Public Document Pack

AUDIT AND RISK
MONDAY, 11TH MAY, 2015

A MEETING of the AUDIT AND RISK will be held in the COUNCIL HEADQUARTERS, COUNCIL HEADQUARTERS, NEWTOWN ST BOSWELLS on MONDAY, 11 MAY 2015 at 10.15 am

J. J. WILKINSON,
Clerk to the Council,

4 May 2015

BUSINESS		
1.	**Apologies for Absence.**	
2.	**Order of Business.**	
3.	**Declaration of Interest.**	
4.	**Minute** (Pages 1 - 6) Minute of Meeting of the Audit & Risk Committee held on 23 March 2015 to be approved and signed by the Chairman. (Copy attached.)	4 mins
5.	**Scottish Borders Council Local Scrutiny Plan 2015/16.** (Pages 7 - 12) Consider the local scrutiny plan by Audit Scotland which sets out the planned scrutiny activity in Scottish Borders Council during 2015/16. The plan is based on a shared risk assessment undertaken by a local area network, comprising representatives of all of the main scrutiny bodies who engage with the Council. (Copies attached)	20 mins
6.	**Scottish Borders Council Annual Governance Statement 2014/15.** (Pages 13 - 20) Consider report and draft Annual Governance Statement 2014/15 by Chief Executive for inclusion in Scottish Borders Council Statement of Accounts 2014/15. (Copy attached.)	10 mins
7.	**Pension Fund Annual Governance Statement 2014/15.** (Pages 21 - 26) Consider report and draft Annual Governance Statement 2014/15 by Chief Financial Officer for inclusion in Pension Fund Annual Report and Accounts 2014/15. (Copy attached)	10 mins
8.	**Housing Benefits Overpayment and Debt Recovery.** (Pages 27 - 36) Consider update report by Service Director Neighbourhood Services on Housing Benefits overpayment and debt recovery information. (Copy attached)	15 mins

9.	**Review of Auditors' Housing Benefit Subsidy Claim Reported Errors 2013/14.** (Pages 37 - 72) Consider report by Audit Scotland published in February 2015 on findings from a thematic review of the certification of the 2013/14 housing benefit subsidy claims of all Scottish Councils. The review focussed on errors identified by auditors during the certification process as well as spending by local authorities which was not fully funded by the Department for Work and Pensions (DWP) and was therefore a direct cost to local authority budgets. (Copy attached)	20 mins
10.	**Internal Audit Work 2014/15.** (Pages 73 - 86) Consider a report by Chief Officer Audit & Risk on recent work carried out by Internal Audit to deliver the Internal Audit Annual Plan 2014/15, including update on progress by management in addressing the Priority 1 recommendations and related Priority 2 recommendations made by Internal Audit to improve internal controls and governance arrangements. (Copy attached)	15 mins
11.	**Internal Audit Annual Report 2014/15.** (Pages 87 - 102) Consider report by Chief Officer Audit & Risk on the annual assurance and audit opinion to Management and Audit & Risk Committee arising from Internal Audit activity in completing the Internal Audit Annual Plan 2014/15. (Copy attached)	20 mins
12.	**Borrowing and Treasury Management in Councils.** (Pages 103 - 144) Consider report by Audit Scotland published in March 2015 on findings from a national review of borrowing and treasury management arrangements across all Scottish councils and presentation by Chief Financial Officer on main findings of the report and actions arising for Scottish Borders Council. (Copy attached)	20 mins
13.	**Any Other Items Previously Circulated.**	
14.	**Any Other Items which the Chairman Decides are Urgent.**	

NOTES

1. **Timings given above are only indicative and not intended to inhibit Members' discussions.**

2. **Members are reminded that, if they have a pecuniary or non-pecuniary interest in any item of business coming before the meeting, that interest should be declared prior to commencement of discussion on that item. Such declaration will be recorded in the Minute of the meeting.**

Membership of Committee:- Councillors M Ballantyne (Chair), W Archibald, J Campbell, A J Nicol, S Scott and B White (Vice-Chairman), Mr D Gwyther, Mr G Tait.

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SCOTTISH BORDERS COUNCIL
AUDIT AND RISK COMMITTEE

MINUTE of MEETING of the AUDIT AND RISK COMMITTEE held in the Council Chamber, Council Headquarters, Newtown St. Boswells on 23 March 2015 at 10.40 a.m.

Present: -	Councillors M. Ballantyne (Chairman), J. Campbell, A. Nicol, B. White; Mr D. Gwyther.
Apologies:-	Councillors W. Archibald, S. Scott; Mr G. Tait.
In Attendance:-	Chief Financial Officer, Chief Officer Audit and Risk, Service Director Strategy and Policy, Corporate Finance Manager, Clerk to the Council, Democratic Services Officer (P. Bolson); Mr H. Harvie – KPMG, Ms. R. Mitchell – KPMG.

MINUTE

1. There had been circulated copies of the Minute of 19 January 2015.

DECISION
APPROVED for signature by the Chairman.

2. With reference to paragraph 9(b)(ii) of the Minute of 19 January 2015, regarding a report to the Audit and Risk Committee on the schedule of loans outstanding over the last 50 years, there were circulated prior to the end of the meeting a list of SBC Loans & Advanced Summary Principal Outstanding as at 23 March 2015 which amounted to £170m over 50 years. A spike for repayment was expected in 2052/53 which reflected previous rescheduling of Public Works Loan Board debt to take up more favourable interest rates at that time. The Council currently had long term assets of £421m at 31 March 2014, including PPP assets. PPP debt of £56m was not included in the aforementioned £170m figure.

3. With reference to paragraph 9(b)(iii) of the Minute of 19 January 2015, regarding a report updating Members on the current position in terms of the Council's policy on housing development and building programme, the Service Director Strategy and Policy advised that he would check on the status of this report.

4. With reference to paragraph 15(c) of the Minute of 19 January 2015, regarding the Revised Risk Management Policy Statement, this had been approved at the meeting of Scottish Borders Council held on 19 February 2015.

DECISION
NOTED.

EXTERNAL AUDIT INTERIM MANAGEMENT REPORT 2014/15

5. There had been circulated copies of an Interim Management Report and Audit Status Summary by KPMG, the Council's External Auditors. Mr Hugh Harvie of KPMG presented the report which gave an update on significant risks and other focus areas which included the revenue and capital financial positions; efficiency savings; reserve levels; valuation of property, plant and equipment; accounting for landfill sites; and pensions. Interim audit fieldwork had looked at the control framework for governance arrangements, including some of the significant changes occurring at the Council and the results of KPMG's consideration

of these from an audit perspective; and in a similar way, systems controls had also been tested. Details were given of the audit timeline and communications, and data analytics. Finally an action plan gave details of the four Grade-3 (minor) recommendations on organisational policies, bank reconciliations, journal authorisation and password policy. In response to a question about the % of savings achieved in line with the Council's Financial Plan, the Chief Financial Officer advised that CMT received a regular update on such performance, with quarterly reports to the Executive Committee. At the end of February 2015, just less than 90% of savings had been achieved in line with the Financial Plan and the Chief Financial Officer confirmed he was comfortable with progress and the way savings were being tracked.

DECISION
NOTED.

EXTERNAL AUDIT SCOTTISH BORDERS PENSION FUND AUDIT STRATEGY 2014/15

6. There had been circulated copies of a report by KPMG, the Council's external auditors, on Scottish Borders Council's Pension Fund Audit Strategy Review and Plan for year ending 31 March 2015. Mr Hugh Harvie of KPMG presented the report which gave details of the financial context and audit focus areas, including significant risks, and also considered KPMG benchmarking analysis, the presentation of financial statements, and mandatory communications in setting audit materiality. In this latter respect there was an error in the figure within the narrative on page 8 of the report, which should have read £21,000 and not £37,500. The Chief Financial Officer confirmed that the diagrams on pages 6 and 7 of the report were theoretical examples and did not reflect the actual position of the Council's Pension Fund.

DECISION
NOTED.

PENSION FUND REFORMS

7. There were issued at the meeting, copies of slides on new governance arrangements for the Council's Pension Fund. Mrs Lynn Mirley, Corporate Finance Manager, advised Members that legislation was introducing a National Scheme Advisory Board to advise Scottish Ministers and Scheme Managers/Pension Boards. A new Pension Board needed to be set up with equal number of employer and employee representatives (min of 4 each), whose members could not also be a member of the Pensions Committee. A copy of the proposed constitution of the Pension Board was also issued at the meeting. The Chair of the Pension Board would rotate between the Trade Unions and the Council as employer; and the primary responsibility of the Board was to assist the Scheme Manager in securing compliance with the 2014 Regulations and other legislation relating to the governance and administration of the Scheme, as well as requirements imposed in relation to the Scheme by the Pensions Regulator. It was intended that the Board would meet at the same time as the Pension Fund Committee on a quarterly basis. The Pension Board could determine the areas it wished to consider, including – reports produced for the Pensions Committee; requisition reports from the Scheme Managers on any aspect of the Fund; monitor investments and the investment principles/strategy/ guidance; the Fund annual report; external voting and engagement provisions; Fund administrative performance; actuarial reports and valuations; Funding policy; and any other matters that the Pensions Board deemed appropriate. The Pension Fund Committee currently had 12 members: 7 Elected Members; and 5 non-voting members appointed from a Scheduled Body, an Active Admitted Body, and each of the 3 recognised Trade Unions. The proposal was that the 5 non-voting members of the Pension Fund Committee be removed as they would be represented on the new Pension Board, thus avoiding the joint meeting of the 2 bodies becoming too large and unwieldy. It was further intended that a new Investment and Performance Sub-Committee of the Pension Fund Committee be set up which would meet with the Individual Fund Managers and make

recommendations to the joint meeting of the Pension Fund Board and Pension Fund Committee. The proposals would be considered by Scottish Borders Council at its meeting on 2 April 2015.

DECISION
NOTED.

INTERNAL AUDIT WORK 2014/15 TO FEBRUARY 2015

8. With reference to paragraph 13 of the Minute of 19 January 2015, there had been circulated copies of a report by the Chief Officer Audit and Risk providing details of the work carried out by Internal Audit from 20 December 2014 to 27 February 2015 along with the recommended audit actions agreed by Management to improve internal controls and governance arrangements, and internal audit work currently in progress. During this period a total of 6 final internal audit reports had been issued. There were 8 recommendations made (0 Priority 1 High Risk, 0 Priority 2 Medium Risk, and 8 Priority 3 Low Risk) specific to 3 of the reports. Management have agreed to implement the recommendations in all cases to improve internal controls and governance arrangements. The report went on to detail current work in progress to deliver the Internal Audit Annual Plan 2014/15 and other productive work relevant to the Internal Audit function fulfilling its remit as set out in its approved Charter. An executive summary of the final internal audit reports issued, including audit objective, findings, good practice, recommendations and the Chief Officer Audit & Risk's independent and objective opinion on the adequacy of the control environment and governance arrangements within each audit area, was shown in Appendix 1 to the report. A position statement on Management's Progress with implementation of Improvement Actions within the Annual Governance Statement 2013/14 was shown in Appendix 2 to the report.

9. Members asked specific questions around the audits on Income Charging, Billing and Collection; Criminal Justice; Neighbourhood Management; and Health and Social Care Integration. The Chief Financial Officer confirmed that the Council policy was to minimise the level of debt outstanding as far as practicable while recognising that some debt was covered as "charging orders" against property for clients currently residing in care homes. With regard to Criminal Justice, the Service Director Policy and Strategy confirmed that where someone had been on a previous Community Payback Order and moved on to a new one, they would need a further assessment. In terms of fault reporting via the website for Neighbourhood Management issues, officers undertook to bring information back to the Committee on the numbers of faults, complaints, etc reported through the website. It was subsequently agreed that this information could best be provided in the form of a presentation by the Service Director Neighbourhood Services to the next Audit and Risk Committee . Members also considered the different elements of risks associated with outsourcing services and Health and Social Care Integration. The risk of delivering statutory services remained with the Council, but with a different set of governance requirements and service delivery now delivered and managed through a contract with SBCares rather than direct service provision by the Social Work Department. With respect to Health and Social Care integration, Audit Scotland was seeking an assurance from Internal Audit that they had been appropriately engaged and consulted in the development of Health and Social Care Integration Schemes. This assurance was provided verbally by the Chief Officer Audit & Risk at the meeting as follows: The Health and Social Care Integration Scheme for the Scottish Borders has been developed with the full involvement of the Council's Internal Audit section. The Chief Officer Audit & Risk confirmed she has been fully involved in developing the governance scheme for the Partnership as a member of the Integration & Governance working group, and has been consulted on the draft Scheme of Integration. Councillor Nicol asked for clarification concerning the current status of the Kelso High School replacement project and received an update from the Chief Financial Officer, with the assurance that a report would be considered by the relevant Committee at the appropriate time.

DECISION

(a) **NOTED the final reports issued in the period from 20 December 2014 to 27 February 2015.**

(b) **AGREED to acknowledge satisfaction with the recommended audit actions agreed by Management to improve internal controls and governance arrangements.**

INTERNAL AUDIT CHARTER

10. With reference to paragraph 6 of the Audit Committee Minute of 11 March 2013, there had been circulated copies of a report by the Chief Officer Audit and Risk providing the Audit and Risk Committee with the updated Internal Audit Charter – which defined the terms of reference for the Internal Audit function to carry out its role - for approval. Internal Audit was an independent appraisal function established for the review of the internal control system as a service to Scottish Borders Council. It objectively examined, evaluated and reported on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources and the management of risk. In terms of the Public Sector Internal Audit Standards (PSIAS), the Council should formally define the terms of reference for the Internal Audit service i.e. the Charter. The authority for Internal Audit to operate in Scottish Borders Council was contained in the Local Code of Corporate Governance and in the Financial Regulations. The Internal Audit Charter expanded upon that framework: defining the detailed arrangements and setting out the Head of Internal Audit's strategy for discharging its role and providing the necessary annual assurance opinions. The Chief Officer Audit and Risk was the Head of Internal Audit at Scottish Borders Council. The Internal Audit Charter was attached as Appendix 1 to the report and would ensure that Internal Audit was tasked to carry out its role in accordance with best Corporate Governance practice.

DECISION
AGREED to approve the updated Internal Audit Charter as detailed in Appendix 1 to the report.

INTERNAL AUDIT ANNUAL PLAN 2015/16

11. With reference to paragraph 9 of the Minute of 10 March 2014, there had been circulated copies of a report by the Chief Officer Audit and Risk providing details of the proposed Internal Audit programme of work 2015/16, which would enable the Chief Officer Audit and Risk to prepare an annual internal audit opinion on the adequacy of the Council's overall control environment and to gain approval of the Internal Audit Annual Plan 2015/16 for Scottish Borders Council. The SBC Internal Audit function followed the professional standards as set out in Public Sector Internal Audit Standards (PSIAS) effective 1 April 2013 which requires the chief audit executive to establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organisation's goals. This plan also required to be sufficiently flexible to reflect the changing risks and priorities of the organisation. A fundamental role of the Council's Internal Audit function was to provide senior management and Members with independent and objective assurance which was designed to add value and improve the Council's operation. In addition, the Chief Officer Audit and Risk was also required to prepare an annual internal audit opinion on the adequacy of the Council's overall control environment. The proposed Internal Audit Annual Plan 2015/16, detailed in Appendix 1 to the report, set out the programme of work necessary to enable the Chief Officer Audit & Risk to prepare such an opinion. Key components of the audit planning process included a clear understanding of the Council's functions, associated risks, and potential range and breadth of audit areas for inclusion within the plan. There were staff and other resources in place to achieve the Internal Audit Annual Plan 2015/16 and to meet its objectives. The Chief Financial Officer confirmed that the relationship between spend and outcomes was audited through the Best Value Review and reviewed

through the quarterly performance monitoring reports considered by the Executive Committee. The Service Director Strategy and Policy further confirmed that the Council's Corporate Management Team met regularly to consider finance, performance and corporate transformation at the same time and, through transformation, services had now been base-lined.

DECISION
AGREED to approve the Internal Audit Annual Plan 2015/16.

The meeting concluded at 12.30 p.m.

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Scottish Borders Council

Local Scrutiny Plan 2015/16

Introduction

1. This local scrutiny plan sets out the planned scrutiny activity in Scottish Borders Council during 2015/16. The plan is based on a shared risk assessment undertaken by a local area network (LAN), comprising representatives of all of the main scrutiny bodies who engage with the council. The shared risk assessment process draws on a range of evidence with the aim of determining any scrutiny activity required and focusing this in the most proportionate way.

2. This plan does not identify or address all risks in the council. It covers only those risk areas that the LAN has identified as requiring scrutiny, or where scrutiny is planned as part of a national programme. Planned scrutiny activity across all councils in Scotland informs the National Scrutiny Plan for 2015/16, which is available on the Audit Scotland website.

Scrutiny Risks

3. Last year's Assurance and Improvement Plan (AIP), covered the period 2014-17. The AIP noted that the council was in the process of implementing a range of organisational changes to create a structure with sufficient capacity and resilience to allow the council to improve services and deliver better outcomes for local people at a time of significantly reducing resources. This involved the creation of a new corporate management structure with two depute chief executive posts covering people (social work, education and health and social care integration) and place (neighbourhood services, capital projects and regulatory services and commercial services) alongside twelve service directors, one of which is responsible for corporate transformation and services.

4. The March 2013 audit of community planning in Scottish Borders found that the Community Planning Partnership (CPP) had recognised that it needed to provide stronger collective leadership to place itself at the core of public service reform for the area, drive the pace of service integration, increase the focus on prevention and achieve better outcomes for communities. A number of important changes were being made to improve governance and performance management arrangements at the time of last year's AIP, which it was hoped would help ensure that the partnership is better able to demonstrate its impact on improving outcomes. Audit Scotland visited Scottish Borders CPP in July 2014 to follow-up on progress made since the 2013 CPP audit and were encouraged by the progress made by the CPP against its improvement agenda. A formal follow-up audit is being considered during 2015/16 which will allow Audit

Scotland to assess what further progress has been made in addressing outstanding improvement areas such as aligning the budgets of partners to the CPP's Single Outcome Agreement (SOA) priorities, improving partnership performance management, established a shared approach to community consultation, and developing shared approaches to deploying assets across the partnership.

5. The council restructuring was an important aspect of the CPP improvement agenda as it was designed to creating a structure that would enable the council to work effectively in partnership with other local public bodies, the third sector and local communities to deliver improved local public services.

6. The May 2014 AIP included a commitment by the council's appointed auditors (KPMG) to undertake targeted audit work on the effectiveness of the council's revised governance and scrutiny arrangements. To avoid duplication of effort that work was planned to take place after the council had concluded its own review of the impact of its changed governance and scrutiny arrangements. As that work has not yet been concluded by the council the KPMG targeted audit work will form part of the corporate governance element of the 2014-15 annual audit.

7. Targeted Best Value audit work to provide independent assurance to the Accounts Commission on progress that is being made in delivering continuous improvement since the council's Best Value 2 Pathfinder audit in 2009 was proposed in last year's AIP. The timing of that work was to be informed by the outcome of the 2015/16 shared risk assessment. The LAN has concluded that Best Value scrutiny work should be scheduled for 2016/17 to allow time for the council's restructuring to bed down before its impact can be assessed.

8. The May 2014 AIP described an improving position in relation to the leadership of the council's education service in the context of considerable challenges associated with reviewing the school estate, integration of children's services and primary and secondary school services, and closing the attainment gap. Inspection activity of schools and early years centres undertaken throughout 2014 has generated mixed outcomes in Scottish Borders and performance data shows aspects of inconsistent performance across the service. The council acknowledges these findings and is working to address the identified areas for improvement. The LAN has therefore concluded that no specific education scrutiny beyond the ongoing school and early years inspection activity and related challenge and support that Education Scotland provides to the council is required at this time.

9. The May 2014 AIP identified no major scrutiny risks in relation to social care services. Although social work services in Scottish Borders have experienced significant change during 2014, through the creation of the new 'People' department and the future financial outlook indicates significant challenges in delivering affordable and sustainable social work services, no significant risks have been identified in the performance of social work services in Scottish Borders. The LAN has concluded that no specific social work scrutiny activity is required at this time beyond the ongoing routine regulatory

inspection activity undertaken by the Care Inspectorate and the continuing engagement, challenge and support provided by the Care Inspectorate link inspector.

10. There are though two significant strategic developments taking place within Scottish Borders social work services that the LAN will monitor during 2015. Firstly, from April 2015 several of the council's adult care services (care at home, residential care, extra care housing, Bordercare, older peoples' day services, learning disability services and Borders ability equipment store) are set to transfer to the 'Council Care Company' an arms-length external organisation (ALEO). Secondly, the council will be working with NHS Borders to implement a body corporate model of health and social care integration. The Chief Officer for Health and Social Care Integration was appointed in July 2014 and the local Health and Social Care Pathfinder Board was formalised into a Shadow Integration Board in April 2014. Consultation on the local integration scheme has commenced and relevant work streams to progress activities resulting from the integration scheme are already in place.

11. The May 2014 AIP identified mixed performance in relation to homelessness. At that time Scottish Borders Council was taking forward improvements arising from the 2011 Scottish Housing Regulator inspection of its homelessness services. Performance remains mixed. The levels of applicants resolved prior to homelessness decisions and the percentage of applicants that lost contact before discharge of the council's homelessness duty are significantly higher than the national average, whilst the percentages of withdrawn applications and percentages of lost contacts prior to decisions are significantly below the national average. These mixed findings mean that follow-up scrutiny of the council's homelessness service is planned by the Scottish Housing Regulator towards the end of 2015/16.

Planned scrutiny activity

12. As shown in Appendix 1, the council will be subject to a range of risk-based based and nationally driven scrutiny activity during 2015/16. For some of their scrutiny activity in 2015/16, scrutiny bodies are still to determine their work programmes which specific council areas they will cover. Where a council is to be involved, the relevant scrutiny body will confirm this with the council and the appropriate LAN lead.

13. In addition to specific work shown in Appendix 1, routine, scheduled audit and inspection work will take place through the annual audit process and the ongoing inspection of school and care establishments by Education Scotland and the Care Inspectorate respectively. Audit Scotland will carry out a programme of performance audits during 2015/16 and individual audit and inspection agencies will continue to monitor developments in key areas of council activity and will provide support and challenge as appropriate. This will help to inform future assessment of scrutiny risk.

March 2015

Appendix 1: Scrutiny plan: 2015/16

Scrutiny body	Scrutiny activity	Date
Audit Scotland	CPP audit follow-up work to assess what further progress has been made in addressing outstanding improvement areas such as aligning the budgets of partners to the CPP's Single Outcome Agreement (SOA) priorities, improving partnership performance management, established a shared approach to community consultation, and developing shared approaches to deploying assets across the partnership.	September 2015
Care Inspectorate and Healthcare Improvement Scotland	Ongoing monitoring by the LAN of: • progress with the transfer of the council's Care at Home Services for adults to an arms-length external organisation (ALEO) • Local progress with NHS Borders to implement a body corporate model of health and social care integration.	Throughout 2015/16
Care Inspectorate, Healthcare Improvement Scotland, Education Scotland and HMICS	The Care Inspectorate will lead joint inspection of services for children and young people, and will also involve participation by Healthcare Improvement Scotland, Education Scotland and HMICS. These inspections are part of the Care Inspectorate's wider planned programme of national scrutiny work.	January - February 2016
Care Inspectorate and HMICS	The Care Inspectorate and HMICS will be undertaking a joint thematic review of Multi-Agency Public Protection Arrangements (MAPPA) in Scotland during 2015. The purpose of the review will be to assess the status, efficiency and effectiveness of the MAPPA process in Scotland, in terms of keeping people safe and reducing the potential risk of serious harm by registered sex offenders in our communities. It will cover all 32 local authorities and involve local authorities, Police Scotland, NHS Boards and the Scottish Prison Service. The joint review will cover the Scottish Borders Council area during May 2015	May 2015
Education Scotland	Education Scotland will be working in partnership with councils to carry out a validated self-evaluation (VSE) of educational psychology services across all councils over a two-year period beginning in 2015/16. Education Scotland will notify councils of its VSE plans each academic term.	Date over the next two years to be determined
	Education Scotland will review the quality of Careers Information Advice and Guidance services delivered by Skills Development Scotland across all council areas over the next three years. The review in Scottish Borders Council will take place in September 2015.	September 2015
Her Majesty's Inspectorate	HMICS will be inspecting local policing across Scotland over the	Date over the next three

of Constabulary (HMICS)	next three years. These inspections will examine, amongst other things, local scrutiny and engagement between Police Scotland and councils. Two local Policing Divisions are programmed to be inspected in addition to Edinburgh Division in 2015/16. The Divisions will be identified approximately three months prior to inspection, the first being no earlier than October.	years to be determined
Her Majesty's Fire Service Inspectorate (HMFSI)	HMFSI will be inspecting local fire and rescue services across Scotland over the next five years. These inspections will examine, amongst other things, local scrutiny and engagement between the Scottish Fire and Rescue Service and councils. As part of its programme, HMFSI will inspect four local fire and rescue services during 2015/16. It has yet to confirm all the local areas in its 2015/16 programme. .	Date over the next five years to be determined
Scottish Housing Regulator (SHR)	Follow-up scrutiny of the council's homelessness service in relation to the discharge of its homelessness duty.	End of 2015/16
	The Scottish Housing Regulator (SHR) has a planned programme of thematic inquiries into housing services which will be carried out largely in the first quarter of 2015-16, with publication of inquiry reports in the first and second quarters of the year. The thematic inquiries will cover a range of housing services including: Gypsy/Travellers; factoring services; gas safety; complaints handling; customer service standards; repairs; rent consultation; equalities; and openness and accessibility. Some of the thematic inquiries will not involve any on-site work at all and no local authority will be selected for on-site work in more than one thematic. The SHR will contact individual landlords with details about their potential inclusion. During the first and second quarters of the year, the SHR will review the Charter data submitted by social landlords in May 2015 and identify topics for a further programme of thematic inquiries to be taken forward in the second and third quarters of the year.	To be determined

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ANNUAL GOVERNANCE STATEMENT 2014/15

Report by Chief Executive

AUDIT & RISK COMMITTEE

11 May 2015

1 PURPOSE AND SUMMARY

1.1 **This report proposes that the Audit & Risk Committee considers and approves the Annual Governance Statement that will be published in the Statement of Accounts 2014/15 of Scottish Borders Council.**

1.2 The CIPFA/SOLACE framework 'Delivering Good Governance in Local Government' urges local authorities to review the effectiveness of their existing governance arrangements against their Local Code, and prepare a governance statement in order to report publicly on the extent to which they comply with their own code on an annual basis, including how they have monitored the effectiveness of their governance arrangements in the year, and on any planned changes for the coming period.

1.3 Part of the Audit & Risk Committee's remit is to assess the effectiveness of internal controls, risk management, and governance arrangements in place and this includes to 'Be satisfied that the authority's assurance statements, including the Annual Governance Statement, properly reflect the risk environment and any actions required to improve it, and demonstrate how governance supports the achievements of the authority's objectives'[1].

1.4 The Annual Governance Statement 2014/15 at Appendix 1 details the Governance Framework including the key elements of the Council's governance arrangements and the Review Framework outlining the annual review process, overall opinion and areas of further improvement.

1.5 In terms of overall corporate governance it is the Chief Executive's opinion that, although there are a few areas of work to be completed for full compliance with the Local Code, the overall governance arrangements of the Council are considered sound. The Annual Governance Statement is informed by the self-assessment of compliance against the Local Code by the officer self-evaluation working group, the work of internal audit, external audit and inspection agencies, and by Depute Chief Executives and Service Directors assurance statements. This statement will be published in the Statement of Accounts 2014/15.

2 RECOMMENDATIONS

2.1 **I recommend that the Audit & Risk Committee considers the details of the Annual Governance Statement at Appendix 1, and approves the actions identified by Management to improve internal controls and governance arrangements.**

[1] CIPFA guidance note for local authorities 'Audit Committees' (2013)

3 BACKGROUND

3.1 Scottish Borders Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively. The Council approved a revised local code of corporate governance ('Local Code') on 23 February 2012, consistent with the principles and requirements of the new CIPFA/SOLACE framework 'Delivering Good Governance in Local Government' (the 'Framework') to ensure proper arrangements are in place to continue to meet that responsibility.

3.2 The 'Framework' urges local authorities to review the effectiveness of their existing governance arrangements against their 'Local Code', and prepare a governance statement on an annual basis in order to report publicly on the extent to which they comply with their own code, including how they have monitored the effectiveness of their governance arrangements in the year, and on any planned changes for the coming period.

3.3 Part of the Audit Committee's remit is to assess the effectiveness of internal controls, risk management, and governance arrangements in place and this includes to 'Be satisfied that the authority's assurance statements, including the Annual Governance Statement, properly reflect the risk environment and any actions required to improve it, and demonstrate how governance supports the achievements of the authority's objectives''[2].

4 ANNUAL GOVERNANCE STATEMENT

4.1 In March and April 2015 the officer self-evaluation working group on corporate governance has undertaken an annual self-assessment of the effectiveness of internal control and governance arrangements and compliance against the Local Code for the year ended 31 March 2015. This group has responsibility for monitoring compliance with the Local Code and making recommendations to ensure continuous improvement of the systems in place. The Chief Officer Audit & Risk has led on this process as part of HIA[3] role to be champion for sound governance.

4.2 The Annual Governance Statement 2014/15 at Appendix 1 sets out the Governance Framework including the key elements of the Council's governance arrangements as set out in the Local Code which has been updated to reflect the strategic developments and changes to governance within the year including SB Cares and Health and Social Care integration programme. It also sets out the Review Framework outlining the annual review process, overall opinion and areas of further improvement to enhance governance arrangements.

4.3 In terms of overall corporate governance it is the Chief Executive's opinion that, although there are a few areas of work to be completed for full compliance with the Local Code, the overall governance arrangements of the Council are considered sound. The Annual Governance Statement is informed by the self-assessment of compliance against the Local Code by the officer self-evaluation working group, the work of internal audit, external audit and inspection agencies, and by Depute Chief Executives and Service Directors assurance statements. This statement will be published in the Statement of Accounts 2014/15.

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[2] CIPFA guidance note for local authorities 'Audit Committees' (2013)

[3] CIPFA 'the role of the head of internal audit in public service organisations' (2010)

5 IMPLICATIONS

5.1 Financial

(a) There are no direct financial implications arising from this report.

5.2 Risk and Mitigations

(a) The Annual Governance Statement details areas where additional work would further enhance the internal control environment, risk management, and corporate governance arrangements. Implementing this work will ensure that internal controls, risk management, and other governance arrangements remain adequate.

5.3 Equalities

(a) It is anticipated there will be no adverse impact due to race, disability, gender, age, sexual orientation or religious/belief arising from the work contained in this report.

5.4 Acting Sustainably

(a) There are no direct economic, social or environmental issues with this report.

5.5 Carbon Management

(a) There are no direct carbon emissions impacts as a result of this report.

5.6 Rural Proofing

(a) This report does not relate to new or amended policy or strategy and as a result rural proofing is not an applicable consideration.

5.7 Changes to Scheme of Administration or Scheme of Delegation

(a) No changes to the Scheme of Administration or Scheme of Delegation are required as a result of this report.

6 CONSULTATION

6.1 The annual self-assessment completed in March and April 2015 by the officer self-evaluation working group on effectiveness of internal control and governance and compliance against the Local Code of Corporate Governance and associated assurance statements received from Depute Chief Executives and Service Directors within the Council have been taken into account when compiling the Annual Governance Statement.

6.2 The Corporate Management Team has been consulted on the report and any comments received have been incorporated into the report.

6.3 The Chief Financial Officer, the Monitoring Officer, the Chief Legal Officer, the Service Director Strategy and Policy, the Chief Officer Human Resources, and the Clerk to the Council have been consulted on the report and any comments received have been incorporated into the report.

Approved by

Chief Executive, Tracey Logan **Signature ....**

Author(s)

Name	Designation and Contact Number
Jill Stacey	Chief Officer Audit & Risk Tel: 01835 825036

Background Papers: CIPFA/SOLACE framework 'Delivering Good Governance in Local Government'; Scottish Borders Council Local Code of Corporate Governance
Previous Minute Reference: Scottish Borders Council 23 February 2012; Audit Committee 21 April 2014

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. Jill Stacey, Chief Executive's Directorate can also give information on other language translations as well as providing additional copies.

Contact us at Jill Stacey, Chief Executive's Directorate, Scottish Borders Council, Council Headquarters, Newtown St Boswells, Melrose, TD6 0SA
Tel: 01835 825036 jstacey@scotborders.gov.uk

Annual Governance Statement 2014/15

Introduction

Scottish Borders Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for. The Council also has a statutory duty of Best Value under the Local Government in Scotland Act 2003 to make arrangements to secure continuous improvement and performance, while maintaining an appropriate balance between quality and cost; and in making these arrangements and securing that balance, to have regard to economy, efficiency and effectiveness.

In discharging this overall responsibility, elected members and senior officers are responsible for putting in place proper arrangements for the governance of Scottish Borders Council's affairs and facilitating the exercise of its functions. This includes setting the strategic direction, vision, culture and values of the Council, effective operation of corporate systems, processes and internal controls, engaging with communities, monitoring whether strategic objectives have been achieved and services delivered cost effectively and ensuring that appropriate arrangements are in place for the management of risk.

To this end, the Council has approved and adopted a Local Code of Corporate Governance which is consistent with the principles and recommendations of the CIPFA/SOLACE framework Delivering Good Governance in Local Government and the supporting guidance notes for Scottish authorities. A copy of our Local Code of Corporate Governance is available on the Council's website at www.scotborders.gov.uk.

This Annual Governance Statement explains how the Council has complied with the terms of the Local Code for the year ended 31 March 2015. The statement also covers relevant governance issues as they affect those entities included as part of the Council's Group Accounts.

The Governance Framework

The Council's Local Code of Corporate Governance provides the framework against which compliance is measured. This Local Code sets out the key principles, which require to be complied with, to demonstrate effective governance.

The key elements of the Council's governance arrangements as set out in the Local Code include:

- The Council has a Single Outcome Agreement in place agreed with the Scottish Government and Scottish Borders community planning partners. The Council's vision, strategic objectives and priorities are reflected in the Council's Corporate Plan and the Single Outcome Agreement which are approved by Council and published on the Council's website.
- The Council has an approved Performance Management Framework in place to enable progress to be monitored against the Council's Corporate Plan and Priorities, Single Outcome Agreement, and associated Service Business Plans and Financial Plans and to ensure it reports publicly on its performance.
- The Council responds to findings and recommendations of external audit, scrutiny and inspection bodies and its own independent internal audit section. The Audit & Risk Committee is integral to overseeing independent and objective assurance and monitoring improvements in internal control and governance.
- The Council seeks community views on a wide range of issues and undertakes regular consultation and engagement with citizens and service users.
- The Council's system of internal financial control is based on a framework of financial regulations, regular management information, administrative procedures (including segregation of duties), management supervision and a system of delegation and accountability. In particular, the system includes annually approved revenue and capital financial plans, medium term financial planning, setting and monitoring targets to measure financial performance, and regular reviews of periodic and annual financial reports which indicate financial performance against budgets.

- The Council is committed to the delivery of efficiencies through its transformation programme with the objective to deliver efficient and effective services to customers, whilst maintaining a robust control environment. On an annual basis it identifies efficiency savings to be made within the financial plans, and monitors their achievement on a regular basis.
- The Council is currently undertaking two significant strategic developments involving different structures for delivering its services. Firstly, from 1 April 2015 delivery of the Council's adult care services transferred to SB Cares, a wholly owned subsidiary as a Limited Liability Partnership. Secondly, a feasibility study of options for Cultural services is underway including an option for an integrated sports and culture trust.
- The Council fosters relationships and partnerships with other public, private, and voluntary organisations in delivering services that meet the needs of the local community. Significant work has been undertaken to develop the governance arrangements in respect of the Health and Social Care integration programme with the appointment of the Chief Officer for Health and Social Care Integration in July 2014, the submission of the final Scheme of Integration to Scottish Ministers on 31 March 2015, the establishment of an Integration Joint Board with effect from 2 April 2015, and the commencement on the development of the strategic plan which will become live on 1 April 2016.
- The roles and responsibilities of elected members and officers and the processes to govern the conduct of the Council's business are defined in procedural standing orders, scheme of administration, scheme of delegation, and financial regulations which are regularly reviewed and revised where appropriate.
- In 2014 a new corporate management structure was implemented. Alongside the existing Chief Executive, this created two Depute Chief Executive posts and twelve service directors. In addition there were a number of changes lower down the organisational hierarchy. The roles of officers are defined in agreed job descriptions. Staff performance is reviewed on an annual basis in accordance with the performance review and development (PRD) process.
- The Chief Executive is responsible and accountable to the Council for all aspects of management including promoting sound governance, providing quality information/support to inform decision-making and scrutiny, supporting other statutory officers, and building relationships with all Councillors.
- The Chief Social Work Officer (CSWO) provides the Council with professional advice on the discharge of her statutory social work duties. She promotes values and standards of professional practice and acts as the 'agency decision maker' taking final decisions on a range of social work matters including adoption, secure accommodation, guardianship, etc. The CSWO presents an account of this work in an annual report to Council. The report also gives an overview of regulation and inspection, workforce issues and social policy themes over the year and highlights some of the forthcoming challenges.
- The Chief Financial Officer (the Section 95 officer) is responsible for the proper administration of the Council's financial affairs including ensuring appropriate advice is given to the Council on all financial matters, keeping proper financial records and accounts, and maintaining an effective system of internal financial control under the terms of the financial regulations.
- The Service Director Regulatory Services (the Monitoring Officer) is responsible for ensuring that agreed procedures are followed and that all applicable statutes and regulations are complied with. In line with the Council's Monitoring Officer Protocol, an annual report is presented to the Standards Committee on councillors' compliance with the ethical standards framework.
- The Chief Officer Audit & Risk (Head of Internal Audit (HIA)) reports administratively to the Service Director Strategy & Policy, reports functionally to the Audit & Risk Committee, meets regularly with the Chief Financial Officer, and has direct access to the Corporate Management Team. The HIA reports in her own name and retains final edit rights over all internal audit reports and provides an independent and objective annual opinion on the effectiveness of internal control, risk management and governance based on the delivery of an approved plan of systematic and continuous internal audit review of the Council's arrangements.

- The Council has reviewed and refreshed its risk management policy and approach whose main priorities are the robust systems of identification, evaluation and control of risks which threaten the Council's ability to meet its objectives to deliver services to the public.
- The Council has in place business continuity plans which set out the arrangements to ensure it can continue to deliver critical services if an incident of any kind occurs, has in place emergency plans to ensure it responds to any civil emergency in a way which meets the expectations of the Borders community, and is leading a Resilient Communities Initiative to enable communities working together in emergencies.
- The Council has reviewed and refreshed its proactive, holistic approach to tackling fraud, theft, corruption and crime, as an integral part of protecting public finances, safeguarding assets, and delivering services effectively and sustainably.
- The scheme of members' remuneration sets out the terms of remuneration of elected members. Details of all members' allowances and expenses are published.
- Personal development plans for elected members are being developed and these will be periodically supplemented by additional training further to the comprehensive Induction programme. Members appointed to certain committees have also received specific training related to the responsibilities on these committees e.g. licensing, planning, audit, pensions, employment.
- Codes of conduct are in place for, and define the standards of behaviour expected from, elected members and officers to make sure that public business is conducted with fairness and integrity.
- A range of systems and procedures are in place to ensure that elected members and employees are not influenced by prejudice or conflicts of interest in dealing with our citizens. A register of elected members' interests is maintained and published on the Council's website.

Review of Framework

The Council conducts an annual review of the effectiveness of its overall governance framework which is presented to the Audit & Risk Committee whose role includes high level oversight of the Council's governance, risk management, and internal control arrangements.

The review is informed by the work of an officer self-evaluation working group on corporate governance which undertakes an annual self-assessment against the Council's Local Code of Corporate Governance. This group has responsibility for monitoring compliance with the Local Code and making recommendations to ensure continuous improvement of the systems in place.

The review is also informed by assurances from the depute chief executives and service directors who have responsibility for the development and maintenance of the governance environment within their departments and services and who in turn identify actions to improve governance at a departmental level, the Chief Officer Audit & Risk's annual report on the work of internal audit and independent opinion on the adequacy and effectiveness of the systems of internal control and governance, and by comments made by external auditors and other external scrutiny bodies and inspection agencies.

The conclusion from the review activity outlined above is that in 2014/15 the Council continued to demonstrate that the governance arrangements and framework within which it operates are sound and effective.

The review has however identified a number of areas where further improvement in our governance arrangements can be made to ensure full compliance with our Local Code:

(a) The ongoing implementation of recommendations made by Internal Audit, External Audit and other external scrutiny and inspection bodies relating to internal control and governance, with particular emphasis on prompt implementation of high priority recommendations.

(b) Further implementation of approved governance arrangements associated with the Integration programme for Health & Social Care, ensuring delivery of structural reforms in local authority and NHS services in compliance with new legislation and regulations.

(c) In light of the ongoing significant challenges in addressing cost pressures and responding to the changes in government funding: (i) ensuring that financial, workforce and business plans are aligned to the Council's corporate plan and priorities, (ii) ensuring that options are fully appraised for alternative models and structures to enable delivery of efficient and effective services to customers in a sustainable way, and (iii) continuing to implement the welfare reform programme.

(d) Ongoing implementation of the Performance Management Framework to ensure performance measurement accurately and effectively linked to the delivery of the Single Outcome Agreement and the Council's Corporate Plan and Priorities informs improvement activity and decision making.

(e) Development and application of appropriate self-assessment processes in all Council services as a self-evaluation tool to demonstrate achievement of Best Value.

(f) Evaluation of the new Committee structure arising from the 2014 review within 12 months of its operation to assess the effectiveness of elected member scrutiny of plans and performance.

(g) Ongoing development of written guidelines and procedures of the key financial planning, management and administration processes linked to the Financial Regulations and provision of financial training to managers and budget holders across the whole Council.

(h) Consistent application across all the activity in the Corporate Transformation Programme of the demonstrated key success factors including the robust definition of Business Case and Benefits, Return on Investment, and Programme and Change Management to ensure there is confidence of the delivery of improvements and savings.

(i) Ensuring comprehensive information management across the Council and within each department in all relevant aspects of service delivery through appropriate awareness of and adherence to procedures, practices and guidelines to ensure full compliance with legislation and regulations.

(j) Monitoring and review to ensure there is a consistent approach to staff performance review and development (PRD) in all Council services, and roll out workforce planning and succession planning across the Council as part of its people management arrangements.

(k) Capturing compliments and other comments to gather a wide range of feedback from service users to complement the arrangements in place for dealing with complaints.

(l) Reviewing strategic asset management plans to inform investment in assets and infrastructure to ensure they are fit for the future and enhancing ongoing delivery of capital programmes and projects linked to corporate transformation programme.

These actions to enhance our governance arrangements in 2015/16 are incorporated where appropriate within the Council's business plans and their implementation and operation will be monitored in order to inform our next annual review.

Certification

It is our opinion that reasonable assurance can be placed upon the adequacy and effectiveness of Scottish Borders Council's systems of internal control and governance. Although areas for further improvement have been identified the annual review demonstrates sufficient evidence that the Council's Local Code of Corporate Governance is operating effectively and that the Council complies with that Code in all significant respects.

Tracey Logan Chief Executive mm 2015	Councillor David Parker Leader of the Council mm 2015

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ITEM NO. 7

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PENSION FUND ANNUAL GOVERNANCE STATEMENT 2014/15

Report by Chief Financial Officer

AUDIT & RISK COMMITTEE

11 May 2015

1 PURPOSE AND SUMMARY

1.1 This report proposes that the Audit & Risk Committee considers and approves the Pension Fund Annual Governance Statement that will be published in the Statement of Accounts 2014/15 of Scottish Borders Council Pension Fund.

1.2 The Local Government Pension Scheme (Scotland) Regulations 2014 require Administering Authorities to measure their governance arrangements set out against standards set by Scottish Ministers. These standards are established via a number of best practice principles.

1.3 Part of the Audit & Risk Committee's remit is to assess the effectiveness of internal controls, risk management, and governance arrangements in place for the Scottish Borders Council Pension Fund and this includes being satisfied that the Pension Fund Annual Governance Statement demonstrates compliance with its governance policy and best practice principles and identifies any actions required to improve governance arrangements.

1.4 The Pension Fund Annual Governance Statement 2014/15 details the Governance Framework including the key elements of the Pension Fund's governance arrangements and the Review Framework, as shown in Appendix 1.

1.5 In terms of overall corporate governance it is the Chief Financial Officer's opinion that the overall governance arrangements of the Pension Fund are considered sound. The Annual Governance Statement is informed by the self-assessment of the Fund's compliance with the best practice principles, the work of professional accountancy staff, and the work of internal audit, external audit and inspection agencies. Improvement actions are identified. This statement will be published in the Pension Fund Annual Report and Accounts for the year to 31 March 2015.

2 RECOMMENDATIONS

2.1 It is recommended that the Audit & Risk Committee considers the details of the Pension Fund Annual Governance Statement at Appendix 1, and approves the actions identified by Management to further improve internal controls and governance arrangements.

3 BACKGROUND

3.1 The Local Government Pension Scheme (Scotland) Regulations 2014 require Administering Authorities to measure their governance arrangements set out against standards set by Scottish Ministers. These standards are established via a number of best practice principles.

3.2 Part of the Audit & Risk Committee's remit is to assess the effectiveness of internal controls, risk management, and governance arrangements in place for the Scottish Borders Council Pension Fund and this includes being satisfied that the Pension Fund Annual Governance Statement demonstrates compliance with its governance policy and best practice principles and identifies any actions required to improve governance arrangements.

4 PENSION FUND ANNUAL GOVERNANCE STATEMENT

4.1 The Pension Fund Annual Governance Statement 2014/15 details the Governance Framework including the key elements of the Pension Fund's governance arrangements, which is shown in Appendix 1. It also sets out the Review Framework outlining the annual review process to assess the Fund's compliance with its Governance Policy and the best practice principles, overall opinion and areas of further improvement.

4.2 In terms of overall corporate governance it is the Chief Financial Officer's opinion that the overall governance arrangements of the Pension Fund are considered sound. The Annual Governance Statement is informed by the self-assessment of the Fund's compliance with the best practice principles, the work of professional accountancy staff, and the work of internal audit, external audit and inspection agencies. The annual review demonstrates sufficient evidence that the Pension Fund's Governance Policy is operating effectively and that the Pension Fund fully complies with the best practice principles. Improvement actions are identified. This statement will be published in the Pension Fund Annual Report and Accounts for the year to 31 March 2015.

5 IMPLICATIONS

5.1 Financial

(a) There are no direct financial implications arising from this report.

5.2 Risk and Mitigations

(a) The Pension Fund Annual Governance Statement details areas where additional work would further enhance the internal control environment, risk management, and corporate governance arrangements. Implementing this work will ensure that internal controls, risk management, and other governance arrangements remain sound.

5.3 Equalities

(a) It is anticipated there will be no adverse impact due to race, disability, gender, age, sexual orientation or religious/belief arising from the work contained in this report.

5.4 Acting Sustainably

(a) There are no direct economic, social or environmental issues with this report.

5.5 **Carbon Management**

(a) There are no direct carbon emissions impacts as a result of this report.

5.6 **Rural Proofing**

(a) This report does not relate to new or amended policy or strategy and as a result rural proofing is not an applicable consideration.

5.7 **Changes to Scheme of Administration or Scheme of Delegation**

(a) No changes to the Scheme of Administration or Scheme of Delegation are required as a result of this report.

6 CONSULTATION

6.1 The Monitoring Officer, the Chief Legal Officer, the Service Director Strategy and Policy, the Chief Officer Audit & Risk, the Chief Officer HR, and the Clerk to the Council are being consulted on the report and any comments received will be reported at the meeting.

Approved by

David Robertson
Chief Financial Officer **Signature ……………………….....**

Author(s)

Name	Designation and Contact Number
Jill Stacey	Chief Officer Audit & Risk Tel: 01835 825036

Background Papers: Local Government Pension Scheme (Administration) (Scotland) Regulations 2008
Previous Minute Reference:

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. Jill Stacey, Chief Executive's Directorate can also give information on other language translations as well as providing additional copies.

Contact us at Jill Stacey, Chief Executive's Directorate, Scottish Borders Council, Council Headquarters, Newtown St Boswells, Melrose, TD6 0SA
Tel: 01835 825036 jstacey@scotborders.gov.uk

Appendix 1

Scottish Borders Council Pension Fund
Annual Governance Statement 2014/15

Introduction

The Local Government Pension Scheme (Scotland) Regulations 2014require Administering Authorities to measure their governance arrangements set out against standards set by Scottish Ministers. These standards are established via a number of best practice principles.

The Governance Framework

The key document summarising the governance arrangements for the Pension Fund is the Governance Policy which is contained in Annex 1, and also available on the website www.scotborders.gov.uk/pensions. The Pension Fund Governance Policy provides the framework against which compliance is measured.

The key elements of the Pension Fund's governance arrangements include:

- Scottish Borders Council is the Administering Authority for the Local Government Pension Scheme set up for the Scottish Borders geographic area.
- The Council has delegated its pension's functions to the Pension Fund Committee. The members of the Committee act as quasi-trustees and oversee the management of the Scottish Borders Council Pension Fund.
- The Pension Fund appoints professional advisers and external service providers.
- The system of internal financial control operates within a financial strategy and is based on a framework of delegation and accountability for officers and elected members embodied in procedural standing orders, financial regulations, scheme of delegation, scheme of administration, supported by a framework of administrative procedures including the segregation of duties, and regular financial management information. In particular, the system includes comprehensive accounting systems that record income and expenditure for both member and investment activities, regular reviews of investment reports that measure investment returns against agreed benchmarks, regular reviews of investment manager reports that measure performance against agreed targets, and independent performance reviews of the Fund by the Fund's investment consultant and performance monitoring services provider.
- The Chief Financial Officer (Section 95 officer) for the Council is responsible for ensuring the proper administration of the financial affairs of the Pension Fund. This includes ensuring appropriate advice is given to the Pension Fund on all financial matters, keeping proper financial records and accounts, and maintaining an effective system of internal financial control.
- The Chief Officer HR for the Council is responsible for the pension benefit policy oversight and day-to-day administration of member benefits in accordance with statutory legislation.
- The Chief Officer Audit & Risk (Head of Internal Audit (HIA)) reports administratively to the Service Director Strategy & Policy, reports functionally to the Audit & Risk Committee, meets regularly with the Chief Financial Officer, and has direct access to the Corporate Management Team. The HIA reports in her own name and retains final edit rights over all internal audit reports and provides an independent and objective annual opinion on the effectiveness of internal control, risk management and governance based on the delivery of an approved plan of systematic and continuous internal audit review of the Council's arrangements.
- The Pension Fund responds to findings and recommendations of external audit, scrutiny and inspection bodies and its own independent internal audit section. The Audit & Risk Committee is integral to overseeing independent and objective assurance and monitoring improvements in internal control and governance.

Review of Framework

The Council as Administering Authority of the Pension Fund conducts an annual review of the effectiveness of its overall governance framework which is presented to the Audit & Risk Committee whose role includes high level oversight of the Pension Fund's governance, risk management, and internal control arrangements.

The review is informed by the work of an officer assessment of the Fund's compliance with the best practice principles.

The review of the effectiveness of the system of internal financial control is informed by the work of professional accountancy staff within the Council, the assurances from the Chief Officer Audit & Risk's annual internal audit opinion and report on the work internal audit, and by the external auditors' reports.

The conclusion from the review activity outlined above is that in 2014/15 the Pension Fund continued to demonstrate that the governance arrangements and framework within which it operates are sound and effective.

The review has however identified some areas where further improvements in internal controls and governance arrangements can be made:

a) The ongoing implementation of recommendations made by Internal Audit and External Audit, with particular emphasis on prompt implementation of high priority recommendations.
b) Development of a communications plan to improve awareness and understanding of stakeholders and encourage maximum membership of the Fund.
c) Development of a business plan to improve planning and monitoring of the performance of the Fund.
d) Implementation of new governance arrangements in response to reforms including committee structure, review of pensions' administration strategy, and training policy.
e) Work to fully evaluate the implications of new national policy on freedom of choice of pension sums.

Certification

It is my opinion that reasonable assurance can be placed upon the adequacy and effectiveness of Scottish Borders Council Pension Fund's systems of internal control and governance. Although areas for further improvement have been identified the annual review demonstrates sufficient evidence that the Pension Fund's Governance Policy is operating effectively and that the Pension Fund fully complies with the best practice principles.

Signed
David Robertson CPFA
Chief Financial Officer
xx 2015

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HOUSING BENEFIT OVERPAYMENT AND DEBT RECOVERY REPORT

Report by Service Director Neighbourhood Services

AUDIT & RISK COMMITTEE

11 May 2015

1 PURPOSE AND SUMMARY

1.1 **This report details the activity on Housing Benefit (HB) overpayments and debt recovery as requested by the Audit Committee at its meeting on 23 September 2014. The report provides an update on the performance during 2014/15 in comparison to 2013/14.**

1.2 The value of overpayments outstanding at the start of quarter 4 of 2014/15 is £1.4m in comparison to 2013/14 when it was £1.3m.

1.3 During 2013/14, SBC made awards of Housing Benefit totalling £30m. Of this, £746,340 (2.5%) was subsequently classed as overpaid. The awards for 2014/15 also totalled £30m however the percentage of Housing Benefit overpaid increased to 3.3%.

1.4 In comparison with all 32 Scottish Local Authorities, SBC have the 10th lowest level of total overpayments outstanding at the start of quarter 2 of 2014/15 financial year.

2 RECOMMENDATIONS

2.1 **I recommend that the Committee:-**

(a) notes the comparative activity relating to Housing Benefit overpayments and debt recovery during the period 1 April 2013 to 31 March 2014 and 1 April 2014 to 31 March 2015;

(b) notes the intended improvement actions outlined in the report;

(c) requests that a further performance report be brought back to the Committee in six months.

3 BACKGROUND

3.1 Housing Benefit is administered by local authorities on behalf of the Department for Work and Pensions (DWP). Each year Scottish Borders Council (SBC) pays out housing benefit in the region of £30m to approximately 8,400 claimants. In terms of funding, Local Authorities are paid "subsidy" in respect of Housing Benefit both paid and overpaid.

3.2 Overpayments arise where claimants are paid benefit to which they are not entitled and are caused by a number of reasons. The main reasons are as follows:

(a) Claimant error – this is by far the most common reason and is due to claimants either providing incorrect information at the time of their claim or by not informing the Council of a change in their circumstances at the time the change occurs;

(b) Local Authority error and administrative delay - for example not acting on a notified change of circumstances on time;

(c) Fraud – where benefit has knowingly been claimed based on incorrect information.

3.3 The value of overpayments is an indication of the level of fraud and error in the benefits system and under the duty to protect public funds, local authorities must take appropriate steps to ensure that overpayments are minimised and when they do occur that recovery is sought.

3.4 In terms of subsidy for overpayments, for example, caused by claimant error, local authorities receive 40% subsidy on any overpaid benefit. However, local authorities are penalised where overpayments are caused by 'local authority error and administrative delay' overpayments and reach trigger levels determined by the DWP. These are expressed as a percentage of the value of correct payments and are calculated as follows:

(a) Less than or equal to 0.48% - 100% subsidy

(b) Between 0.48% and 0.54% - 40% subsidy

(c) Above 0.54% - nil subsidy

3.5 There are a number of options available for local authorities to recover overpayments. The most efficient and effective method is recovery from ongoing deductions when the claimant is still entitled to Housing Benefit. Where those deductions are not an option, local authorities can pursue overpayments by, for example, invoicing, recovery from certain other DWP Benefits or engaging external debt recovery agents.

4 PERFORMANCE

4.1 As shown in table 1 below the value of overpayments outstanding to SBC was £1.5m at the start of quarter 4 2014/15. This is a cumulative figure covering all overpayments which have been identified over a number of years and remain outstanding.

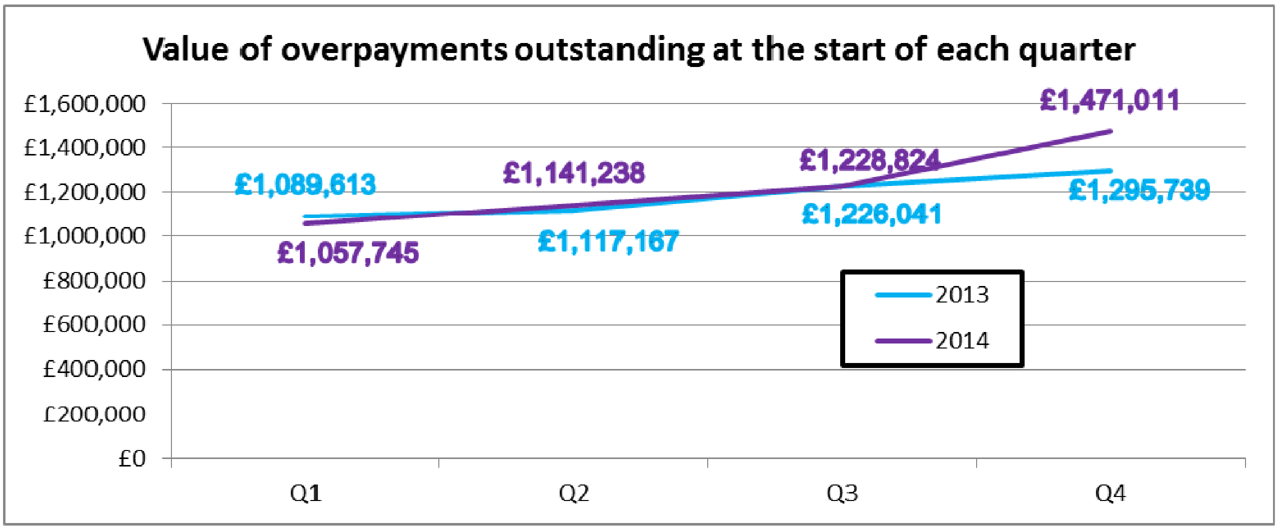

Table 1

4.2 Table 1 shows a fluctuation in the value of outstanding overpayments each quarter compared to the same period the previous year.

4.3 Table 2 below shows the increase in the level of overpayments identified in quarter 3 and 4 of this year which reflects the impact of a new initiative, (Real Time Information) introduced by the DWP, to improve the speed and quality of information available to reassess benefit claims.

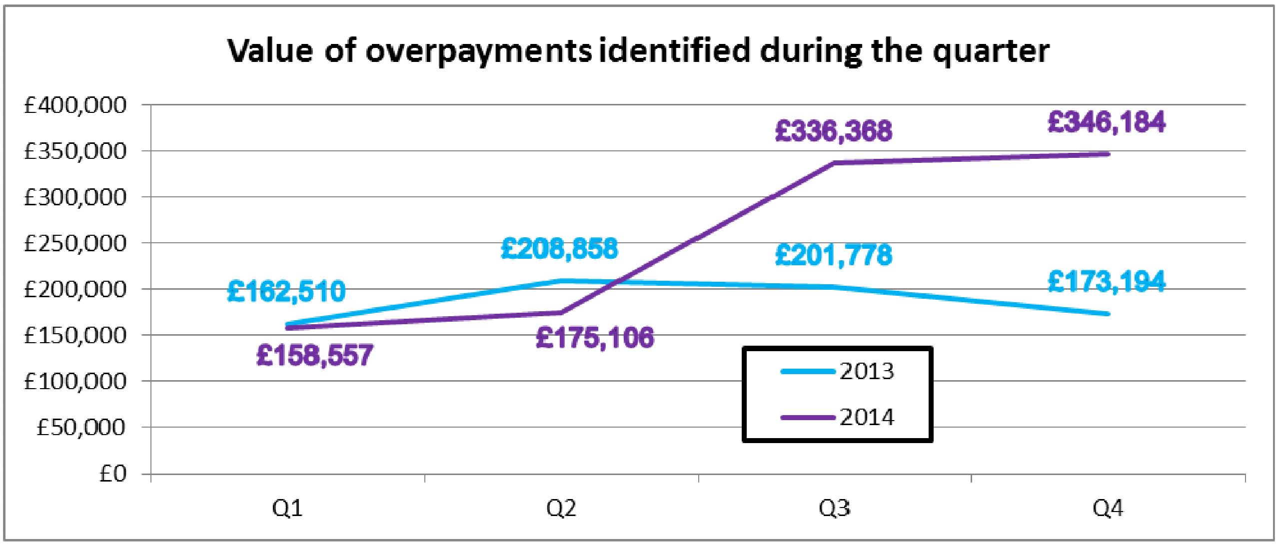

Table 2

4.4 This allows local authorities access to information on earnings and private pensions from HMRC via 'Real Time Information'. The first data exchange supplied in September 2014 included changes back to April 2013 resulting in the large increase in identified overpayments in quarter 3 of 2014/15. The initiative was temporary to 31 March 2015 however it has been extended into 2015/16. This will continue to produce overpayments but of lesser amounts and will help ensure the correct entitlement is being paid to the claimant.

4.5 During 2013/14, SBC made awards of Housing Benefit totalling £30m. Of this, £746,340 (2.5%) was overpaid. The percentage of Housing Benefit overpaid during 2014/15 has increased to 3.3% on the same level of spend (£30m).

Year	Overpayments Identified	Overpayments Recovered	% of debt recovered in year
2013-14	£746,340	£489,979	65.7%
2014-15	£1,016,215	£522,311	51.4%

Table 3 (source DWP HBRF)

4.6 The table above demonstrates that SBC have recovered 65.7% of overpayments identified during 2013/14. This has decreased during 2014/15 to 51.4%. Action is proposed at paragraph 6 onwards to address that downward trend.

5 BENCHMARKING

5.1 Every quarter, each Local Authority is required to provide a Housing Benefit Recoveries and Fraud (HBRF) return to the DWP. A link to those figures including those published on 10 September 2014 for 2013/14 can be found here https://www.gov.uk/government/collections/housing-benefit-recoveries-and-fraud-data

5.2 The data in Appendix 1 table 1 demonstrates that SBC's value of outstanding overpayments during 2013/14 at the start of each quarter is similar to Inverclyde and is at the median level for the Councils compared. The value of overpayments created by each Local Authority fluctuates quarterly so comparisons are of limited value.

5.3 Table 2 reflects that during quarter 1 of 2013/14, Scottish Borders Council identified a low number of overpayments compared to other councils. This increases substantially during the other 3 quarters.

5.4 The data in table 3 demonstrates that Scottish Borders Council recovered a low amount of overpayments during quarter 1. However, this increased during the other 3 quarters and during quarter 2 when we recovered a similar amount to Inverclyde.

5.5 Table 4 shows that the net amount written off by SBC during each quarter of 2013/14 was £6,000 or less which compares favourably with the comparator Councils.

5.6 As detailed in Audit Scotland's report 'Review of auditors' housing benefit subsidy claim reported errors 2013/14' five councils in Scotland exceeded either the lower or higher threshold for local authority and administrative delay overpayments. SBCs performance relating to local authority error and administrative delay overpayments is 0.21%, well below (15th best in Scotland) the lower threshold resulting in 100% subsidy.

5.7 In comparison with all 32 Scottish Local Authorities, SBCs performance is within the top third of Scottish Local Authorities in terms of achieving the lowest total amounts of overpayments outstanding at the start of quarter 2 of 2014/15 financial year.

5.8 The amount of overpayments recovered during the first 2 quarters of 2014/15 totals circa. £235k. SBC falls within the top performing half of all Scottish Local Authorities for the percentage of overpayments recovered against overpayments identified during the first 2 quarters of 2014/15

6 IMPROVEMENT PLAN

6.1 Officers will evaluate the current recovery methods and agree the best combination of methods to be utilised in the future.

6.2 Officers will utilise funding received under the Fraud and Error Reduction Incentive Scheme (FERIS) to carry out more reviews to ensure the correct rate of entitlement is in payment but also to target areas where work will improve collection levels. Whilst the FERIS scheme is likely to identify more overpayments the level of each is likely to be lower leading to a reduction in the level of overall increase. The DWP has extended the submission of Real Time Information scheme into 2015/16 therefore the impact is likely to continue in the same manner i.e. an increase in the number of overpayments created but at lower amounts.

6.3 Staffing initiatives are being implemented to direct experienced staff resources onto collection of Housing Benefit overpayments whilst maintaining ongoing workloads through post backfilling.

6.4 Revised monitoring and responsibility arrangements are being drafted along the lines of the monthly Council Tax collection monitoring to set and achieve monthly and annual targets focussed on reducing the outstanding debt levels.

6.5 The mid year renegotiation of the Sheriff Officers contract currently in its early stages will allow an option to change collection arrangements to give greater emphasis to Housing Benefit overpayment recovery.

7 IMPLICATIONS

7.1 Financial

(a) There are no costs attached to any of the recommendations contained in this report. However, there are financial implications from the creation of Housing Benefit overpayments.

(b) When an overpayment is created as a result of Local Authority error, the amount of subsidy paid to SBC depends on the level of our total Local Authority error overpayments compared to the total amount of Housing Benefit SBC has paid out.

(c) Where that percentage is less than 0.48% subsidy is paid at the rate of 100%. Where the percentage is more than 0.54% the subsidy paid is nil. Between 0.48% and 0.54% the subsidy paid is 40%

(d) When an overpayment is created for claimant error the subsidy paid to SBC is 40% for example, if the overpayment was £100, we would receive £40 subsidy.

(e) When we recover most types of overpaid Housing Benefit, either in part or in full, including in the examples at 7.1 (c) and (d) those funds recovered are retained by the Council.

(f) There are various other categories where differing levels of subsidy may apply however the examples at 7.1 (c) and (d) and the provision covered at 7.1(e) illustrate how the identification of and proper categorisation of overpaid Housing Benefit together with debt recovery action can amount to an income stream for the Council. Conversely these may result in budget shortfalls if expected identification, processing, error rate and recovery targets are not achieved.

7.2 Risk and Mitigations

(a) As the roll out of Universal Credit begins, the number of new overpayments will gradually diminish however if a bulk transfer of cases is implemented at some stage, the level of new overpayments will reduce significantly from that point in time.

(b) An alternative route of collection from Universal Credit will arise for cases no longer in receipt of Housing Benefit. This may mean the level of overpayment debt recovery may slow as individual debtor action will be required rather than automatic deduction from ongoing Housing Benefit entitlement.

7.3 Equalities

There are no adverse equality implications.

7.4 Acting Sustainably

There are no economic, social or environmental implications.

7.5 Carbon Management

There are no effects on carbon emissions.

7.6 Rural Proofing

This is not a new or amended policy or strategy.

7.7 Changes to Scheme of Administration or Scheme of Delegation

There are no changes to the Scheme of Administration or the Scheme of Delegation required.

8 CONSULTATION

8.1 The Chief Financial Officer, the Monitoring Officer, the Chief Legal Officer, the Service Director Strategy and Policy, the Chief Officer Audit and Risk, the Chief Officer HR, and the Clerk to the Council have been consulted and their comments have been incorporated into the final report.

Approved by

Service Director Neighbourhood Services **Signature …………………………**

Author(s)

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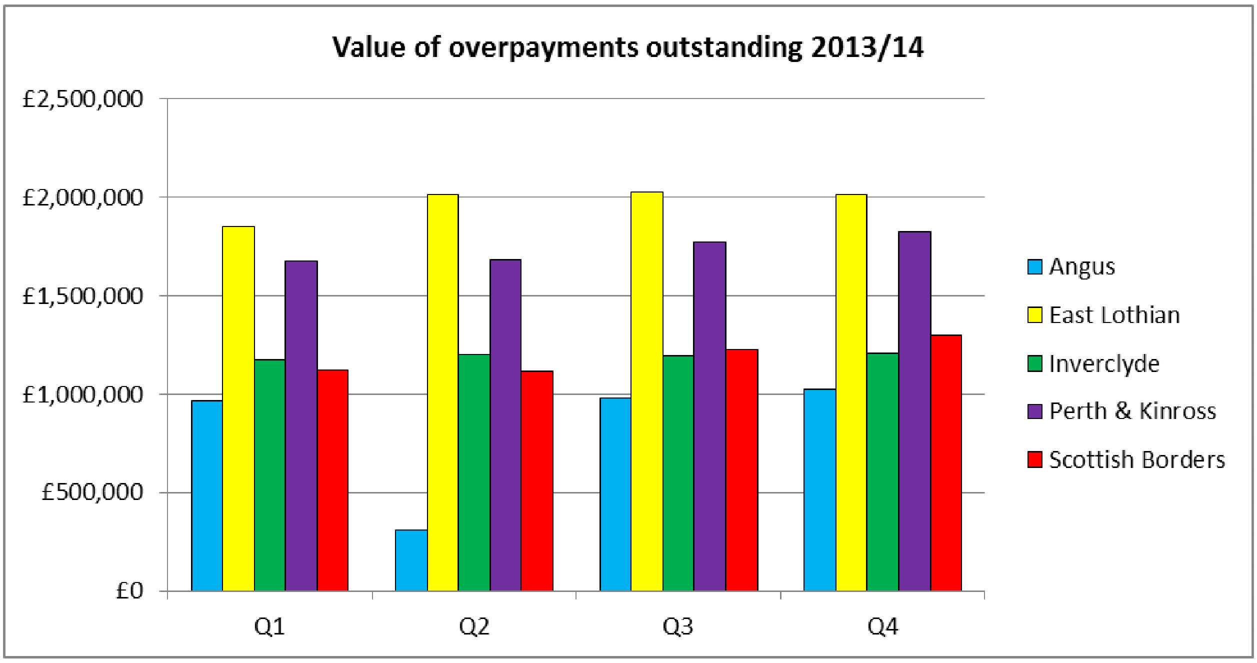
Background Papers: None
Previous Minute Reference: 23 September 2014 Audit Committee

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. Gary Murdie can also give information on other language translations as well as providing additional copies.

Contact us at Scottish Borders Council, Customer Services, Council Headquarters, Newtown St Boswells, TD0 6SA

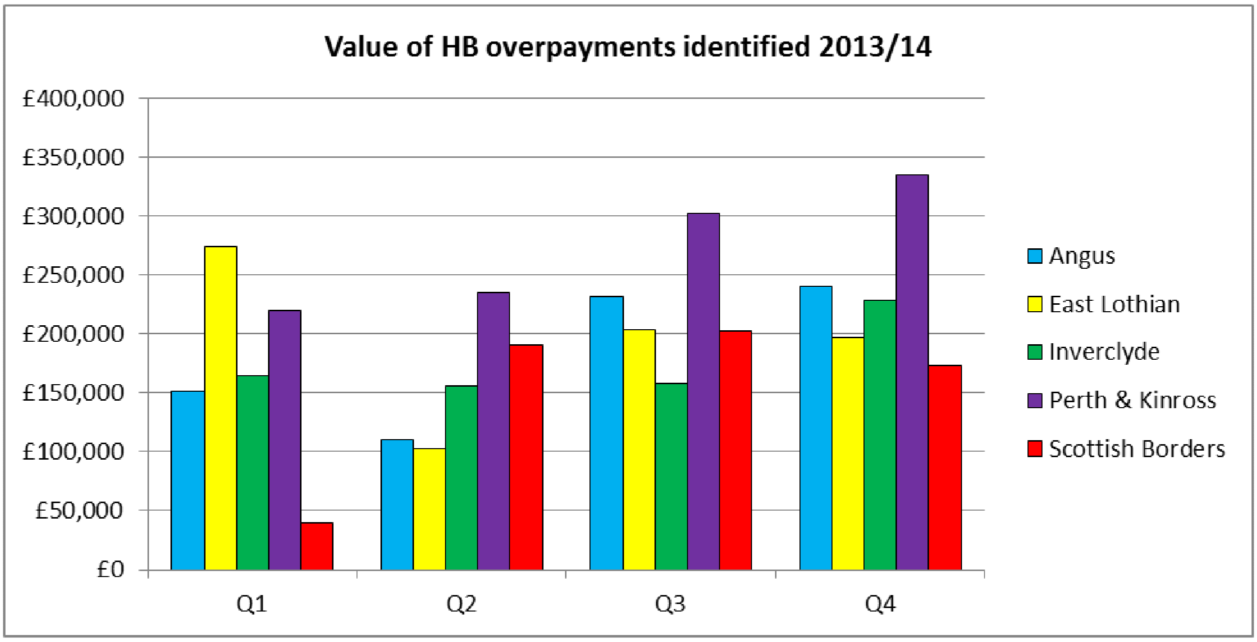
Appendix 1

Table 1



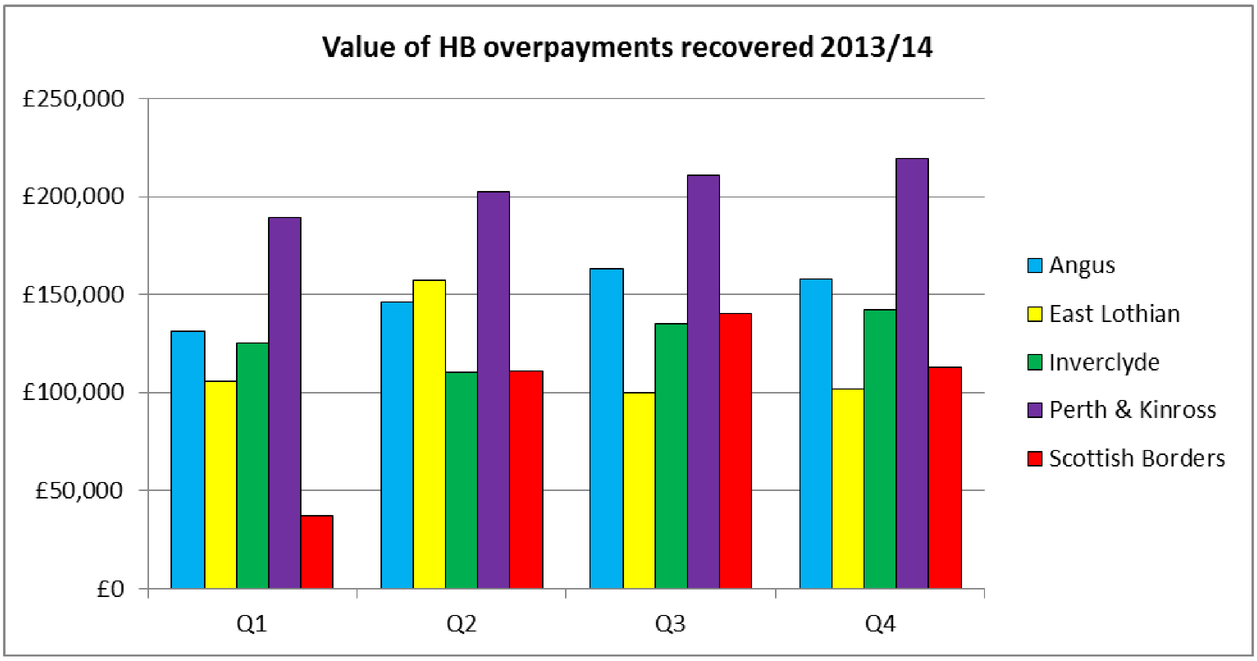
(Source - HB recoveries and fraud data: April 2013 to March 2014)

Table 2



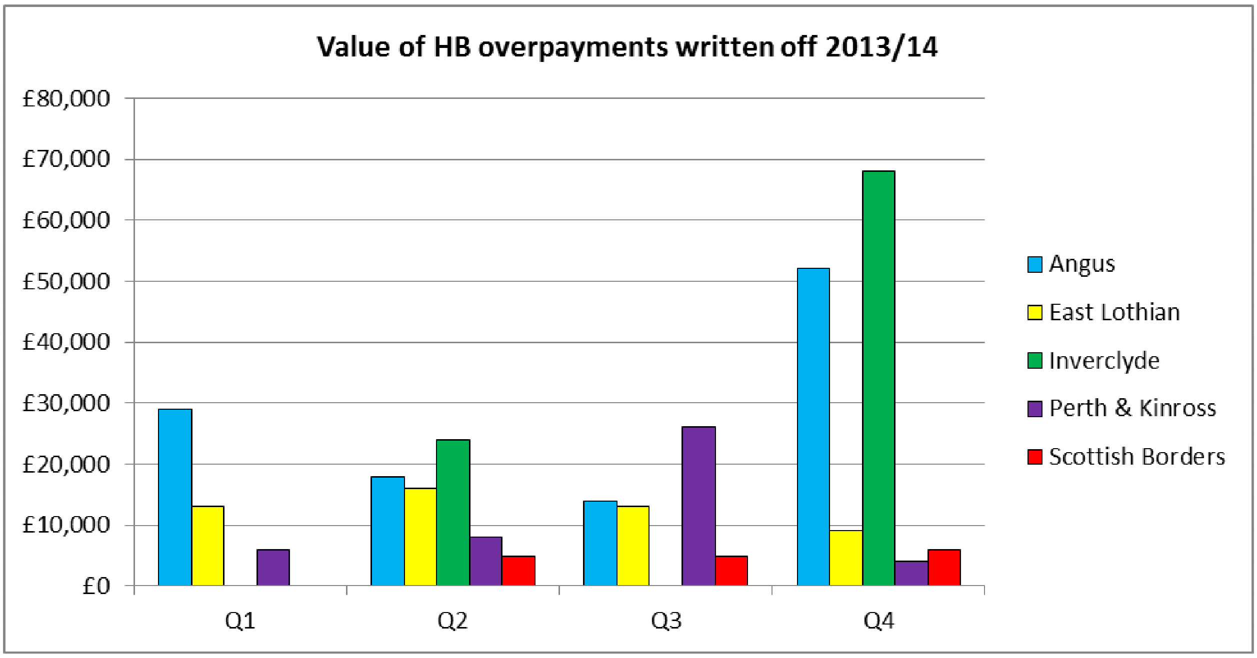
(Source - HB recoveries and fraud data: April 2013 to March 2014)

Table 3



(Source - HB recoveries and fraud data: April 2013 to March 2014)

Table 4



(Source - HB recoveries and fraud data: April 2013 to March 2014)

NB - Where there is no data, the Local Authority has not reported any write offs or has reported a very small amount of write offs during that quarter.

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Review of auditors' housing benefit subsidy claim reported errors 2013/14

AUDIT SCOTLAND

Prepared for Audit Strategy
February 2015

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Introduction

1. Housing benefit (HB) is a means tested social security benefit, administered by local authorities on behalf of the Department for Work and Pensions (DWP). HB is intended to help claimants meet housing costs for rented accommodation both in the private and social rented sector.

2. HB is split into two different categories; rent rebates, where the local authority is the landlord, and rent allowances, where the landlord is for example, either a social sector organisation or a private individual.

3. Local authorities reclaim most of the HB that they pay to claimants by submitting subsidy claims to the DWP that are certified annually by each authority's appointed external auditor. The subsidy claim form details the authority's HB expenditure which is recorded in various cells on the form. These cells include total rent rebate and total rent allowance expenditure and the amounts paid in respect of the total value of overpayments, the value of backdated HB awarded, and the amount of HB paid in respect of customers in temporary accommodation.

4. The HB subsidy scheme has built in incentives to encourage local authorities to take appropriate action to minimise overpayments of HB, expenditure above DWP set limits and administrative delays.

Purpose of report

5. Each local authority's appointed external auditor is required to conclude annually whether the subsidy claim is fairly stated and certify it accordingly. Any errors identified are reported to the DWP in a covering letter that accompanies the final claim.

6. The purpose of this report is to provide insight into the extent to which auditors reported errors during the certification of the 2013/14 HB subsidy claim process, and the type of errors identified that could result in a local authority losing subsidy.

7. Audit Scotland reviewed the subsidy claim covering letters of all 32 Scottish local authorities for 2013/14. The review focused on errors reported by auditors as well as where levels of overpaid HB exceeded DWP thresholds for subsidy.

8. This report sets out the main findings from the review. As well as identifying areas where the DWP may reclaim subsidy from local authorities, it also identifies issues which may be common across a number of local authorities and therefore where attention should be focused in order to maximise subsidy claimed in the future.

Summary of findings

9. During 2013/14, Scottish local authorities paid out £1.772 billion in HB (£1.791billion in 2012/13). The DWP contributed £1.728 billion (£1.748 billion in 2012/13) to this expenditure through subsidy payments.

10. The certification of the 2013/14 subsidy claims by auditors identified errors which resulted in subsidy being over claimed by £0.274 million, 0.01% of expenditure (£0.149 million in 2012/13) which the DWP may decide to reclaim. In addition, five local authorities were unable to claim a total of £0.784 million (£0.809 million in 2012/13) in subsidy as a result of exceeding the pre-agreed DWP threshold limits for local authority and administrative delay HB overpayments.

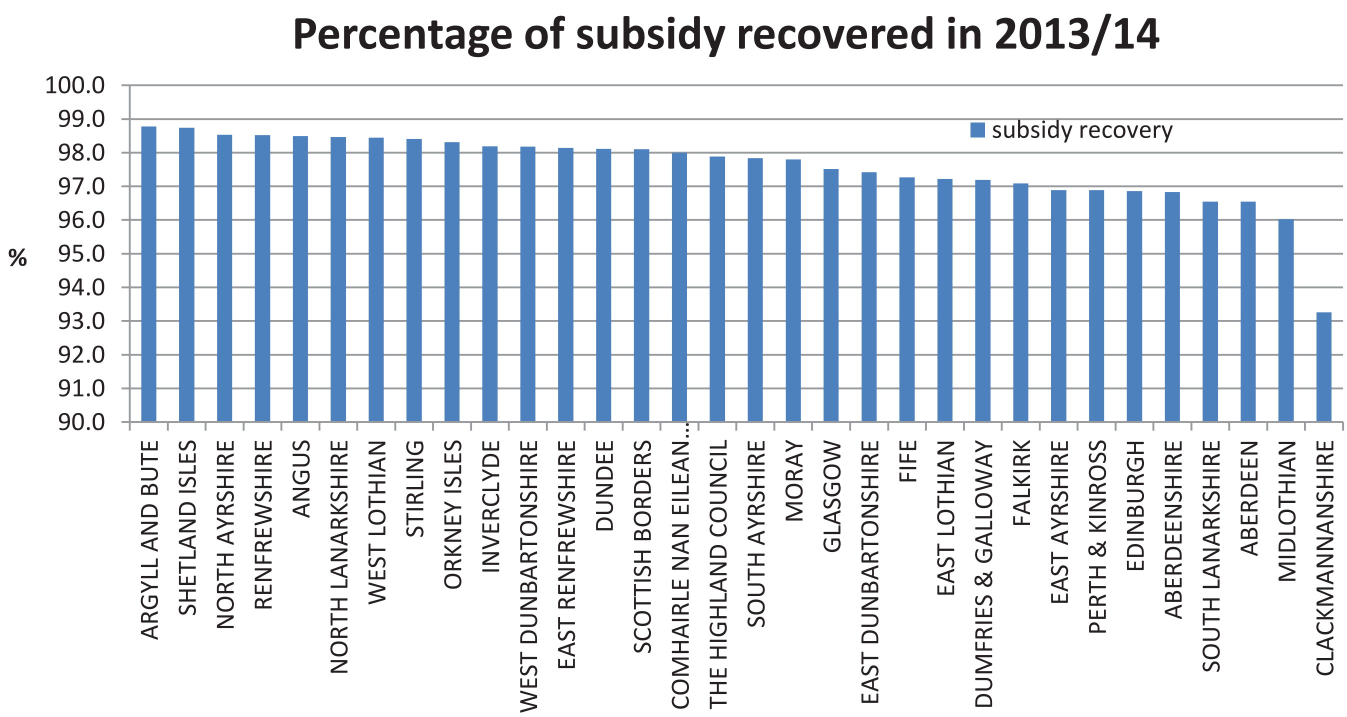
11. Auditors reported 60 errors in their 2013/14 certification letters in respect of 19 of the 32 Scottish local authorities. No issues were identified in the certification of the remaining 13 local authority's subsidy claims. This is an increase in the number of errors reported from 2012/13 where auditors identified 40 errors across 20 local authorities.

12. The areas where most errors were identified were the calculation of claimant income and the classification of overpaid HB. Auditors reported that, in order to help reduce subsidy loss, effective management arrangements should be in place to ensure overpayments, processing errors and administrative delays are minimised and, where they do occur, that overpayments are correctly classified and calculated.

Auditor testing and reporting methodology

13. In 2013/14, £1.772 billion (£1.791 billion in 2012/13) was paid out in HB and £1.728 billion (£1.748 billion in 2012/13) of this expenditure was recovered from the DWP in subsidy. The DWP also pay administration subsidy of £40.8 million (£46.5 million in 2012/13) which is paid to local authorities to administer the HB scheme. As shown in Exhibit 1, the percentage of subsidy recovered (net of administration subsidy) from the DWP varies across local authorities from 93.3% to 98.8%.

Exhibit 1: percentage of HB expenditure recovered through subsidy



Note: Clackmannanshire Council's low recovery rate was partially due to not receiving subsidy on a significant amount of their expenditure on certain types of temporary homeless accommodation.

14. Local authorities should ensure that effective arrangements are in place to review subsidy claims to identify areas for potential improvement. This may include the identification of areas where staff training would be beneficial, proactive monitoring of workloads, and areas requiring additional quality review checks and/or intervention activity.

15. The DWP requires that final subsidy claims are reviewed by external auditors using the HB COUNT testing and reporting methodology.

16. Where auditors identify errors and are unable to conclude that the errors are isolated, HB COUNT methodology requires that an additional sample of cases is tested which is focused on the particular error that had been found.

17. HB COUNT methodology also requires auditors to extrapolate the results of the initial and additional testing by multiplying the subsidy cell (or sub-population) total by the proportion of the sample value that is found to be in error, and agree an amendment to the claim form with the local authority. Where an amendment cannot be agreed, the auditor includes details of the error and testing carried out in their covering letter to the DWP.

2013/14 errors reported

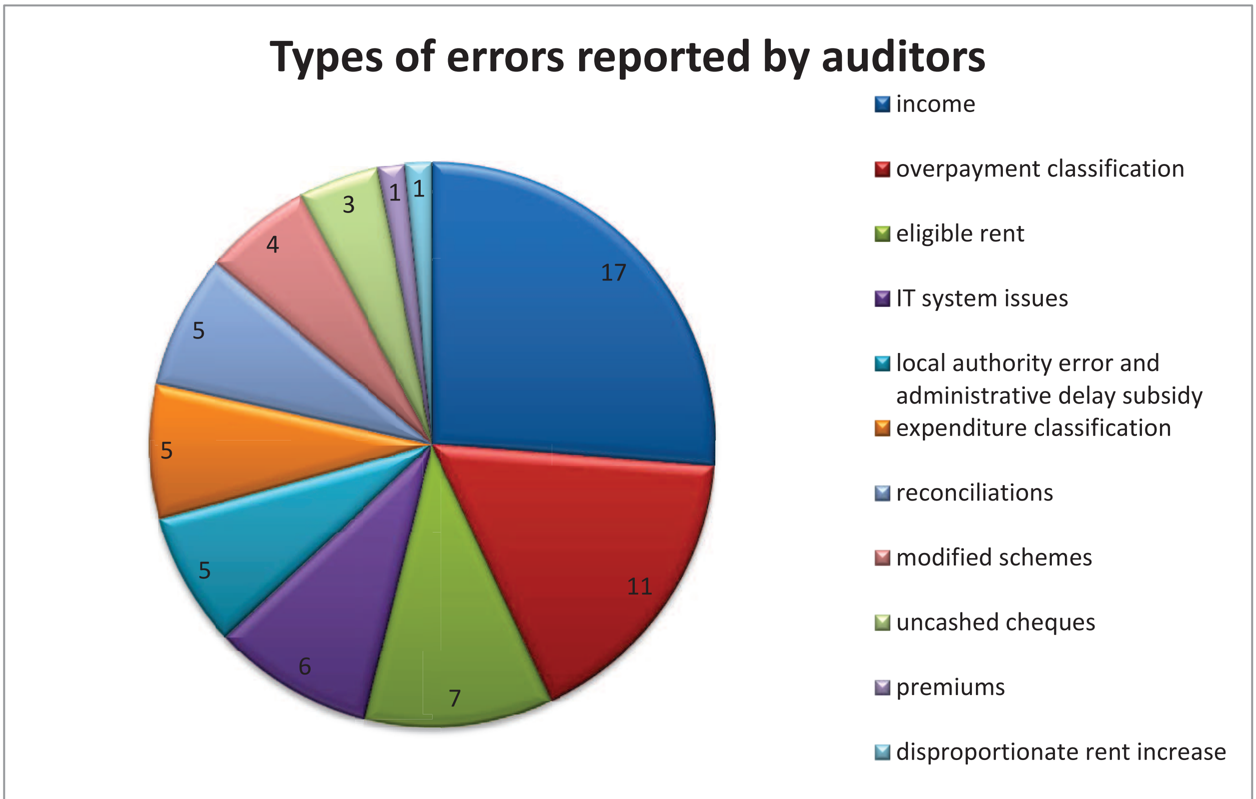
Introduction

18. Auditors reported 60 errors in the covering letters sent to the DWP in respect of 19 of the 32 Scottish local authorities. No issues were identified in the certification of the remaining 13 local authorities' subsidy claims. This is an increase in the number of errors from 2012/13 where auditors reported 40 errors and issues across 20 local authorities. In addition, five local authorities breached the DWP threshold limits for local authority error and administrative delay overpayments in 2013/14 (four in 2012/13).

19. The nature and number of the errors reported, along with the potential impact should the DWP decide to reclaim subsidy in respect of those errors, are discussed in the following paragraphs. Appendix 1 provides further detail of the errors in respect of the eleven local authorities where these errors resulted in overpayments of HB and where there the DWP might potentially reclaim subsidy. If the DWP do decide to reclaim subsidy, over £0.274 million (£0.149 million in 2012/13) may be reclaimed across Scotland. Although, the DWP can reclaim subsidy where overpayments are identified, no additional funding is provided where underpaid benefit is identified by auditors.

20. As shown in exhibit 2 below, the errors identified by auditors in 2013/14 were mainly due to the miscalculation of income and overpayment classification. These errors could equally apply to either rent rebates or rent allowances. In order to help reduce subsidy loss, local authorities should ensure that effective management arrangements are in place to help minimise processing errors, overpayments and administrative delays and, where overpayments have occurred, they are correctly classified and calculated.

Exhibit 2: Types of errors reported by auditors



21. The various types of error identified during the certification of the 2013/14 subsidy claims are discussed in the following paragraphs and referenced to the appropriate cells on the subsidy claim form. Where adjustments could not be made to subsidy claims, the potential impact should the DWP decide to reclaim subsidy in respect of these errors is shown.

22. The auditors' findings demonstrate that the identification of low value errors in their sample testing can result in relatively large amounts of subsidy being reclaimed as a result of the extrapolation process carried out as part of the HB COUNT methodology.

23. Errors reported in covering letters to the DWP that do not affect subsidy for 2013/14 are also discussed because they could also result in a loss of subsidy in the future.

Income

24. Claimant income is a key factor in determining whether a claimant qualifies for HB and, if they qualify, how much benefit they are entitled to received. It is vital therefore, that local authorities accurately calculate claimant income in HB assessments. This area is where auditors identified most errors.

25. A total of 17 errors were reported by auditors in eight local authorities which are detailed in appendix 2. These relate to errors in respect of claimant income, such as salaries, occupational pensions and tax credits, being incorrectly entered in HB entitlement calculations.

26. For example, in one case it was identified that HB had been underpaid by £5.84 as a result of miscalculating the claimant's salary. Additional audit testing identified a further two errors (total value £80). The effect of these errors following extrapolation using HB COUNT methodology was to overstate rent rebate expenditure attracting full subsidy by £27,030 with a corresponding understatement of local authority error and administrative delay overpayments.

27. Local authorities should ensure effective, risk based accuracy checking processes and appropriate training are in place to help minimise errors in the accurate calculation of claimant income.

Overpayment classification

28. The DWP does not fully fund overpayments of HB to encourage local authorities to take due care when processing claims to ensure that they are accurate and also to encourage local authorities to vigorously recover overpayments, where appropriate.

29. HB may be overpaid to claimants for a number of reasons. The subsidy claim form categorises overpayments as follows:

- DWP error
- local authority error and administrative delays
- claimant error (eligible overpayments)
- timing issues (technical overpayments).

30. The type of overpayment affects the amount of subsidy received. For example eligible overpayments receive 40% subsidy and local authority error and administrative delay overpayments can receive up to 100% subsidy.

31. Where local authority error and administrative delay overpayments are less than or equal to the DWP's pre-agreed lower threshold, local authorities receive 100% subsidy (see paragraph 40). Therefore misclassification of overpayments as eligible (i.e. claimant error) instead of local authority error will result, in those local authorities that are below the DWP threshold losing subsidy as only 40% subsidy would have been claimed instead of 100%.

32. The errors that follow relate to the detailed cells where the expenditure was recorded, including local authority error and administrative delay overpayment details which receive a zero subsidy recovery rate.

33. Eleven errors were reported by auditors in five local authorities. These mainly relate to errors where overpayments had been classified as eligible overpayments instead of local authority error.

34. For example, nine eligible overpayments (total value £768.30) were identified in one local authority which had been classified as claimant error when they should have been classified as local authority error. Following extrapolation of these errors using HB COUNT methodology, the effect of these errors was to overstate the value of rent rebate expenditure attracting full subsidy by £1,636.17 and rent rebate eligible overpayments by £40,920.25 with a corresponding understatement in local authority error and administrative delay overpayments of £42,556.42.

35. Local authorities should have effective accuracy checking processes in place to ensure the accuracy of overpayment calculations and classifications. In addition, as a final check, the annual subsidy claim should be reviewed prior to submission to the DWP and auditors for certification. Errors reported by auditors are detailed in appendix 3.

Eligible rent

36. An essential element of every HB calculation is the accurate calculation of the claimant's eligible rent. Eligible rent means the reasonable rent for a suitable property in a particular area. It can include certain service charges (e.g. lift maintenance or a communal laundry) but not charges such as heating, meals, or the provision of furniture. In addition, the introduction by the DWP of the removal of the spare room subsidy (RSRS) for working age social tenants from 2013 resulted in an element of rental payments not being eligible for HB for those claimants whose properties had more rooms than the DWP's size criteria stated that they needed.

37. Seven errors were reported by auditors in five local authorities. These are detailed in appendix 4 and included issues relating to the RSRS , and errors in calculating eligible rent due to, for example, not excluding ineligible service costs.

38. For example, three cases were identified in one local authority where HB had been underpaid (total value £88.30) as a result of incorrect eligible rent figures being used in the HB calculation. Additional testing identified one other case where HB had been overpaid by £627. The effect of these errors was to overstate total rent allowance expenditure, at or below the

rent officer's determination, by £75,788 with a corresponding understatement in local authority error and administrative delay overpayments.

Information Technology (IT) issues

39. HB is a complex benefit to calculate and therefore it is important that HB IT systems operate effectively and system parameters are updated appropriately to ensure that claims are accurately calculated.

40. Seven errors were reported by auditors in five local authorities. These included issues relating to system parameters being incorrectly set. Local authorities should ensure that parameters within the HB system are accurate and agree to all uprating information provided by the DWP in its circulars. When parameters are updated, independent checks should be carried out to ensure that the update is accurate. Errors reported by auditors are detailed in appendix 5.

Local authority error and administrative delay subsidy

41. In April 2004, an initiative was introduced by the DWP to allow local authorities to receive additional subsidy in respect of their local authority error and administrative delay overpayments where the total value of these overpayments was within a specified percentage of the total value of all correct payments made.

42. The level of subsidy that local authorities may claim for local authority error and administrative delay overpayments is determined by these thresholds, expressed as a percentage of the value of correct payments made. The thresholds are as follows:
    - lower threshold 0.48%
    - upper threshold 0.54%.

43. Where the local authority error and administrative delay overpayments are less than or equal to the lower threshold, local authorities receive 100% subsidy. Where they are more than the lower threshold but less than the upper threshold, local authorities receive 40% subsidy on the value of overpayments above the lower threshold. No subsidy is payable on the value of overpayments that are above the upper threshold.

44. As illustrated in exhibit 3 below, five local authorities exceeded the upper threshold in 2013/14 (two local authorities were above the upper threshold with a further two between the upper and lower threshold in 2012/13), with the remaining 27 authorities below the threshold. The total value of local authority error and administrative delay overpayments in respect of these five local authorities was £1,156,048 (£1,187,179 for the four local authorities in 2012/13). As a result no subsidy was paid to these local authorities in respect of these overpayments. The

maximum amount of additional subsidy unable to be claimed was 100% of the lower threshold which equalled £783,849 (£809,042 in 2012/13). The value of subsidy unable to be reclaimed for the individual local authorities ranged from £23,281 to £243,321 (£112,297 to £308,547 in 2012/13).

45. East Ayrshire Council was unable to claim subsidy in 2012/13 due to being above the upper threshold and Falkirk Council also was unable to claim part of their local authority error and administrative delay subsidy in 2012/13 due to being above the lower threshold.

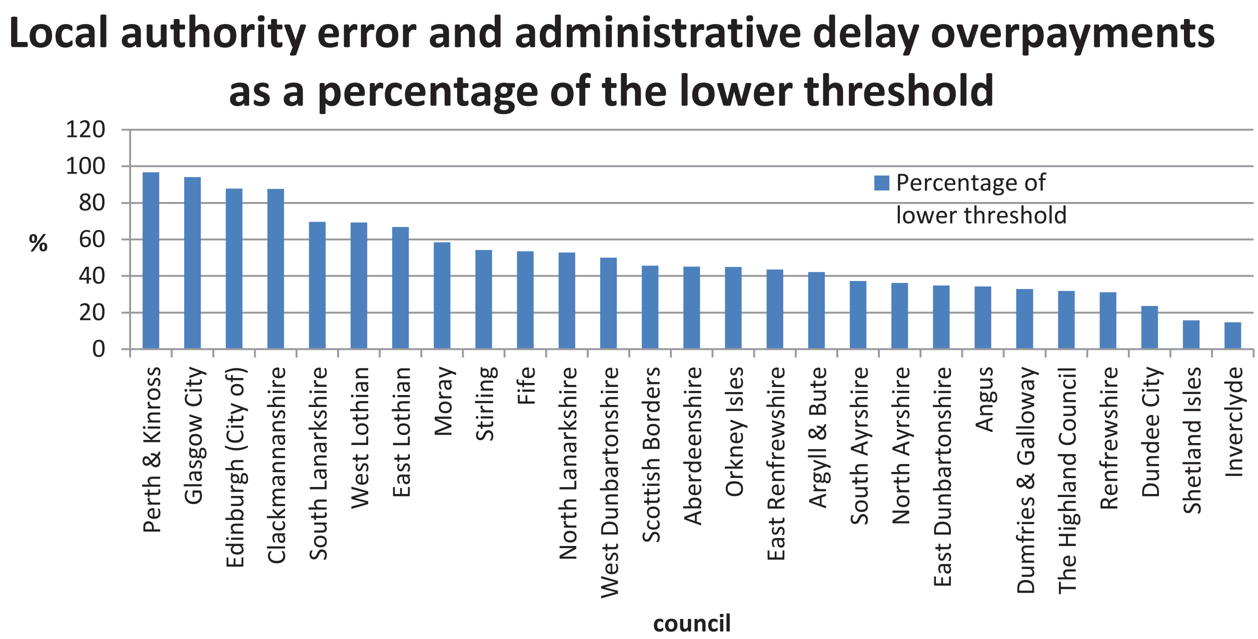
Exhibit 3: Local authority error and administrative delay overpayment subsidy

Local authority	Lower threshold	Upper threshold	Actual overpayments
Aberdeen City	£243,321	£273,739	£303,180
Comhairle nan Eilean Siar	£23,281	£26,191	£31,292
East Ayrshire	£202,986	£228,359	£375,812
Falkirk	£190,662	£214,495	£247,301
Midlothian	£123,599	£139,048	£198,463
TOTAL	**£783,849**		**£1,156,048**

46. As shown in Exhibit 4, a review was undertaken by Audit Scotland of the other 27 local authorities where the level of local authority error and administrative delay overpayments was below the DWPs lower threshold.

47. Local authorities should have arrangements in place to monitor overpayment levels on an on-going basis in order to avoid subsidy loss where possible. Effective accuracy checking processes should also be in place to help minimise errors.

Exhibit 4: local authority error and administrative delay overpayments



Expenditure classification

48. The DWP subsidy claim requires that HB expenditure is correctly classified across the various cells contained in the form. This is particularly important as different types of expenditure attract different rates of subsidy.

49. Five errors were reported by auditors in four local authorities. These are detailed in appendix 6 and include issues relating to rent rebates being classified as rent allowances and vice versa.

50. For example, in one local authority, sample testing of rent rebate cases identified two claims in relation to properties that had been transferred to the control of a local housing association. These claims should have been recorded within the rent allowance cells. Further testing identified that 7.8% of the total value of rent rebates claimed under expenditure in respect of leased or self-contained licensed accommodation should have been recorded in the rent allowances cells resulting in adjustments of £86,374.63 and £7,626.84 being agreed with the local authority.

51. Local authorities should ensure that effective accuracy checking processes are in place to ensure that HB entitlement is accurately calculated and the expenditure is correctly recorded. In addition, local authorities should ensure checks are carried out on subsidy claims prior to being submitted to the DWP and for certification by auditors.

Reconciliations

52. Reconciliations are an important part of the subsidy claim and as part of the certification process, auditors are required to check that benefits granted per the subsidy claim form agree with the reconciliation figures within the HB IT system for the amount of benefit granted and paid. In addition, the subsidy claim form contains an in-year reconciliation cell which is calculated automatically and seeks to confirm that the figure in each total expenditure cell is supported by an analysis of expenditure.

53. Five errors were reported by auditors in four local authorities where there were anomalies in the reconciliation data. Local authorities should ensure that regular reconciliations are carried according to the software suppliers' guidance, and ensure that any issues identified are investigated and rectified. Errors reported by auditors are detailed in appendix 7.

Modified schemes

54. Modified schemes are where a local authority operates a discretionary local scheme to disregard any war pension over and above the statutory disregards. This discretionary expenditure receives subsidy of 0.2% of the total subsidy claimed before any local scheme expenditure and is capped at 75% of the total cost of the discretionary scheme.

55. Four errors were reported by auditors in four local authorities. These included errors regarding the assessment of the claimants' income and software issues. Local authorities again should ensure effective accuracy checking processes are in place to try to minimise errors. In addition, local authorities should ensure checks are carried out on subsidy claims prior to being submitted to the DWP and for certification, and that any issues identified are investigated and rectified. Errors reported by auditors are detailed in appendix 8.

Uncashed cheques

56. Local authorities may pay HB by cheque to claimants and/or landlords. At the year end, an adjustment is required in the subsidy claim form to account for cheques which were issued prior to 1 April 2013 that have not been cashed.

57. Errors were reported by auditors in three local authorities. These relate to uncashed cheques being not included on the subsidy claim form in error as well as the treatment of cheques included on the subsidy claim form. Local authorities should ensure DWP guidance on the completion of subsidy claim forms is reviewed annually and action taken to ensure subsidy claims are completed in accordance with the guidance. Errors reported by auditors are detailed in appendix 9.

Premiums

58. Where a claimant has a special need, there are a number of premiums which can be awarded when entitlement to HB is calculated.

59. Testing in North Lanarkshire Council identified one claim where a carer's premium had been applied in error when calculating the HB award.

60. Additional testing identified one further case (value £220.32) where a carer's premium had been applied in error. The result of this error was to overstate cell 023, rent rebate expenditure attracting full subsidy by £2,297 with a corresponding understatement in cell 026 local authority error and administrative delay overpayments.

Disproportionate rent increase

61. Disproportionate rent increase is where deductions are made in calculating qualifying expenditure for subsidy purposes where a local authority has increased the average rent of local authority tenants receiving rent rebates by a higher percentage increase than the percentage increase in the averages rents of tenants who are not receiving rebates.

62. Local authorities receive exemption from this deduction where it can be demonstrated that the authority has set its rent charges to reflect the characteristics of the individual properties and services rather than the HB status of the tenants.

63. In Angus Council, cell 181b on the subsidy claim form had been completed to reflect that the local authority was seeking exemption from the disproportionate rent increase on the basis of a rent increase by a common percentage. For completeness, cell 180a should also have been completed to reflect that the local authority has open and transparent rent setting policies. This error did not affect subsidy claimed.

Appendix 1

Potential recovery of subsidy by DWP for those local authorities where errors resulted in overpaid HB

Local authority	Error	Rent rebate	Rent allowance	Total potential recovery of subsidy by DWP
Aberdeen	• Earned income errors • Misclassification of overpayments • Occupational pension income errors • Tax credit errors	• £22,886 • £18,004 • £1,147 • £838	• £8,497 • £4,561 • £477	£56,410
Aberdeenshire	• Calculation over a 52 week period instead of a 53 week period	• £15,488		£15,488
Comhairle Nan Eilean Siar	• Income errors • Incorrect eligible rent	• £127 • £81		£208
Dumfries & Galloway	• Earned income error • Misclassification of overpayments	• £55 • £8		£63
East Renfrewshire	• In year reconciliation	• £316	• £316	£632
Fife	• In year reconciliation • Prior year uncashed payments		• £2,971 • £5,985	£8,956
Highland	• Incorrect eligible rent figures • Earned income errors • Prior year uncashed payments	• £27,030	• £75,788 • £5,006	£107,824

Local authority	Error	Rent rebate	Rent allowance	Total potential recovery of subsidy by DWP
Midlothian	• Misclassification of overpayments • Earned income errors	• £615 • £68	• £342 • £15	£1,040
North Lanarkshire	• Incorrect eligible rent-under occupancy deduction errors • Error with a carer's premium • Misclassification of overpayments	• £69,926 • £2,297 • £505	• £116	£72,844
Perth & Kinross	• Child benefit income error	• £212		£212
Stirling	• Earned income errors	• £10,385		£10,385
	TOTAL			**£274,062**

Appendix 2

Details of reported errors relating to income
Aberdeen City Council
Three rent rebate cases (total value £262.31) were identified where HB had been overpaid due to the miscalculation of the claimant's wages. Additional testing identified a further four cases (total value £789.64) where HB had been overpaid, a further two cases where benefit had been underpaid and two cases where the miscalculation of employed earnings did not result in a monetary error. The effect of the error was to overstate cell 023, rent rebate expenditure attracting full subsidy by £22,886.31 with a corresponding understatement in cell 026, local authority error and administrative delay overpayments.
Testing was carried out on rent rebate claimants with occupational pension due to errors identified in previous years. This identified seven rent rebate cases (total value £88.61) where HB had been overpaid. The effect of this error was to overstate cell 023 by £1,147.33 with a corresponding understatement in cell 026.
Testing carried out on rent rebate claims containing Working Tax Credits due to errors identified in previous years, identified two cases (total value £43.54) where HB had been overpaid and a further two cases where HB had been underpaid. The effect of these errors was to overstate cell 023 by £838.12 with a corresponding understatement in cell 026.
Testing identified one rent allowance case where there was a miscalculation of the claimant’s wages. Testing of an additional sample of cases identified a further five cases (total value £607.85) where HB had been overpaid, six cases where benefit had been underpaid, and a further case where an error had no impact on the level of benefit paid. The effect of this error was to overstate cell 102, rent allowance expenditure not requiring referral to the rent officer, by £3,799.14 and cell 103, expenditure administered under local housing allowance rules by £4,698.46 with a corresponding understatement of £8,497.60 in cell 113, local authority error and administrative delay overpayments.
Testing identified ten rent allowance cases (total value £168.03) where HB had been overpaid as a result of the miscalculation of the claimant's earnings from an occupational pension. Additional

Details of reported errors relating to income
testing identified a further four cases where HB had been underpaid and two cases where errors did not result in a monetary error. The effect of this error was to overstate cell 099, rent allowance expenditure administered under rent officer arrangements up to the maximum rent by £8.10 and cell 102, expenditure not requiring referral to the rent officer by £469.66 with a corresponding understatement of £477.76 in cell 113, local authority error and administrative delay overpayments.
Testing identified two cases where an error was made when calculating Employment Support Allowance (ESA). There was no impact on the level of benefit paid.
Comhairle Nan Eilean Siar
Testing identified one case where an incorrect salary was used in the HB calculation. This error however did not impact on the claimant's benefit entitlement. Additional testing identified one case where HB had been underpaid as a result of the authority miscalculating weekly earned income. As there is no eligibility to subsidy for benefit which has not been paid, these errors have not been classified as errors for subsidy purposes.
Testing identified one rent allowance case (£2.91) where HB had been overpaid as a result of applying an incorrect ESA component in the HB calculation, and one case (£0.68) where HB had been overpaid as a result of using an incorrect savings credit amount. Testing of an additional sample of cases identified no further errors. The effect of these errors was to overstate cell 102, rent allowance expenditure not requiring referral to the rent officer, by £127 with a corresponding understatement of cell 113, local authority error and administrative delay overpayments.
Dumfries & Galloway Council
Testing identified one case where the average weekly income for the claimant had been calculated incorrectly. The claimant's average income had been calculated based on 2 four-weekly payslips which had been provided. However, the claimant worked on a 4/4/5 week basis and therefore his average income had not been calculated correctly. As testing of an additional sample of cases identified no further errors, the error was deemed to be an isolated incident. The effect of the error was to overstate cell 014, leased or self-contained licensed accommodation where the local authority is the landlord by £55.45 with a corresponding understatement of cell 026, local authority error and administrative delay overpayments.

Details of reported errors relating to income
The Highland Council
Testing identified one case where HB had been underpaid by £5.84 as a result of miscalculating the claimant's salary. Testing of an additional sample of cases identified two cases where HB had been overpaid benefit (total value £80). The effect of these errors was to overstate cell 023, rent rebate expenditure attracting full subsidy by £27,030 with a corresponding understatement of cell 026, local authority error and administrative delay overpayments.
Midlothian Council
Testing identified one rent rebate case (total value £4.67) where HB was overpaid due to an error in the calculation of the claimant's salary. Additional testing identified one case (total value £2.52) where benefit was overpaid and four cases (total value £58.80) where benefit was underpaid. The combined effect resulted in an understatement of £68.83 in cell 026, local authority error and administrative delay overpayments, with corresponding overstatements of £44.70 in cell 012, board and lodging or non-self-contained licensed accommodation where the local authority is the landlord, and £24.13 in cell 023, rent rebate expenditure attracting full subsidy.
Testing identified one rent allowance case (total value £0.12) where HB had been overpaid due to an error in the calculation of a claimant's salary. Additional testing identified one case (total value £0.75) where benefit was overpaid and one case (total value £0.26) where benefit was overpaid. The effect is an overstatement in cell 102, rent allowance expenditure not requiring referral to the rent officer of £10.44, an overstatement in cell 103, rent allowance expenditure administered under local housing allowance rules, of £5.29, with a corresponding understatement of £15.73 in cell 113, local authority error and administrative delay overpayments.
Testing identified one case (total value £0.56) where HB had been underpaid due to the wrong tax credit amount being applied. Additional testing identified one case (total value £0.13) which again resulted in an underpayment of benefit. As there is no eligibility to subsidy for benefit that has not been paid, the above underpayment does not affect subsidy.

Details of reported errors relating to income
Perth & Kinross Council
Testing identified one case where HB had been overpaid (value £212) due to mistakenly removing child benefit from a claim. This had reduced the claimant's income for a subsidy period (2008/09) when child benefit was not disregarded as income. The auditor reviewed the other two cases where adjustments were made to HB relating to 2008/09. For these two cases child benefit was not applicable. It was concluded that this error is isolated and that cell 031, prior year rent rebate local authority error and administrative delay overpayments is understated by £212 with a corresponding overstatement in cell 034, rent rebate subsidy claimed at full rate.
Stirling Council
Testing carried out in a local authority on rent rebate claimants' earned income due to errors identified in previous years, identified three errors resulting in two cases (total value £2192.19) where benefit was overpaid, and one case (total value £0.01) where benefit was underpaid. The effect of these errors is to overstate cell 023, rent rebate expenditure attracting full subsidy by £10,385.66 with a corresponding understatement in cell 026, local authority error and administrative delay overpayments.
Testing identified one rent allowance case (total value £1.31) where HB had been underpaid as a result of the authority miscalculating the claimant's income. Additional testing identified one additional error which resulted in an underpayment (total value £2.07). As there is no eligibility for subsidy for benefit that has not been paid, the underpayment does not affect subsidy.
Inverclyde Council
Testing identified one case (total value £1,435.94), where HB had been underpaid as a result of the authority miscalculating the earned income of the claimant's non-dependent resulting in the wrong non-dependent deduction amount being applied to the HB award. No further underpayments or overpayments were identified. As there is no eligibility for subsidy for benefit which has not been paid, the underpayment identified does not affect subsidy.

Appendix 3

Details of reported errors relating to overpayment classification
Aberdeenshire Council
One authority informed their auditor that an error had been identified where the weekly rent rebate had been calculated on a 52 week period instead of a 53 week period, resulting in overpayments being made throughout the year. The affected claims were re-assessed via a mass calculation in March 2014 which resulted in the overpayments being automatically classified as claimant error when the classification should have been local authority error. The local authority manually carried out a re-classification exercise in subsidy year 2014/15 and the change of overpayment classification will be reflected in the 2014/15 subsidy claim. A total of 2,519 claims were affected, resulting in overpayments totalling £38,721.67.The effect of this error resulted in an overstatement in cell 028, rent rebate eligible overpayments (40% subsidy recover rate) by £38,721.67 with a corresponding understatement in cell 026, local authority error and administrative delay overpayments (zero subsidy recovery rate).
Aberdeen City Council
Testing of rent rebate eligible overpayments identified nine cases (total value £768.30) where the overpayment had been wrongly classified as an eligible error when it should have been classified as a local authority error. The effect of this error resulted in an overstatement in cell 023, rent rebate expenditure attracting full- rate subsidy (100% subsidy recovery rate) by £1,636.17 and cell 028, rent rebate eligible overpayments by £40,920.25 (40% subsidy recovery rate) with a corresponding understatement in cell 026, local authority error and administrative delay overpayments of £42,556.42 (zero subsidy recovery rate).
Three rent allowance eligible overpayment cases (total value £307.71) were identified where the overpayments had been wrongly classified as an eligible error when they should have been classified as a local authority error. Additional testing identified a further two cases where the overpayment was correctly classified, but had been overstated. The effect of this error resulted in an overstatement to cell 103, claims administered under local housing allowance rules, by £2,115.27 (100% subsidy recovery rate) and cell 114, eligible rent allowance overpayment, by £4,298.29 (40% subsidy recovery rate) with a corresponding understatement in cell 113, local authority error and administrative delay overpayments of £6,413.56 (zero recovery rate).

Details of reported errors relating to overpayment classification
Testing identified one rent allowance case (total value £71.11) where a prior year overpayment had been wrongly classified as an eligible error when it should have been classified as a local authority error. Additional testing identified a further three cases (total value £171.91) where the eligible overpayment had been overstated and two cases where the overpayment was correctly classified, but had been overstated. The effect of this error resulted in an overstatement to cell 114, current year eligible overpayments, by £193.01 (40% subsidy recovery rate) and cell 121 by £1,625.29 (40% subsidy recovery rate) with a corresponding understatement in cell 113, current year local authority error and administrative delay overpayments, of £193.01 (zero subsidy recovery rate) and cell 120, prior year local authority error and administrative delay overpayments, by £1,625.29 (zero subsidy recovery rate).
Dumfries & Galloway Council
Testing identified one case where the local authority's homeless service provided an incorrect date when reporting the date a tenant moved out. No other instances were noted during testing and it was concluded that this was an isolated incident. The error resulted in an overpayment of £21.69 which should have been detailed in cell 026, rent rebate local authority error and administrative delay overpayments (zero subsidy recovery rate) but was instead included in cell 028, rent rebate eligible overpayments (40% subsidy recovery rate).
Testing identified one claim (£50) which had been included as an eligible rent allowance overpayment for the prior year instead of expenditure under the rent officer arrangements for cases excluded from the requirement to refer to the rent officer. This error did not affect the subsidy claimed as the error resulted in an under claim and there is no eligibility for subsidy which has not been claimed.
Midlothian Council
Testing identified one case (total value £19.76) where an overpayment had been recorded as claimant error, when it should have been classified as a local authority error. Additional testing identified one other case (£24.08) where the overpayment had been wrongly classified as claimant error. The errors resulted in the overstatement of £1,537 in cell 028, rent rebate eligible overpayments, (40% subsidy recovery rate) and a corresponding understatement in cell 026 rent rebate local

Details of reported errors relating to overpayment classification
authority error and administrative delay overpayments (zero subsidy recovery rate).
Testing identified one case (total value £53.54) where an overpayment had been recorded as rent allowance claimant error when it should have been classed as local authority error. Additional testing identified no further errors. The error resulted in an overstatement in cell 114, rent allowance eligible overpayments, (40% subsidy recovery rate) of £856.95 with a corresponding understatement of cell 113, local authority error and administrative delay overpayments (zero recovery rate).
North Lanarkshire Council
Testing identified one case (value £311.55) which had been incorrectly included as an overpayment in the claim form due to a housing officer incorrectly classifying it on the HB IT system. The local authority amended and rectified the claim for this error and therefore there was no effect on the amount of subsidy claimed.
Testing identified one case (value £1.96) where a change of circumstances had been processed from the incorrect date, resulting in an overpayment of HB. Testing of an additional sample of cases identified no further errors. The extrapolation of this error resulted in an overstatement in cell 023, rent rebate expenditure attracting full subsidy, (100% subsidy recovery rate) by £505 with a corresponding understatement of cell 026, local authority error and administrative delay overpayments (zero subsidy recovery rate).
One case (value of error £1) was identified where an overpayment should have been classified as local authority error and administrative delay overpayments, and not as an eligible overpayment. Additional testing identified one further case (value £1.40) that had been incorrectly classified The effect of these errors resulted in an overstatement in cell 114, eligible overpayments (40% subsidy recovery rate) by £289 with a corresponding understatement in cell 113, local authority error and administrative delay (zero subsidy recovery rate).

Appendix 4

Details of reported errors relating to eligible rent
North Lanarkshire Council
Testing identified one case (value £706) where benefit had been overpaid due to the local authority's failure to correctly apply an under-occupancy deduction. Additional testing identified a further 14 cases (value £6,558) where the under-occupancy charge had not been correctly applied. This resulted in cell 023, rent rebate expenditure attracting full rate subsidy being overstated by £69,926 with a corresponding understatement in cell 026, local authority error and administrative delay overpayments.
The auditor commented on their audited body's approach to applying the size criteria rules. The auditor pointed out that the HB size criteria rules do not apply to claimants, inter alia, that fall within paragraph 4(1)(a) of Schedule 3 of the Consequential Provisions Regulations. While the DWP recognised that it may be difficult for local authorities to ensure compliance, it was noted that local authorities should not revise awards unless they were satisfied on the basis of evidence that the claimant met the required criteria. During 2013/14, the auditor's audited body identified all claimants where the exemption criteria applied. Unfortunately the local authority's records for HB dated back to 1 January 1998 and not 1 January 1996. On the balance of probabilities, however, this was taken to be sufficient for the exemption to be applied. This had no impact on subsidy.
Comhairle Nan Eilean Siar
Testing identified one case (value £50.91) where HB had been overpaid as the authority did not exclude contributions paid by the claimant towards TV licence costs. Additional testing of the remainder of the population identified one further case (value £30.39) where HB had been overpaid. The overall impact on the claim was that cell 023, rent rebate expenditure attracting full rate subsidy was overstated by £81 and cell 026, local authority error and administrative delay overpayments was understated by £81.
Testing identified one case where HB had been underpaid as a result of the local authority applying an incorrect rent override. Additional testing identified a further ten cases where HB had been underpaid as a result of the authority applying an incorrect rent override. As there is no eligibility to subsidy for benefit which has not been paid, the underpayment identified did not affect subsidy.

Details of reported errors relating to eligible rent
Dumfries & Galloway Council
Testing identified one case where the claimant's rent had increased. However this information had not been updated within the HB IT system. No other such instances were noted The error had no effect on the subsidy claim as the correct Local Housing Allowance cap of £106.13 had been applied to the claimant's benefit paid.
The Highland Council
Testing identified three cases where HB had been underpaid (total value £88.30) as a result of incorrect eligible rent figures being used in the HB calculation. Additional testing identified one other case where benefit had been overpaid by £627. The effect of this error resulted in an overstatement in cell 098, total rent allowance expenditure at or below the rent officer's determination by £75,788 with a corresponding understatement in cell 113, local authority error and administrative delay overpayments.
Midlothian Council
Testing identified one case (total value £7.80) where benefit had been underpaid due to the wrong weekly rent being applied. Additional testing identified no other errors. As there is no eligibility to subsidy for benefit that had not been paid, the underpayment does not affect subsidy.

Appendix 5

Details of reported errors relating to IT system issues
Midlothian Council
Testing identified that the HB IT system had not reported the correct amount of benefit awarded, in some cases, resulting in an incorrect amount of subsidy being claimed. Due to the complexity of the issue, and the fact that this had only recently been identified, the auditor was not in a position to quantify the value or the number of cases affected. The software provider is currently working on a solution to correct this issue and will release a correction patch for 2014 once they have identified the cause of the software error.
Initial testing identified three cases (total value £39.76) where the local housing allowance rate was incorrect. This resulted in an underpayment of HB. Subsequent investigation established that the error had been caused by a system parameter within the HB IT system being incorrectly set during system uprating for the start of the 2013/14 financial year. The error was not found during system testing. This resulted in 317 HB cases being affected resulting in an underpayment of benefit totalling £4,962.25. This error does not affect subsidy as the error resulted in an underpayment being made in each case and there is no eligibility for subsidy which has not been paid.
Dumfries & Galloway Council
Testing identified one underpayment in relation to the calculation of the upper and lower allowance limits within expenditure on board and lodging or non-self-contained licenses accommodation where the local authority is the landlord. This was due to the HB IT system applying the weekly cap pro-rata instead of cumulatively applying the cap for the week. Additional testing identified one further underpayment. As there is no eligibility to subsidy for benefit which has not been paid, the two underpayments identified do not affect the subsidy claimed.
It was noted that Industrial Injuries Payments made by the local authority to claimants rose 2.51% on the prior year as opposed to 2.2% as per the DWP's guidance. Further investigation showed that this error related to the whole population of claimants receiving Industrial Injuries Disablement Payments. This error does not affect subsidy claimed as the error resulted in an underpayment being made in each case.

Details of reported errors relating to IT system issues
City of Edinburgh Council
Testing identified that the HB IT system parameter for an Armed Forces Independence Payment was incorrect. The correct weekly amount should have been £134.40; however a figure of £134.30 was input to the benefit system. There is no impact on subsidy as these payments are fully disregarded for the purposes of the HB calculation.
Dundee City Council and The Scottish Borders Council
It was noted during testing in two other local authority's that the HB rates for polygamous marriages had not been entered into the HB IT system during the annual uprating exercise. No instances of such marriages were identified and, therefore, there was no effect on the subsidy claimed.

Appendix 6

Details of reported errors relating to expenditure classification
Comhairle Nan Eilean Siar
Testing identified claims recorded as rent allowance expenditure on board and lodging or non-self-contained licensed accommodation provided as temporary or short term accommodation where a registered housing association is the landlord, which should have been recorded as rent rebates where board and lodging or non-self-contained licensed accommodation provided as temporary or short term accommodation where the local authority is the landlord. However, as the authority had amended and recertified the claim for this misclassification. There is therefore no impact on subsidy claimed.
Dumfries & Galloway Council
Although the local authority had transferred its housing stock to a local housing association, testing of rent rebates identified two claims in relation to properties transferred to the housing association. These claims should have instead been recorded within the rent allowance cells which relate to accommodation on board and lodging and non-self-contained licensed accommodation where a registered housing association is the landlord. Further testing identified that 7.8% of the total rent rebates claimed under expenditure on leased or self-contained licensed accommodation where the local authority is the landlord should have instead been claimed under rent allowances. £86,374.63 in cell 014 and £7,626.84 in cell 015 rent rebate expenditure on leased or self-contained licensed accommodation where the local authority is the landlord, was reclassified in cells 104 and 105 accommodation on board and lodging and non-self-contained licensed accommodation where a registered housing association is the landlord. The total subsidy claim is not affected as cells 014 and 104 both receive 100% subsidy and cells 015 and 105 do not receive any subsidy.
East Lothian Council
Testing identified one case (total value £961.75) where rent allowance expenditure had been misclassified between cases excluded from the requirement to refer to the rent officer, and expenditure in claims administered under local housing allowance rules. The claim related to a two homes payment. Additional testing of two homes payment cases did not identify any other errors. There is no effect on subsidy claimed as both types of expenditure qualify for 100% subsidy.

Details of reported errors relating to expenditure classification
North Lanarkshire Council
Prior to submission of the original subsidy claim form, the local authority identified one claim which was incorrectly classified as a rent rebate instead of a rent allowance. The local authority amended this misclassification prior to the submission of the original subsidy claim with the exception of the backdated expenditure. The local authority has amended and rectified the claim in respect of this omission and therefore there is no impact on subsidy claimed.
Testing identified two cases where expenditure where the landlord is a women's' refuge had been misclassified. Expenditure was classified in cell 102, cases not requiring referral to the rent officer, instead of cells 096 to 098, cases referred to the rent officer and administered under the pre-1996 rules. The effect of this error resulted in an overstatement in cell 102 with a corresponding understatement in cells 096 to 098. All relevant cases were identified for this landlord (value £351,074). All were found to be assessed as below or at a reasonable market rent and therefore should have been recorded in cell 098, cases referred to the rent officer and eligible rent was found to be at or below the rent officer's determination. There is no impact on subsidy as cells 102 and 098 both receive a 100% recovery rate.

Appendix 7

Details of reported errors relating to reconciliations
Clackmannanshire Council
A difference of £37,218.87 was noted between rent allowance payment summaries from the local authority's ledger system and the amount of HB claimed per the subsidy form. The difference indicated that the local authority had paid out more in the period than it had claimed. This was due to the local authority's decision to disregard income through the local scheme for war widows' and disablement pensions in excess of that disregarded by DWP. The local authority performed reconciliations between the amount of HB claimed per the HB IT system to the finance departments' figures of amounts paid. As there was only a 1.3% explainable difference in payments the local authority did not adjust the claim.
East Renfrewshire Council
In-year reconciliation highlighted a discrepancy of £316 between the HB IT system for rent rebates and rent allowances and the underlying local authority systems.
Fife Council
The local authority uses an HB IT system only used by a small number of other local authorities. The software provider had not provided instructions on the process for reconciling benefit granted, as recorded on the benefit system, to benefit paid. The authority used its own methodology to carry out the reconciliation. Overall the reconciliation showed that the HB paid was £18,638 more than benefit granted. The authority used the lower amount as the basis of its subsidy claim.
Cells 037, in year reconciliation of rent rebate expenditure and 130, in year reconciliation of rent allowance expenditure, on the subsidy claim form should agree to the entries in cells 011 total rent rebate and 094, total rent allowance expenditure respectively. Differences of £2 in rent rebate cells 011 and 037 and £2,971 in rent allowance cells 094 and 130 were noted.
North Lanarkshire Council
A difference of £1 was noted between rent allowance cells 094, total rent allowance expenditure and 130, in year reconciliation of rent allowance expenditure.

Appendix 8

Details of reported errors relating to modified schemes
City of Edinburgh Council
The analysis of modified subsidy across rent rebates and rent allowances, did not agree to the total expenditure due to the voluntary disregarding of war disablement pensions or war widows pensions. The difference of £2,442 was due to a local authority error when compiling expenditure analysis. A rent allowance adjustment for £1,221 was added in error when it should have been deducted. The figures on the subsidy claim have subsequently been updated to reflect the correct analysis and therefore there is no impact on the level of subsidy claimed.
Comhairle Nan Eilean Siar
Initial testing identified one case (£92) which had been included in the modified scheme cell in error as a result of the authority overstating the claimant's income. The effect of this error resulted in an overstatement in cell 214, total expenditure due to the voluntary disregarding of war disablement pensions or war widows pensions by £92 with a corresponding understatement of cell 102, rent allowance expenditure excluded from the requirement to refer to the rent officer resulting in an under claim of subsidy.
Perth & Kinross Council
Testing identified one case where the authority had not disregarded a pre-1973 war widow's pension when calculating the expenditure incurred as a result of the modified scheme subsidy. The value of the error was £819.This case was the only active claim which included a pre-1973 war widow's pension. It was concluded that this error was isolated and that cells 225 and 214, total expenditure due to the voluntary disregarding of war disablement pensions or war widows pensions were overstated by £819. Correspondingly cells 094 total rent allowance expenditure and 103, expenditure administered under local housing allowance rules were understated by the equivalent amount. As this resulted is an under payment of HB there is no impact on subsidy.
North Lanarkshire Council
During 2013/14 the authority upgraded its HB IT system. This created two issues: • the war pension disregard was not recorded for those claims, within modified schemes that have not been subject to a benefit recalculation after the new system went live.

Details of reported errors relating to modified schemes

- an issue has been identified with retrospective change of circumstances on rent allowance modified schemes.

The local authority had been in discussion with the software provider and had been advised that the issue cannot be corrected via the system. There is no impact on subsidy as the local authority amended and rectified the 2013/14 subsidy claim for these issues.

Appendix 9

Details of reported errors relating to uncashed cheques
Falkirk Council
The local authority's treatment of uncashed cheques for rent allowances did not comply with the DWP's guidance. The local authority showed the adjusted figure (£10,283) in the rent allowance cells 004, subsidy claimed for rent allowances and 129S, total subsidy for rent allowances and left cells 007, reduction for prior year uncashed payments, and 179S, uncashed payments blank. This treatment does not affect subsidy but does not provide visibility of the prior year uncashed cheques element in line with other authorities for comparative purposes.
Fife Council
Cell 007, reduction for prior year uncashed payments, had been left blank in the subsidy claim. Testing identified that 33 prior year uncashed cheques to the value of £5,985.37 had been omitted. This resulted in the subsidy claim being overstated by £5,985.37.
The Highland Council
Prior year uncashed cheque payments had been excluded in cells 007, and 179S, uncashed payments for the six months to 31 March 2014 as the information was not available at the time the claim was prepared. This resulted in the subsidy claim being overstated by £5,006.

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Scottish Borders COUNCIL

Internal Audit Work 2014/15 to March 2015

Report by Chief Officer Audit & Risk

Audit & Risk Committee

11 May 2015

1 PURPOSE AND SUMMARY

1.1 The purpose of this report is to provide the Audit & Risk Committee with details of:

(a) the recent work carried out by Internal Audit and the recommended audit actions agreed by Management to improve internal controls and governance arrangements, and

(b) further information on management's progress in implementing previous internal audit recommendations in line with the revised target completion dates.

1.2 The work Internal Audit has carried out in the period from 28 February to 3 April 2015 to deliver the Internal Audit Annual Plan 2014/15 is detailed in this report. During this period a total of 4 final internal audit reports have been issued. There were 3 recommendations made (0 Priority 1 High Risk, 0 Priority 2 Medium Risk, and 3 Priority 3 Low Risk) specific to 1 of the reports. Management have agreed to implement the recommendations in all cases to improve internal controls and governance arrangements.

1.3 An executive summary of the final internal audit reports issued, including audit objective, findings, good practice, recommendations and the Chief Officer Audit & Risk's independent and objective opinion on the adequacy of the control environment and governance arrangements within each audit area, is shown in Appendix 1 to this report.

1.4 Further information on Management's Progress with implementation of previous internal audit recommendations in line with the revised target completion dates is shown in Appendix 2 to this report.

2 RECOMMENDATION

2.1 I recommend that the Audit & Risk Committee:

a) Notes the final reports issued in the period from 28 February to 3 April 2015 to deliver the Internal Audit Annual Plan 2014/15;

b) Acknowledges that it is satisfied with the recommended audit actions agreed by Management; and

c) Considers whether it is satisfied with Management's Progress with implementation of previous internal audit recommendations.

3 PROGRESS REPORT

3.1 The Internal Audit Annual Plan 2014/15 was approved by the Audit Committee on 10 March 2014. Internal Audit has carried out the following work in the period 28 February to 3 April 2015 to deliver the plan to meet its objective of providing an opinion on the efficacy of the Council's risk management, internal control and governance arrangements.

3.2 **Audit Reports**

Internal Audit issued final internal audit reports on the following subjects:

- Revenues (Council Tax and Non Domestic Rates)
- Benefits Assessment
- Home Tuition
- Passenger Transport - DRAFT

3.3 An executive summary of each final internal audit report including audit objective, findings, good practice, recommendations and the Chief Officer Audit & Risk's independent and objective opinion on the adequacy of the control environment and governance arrangements within each audit area, is shown in Appendix 1 to this report.

The definitions for Internal Audit assurance categories are as follows:

Level of Assurance	Definition
Comprehensive assurance	Sound risk, control, and governance systems are in place. These should be effective in mitigating risks to the achievement of objectives. Some improvements in a few, relatively minor, areas may be required.
Substantial assurance	Largely satisfactory risk, control, and governance systems are in place. There is, however, some scope for improvement as current arrangements could undermine the achievement of objectives or leave them vulnerable to error or misuse.
Limited assurance	Risk, control, and governance systems have some satisfactory aspects. There are, however, some significant weaknesses likely to undermine the achievement of objectives and leave them vulnerable to an unacceptable risk of error or misuse.
No assurance	The systems for risk, control, and governance are ineffectively designed and operated. Objectives are not being achieved and the risk of serious error or misuse is unacceptable. Significant improvements are required.

Other Productive Work

3.4 Internal Audit have been involved in reviewing outstanding and overdue audit recommendations to ensure management action has been taken and has had the desired effect in improving internal controls and governance. The standard follow-up process has a particular focus on Priority 1 and 2 recommendations and those audit recommendations arising from previous years that have not yet been implemented. In this period this included the follow-up on Management's Progress with implementation of previous internal audit recommendations in line with the revised target completion dates agreed by Audit Committee on 10 November 2014. A position statement is shown in Appendix 2 to this report.

3.5 Recommendations in reports are suggested changes to existing procedures or processes, to improve the controls or to introduce controls where none exist. The grading of each recommendation reflects our risk assessment of non-implementation, being the product of the likelihood of the risk materialising and its impact. The gradings are:

a) **Priority 1**: Significant weaknesses in existing controls, leaving the Council or Service open to error, fraud, financial loss or reputational damage, where the risk is sufficiently high to require immediate action and to be included in the relevant risk register and for the matter to be reported in the relevant Assurance Statement on Internal Control and Governance;

b) **Priority 2**: Substantial weaknesses in existing controls, leaving the Council or Service open to high risk of error, fraud, financial loss or reputational damage requiring reasonably urgent action;

c) **Priority 3**: Moderate weaknesses in existing controls, leaving the Council or Service open to medium risk of error, fraud, financial loss or reputational damage requiring action to improve the efficiency, effectiveness and economy of operations or which otherwise require to be brought to the attention of senior management;

d) **Other**: Minor administrative weaknesses posing little risk of error, fraud, financial loss or reputational damage.

The action plans in audit reports address only recommendations rated **Significant, Substantial** or **Moderate**. Outwith the audit report, we inform local management about **Minor** matters.

3.6 **Recommendations**

	2014/15 Number of Recommendations
Reported this period	
Priority 1	0
Priority 2	0
Priority 3	3
Total reported this period	**3**
Previously reported	31
Total	**34**

Recommendations agreed with action plan	34
Not agreed; risk accepted	0
Total	**34**

4 IMPLICATIONS

4.1 Financial

(a) It is anticipated that cost efficiencies will arise as a direct result of Management implementing some of the recommendations made by Internal Audit.

4.2 Risk and Mitigations

(a) The Objectives of Internal Audit are set out in its Charter, including "As part of Scottish Borders Council's system of corporate governance, Internal Audit's purpose is to support the Council in its activities designed to achieve its declared objectives and to do so: As a contribution to the Council's corporate management of risk." Internal Audit provides assurance to Management and the Audit & Risk Committee on the effectiveness of internal controls and governance within the Council.

(b) Key components of the audit planning process include a clear understanding of the Council's functions, associated risks, and potential range and breadth of audit areas for inclusion within the plan. During the development of the Internal Audit Annual Plan 2014/15, to capture potential areas of risk and uncertainty more fully, key stakeholders have been consulted and risk registers have been considered.

(c) If audit recommendations are not implemented, there is a greater risk of financial loss and/or reduced operational efficiency and effectiveness, and management may not be able to demonstrate improvement in internal control and governance arrangements.

4.3 Equalities

(a) It is anticipated there will be no adverse impact due to race, disability, gender, age, sexual orientation or religious/belief arising from the work contained in this report.

4.4 Acting Sustainably

(a) There are no direct economic, social or environmental issues with this report.

4.5 Carbon Management

(a) There are no direct carbon emissions impacts as a result of this report.

4.6 Rural Proofing

(a) This report does not relate to new or amended policy or strategy and as a result rural proofing is not an applicable consideration.

4.7 Changes to Scheme of Administration or Scheme of Delegation

(a) No changes to the Scheme of Administration or Scheme of Delegation are required as a result of this report.

5 CONSULTATION

5.1 The Service Directors relevant to each of the internal audit reports have signed off the executive summaries in Appendix 1 and the progress status summaries in Appendix 2.

5.2 The Corporate Management Team has been consulted on this report and any comments received have been taken into account.

5.3 The Chief Financial Officer, the Monitoring Officer, the Chief Legal Officer, the Service Director Strategy and Policy, the Chief Officer HR, and the Clerk to the Council have been consulted on this report and any comments received have been incorporated into the report.

Approved by

Jill Stacey, Chief Officer Audit & Risk Signature ....

Author(s)

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Background Papers: Appropriate Internal Audit files
Previous Minute Reference: Audit Committee 10 March 2014

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. James Collin, Chief Executive's Department, can also give information on other language translations as well as providing additional copies.

Contact us at James Collin, Chief Executive's Department jcollin@scotborders.gov.uk

APPENDIX 1

Report	Summary of key findings and recommendations	Recommendations 1	Recommendations 2	Recommendations 3	Status
Subject: Revenues (Council Tax / Non Domestic Rates) No: 084/008 Date issued: 23 April 2015 Risk rating: High Level of Assurance: Comprehensive assurance	The purpose of the review was to ensure that controls are adequate to ensure that Revenues (Council Tax and Non Domestic Rates) income is complete and accurate, including relevant discounts and reliefs. The scope of this year's review included: Council Tax Reduction; Discounts, Reliefs and Exemptions - Council Tax (2nd Homes / Long Term Empty Property Relief / Disabled Band Reductions) - Non Domestic Rates (Charities / Small Business Bonus Relief / Rural Relief); Levels of Authorisation / Account Reviews planning; Staff Training; and Performance Reporting. We found good practice in the following areas: • There has been a considerable improvement in the completion of history sheets associated with accounts for Council Tax and Non Domestic Rates; • Discounts, reliefs and exemptions awarded are supported by appropriate evidence; • Performance for Council Tax and Non Domestic Rates is regularly monitored and reviewed by management. Whilst there is currently no timetable in place for account reviews, this is work in progress and it is planned that a review of all accounts for both Council Tax and Non Domestic Rates will be completed within the next financial year. There is appropriate segregation of duties regarding levels of authorisation for Council Tax and Non Domestic Rates accounts processing purposes. Staff training is carried out, and new developments and changes are communicated appropriately. Internal Audit considers that the level of assurance we are able to give is comprehensive. Sound risk, control, and governance systems are in place. These should be effective in mitigating risks to the achievement of objectives. We have made no recommendations.	0	0	0	Management have agreed the report findings. During 2015/16 Internal Audit will monitor progress of the planned review of all accounts.

Report	Summary of key findings and recommendations	Recommendations			Status
		1	2	3	
Subject: Benefits Assessment No: 085/008 Date issued: 23 April 2015 Risk rating: High Level of Assurance: Comprehensive assurance	The purpose of the review was to ensure that Benefits are correctly calculated and paid only when eligible, and controls are adequate to ensure eligibility testing is accurately and correctly carried out and acted upon by means of payment. The scope of this year's review included: Accuracy of new Housing Benefit claims and Reconsiderations; Free School Meals and Clothing Grant claims; Discretionary Housing Benefit claims (DHP); Staff training; and Performance Reporting. We found good practice in the following areas: • There is a substantial improvement in the completion of history sheets associated with claims; • Awards made were supported by appropriate evidence; • Performance for benefit assessment is regularly monitored and reviewed by management. Housing Benefit payments made are appropriate, accurate, consistent and authorised. Reconsiderations are recorded for performance purposes which is a demonstrable improvement since Audit Scotland's Housing Benefit risk assessment report 2012. Free School Meals and Clothing Grant applications are managed correctly, and decisions and awards made are within prescribed guidance. An approved Discretionary Housing Benefit (DHP) policy is in place, and only genuine and appropriate payments are made. Staff training is carried out and new developments and changes are communicated appropriately. Internal Audit considers that the level of assurance we are able to give is comprehensive. Sound risk, control, and governance systems are in place. These should be effective in mitigating risks to the achievement of objectives. We have made no recommendations.	0	0	0	Management have agreed the report findings. Internal Audit will continue to be involved in the Welfare Reform programme relevant to this area during 2015/16.

Report	Summary of key findings and recommendations	Recommendations			Status
		1	2	3	
Subject: Home Tuition No: 127/999/001 Date issued: 23 April 2015 Risk rating: Contingency Level of Assurance: Substantial assurance	We have undertaken this review on request by Schools Senior Management regarding discussions held around assurance which arose during the Counter Fraud Management Review. The purpose of the review was to determine whether the policy, processes, guidelines and administrations systems regarding Home Tutors are efficient, effective and appropriate. Internal Audit considers that the level of assurance we are able to give is substantial. Largely satisfactory risk, control, and governance systems are in place. There is, however, some scope for improvement as current arrangements could undermine the achievement of objectives or leave them vulnerable to error or misuse. We have made the following recommendations which are designed to enhance accountability and oversight: • Fully develop and implement a suite of appropriate policies, procedures, guidance notes and handbook for the Home Tuition Service and Home Tutors which documents and clearly defines roles and responsibilities, referral review and reporting processes, and ensure training is provided to those staff involved. (P3) • Authorisation of expenses should be completed at the appropriate level and closer scrutiny of mileage claims carried out with random sample checking completed. (P3) • Appoint a person with responsibility for the end-to-end process for the Home Tuition service to ensure accountability and ownership. The same person should regularly receive management information for monitoring, analysis and planning of the service. (P3)	0	0	3	Management have agreed to implement the recommendations

Report	Summary of key findings and recommendations	Recommendations			Status
		1	2	3	
Subject: Passenger Transport No: 211/007 Date issued: 27 April 2015 Risk rating: High Level of Assurance: Substantial assurance	The purpose of the review was to ensure that there are adequate operational and financial controls in place for the provision of transport service to internal clients to demonstrate efficient and effective use of resources. The scope of this year's review included: Progress towards greater integration and sharing of services with partners including Borders College and NHS; Actions towards achieving savings shown in the Council's Revenue Financial Plan; and Procurement of transport services. A Strategic Transport Board, reporting to the Scottish Borders Community Planning Partnership, has been formed with members from a number of Borders organisations and its planned reviews cover community transport and the best mix of integrated transport links. Discussions have been held on the procurement of transport services for SB Cares and appropriate arrangements have been put in place. The target 2014/15 savings of £270k have been achieved but by other means so they will therefore be carried forward into the targeted savings to be permanently achieved within the 2015/16 revenue financial plan. As part of the business planning process, Transport service management have recently been through a risk management workshop to develop its risk register which will be monitored as part of the new regular performance reporting framework. Internal Audit considers that the Transport service has put in place a good foundation from which to manage the continuing and new challenges facing community transport in the Scottish Borders. We have made no recommendations.	0	0	0	Management have agreed the report findings.

086/008 Income Charging, Billing and Collection (Final Report Issued 28 February 2014)
Department: Corporate

Recommendation	Management Progress in Addressing this Recommendation	Key
5.1 Management should assess and identify staff who require training regarding the income policy framework in order that they may take any appropriate action concerning raising invoices, income collection and debt recovery. (P1)	Action assigned to the Financial Services Manager and the Senior Credit Controller. The Credit Control team provides training on the Sundry Debt Recovery process to staff who undertake FIS training. The Credit Control Manager is currently in discussion with the Finance Business Partners with a view to targeting staff not covered by FIS training. The Finance Business Partners will highlight to departments at their regular meetings the need for all staff involved in raising invoices to complete the SB Learn module on Debt Recovery. Action partly complete – target completion date 30 June 2015.	IFC
5.2 The tools necessary to distributing a range of performance reports to management should be made available in order that the Council's processes can be strengthened to maximise income collection. These should be subject to regular senior management and elected member scrutiny. (P2)	Action assigned to the Financial Services Manager and the Senior Credit Controller. The Credit Control team has not yet migrated to Windows 7. Reports will be rolled out when Windows 7 is fully available. In the meantime, departments are still made aware of any significant debts and provide assistance to the Credit Control team where possible. Liaison meetings are held with Social Work and Estates where overall debt figures are relayed, individual high value debts and difficult to collect debts are discussed and progressed. Action partly complete – target completion date 31 July 2015 (dependent upon timescales to upgrade to Windows 7).	IFC

173/555/001 Social Care Charging Review (Consultancy) (Final Report Issued 20 December 2013)
Department: People

Recommendation	Management Progress in Addressing this Recommendation	Key
5.2 Monthly reports should be provided to Corporate Management Team and Social Work management regarding the number of clients not billed / outstanding, together with revenue monitoring. (P1)	Action assigned to the Group Manager Social Care & Health (Currently Principal Assistant). <u>Statistical analysis and reporting</u> Framework-i processes have been developed to ensure all activity with regards to financial assessments can be recorded. The new process was implemented April 2015. This will enable clear reporting on timescales from date of referral to completion. This will enable service managers to provide robust reports to Corporate Management Team (CMT) giving the number of referrals, number of assessments completed and timescales to complete assessments, together with invoicing and collection performance. Reports will be generated which should provide information on numbers of assessments, time taken by Community Care Assessors (Finance) staff (CCA F), and time taken to complete by Care Resource Team (CRT). Action partly complete - reports to CMT to commence July 2015.	IFC
5.5 Roll out Social Care Charging training across Social Work adopting a similar approach to the Financial Management training carried out earlier this year. (P2)	Action assigned to the Group Manager Social Care & Health (Currently Principal Assistant). Induction training for new staff and basic benefit awareness training has been provided. Further workshops are planned to develop a team plan for CCA F staff to look at the remit of the role, making any relevant recommendations for development of the role going forward. Formalised training by the Welfare Benefits team is planned for June 2015. CRT will be invited to participate but all CCA F staff will be involved as mandatory update training. Action mostly complete - full implementation 30 June 2015.	IFC

236/007 Data Security & Information Management (Final Report Issued 4 April 2014)
Department: Corporate

Recommendation	Management Progress in Addressing this Recommendation	Key
5.1 Management should design processes to confirm that records are weeded in line with retention schedules. (P2)	Action re-assigned to the Chief Legal Officer and acting Information Manager. Management have circulated a reminder to departments of the need to weed records in line with retention schedules. Departments are asked to confirm annually that data is reviewed in line with retention schedules. Complete.	Gov
5.2 An annual report should be presented to the Executive Committee by the Senior Information Risk Owner (SIRO) detailing: ○ an assessment of the Council's compliance with the Data Protection Act; ○ a description of the Information Governance Group's activities during the year; ○ a self-assessment on behalf of the Group on its effectiveness in meeting its agreed objectives (P2)	Action re-assigned to the Service Director Regulatory Services. It is anticipated that the SIRO's annual report will be presented to the Executive Committee in May 2015. Revised target completion date 31 May 2015 (original June 2014).	Gov

Recommendation	Management Progress in Addressing this Recommendation	Key
5.4 Processes for identifying, recording and reporting incidents of data loss, or near misses, should be designed and implemented. (P1)	Action re-assigned to the Chief Legal Officer and the acting Information Manager. A register has now been established and is in use. Complete.	Gov
5.5 Management should design and introduce housekeeping processes which would provide assurance that all physical records containing personal data have been identified and are stored appropriately. (P2)	Action re-assigned to the Chief Legal Officer and the acting Information Manager. Management have identified the need to refresh and supplement the training currently in place with a more tailored programme designed to target services within the Council which are perceived to be high risk. Management have started working with the Workforce Planning section on the design and delivery of this training, which will cover the need for good practice with regard to the physical security of paper records. The agenda for the Information Governance Group meeting scheduled on 19 May 2015 includes a discussion to agree appropriate processes within specific departments. Revised target completion date 30 September 2015 (original June 2014).	Gov

Key: IFC = Internal Financial Control; Gov = Internal Control and Governance

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Internal Audit Annual Report 2014/15

Report by Chief Officer Audit & Risk

Audit & Risk Committee

11 May 2015

1 PURPOSE AND SUMMARY

1.1 The purpose of this report is to present to the Audit & Risk Committee the Internal Audit Annual Report for the year to 31 March 2015 which includes the Chief Officer Audit & Risk's independent assurance opinion on the adequacy of the Council's overall control environment.

1.2 In support of the overall governance arrangements of the Council the Local Code of Corporate Governance and the Public Sector Internal Audit Standards require that the Chief Officer Audit & Risk provides an annual internal audit opinion and report to the Chief Executive on the adequacy and effectiveness of the Council's internal control and governance arrangements to support the preparation of the Annual Governance Statement.

1.3 In addition the Chief Financial Officer requires a specific opinion on how adequate and effective the Council's systems of internal financial control are to support the fulfilment of his Section 95 statutory role.

1.4 The Remit of the Audit & Risk Committee indicates that it should ensure an adequate framework of internal control, risk management and governance throughout the Council.

1.5 The Internal Audit Annual Report 2014/15, at Appendix 1, includes the annual internal audit opinion regarding the adequacy and effectiveness of internal control within the Council, and provides details of the Internal Audit activity and performance during the year to fulfil its role.

1.6 The Chief Officer Audit & Risk's opinion is that, based on internal audit reviews, risk assessments and knowledge, the systems of internal financial control and internal control and governance arrangements within the Council are operating satisfactorily.

1.7 The Internal Audit Annual Report 2014/15 has been used to inform the Chief Executive's Annual Governance Statement 2014/15.

2 RECOMMENDATIONS

2.1 I recommend that the Audit & Risk Committee:

a) Considers the Internal Audit Annual Report 2014/15 and provides any commentary thereon.

b) Agrees that the Internal Audit Annual Report 2014/15 be published on the Council's website.

3 BACKGROUND

3.1 The Public Sector Internal Audit Standards (PSIAS) that became effective for local authorities on 1 April 2013 requires that:

"The chief audit executive [Chief Officer Audit & Risk] must deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement.

The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.

The annual report must incorporate:

- the opinion;
- a summary of the work that supports the opinion; and
- a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme."

3.2 In addition the Chief Financial Officer requires a specific opinion on how adequate and effective the Council's systems of internal financial control are to support the fulfilment of his Section 95 statutory role.

3.3 The Remit and Terms of Reference of the Audit & Risk Committee indicate that the Audit & Risk Committee should:

- Ensure adequate framework of internal control, risk management and governance throughout the Council
- Encourage propriety and probity throughout the Council
- Assist in accountability to stakeholders

4 INTERNAL AUDIT ANNUAL REPORT 2014/15

4.1 The Internal Audit Annual Report 2014/15, at Appendix 1, includes the Chief Officer Audit & Risk's independent and objective opinion regarding the adequacy and effectiveness of internal control within the Council, and provides details of the Internal Audit activity and performance during the year to fulfil its role.

4.2 The Chief Officer Audit & Risk's opinion is that, based on internal audit reviews, risk assessments and knowledge, the systems of internal financial control and internal control and governance arrangements within the Council are operating satisfactorily.

4.3 Internal Audit reports during the year confirm continuous improvements in internal financial control and internal control and governance by Management through the implementation of audit recommendations, complemented by other Management initiated improvements, which are designed to address control weaknesses or to ensure more robust controls and governance. Further improvements in internal financial control and internal control and governance have been agreed by Management in specific areas as highlighted in internal audit reports and recommendations made during the year.

4.4 The Internal Audit Annual Report 2014/15 provides assurances in relation to the Council's corporate governance framework that is a key component in underpinning delivery of the corporate priorities within the Council's Corporate Plan and has been used to inform the Chief Executive's Annual Governance Statement 2014/15.

4.5 The Internal Audit Annual Report 2014/15 also provides details of the Internal Audit activity during the year that supports the opinion and outlines performance of the delivery of the annual plan to fulfil its role.

4.6 A statement on conformance with the PSIAS and the results of the quality assurance and improvement programme is also included in the Internal Audit Annual Report 2014/15. Although areas for further improvement have been identified in the Quality Assurance and Improvement Plan the annual internal self-assessment demonstrates sufficient evidence that the Council's Internal Audit section complies with the PSIAS in all significant respects. There is a reasonable level of conformance with both the Attribute Standards (Purpose, Authority and Responsibility; Independence and Objectivity; Proficiency and Due Professional Care; Quality Assurance and Improvement Programme) and the Performance Standards (Managing the Internal Audit Activity; Nature of Work; Engagement Planning; Performing the Engagement; Communicating Results; Monitoring Progress).

5 IMPLICATIONS

5.1 Financial

(a) It is anticipated that efficiencies will arise either as a direct or indirect result of Management implementing the recommendations made by Internal Audit during 2014/15 through improved internal controls and governance arrangements.

5.2 Risk and Mitigations

(a) Internal Audit provides assurance to management and the Audit & Risk Committee on the adequacy and effectiveness of internal controls and governance within the Council including risk management, and to highlight good practice and recommend improvements. Key components of the audit planning process include a clear understanding of the Council's functions, associated risks, and potential range and breadth of audit areas for inclusion within the plan. During the development of the Internal Audit Annual Plan 2014/15, to capture potential areas of risk and uncertainty more fully, key stakeholders were consulted and risk registers were considered.

(b) Internal Audit reports during the year confirm continuous improvements in internal financial control, and internal control and governance by Management through the implementation of audit recommendations, complemented by other Management initiated improvements, which are designed to address control weaknesses or to ensure more robust controls and governance.

(c) It is anticipated that improvements in the management and mitigation of risks will arise as a direct result of Management implementing the internal audit recommendations made during the year which will enable Management to demonstrate further improvement in internal control and governance arrangements.

5.3 Equalities

(a) It is anticipated there will be no adverse impact due to race, disability, gender, age, sexual orientation or religious/belief arising from the work contained in this report.

5.4 Acting Sustainably

(a) There are no direct economic, social or environmental issues with this report.

5.5 **Carbon Management**

(a) There are no direct carbon emissions impacts as a result of this report.

5.6 **Rural Proofing**

(a) This report does not relate to new or amended policy or strategy and as a result rural proofing is not an applicable consideration.

5.7 **Changes to Scheme of Administration or Scheme of Delegation**

(a) No changes to the Scheme of Administration or Scheme of Delegation are required as a result of this report.

6 CONSULTATION

6.1 As the Chief Officer Audit & Risk is required to give an independent opinion on the internal control and governance arrangements of the Council, consultation on Appendix 1 is not appropriate.

6.2 The Corporate Management Team has been advised to take into account the Chief Officer Audit & Risk's annual report on the work of internal audit and independent opinion on the adequacy and effectiveness of the systems of internal control and governance when completing the annual self evaluation and assurance process for the annual governance statement.

6.3 The Chief Financial Officer, the Monitoring Officer, the Chief Legal Officer, the Service Director Strategy and Policy, the Chief Officer HR, and the Clerk to the Council have been consulted on the covering report and any comments received have been incorporated into the report.

Approved by

Jill Stacey, Chief Officer Audit & Risk **Signature ....**

Author(s)

Name	Designation and Contact Number
Jill Stacey	Chief Officer Audit & Risk Tel: 01835 825036

Background Papers: Appropriate Internal Audit files
Previous Minute Reference: Audit Committee 21 March 2014

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. James Collin, Chief Executive's Directorate can also give information on other language translations as well as providing additional copies.

Contact us at James Collin, Chief Executive's Directorate, Scottish Borders Council, Council Headquarters, Newtown St Boswells, Melrose, TD6 0SA
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Chief Officer Audit & Risk's Annual Report and Opinion 2014/15

1 Introduction

1.1 In support of the overall governance arrangements of the Council the Local Code of Corporate Governance and the Public Sector Internal Audit Standards require that the Chief Officer Audit & Risk provides an annual internal audit opinion and report to the Chief Executive on the adequacy and effectiveness of the Council's internal control and governance arrangements to support the preparation of the Annual Governance Statement.

1.2 In addition the Chief Financial Officer requires a specific opinion on how adequate and effective the Council's systems of internal financial control are to support the fulfilment of his Section 95 statutory role.

1.3 The opinions are based on:

- the internal audit work carried out during the year to 31 March 2015
- my assessment of risk completed during the preparation of the internal audit strategic and annual plans
- reports issued by the Council's external auditors and other external scrutiny, audit and inspection agencies
- my knowledge of the Council's governance, risk management, and performance monitoring arrangements

1.4 This Annual Report provides those opinions and summarises the activities of Internal Audit for the period from 1 April 2014 to 31 March 2015.

2 Opinion on the systems of Internal Control and Governance

2.1 My opinion is that, based on our reviews, risk assessments and knowledge, the systems of internal control and governance are operating satisfactorily.

2.2 Continuous improvements in internal controls and governance can be demonstrated by Management through the implementation of audit recommendations, complemented by other Management initiated improvements, which are designed to address control weaknesses or to ensure more robust controls. Internal Audit reports during the year confirm improvements in internal controls and governance in:

- The Council is undertaking two significant strategic developments involving alternative service delivery arrangements. Firstly, from April 2015 several of the Council's adult care services (care at home, residential care, extra care housing, Bordercare, older peoples' day services, learning disability services and Borders ability equipment store) transferred to SB Cares, an arms-length external organisation (ALEO). Secondly, a feasibility study of options for Cultural services is underway including an option for an integrated sports and culture trust. Within both projects at appropriate stages Management have reviewed the guidance from the Accounts Commission issued in 2011 – *How Councils Work: an improvement series for councillors and officers – Arm's length external organisations (ALEOs): are you getting it right*? – and have used the toolkit included in that document in designing governance and scrutiny processes relating to the projects;
- Good progress has been made against each element of the Community Planning Partnership (CPP) improvement plan. Where actions have not yet been completed, the partnership has a clear understanding of dependencies on other processes and has made a realistic appraisal of timescales for completion;

- Effective management and administration of the Carbon Reduction Commitment Energy Efficiency Scheme (CRC) within governance of Carbon Management Programme to meet obligations on energy efficiency;
- Restructured and integrated Communications, Graphics and Print functions resulting in closer working, enhancing the work processes and ultimately the end to end service provided by the team including the range of products on offer.
- The inspections, planning and work schedules within Neighbourhood Operations show that the area teams now work on a more flexible approach which ensures that the Council has the ability to move teams or target specific areas as necessary regarding parks and open spaces, street cleansing, litter picking, snow clearing, gritting, etc.;
- Progress has been made to integrate the corporate plan, service business plans, employees' performance review and development process, the programme of change and transformation, and the financial plan aligned to the Single Outcome Agreement;
- Progress has been made on corporate performance monitoring. For each of the eight identified corporate priorities there is a set of more outcome focussed performance indicators, which management reports on quarterly, allowing elected members and officers to assess how well work is progressing towards addressing the priorities. Significant development work has been carried out to complete the Local Government Benchmarking Framework exercise developed to help Councils compare their performance using a standard set of indicators;
- There is evidence of effective information management processes and procedures which has resulted in improved response times to Freedom of Information requests.

2.3 The Health and Social Care Integration Scheme for the Scottish Borders has been developed with the full involvement of the Council's Internal Audit section. The Chief Officer Audit & Risk has been fully involved in developing the governance scheme for the Partnership as a member of the Integration & Governance working group since November 2013 and has been consulted on the draft Scheme of Integration. Significant work has been undertaken for the Scottish Borders to develop the governance arrangements in respect of the Health and Social Care integration programme including the appointment of the Chief Officer for Health and Social Care Integration in July 2014, the submission of the final Scheme of Integration to Scottish Ministers on 31 March 2015, the establishment of an Integration Joint Board with effect from 2 April 2015, and the commencement on the development of the strategic plan which will become live on 1 April 2016.

2.4 The Council has reviewed and refreshed its risk management policy and approach whose main priorities are the robust systems of identification, evaluation and control of risks which threaten the Council's ability to meet its objectives to deliver services to the public.

2.5 The Council has a number of IT security policies in place which are designed to minimise the risks to the Council's electronic assets from attacks on confidentiality, integrity and availability, the SBC Computer Security Policy and Standards being the overarching policy.

2.6 The Chief Officer Audit & Risk facilitates the annual review of the Council's governance arrangements against its Local Code of Corporate Governance carried out by a self-evaluation working group of officers from across the Council's services. This is part of the process to produce the Annual Governance Statement for assurance purposes which is published in the Statement of Accounts to report publicly on the extent of compliance with the Local Code. There is a commitment to update and gain approval to the revised Council's Local Code of Corporate Governance. This is to ensure this key document continues to be relevant and complete to reflect the appropriate framework for effective governance of the Council's affairs and facilitate the exercise of its functions.

2.7 There were nil Priority 1 (Significant weaknesses in existing controls) recommendations issued during the year that related to Internal Control and Governance (3 in 2013/14).

2.8 Reasonable assurance can be provided on the adequacy of the internal controls and governance arrangements in place. There is adequate awareness and observation of the Council's Local Code of Corporate Governance (February 2012) and key governance documents Scheme of Delegation (June 2014), Scheme of Administration (November 2014), Procedural Standing Orders (December 2013), Financial Regulations (March 2012), and Codes of Conduct for Councillors and for Employees which can be demonstrated by way of the findings of Internal Audit reviews during 2014/15.

2.9 Further improvements in internal control and governance have been agreed by Management in the following areas as highlighted in internal audit reports and recommendations made during the year:

- Arrangements for monitoring the financial and service performance of the Sports Trusts and for maintaining accountability for the public funding given to the Sports Trusts;
- Additional asset types to be included within the Road Asset Management Plan, development of a road maintenance manual to reflect policy and standards, and monitoring and review of road safety inspection and related repairs performance information.
- Implementation in full of the Council's new approach and governance for the corporate transformation programme, utilise the project managers' forum to facilitate sharing best practice and lessons learned, and implement robust mechanisms to ensure consistent use of methodologies and toolkits to positive effect for the Council. This is of particular importance as the Council continues to review and transform its service provision to deliver the required efficiency savings in light of the significant financial challenges it continues to face in the medium term;
- Fully implement the Performance Management Framework including the establishment of an appropriate self-assessment process in all Council services to demonstrate achievement of Best Value. Evaluation of the new Committee structure arising from the 2014 review within 12 months of its operation to assess the effectiveness of elected members scrutiny of plans, progress, performance and quality;
- Implement further Information Management actions facilitated by the re-established Information Governance Group: design processes to confirm that records are weeded in line with retention schedules; measure and report annually by the Senior Information Risk Officer (SIRO) on the Council's compliance with the Data Protection, the activities and effectiveness of the Information Governance Group; design and implement processes for identifying, recording and reporting incidents of data loss, or near misses; and design and introduce housekeeping processes to securely store data and records;
- Enhanced recording of staff performance appraisal and development (PRD) completion dates to enable monitoring and review to ensure there is a consistent approach to staff performance appraisal and development (PRD) in all Council services. Full roll out of workforce planning and succession planning across the Council, building on the successful pilots that have been undertaken in targeted areas.
- Need for a consistent approach to the development of strategic asset management plans by officers and their subsequent review by elected members to inform the capital financial planning process. Establish a Capital Governance Group to formally assess and prioritise business need within the Council, and to consider the implications of how resources are allocated.

3 Opinion on the Systems of Internal Financial Control

3.1 My opinion is that, based on our reviews, risk assessments and knowledge, the systems of internal financial control are operating satisfactorily.

3.2 Continuous improvements in internal financial controls can be demonstrated by Management through the implementation of audit recommendations, complemented by other Management initiated improvements, which are designed to address control weaknesses or to ensure more robust controls. Internal Audit reports during the year confirm improvements in internal financial control in:

- Financial administration and management arrangements of the Early Years' service, Building Standards Emergency Works, one Residential Home, one Day Service, and three Secondary Schools are effective and adhere to Financial Regulations;
- Significant work to incorporate the Plant and Vehicle asset planning process into the capital and revenue budget planning process and to improve governance and controls over this expenditure.
- Specific procedures and measures in place for LEADER and European Fisheries Fund grant funded projects to enable compliance with the terms of the Service Level Agreements including strengthening of file compliance and documentary evidence of eligibility and transparency of procurement compliance at individual project level, and enhanced scrutiny of project application and assessment documentation;
- Enhanced Procurement to Payment processes including completion of the Proactis e-procurement system rollout covering 72% of payments and thereby ending the use of the manual "pink slip" payment authorisation process, significant work to populate the Scottish Government Information Hub ('Spikes Cavell') Contracts Register to meet the statutory obligation to publish a public facing version by April 2016, ongoing positive outcome on performance arising from the Procurement Capability Assessment, and 93% of invoices paid within 30 days (Q1 2014/15);
- Significant improvement in the average time taken to raise an invoice and to receive the invoice payment, heightened income collection and recovery processes and procedures resulting in significantly reduced write-offs and reduced overdue debt and aged debt balances, and extensive review of Social Work fees and charges regime;
- There has been a considerable improvement in the completion of history sheets associated with accounts for Council Tax and Non Domestic Rates. Discounts, reliefs and exemptions awarded are supported by appropriate evidence. Performance for Council Tax and Non Domestic Rates is regularly monitored and reviewed by management.
- There is a substantial improvement in the completion of history sheets associated with benefit claims. Awards made were supported by appropriate evidence. Performance for benefit assessment is regularly monitored and reviewed by management.

3.3 The Council has reviewed its counter fraud management arrangements and Corporate Management Team have endorsed the recommended areas of improvement from the review which are key to the Council's proactive, holistic approach to tackling fraud, theft, corruption and crime, as an integral part of protecting public finances, safeguarding assets, and delivering services effectively and sustainably.

3.4 There is a commitment to complete the review the Council's Financial Regulations to ensure they continue to reflect the appropriate framework for sound financial management, and to ensure they are relevant and complete. They complement the other key governance documents by establishing the accountabilities, responsibilities and authority levels for officers and elected members.

3.5 There were nil Priority 1 recommendation (Significant weaknesses in existing controls) issued during the year that related to internal financial control (4 in 2013/14).

3.6 Reasonable assurance on the systems of internal financial control can be provided based on the extent of compliance with fundamental financial systems as set out in the Council's Financial Regulations (March 2012) and Procedural Standing Orders (December 2013). There is adequate awareness and observation of the regulations and procedures that can be demonstrated by way of the findings from Internal Audit reviews during 2014/15 and other key indicators.

3.7 Further improvements in internal financial control have been agreed by Management in the following areas as highlighted in internal audit reports and recommendations made during the year:

- Setting realistic income budgets specifically Development Management Fees to ensure these are based on trend analysis and anticipated growth or reduction;
- Opportunity to improve controls and governance of workforce utilisation prior to commitment of overtime and to improve authorisation of overtime hours and claims in order to more easily demonstrate delivery of services at costs which represent good value for money and to ensure compliance with legislation;
- Some improvements required relating to the arrangements for monitoring external carers' provision of service and for monitoring the financial and service performance of the Homecare service as a whole;
- Further improvements are planned to deliver an effective Contract Management Framework which to be a success will require to be embedded in the business practices and culture of the Council. Improving contract management at performance and supplier management stage has been identified at a national level as key to unlocking the Supply Chain Value;
- Full implementation of improvements to Social Care Charging process including monthly reporting on billing, policies and procedures that ensure timely assessment and billing, key performance measures and targets, and staff training;
- Further policy awareness training relating to Income Management and External Charging and full development of performance management reporting which are designed to strengthen these processes further;
- Requirement to update budget monitoring codes of practices and to fully develop written guidelines and procedures for financial processes linked to the Financial Regulations and to make improvements to their availability.

4 Internal Control Systems

4.1 Senior Management have a duty to:

- set up suitable and sound systems of internal control
- monitor the continuing effectiveness of these systems

4.2 The main aims of these systems are to ensure that :

- assets are safeguarded
- statutory requirements, management policies and procedures are observed
- information and records are appropriate, reliable, complete and accurate

4.3 Control systems can only ever provide reasonable and not complete assurance that:

- control weaknesses or irregularities do not exist
- there is no risk of material errors, losses, fraud, or breaches of laws and regulations

4.4 The system of internal control is not fixed but should change as the local government environment evolves.

5 Internal Audit Background

5.1 I, Jill Stacey BA(Hons) ACMA CGMA, have been in the role of Head of Internal Audit (HIA) from January 2005, currently Chief Officer Audit & Risk.

5.2 The Internal Audit resources were made up of:

- Chief Officer Audit and Risk (50%)
- Internal Audit Manager (75%)
- two Senior Internal Auditors, and
- two Internal Auditors

5.3 The Internal Audit function operates in line with the professional standards as set out in the Public Sector Internal Audit Standards (PSIAS) effective from 1 April 2013. The PSIAS sit alongside the CIPFA Role of the Head of Internal Audit document. The Audit Manual outlines the policies, procedures, processes and systems in place that underpin the continued provision of independent and objective internal audit assurance to guide staff in performing their duties and conform to the PSIAS.

5.4 The Chief Officer Audit & Risk reports administratively to the Service Director Strategy & Policy, reports functionally to the Audit & Risk Committee, meets regularly with the Chief Financial Officer, and has direct access to the Chief Executive, Depute Chief Executives, and Service Directors who make up the Corporate Management Team. The HIA reports in her own name and retains final edit rights over all internal audit reports.

5.5 The Chief Officer Audit & Risk has managerial responsibility for the functions which develop, support and advise on the frameworks in place at the Council on Risk Management and Counter Fraud. In order to ensure that internal audit independence and objectivity is maintained in this scenario, the internal audit work on these areas will be carried out with the Chief Officer Audit & Risk as the client and with the Internal Audit Manager fulfilling the HIA role in accordance with the Internal Audit Charter.

5.6 The net cost (projected outturn at February 2015) of the Internal Audit service was £256k (2013/14 £234k) to deliver the Internal Audit Annual Plan 2014/15 and to provide assurance on the adequacy and effectiveness of the Council's internal controls, risk management and governance arrangements. The majority of internal audit service expenditure related to staff costs £252k – 98% (2013/14 £229k – 98%) including training costs associated with a staff member undertaking professional accountancy qualification (£5k) and internal audit specialist resources to cover temporary secondments (£36k). In addition there were travel expenses £2k – 1% (2013/14 £2k - 1%) and supplies and services £2k - 1% (2013/14 £3k - 1%).

5.7 Internal Audit is continuously improving its service in accordance with the Council's corporate performance improvement framework. Activities that will ensure Internal Audit has the resources and competences to deliver the standard of service expected to provide the required assurance to Management and the Audit & Risk Committee include:

Support Audit & Risk Committee members' development to enable effective scrutiny and challenge to fulfil its remit.

Set personal objectives and development plans for all staff, interim reviews of progress, and annual appraisal of performance against objectives and plans.

Maintain staff knowledge and competency: Staff development workshops and attendance at relevant forums/training events; Key messages from these have been discussed with the team members; a programme of continuing professional development (CPD) has been undertaken by internal auditors as appropriate.

Achieve internal audit standards: An internal self-assessment of internal audit practices was carried out during 2014/15 against the PSIAS. Demonstrated improvements have been made during the year through implementation of agreed actions arising from the 2013/14 self-assessment, and the 2014/15 self-assessment has indicated a reasonable level of conformance with both the Attribute Standards (Purpose, Authority and Responsibility; Independence and Objectivity; Proficiency and Due Professional Care; Quality Assurance and Improvement Programme) and the Performance Standards (Managing the Internal Audit Activity; Nature of Work; Engagement Planning; Performing the Engagement; Communicating Results; Monitoring Progress). Scottish Borders Council will be one of the local authorities in Scotland piloting the external quality assessment framework developed by the Scottish Local Authorities' Chief Internal Auditors' Group (SLACIAG). The Quality Assurance and Improvement Plan which is designed to enable evaluation of Internal Audit's conformance with the Definition of Internal Auditing and the Standards, along with an evaluation of whether Internal Auditors apply the Code of Ethics, includes an action plan to implement further improvements during 2015/16. Specifically the Audit Manual will be reviewed and updated to reflect changes in working practices and standards to conform to the PSIAS.

6 Internal Audit Plan Delivery in 2014/15

6.1 The Internal Audit Annual Plan 2014/15 was delivered using the following approach:

There has been consultation and engagement with senior management in departments to schedule, plan and scope audit work on a regular basis to co-ordinate with management review, change and development work and external audit and inspection activity.

Each auditor has been assigned audits to complete as part of their individual performance targets.

Staff development workshops have been held and personal learning and development plans have been implemented to ensure internal auditors continue to have the skills and knowledge to deliver the service in an ever-changing and complex environment.

Resources were deployed in the delivery of the follow-up work to check that recommendations have been implemented. In cases where recommendations were priority 1 or 2 further testing work was carried out to ensure that the new controls had the desired effect on improving internal control and governance.

Internal Audit responded to specific control issues highlighted by managers during the year by incorporating those aspects within specific audit scopes or performing contingency audits approved by the Chief Officer Audit & Risk.

6.2 The following table shows the analysis of hours and audit numbers by audit type:

	Plan hours 2014/15	**Actual hours 2014/15**	**Plan Audit Nos. 2014/15**	**Actual Audit Nos. 2014/15**
High Risk Audits	2520	2332	23	21
Medium Risk Audits	1085	1154	15	13
Low Risk Audits	245	158	6	2
Follow-up	70	67		
Planned Audits Sub-Total	**3920**	**3711**	**44**	**36**
Consultancy	1730	1263		4
Contingency Audits		509		5
Advice		274		
Total	**5650**	**5757**	**44**	**45**

6.3 The following table shows the analysis of hours and audit numbers by department combining planned, consultancy and contingency audit work:

	Plan hours 2014/15	Actual hours 2014/15	Plan Audit Nos. 2014/15	Actual Audit Nos. 2014/15
Corporate	2590	2711	17	18
Place	1670	1627	18	16
People	1070	1078	9	11
Follow-up	70	67		
Advice	250	274		
Total	**5650**	**5757**	**44**	**45**

6.4 The level of Actual hours was broadly on plan (102%). This was despite the temporary reduction in internal audit staff resources in 4th quarter 2014/15 due to long-term sickness absence of one member of staff. This performance can be attributed to the greater direct audit productivity from the Internal Audit team than anticipated in the audit plan. This has been achieved by individual internal auditors striving to meet their personal objectives and performance targets, and by deploying internal auditors to audit work which uses their specific qualifications, skills, knowledge and experience thus lessening the learning curve and familiarisation process.

6.5 The allocation of audit plan hours is not an exact science and some of the audit scopes have been carried out using less than planned hours and some using more than planned hours.

6.6 Internal Audit completed 45 audits during the year (43 - 2013/14) with reports containing a total of 34 recommendations (51 – 2013/14), which have been agreed with management with acceptable timescales for their implementation.

6.7 Not all planned audits have been completed for the following reasons in agreement with the relevant Senior Management:

The Economic Development & Regeneration audit was not carried out as there has been a high level of corporate management and elected member scrutiny of this area given the corporate priority of ‘encourage sustainable economic growth’ and assurance was gained from contingency audit work on LEADER and European Fisheries Fund grants and compliance with service level agreements.

The audits on Winter Service, Developer Contributions, Licensing and Registrars were not carried out in full as internal control systems and governance in these areas had not changed significantly since the previous audits when satisfactory assurances were gained and therefore only light touch audits were deemed of value.

The Homelessness audit has been rescheduled to 2015/16 to align with system review and development work within the service.

The specific audit on People with Mental Health Needs was not carried out as this service area is included within Health and Social Care Integration which was covered by the wider consultancy audit work.

The audit on Treasury Management was not carried out in light of the national study carried out by Audit Scotland on Treasury Management during 2014 from which assurance will be gained.

6.8 The above have not affected the assurance that internal audit is able to give to Management and the Audit & Risk Committee on the adequacy and effectiveness of internal control systems and governance arrangements.

6.9 Internal Audit received positive customer comments from clients relating to 2014/15 audits, advice and consultancy work which indicates positive feedback of the value and performance of the Internal Audit section. Opportunities for improvements are discussed with Management on a regular basis as part of reporting on progress with delivery of the internal audit programme of work or when consulting on audit plans being developed.

7 Internal Audit activity during 2014/15

7.1 The wide range of internal audit work performed during the year is listed below:

Governance Audits

7.2 To provide assurances in relation to the Council's corporate governance framework that is a key component in underpinning delivery of the corporate priorities within the Council's Corporate Plan, reviews during 2014/15 included:

- Business Transformation Programme & Project Management
- Local Code of Corporate Governance
- Performance Management
- Workforce Planning
- Sports Trusts (ALEOs)
- Proposed Culture Trust (Consultancy)
- Community Planning, Joint Working and Partnership
- Social Enterprise review (Consultancy)
- Communications
- Early Years' Service
- Home Tuition (Contingency)
- EU LEADER Grants compliance with Service Level Agreement (Contingency)
- European Fisheries Fund compliance with Service Level Agreement (Contingency)
- Criminal Justice
- Proposed Social Care ALEO (Consultancy)
- Health & Social Care Integration (Consultancy)
- Carbon Management Programme
- Roads Asset Management
- Waste & Recycling Services
- Passenger Transport
- Flood Risk and Coastal Management
- ICT Infrastructure
- ICT Business Systems
- Data Security and Information Management

7.3 Where governance improvements were identified these were highlighted to management and actions were agreed to make improvements to manage the risks to the Council.

Financial Control Systems Audits

7.4 To provide assurance on the internal financial controls in place, reviews during 2014/15 of the Council's financial and management information systems and fraud prevention and detection controls included:

- Capital Investment
- Property Asset Management
- Financial Planning & Reporting including Efficiency Savings
- Procurement to Payment
- Contract Management (Consultancy)
- HR Shared Services
- Overtime (Contingency)
- Revenues – Council Tax & Non Domestic Rates
- Benefits Assessment
- Scottish Welfare Fund (Contingency)
- Income Charging, Billing & Collection
- Secondary Schools – Earlston High School
- Secondary Schools – Eyemouth High School
- Secondary Schools – Hawick High School
- Development Management Fees
- Building Standards Emergency Works
- Homecare
- St Ronan's Residential Home and Tweeddale Day Service
- Fleet Management
- Neighbourhood Management
- Safer Communities – Pathway Project Grant Funding Compliance

7.5 Where control improvements were identified these were highlighted to management and actions were agreed to make improvements to manage the financial risks to the Council.

Advice and Consultancy Work

7.6 Internal Auditors provided advice and consultancy services in accordance with the approved Internal Audit Charter as set out in the Internal Audit Annual Plan 2014/15. The two significant pieces of consultancy work related to the development and implementation of approved governance arrangements associated with the Integration programme for Health & Social Care, and the development and implementation of alternative service delivery arrangements including feasibility of options for Cultural services and SB Cares for Adult Social Care services, resulting in reports to provide assurance on governance arrangements being designed.

7.7 Internal Auditors responded to a number of requests for ad hoc advice and assistance on internal controls, risk management and governance. There has been an increase in the number and range of requests indicating management's awareness of this value-added service provided by Internal Audit and acknowledgement by Management of the benefits of proactively engaging with Internal Audit as the Council's continues to transform its services and processes.

7.8 The two Senior Internal Auditors each continue to provide quality assurance on the Welfare Reform Programme and the Information Governance Group. Internal Audit resources have also been deployed on corporate process reviews to inform revised policy and strategy, specifically the Corporate Risk Management Review and the Counter Fraud Management Review.

Meetings and user groups

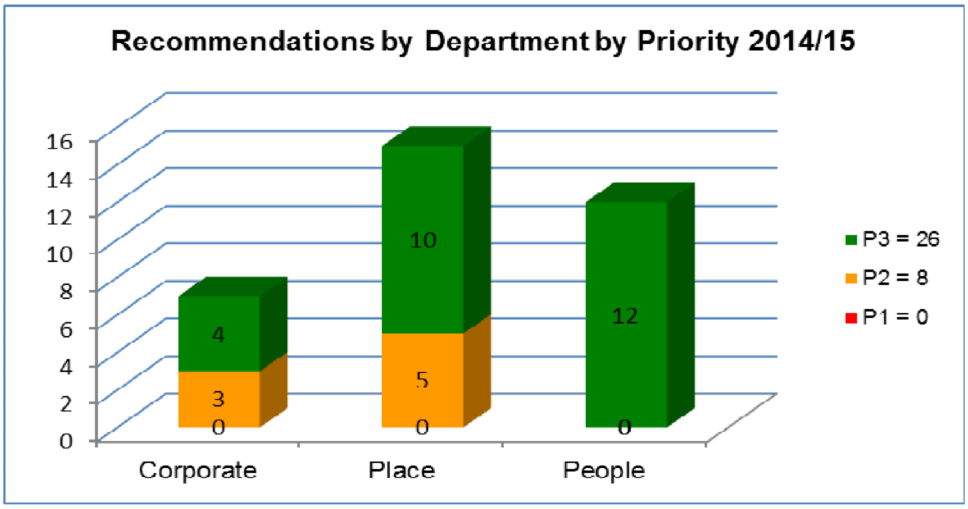
7.9 Internal Audit staff regularly attended the following meetings and user groups:

- Audit & Risk Committee: the Chief Officer Audit & Risk (HIA) developed a structured work programme of Informal Sessions to support the development of the members of the Audit & Risk Committee including formal assessment against the Knowledge and Skills Framework within CIPFA 'audit committees' Guidance 2013 and a formal Evaluation of the Effectiveness of the Committee using the toolkit within CIPFA 'audit committees' Guidance 2013.
- Department Management Teams: the Chief Officer Audit & Risk attended meetings to update Depute Chief Executives, Service Directors and Managers on key internal control and governance issues, to provide assurance arising from recent internal audit work, and to discuss key risks and assurance requirements as part of consultation on planning specific audit assignments and future internal audit plans.
- Scottish Local Authorities Chief Internal Auditors Group (SLACIAG): the Chief Officer Audit & Risk was appointed as Chairman of this internal audit forum in March 2014 having served as Vice Chairman for the previous two years. The purpose of the group is to develop and improve the practice of Internal Audit in Scottish local authorities, police, fire and public transport bodies. It achieves this by meeting to discuss issues of common concern, commissioning work to develop ideas, sharing good practice, working in partnership with other professions/governing bodies and promoting SLACIAG as the representative body for internal audit in public authorities.
- SLACIAG Computer Audit sub group: one of the Senior Internal Auditors is a member on this forum which has the aim of furthering the practice of technical Information Systems auditing across member Authorities.
- IDEA Scotland User Group: one of the Senior Internal Auditors is a member on the Committee. IDEA is a computer assisted audit technique (CAAT) tool employed for data analysis, data mining, and forensic auditing.

8 Audit Recommendations

8.1 Management has responsibility for ensuring that agreed audit actions are implemented to address the identified weaknesses and mitigate risks. At final internal audit report stage the Audit Recommendations have been input to Covalent to assist with management tracking of implementation, to link with relevant risks and to evidence improvement in internal control and governance arrangements.

8.2 During the year 2014/15 Internal Audit have made 34 recommendations categorised as Priority 1 - 0 (7 in 2013/14), Priority 2 - 8 (28 in 2013/14) and Priority 3 - 26 (16 in 2013/14). The following table summarises the 2014/15 Internal Audit Recommendations:



8.3 Internal Audit accepts that its responsibility does not cease at the point where a report is issued and will take reasonable action to follow up the implementation of agreed actions to ensure they are in place and are effective. The following table highlights the latest position with regards to internal audit recommendations arising from previous years:

Year identified	Total	Implemented	Not Yet Due	Overdue
2014/15	34	8	16	10
2013/14	51	34	10	7

8.4 Internal Audit will continue to follow their standard quarterly follow-up activity and continue to work with management to address any actions that become overdue, and bring any matters to the attention of the Audit & Risk Committee. The follow-up activity takes into consideration their priority status, what target timescales are in place for full implementation, the explanation of the reason for any delay in implementation, and a review of their status to ensure the recommendations are still relevant or whether alternative solutions are required to address the identified weakness.

Jill Stacey
Chief Officer Audit & Risk
30 April 2015

Borrowing and treasury management in councils

ACCOUNTS COMMISSION

Prepared by Audit Scotland
March 2015

The Accounts Commission

The Accounts Commission is the public spending watchdog for local government. We hold councils in Scotland to account and help them improve. We operate impartially and independently of councils and of the Scottish Government, and we meet and report in public.

We expect councils to achieve the highest standards of governance and financial stewardship, and value for money in how they use their resources and provide their services.

Our work includes:

- securing and acting upon the external audit of Scotland's councils and various joint boards and committees
- assessing the performance of councils in relation to Best Value and community planning
- carrying out national performance audits to help councils improve their services
- requiring councils to publish information to help the public assess their performance.

You can find out more about the work of the Accounts Commission on our website: www.audit-scotland.gov.uk/about/ac

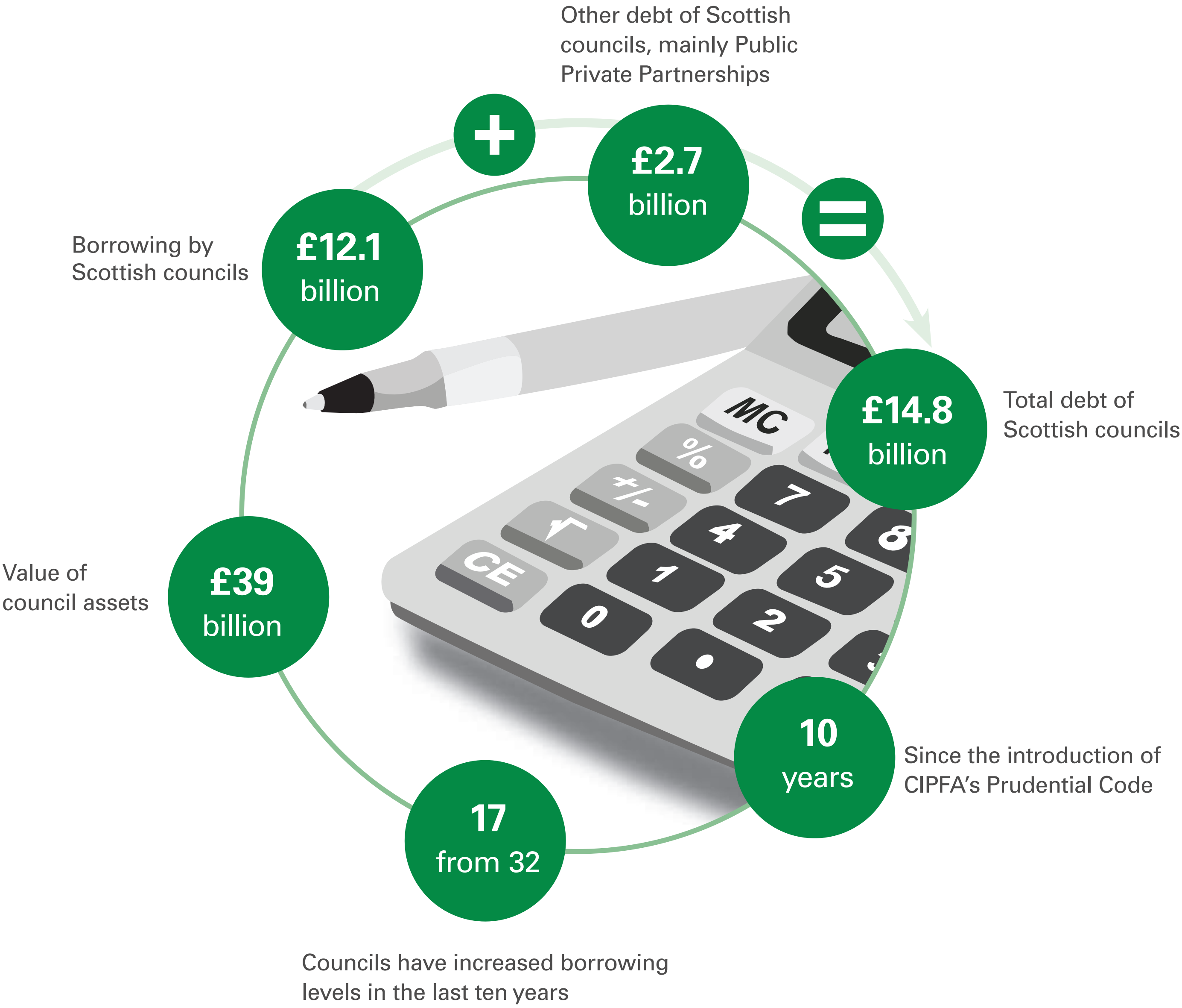
Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Exhibit data

When viewing this report online, you can access background data by clicking on the graph icon. The data file will open in a new window.

Key facts


Other debt of Scottish councils, mainly Public Private Partnerships
£2.7 billion
Borrowing by Scottish councils
£12.1 billion
Total debt of Scottish councils
£14.8 billion
Value of council assets
£39 billion
10 years
Since the introduction of CIPFA's Prudential Code
17 from 32
Councils have increased borrowing levels in the last ten years

Summary

Key messages

1 Councils have total debt of £14.8 billion of which £12.1 billion, 82 per cent, is from borrowing. Debt commits councils to charges over the long term. There are different types of debt with different features and varying degrees of risk.

2 Borrowing is a key source of finance for councils to invest in vital public services. Overall borrowing has remained at around £12 billion for the last three years, with total assets of £39 billion. Councils have developed borrowing strategies to suit their own local priorities and needs, in response to the flexibility introduced by the Prudential Code in 2004. Seventeen councils have increased their borrowing levels, in real terms, over the last ten years.

3 Councils are following the general principles of the relevant codes of practice in demonstrating short-term affordability, but they are not always highlighting the strategic importance of borrowing and treasury management or clearly analysing and reporting the long-term affordability and sustainability of their borrowing. Councils need to develop detailed analysis to support borrowing decisions and to demonstrate they represent best value for the council.

4 Treasury management is a professionally run function in councils with appropriately qualified officers. Succession planning, ongoing training and the availability of appropriate professional qualifications are important. Councils have started to integrate their treasury management and capital investment functions which is a positive step.

5 Councils need to improve scrutiny of borrowing and treasury management. This is a complex and technical subject and officers need to provide wider training and support to councillors, and also provide clearer, more accessible reports. The current governance structures in some councils could be improved to support more effective scrutiny.

Recommendations

These recommendations focus on the evidence gathered and our findings on borrowing within councils. We suggest councils consider the wider relevance of these to total debt.

Council officers should:

- use the treasury management strategy to present a wider strategic view of borrowing and treasury management. It should use clear and accessible language and be prepared for councillors as the key audience. It should include how the borrowing strategy is informed by corporate priorities and capital investment needs. The strategy should include:
  - links to capital investment plans and corporate objectives
  - all borrowing and other debt
  - prudential indicators as a core part of the strategy
  - a clear assessment of the affordability and the impact on revenue budgets both in the short and long term
- create more detailed and longer-term borrowing and treasury management analysis as informed by the council's financial strategy. It should include:
  - scenario planning to show the potential impact of different budget scenarios, income generation plans, and changes in external factors such as interest rates
  - analysis of capital financing options to compare affordability and sustainability between different debt and borrowing options
  - the use of indicators over a longer period than the minimum three years set by the Prudential Code
- share strategies with other councils to help inform good practice, and exchange of ideas
- carry out joint planning with other councils to identify future qualification and training needs and enhance their capacity, in order to negotiate with training providers
- review the content of year-end reports to ensure they provide an assessment of the effectiveness of the year's borrowing and treasury management activities and the performance of the treasury management function. This should include appropriate indicators, comparative figures, and appropriate explanations.

Council officers and councillors involved in treasury management should:

- review governance arrangements, and update as necessary, to ensure they provide:
  - the treasury management strategy, mid-year and year-end reports to the same council committee, and that the full council has access to them
  - councillors with mid-year reports by the end of December each year
  - councillors with the wider picture, that is, make the links to capital investment decisions and revenue budgets
  - councillors with access to all reports relating to borrowing and treasury management activity including risk registers
- ensure scrutiny arrangements are robust by:
  - considering widening the range of training options to councillors on borrowing and treasury management activities and whether this training should be mandatory
  - considering whether training for councillors provides a balance of scrutiny skills and knowledge of treasury management.

About the audit

1. This audit assesses how councils show best value in borrowing and treasury management decisions. Its specific objectives are to answer:

- What is borrowing and treasury management in councils?
- To what extent do councils' borrowing and treasury management strategies meet good practice and contribute to corporate plans and priorities?
- Can councils demonstrate the affordability and sustainability of borrowing decisions? For example, can they show that borrowing will not adversely affect their financial position? Will that continue to be the case in future?
- How effective are the governance arrangements for borrowing and treasury management? Governance covers areas such as responsibility and accountability for borrowing and treasury management decisions, arrangements for reporting decisions and for scrutinising them.

2. Councils have total debt of £14.8 billion, of which 82 per cent (£12.1 billion) is as a result of borrowing (Exhibit 1, page 9). Total debt includes Private Finance Initiative/Non Profit Distributing (PFI/NPD) contracts, Tax Incremental Financing (TIF), the City Deal agreement, the Growth Accelerator Model (GAM) and borrowing. Each type of debt has unique features, is at different stages of development and implementation and has varying degrees of risk. This is the first report that we have produced on council debt with the focus specifically on borrowing. This allows us to focus on the arrangements that councils have in place to assess the affordability of borrowing. We may propose further work on other elements of council debt in due course.

3. This report focuses on whether councils openly and clearly demonstrate the affordability and sustainability of borrowing decisions over the short term, ie the next couple of years, and long term, that is ten years onwards to cover the term of the borrowing. It also looks at whether councils' approach to borrowing, as outlined in their treasury management strategy, reflects their corporate priorities and aims. Councillors have a key role in holding officers to account and this report evaluates the councillor's role in considering borrowing and treasury management reports, including the strategy. We use the term borrowing to mean borrowing from a source outwith the council.

4. Our focus is on borrowing to fund capital expenditure, such as building schools or improving roads. We did not evaluate day-to-day cash, investment and borrowing transactions. We have not explored in detail other forms of debt. This includes the new capital financing options available to councils including TIF, or City Deal that may have an element of borrowing to them (Exhibit 1, page 9). These new options are just being introduced and are not yet fully operational. Although the messages in our report are based on current borrowing, they will apply equally to other forms of debt including these new financing options.

5. We gathered audit evidence from:

- published and unpublished data on borrowing and treasury management activity including audited accounts, Chartered Institute of Public Finance and Accountancy (CIPFA) statistics and Scottish Government data
- our review of the treasury management strategies of 12 councils
- fieldwork at six councils involving interviews with officers and councillors
- interviews with representatives from organisations including the Scottish Government, CIPFA, CIPFA Treasury managers' forum and the Society of Local Authority Chief Executives (SOLACE).

6. Appendix 1 provides further details of our audit approach.

7. This report has three parts:

- Part 1: setting the scene
- Part 2: demonstrating the affordability and sustainability of borrowing
- Part 3: effective management and scrutiny.

8. Our website contains a *Supplement: Scrutiny guidance and questions for councillors* [PDF] to help them implement the recommendation we make in this report.

Exhibit 1
Borrowing is 82% of total debt

Total debt £14.8bn

Borrowing £12.1bn

From Public Works Loan Board (public sector source of lending for public bodies)

From banks

Borrowing charges paid from revenue budget over life of loan.

Public Private Partnership £2.7bn

Private Finance Initiative

Partnership where public and private sector partners agree a contract to build and maintain an asset for public sector use.

Public body pays an annual charge over the life of the asset to the contractor from its revenue budget.

Non-profit distributing contracts

Similar to PFI, but limits the profits that the private sector contractor may retain.

Public body pays an annual charge over the life of the asset to the contractor from its revenue budget.

Tax Incremental Financing

New capital financing method. Council borrows to invest in infrastructure projects which will deliver economic growth. Additional business rate income from the new business generated pays for borrowing charges.

Growth Accelerator Model

Public body borrows to invest in capital investment project.

Expected that additional business rates will accrue to Scottish Goverment owing to investment.

Scottish Government makes payment to public body, based on additional economic growth.

City deal

Agreement signed with UK and Scottish Governments by the 8 Glasgow and Clyde Valley councils. Currently the only deal in Scotland.

The deal involves the councils investing an additional £130 million to unlock additional grants of £1 billion from the UK and Scottish Governments combined.

Investment by councils will involve additional borrowing, with charges covered by additional grant income.

Note: £2.7bn includes finance leases. TIFs, GAM and City Deal are just introduced and are not yet fully operational.

Source: Audit Scotland

Part 1

Setting the scene

Key messages

1 Councils' outstanding debt was £14.8 billion at 31 March 2014, with borrowing making up £12.1 billion, 82 per cent of this.

2 Councils use borrowing to pay for assets such as schools and roads to provide local services and meet local priorities. This has an impact on future revenue budgets, as the council needs to pay interest on the borrowing. Total assets were £39 billion at 31 March 2014.

3 The Prudential Code was introduced in 2004 to provide greater flexibility for councils to manage and control their own capital investment activity following a period of government regulation. Councils' borrowing strategies, levels of borrowing and debt profiles differ widely.

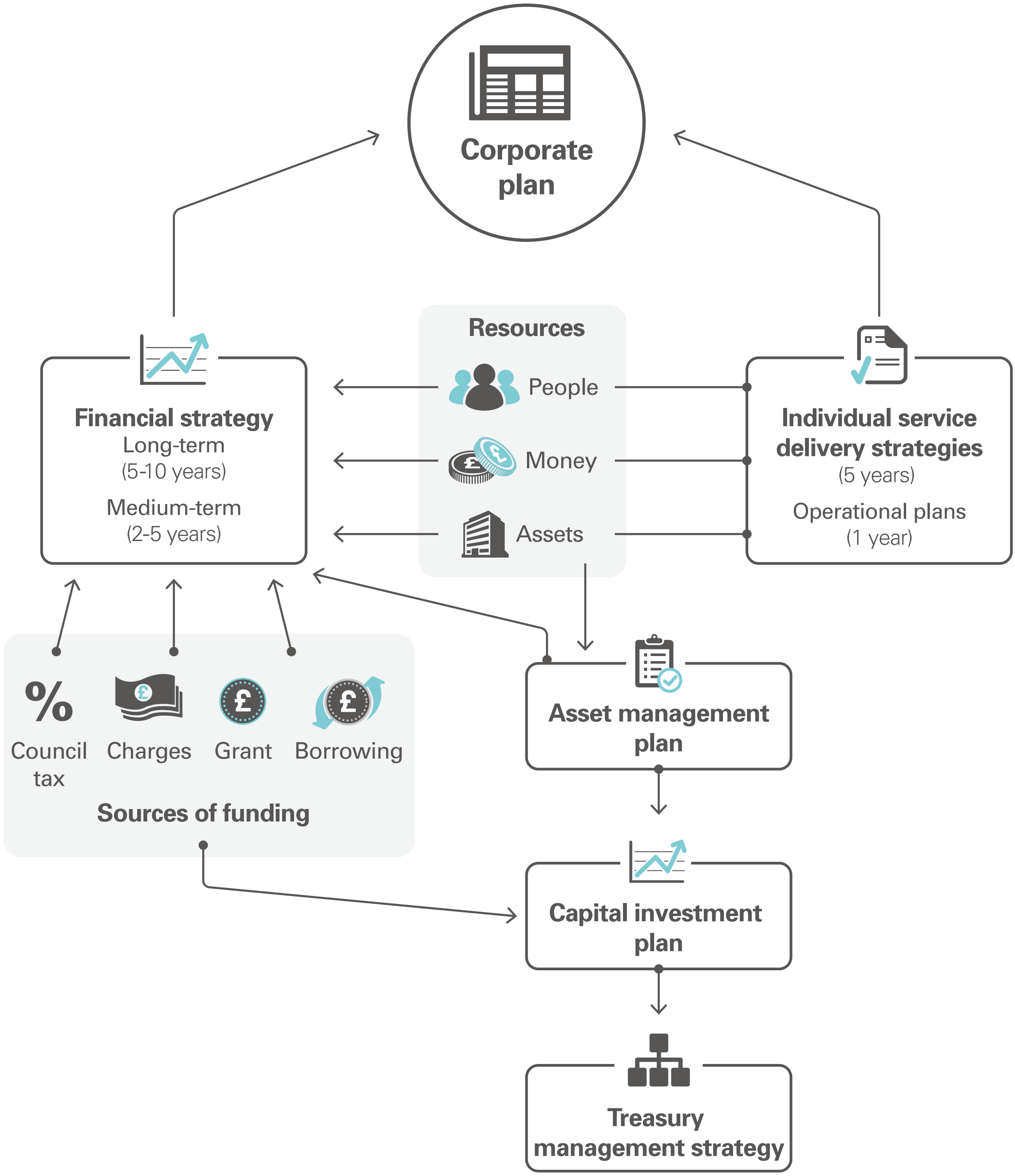
councils' ability to manage and control their own investment activity is reflected in borrowing levels and strategies

Councils invest in services for communities

9. A council has a corporate plan setting out its priorities and objectives and how it plans to achieve them (Exhibit 2, page 11). This may, for example, include the priority to build a new school to deal with an expected increase in demand as a result of significant new housing. These plans are often over the medium term, typically three to five years, but may be over a longer term, ie up to 15 years. The council targets its resources, that is people, money and assets, at its priorities and objectives. The corporate plan should feed into the asset management plan to identify what assets are needed to achieve its objectives. For example, this could be building new housing. The council, through a capital investment plan, sets out how it will finance the spending on these assets. This may be by using cash resources, for example cash reserves built up over time or capital grants, or through external finance.

10. Methods of external finance include borrowing, PFI schemes and other mechanisms including NPD schemes, TIF schemes, or the new GAM. Entering into external financing arrangements will create debt for the council, and means that the council needs to pay financing charges each year over the life of the arrangement, which may be up to 50 years. It is important for a council to assess the affordability of decisions in the context of the financing charges of its total debt.

Exhibit 2
Corporate and strategic influences on treasury management strategy



Source: Audit Scotland

11. Councils should also have medium (two to five year) and long-term (five to ten year) financial strategies. The council will estimate future funding and income, costs and demand for services, and how much it will need to spend to achieve its future objectives. The strategy should identify how the council will make up any shortfall between estimated funding and projected costs and demand. The financial strategy should include the financing cost of borrowing and other debt. This is the annual repayment of interest charged on borrowing or other external financing and any other associated costs. Councils make this repayment out of future budgets, so it decreases the level of available budget remaining and reduces flexibility in future budget decisions.

12. Borrowing involves accessing finance and then repaying it over a longer period of time. These periods can be for up to 50 years, so today's decisions can have a sustained impact on future generations. Borrowing decisions involve a careful balancing act between prioritising investment, and making sure the council can:

- manage the consequences of its decisions over the whole life of the borrowing
- provide evidence showing how it will manage these long-term consequences.

13. Borrowing therefore is set firmly within the framework of wider council activity and should be driven by the corporate plan, capital investment plan and medium and long-term financial plans (Exhibit 2, page 11).

Borrowing is the main element of total debt

Councils' outstanding borrowing is £12.1 billion and has been between £10.5 and £12 billion for the last six years

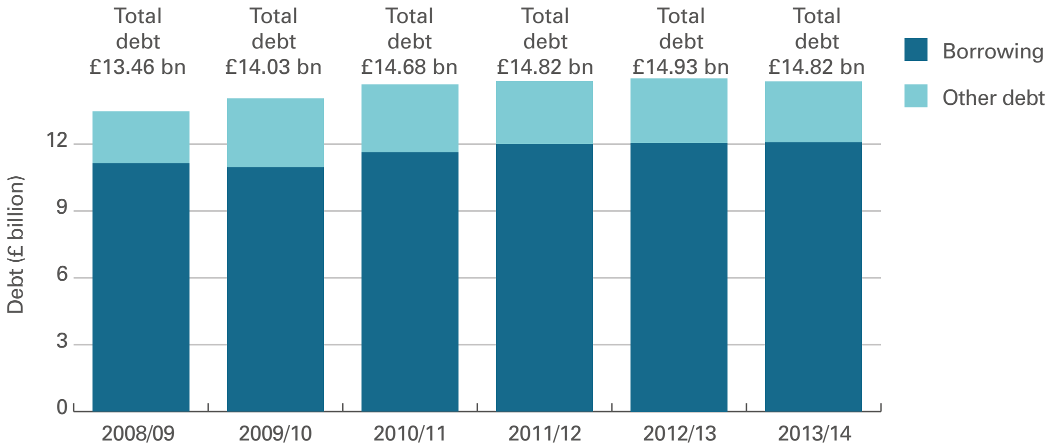
14. Councils spend around £20.8 billion a year. Of this, £18.6 billion is for day-to-day expenses including salaries, and £2.2 billion on buying, building and maintaining assets such as schools, housing and care homes.

15. Councils' total debt at 31 March 2014 was £14.8 billion, with total assets of £39 billion. Borrowing is the main form of debt for Scottish councils (Exhibit 1, page 9). Councils had overall borrowing of £12.1 billion at 31 March 2014 and other debt of £2.7 billion (Exhibit 3, page 13). Borrowing has remained between £10.5 and £12 billion for the last six years. Other debt levels have fluctuated between £2.2 billion and £2.8 billion over the last six years. Other debt comprises both PFI and NPD schemes and the new financing methods, including TIF, GAM and City Deal that are just being introduced.

16. Comparing council borrowing levels over the last ten years, between 2003/04 and 2013/14, shows that 17 of Scotland's 32 councils have increased borrowing levels in real terms, that is, including the effects of inflation (Exhibit 4, page 13). Changes in borrowing levels over this period reflect differences in councils' corporate priorities, capital investment plans, levels of cash resources and other available financing options, amongst other factors.

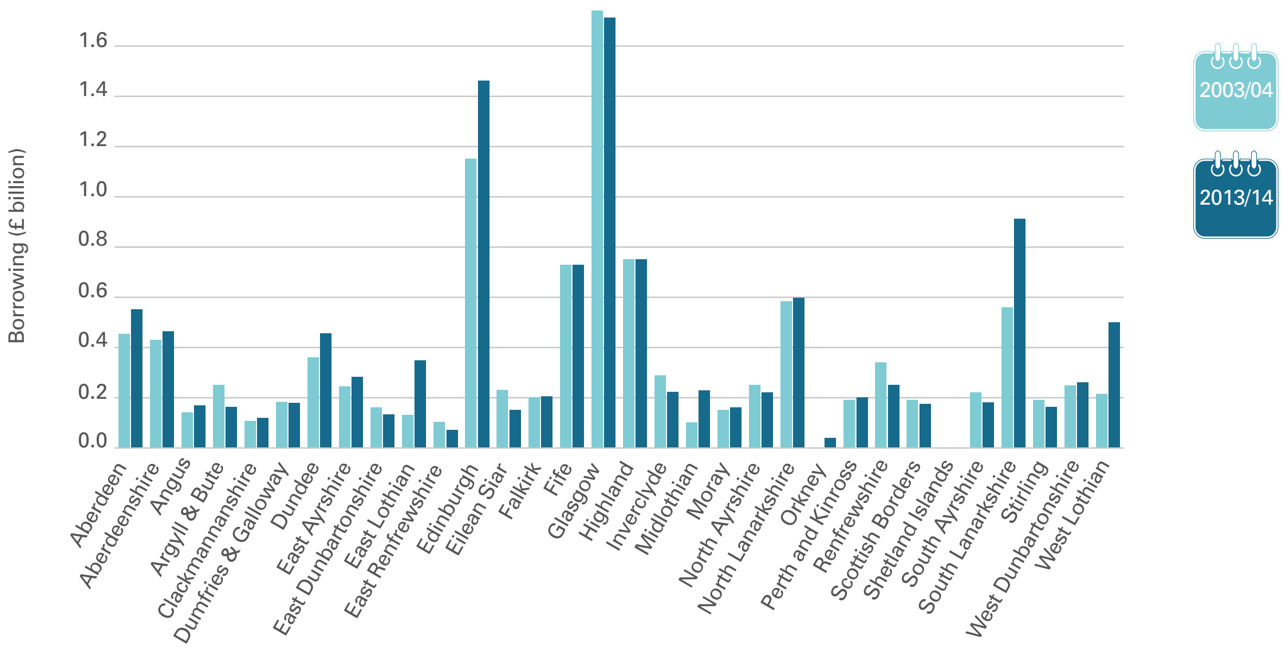
17. Councils do not always need to increase debt or borrowing if internal sources of finance are available to them. This includes using cash reserves that have been built up over time or capital grants.

Exhibit 3
Total debt of Scottish councils (2013/14 real terms prices)



Source: Council audited annual accounts 2008/09 to 2013/14

Exhibit 4
Comparison of total borrowing by councils in 2003/04 and 2013/14 (2013/14 real terms prices)



Source: Council audited annual accounts 2003/04 and 2013/14

18. Current interest rates are low, which is an advantage to councils that need to borrow for capital investment as interest charges are cheaper than when rates are higher. Our analysis shows that two-thirds of councils are currently borrowing, although fewer councils are borrowing now than ten years ago. Councils are borrowing shorter term, typically for less than 15 years, at fixed rates, from government-backed institutions such as the Public Works Loan Board (PWLB), as this has offered the most competitive rates.

Borrowing is a long-term commitment, with a third of current borrowing due to be repaid in over 40 years

19. The repayment of a council's borrowing influences its long-term financial planning and its assessment of whether it will be able to afford its existing borrowing in the future. To manage levels of borrowing we would expect to see a spread of borrowing with different maturity periods so that it is more manageable. We would also expect councils to avoid periods when high levels of repayments may impact on money available for other priorities. On maturity, councils can either decide to repay borrowing, or take a new loan to replace the old borrowing. Exhibit 5 (page 15) shows the profile of borrowing for 2009/10 to 2012/13 and highlights:

- the profile of borrowing is evening out and the percentage of loans maturing in over 20 years has fallen. At 2009/10, over 61 per cent of borrowing would mature in over 20 years; this decreased to 52 per cent by 2012/13
- councils have increased short-term borrowing. At 2009/10, around five per cent of borrowing was for less than two years, increasing to 8.5 per cent at 2012/13
- around a third of councils' borrowing is due to be repaid in the next ten years (35 per cent)
- around another third of borrowing will be due for repayment in over 40 years (34.8 per cent).

Borrowing is a key part of treasury management

20. Treasury management is the process that councils use to ensure cash is available when needed. This includes day-to-day expenses like paying salaries or electricity bills, and building new assets, such as a new school, or improving existing ones, such as roads. It also involves ensuring that any temporary surplus cash is safely invested. Borrowing is one of the larger cash flows that a council needs to manage, so borrowing is a central part of treasury management. Exhibit 6 (page 16) shows examples of the typical cash flows in a council together with their timing.

21. Councils have two types of budgets to finance and to balance: revenue and capital. Revenue expenditure pays for daily activities like salaries or electricity bills. Capital expenditure is what councils spend on premises, equipment and vehicles; on improvements like roads repairs; and on providing new assets like schools or council houses. Councils can borrow to finance capital expenditure but not revenue expenditure, unless approved by Scottish ministers. Borrowing charges are revenue expenditure. Councils that own council houses must keep a separate budget and account for revenue and capital expenditure on the housing stock.

Exhibit 5

Scottish councils–maturity of total borrowing 2009/10 to 2012/13

Percentage of borrowing due to be repaid in the periods shown.

Source: *Capital Expenditure and Treasury Management*, CIPFA Statistics, June 2014

Borrowing to invest in housing must be repaid from the future housing budget, and therefore funded from future housing rental income.

Councils must comply with borrowing and treasury management rules and regulations

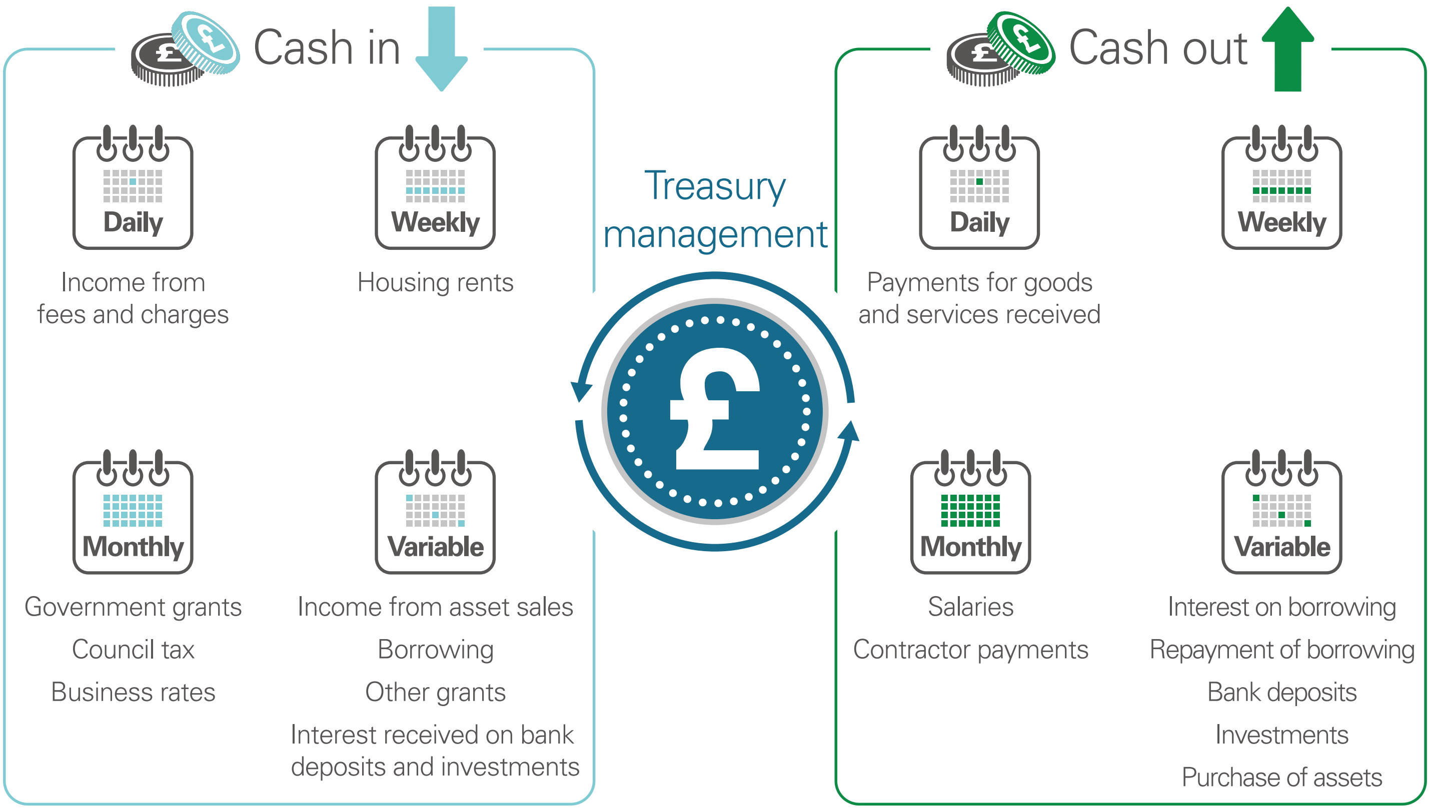
22. In recognition of the importance of capital investment in assets and treasury management to council activities, CIPFA and the Scottish Government set codes of practice and regulations for councils to follow. These ensure that councils have effective processes and practices in place to control, manage and govern capital investment decisions, that include borrowing, and treasury management practices (Exhibit 7, page 17).

23. The Prudential Code was introduced in 2004 as a framework to support councils and help them show effective control over levels of, and decisions relating to, capital investment activity, including borrowing. Before this, capital investment levels in councils were government-regulated.

Exhibit 6

Treasury management activities

An example of a council's cash flows with their timing to demonstrate their variability and predictability.



Source: Audit Scotland

24. This self-regulating approach has enabled councils to adopt borrowing and treasury management strategies that fit with their corporate plans and objectives. The framework allows for councils themselves to judge what is affordable and sustainable and will differ depending on local circumstances. The Prudential Code sits alongside CIPFA's treasury management code, which sets out the requirements for professional treasury management practice.

25. A key requirement of the codes is for councils to produce an annual treasury management strategy before the start of each financial year. CIPFA and the Scottish Government recommend that this is a single integrated strategy that combines plans for capital investment, including borrowing, treasury management, and investment. It also recommends that the strategy includes prudential indicators that are set out within the Prudential Code. These form a set of 12 limits and ratios that all councils must calculate and use to show to councillors and the public that capital investment plans are affordable and sustainable.

Exhibit 7
Codes of Practice and Regulations

The Prudential Code for Capital Finance in Local Authorities–CIPFA	A professional code of practice to help councils with capital investment decisions by providing a framework. The Prudential Code sets out indicators that councils must use to help demonstrate public accountability. It also recommends that councils have an integrated treasury management strategy within which its borrowing and investments are managed.
Treasury management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes–CIPFA ('the CIPFA treasury management code')	Adopting this code is a requirement of the Prudential Code. This makes recommendations to provide a basis for councils to create clear treasury management objectives and to structure and maintain sound treasury management policies and practices. A key recommendation is for a treasury management strategy before the start of the year, a mid-year report and an end-year review report.
Finance Circular 5/2010–The investment of money by Scottish local authorities	Provides Scottish ministers' consent for councils investing money and sets out the recommendations and requirements they must meet when making investments. It requires local authorities to 'have regard' to the Prudential Code and the Treasury Management Code and recommends that the strategy form part of a wider single annual strategy covering capital investment, treasury management and prudential information.
Local Government (Scotland) Act 1975	Sets out the statutory basis on which councils can borrow and lend.

Source: Audit Scotland

26. This report focuses on borrowing, to finance capital investment, and treasury management. Most of the indicators are not specific to borrowing but relate to total capital investment and are calculated using figures for total finance costs, total capital expenditure or total debt. This allows councils to assess the affordability of borrowing in the context of the total debt position of the council. The indicators relating specifically to borrowing are the estimated and actual capital financing requirement. This calculates the amount of capital investment that needs to be met from borrowing or other method of external finance.

27. The prudential indicators are designed to help councils make and record local decisions. They are not designed to be comparative performance indicators across councils as they are set according to the individual needs of each council. In particular, councils had widely different debt positions when the Prudential Code was introduced. These differences are likely to increase over time as councils' choices reflect local priorities. The system is designed specifically to help councils take local decisions in ways that are publicly accountable.

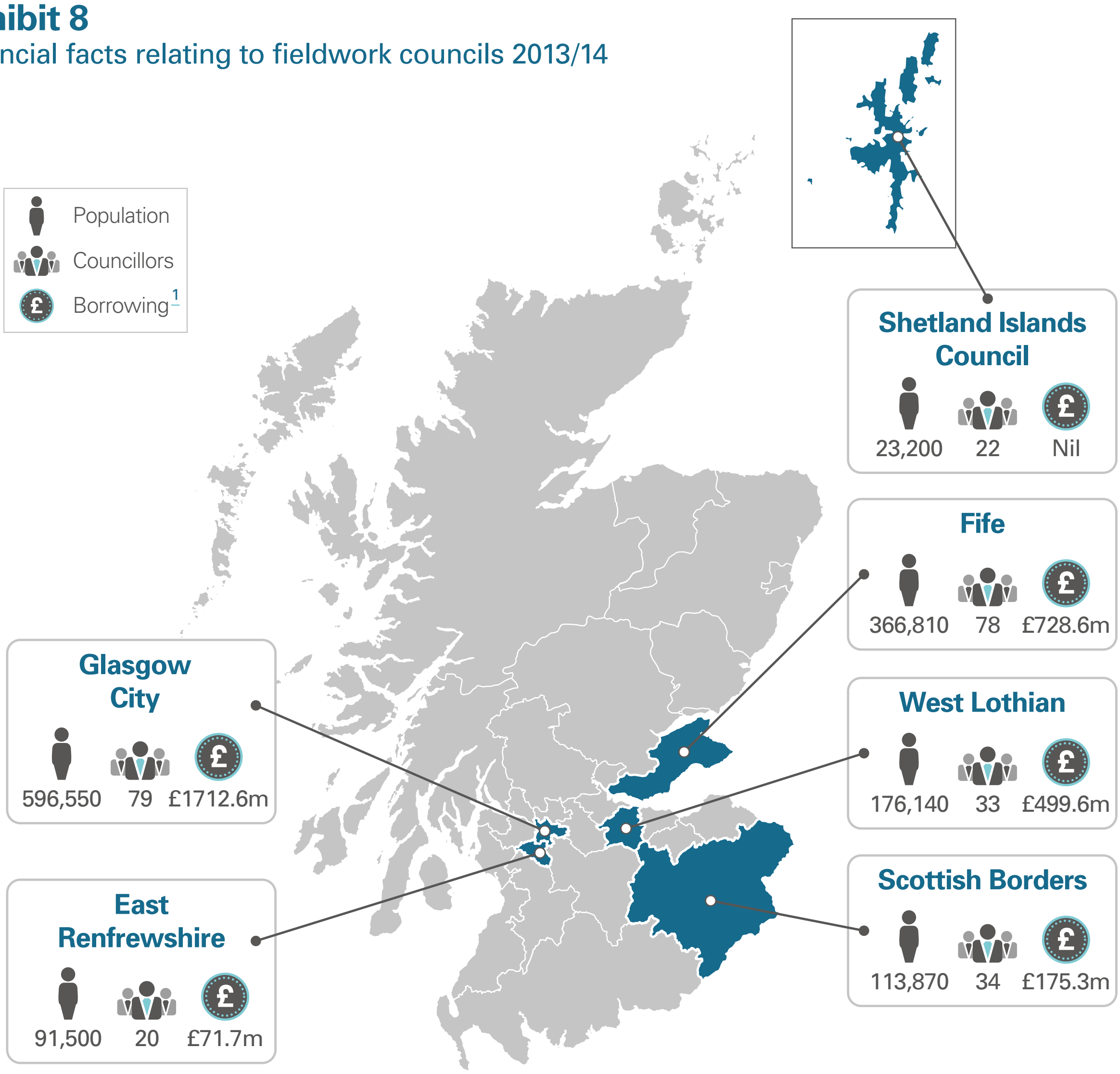
Our fieldwork sites reflect the variation in councils' borrowing and treasury management strategies

28. We reviewed the strategies of 12 councils to give us a better indication of the variation in local circumstances, the need for borrowing and the resulting treasury management strategy. We selected six councils out of the 12 to undertake more detailed fieldwork, including interviews.

29. Our six fieldwork sites reflect the level of variation in councils' borrowing and treasury management strategies, and therefore their levels of borrowing (Exhibit 8, page 19 and (Exhibit 9, pages 20 and 21). Although interest rates are currently low and expected to increase, not all councils have set their strategy to borrow for future capital investment. For example, East Renfrewshire Council has not borrowed externally for five years, but it has previously financed a higher proportion of investment through other methods of external financing such as the PFI scheme, and therefore has a higher proportion of other debt. Shetland Islands Council had never borrowed until July 2014. This change in strategy was as a result of appraising whether using internal cash reserves or borrowing at low interest rates represented the best value for the council.

30. Councils have different sizes of capital investment programmes to finance. Some councils have no housing stock to improve and add to, while others must consider how to invest in their housing stock without placing too high a burden on future housing budgets and rents. Councils must repay the borrowing and interest charges for investment in housing from the housing revenue budget; whereas investment in other assets must be repaid from the general budget.

Exhibit 8
Financial facts relating to fieldwork councils 2013/14



	Shetland Islands	East Renfrewshire	Scottish Borders	West Lothian	Fife	Glasgow City
Fixed assets [2]	£406m	£770m	£416m	£1,346m	£2,151m	£4,367m
Investments [3]	£211.4m	£45.1m	£13.7m	£117.1m	£3.1m	£136.5m
Cash reserves [4]	£240.9m	£53m	£25.7m	£114.8m	£90.6m	£135m
General capital programme [5]	£69.5m (2014-19)	£100.7m (2014-22)	£271.4m (2014-24)	£277.3m (2013-18)	£532.2m (2013-23)	£455.7m (2013-18)
Housing capital programme [5]	£5.8m (2014-19)	£17.2m (2014-19)	No housing	£202.9m (2013-18)	£390.4m (2013-23)	No housing

Notes:
1. Borrowing is long and short-term borrowing from council audited accounts at 31 March 2014. 2. Fixed assets is the value of long-term tangible fixed assets, such as buildings and equipment, and long-term intangible assets such as software, from the audited accounts at 31 March 2014. 3. Investments includes long and short-term investments, investment property where relevant, and cash and cash equivalents from the audited accounts at 31 March 2014. 4. Cash reserves is the total usable reserves of the council, from the audited accounts at 31 March 2014. 5. The length of councils' capital programmes can vary and spending is phased over the length of the programme. The timeframe of each council's programme is given in brackets.

Source: Council audited annual accounts 2013/14; *Mid 2013 Population Estimates Scotland*, National Records of Scotland, June 2014

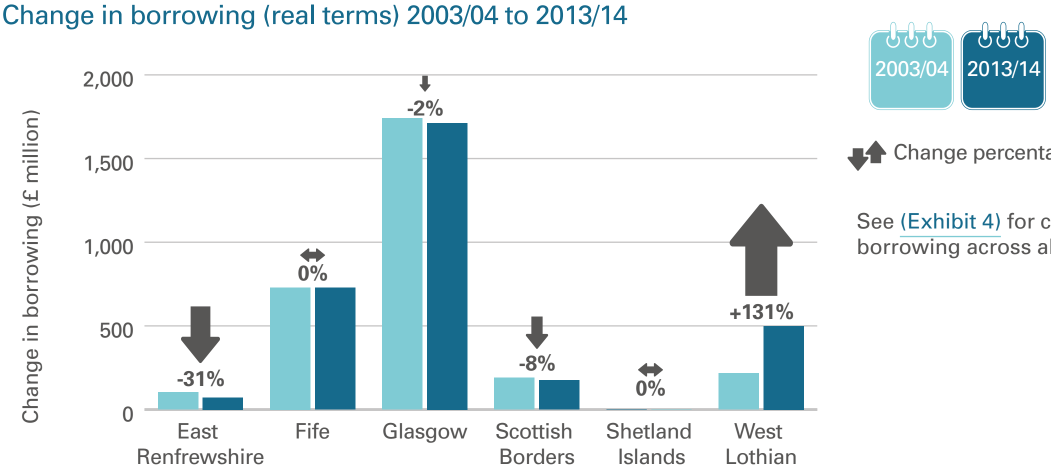
Exhibit 9
Key borrowing facts for our six fieldwork councils

Graph A
2013/14 debt levels

See (Exhibit 3) for overall picture and councils' debt levels

Source: Council audited annual accounts 2013/14; *Mid 2013 Population Estimates Scotland*, National Records of Scotland, June 2014

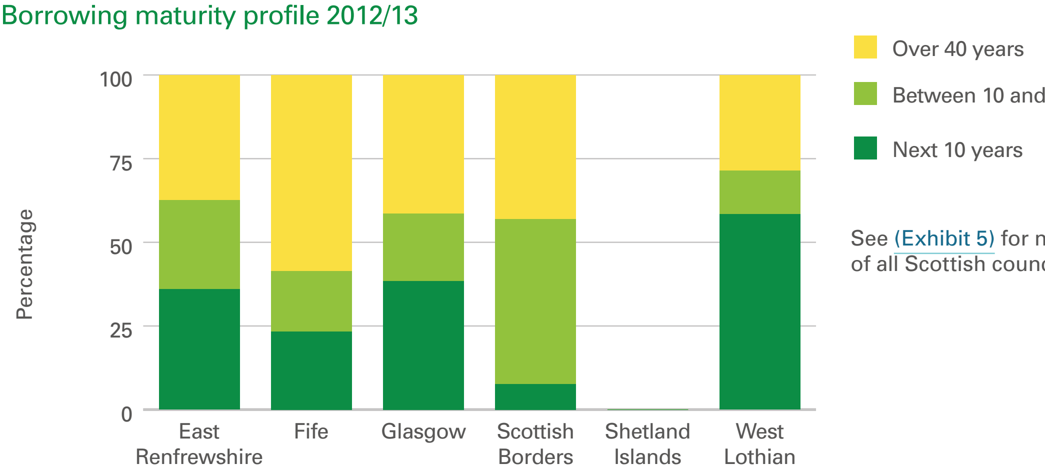
Graph B
Change in borrowing (real terms) 2003/04 to 2013/14



See (Exhibit 4) for change in borrowing across all councils

Source: Council audited annual accounts 2013/14

Graph C
Borrowing maturity profile 2012/13



See (Exhibit 5) for maturity profile of all Scottish councils' debt

Source: *Capital Expenditure and Treasury Management*, CIPFA Statistics, June 2014

Exhibit 9 (continued)

East Renfrewshire Council

- Just over half of East Renfrewshire's debt relates to PFI/PPP schemes for schools and roads **(Graph A)**.
- The council has not undertaken any external borrowing since 2009/10. The overall level of borrowing has been reduced by 31 per cent compared to ten years ago **(Graph B)**.
- The borrowing maturity profile generally follows the national profile with approximately one-third of borrowing to be repaid in next 10 years and one-third over 40 years **(Graph C)**.
- Capital investment requirements are currently being met with cash from reserves, cash balances and cash flow.
- The council will need to borrow to participate in the City Deal project.

Fife Council

- Borrowing makes up 90 per cent of the council's total debt **(Graph A)**.
- The council has borrowed £165m since 2008/09. The level of borrowing has remained static compared to ten years ago **(Graph B)**.
- Almost two-thirds of borrowing needs to be repaid in 40 years or more **(Graph C)**.
- The council uses a combination of cash, council reserves and borrowing to meet capital investment requirements.
- The council is a pilot site for a TIF scheme which will involve an element of borrowing.

Glasgow City Council

- Borrowing makes up 90 per cent of the council's total debt **(Graph A)**.
- The council has taken out loans of £677m since 2008/09. The overall level of borrowing has decreased slightly, by two per cent, compared to ten years ago **(Graph B)**.
- The borrowing maturity profile is broadly aligned with the national profile **(Graph C)**.
- The council uses funds and reserves, and has a preference for cheaper short-term borrowing for capital investment purposes.
- The council will need to borrow to participate in the City Deal project.

Scottish Borders Council

- Borrowing makes up 75 per cent of the council's total debt **(Graph A)**.
- The council has taken out loans of £7.5m since 2008/09. Overall level of borrowing has fallen by eight per cent compared to ten years ago **(Graph B)**.
- It has a small proportion of borrowing maturing in the next ten years when compared to other councils **(Graph C)**.
- The council has been using reserves cash balances and cash flow for capital investment.
- It has received consent to borrow for lending to support the National Housing Trust and Registered Social Landlords.

Shetland Islands Council

- The council borrowed for the first time in 20 years in summer 2014. Borrowing is only planned to fund the new Anderson High School, the council is using cash balances or reserves to fund other capital expenditure.
- It will borrow for capital expenditure if interest rates are lower than average investment return.

West Lothian Council

- Borrowing makes up around 90 per cent of the council's total debt **(Graph A)**.
- Has taken out £371m in new loans since 2008/09. Overall level of borrowing has increased compared to ten years ago **(Graph B)**.
- Over half (59%) of the council's borrowing is due to mature in the next ten years **(Graph C)**.
- Will continue to borrow externally while interest rates remain low.

Source: Audited accounts 2003/04–2013/14, Audit Scotland; CIPFA Statistics

Part 2

Demonstrating the affordability and sustainability of borrowing

Key messages

1 The six councils in our sample are following the general principles and framework of relevant codes and regulations.

2 Councils are using the prudential indicators to demonstrate and monitor the short-term affordability of borrowing. But councils are not clearly analysing and reporting their assessment of the longer-term affordability and sustainability of borrowing. Officers present the repayment profile of borrowing to councillors, but are not presenting this together with other information such as different budget scenarios, interest rates scenarios, or capital investment strategies. This is important to inform councillors of the future risks to the affordability and sustainability of current and new borrowing.

3 Long-term financial planning will help councils develop more detailed analysis on the longer-term affordability and sustainability of borrowing.

4 Councils could present information more clearly to councillors. Some councils are not presenting councillors with all the relevant information at one time to support borrowing decisions, for example in the treasury management strategy. This is important to ensure that decisions made are based on an assessment of all the relevant analysis and risks.

clear reporting to councillors on affordability and sustainability is important for sound decision making

Councils assess the short-term affordability of borrowing

31. Councils should have short, medium and long-term financial strategies that include the financing cost of borrowing and other debt and show the impact on the revenue budget. Decisions on borrowing and other debt need to be taken on the basis of affordability.

32. Our evidence shows that councils demonstrate the short-term implications of borrowing and other debt financing on the revenue budget through use of the prudential indicators. There are 12 prudential indicators that councils must set for each year. Eleven of them must be set for a minimum of three years ahead. Two of these 11 indicators specifically highlight the affordability of capital investment decisions, including borrowing (Exhibit 10, page 23). These indicators cover all debt and are not specific to borrowing.

Exhibit 10
Affordability prudential indicators

Indicator	What it means	What it is used for
Financing cost to net revenue stream: actual and estimated for next three years	The percentage of the revenue budget set aside each year to pay debt financing costs	• Assesses the risk to future budgets, eg from changing interest rates • Provides comparisons over time • Measures the impact of changing financing costs on the financial strategy
Impact of capital investment decisions on council tax and housing rents	This estimates the impact of new capital investment decisions on council tax and on the average weekly housing rent	• Allows councillors to consider all the council's plans at budget setting time • Allows comparison of different capital financing options by assessing the potential impact on council tax or housing rents

Source: CIPFA Prudential Code

33. The Prudential Code requires councils to estimate the impact of capital investment on the budget for the next three years, as a minimum. No councils in our sample reported estimates for a longer timeframe, and no councils had developed their own indicators to assess affordability. The Prudential Code suggests that councils use their own additional indicators, and this would be a good option for councils to monitor an impact that was important and relevant to their strategy.

34. The indicator 'financing costs to net revenue stream' is used to show how much of council income would be used to pay borrowing and debt charges. For councils with housing, they must separately calculate this indicator showing how much of housing rents income will be required to finance housing-related borrowing and debt charges. Exhibit 11 (page 24) shows the data published by West Lothian Council to provide an example of how this indicator is used.

Exhibit 11

An example of a council's ratio for 'financing costs to net revenue stream'

West Lothian Council is planning to invest in its assets over the next three years, including a council house new build programme. This is shown by the increasing capital financing requirement. Its strategy is to borrow in order to finance this capital investment. The impact of this is to increase the ratio of 'financing costs to net revenue stream' for both the general revenue budget, and the housing budget. This example shows that there is an expected increase in the proportion of income used to finance capital investment over the next three years. It will increase from 7.3 pence of every £1 to 8.6 pence. In relation to investment in housing the expected increase is from 20.8 pence in every £1 of housing rent income to 31.2 pence.

	2013/14 actual	2014/15 estimate	2015/16 estimate	2016/17 estimate
Capital financing requirement				
General Fund	£438,788	£444,404	£446,834	£446,534
Housing	£148,885	£174,561	£200,871	£226,174
Ratio of financing costs to net revenue stream				
General Fund	7.3%	7.8%	8.3%	8.6%
Housing	20.8%	25.4%	28.9%	31.2%

Source: West Lothian Council treasury management annual and prudential indicator reports

Councils are not making good use of all prudential indicators

35. The indicator for the 'impact of capital investment decisions on the council tax/housing rents' is a good example of how councils demonstrate, to councillors and the general public, what the financial implications of council decisions could be for members of the public. This could be an increase or decrease in council tax or housing rents.

36. We found that all councils are reporting this indicator. Out of our sample, three of the 11 councils that we reviewed did not report any impact of capital investment on council tax.[1] The main reason for councils not doing this is that there is currently a freeze on councils' ability to increase council tax. We acknowledge that while the council tax freeze remains, council tax may not increase, but the indicator can still be used to demonstrate what the potential impact of capital investment plans would be. The council tax freeze makes it more important to show how much of the budget is being used to finance capital investment. Councils may also seek to reduce any impact on the budget through making savings. In these cases, we would expect this to be clear in the narrative to the indicator.

Councils are not clearly analysing and reporting the long-term affordability and sustainability of borrowing decisions

37. Councils face reducing revenue budgets and increasing demand for services. As a result many councils have projected funding gaps and need to generate recurring long-term savings. Councils' existing borrowing commitments extend for up to 50 years, and while any current decisions to borrow allow the council to invest in services they also place more pressure on revenue budgets. Councils therefore need to clearly set out how current and past borrowing decisions impact on the future revenue budget over the life of the borrowing term. The Prudential Code sets out a minimum three years for reporting prudential indicators. Borrowing commitments can extend up to 50 years and, in our view, three years is inadequate to demonstrate to councillors the affordability of borrowing.

38. We found that, while councils were demonstrating the impact of borrowing decisions over a three-year period using prudential indicators, none of the councils in our sample presented councillors with a longer-term view. The Prudential Code provides a minimum framework for councils to demonstrate and monitor the impact of their capital financing decisions on their future budget and income streams. In our view councils could extend the use of the framework and provide an extended analysis to demonstrate the longer-term affordability of borrowing. Officers could provide us with: information on capital investment requirements for up to ten years, when borrowing is due to be repaid and what this will cost, and interest rate forecasts, but there was no analysis bringing this together with budget scenarios to assess affordability. Councillors are not therefore always provided with information on the future affordability of new borrowing and the potential risks. This analysis should bring together the financing charges for all debt, to consider peaks in charges, and the additional risks of new borrowing or debt to this affordability profile.

Demonstrating the affordability and sustainability of borrowing needs effective long-term planning

39. Our report on *Scotland's public finances: Progress in meeting the challenges* [PDF] highlighted a lack of long-term financial planning. Long-term financial planning should include scenario planning to outline the different options available to the council based on a range of different assumptions about income, expenditure and activity. The borrowing and treasury management analysis could expand on this financial planning to look at the impact on affordability of using borrowing or different finance methods within each of the options. It could also add external assumptions including changes in interest rates to look at future risk factors to the affordability of borrowing. Exhibit 12 (page 26) highlights how the information in a long-term financial plan can be used to inform detailed analysis on borrowing and treasury management.

40. This more detailed analysis and scenario planning would allow officers and councillors to be clear about the evidence supporting decisions on borrowing. It would highlight all the financing options available and the risks and affordability of each option. Councillors would be aware of any risks when making a decision. As councils are required to produce an annual treasury management strategy, such analysis could be included in the strategy. The strategy would bring together all the key information and set out the supporting evidence. As a public document this would increase the transparency of council decisions.

Councils' treasury management strategies need to clearly demonstrate a more integrated approach

41. The treasury management strategy provides the council with an opportunity to set out its approach and rationale to borrowing, and to provide assurance on how borrowing and treasury management activity will help the council to meet its objectives. Strategies should clearly demonstrate the links to other council

Exhibit 12
The key components of long-term borrowing analysis

Components of long-term financial planning	Essential elements to inform a long-term borrowing analysis	Example
Scenario planning Scenario planning to outline the best, worst and most likely scenarios of the financial position and the assumptions used	• Projections for financial settlements, both revenue and capital • Long-term economic forecasts and inflation rates • Projections for interest rates	The council develops scenario plans for the revenue budget based on a range of assumptions about future revenue streams. This is compared with projected borrowing charges to highlight potential periods of pressure on the revenue budget
Assets and reserves Details of assets and reserves and how these will change over time	• Borrowing profile and schedule of repayments • Future reserves policy and contingency levels • Projected reserve levels (based on scenario planning above) • Future impact of asset management plans	A council is currently using reserves to finance capital investment. It could use different combinations of borrowing and reserves to finance projected capital investment needs. The council should model these different combinations to show the impact on reserve levels and the revenue budget. This would highlight the risks and benefits of each combination
Capital investment activity Details of investment needs and plans and how these will be paid for	• The impact of future service demands on capital investment needs. There may be a range of options • Estimated cost of the capital investment options • Future available funding options • Projected borrowing rates	A council has a range of existing borrowing and wider debt, including PFI. The council should prepare analysis showing the combined financing charge to the revenue and service level budget over the life of the asset or borrowing term. This would be based on different scenarios of interest rates or inflation. If the council wants to invest in more capital, it can model the additional impact of borrowing or debt onto this analysis

Source: Audit Scotland

strategies and plans such as the capital programmes, short, medium and long-term financial strategies, reserves policies, etc. The strategy enables councils to bring together this key information and to show how borrowing decisions fit into this bigger picture.

42. We evaluated strategies against the requirements and good practice recommendations of the Prudential Code, Treasury Management Code and Scottish Government investment regulations. The codes and regulations largely cover operational practice, and councils generally met their requirements. We found the language of the codes and regulations difficult to interpret. Strategies that followed the good practice recommendations as well as the requirements were clearer and told a better story about the council's intended direction for borrowing and treasury management. Scottish Borders Council presents this wider story within its strategy and it is a good example of a clearer strategy.

Not all strategies clearly show the link to corporate and capital plans

43. None of the strategies of our fieldwork councils refers directly or provides links to corporate objectives. This is important to demonstrate how the proposed strategy will help the council to meet its overall aims and objectives and improve services to communities.

44. Councils' treasury management strategies link plans for future capital investment, the financing and affordability of those plans and how cash will be safely managed to meet a council's financial commitments. We acknowledge that there is a wider process within councils to consider and agree capital investment programmes and plans. This includes the use of capital working groups or committees, usually comprising a mix of officers and councillors. These are not usually public forums and the associated reports and papers are not usually public documents. As outlined at paragraph 41, the treasury management strategy is the public document that should bring together capital investment plans and the financing of those plans, including borrowing. In our view, it is the appropriate document for councils to use to demonstrate that other options have been considered. Some councils choose not to approve annual capital investment plans, for example Glasgow City Council approved a two-year capital plan for 2013/14 and 2014/15. It is important therefore for councils to reflect the links to capital investment plans in their annual strategy.

45. Councils do not borrow for specific projects but consider how to finance their whole capital investment programme each year. In identifying the capital expenditure for the year they identify internal sources available before considering borrowing. The Prudential Code requires councils to calculate their 'capital financing requirement', which is the capital expenditure that they need to finance from other sources, that is, through borrowing or other method of external finance.

46. References to the capital programme and capital investment plans vary in detail within strategies. Councils are making better links between treasury management and capital investment at operational level through closer working between treasury management and capital functions but this link is not always reflected in strategies. Glasgow City and East Renfrewshire councils refer to the capital financing requirement and prudential indicators within their strategy, making the link to capital investment. The Scottish Borders Council strategy is clearer and provides a much wider perspective on its capital investment plans in the strategy including capital expenditure forecasts, capital financing assumptions, the predicted borrowing need and affordability. Relevant prudential indicators are used throughout the strategy.

47. We found little evidence of councils actively sharing strategies with each other to inform good practice, or different ways of presenting information. Some strategies, for example councils in the Lothian region, had similar sections and wording.

Councils are not always using the strategy to clearly explain the prudential indicators

48. We found variation in how councils link the prudential indicators with the treasury management strategy and how the strategy fits with the revenue budget setting process. Councils should use the prudential indicators to demonstrate affordability, prudence and sound treasury management in capital investment decisions. The local authority investment regulations recommend that the treasury management strategy will cover capital, investment and borrowing and the prudential indicators.

49. Only two of six fieldwork councils (Scottish Borders and Shetland Islands councils) included the prudential indicators as a key part of the strategy. Other councils included these indicators as an appendix, and East Renfrewshire Council reports the indicators separately in a different report.

50. We found that councils are setting and reporting on prudential indicators to the full council and appropriate committees but the level of commentary provided within reports is variable. References in reports to the indicators are based on the technical definitions, with few giving the overall context and implications. This is particularly the case where the prudential indicators are provided solely as an appendix to the treasury management strategy or a separate report. A lack of context means that the council is not providing an explanation of how it is actively using the indicators to measure and monitor the affordability of borrowing. Nor is it explaining what the indicators actually mean for the council and its communities, in terms of increasing or decreasing pressure on budgets, or any risks highlighted by the forecast indicators.

Recommendations

Council officers should:

- use the treasury management strategy to present a wider strategic view of borrowing and treasury management. It should use clear and accessible language and be prepared for councillors as the key audience. It should include how the borrowing strategy is informed by corporate priorities and capital investment needs. The strategy should include:
  - links to capital investment plans and corporate objectives
  - all borrowing and other debt
  - prudential indicators as a core part of the strategy
  - a clear assessment of the affordability and the impact on revenue budgets both in the short and long term
- create more detailed and longer-term borrowing and treasury management analysis as informed by the council's financial strategy. It should include:
  - scenario planning to show the potential impact of different budget scenarios, income generation plans, and changes in external factors such as interest rates
  - analysis of capital financing options, to compare affordability and sustainability between different debt and borrowing options
  - the use of indicators over a longer period than the minimum three years set by the Prudential Code
- share strategies with other councils to help inform good practice and exchange of ideas.

Part 3

Effective management and scrutiny

Key messages

1 Treasury management is a professionally run function in councils with appropriately qualified officers. Joint planning with other councils, ongoing training and the availability of appropriate professional qualifications are important.

2 Scrutiny of borrowing and treasury management decisions could be improved. This involves officers providing clearer information to councillors to help them in their scrutiny role. In most councils the content and clarity of reports could be improved, particularly performance information in year-end reports. All reports need to be to be easily accessible to councillors and the public.

3 Councils need to provide a range of training and support to councillors to help improve scrutiny of treasury management. We found no additional formal arrangements in place specifically aimed at helping councillors in this complex area.

4 We found some examples where governance structures do not fully meet the codes' requirements and where there could be more consistency in reporting arrangements.

councillors need a combination of scrutiny skills and knowledge of treasury management to carry out their role effectively

Treasury management is a professionally run function

51. Treasury management staff in councils deal with the day-to-day treasury functions, including managing short-term cash. They also develop the treasury management strategy and related reports to councillors. The links between the capital investment function and treasury management functions have been strengthened over the last ten years in the councils we visited. The staffing structure within most councils deliberately brings the functions together. For example Scottish Borders Council has a structure that places capital investment and treasury management functions together. It also undertook a recent restructuring to separate out day-to-day transactions, allowing capacity for the development of forward planning and strategic development. In Fife Council the treasury management and capital investment functions are separate. However, staff from the capital investment function have been working in the treasury management function and this has strengthened the links between the two functions.

52. The size of the treasury management function is related to a council's size and budget. The number of personnel involved in treasury management in our sample varied from less than a full-time equivalent at East Renfrewshire Council to two full-time equivalents at Glasgow City Council. We would expect staff numbers to vary across councils according to the level of treasury management and borrowing activity, and the budget.

53. Officers involved in treasury management have relevant experience and qualifications, and some hold the CIPFA treasury management qualification. Training for new officers is currently provided by on-the-job experience, CIPFA treasury management network events, the treasury management forum, technical updates and toolkits, Capita seminars and training sessions.

54. Treasury management is an important function in councils and they need to actively plan for the succession of qualified staff members and other professional training needs that may arise. CIPFA do not currently provide the treasury management qualification owing to insufficient demand but have enhanced their treasury management network. Other treasury management qualifications are available for councils to consider.

55. Officers recognise that keeping in contact with other treasury managers and those involved in treasury management is critical. The CIPFA treasury management forum provides a source of information that enables officers to develop knowledge, discuss areas of concern and share information.

56. All councils use external treasury management advisers. The services provided include professional treasury management advice, seminars and training for officers and elected members and regular information on economic forecasts. Capita provides services to 28 Scottish councils, including all of those in our sample. There is an inherent risk in having a single provider of advice to so many councils, however, we found that all councils had bought services through open tendering processes within the last four years for terms of between three to five years. All council officers meet regularly with Capita to review their objectives, options, strategies and performance.

Council governance structures are in place but not all meet code requirements

57. The codes of practice and regulations place certain requirements on a council's governance structures:

- They recommend that the full council should approve the treasury management strategy.
- They require a specific committee to be responsible for scrutinising reports.
- They also require borrowing and treasury management activities to be structured and managed in a fully integrated manner and for responsibilities to be clear.

58. CIPFA considers that it is an essential part of a public service organisation's treasury management arrangements to have clearly defined responsibilities for approving and scrutinising borrowing and treasury management activities. Exhibit 13 (page 32) includes a summary of the main tasks involved in treasury management and suggested allocation of duties.

Exhibit 13
Allocation of responsibilities for scrutinising borrowing and treasury management activities

Full council	• Receives and reviews reports on treasury management policies, practices and activities • Approves annual strategy
Committee or panel with responsibility for scrutiny	• Approves or amends the organisation's treasury management policy statement and treasury management practices • Considers and approves budget • Approves the division of responsibilities • Receives and reviews regular monitoring reports and acts on recommendations • Approves the selection of external service providers and agrees terms of appointment • Reviews the treasury management policy and procedures and makes recommendations to the responsible body
The responsible officer	• Monitors the council's compliance with policy and practices • Submits regular treasury management policy reports • Submits budgets and budget variations • Recommends the appointment of external service providers

Source: Audit Scotland

59. For our sample of 12 councils we looked at the approval, recommendations and scrutiny for each report. Most councils fully met the requirements of the codes but we found the following arrangements that were not in line with the codes' requirements and other arrangements that may not give members the opportunity to scrutinise reports consistently:

- The treasury management strategy at Glasgow City Council is considered and approved by the Executive Committee. The full council considers and approves the minutes of the Executive Committee.
- The governance structure at Fife Council is such that the Executive Committee has responsibility for all budget and treasury management decisions. Full council then approves treasury management reports through the minutes.
- Shetland Island Council's Executive Committee approves the treasury management strategy but receives no other reports.

- In East Renfrewshire Council, the Audit and Scrutiny Committee approves the strategy but the Executive Cabinet scrutinises the mid-year, and year-end reports.

Councillors need further support to improve their scrutiny role

60. Borrowing and treasury management decisions are complex and involve a significant level of financial risk. It is essential that any decisions are effectively scrutinised to demonstrate sound financial management and help councils achieve their local outcomes and priorities. Councils' scrutiny committees are a vital part of a council's governance arrangements and it is important that these committees are effective. Councils have a responsibility to ensure that those charged with governance have access to the skills and knowledge they need to carry out their role effectively. The councillors on committees need to have a combination of technical knowledge and scrutiny skills for the committee to be most effective. Those charged with governance also have a personal responsibility to ensure that they have the appropriate skills and training for their role. We found that councils provide both scrutiny training and treasury management training to councillors. Scrutiny training tends to be provided at the start of a political term, or for new councillors, as part of the induction process.

61. In areas of high importance and complexity, such as treasury management, additional scrutiny arrangements can be put in place. For example:

- Councils seek members with appropriate expertise for the relevant scrutiny panel.
- Councils nominate lead members for borrowing and treasury management to help guide other members.
- Councils seek external expertise to help members on the scrutiny committee.

62. We found some examples where this was being applied. Scottish Borders Council appoints non-executive members to its Audit Committee to provide financial expertise. Fife Council has a lead member for finance. Some councillors on scrutiny committees have highly relevant financial experience but, apart from Scottish Borders Council, councils do not have formal processes in place for selecting councillors with relevant skills.

63. The most important aspect of scrutiny is the challenge of reports and information presented to councillors through asking questions. We found variation in the type of questions that councillors ask, from issues of detail to clarification of the meaning of phrases in reports. Some councillors told us that they are not always confident in challenging the strategy and framework for future decisions and asking questions about the content of reports. Many have built up trust and confidence in officers and look for officers to highlight issues or problems for them. All councillors we spoke to would welcome additional support in their scrutiny role. We have prepared a supplement to this report which includes questions to help councillors in their scrutiny role.[2]

Officers need to present clearer and fuller information to councillors to help them scrutinise treasury management activity and risks

64. CIPFA's Treasury Management Code states that councils or committees will receive regular monitoring reports on treasury management activity and risks. Regular reporting with a clear and full analysis of performance and activity helps members to:

- understand why officers are proposing decisions
- understand the risks
- ask relevant questions.

65. The Treasury Management Code sets out three minimum reporting requirements for councils:

- a strategy in advance of the year
- a mid-year review
- an annual report after the financial year-end.

66. We found that all councils meet these requirements. However, both Fife and Glasgow City councils prepare a single report covering both the annual report for the previous year and the mid-year review for the current year. In our view this does not meet the intention of the code. These mid-year and annual reports are an important source of information to help councillors effectively monitor and review treasury management activity. Councillors need time to consider any comments or make changes from scrutiny of the annual report to influence activity or performance for the following year.

67. No councils have reporting arrangements that go further than the minimum required by the code, for example quarterly performance or monitoring reports, or more detailed performance reports for the scrutiny committee.

68. We found that councils do not hold separate risk registers for treasury management but they are included in their wider finance risk registers. Reports on the wider finance risks may not be considered by the same committee considering treasury management reports. This means that councillors are not informed of any relevant treasury management risks.

Councils could improve the content and clarity of reports

69. We found that both the layout and content of treasury management reports could be improved, particularly year-end reports on performance. Annual reports are the main performance report and vary in quality. Performance monitoring, including information on the actual figures for the prudential indicators against forecast figures, is not reported fully or consistently across all councils. Some councils only report against indicators and some do not report performance at all. Some of the reports we reviewed did not provide any comparative data. This meant that readers could not reach an objective opinion on performance.

70. From the review of the councils in our sample, we found the following:

- Clackmannanshire, East Lothian, Midlothian, Scottish Borders, Shetland Isles, West Dunbartonshire and West Lothian councils all provided comparative information in their annual reports on all indicators.
- East Renfrewshire, Fife and Renfrewshire councils provided comparative information on some of their indicators.
- Glasgow City Council provided information only on the actual performance without any estimates.
- City of Edinburgh Council did not include any detail on indicators in the annual report, but some are reported in capital monitoring reports.

71. Most treasury management reports are publicly available, although they were not always easy to find on councils' websites. This lack of clear and accessible information means that it is difficult for members of the public to understand how borrowing and treasury management activity is contributing to their council's priorities, and to understand what the performance of the council has been.

72. Officers must use accessible language when reporting on borrowing and treasury management but many strategies and reports contain a lot of technical language. This does not help councillors scrutinise effectively as any questions they ask are more likely about clarity rather than challenge. Exhibit 14 (page 36) shows how Shetland Islands Council used worked examples to explain to councillors why it was recommending to borrow for the first time.

Councils should provide a wider range of training and support to improve councillor attendance and help them in their scrutiny role

73. All councils provide training on treasury management to councillors. This consists of courses provided once or twice a year and, in West Lothian Council, when a new administration is formed as a minimum. Attendance is voluntary although it has been generally poor (varies between 40 and 100 per cent attendance for these sessions), (Exhibit 15, page 37). Attendance at training events is focused mainly towards councillors who sit on relevant scrutiny committees rather than all councillors.

74. Councillors' views on the training they attend are positive. Councillors also felt officers gave them extra support if required, for example by providing additional information or responses to any questions they had.

75. Training and support for councillors should aim to equip all councillors with a minimum level of knowledge and understanding. We found councillors' experience varied, for example from councillors who had been accountants or finance directors to those with little or no previous finance experience.

76. Councillors told us that it was often difficult to attend training owing to other commitments. In their view, a full-day training course was a substantial commitment. Regular training will be required to keep councillors up to date with economic developments. As councillors only consider treasury management issues, on average, three times a year, the timing of the training is important. Councils should consider different ways to provide training including courses, short briefings and perhaps online training.

Exhibit 14
How officers at Shetland Islands Council explained why it was recommending the council borrow

The economic case for borrowing externally, or using the council's own reserves to finance capital expenditure, is essentially down to whether interest rates are higher or lower than the long-term average return on the council's external investments.

If interest rates are higher than the long-term average return on the council's investments (currently 5.75%) then it means the cost of borrowing is higher than the lost income forgone by using reserves. So it would make financial sense to use reserves for capital expenditure.

For example, if interest rates were 10% for a £1m loan:

- Annual interest payable on £1m at 10% = £100,000
- Investment income of 5.75% generated on £1m = £57,500.

In this example to borrow would cost £100,000 a year, and to use reserves would present an opportunity cost of £57,500 in lost investment income. In this example, using reserves would present a saving of £42,500 per year over using borrowing.

However, the reverse is true if interest rates are lower than the long-term average return on the Council's investments (currently 5.75%).

For example if interest rates were 2% for a £1m loan:

- Annual interest payable on £1m at 2% = £20,000
- Investment income of 5.75% generated on £1m = £57,500.

In this example, to borrow would cost £20,000 a year and to use reserves would present an opportunity cost of £57,500 in lost investment income. In this example borrowing would save the council £37,500 per year.

Therefore when interest rates are lower than long-term investment returns, the default position of the council should be to borrow in order to achieve a Best Value outcome.

Source: Shetland Islands Council Borrowing Strategy 2014/15

Exhibit 15
Councillor attendance at treasury management training

	East Renfrewshire	Fife	Glasgow City	Scottish Borders	Shetland Islands	West Lothian
Date of last training	2014	2014	2013	2012	2014	2011
Frequency	Annually	Biannually	Annually	Biannually	Annually	Each administrative term
Offered to	Full council	Full council - but target Executive Committee members	Members of Executive Committee and members of Finance and Audit Scrutiny Committee	Audit Committee	Full council	Full council
% attendance full council	40%	11.5%	22.8%	91%	Not available	46.8%
% attendance Scrutiny committees	57% Scrutiny 37.5% Cabinet	40.9%	66.7% Scrutiny 40% Executive	100%	Not available	Not available Committee structure changed

Source: Audit Scotland

Recommendations

Council officers involved in borrowing and treasury management should:

- carry out joint planning with other councils to identify future qualification and training needs and enhance their capacity, in order to negotiate with training providers
- review the content of year-end reports to ensure they provide an assessment of the effectiveness of the year's borrowing and treasury management activities and the performance of the treasury management function. This should include appropriate indicators, comparative figures, and appropriate explanations.

Council officers and councillors involved in treasury management should:

- review governance arrangements, and update as necessary, to ensure they provide:
  - the treasury management strategy, mid-year and year-end reports to the same council committee, and that the full council has access to them
  - councillors with mid-year reports by the end of December each year
  - councillors with the wider picture, that is, make the links to capital investment decisions and revenue budgets
  - councillors with access to all reports relating to borrowing and treasury management activity including risk registers
- ensure scrutiny arrangements are robust by:
  - considering widening the range of training options to councillors on borrowing and treasury management activities and whether this training should be mandatory
  - considering whether training for councillors provides a balance of scrutiny skills and knowledge of treasury management.

Endnotes

◀ 1 Glasgow City Council, Renfrewshire Council and West Lothian Council. As Shetland Islands Council did not borrow until 2014/15, we would not expect this indicator to be set for 2013/14.

◀ 2 *Borrowing and treasury management in councils: Scrutiny guidance and questions for councillors,* [PDF] Audit Scotland, March 2015.

Appendix 1

Audit approach

Our audit looked at councils' strategies for borrowing and treasury management and whether councils can demonstrate the affordability and sustainability of their borrowing decisions over the short and long term. Councillors have a crucial role in holding officers to account and this report also evaluates this. We did not evaluate day-to-day cash, investment and borrowing transactions.

Methodology

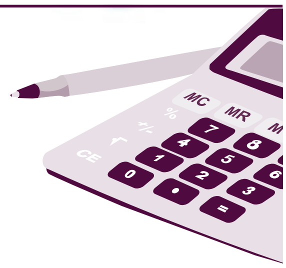
To achieve our aim and objectives, our audit included reviewing documents, analysing data and interviews. The audit had three main components:

Data analysis: We analysed information on borrowing and debt from councils' audited accounts, CIPFA statistics and the Scottish Government in order to inform a selection of 12 councils for further desk research. The 12 that were selected were City of Edinburgh, Clackmannanshire, East Lothian, East Renfrewshire, Fife, Glasgow City, Midlothian, Renfrewshire, Scottish Borders, Shetland Islands, West Dunbartonshire and West Lothian councils. The councils were selected to include a mix of council size and to reflect initial thoughts, based on our financial analysis, that they had different approaches and strategies to borrowing and treasury management.

Desk research: We reviewed a range of relevant written material on borrowing and treasury management, focusing on the treasury management strategies for our 12 councils. We also looked at the committee arrangements for consideration of these and other treasury management reports. This informed our sample of six councils for interview. We selected the sample so that it included large, small, urban and rural councils and reflected different levels of borrowing and other forms of debt.

Interviews with councils and stakeholders: We visited six councils to find out more about their approach and strategy for treasury management, their governance arrangements and scrutiny and training for councillors. We spoke to council leaders and councillors about their role in scrutinising borrowing and treasury management and their experience of the training and support received. We also interviewed representatives from organisations including the Scottish Government, CIPFA and the CIPFA Scottish Treasury Managers' forum.

Appendix 2



Membership of the project advisory group

We would like to thank members of the advisory group for their input and advice throughout the audit.

Member	Position
Andy Witty	Policy Officer, COSLA
David Robertson	Chief Financial Officer, Scottish Borders Council
Gareth Davies	Policy and Technical Officer, CIPFA Scotland
Hazel Black	Head of local authority accounting, Scottish Government
Innes Edwards	Treasury Manager, City of Edinburgh Council

Note: Members of the project advisory group sat in an advisory capacity only.

Borrowing and treasury management in councils

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