

Orkney Islands Council

2016/17 Annual Audit Report



 AUDIT SCOTLAND

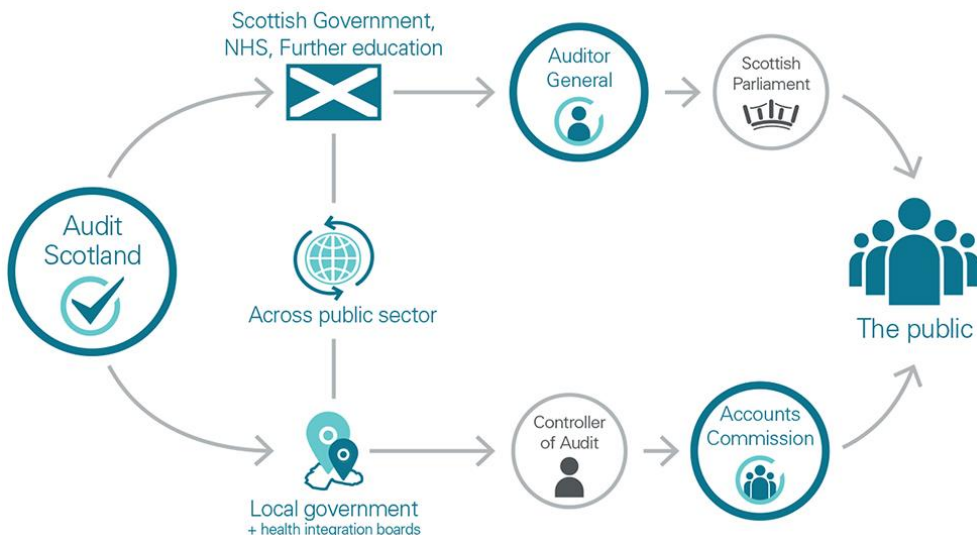
To the Members of the Orkney Islands Council and the Accounts Commission

29 September 2017

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Key messages

Audit of the 2016/17 annual accounts

- 1 Our audit opinions were all unqualified. These covered the financial statements, management commentary, remuneration report and the annual governance statement.
- 2 An unqualified opinion was issued for Orkney Islands General Charitable Trust administered by the Council.

Financial management

- 3 Financial management arrangements are broadly satisfactory. However, the Council needs to improve the financial management of its capital programme arrangements in order to improve its overall financial management.
- 4 Our testing of the design and operation of the financial controls over significant risk areas confirmed that controls relating to financial systems and procedures are designed appropriately and operating effectively.

Financial sustainability

- 5 The council continues to hold substantial levels of reserves largely due to the strength of its Strategic Reserve Fund. This provides the council with a relatively strong longer-term financial position compared with most other councils in Scotland.
- 6 The Council has financial strategies and plans over the short and medium term and these are robust with linkages to wider Council initiatives however there is no long term financial plan in place to demonstrate the feasibility of significant longer term projects.

Governance and transparency

- 7 The Council has appropriate governance arrangements in place that support the scrutiny of decisions made by the Council.
- 8 Information technology has been a long term challenge for the Council but recent changes in reporting lines and staff appointments have resulted in completion of the IT Strategy and the Digital Strategy.

Value for money

- 9 The Council has developed a change review programme intended to drive an evaluation of key business processes and review options for modernising and delivering frontline services more efficiently.
- 10 The Council has improved performance management arrangements and there is a clear performance management framework in place.

Introduction

1. This report is a summary of the findings arising from the 2016/17 audit of Orkney Islands Council.

2. The scope of the audit was set out in our Annual Audit Plan presented to the February 2017 meeting of the Monitoring and Audit Committee. This report comprises:

- an audit of the annual report and accounts
- consideration of the four dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 1](#).

Exhibit 1

Audit dimensions



Source: Code of Audit Practice 2016

3. The main elements of our audit work in 2016/17 have been:

- an interim audit of the Council's main financial systems and governance arrangements
- audit work covering the Council's arrangements for securing Best Value relating to Orkney Islands for specific areas (e.g. financial management, financial sustainability and the use of resources)
- an audit of the Council's 2016/17 annual report and accounts including the issue of an independent auditor's report setting out our opinions.

4. Orkney Islands Council is responsible for preparing the annual report and accounts that show a true and fair view in accordance with the Local Authority

Accounts (Scotland) Regulations 2014. It is also responsible for establishing effective governance arrangements and ensuring financial management is effective.

- 5.** Our responsibilities as independent auditor are established by the Local Government in Scotland Act 1973 and the Code of Audit Practice 2016 guided by the auditing profession's ethical guidance.
- 6.** As public sector auditors we provide an independent auditor's report on the annual report and accounts. We also review and report on the arrangements within Orkney Islands Council to manage its performance and use of resources such as money, staff and assets. Additionally, we report on the Council's best value arrangements. In doing this, we aim to support improvement and accountability.
- 7.** Further details of the respective responsibilities of management and the auditor can be found in the [Code of Audit Practice 2016](#).
- 8.** This report raises matters from the audit of the annual report and accounts, risks or control weaknesses. Communicating these does not absolve management from its responsibility to address the issues we raise, and to maintain adequate systems of control.
- 9.** Our annual audit report contains an action plan at [Appendix 1 \(page 30\)](#). It sets out specific recommendations, responsible officers and dates for implementation.
- 10.** As part of the requirement to provide fair and full disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2016/17 audit fee for the audit was set out in our Annual Audit Plan and as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.
- 11.** This report is addressed to both the Council and the Controller of Audit and will be published on Audit Scotland's website www.audit-scotland.gov.uk.
- 12.** We would like to thank management and staff who have been involved in our work for their co-operation and assistance during the audit.

Part 1

Audit of 2016/17 annual report and accounts



Main judgements

We provided unqualified audit opinions on the Council's annual report and accounts.

We provided an unqualified audit opinion on the Orkney Islands General Charitable Trust administered by the Council

Unqualified audit opinions

13. The annual report and accounts for the year ended 31 March 2017 were approved by the Monitoring and Audit Committee on 28 September 2017. We reported, within our independent auditor's report:

- an unqualified opinion on the financial statements
- unqualified opinions on the management commentary, remuneration report and annual governance statement.

14. Additionally, we have nothing to report in respect of those matters which we are required by the Accounts Commission to report by exception.

Audit of Orkney Islands General Charitable Trust administered by Orkney Islands Council

15. Due to the interaction of the Local Government in Scotland Act 1973 with the charities legislation, a full and separate audit and auditor's report is required for each registered charity where members of Orkney Islands Council are sole trustees, irrespective of the size of the charity.

16. Our duties as auditors of the charitable trust administered by Orkney Islands Council are to:

- express an opinion on whether the charity's financial statements properly present the charitable trusts' financial position and are properly prepared in accordance with charities legislation
- read the trustees' annual report and express an opinion as to whether it is consistent with the financial statements
- report on other matters by exception to the trustees and to the Office of the Scottish Charity Regulator.

17. We received the Charitable Trusts' accounts in line with the agreed timetable and after completing our audit we issued unqualified audit opinions in respect of the 2016/17 financial statements.

The Council's annual report and accounts are the principal means of accounting for the stewardship of its resources and its performance in the use of its resources.

Submission of the Council's annual report and accounts for audit

18. We received the unaudited annual report and accounts on 28 June 2017, in line with the audit timetable set out in our 2016/17 Annual Audit Plan. In 2016/17, for the first time, the Council's group accounts included the financial results of Orkney Integration Joint Board within its area. We worked with officers of the Integration Joint Board to obtain the correct figures and presentation of the Integration Joint Board disclosures in the Council's group accounts.

19. The working papers provided with the unaudited report and accounts were of a good standard and finance staff provided good support to the audit team during the audit. This assisted the delivery of the audit to deadline.

Risk of material misstatement

20. [Appendix 2](#) provides a description of those assessed risks of material misstatement that were identified during the planning process which had the greatest effect on the overall audit strategy, the allocation of resources to the audit and directing the efforts of the audit team. Also, included within the appendix are wider audit dimension risks, how we addressed these and conclusions.

Materiality

21. Materiality defines the maximum error that we are prepared to accept and still conclude that our audit objective has been achieved (i.e. true and fair view). The assessment of what is material is a matter of professional judgement. It involves considering both the amount and nature of the misstatement.

22. Our initial assessment of materiality for the annual report and accounts was undertaken during the planning phase of the audit and is summarised in [Exhibit 2 below](#). Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.

23. On receipt of the annual report and accounts and following completion of audit testing we reviewed our original materiality calculations and concluded that they required to be revised. The revised materiality figures are shown in brackets in exhibit 2. As the revised figures were not significantly different to those calculated at the planning stage of the audit we did not need to change our audit approach.

Exhibit 2

Materiality values

Materiality level	Amount
Overall materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It was set at 1% of gross expenditure for the year ended 31 March 2017.	£1.26 million (subsequently revised to £1.39 million)
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 50% of overall materiality.	£0.630 million (subsequently revised to £0.69 million)
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold'	£0.013 million

Materiality level	Amount
amount. This has been calculated at 1% of overall materiality.	(subsequently revised to £0.014 million)

Source: Audit Scotland Annual Audit Plan 2016/17

How we evaluate misstatements

24. There were no material adjustments to the unaudited financial statements arising from our audit which impact the council's primary financial statements. [Exhibit 3](#) highlights one significant finding of this nature arising from our audit.

25. It is our responsibility to request that all errors are corrected although the final decision on this lies with those charged with governance taking into account advice from senior officers and materiality. There were no unadjusted errors above the reporting threshold which impact the council's primary financial statements.

Significant findings

26. International Standard on Auditing 260 (UK & Ireland) requires us to communicate to you significant findings from the audit. These are summarised in [Exhibit 3](#) (where a finding has resulted in a recommendation to management, a cross reference to the Action Plan in [Appendix 1](#) has been included).

Exhibit 3

Significant findings from the audit of Orkney Islands Council

Issue	Resolution
<p>1. Non-current asset valuations</p> <p>Our audit identified a number of investment properties in the council's asset register and valuers report which were inconsistently classified.</p> <p>We also found that the valuers report included four council houses which had been sold during 2016/17.</p> <p>Further work was required to confirm the correct value of investment properties and council houses.</p>	<p>A revised valuation certificate was provided by the valuer with assets correctly classified and this was agreed to the figure in the balance sheet and note 12 to the accounts. No adjustment was required to the primary financial statements or note 12 to the accounts.</p>
<p>2. External Funding Analysis</p> <p>The External Funding Analysis provides a reconciliation of the main adjustments to the Net Expenditure to Fund Balances to arrive at the amounts in the Comprehensive Income and Expenditure Statement.</p> <p>The External Funding Analysis included in the draft accounts was not presented in accordance with Code of Practice on Local Authority Accounting in the United Kingdom 2016/17. This resulted in additional audit work to confirm the overall surplus/deficit figures.</p>	<p>The Council has agreed to leave the presentation of the External Funding Analysis for 2016/17 as the figures are correct overall.</p> <p>The Council has also agreed to revise the presentation in the 2017/18 accounts to provide clarity over adjustments to service cost figures through transfers to/from reserves.</p>

Going concern

27. The financial statements of the Council, its group and the associated charitable trusts have been appropriately prepared on the going concern basis.

Other findings

28. Our audit identified a number of presentational, consistency and disclosure issues as well as errors in a number of prior year figures. The presentational issues and errors were discussed with management and were subsequently adjusted and reflected in the audited annual report and accounts.

Governance Statement

29. Significant changes were required to the Governance Statement which was submitted for audit. We liaised with officers to ensure the revised Governance Statement complied with new guidance which was issued for 2016/17 and included appropriate disclosures and assurances.

30. The Council placed reliance on our interim audit work for the purpose of obtaining assurances for the internal systems of control. We confirmed this to be appropriate for 2016/17 however we are not required to complete full system reviews for all key financial systems each year of the audit.

Recommendation 1

The Council will need to reflect on how to obtain assurances over systems of internal control in future years when we are not required to complete full system reviews for all key financial systems.

Objections

31. The Local Authority Accounts (Scotland) Regulations 2014 require a local authority to publish a public notice on its website that includes details of the period for inspecting and objecting to the accounts. This must remain on the website throughout the inspection period. The Council complied with the regulations.

32. No objections were submitted on the 2016/17 accounts.

Part 2

Financial management



Main judgements

Financial management arrangements are broadly satisfactory. However, the Council needs to improve the financial management of its capital programme arrangements in order to improve its overall financial management.

Our testing of the design and operation of the financial controls over significant risk areas confirmed that controls relating to financial systems and procedures are designed appropriately and operating effectively. We did not identify any significant internal control weaknesses.

The Council has satisfactory arrangements in place for investigating and reporting data matches identified by the NFI, but there is some scope for improvement in their processes.

Financial performance in 2016/17

33. The net cost of General Fund services for 2016/17 amounted to £82.871 million, which was £0.061 million more than the budget. Sources of finance totalled £82.392 million including a budgeted contribution of £6.715 million from reserves. A further contribution from reserves was therefore required to achieve a break even position resulting in a reduction in general fund balance for the year of £0.479 million.

34. After taking into account other comprehensive income, overall the activities of the Council returned a surplus of £10.937 million to both useable and unusable reserves for the year.

Capital programme 2016/17

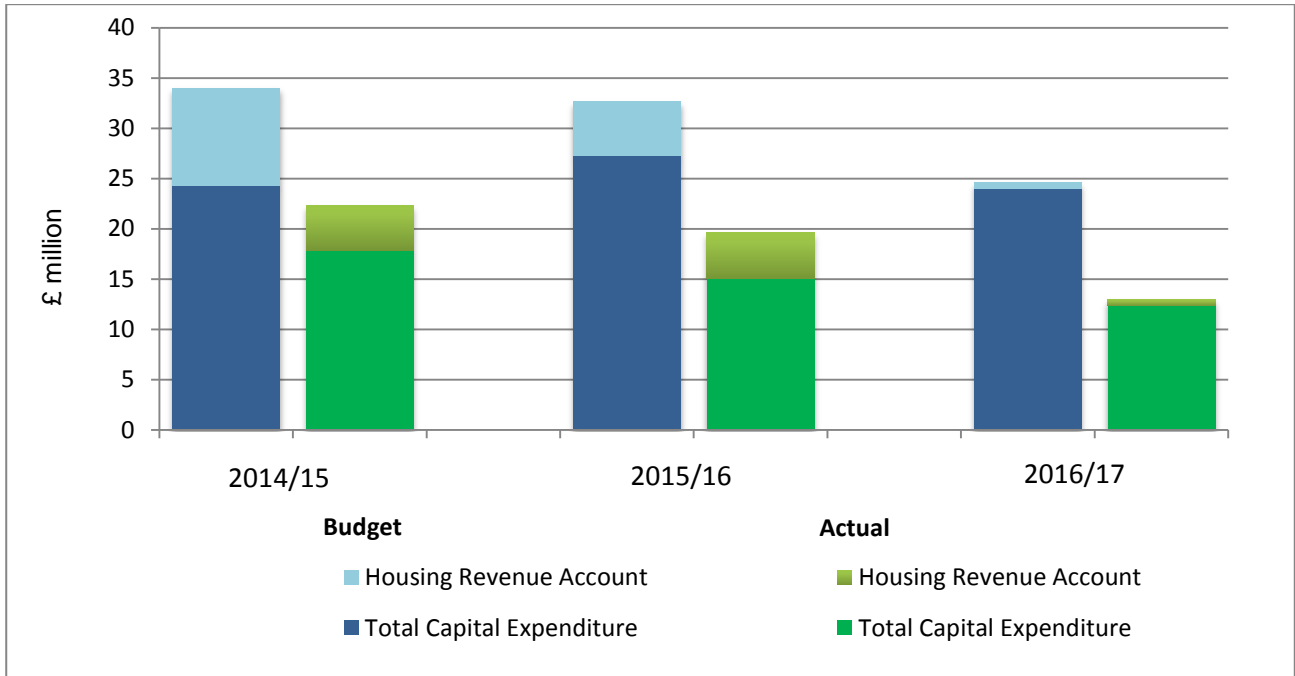
35. Total capital expenditure in 2016/17 was £12.401 million against an original planned capital investment of £24.033 million.

36. The Council has a history of slippage in its capital programme as outlined in [Exhibit 4](#).

Financial management is about financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

Exhibit 4

Capital slippage compared to budget (General Fund and HRA)



Source: Orkney Islands Council Annual report and accounts 2014/15 to 2016/17

37. Significant slippage in the capital programme in 2016/17 was identified early in the financial year and a proposal to re-profile planned capital investment was approved by Policy and Resources Committee in November 2016. Officers have prepared a re-profiled capital investment plan which will be submitted to Policy and Resources Committee in September 2017. The re-profiled capital investment plan has been prepared to reflect current timescales for completion of individual capital projects.

Recommendation 2

The Council should ensure that slippage and rescheduling of general fund capital projects does not have a significant impact on strategic priorities that are dependent on capital projects being completed on time.

Housing Revenue Account

38. The Council is required by legislation to maintain a separate Housing Revenue Account (HRA) and to ensure that rents are set to at least cover the costs of its social housing provision. Rent levels are therefore a direct consequence of the budget set for the year.

39. The HRA returned a gain on its operations of £2.133 million for 2016/17 representing an improved position from 2015/16 which returned a deficit of

£2.420million. The reason for the increase in net position is that during 2016/17 there was a revaluation carried out on council houses. The revaluation resulted in a revised increase in value of £12.773 million for housing stock and a write back of £5.738 million of depreciation.

Efficiency savings

40. With reduced funding from government and increased demand for financial services, efficiency savings are an important means of bridging the gap between funding received and spending commitments.

41. The Council is required to make an annual return to the Scottish Government in respect of recurring efficiency savings. The Policy and Resources Committee routinely receives budget monitoring reports including savings plans which have been risk assessed.

42. The 2016/17 annual return to the Scottish Government indicated that £1.1 million of savings were achieved against a target savings figure of £1.4 million. Going forward the Council recognises that achievement of further savings will prove challenging.

Borrowing in 2016/17

43. The Council's outstanding short and long term loans at 31st March 2017 totalled £35.718 million representing a decrease of £4.824 million on the previous year. New borrowing during 2016/17 amounted to £0.228 million in respect of an interest free loan to fund the street lighting project.

Budgetary monitoring and control

44. Members have a key role in agreeing the council budget each year and all Members receive training on the budget process each year to ensure they fully understand underlying assumptions and implications of the spending decisions they make.

45. Within the Council the detailed scrutiny of financial performance is delegated to the Policy and Resources Committee which receives quarterly revenue and capital monitoring reports. From our review of these reports and attendance at committee we concluded that they provided an overall picture of the budget position at service level but can be three months out of date by the time they are reviewed.

Recommendation 3

Financial monitoring reports should be prepared and reported on a timely basis so that members can make timeous informed decisions on the financial position of the Council.

46. Notwithstanding the issue regarding timing of reporting we have observed that the reports forecast out-turn position for the year and include good narrative explanations for significant variances against budget. They allow both members and officers to carry out scrutiny of the Council's finances.

47. There has been no evidence of a clear link between budgets and corporate priorities to date. To comply with good practice, the priorities of the council that are set out in the council plan should feed into the allocation of revenue and capital resources for each service. This will ensure that the council optimises the use of resources at its disposal.

Internal controls

48. As part of our audit we identify and inspect the key internal controls in those accounting systems which we regard as significant for the production of the financial statements. Our objective is to gain assurance that the Council has systems of recording and processing transactions which provide a sound basis for the preparation of the financial statements.

49. No significant control weaknesses were identified which could affect the Council's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

50. However, we performed a review of access rights to the financial management system and found there to be a significant number of users with system administration/super user rights including eleven officers within the IT service. The general ledger records the council's financial transactions and is the primary source of information for compiling the annual accounts. The integrity of the ledger is therefore crucial to ensuring the accounts are accurate.

Recommendation 4

User access to council systems should be reviewed on a regular basis to ensure that only users with a business need have access to those systems.

Prevention and detection of fraud

51. We have responsibility for reviewing the arrangements put in place by management for the prevention and detection of fraud. We reviewed the Council's arrangements including policies and codes of conduct for staff and elected members, whistleblowing, fraud prevention and fraud response plan.

52. Based on the evidence reviewed by us, we concluded that the Council has adequate arrangements in place for the prevention and detection of fraud.

National Fraud Initiative

53. The National Fraud Initiative (NFI) in Scotland is a counter-fraud exercise co-ordinated by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different financial systems, to identify 'matches' that might suggest the existence of fraud or error.

54. The latest position on NFI investigations by the Council is summarised in [Exhibit 5](#).

Exhibit 5

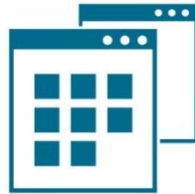
National Fraud Initiative

Total number of matches



1,361

Number recommended for investigation



315

Completed/closed investigations



467

Source: NFI website

55. Orkney Islands Council has satisfactory arrangements in place for investigating and reporting data matches identified by the NFI, but there is some scope for improvement in their processes, including:

- Internal Audit formally monitoring/addressing the NFI process
- the NFI process being included in the Council's corporate policies and strategies in relation to fraud detection and prevention
- local outcomes of the NFI process being fully reported upon for the consideration of the Monitoring & Audit Committee
- follow-up comments and checks on investigative work by the NFI Co-ordinator being clearly documented as part of the NFI exercise.

56. The 467 matches investigated by the Council did not identify any frauds or errors.

Part 3

Financial sustainability



Main judgements

The Council has a high level of reserves for a Council of its size.

The Council's Medium Term Resource Strategy predicts a likely funding gap of £12.0 million over the next 5 years. Detailed proposals on how to achieve further savings to plug the gap are being developed.

The Council should prepare longer term financial plans to ensure the sustainability, feasibility and practicalities of current spending plans.

Financial planning

57. It is important that long-term financial strategies (typically covering five to ten years) are in place which link spending to the council's strategies. Although councillors only approve the budget for a single year, this should be supported by indicative future spending plans (covering three years at least) that forecast the impact of relevant pressures on the council.

58. The Council has been slow to respond to the need to prepare medium to long term financial plans due to its strong financial position. The Strategic Reserve Fund which has a total value of £207.2 million at 31 March 2017 has enabled the Council to fully fund service costs up to now and plans are in place for this practice to continue for the foreseeable future.

59. In 2014/15 following the economic downturn the Council prepared a four year Medium Term Resource Strategy (MTRS) for the period 2015/16 to 2019/20 which was approved by the Policy and Resources Committee in February 2015. Since then the strategy has been updated annually and the current MTRS now covers a five year period for the period 2017/18 to 2021/22. The MTRS includes different scenarios and is based on reasonable assumptions.

60. The Council has commenced the preparation of savings proposals to cover the period of the Medium Term Resource Strategy but has not yet developed a longer term financial plan. The Council accepts that longer term financial plans are essential to ensure that funds are used to deliver the priorities of the Council and that the reserves continue to provide benefit for the people of Orkney in the way intended. The Council has advised that capacity issues are preventing progress with longer term financial planning.

Funding position

61. The Council approved its 2017/18 budget in February 2017. The budget was set at £82.441 million with confirmed Scottish Government revenue funding to the Council for 2017/18 of £67.144 million. This leaves a funding gap of £15.297 million. The Council has agreed to fund £7.363 million of the gap with a transfer from reserves and the remainder will be met through income fees and charges.

Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

62. Looking at the Council's budget information/financial projections for 2017/18 to 2021/22, it is forecasting a likely funding gap of £33 million over the five years. The Council plans to bridge this gap mostly through transfers from reserves from the Strategic Reserve Fund of £17.8 million and efficiency savings of £12.0 million. These savings are additional to the budget savings of £10.6 million that have been delivered by the council since 2011/12. Detailed proposals on how to achieve the further savings of £12.0 million are under development and some plans to bridge the gap have been identified including savings generated from delivery of the Council's change programme.

Recommendation 5

The council should finalise detailed savings plans for the period 2017/18 to 2021/22 which identify how the residual funding gap of £12.0 million will be addressed.

Reserves

63. One of the key measures of the financial health of a local authority is the level of reserves held. The total level of reserves held by the Council increased from £536.312 million in 2015/16 to £547.249 million for the financial year to 31 March 2017. The useable element of the reserves increased from £234.815 million in 2015/16 to £260.852 million in 2016/17 representing an increase of 11%. This very strong usable reserves position provides a good degree of reassurance to the Council's financial sustainability.

64. Ninety one percent of the value of useable reserves, (£237.375 million at 31 March 2017) are held in the Strategic Reserve Fund (SRF). The SRF is an investment fund established under the Orkney County Council Act 1974. It holds investment returns from surplus funds relating to harbour fees from the Scapa Flow Oil Port and previous marine and disturbance payments made by the terminal operators.

65. The purpose of the SRF is to provide for the benefit of Orkney and its inhabitants. The Council has an established policy on disbursements from the SRF which ensures that the value of the fund does not fall in real terms, measured against a minimum floor balance. SRF investments have performed well with an overall increasing trend in value. In recent years, the council has approved contributions from the fund to supplement its funding from the Scottish Government and local taxes raised through council tax and non-domestic rates.

66. The high level of reserves further supports the need for long term financial planning to ensure the funds will be used to achieve strategic aims and benefit the people of Orkney.

Recommendation 6 ([Appendix 1, action plan point 5](#))

The Council should prepare a longer term (five to ten year) financial plan to ensure the sustainability, feasibility and practicalities of current spending plans.

67. The general fund reserve is the Council's second largest useable reserve. This reserve has no restrictions on its use. Its main purpose is to provide a contingency fund to meet unexpected expenditure and as a working balance to help cushion the impact of uneven cash flows. The General Fund Reserve has a balance of £15.781 million at 31 March 2017.

68. [Exhibit 6](#) provides an analysis of the allocation of reserve balances over the last five years and details the value of useable reserves earmarked for specific

purposes. The table highlights that the general fund balance accounts for 6.05% of total useable reserves which is significantly less than in 2012/13 when the general fund balance accounted for 11% of useable reserves.

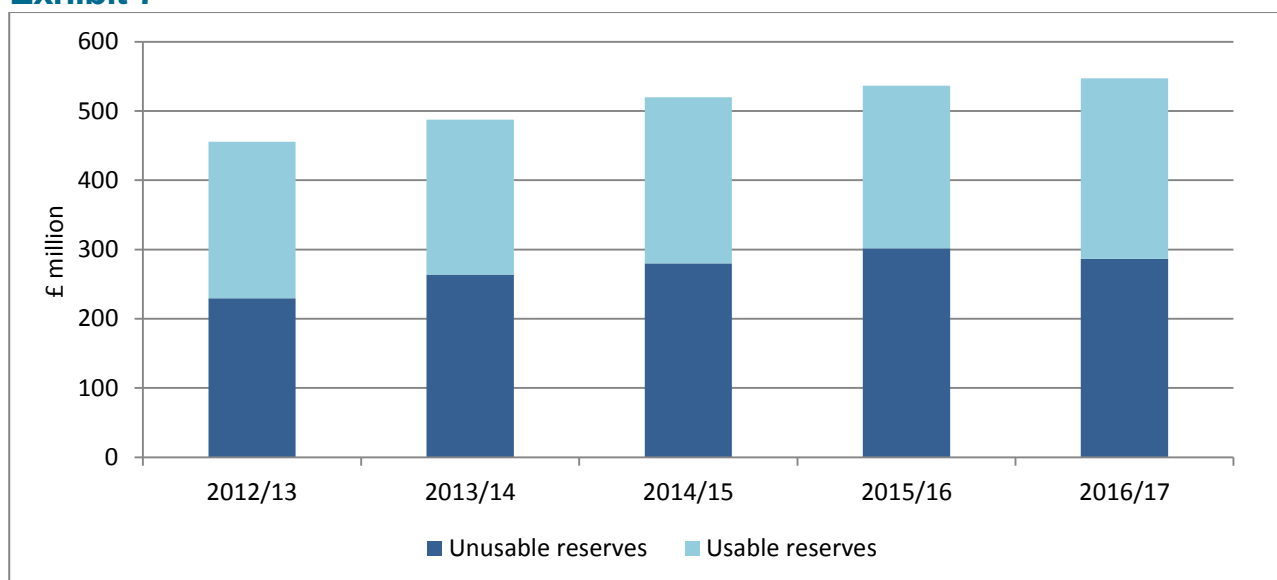
Exhibit 6

Analysis of allocation of reserve balances over the last five years

	2012/13	2013/14	2014/15	2015/16	2016/17
	£'000	£'000	£'000	£'000	£'000
General fund	24.917	23.768	18.521	21.185	15.781
Housing revenue reserve	0	0	0	0.476	0.177
Strategic reserve fund	197.546	196.784	214.255	207.841	236.459
Repair and renewal fund	2.939	2.917	3.811	4.785	7.377
Capital receipts reserve	0.077	0.020	0.020	0.020	0.530
Other statutory funds	0.508	0.508	0.508	0.508	0.528
Total usable reserves	225.987	223.997	237.115	234.815	260.852
Unusable reserves	229.506	263.566	258.913	301,497	286,397

69. Exhibit 7 provides an analysis of the total reserves held by the Council over the last five years split between usable and unusable reserves. This shows a steady increase in net worth over the five years and slight fluctuations in useable reserves over the period with an overall increase of £34.8 million since 2012/13.

Exhibit 7



Source: OIC Annual report and accounts

70. The Council has an investment strategy which is updated on an annual basis. In 2016/17, £185m of the Council's funds were managed on a discretionary basis by externally appointed fund managers who are required to comply with the Council's investment strategy. The investment management agreements between

the Council and the fund managers additionally stipulate guidelines and duration and other limits in order to contain and control risk.

71. The Council aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The performance of the managed funds for the SRF are measured on a rolling 3 year average.

Asset management

72. Orkney Islands Council is required to manage its assets in an effective way to ensure the delivery of quality public services.

73. The corporate asset management planning process is currently being developed through the Capital Planning and Asset Management Strategy Group. A management framework structure has been established to support the integration of asset management planning and investment decisions. This framework ensures that asset management planning is dealt with at a sufficiently senior level. The Senior Management Team, acting in its capacity as an Officers' Capital Working Group, is chaired by the Chief Executive. The group provides oversight of the management of corporate assets within Orkney Islands Council and a decision-making gateway to ensure that management decisions are undertaken in a corporate manner. It is supported by a Capital Planning and Asset Management Strategy Group.

74. The Council now has asset management plans for all services in place and is working to ensure a new corporate asset management plan is in place in 2018 when the current plan expires.

Part 4

Governance and transparency



Main Judgements

The Council has appropriate arrangements in place that support scrutiny of decisions made by the Council and its standing committees.

Information technology has been a long term challenge for the Council but recent changes in reporting lines and staff appointments have resulted in progress in a number of areas including monitoring and reporting on performance of the service, and completion of the IT Strategy and the Digital Strategy.

The Council is open and transparent in the way that it conducts its business, with the public able to attend meetings of the Council and its committees. Minutes of committee meetings and agenda papers are readily available on the Council's website for public inspection.

Orkney Integration Joint Board is bedding in and functioning well. Overall the process of integration has gone smoothly with no significant issues having been identified in respect of the governance of the Integration Joint Board and the associated budgeting process.

Governance arrangements

75. The council's governance arrangements provide an appropriate framework for decision making and scrutiny.

76. The council conducts its business in an open and transparent manner. Councillors have good access to officers and are of the view that conversations they have do not impact on the transparency of full discussion and challenge in public forums.

77. The Council audio casts committee meetings via its website offering a listen live and listen again service to its stakeholders, improving the transparency of decision making. Committee agendas, reports, minutes and audio files are available on the OIC website.

78. The standard of member scrutiny is generally good with some areas for improvement.

79. Following the council elections in May of this year, a comprehensive programme of member induction was provided to support new members in discharging their governance and scrutiny role.

80. The quality of reports to council/committee is in the main good with some exceptions where further information has been required. Councillors indicated they are broadly happy with the quality and range of information provided to them.

Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making and transparent reporting of financial and performance information.

Management commentary, annual governance statement and remuneration report

81. The Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 requires councils to prepare and publish, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. The management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body.

82. Based on our knowledge and work performed, we concluded that the management commentary, revised annual governance statement and remuneration report are consistent with the financial statements.

Internal audit

83. Internal audit provides senior management and elected members with independent assurance on the Council's overall risk management, internal control and corporate governance processes.

84. Internal audit is provided by the Internal Audit section of Orkney Islands Council. We carried out an overview of the adequacy of the internal audit function and concluded that it operates in accordance with the Public Sector Internal Audit Standards and has sound documentation standards and reporting procedures in place.

85. To avoid duplication of effort we place reliance on the work of internal audit wherever possible. In 2016/17 we placed formal reliance on internal audit's work in the following areas:

- housing rents
- grant claims.

86. In respect of our wider dimension audit responsibilities we also placed formal reliance on internal audit's work in the following areas:

- capital projects
- grants to funded bodies/third sector
- procurement
- statutory performance indicators
- stock checks
- corporate governance/risk management.

87. Internal audit have planned limited reviews of key financial systems during 2017/18. We will liaise with internal audit to ensure there are satisfactory arrangements in place to obtain assurances for the annual Governance statement for 2017/18 and for our audit of the financial statements.

IT

88. Information technology (IT) has been a long term challenge for the Council. Its wider digital strategy has also been slow to progress.

89. Responsibility for IT transferred in 2016 from the Chief Executive Office to the Director of Corporate Services with the aim of improving efficiencies and delivering improvements in the service provision.

90. Since 2016 there has also been improved management with IT included in the remit of the Head of IT and Facilities and the service team structure is now being reviewed to add in additional capacity. The Head of IT and Facilities is contemplating new more flexible ways of working within the Orkney context to deliver more efficient, better services.

91. The increase in management capacity has resulted in delivering positive changes including monitoring and reporting on performance of the service, and completion of the IT Strategy and the Digital Strategy. The IT strategy sets out how the Council will enable the Digital Strategy. The Digital Strategy sets out how the Council plans to modernise and change its service delivery processes to meet customer needs using technology.

92. The IT Service Manager has reviewed the infrastructure and has identified a proposed IT Capital Replacement Programme allocation for financial years 2017/18 and 2018/19 including replacement servers and networks. This work started on 1 April 2017.

Workforce planning

93. Audit Scotland's [*Local government in Scotland – performance and challenges 2017*](#) report highlighted the need to plan and manage reductions to Council workforces. Failing to do this can affect the skills mix and ability of the organisation to deliver, manage and scrutinise services effectively. This is particularly important for Orkney Islands Council with specific contextual issues to consider. These include:

- an ageing population and workforce profile
- the council's small scale (1,523 FTE staff in March 2017) which has inherent resourcing challenges. Losses of a few staff can have an amplified effect on the capacity of a team and the skills range.
- geography and islands economy: job losses will have a significant effect on the local economy and individuals may have to leave the islands.

94. The report advises councils to have effective systems in place for managing their workforce and monitoring staffing levels, and that information should be aligned to other long-term plans such as financial plans.

95. Councillors and officers recognise the importance and risks associated with workforce planning and that it is a corporate priority. In June 2016, the Policy and Resources Committee noted that the need to reduce workforce costs was critical to making anticipated budget reductions. In the autumn/winter of 2016/17, service level workforce plans and an organisation wide plan were produced and agreed by the relevant committees. These recent workforce plans are basic but provide a good base for the council to now build its arrangements to support effective workforce planning, succession planning and long-term forecasting as it progresses its change programme.

Transparency

96. Transparency means that the public, in particular local residents, have access to understandable, relevant and timely information about how the Council is taking decisions and how it is using resources such as money, people and assets.

97. There is evidence from a number of sources which demonstrate the Council's commitment to transparency. Members of the public can attend meetings of the full

Council, executive and other committees. Minutes of these committee meetings and supporting papers are readily available on the Council's website.

98. The Council's website allows the public to access a wide range of information including the register of members' interests, current consultations and surveys and how to make a complaint.

99. The Council makes its annual accounts available on its website. These include a management commentary which provides details of performance against budget, information on the use of reserves and risks and uncertainties facing the Council.

100. Overall, we concluded that the Council conducts its business in an open and transparent manner.

Integration of health and social care

101. Legislation to implement health and social care integration, passed by the Scottish Parliament in February 2014, came into force on April 1, 2016. This brings together NHS and local council care services under one partnership arrangement for each area.

102. The Scottish Government's 2020 vision places greater emphasis on enabling people to stay in their homes, or another homely setting, where possible, sharing their lives with their family and friends and doing the things that give life meaning and value. The integration of health and social care is seen as a means of achieving this.

103. There is a single Integration Joint Board (IJB) within Orkney whose responsibility includes planning, commissioning and overseeing service delivery performance for those functions delegated. The IJB became fully operational on 1 April 2016. However working in a co-operative fashion between Orkney Islands Council and the health board has been in place since 2011 through Orkney Health and Care Partnership. This meant that the IJB had a solid base from which to develop with well embedded arrangements in place prior to the requirements of IJBs.

104. Nevertheless, changing the governance arrangements took a significant amount of time and resources to address and put in place but it is clear that the IJB is now bedding in and functioning well.

105. Regular discussion forums are held between the Chair and Vice Chair of the IJB, the Leader of Orkney Island Council, the Chair of NHS Orkney, the two Chief Executives and senior officials, including the Chief Officer of the IJB.

106. Overall the process of integration has gone smoothly with no significant issues having been identified in respect of the governance of the IJB and the budgeting process.

107. This is the first full year of the IJB and it is therefore still early days for commissioning changes to lead to service change but the IJB has a wider integrated scheme than required by the legislation. Audit Scotland, as part of a series of reports, will be reporting on integration authorities' progress after the first year of IJBs being established. This will be available in spring 2018 and as such, we will be in a better position to assess IJB progress in Orkney once the work on this national report has been completed.

Local scrutiny plan

108. The 2017/18 Local Scrutiny Plan (LSP) prepared by the Local Area Network (LAN) of scrutiny partners for the Council was presented to the Monitoring and Audit Committee on 8 June 2017. The LAN did not identify any new scrutiny risks

in the year which would require specific scrutiny work during 2017/18. The Council will be subject to a range of nationally driven scrutiny activity as set out in the LSP.

Equalities

109. The Equality Act 2010 introduced a public sector general duty that encourages public bodies to mainstream equality, that is, ensure it is part of their core work. The Act requires that by no later than 30 April 2015 and every two years thereafter, public bodies must publish a report on the progress made to achieve the quality of outcomes it has set.

110. We reviewed the current 2017 equalities report and concluded the Council has met its statutory duty to:

- publish information on progress made in mainstreaming equality within the Council
- report on progress made towards achieving equality outcomes published in 2013
- publish annual employee information and details of the progress made in gathering and using information to better meet the duty
- publish updated gender pay gap information.

111. We concluded, on the basis of evidence reviewed, that the Council is proactive in ensuring that equality is mainstreamed.

Equal pay

112. In September 2017, the Accounts Commission published its findings from an audit of equal pay across local government. The audit found that councils underestimated the challenges involved in implementing the Single Status Agreement (SSA) and some of the approaches taken by councils did not always prioritise pay equality and were later found to be discriminatory. Orkney Islands Council implemented single status in 2008 and reports that between 2004/05 and 2015/16 it has spent £1.8m compensating workers who had been unfairly paid and settling equal pay claims.

113. Almost 27,000 equal pay claims across Scotland remain live. Orkney Islands council has no live claims. However, workers could potentially still make new claims against councils. This means that councils need to be confident that they have fair and transparent pay arrangements and take necessary action, such as regular equal pay audits, to deliver pay equality in line with their public sector equality duty.

Part 5

Value for money



Main judgements

The Best Value audit found the Council has a number of improvement activities planned as part of the Change programme but it is too early to assess the effectiveness or potential impact of the developing plans.

The Council has improved arrangements for ensuring compliance with the Code of Guidance on funding external bodies and following the public pound for the three arm's length organisations.

Councillors have ownership of the council plan and monitor progress against the actions to support the priorities every six months but the outcomes for the community are difficult to evidence.

Best Value

114. The Accounts Commission agreed the overall framework for a new approach to auditing Best Value in June 2016. Best Value will be assessed over the five year audit appointment, as part of the annual audit work. In addition a Best Value Assurance Report (BVAR) for each council will be considered by the Accounts Commission at least once in this five year period. A Best Value audit has been undertaken of Orkney Islands Council in 2017 and the report will be discussed by the Accounts Commission on 7 December 2017. The findings in the report and the Council's response will be followed up and reported on as part of next year's audit.

Value for money is concerned with using resources effectively and continually improving services.

Business transformation

115. Audit Scotland's *An overview of local government in Scotland 2016* (March 2016) highlighted that local authorities have not made enough progress in developing alternative forms of service delivery to meet the challenges of tightened budgets and to transform public services in Scotland.

116. With its high level of reserves there has been less need for the Council to respond to change in how it delivers services. However since 2014 there has been a change review team in place which has resulted in completion of the MTRS and a change review programme. The change review programme is intended to drive an evaluation of key business processes and review options for modernising and delivering frontline services more efficiently. The change programme has become the focus of improvement review activity and six projects are currently in progress in relation to:

- property asset management
- procurement
- staff and workforce planning

- fees and charges
- outsourcing and partnerships
- modernising IT.

117. It is too early to assess the effectiveness or potential impact of the developing plans but we will monitor and report on progress throughout the period of our audit appointment.

Shared services

118. The Accounts Commission and Auditor General have highlighted the benefits to the people who use council services, communities and public sector organisations of working well together. Our recent report, Local government in Scotland: Performances and Challenges 2017, however, identified limited evidence of councils collaborating or sharing services.

119. The Council works well with other Island Councils learning and sharing intelligence and ideas but there are no specific examples of shared services. This is an area the Council is currently exploring and we will monitor progress against this agenda over the course of our audit appointment.

Following the public pound

120. Local authorities have a statutory responsibility to comply with the Accounts Commission / COSLA Code of Guidance on funding external bodies and following the public pound (FPP).

121. The Council's financial regulations contain a specific section on following the public pound. These emphasise that services must adhere to the Council's guidance for allocating funds to external organisations. The guidance applies where funding is provided, or transferred, to arm's-length bodies such as companies, trusts and voluntary organisations.

122. The following companies are regarded as arm's length organisations through their association with the Council:

- The Council holds 100% of the shares in 2 Companies: Orkney Towage Company Limited and Orkney Ferries Limited which are managed by the Executive Director Development & Infrastructure.
- The Pickaquoy Centre Trust is a charitable trust formed in 1999 and is registered in Scotland. The Trust provides leisure facilities within Orkney Islands Council's area to the general public. Internal Audit carried out a review of the Pickaquoy Centre Trust in relation to the FPP code and noted within their annual report that generally the principles of the Code of Practice of Following the Public Pound were being followed to varying extents within the Service Agreement and that areas of good practice were evident. Areas where improvements could be made were also identified, both with regard to the content of the Service Agreement and the actual operating arrangements between the Council and the Trust.
- Orkney Islands Council provides further and higher education provision through Orkney College using a devolved Board of Management arrangement. Orkney College is funded by direct grant from the Scottish Funding Council (SFC). The trading position from these activities is reflected within the council's comprehensive income and expenditure statement as part of financing and investment expenditure. In 2016/17 the net effect of Orkney College activities resulted in an increase on reserves of £0.067M from a nil opening reserve balance. This is an improved position from

previous years in which the Council has provided funds to enable the College to break-even.

Performance management

123. There is a clear corporate planning framework. The council plan sets out the corporate priorities and these are disseminated through reports to council committees and through service level plans. Councillors have ownership of the council plan and monitor progress against actions to support the priorities every six months.

124. Services also report performance to their respective management teams and service committees on a six-monthly basis. Performance reports are sufficiently detailed to support scrutiny.

125. While improved performance management arrangements are in place they do not systematically include monitoring the impact of the council's policies and actions. The priorities reflect the issues for the communities and the plans clearly support the priorities, but they do not set out how the processes and actions will contribute to improved outcomes for its communities.

126. The council publishes an annual performance report (APR), which is available on its website. The APR shows the council's performance towards meeting the targets set out in its council plan. It also outlines how well the council performed against the national Local Government Benchmarking Framework indicators.

Statutory performance indicators (SPIs)

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

128. For 2016/17 three (SPIs) were prescribed:

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

129. Overall we placed reliance on the work of Internal Audit and concluded that the Council's arrangements for publication are satisfactory.

National performance audit reports

130. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2016/17, a number of reports were issued which are of direct interest to the Council. These are outlined in Appendix 4.

131. The council has processes in place to ensure that all national reports and their impact on the council are considered by Members.

Appendix 1

Action plan 2016/17

2016/17 recommendations for improvement

Page no.	Issue/risk	Recommendation	Agreed management action/timing
10	<p>1. Governance Statement assurances</p> <p>The Council placed reliance on our interim audit work for the purpose of obtaining assurances on systems of control. We confirmed this to be appropriate for 2016/17.</p> <p>However the Council will need to reflect on how to obtain assurances in future years when we are not required to complete full system reviews for all key financial systems.</p>	<p>The Council should ensure appropriate procedures and processes are in place to obtain assurances for the annual Governance Statement in 2017/18.</p>	<p>The Council's Internal Audit Section will be requested to perform a financial systems health check to provide assurance for the 2017/18 annual governance statement.</p> <p>The Council's Internal Audit Service has a rolling five year programme that covers all key financial systems. In 2017/18 the systems that will be audited are Nominal Ledger, Housing Rents and Pensions Administration.</p> <p>Responsible Officer Head of Internal Audit</p> <p>Target date: June 2018</p>
12	<p>2. Capital slippage</p> <p>The Council has a history of slippage in its capital programme and in 2016/17 total capital expenditure was £12.401 million against an original planned capital investment of £24.033M. Officers have prepared a re-profiled capital investment plan to reflect current timescales for completion of individual capital projects. The re-profiled capital investment plan will be submitted to the Policy and Resources Committee in September 2017.</p>	<p>The Council should ensure that slippage and rescheduling of general fund capital projects does not have a significant impact on strategic priorities that are dependent on capital projects being completed on time.</p>	<p>The Council has had a very ambitious capital programme over recent years with capital expenditure in excess of £77 million over the last four years. There has consequently been some delay on projects due to capacity of the project teams being stretched, but improved monitoring of progress has been implemented and a capital projects team has been established to manage the capital programme. Several of the projects that have slipped are now making good progress. The flood wall in Kirkwall is well underway, whilst pier works in Westray</p>

have recently commenced and the contract award for a replacement care home in Stromness has just been issued.

Going forward the scale of the programme is expected to be smaller and therefore more manageable.

Responsible officer: Head of Finance

Agreed date: Ongoing

13	<p>3. Financial monitoring reports</p> <p>Within the Council the detailed scrutiny of financial performance is delegated to the Policy and Resources Committee which receives quarterly revenue and capital monitoring reports. From our review of these reports and attendance at committee we concluded that they provided an overall picture of the budget position at service level but can be three months out of date by the time they are reviewed.</p>	<p>Financial monitoring reports should be prepared and reported on a timely basis so that members can make informed decisions on the financial position of the Council.</p>	<p>It is acknowledged that the Financial Monitoring reports that are presented to Committee can be somewhat out of date at the time of presentation. The extent to which the reported monitoring lags behind varies depending on the when the Committee cycles fall.</p> <p>The Committee reports are however supplemented with monthly budget monitoring statements which are more current and distributed to members in briefing note format by email to provide more timely financial performance information.</p> <p>Budget holders also receive budget monitoring statements on a monthly basis.</p>
14	<p>4. Financial ledger user access</p> <p>The general ledger records the council's financial transactions and is the primary source of information for compiling the annual accounts. The integrity of the ledger is therefore crucial to ensuring the accounts are accurate.</p> <p>We performed a review of access rights to the financial management system and found there to be a significant number of users with system administration/super user rights including eleven officers within the IT service.</p>	<p>User access to council systems should be reviewed on a regular basis to ensure that only users with a business need have access to those systems.</p>	<p>The Council's Internal Audit Section has been alerted by the Head of Finance to a fraud that occurred in another local authority and has been asked to carry out a check of the payment processes operated in Orkney to try and ascertain if there are any access control improvements required.</p> <p>The Internal Audit Plan for 2017/18 also includes a review of the Nominal Ledger.</p> <p>User access controls will also be checked to ensure that only users who have a business need continue to have system access.</p>

There is a risk that erroneous or fraudulent transactions are made as inappropriate or unauthorised access to the computer systems is not prevented.

Responsible officer: Head of Finance and Head of Internal Audit

Agreed date: June 2018

17	5. Funding Position	<p>The council should finalise detailed savings plans for the period 2017/18 to 2021/22 which identify how the residual funding gap of £12.0 million will be addressed.</p>	<p>The Council is very aware of the financial pressures that it will face in the coming years and the Senior Management Team has prepared a range of savings options for Members' consideration.</p> <p>Presentation of the savings options to Members has commenced as an early step in the process of setting a budget for the period 2018/19 to 2021/22.</p> <p>Approved savings targets totalling £3.9 million emanating from the change review projects have been integrated within these savings options.</p> <p>Baseline savings of £0.864 million have already been approved over the 3-year period 2015/16 to 2017/18 from a range of Programme ideas, projects and other initiatives.</p>
17.	<p>6. Long Term Financial Planning</p> <p>The Council's very strong usable reserves position provides a good degree of reassurance to the Council's financial sustainability.</p> <p>Ninety one percent of the value of useable reserves, (£237.375 million at 31 March 2017) are held in the Strategic Reserve Fund (SRF) and 11% of the value of reserves £15.781 million at 31 March 2017) are held in the General Fund.</p> <p>There is a risk that suitable spending plans are not in place to support delivery of the council's strategic aims.</p>	<p>The Council should prepare a longer term (five to ten year) financial plan to ensure the sustainability, feasibility and practicalities of current spending and investment plans.</p>	<p>A longer term financial plan will be developed to supplement the Medium Term resource Strategy.</p> <p>Responsible officer Head of Finance</p> <p>Agreed date June 2018</p>

Appendix 2

Significant audit risks identified during planning

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

Audit risk	Assurance procedure	Results and conclusions
Risks of material misstatement in the financial statements		
<p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p>	<ul style="list-style-type: none"> Detailed testing of journal entries. Review of accounting estimates. Focused testing of accruals and prepayments. Evaluation of significant transactions that are outside the normal course of business. 	<ul style="list-style-type: none"> Journals - a sample of journal entries was tested. We found no evidence to suggest that management were overriding controls. Estimates - based on testing of debtors, creditors and provisions/contingencies, we found no evidence of bias in accounting estimates. Significant transactions - based on our work on the annual accounts, we did not find any evidence of transactions outwith the scope of the council. <p>No fraud concerns identified in respect of management override of controls.</p>
<p>2 Risk of fraud over income</p> <p>Orkney Islands Council receives a significant amount of income in addition to Scottish Government funding. The extent and complexity of income means that, in accordance with ISA240, there is an inherent risk of fraud.</p>	<ul style="list-style-type: none"> Analytical procedures on income streams. Detailed testing of revenue transactions focusing on the areas of greatest risk. 	<ul style="list-style-type: none"> Analytical procedures – no fraud concerns identified Revenue transactions - based on our work on the annual accounts we did not identify any risk of fraud. <p>Our conclusion is that the council has arrangements in place to minimise the risk of fraud over income.</p>
<p>3 Risk of fraud over expenditure</p> <p>Practice Note 10: Audit of financial statements of public sector bodies in the United Kingdom and the Code of Audit Practice requires consideration of risk of fraud</p>	<ul style="list-style-type: none"> Audit work on the National Fraud Initiative matches. Specific audit work on benefits and grants. Evaluation of the effectiveness of internal controls for expenditure 	<ul style="list-style-type: none"> Sample testing of expenditure transactions confirmed that these were in the normal course of business. We obtained satisfactory explanations for any significant increases or decreases in expenditure.

Audit risk	Assurance procedure	Results and conclusions
<p>over expenditure (excluding payroll costs which are already a core part of all annual audits). The council incurs significant expenditure on benefits and grants which require audit coverage.</p>	<p>recognition and recording.</p>	<ul style="list-style-type: none"> • Our sample cut off testing confirmed that transactions are processed in the correct accounting year. • NFI work is on-going; so far no frauds have been identified. • The council has adequate counter fraud arrangements. <p>Our conclusion is that the council has arrangements in place to minimise the risk of fraud over expenditure.</p>
<p>4 Estimation and judgements</p> <p>There is a significant degree of subjectivity in the measurement and valuation of the material account areas of non current assets and provisions. This subjectivity represents an increased risk of misstatement in the financial statements.</p>	<ul style="list-style-type: none"> • Completion of 'review of the work of an expert' for the professional valuer. • Focused substantive testing of key areas 	<ul style="list-style-type: none"> • A number of estimations and judgements in the accounts were based on the opinion of experts. We assessed the reliability of these experts and reviewed their work. • We tested samples of accruals and provisions and confirmed them to appropriate back up evidence. • The council's accounting policies are appropriate. <p>We concluded that estimations and judgements included in the accounts are supported by appropriate audit evidence.</p>
<p>5 Orkney College</p> <p>The college is responsible for managing its own finances and aims to achieve a surplus each financial year. For a number of years now, the college has not achieved this and relies on financial support from the council's reserves. In 2015/16, support from the council amounted to £0.110 million. The council has no obligation to fund the college and although the college assumed a balanced budget for 2016/17, their recent history of poor financial results suggests the council may be expected to provide further financial support.</p> <p>There is a risk that the council may be expected to provide further financial support which</p>	<ul style="list-style-type: none"> • We will monitor progress in establishing a clear framework for how the council may provide future financial support to the college. • Include comment in our annual audit report 2016/17. 	<p>Refer to paragraph 122.</p>

Audit risk	Assurance procedure	Results and conclusions
could be significant.		
<p>6 Strynd Houses and Common Room</p> <p>In reviewing a sample of title deeds for property assets in 2016, we found that the council does not hold the title for seven properties, commonly referred to as the Strynd Houses and Common Room. These properties were obtained by Orkney Heritage Property Trust, a subsidiary of Orkney Heritage Society in the 1960s and 1970s. After refurbishment, the properties were transferred to the management of the council for housing purposes. There is no legal agreement in place that settles a lease or other type of arrangement for the properties.</p> <p>Without a legal agreement in place there is a risk that ownership of the properties may be subject to dispute</p>	<ul style="list-style-type: none"> • We will monitor progress in establishing a lease with Orkney Heritage Property Trust • Consideration and evaluation systems of internal control to ensure completeness of income. • Include comment in our annual audit report 2016/17. 	<ul style="list-style-type: none"> • A lease agreement has been in place since 17 February 2017. • Evaluation and testing of controls over income did not identify any weaknesses.
<p>7 Integration Joint Board</p> <p>The IJB transactions will be consolidated into the accounts of the council for the first time in 2016/17.</p> <p>The council needs to agree a timetable and approach to obtaining the IJB figures for consolidation, and assurances required for the group governance disclosures.</p> <p>As this is the first year, there is a risk that the timetable may not be achieved. There is also an increased risk of errors in accuracy and disclosure.</p>	<ul style="list-style-type: none"> • We will consider the timetable and process for consolidation of the group accounts. • We will consider the assurances obtained by the council's S95 officer for the group governance disclosures. • We will confirm that the consolidation adjustment is accurate and correctly disclosed. • We will confirm that any balances relating to IJBs have been agreed by the partner bodies. 	<ul style="list-style-type: none"> • IJB figures were accurately incorporated into the consolidated accounts. • Satisfactory assurances were received for the group. • Sample testing of income and expenditure transactions confirmed they were accurately recorded as IJB or non-IJB. • IJB position against budget was monitored throughout the audit and the treatment for year end results considered in line with accounting guidelines. • Confirmation of year end balances was received from each party of the IJB. • The council's share of the results of the IJB has been appropriately consolidated into the group accounts. <p>Our conclusion is that transactions and balances of the IJB were correctly classified within the council's ledger.</p>

Audit risk	Assurance procedure	Results and conclusions
Balances between the council and its partners were agreed, and full financial details were provided to audit within the required timescales.		
Risks identified from the auditor's wider responsibility under the Code of Audit Practice		
Financial Sustainability		
<p>8 Financial planning</p> <p>The 2016/17 Scottish Budget outlined significant reductions for councils' revenue grants. The financial settlement for Orkney Islands Council was a reduction of 3.9 per cent, significantly greater than the 'worst' case scenario of a 2.5 per cent reduction outlined in the medium term financial strategy. The strategy has not been updated in light of these reductions.</p> <p>There is a risk that the council may take future spending decisions based on incomplete information.</p>	<ul style="list-style-type: none"> We will monitor the council's financial position via revenue budget reports presented to full Council and meetings with officers. <p>We will perform a review of the council's revised Medium Term Resource Strategy</p>	Refer to paragraphs 61-62.
<p>9 Change programme and financial planning</p> <p>The council's Change Programme aims to deliver significant savings towards the identified funding gap of £12 million between 2017/18 and 2021/22. To date the wider service reduction options necessary to meet the remainder of the funding gap have not been consolidated.</p> <p>Risk: There is a risk that the planned budget savings will not be achieved by 2021/22.</p>	<ul style="list-style-type: none"> We will review and assess the savings programmes in place. <p>Include comment in our annual audit report 2016/17.</p>	Refer to paragraph 116.
Financial management		
<p>10 The council has a number of significant capital projects underway including the development of new social housing, new schools and its harbour infrastructure. Undertaking multiple capital projects of different types and sizes requires careful</p>	We will monitor the council's capital position and comment in our annual audit report 2016/17.	Refer to paragraphs 35-37.

Audit risk	Assurance procedure	Results and conclusions
<p>oversight. Unrealistic timescales and budgets are likely to result in slippage in completion dates or overspends and therefore delaying or reducing the benefits expected from investment. In addition the council does not have a long-term capital investment strategy that identifies the needs and constraints for local capital investment.</p> <p>There is a risk that ineffective direction and control of the capital investment programme may lead to further slippage in completion dates, overspends on projects or a reduction in the expected benefits from investment.</p>		
Governance and transparency		
<p>11 Members</p> <p>Council elections are to be held in May 2017 and there are indications that a number of elected members are or may be standing down. This will represent a loss of skills and experience amongst members. To ensure members fully understand their roles and have the necessary skills to make informed decisions and provide effective scrutiny, appropriate development and training will be required.</p>	<p>We will monitor the council's arrangements for developing members and preparations for inducting newly elected members.</p>	<p>A comprehensive induction training package was delivered to all members following the council elections and members should be well equipped to begin their roles effectively with necessary skills.</p>
<p>12 Asset management plans</p> <p>The council's Corporate Asset Management Plan (2013-18) highlighted plans to develop detailed asset management plans across six main asset types. At the time of planning our audit, only three were complete.</p> <p>There is a significant risk that the council is unable to gain a comprehensive understanding of the condition and maintenance requirements of its estate. The council may also be unable to meet the objectives of their Corporate</p>	<p>We will review and assess progress in developing the remaining asset management plans in relation to:</p> <ul style="list-style-type: none"> • ICT • Open spaces and heritage • Roads and Infrastructure. <p>Include comment in our annual audit report 2016/17.</p>	<p>Asset management plans have now been completed for all services.</p>

Audit risk	Assurance procedure	Results and conclusions
<p>Asset Management Plan without detailed plans in place.</p>		
<p>13 ICT strategy</p> <p>The council's current ICT strategy covers the period to the end of March 2017. Work has started on the revised strategy but it is uncertain if it will be completed and approved by April 2017.</p> <p>There is a risk that this affects the delivery of council services for the people of Orkney and the council change programme designed to improve performance and secure budget savings.</p>	<ul style="list-style-type: none"> We will discuss progress in preparing a new ICT strategy with officers. <p>We will review the new strategy when available.</p>	<p>Refer to paragraph 91.</p>
<p>14 Workforce planning</p> <p>It was reported to the Monitoring and Audit Committee in June 2016, that the council did not have an organisation-wide workforce plan in place, but work on developing service workforce plans was underway. The council's HR strategy 2014/18 outlines the priorities for workforce planning but does not consider workforce needs reflecting financial constraints and skills.</p> <p>Lack of workforce planning means that the council will find it difficult to identify and address its future staffing and skills needs as well as deliver planned workforce savings.</p>	<ul style="list-style-type: none"> We will review and assess progress in developing workforce plans. <p>Include comment in our annual audit report 2016/17.</p>	<p>Refer to paragraphs 93-95.</p>
<p>15 Pickaquoy Centre Trust</p> <p>The Service Agreement for the Trust covered the period 1 April 2012 to 31 March 2015. A review of the agreement by the council has not yet taken place.</p> <p>There is a risk that the existing, expired agreement no longer meets the requirements of the council.</p>	<p>We will monitor progress in reviewing the service agreement between the council and the Trust providing comment in our annual audit report 2016/17.</p>	<p>Refer to paragraph 122.</p>

Orkney Islands Council

2016/17 Annual Audit Report

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