

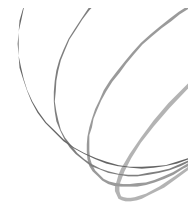
Lothian and Borders Fire and Rescue Board

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



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Introduction

1. This report summarises the findings from our 2007/08 audit of the Lothian and Borders Fire and Rescue Board. The scope of our audit was set out in our audit plan issued in April 2008.
2. The financial statements of the board are the means by which it accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources. It is the responsibility of the board to prepare financial statements that present fairly its financial position and the income and expenditure for the year.
3. The members and officers of the board are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:
 - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed
 - the board's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests
 - the board has adequate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability
 - the systems of internal control provide an appropriate means of preventing or detecting material misstatement, error, fraud or corruption
 - the board has proper arrangements for securing best value in its use of resources.



Financial statements

Introduction

4. In this section we summarise key outcomes from our audit of the board's financial statements for 2007/08. We also summarise key aspects of the board's reported financial position and performance to 31 March 2008.
5. We audit the financial statements and give an opinion on:
 - whether they present fairly the financial position of the board and its expenditure and income for the year
 - whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.
6. We also review the statement on the system of internal financial control by considering the adequacy of the process put in place by the board to obtain assurances on systems of internal financial control and assessing whether disclosures in the statement are consistent with our knowledge of the council.

Overall conclusion

7. We have given an **unqualified** opinion on the financial statements of the Lothian and Borders Fire and Rescue Board for 2007/08.
8. The unaudited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June. The only amendment to the unaudited figures was a prior year adjustment relating to accounting for fixed assets of £1.144 million
9. In addition on 10 September an adjusting post balance sheet event occurred when the Scottish Public Pensions Agency issued Scottish Fire and Rescue Service Circular 14/2008. Essentially this circular resulted in the crystallisation of a contingent liability that was disclosed in the unaudited accounts with respect to the Firefighters Pension Scheme, changes with an estimated cost of £0.341 million, and a commitment by the Scottish Government to fund these costs.
10. The board is required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP'). A number of presentational changes were made to the draft accounts made available for public inspection to reflect the disclosure requirements set out in the SORP and for typographical errors. We would recommend that the draft accounts are subject to full review by management prior to submission for audit.



11. Audited accounts were finalised by the target date of 30 September 2008 and are now available for presentation to the board and publication. The financial statements are an essential means by which the board accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources.

Financial position

12. The surplus or deficit on the income and expenditure account measures the board's financial result for the year, recognising the resources that have been consumed and generated in accordance with Generally Accepted Accounting Principles. The board's net operating expenditure in 2007/08 amounted to £65.0 million and was met by constituent authorities' contributions of £47.2 million (including additional contributions of £0.341 million in respect of revised pension commutation factors), resulting in a net expenditure deficit for the year of £17.8 million.
13. However, the movement on the general fund balance is an important aspect of the board's stewardship as the main budget reference point, the main differences being:
 - capital investment is accounted for as it is financed, rather than when assets are consumed
 - retirement benefits are charged as amounts become payable to pension funds and pensioners rather than as future benefits are earned.
14. After adjusting for these items, the board achieved a general fund deficit of £0.640 million. During the year there was a transfer from earmarked to unallocated reserves of £1.689 million. This, together with the general fund deficit for 2007/08 results in an increase of £1.049 million and represents an improvement of £0.612 million on the approved budget of £0.437 million. This arose from savings in a range of costs including reductions in staff costs and capital charges and an increase in income from secondments. These savings were, however, reduced by a £0.334 million overspend on operating costs; predominantly on supplies and services.
15. The Police and Fire (Scotland) (Finance) Act 2001 limits the carry forward of unspent requisitions for the year to 3% of the annual funding received from the board's constituent councils, cumulative reserves are limited to 5% of this annual funding. Excluded from this carry forward limit are earmarked amounts held in respect of future commutation liabilities. At 31 March 2008, the service held a reserve of £4.082 million, of which £1.290 million has been earmarked for future pension commutations. While a further amount of £1.282 million has been earmarked for future capital expenditure this needs to be included with unallocated balances in determining whether the prescribed limits for the general fund have been exceeded. At 31 March 2008 unallocated balances totalled £2.792 million, which is within the permitted limit.



16. Capital expenditure totalled £3.2 million and was funded through government grants of £2.85 million, revenue contribution of £0.252 million and capital receipts of £0.083 million. This represents an underspend of £3.260 million against the budget of £6.445 million principally due to slippage in the progress of the board's service improvement plan.

Accounting practice

Going concern

17. The board's balance sheet shows a net liability of £217.2 million. The negative balance reflects the pensions liabilities falling due in future years. Auditing standards require auditors to consider an organisation's ability to continue as a going concern when forming an opinion on financial statements. One of the indications that may give rise to going concern considerations is an excess of liabilities over assets.
18. The board's statement of accounting policies confirms that it has been considered appropriate to adopt a going concern basis for the preparation of the financial statements as the constituent councils have a legal obligation to fund the net expenses of the board. Future pension liabilities will therefore be met, as they fall due by contributions from constituent authorities and government grant in the normal way. We are satisfied that the process the board has undertaken to consider going concern is reasonable.

Pension liabilities

19. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions. Financial Reporting Standard 17 (Retirement Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future.
20. The board's estimated pension liabilities at 31 March 2008 were £243.0 million, reducing from £289.9 million in the previous year. This largely relates to the Firefighters Pension Scheme which is unfunded and therefore the pension liability will fall to be met by serving firefighters' contributions and by taxpayers in the future. In respect of the non-uniformed and control staff budgeted contributions are to be 295% of employee contributions in 2007/08 and 2008/09, reflecting the actuarial valuation as at 31 March 2005. The next full actuarial valuation will assess the position as at 31 March 2008. Recent changes to the Local Government Pension Scheme regulations are expected to release some future financial benefits, while providing additional flexibility to future pensioners.



Legality

21. Each year we request written confirmation from the Treasurer that the board's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of the Chief Fire Officer and Senior Management Team, the financial transactions of the board were in accordance with the relevant legislation and regulations governing its activities.

22. There are no additional legality issues arising from our audit which require to be brought to members' attention.



Governance

Introduction

23. In this section we comment on key aspects of the board's governance arrangements during 2007/08.

Overview of arrangements in 2007/08

24. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. The board has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.

25. A Statement on the System of Internal Financial Control is included within the annual financial statements, and highlights the Treasurer's view that reasonable assurance can be placed upon the adequacy and effectiveness of the board's internal financial control system.

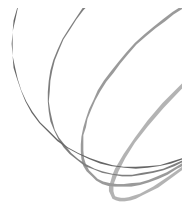
26. In accordance with good practice the statement was reviewed by the Scrutiny Committee in August 2008 and is supported by a high level review of the adequacy and effectiveness of internal financial controls undertaken by internal audit. The statement complies with accounting requirements and is not inconsistent with the findings of our audit. However, as this statement forms part of the board's financial statements it would be appropriate to review this statement and the underlying assurances prior to the submission of the financial statements for audit.

Action plan, no 1

Audit committee and internal audit

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

28. Internal audit plays a key role in the board's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. An internal audit service is provided to the board by the City of Edinburgh Council's Chief Internal Auditor. From our review of the service, we found that the work is conducted in accordance with CIPFA's Code of Practice for Internal Audit in Local Government, that the plan was sufficient and



that all work on which we planned to place reliance was completed and the relevant assurances obtained.

29. The Chief Internal Auditor reported that a follow-up review of the board's procurement arrangements had identified that some further recommendations had been made following the introduction of phase 2 of the board's Purchase Card Scheme. An action plan has been agreed by the board.

Systems of internal control

30. The board's financial transactions are processed through the City of Edinburgh Council's financial systems. It is therefore the responsibility of the council's management to maintain adequate financial systems and associated internal controls. The auditor evaluates significant financial systems and associated internal controls both for the purposes of giving an opinion on the financial statements and as part of a review of the adequacy of governance arrangements.
31. Our review of these systems was conducted as part of the audit of City of Edinburgh Council, supplemented by specific audit work on the board's financial statements. Overall there are no material issues of concern in relation to the operation of the main financial systems.
32. We noted however that no formal Service Level Agreement (SLA) exists to define the relationship between the City of Edinburgh Council and the board. Such an agreement detailing the services to be provided, the standards to be delivered, performance indicators, legal compliance and procedures for the resolution of problems and/or disputes would enhance the governance of the board by allowing members to ensure that the service provided by the City of Edinburgh Council supports continuous improvement and best value. The City of Edinburgh Council would also benefit from having a clearly documented remit.

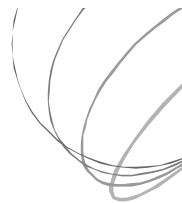
Action plan, no 2

Prevention and detection of fraud and irregularities

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

NFI in Scotland

34. In 2007/08 the board again took part in the National Fraud Initiative (NFI) in Scotland. The exercise is undertaken as part of the audits of the participating bodies. NFI brings together data from councils,



police and fire and rescue boards, health bodies and other agencies, to help identify and prevent a wide range of frauds against the public sector. These include housing benefit fraud, occupational pension fraud and payroll fraud. The NFI has generated significant savings for Scottish public bodies: (£37 million to date including £8.7 million from the 2006/07 exercise). If fraud or overpayments are not identified in a body, assurances may be taken about internal arrangements for preventing or detecting fraud.

35. The NFI 2006/07 results (data matches) were made available to the board on 29 January 2007 via a secure web based application. Participating bodies follow up the matches, as appropriate, and record the outcomes of their investigations in the application. We monitored the board's involvement in NFI 2006/07 during the course of our audit.
36. The board received information on some 63 data matches through payroll matching. All were investigated with a satisfactory outcome and no fraud was identified.

Looking ahead

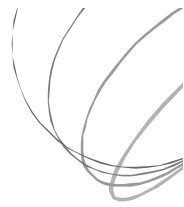
37. The concordat between the Scottish Government and COSLA sets out the terms of a new relationship between the Scottish Government and local government. This gives councils greater flexibility in how they spend money and provide services in return for clear commitments to achieve outcomes that relate to national policies. To date these new arrangements have focussed on the relationship between local authorities and the Scottish Government. At present it is unclear how the board will fit into the future development of Single Outcome Agreements as they are extended to Community Planning Partnerships in 2009. As the board covers an area which encompasses five local authorities it will face significant challenges.
38. These new arrangements may also impact on the funding streams available from constituent authorities as they re-focus towards achievement of the SOAs. In the current environment of tightening financial circumstances in the public sector and rising costs, in particular those of pensions and fuel, the board will face significant challenges to identify and realise efficiency gains.



Performance

A performance audit of the Scottish fire and rescue authorities

39. The Fire (Scotland) Act 2005 established a statutory framework to enable Scottish fire and rescue authorities to modernise their service. The Act was accompanied by a statutory Fire and Rescue Framework for Scotland.
40. In July 2008 Audit Scotland published its *Scottish fire and rescue authorities 2007/08 – progress report*, a follow-up to the March 2007 publication *A review of service reform in Scottish fire and rescue authorities*. Whilst it was recognised that there was little more than a year between the two reports it was considered important that the pace of change in reforming services and increasing efficiency be sustained. The review is intended to reinforce and support that process.
41. Overall the review found that fire and rescue authorities had made progress in a number of areas, namely:
- implementing initiatives to increase the engagement of elected members, which has resulted in greater awareness of their responsibilities around governance and scrutiny
 - taking a more strategic approach to partnership work, with more partnership registers and a more proactive role in Community Planning partnerships
 - continuing to prioritise resources into community safety and fire prevention, within the context of their Integrated Risk Management Plans.
 - developing personal appraisal systems for staff and implementing the Integrated Personal Development System for retained staff
 - taking positive steps to achieve a more diverse workforce and updating policies to reflect equalities issues.
42. The report also drew attention to areas where progress had been slower, in particular:
- evaluating the impact, outcomes and cost-effectiveness of community safety activities
 - developing comprehensive performance management arrangements and using these to drive improvement activity
 - providing robust evidence to demonstrate whether efficiency savings are being delivered
 - public reporting arrangements still have some way to go before meeting statutory Best Value guidance on public performance reporting



Performance indicators

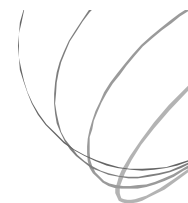
43. The service has a statutory duty to collect, record and publish specified performance indicators and so far as is practicable, ensure they are accurate and complete. The Accounts Commission issue a Direction each year detailing the indicators that require to be published and external auditors review the service's arrangements and return details of the indicators, including an opinion on their reliability to enable compilation of national reports on performance. I am pleased to report that all indicators prescribed for 2007/08 were classified as reliable.
44. The indicators published by the board show a slight increase in the number incidents resulting in casualties to 1.8 per 10,000 population (2006/07 – 1.6). This is accompanied by a small rise in the number of fatal and non-fatal casualties to 2.4 per 10,000 population (2006/07 – 2.1) and a similar small rise in the number of accidental dwelling fires to 11.9 per 10,000 population (2006/07 – 11.6). The service profile shows that the board is responding with increases in the number of home safety fire inspections and community education initiatives.
45. The performance indicators also highlight the progress the board is making in reducing the incidence of sickness absence with reductions in the percentage of rider shifts lost to sickness during the year and the percentage of time lost for other staff.



Final Remarks

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

Audit Scotland
October 2007



Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1.	26	Statement on the System of Internal Financial Control The draft SSIFC was not reviewed by the board until after the draft financial statements were submitted for audit Risk: the board members may not be able to exercise effective scrutiny over the contents of the SSIFC	The Committee Officer, in consultation with the Convenor, will give consideration to rescheduling the Scrutiny Committee meetings to include a June meeting when the members of the Scrutiny Committee can review the draft SSIFC as part of Internal Audit's annual report	Committee Officer	November 2008
2.	32	Service Level Agreement There is no formal SLA between the board and the City of Edinburgh Council, to define the relationship between the two parties. Risk: service provision may not adequately meet the needs of the board and may not support continuous improvement and best value..	To develop a Service Level Agreement with the City of Edinburgh Council	Head of Central Services	July 2009