoring arrangements agreed between the parties. We note that the council will be undertaking a further review of Trust arrangements for culture in early 2017

Audit Risk	Assurance procedure	Results and conclusions
Cyber security Scottish public organisations continue to be the target of cyber attacks and related activities. Previously the council experienced degradation in its internet connection as a consequence of a targeted hacking attack and has been subjected to increasingly sophisticated and targeted threats. *Risk: Cyber attacks result in the loss of personal or sensitive data or systems are unavailable impacting on service delivery.*	We will review the council's preparedness to deal with cyber attacks. Review of internal audit findings for IT disaster recovery.	Our report submitted to the June 2016 Audit Committee found the council is aware of the issues faced and the actions taken to address the risks identified should help it to minimise the impact.

Appendix II: Summary of local audit reports 2015/16



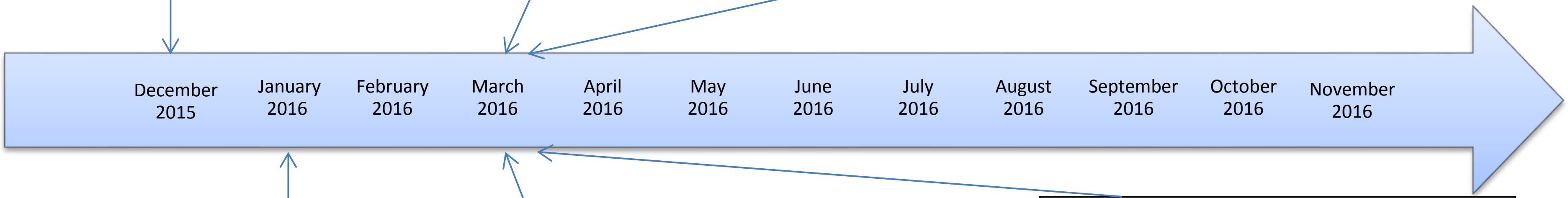
Appendix III: National reports

Summary of Audit Scotland national reports 2015/16

Health and social care integration (December 2015) – Significant risks must be addressed if a major reform of health and social care is to fundamentally change how services are delivered, and improve outcomes for the people who use them.

Community planning: an update (March 2016) – Progress on community planning has not yet achieved the major change needed to fulfil its potential to reduce inequalities and put communities at the heart of delivering public services.

An overview of local government in Scotland (March 2016) – Budget reductions mean starker choices ahead for councils which will not be met simply by continuing to cut staff and services.



Major capital investments in councils: follow-up (January 2016) - Councils need to improve further the way they manage major projects like schools, roads, housing and flood prevention, says the Accounts Commission.

Changing models of health and social care integration (March 2016) - A lack of national leadership and clear planning is preventing the wider change urgently needed if Scotland's health and social care services are to adapt to increasing pressures.

National scrutiny plan for local government (March 2016) – Provides a summary of strategic scrutiny activity for all councils in 2016/17.

Appendix IV: Action plan

No. AS ref.	Paragraph ref.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
1.	26	A new approach to compiling the Annual Governance Statement (AGS) was introduced for the 2015/16 financial statements. It was however difficult to evaluate how effective the new approach was as there was no audit trail to evidence the process applied. ***Risk*** *The AGS does not accurately reflect the governance arrangements within the council's group.* **Recommendation** Prior to members' consideration of the AGS all appropriate assurances should be received and considered.	Whilst verbal assurances had been received prior to consideration of the draft Governance Statement, written Certificates of each Service's assurance were available prior to submission of the Final Accounts. For the AGS 2016/17 we will ensure that written certificates are available prior to submission of the draft statement	Head of Legal & Governance Services June 2017

No. AS ref.	Paragraph ref.	Issue/risk/Recommendation	Management action/response	Responsible officer / Target date
2.	43, 65	The council continues to underspend against budget (both revenue and capital). There is scope to better align budgets with services' actual spend. In addition, the monitoring reports presented to committee do not include information on service performance so members are unable to evaluate whether the underspends are having a detrimental impact on service delivery. ***Risk*** *There is an adverse impact on service delivery.* **Recommendation** The council should review its budget setting and monitoring procedures to ensure they remains fit for purpose. This review should consider the inclusion of performance information to provide a clearer basis for decision making.	The Council is aware of this position and has managed under spends and additional income effectively over the medium term. Significant sums were removed from the 2016/17 revenue budget when the final revenue budget was set in February 2016 to reflect historical spend. In addition the executive officer team has already met (06/09/16) to discuss the 2015/16 final outturns with a view to removing any recurring underspends from Service base budgets prior to setting the 2017/18 final revenue budget in February 2017. The revenue monitoring report has also been amended to remind members that reported underspends may be considered for use during the current financial year or as part of the revenue budget strategy for future years.	Head of Finance (ongoing)