

# Dundee City Council

## Report to Members on the 2005/06 Audit



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# Key Messages

## Introduction

In 2005/06 we looked at the key strategic and financial risks being faced by the Council. We audited the financial statements and we looked at aspects of performance management and governance. This report sets out our main findings, summarising key outcomes in 2005/06 and the outlook for the period ahead.

## Key outcomes from 2005/06 audit

We have given an **unqualified** opinion on the financial statements of Dundee City Council for 2005/06.

The Council had corporate governance systems in place during 2005/06 that operated well within a sound control environment. Risk management arrangements, however, require to be improved and embedded throughout the organisation.

The 2005 best value audit recommended that scrutiny arrangements within the Council should be strengthened and, as a result, the remit of the Best Value Sub Committee has been expanded to give members better opportunities to exercise scrutiny and greater public accountability. Given that these changes are recent, we have not yet had the opportunity to assess how effective they are in practice.

Overall the Council has made some progress against most of the improvement actions agreed as a result of the 2005 best value audit. There has been a degree of slippage, with action dates being revised in some cases. For example, actions relating to service planning, including the use of benchmarking and option appraisals, which were initially planned for June 2006 are now expected by the end of October.

Consideration has also still to be given to the development of wider public consultation and communication strategies to ensure that services can demonstrate they respond to customer views. The Council requires to maintain the pace of change and should take account of issues raised in other councils' best value reports to ensure they are well-placed to demonstrate continuous improvement.

The functions of the Council Management Team have been reviewed and specific meetings dealing with performance monitoring and strategic issues have been held since October 2005. The Council has made good progress against the actions outlined in the Council Plan, with only 9% behind target. Performance as measured by statutory performance indicators (SPIs) also showed an upward trend, with 20 indicators improving since last year and performance declining in 10 areas. Arrangements to ensure the accuracy of SPIs were much improved this year.

The Council has demonstrated a clear commitment to the efficient government agenda but, in common with other councils, is not yet in a position to fully demonstrate that its efficiency savings have not impaired service outcomes or quality.



Development of the second Community Plan covering the period up to 2010 drew more heavily on the views of citizens and community groups than the first plan, and provides a good illustration of the Council's commitment to community engagement.

At the end of the year the Council had a favourable variance against its 2005/06 budget, largely as a result of underspends within a number of departmental budgets and receipt of additional government grants. Significant effort was required during the year to meet the costs of equal pay compensation payments within the overall budget. The Council has concerns about its funding position moving forward, with the absence of a comprehensive policy-led approach to budgeting presenting further risks to the Council's ability to resource sustainable service improvements and accommodate new demands for services. There has been progress in this area over the past year, with a working group established to look at measures to integrate service planning and budgeting. A 20 year revenue budget model is also being tested.

## Outlook for future audits

In common with many other Scottish councils, Dundee has sought to limit its exposure to the financial risk associated with equal pay claims by agreeing to offer payments to specific groups of employees as part of a compensation package. Costs of £3.5 million have been recognised in the 2005/06 financial statements for the estimated one-off cost of these payments. While moves to agree compensation payments will help to reduce financial risk in this area to some extent, there remain risks while existing pay and reward structures remain in place. The future implementation of the single status agreement provides an opportunity to address any underlying inequalities in pay and other conditions of service.

The planned implementation of the single status agreement in the Council has been delayed until 2007. Until a local agreement is concluded the initial and continuing costs of single status cannot be reliably estimated. This represents a financial risk to the Council. The amount currently budgeted by the Council in 2006/07 represents around 0.9% of pay costs (excluding teachers). In securing a local agreement the Council needs to ensure it maximises the opportunity for service and job redesign to ensure it achieves value for money from its investment in staff.

The Council aims to deliver the indicative three year efficiency gain targets set by the Scottish Executive for 2005 – 2008, but has some work to do to identify additional savings required in year three. It will be challenging for the Council to deliver on its programme of savings while managing the impact on services, service users and the Council's overall objectives.



A need for significant investment in the future has been identified in a wide range of areas including school buildings, housing, transport, waste management, care homes and information systems. The Council estimates that an investment of £140.8 million is required in council housing core stock over the next ten years, with an additional £45 million to be spent on maintenance over the same period. Funding an investment of this scale will be a significant challenge, however, the Council has a robust plan to address this which has been approved by Communities Scotland. The Council also needs to further develop its asset management planning process to ensure that all assets are used effectively and efficiently to deliver services in line with the Council's priorities.

The forthcoming local government elections in May 2007, bringing the introduction of proportional representation and multi-member wards, have potential implications for the political make-up and governance of the Council. The Scottish Executive's intention is also to remove barriers to encourage the widest possible range of people to serve as councillors. These reforms will require significant input from the Council to ensure its governance arrangements are fit for purpose, including committee structures, role/remits of members and arrangements for training new members.

Changes to accounting rules will have an impact on the presentation of the 2006/07 annual financial statements. The Council should take this opportunity to review the presentation of its budget and summary financial results to members and the wider public to ensure transparency.

This is the final year of our current appointment to the audit of the Council. From 2006/07 Audit Scotland will remain as the Council's appointed auditor and the new engagement lead will be Mark Taylor.

**Audit Scotland  
October 2006**



# Introduction

1. This report summarises the findings from our 2005/06 audit of Dundee City Council. The scope of the audit was set out in our Audit Risk Analysis and Plan, which was issued on 28 April 2006. This plan set out our views on the key business risks facing the Council and described the work we planned to carry out on financial statements, performance and governance.
2. We have issued a range of reports this year, and this final report briefly touches on some of the issues. Each report set out our findings and the Council's risk exposure along with agreed responses. Appendix A of this report sets out the key risks highlighted in this report and the action planned by management to address them.



# Performance

## Introduction

3. In this section we summarise key aspects of the Council's reported performance and provide an outlook on future performance, including our views on the current status of identified risks. We also comment on the progress against agreed improvement actions arising out of the 2005 best value audit and the findings of national performance audit studies.

## Corporate objectives and priorities

4. The Council Plan for 2003 – 2007 sets out the key goals and priorities for the Council and explains how it plans to achieve these. The plan is based on five themes, cutting across a variety of services:
  - learning and working;
  - health and care;
  - community safety;
  - building stronger communities;
  - caring for the Dundee environment.
5. A total of 51 objectives are established across these themes. In meeting the challenge to modernise services, the Council aims to:
  - deliver best value, and demonstrate to the public and stakeholders that this has been done;
  - be customer focused and less concerned about institutional boundaries;
  - renew democracy and public involvement in local government.

## Overview of performance in 2005/06

### Annual report

6. The Council's annual Performance Report for 2005/06 highlights progress against the five themes in the Council Plan, the main achievements in the previous year and ongoing major areas of work. Service performance improvements highlighted include:
  - the launch of a draft Environmental Strategy by the Dundee Partnership for the Environment and a recycling rate of over 30%, well above the national 25% target (although performance did fall short of the Council's own target of 37%);
  - 44,000 Dundee Discovery Cards in operation;

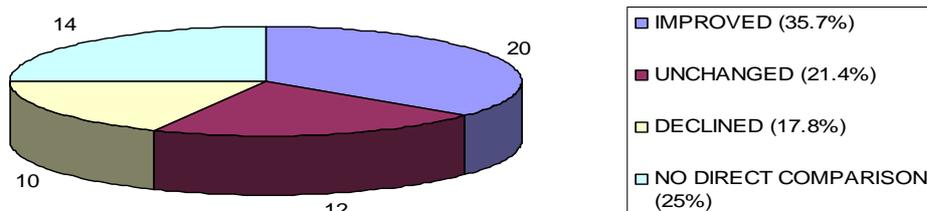


- six departments which have now attained Investors in People accreditation;
- a reduction in the number of young offenders by 27% in the period 2004-2006 and community safety teams which are now fully operational in all designated areas;
- a net job gain of 1,041 (1.3%) in the city between 2005 and 2006;
- improvements in the performance of the housing repairs service, with 90.3% of jobs completed on time at March 2006 (86.7% at July 2005).

7. The Council has made good progress against the actions outlined in the Council Plan as highlighted in the progress report on the Plan submitted to the June Policy & Resources Committee. This report measured performance against 197 separate areas and highlighted that 89% of actions were completed or were on schedule, 2% were ahead of schedule and only 9% were behind target.

### Statutory performance indicators

8. One of the ways of measuring the Council's performance is the statutory performance indicators (SPIs). There are many areas where the Council performs well (33% in the top quartile in 2004/05) and others where performance could be improved (19% in the bottom quartile in 2004/05). This year, a number of indicators demonstrated improvement in year on year performance:



9. Substantial improvements have been made in a wide range of areas such as:

- quality of residential care for older people and other adults;
- reduced processing time for benefits claims and improved collection rates for council tax and non-domestic rates;
- academic attainment of looked after children;
- rent lost on empty houses, rent arrears and the percentage of council house sales completed within 26 weeks;



- timely inspection of trading premises;
- reduction in the percentage of the road network requiring consideration for maintenance treatment.

10. However, performance has declined markedly in other areas such as:

- a reduction in the proportion of new probationers seen by a supervising officer within one week and a reduction in the percentage of new supervised children seen by a supervising officer within one week;
- increased time required to complete homeless assessments;
- a reduction in the percentage of trading standards enquiries, complaints and advice dealt with within 14 days;
- increased costs of refuse collection and disposal costs.

11. In 2004/05 we reported that there were weaknesses in the Council's arrangements to ensure the accuracy of SPIs. Arrangements were much improved this year, with internal audit undertaking an independent check on a number of indicators.

## **Performance outlook – opportunities and risks**

### **Introduction**

12. In our Audit Risk Analysis and Plan we identified some of the strategic risks to Dundee City Council delivering on its stated objectives and priorities. These risks have been grouped into six risk themes.

### **Funding future improvement**

13. The Council has concerns about its funding position and, in line with agreed Council policy, only moderate reserves are held so there are clearly risks to the Council's ability to maintain the current level of services it provides. The absence of a comprehensive policy-led approach to budgeting presents further risks to the Council's ability to resource sustainable service improvements and accommodate new demands for services.

14. In May 2006 a Working Group was established with the specific remit to bring forward measures aimed at integrating resource planning, including the financial costing of corporate/service objectives and new initiatives, into both corporate and service plans. The Working Group is currently evaluating professional guidance and best practice, with a view to improving alignment and integration through revised service planning guidance.



15. In the short-term, priority continues to be given to securing a budget for 2007/08 which meets elected members' aspirations and is within Council Plan targets. Longer-term developments include a 20 year revenue budget model which is being tested using various assumptions.

## **Delivering improved performance**

16. The Council needs to work hard to support continuous improvement in areas where performance is already relatively high and to address areas where performance is poorer than average or declining. The 2005 best value audit also identified scope for the benefits of service review and option appraisal to be applied more widely to ensure value for money in the use of resources.
17. The Council's Strategic Plan Monitoring Database records details of action points from performance improvement areas, the best value improvement plan and other external audit reports. It is a self-assessment approach and responsible officers are required to keep the database up to date with progress. The database has been in place since 2005 and consideration is now being given to ways of better utilising this facility.
18. The functions of the Council Management Team have been reviewed and specific meetings dealing with performance monitoring and strategic issues have been held since October 2005. Best value improvement plan actions relating to service planning, including the use of benchmarking and option appraisals, which were initially planned for June 2006 are now expected by the end of October.

## **Political and management structures**

19. Significant change in 2007, with the introduction of proportional representation and multi-member wards, may mean that current political governance structures will no longer be appropriate. The best value audit also recommended that the Council should review the transparency of its decision-making and scrutiny processes. Whilst there has been no review of the political governance structure within the Council in recent years, officers indicate that the newly elected Council will consider both the Council's priorities and any changes that may be required to the political governance structure.
20. Councillor's roles have become more complex and demanding. The Kerley Report stressed that members have an obligation to take advantage of relevant, available training and that all councils should set aside a specific training budget for members. The Improvement Service has identified core objectives which may include national standards for elected member training. The Scottish Local Authorities Remuneration Committee has recommended that '*Councillors should have a role description, participate in a training needs assessment and have a personal development plan in place once they are in receipt of the new remuneration package*'.



21. To date the Council has focused on the practical application of these changes. It is anticipated that consideration will be given to the training needs of new members early in 2007.

## **Workforce management**

22. People play the key role in delivering high performing services. The Council needs to make sure it has the right skills, in the right place, at the right time. The Council has a high staffing complement, and high absence levels, compared to other Scottish councils. Improvement is dependent on effective workforce planning, successful recruitment and retention practices and good industrial relations.
23. The Council has yet to implement its human resources strategy but anticipates that a report will be taken to the Personnel Committee in November. New absence management procedures were adopted in 2005/06 and absence levels have fallen this year.

## **Effective partnership working**

24. Increasingly, if the Council is to deliver effectively on the themes and objectives set out in its Council Plan, it needs to ensure that services and professions work more closely together to focus the design of services around the needs of individuals and communities.
25. In June 2006, Audit Scotland published *Community planning – an initial review* which found that community planning is progressing, but complexities make aims difficult to achieve. While community planning partnerships have made progress, they need to do more to show how their work is improving public services. The report also calls on the Scottish Executive to support community planning more effectively. In particular, the large number of national policy initiatives, each with their own funding arrangements, can make it difficult for partnerships to plan and deliver effectively.
26. The Council is committed to joint working and its approach is well developed in areas such as co-ordinating financial planning and decision-making. In 2005/06 the Council has been taking steps to improve joint governance arrangements with partners and aims to have guidelines in place by the end of 2006.
27. The process for determining the content of the first community plan covering the period 2001-2006 could be described as top-down, driven by the Council as lead partner. The second community plan published in the summer of 2005 and covering the period up to 2010 drew more heavily on the views of citizens and community groups and provides a good illustration of the Council's commitment to community engagement. Consideration has still to be given, however, to the development of wider public consultation and communication strategies to ensure that services can demonstrate they respond to customer views.



28. New partnership structures continue to be developed, such as the Community Health Partnership, Central and Tay Transport Partnership and Tayside Community Justice Authority. These structures will require partners to develop an agreed and integrated agenda even although there may be differences in governance and resourcing arrangements.

## **Delivering improved infrastructure**

29. The Council needs facilities and infrastructure that are suitable and sufficient to meet the requirements placed on them in the provision of services and the delivery of Council objectives, now and in the future. A requirement for significant investment has been identified in a wide range of areas including school buildings, housing, transport, waste management, care homes and information systems.
30. The Council has not yet fully developed its asset management process which, when operational, should ensure that all the Council's assets are used effectively and efficiently to deliver services in line with priorities. During the year, surveys for sufficiency, suitability and condition, which are a fundamental part of compiling an Asset Management Plan (AMP), were completed and a draft AMP (excluding housing and highways) is being prepared. The Council remains on course to produce a final AMP by May 2007.
31. Recent progress on major projects within the Council includes:
  - appointment of the Discovery Education Consortium to deliver the £85 million Dundee Schools PPP project. This project will see six new primary schools and two new secondary schools being built by summer of 2008. The new schools will enable rationalisation of school provision in areas where there has been a decline in population, as well as replacing poorer quality buildings;
  - appointment of lead consultant architects for the Dundee House Project;
  - further development of the ICT strategy, including redevelopment of the Council's website;
  - integration of the Dundee Discovery Card with the Council's citizen account database, with most cardholders consenting to the sharing of data between services and partners. The integration allows changes notified by citizens to be implemented across multiple systems.

## **Best value**

32. The Local Government in Scotland Act 2003 established best value and community planning as statutory duties for local authorities. In response the Accounts Commission introduced new arrangements for the audit of best value based on a full review by a specialist team once every three years. In the intervening years, short follow-up reviews are carried out by the local auditor.



33. Dundee received a full best value audit in 2005. The Council developed an improvement plan in response to the issues raised and our findings on the Council's progress on the plan are reflected throughout this report.
34. Overall, there has been some progress in most areas, although there has been slippage in a number of actions. The target dates for actions where slippage has occurred have been revised, with progress monitored through the Council Management Team and the Best Value Sub Committee. The Council requires to maintain the pace of change and should take account of issues raised in other councils' best value reports to ensure they are well-placed to demonstrate continuous improvement.

#### **Action point 1**

### **National studies**

35. Audit Scotland carries out a national study programme on behalf of both the Accounts Commission and the Auditor General for Scotland. Reports published in the last year on reviews of public sector pension schemes, community planning and the National Fraud Initiative are summarised elsewhere in this document. Other reports published during the year, and of direct interest to the Council, are set out below. Further information on these studies and reports can be obtained from Audit Scotland's webpage at [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

### **A mid-term report: a first stage review of the cost and implementation of the teachers' agreement *A Teaching Profession for the 21<sup>st</sup> Century***

36. In May 2006 Audit Scotland published the results of a review of the implementation of the teachers' agreement arising from the McCrone report. This found that the agreement has brought benefits for the teaching profession, but the lack of performance measures makes it difficult to assess the wider impact of the £2.15 billion investment. The report recommends that the Scottish Executive work with other parties to the agreement to identify and report on a set of comprehensive performance measures.

### **Council housing transfers**

37. In March 2006 Audit Scotland published the results of a review of how well the Scottish Executive's housing transfer policy has been implemented and whether transfers have provided good value for money. This found that the transfer of council housing ownership is bringing benefits for tenants, including more investment in properties, promoting tenant control, facilitating increased repairs and maintenance and the building of new homes, and keeping rent increases down. The report also found that the management of transfers is improving but better, clearer measures are needed to assess impact and value for money.



38. Dundee City Council has opted not to go for a full housing stock transfer and submitted a Scottish Housing Quality Standard delivery plan to the Scottish Executive. Following discussions with Communities Scotland, the Council re-submitted its delivery plan which has subsequently been approved.

### **Following the public pound – a follow-up report**

39. In December 2005, Audit Scotland published the results of a study of council funding of arms length and external organisations (ALEOs) to provide information on the scale of funding and how councils perform against the code of guidance on funding external bodies and following the public pound. This report stated that Scottish councils provided £220 million to 14,000 organisations, including companies, trusts and voluntary organisations, to deliver a wide range of council-related services such as support for people with disabilities and the management of leisure centres.
40. The study found that no council fully complied with the guidance, although only five councils had a low level of compliance. Dundee City Council was identified as one of nine councils demonstrating a high level of compliance with the code.
41. The report recommends that councils have a register of funding to external organisations, develop a corporate policy on free or subsidised use of council properties, vehicles and facilities, take a risk-based approach to dealing with the organisations they fund, and focus their resources on organisations who contribute to the council's objectives, have arrangements for scrutiny and explore joint working with other councils.



# Financial position

## Introduction

42. In this section we summarise key aspects of the Council's reported financial position and performance to 31 March 2006, providing an outlook on future financial prospects, including our views on potential financial risks.

## Council tax and the general fund

### Revenue performance 2005/06

43. The Council's net revenue expenditure in 2005/06 was £283.517 million and was met by government grants and local taxation of £281.229 million, resulting in a net general fund deficit of £2.288 million compared to a budgeted deficit of £4.770 million.
44. In his Foreword to the financial statements, the Depute Chief Executive (Finance) highlights a number of factors contributing to this favourable variance. In particular, additional costs of £3.481 million relating to equal pay claims were more than compensated for by underspends on services of £3.361 million and additional government grants of £1.102 million. The Council had not included costs for equal pay claims in the 2005/06 budget and the savings made by services during the year were essential to achieve a balanced outcome.

## Reserves and balances

45. At 31 March 2006 the Council had total cash backed reserves and funds of £16.4 million, including a capital fund established to aid delivery of the capital programme and a renewal and repair fund used to finance expenditure to be incurred in repairing, maintaining, replacing and renewing fixed assets.

### *Reserves and Funds 2005/2006*

Description	2005/06 £ Million	2004/05 £ Million
General Fund	6.596	8.884
Renewal & Repair Fund	3.237	4.218
Capital Fund	5.440	4.278
Insurance Fund	1.127	0.011
	<b>16.400</b>	<b>17.391</b>



46. £3.8 million of the general fund reserve at 31 March 2006 was earmarked for specific purposes. This leaves an unallocated balance of £2.8 million which is broadly in line with the Council's policy on reserves.

47. Significant earmarked amounts include:

- outstanding expenditure commitments at 31 March 2006 of £1.648 million;
- devolved school management balances of £0.555 million;
- the car parking reserve of £1.562 million.

The Council faces a range of financial issues which will significantly impact on its reserves position and this is discussed further in our Financial Outlook section below.

## Rents and the housing revenue account

48. The Council is required by legislation to maintain a separate housing revenue account and to ensure that rents are set to at least cover the costs of its social housing provision. The budget set for 2005/06 was based on an average weekly rent level of £46.55, an increase of 4.1% on the previous year. A surplus of £0.336 million was achieved in 2005/06 and was transferred to housing revenue account balances. The budget set for 2006/07 is based on a further increase in rent levels of 4.0% giving a weekly average rent level of £48.41.

## Group balances and going concern

49. The Council has an obligation to meet a proportion of the expenditure of the joint boards of which it is a constituent member. All of these boards (Tayside Joint Police Board, Tayside Fire and Rescue Board, Tayside Valuation Joint Board and Tayside Contracts Joint Committee) had an excess of liabilities over assets at 31 March 2006 due to the accrual of pension liabilities.

50. The overall effect of inclusion of the Council's associates and joint venture on the group balance sheet is to reduce net assets by £283.9 million, substantially as a result of these liabilities. All group bodies' accounts have been prepared on a going concern basis as pension liabilities will be funded as they fall due through a combination of employee and employer contributions, government grants and council tax.

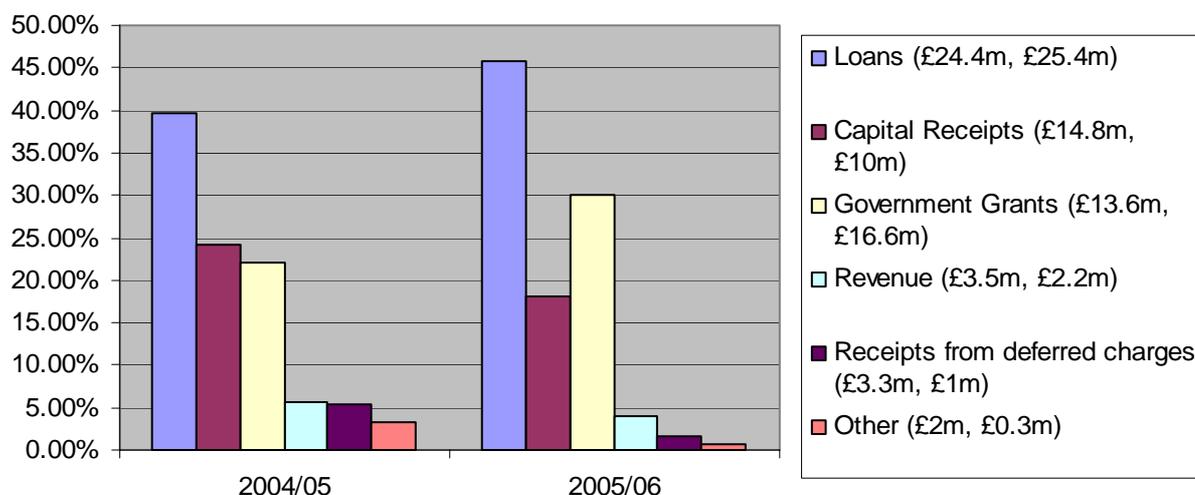


## Spending on assets and long-term borrowing

### Capital performance 2005/06

51. Following the introduction of the prudential code in April 2004 the Council can decide locally on a capital investment strategy which must meet best value requirements as well as being affordable. The Council's prudential indicators for 2005/06 were set in December 2004 and significant increases in capital expenditure have been made under these freedoms as the Council seeks to improve its asset infrastructure.
52. Capital expenditure in 2005/06 totalled £55.6 million, a reduction from the £61.6 million incurred in 2004/05. £47.6 million was spent in 2003/04, the last year of central capital controls. Capital investment in the last two years was funded as shown below. As the Council has increased its capital spending, the proportion funded by debt has increased significantly with aggregate long and medium term borrowing at 31 March 2006 of £302.7 million, an increase of £34.6 million on the previous year.

*Sources of finance for capital expenditure 2005/2006*



(figures reflect the actual expenditure in each category in 2004/05 and 2005/06 respectively)

53. Around 80% of long and medium term loans at the year-end mature after more than 10 years and the Council has actively managed its exposure to variable interest rate movements with most of its debt on fixed interest.

### Forward capital programme

54. General services capital plans for 2006/07 and 2007/08 anticipate expenditure of £49.557 million and £42.539 million respectively. This is expected to be funded by a number of sources including capital receipts, grants and other contributions. This slowing down in the capital programme will be reflected in a reduction in borrowing of £8.3 million over the two years.



55. The Council has recently completed its housing stock review and has submitted a Scottish Housing Quality Standard delivery plan to the Scottish Executive. This plan identified that an investment of £140.8 million is required in council housing core stock over the next ten years. An additional £45 million is planned to be spent on a maintenance investment programme during the same period. Following discussions with Communities Scotland the Council re-submitted its delivery plan which has subsequently been approved.

## Significant trading operations

56. The Local Government in Scotland Act 2003 replaced compulsory competitive tendering regulations with a duty to maintain and disclose trading accounts for significant trading operations, which are required to break even over a three year rolling period. The first three year period ended in 2005/06.
57. The Council has a single significant trading operation, Dundee Contract Services. In the three years to 31 March 2006 it made an aggregate surplus of £1.521 million, meeting the statutory target. Whilst the organisation has consistently achieved a surplus in each of the previous three years, this has fallen significantly from £1.2 million in 2003/04 to £0.164 million in 2005/06. The downturn was due to a fall in turnover in the last two financial years, coupled with above average inflation increases in pension costs, interest charges and transport costs. Action is being taken to improve efficiency and control costs to ensure the organisation continues to meet its financial objectives.

## Pension funds

58. The Council is responsible for the management and administration of two superannuation funds – the Tayside Superannuation Fund and the Tayside Transport Superannuation Fund. The investment assets for both funds are under the management of external fund managers and have fluctuated markedly over the last few years, due to changes in equity markets. The position at 31 March 2006 reflects a significant improvement from a low point in 2002/03:

	31/03/03 £m	31/03/04 £m	31/03/05 £m	31/03/06 £m
Tayside Superannuation Fund*	729.7	942.2	1,101.6	1,432.7
Tayside Transport Superannuation Fund	29.1	32.9	34.5	40.6

\* The Council's share of the assets at 31 March 2006 amounted to 39% of the Fund's assets.



59. A full actuarial valuation of both funds as at 31 March 2005 was reported in early 2006. Factors such as the volatile stock markets and increasing life expectancy have resulted in the funding level for the Tayside Superannuation Fund, calculated as the ratio of fund assets to past service liabilities, falling from 97% at 31 March 2002 to 91% at 31 March 2005. The actuary is required to make a 3-year assessment of the contributions that should be paid by the employing authorities from 1 April 2006 to maintain the solvency of the fund. The contribution levels are based on percentages of employee contributions, normally 5% - 6% of salary. This shows that budgeted contributions are expected to rise from 275% of employee contributions in 2005/06 to 315% by 2008/09.
60. There are proposals to amend the Local Government Pension Scheme which are designed to reduce the ongoing cost, although these have not yet been implemented. The 2005 valuation did not make any allowance for changes to the regulations. Should any amendments be made the actuary may wish to amend the certified levels of contribution.

## Financial outlook

### Current budget

61. The 2006/07 revenue budget was based on a Band D council tax level of £1,211, an annual rise of 2.6%. General allowances for pay and cost inflation pressures were built into the 2006/07 budget, together with additional annual pay costs of £1 million estimated to result from the future implementation of single status.

### Equal pay

62. The 1970 Equal Pay Act makes it unlawful for employers to discriminate between men and women in terms of their pay and conditions where they are doing the same or similar work, work rated as equivalent, or work of equal value. Employees who consider that they have been discriminated against in terms of pay can put forward claims to an Employment Tribunal. Following cases pursued against English councils, the extent of exposure of Scottish councils arising from individual pay claims began to emerge during 2005/06.
63. In common with many other Scottish councils, Dundee City Council has sought to limit its exposure to the financial risk associated with equal pay claims by agreeing to offer payments to specific groups of employees as part of a compensation package. Estimated costs of £3.5 million have been recognised in the 2005/06 financial statements for the total one-off cost of these payments.



64. The extent to which the actual costs vary from current estimates will depend on a number of factors including take-up rates, any employees not covered by the calculations and the level of awards of any cases taken to tribunal. Officers estimate that approximately 91% of the payments have been agreed by employees therefore it is considered that there will be no material impact on future budgets. Costs above that already budgeted will increase the financial pressure on the Council.
65. While moves to agree compensation payments to affected employees will help to reduce financial risk in this area to some extent, there remain risks while existing pay and reward structures remain in place. The future implementation of the single status agreement provides an opportunity to address any underlying inequalities in pay and other conditions of service.

## **Single status**

66. In 1999 a single status agreement was reached between Scottish local authorities and trades unions to harmonise the terms and conditions of manual and administrative, professional, technical and clerical workers (covering pay, working hours, leave and negotiating mechanisms). There was a presumption that single status would be cost neutral with any increased costs being offset by savings arising from changes to other conditions of service or from efficiencies.
67. The original national single status agreement specified that implementation should take place by April 2002 but, following difficulties in establishing a model job evaluation scheme, was extended by agreement between local authorities and unions to April 2004. To date only one council, South Lanarkshire, has implemented single status.
68. Dundee City Council has yet to implement the agreement and estimates that this will be in place by April 2007. At 31 March 2006, the Council had not set aside any funds for the cost of single status, although £1 million, £2 million and £3 million have been allocated respectively in each of the next three financial years.
69. Until a local agreement is concluded the initial and continuing costs to the Council cannot be reliably estimated. This represents a financial risk to the Council. The amount currently budgeted by the Council in 2006/07 represents around 0.9% of pay costs (excluding teachers). In securing a local agreement the Council needs to ensure it maximises the opportunity for service and job redesign to ensure that it achieves value for money from its investment in its staff.

## **Efficient government**

70. The efficient government initiative is a central part of the government's programme of investment, reform and modernisation and is a five year programme aimed at attacking waste, bureaucracy and duplication in Scotland's public sector.



71. The Efficient Government Plan sets targets to achieve £745 million of cash-releasing savings, and £300 million of time-releasing savings, by 2007/08. It is anticipated that local government as a whole will contribute £325 million in cash-releasing savings to the overall target. Although the Scottish Executive has not notified councils of the efficiency savings they should achieve each year, it is anticipated that Dundee City Council's contribution to the target will be £4.984 million over three years, equating to £1.627 million for 2005/06.
72. The majority of these assumed efficiency savings have been incorporated into annual financial settlements, presenting an immediate challenge as efficiency gains through service redesign are likely to take longer than one year to be fully realised. Failure to achieve the level of savings anticipated will increase financial pressures and may impact adversely on services provided. In order to claim an efficiency councils need to demonstrate that service outcomes have been maintained or improved.
73. Based on information supplied by councils across Scotland, it is apparent that:
- few councils have a system in place to properly monitor, measure and report efficiency gains and that effort is still required to ensure that appropriate guidance is issued to staff to clarify what constitutes an efficiency;
  - the level of projected efficiencies varies significantly between councils;
  - the majority of planned efficiencies relate to areas and projects other than the SE's five key work streams of procurement, asset management, absence management, streamlining bureaucracy and shared support services;
  - plans for projects to create time releasing efficiencies are not well developed and little in the way of efficiencies is expected to be generated by 2007/08 through shared support services. In both cases this is indicative of the time required to develop plans for fundamental service redesign.
74. Dundee City Council has approached the efficient government challenge in a structured and systematic manner and has established an Efficient Government Project Board to drive the process. Overall, the Council aims to deliver the indicative three year efficiency gain targets set by the SE for 2005 – 2008, but has some work to do to identify the additional savings required in year three.
75. The Tayside Procurement Consortium of Dundee City, Angus and Perth and Kinross Councils commissioned consultants to prepare a 'scope and readiness assessment' of the three authorities and to develop a combined procurement strategy. The report, which was issued to the Consortium in January 2006, was the basis of a business case and stage 2 Efficient Government Fund bid which was submitted in March 2006. Further progress with the procurement strategy is dependent on approval of the stage 2 bid.



76. The Council is aware of the most challenging aspects of efficient government which require mechanisms to ensure that outcomes and quality are not adversely affected by financial savings. The Council is making good progress in implementing processes and procedures to measure and monitor efficiency savings. Most of these, however, are still at an early stage. Until a single efficiency monitoring and measurement system is in place it will be difficult to evidence claimed efficiencies. In common with other councils, much work is still required to ensure that appropriate guidance is issued to staff to clarify what constitutes efficiency and how it should be measured, monitored and reported.
77. The Improvement Service has commissioned an external partner to develop and implement measures of productivity and efficiency in local government services. These measures will be available for councils to assist in their forward planning and to aid them in demonstrating their efficiency gains for the financial year 2006/07. The Auditor General for Scotland intends to publish a report around the end of 2006 to summarise the position across the Scottish public sector on the efficient government initiative. The Council should consider the findings and any recommendations included in this report when reviewing their own position.

## **Pension liabilities**

78. 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. A recent Audit Scotland report on public sector pension schemes highlighted that the combined funding shortfall and unfunded liabilities of the six local government pension schemes in Scotland may be as high as £53 billion.
79. In accounting for pensions, 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. This requirement results in very large future liabilities being recognised in the annual accounts.
80. The Council's estimated pension liabilities at 31 March 2006 exceeded its share of the assets in the Tayside Superannuation Fund by £195.752 million, increasing from £191.023 million in the previous year. While the net assets attributable to the Council in the main scheme have increased by £96.789 million, the net liabilities have increased by £102.4 million. Estimated liabilities for discretionary pensions, where the Council agrees to fund an early retirement, have fallen by £0.883 million during the year.



# Governance

## Introduction

81. In this section we comment on key aspects of the Council's governance arrangements during 2005/06. We also provide an outlook on future governance issues, including our views on potential risks.

## Overview of arrangements in 2005/06

82. Corporate governance is concerned with structures and processes for decision making, accountability, control and behaviours at the upper levels of the organisation. In previous years we have concluded that the Council had systems in place that operated well within a sound control environment and have reached the same conclusion this year.

83. At a corporate level the Council has appropriate arrangements in place to prevent and detect inappropriate conduct and corruption. These arrangements include codes of conduct for elected members and staff, a whistle blowing policy and defined remits for relevant regulatory committees.

84. Effective scrutiny is central to good governance, with a significant role for members to scrutinise performance, hold management to account on service delivery and support the reform and modernisation agenda. Members in Dundee have the opportunity to challenge service activities and performance through the Best Value Sub Committee and the Audit and Risk Management Sub Committee which deals with financial and governance matters.

85. The 2005 best value audit recommended that scrutiny arrangements within the Council should be strengthened and, as a result, the remit of the Best Value Sub Committee has been expanded to give members better opportunities to exercise scrutiny and greater public accountability. Progress reports in relation to best value and efficient government are to be discussed at the Sub Committee twice a year. Given that these changes are recent, we have not yet had the opportunity to assess how effective they have been in practice. The Council's Audit and Risk Management Sub Committee adheres to CIPFA's guidance note *Audit Committee Principles in Local Authorities in Scotland* and provides a sound contribution to the overall control environment.

86. The Council has a Risk Management Strategic Plan in place, with the Risk and Business Continuity Manager responsible for implementing the strategy. An internal audit review of risk management during the year highlighted a number of areas for improvement, including the need to:



- ensure that risk management issues are considered prior to decisions being taken on projects and procedures introduced to formally consult with the Risk Manager and to record the outcomes by way of a documented risk assessment;
- facilitate control and monitoring of risks, complete the Council Risk Register and assess the adequacy of existing controls as soon as possible;
- embed risk management within the Council, including consideration of further measures to increase staff awareness, to raise the profile of risk management within departments and to increase the accountability of Departmental Managers.

87. Internal audit plays a key role in the Council's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. We carry out an annual review of the Council's internal audit arrangements and found that the function continues to be well managed. Staff are experienced and competent and the work programme for 2005/06 was comprehensive.

## Systems of internal control

88. *A Statement on the System of Internal Financial Control* is included within the annual financial statements, with the aim of providing assurance to stakeholders on the adequacy of arrangements. The statement concluded reasonable assurance could be placed on the Council's internal control system. To support the statement, the Chief Internal Auditor provided her opinion that '*reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal control system in the year to 31 March 2006*'.

89. With effect from 2005/06, recommendations made in previous years' internal and external audit reports are being monitored by management and internal audit, with progress regularly reported to the Audit and Risk Management Sub Committee.

90. As part of our work to provide an opinion on the annual financial statements we assessed the extent to which we could gain assurance on a number of the Council's main financial systems. We assessed the following central systems as having a satisfactory level of control for our purposes:

- Payroll
- creditors payments
- housing rents
- capital accounting
- council tax
- non-domestic rates
- housing benefits
- budgetary control
- treasury management
- debtors and income



## Prevention and detection of fraud and irregularities

91. At the corporate level, the Council has appropriate arrangements in place to prevent and detect fraud, including an anti-fraud and corruption policy and fraud guidelines which were updated in June 2006.
92. Under the National Fraud Initiative (NFI), councils compare information about benefit applicants, students, public sector employees and pensioners with other public bodies to find fraud and errors. The findings of the 2004/05 exercise were published in May 2006, highlighting that across Scotland £15.1 million of fraud, overpayments and savings were found, including:
- 270 cases where pensions were being paid to people who had died;
  - 564 cases of public sector employees and pensioners either fraudulently claiming housing benefits or receiving them in error;
  - 215 cases of housing benefit overpayments to students;
  - 53 cases referred to the Procurator Fiscal and 32 employees who have been dismissed, disciplined or who resigned as a result of the initiative.
93. In 2005/06, by applying data matching, the Council identified £151,610 of overpayments for housing and council tax benefits which represents 0.32% of overall benefits payments. Other fraud investigations, including payroll cases, are ongoing as at September 2006.
94. Audit Scotland is working with the Audit Commission to widen the scope of the NFI during 2006/07. Public bodies will provide information again in October this year and will have fresh information to investigate in early 2007. The Council needs to ensure that it uses the opportunities presented by the NFI on an ongoing basis to assist in the detection of fraud.

## Governance outlook

95. Continuing development of risk management and scrutiny arrangements will further strengthen the Council's corporate governance arrangements. The Council is also working on improving governance arrangements in the community planning arena. The national study identified that the governance of Community Planning Partnerships needs to be improved by clarifying their accountability arrangements and developing more effective scrutiny and risk management arrangements.
96. The forthcoming local government elections in May 2007, bringing the introduction of proportional representation and multi-member wards, have potential implications for the political make-up and governance of the Council. The Scottish Executive's intention is also to remove barriers to encourage the widest possible range of people to serve as councillors. These reforms will require significant input from the Council to ensure its governance arrangements are fit for purpose, including committee structures, role/remits of members and arrangements for training new members.



# Financial statements

## Introduction

97. In this section we summarise key outcomes from our audit of the Council's financial statements for 2005/06. We comment on the significant accounting issues faced and provide an outlook on future financial reporting issues.
98. We audit the financial statements and give an opinion on:
- whether they present fairly the financial position of the Council and its expenditure and income for the year; and
  - whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.
99. We also review the Statement on the System of Internal Financial Control by considering the adequacy of the process put in place by the Council 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

100. We have given an **unqualified** opinion on the financial statements of Dundee City Council for 2005/06.
101. The Council's unaudited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June 2006. Audited accounts were finalised prior to the target date of 30 September 2006 and are now available for presentation to the Council and publication. The financial statements are an essential means by which the Council accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources.

## Accounting practice

102. Local authorities in Scotland are 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 accounting adjustments were made to the figures included in the 2005/06 unaudited accounts. These were generally presentational adjustments where income received had been netted off against expenditure in error. Whilst this resulted in increases in income, expenditure, and debtor and creditor balances, there was no impact on the Council's net financial position.



103. Other adjustments made to the accounts resulted in an increase in the net deficit on the consolidated revenue account of £114,000. Details of other significant accounting issues arising in the course of our audit are summarised below.

### **Debt restructuring costs**

104. Lender option borrower option arrangements (LOBOs) are variable rate loans whereby, if the lender decides to change the interest rate at certain predetermined dates, the borrower has the option whether to accept the change or to repay the loan. Although LOBOs do not fully provide the guaranteed long term interest rate stability of PWLB fixed rate maturity loans, longer term stability has improved in recent years with longer call intervals, and loan maturity now available up to 60 years.

105. There is currently a debate over the appropriate accounting treatment of LOBOs. One issue is whether the characteristics of a LOBO require any premium arising from replacing existing PWLB debt to be recognised immediately rather than over the life of the replacement borrowing.

106. The Council had LOBO debts totalling £40 million at 31 March 2006, £20 million of which replaced existing debt. Its accounting policy is to recognise the cost of premiums arising from all debt restructuring, including that involving the use of LOBOs, over the full life of the replacement borrowing. This approach is only permissible under the SORP if the overall economic effect of the original and replacement borrowing is substantially the same. A total of £1.3 million of rescheduling costs relating to the use of LOBOs was being carried on the balance sheet at 31 March 2006.

107. The Depute Chief Executive (Finance) has confirmed his view to us that, in concluding that it is appropriate to carry-forward these costs, the Council has taken into account the definition of the term 'overall economic effect' offered by the SORP guidance notes, the expected stability of interest rates over the period of replacement borrowing and that there is no evidence that lenders have sought in practice to impose significant interest rate increases or that authorities have refused to accept any changes. We are satisfied that this is a reasonable approach.

### **Group accounts**

108. Modified arrangements for the preparation of group accounts were mandatory for the first time in 2005/06. The widening diversity of service delivery vehicles used by local authorities means that consolidated group accounts are required to present fairly the activities of an authority. The Council prepared group accounts in accordance with the new requirements following a review to determine its interest in subsidiaries, associated entities and joint ventures.



109. Tayside Contracts has been included in the group accounts as a 'joint arrangement' rather than a subsidiary or associate as the Council is of the opinion that the organisation does not constitute a legal entity. Tayside Contracts, however, produces its own financial statements and is subject to a separate audit appointment under the Local Government (Scotland) Act 1973. One of the definitions of an entity included in the SORP is '*a body corporate or statutory body which has a separate legal personality and is legally required to prepare its own single-entity accounts*'. The Council should clarify the formal status of Tayside Contracts prior to the preparation of the 2006/07 financial statements.

**Action point 2**

## **Public Private Partnership**

110. Securing value for money (together with affordability) are key requirements for public bodies to progress PPP projects. We have examined the analysis provided by the Council's financial adviser on the value for money of the Dundee Schools' PPP Project and have concluded that, based on the adviser's analysis, at this stage the quantitative assessment demonstrates that the PPP project represents overall value for money, in accordance with current guidance.

111. We also provided our judgement on the Council's proposed accounting treatment to treat the project as off balance sheet. We concluded that:

- the process followed to determine if the transaction should be on or off the Council's balance sheet was in accordance with the current underlying guidance; and
- the judgment on the accounting treatment is reasonable, subject to the possibility that the assets may not to be recognised on either the balance sheet of the purchaser or the contractor.

## **Legality**

112. Each year we request written confirmation that the Council's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes. The Head of Finance has confirmed that, to the best of her knowledge and belief and having made appropriate enquiries of the Chief Executive and Council Management Team, the financial transactions of the Council were in accordance with the relevant legislation and regulations governing its activities.



113. The 1970 Equal Pay Act makes it unlawful for employers to discriminate between men and women in terms of their pay and conditions where they are doing the same or similar work. As highlighted earlier in this report, the Council has recognised a liability in the financial statements in relation to the potential contravention of this Act. Until the single status agreement is implemented, however, there remains the possibility that the Council could be judged to have contravened the Act.

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

## Financial reporting outlook

115. Overall the Council is well placed to continue to prepare annual financial statements in accordance with accounting and statutory requirements. It has a record of responding positively to audit issues and changing accounting rules. Challenges ahead include a number of changes that have been made to the 2006 SORP:

- replacement of the consolidated revenue account with a traditional income and expenditure account;
- a new statement that reconciles the income and expenditure account surplus or deficit for the year to the general fund surplus or deficit;
- replacement of the statement of total movement in reserves with a statement of total recognised gains and losses; and
- similar changes to the housing revenue account and group accounts.

116. These changes will have a significant impact on the presentation of the 2006/07 annual financial statements to make them more consistent with the accounts of other public and private sector entities. The Council should take this opportunity to review the presentation of its budget and summary financial results to members and the wider public to ensure that financial planning and activity is fully transparent.

### **Action point 3**

117. Further ahead, there are proposed changes to the application of financial reporting standards (FRS) 25 and 26 in 2007. Application of these standards to local authorities may require the premium on loans that have been re-scheduled to be charged to revenue in full in the year it is incurred rather than being written off over the period of the replacement loan, which can be up to 40 to 50 years. Such a change could have significant implications on council tax levels and Directors of Finance have been discussing with the Scottish Executive how this risk can be avoided through the issue of regulations.



## **Change of external auditor**

118. Regular rotation of auditors is required by auditing standards and is an important component in guarding against perceived or actual threats to auditors' objectivity and independence. Audit Scotland's policy is to rotate auditors at least once every five years. Where the audit is carried out by Audit Scotland staff rather than a private firm, the engagement lead and other key staff will be rotated.
119. This is the final year of our current appointment to the audit of Dundee City Council. From 2006/07 Audit Scotland will remain as the Council's appointed auditor but the new engagement lead will be Mark Taylor. The change of auditor represents an opportunity to build on existing good practice to continuously improve accounts preparation processes in partnership with the incoming auditor.



# Final Remarks

120. The members of Dundee City Council are invited to note this report. We would be pleased to provide any additional information that members may require.

121. We have made a number of recommendations in the various reports we have issued during the course of the year and have obtained assurances from officials that action will be taken as appropriate. Attached to this report is a list of significant matters arising from the audit which we consider to be of particular interest to members.

122. The co-operation and assistance given to us by Dundee City Council members and staff over the five years of our audit appointment is gratefully acknowledged.



# Appendix A: Action Plan

## Key Risk Areas and Planned Management Action

Action Point	Refer Para. No	Risk Identified	Planned Action	Responsible Officer	Target Date
1	34	<p><b>Best value</b></p> <p>Overall the Council has made some progress against most of the improvement actions agreed as a result of the 2005 best value audit. The Council requires to maintain the pace of change and take account of issues raised in other councils' best value reports.</p> <p><b><i>Risk: the Council may be unable to demonstrate continuous improvement.</i></b></p>	<p>The Council will continue to implement the actions outlined in the agreed best value audit plan and to address the wider best value agenda by continually reviewing its services and processes. The Council will also benchmark with other organisations and seek to identify and learn from deemed best value practice.</p>	Various – in line with Best Value Improvement Plan	Various – in line with original target dates or revised dates where applicable.
2	109	<p><b>Group accounts</b></p> <p>Tayside Contracts has been included in the group accounts as a joint arrangement as the Council is of the opinion that the organisation does not constitute a legal entity. Tayside Contracts, however, produces its own financial statements which is generally an indicator that a body is an entity. The Council should clarify the formal status of Tayside Contracts prior to the preparation of the 2006/07 financial statements.</p> <p><b><i>Risk: the legal standing of Tayside Contracts is unclear. The Council may fail to comply with accounting requirements.</i></b></p>	<p>We consider our treatment of Tayside Contracts to be correct, however we are happy to review the position as recommended.</p> <p>The approved 2006-2011 business plan for Tayside Contracts includes a full appraisal of the possible legal status options for the organisation. The outcome of this appraisal will, in turn, inform the Council's review of the appropriate accounting treatment of Tayside Contracts.</p>	Head of Finance	20 June 2007

