Accounts Commission for Scotland

S.R. 99/3

OVERVIEW REPORT ON THE 1996/97 AUDITS OF LOCAL AUTHORITIES

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A REPORT BY THE CONTROLLER OF AUDIT TO THE ACCOUNTS COMMISSION IN TERMS OF SECTION 102 (1) OF THE LOCAL GOVERNMENT (SCOTLAND) ACT 1973

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1. INTRODUCTION

1.1 As a result of the reorganisation of local government in Scotland, a new single tier structure of 32 councils came into existence on 1 April 1996. This report describes the context in which the new councils were established and the general environment in which they had to operate in their first year. Because of the difficulties and pressures which they faced, many of the new councils were very late in producing accounts of an acceptable standard and in dealing with audit issues. This led to delays by auditors in completing their audits and also delayed the preparation of this report.

1.2 I have made this report in response to a request from the Accounts Commission under Section 102(1) of the Local Government Act 1973.

2. STRUCTURE AND CONTENT

2.1 My report is based on information drawn from local reports to individual councils which have already been made by auditors. Currently the audits of Highland, Dundee and Dumfries and Galloway Councils for 1996-97 are still outstanding, generally because there are major issues which have still to be resolved to the satisfaction of the auditors. I have included reference in this report to significant issues which are likely to feature in these reports. If any additional matters arise they will be reported by auditors and, if appropriate, by myself under my statutory reporting powers.

2.2 The first part of the report is divided into four sections. The first and second describe the circumstances in which the new councils came into existence and the tasks and difficulties which they faced; the third section summarises the main themes most commonly identified by auditors and the final section comments on significant issues which have arisen at individual councils. The second part of the report describes value for money and management arrangements audit work completed during the year.

3. BACKGROUND TO THE FORMATION OF THE NEW COUNCILS

3.1 The Local Government etc. (Scotland) Act 1994 provided for the winding down of the 53 district councils and nine regional councils and their replacement by 29 unitary councils. The three island councils, which were already multi-functional organisations, continued with their powers relatively unchanged.

3.2 The transfer of functions to the 29 new councils was a major task. In some cases it involved the aggregation of outgoing authorities to form a single new council; in other cases the outgoing authorities were dis-aggregated into several new councils. For example, the new Highland Council was created by bringing together the eight former districts and the former regional council to form a single new authority whereas the former Strathclyde Regional Council was divided into 12 new councils.

3.3 From November 1994, when the Act received royal assent, there was a period of approximately 17 months in which to plan for the termination of the existing authorities and the establishment of the new councils. From 6 April 1995 until they came into operation on 1 April 1996, the new councils existed in shadow form. During this period they made preparations for the assumption of full powers by acquiring accommodation, recruiting staff, designing management structures, developing policies and drawing up budgets.

3.4 While the nature of the changes necessary to transfer the functions from the outgoing authorities to the new councils varied considerably, depending on local circumstances, all 29 new mainland councils were faced with a common set of key tasks to set up their new organisations. The major issues which they had to address were:

- the design of a new corporate management structure
- the formulation of new policies
- rationalisation of systems and working practices
- harmonisation of conditions of service
- the development of IT systems
- the design of new management information systems
- the acquisition of suitable accommodation
- the recruitment and integration of new staff
- the bringing together of different cultures.

3.5 One of the principal arguments advanced in favour of the new local government structure was that the move to single tier authorities would facilitate a reduction in staff numbers. The pressure to reduce staff numbers was accentuated by the financial constraints faced by the new councils. There was a reduction of some 11,000 in the number of local authority staff during the reorganisation process. This figure included a significant number of senior and experienced finance department staff.

3.6 In their first full year the new councils had a wide range of priorities to address, many of them requiring difficult choices to be made. For example, the need to develop new DLO management information systems simultaneously with the need to prepare tenders for major DLO contracts; and the need to prepare budgets and accounts for the new authorities while fulfilling their statutory duty to complete the accounts of the former authorities.

4. GUIDANCE TO INCOMING COUNCILS

4.1 To assist the new councils in identifying and addressing the challenges they would face the Accounts Commission issued a report in August 1995 entitled Local Government Reorganisation and the Stewardship of Public Funds. The report emphasised the need for the new councils to focus on a range of key issues including their corporate governance arrangements, their procedural and financial controls, accounting and audit principles, IT provision, the achievement of value for money and the development of performance standards and indicators.

4.2 The report highlighted the special role of chief executives in ensuring that there is recognition among members and officers of the importance of following the principles of good governance. The guidance also stressed the need for the timely production and publication of councils' annual reports and financial statements, the adoption of audit committee principles and the importance of having proper arrangements in place for achieving value for money.

5. THE COMPLETION OF ACCOUNTS AND AUDITS

5.1 The statutory deadline for the completion of 1996/97 accounts for audit was 31 August 1997. Those authorities that had not submitted their accounts by that date were granted an extension to 30 September by The Scottish Office. Further extensions were allowed to 31 October and, in exceptional circumstances, to 30 November. The following table indicates the dates by which accounts were lodged for audit:

TABLE

DATE BY WHICH 1996/97 ACCOUNTS WERE AVAILABLE FOR AUDIT

Received by	Total received	Cumulative total
31.08.97 (statutory date)	6	6
31.10.97	8	14
31.12.97	9	23
28.02.98	4	27
30.04.98 (or later)	5	32

5.2 With the bulk of councils' accounts available for audit by the end of the 1997 calendar year, it would have been reasonable to expect most of the 1996/97 audits to be completed by the spring of 1998. In the event, as the following table shows, it was only in the first months of 1999 that substantial progress towards completion of these audits was achieved:

TABLE

DATE BY WHICH 1996/97 AUDITS WERE COMPLETED

Completed by	Total	Cumulative total
31.12.97	1	1
31.03.98	-	1
30.06.98	4	5
30.09.98	4	9
31.12.98	7	16
31.03.99	5	21
30.06.99	8	29
(outstanding	3	32)

5.3 The principal cause of the delay in the completion of audits was the quality of accounts presented for audit. Although most councils lodged their accounts by the end of 1997 many continued to make significant adjustments to the accounts with the final version being received for audit a number of months later. The absence, or the delay in the production, of key working papers to support the accounts and the failure to complete fundamental control processes, such as bank reconciliations, also had a significant impact on the time-scale for audit completion. Accounts presented for audit need to be supported by adequate working papers and the fundamental reconciliation and control processes which underpin the accounts need to be in place to enable audits to be completed expeditiously.

6. FINANCIAL STEWARDSHIP

6.1 Many new councils had difficulty in establishing fundamental control mechanisms such as key reconciliations between the main financial systems and subsidiary systems and records. In many cases bank reconciliations had not been undertaken on a regular basis throughout the year or at the financial year end. This led to the accounts of several councils being qualified. There was frequent reference in auditors' reports to an absence of reconciliations in relation to debtors, creditors, housing benefits and other financial systems and to delays in clearing amounts temporarily allocated to suspense accounts. Auditors also reported problems arising from the parallel running of financial systems and weaknesses in a range of other controls.

6.2 Where control procedures are deficient councils must take action to ensure that they operate effectively in order to safeguard public funds and to provide assurance regarding the accuracy and integrity of their financial records.

7. ACCOUNTING ISSUES

7.1 The new councils were given responsibility for preparing the final year's accounts of the former authorities. There were considerable delays in the completion of the 1995/96 accounts and audits for the former authorities. Consequently in many cases audited closing figures for the former authorities were not available when the 1996/97 accounts for the new authorities were being prepared. Negotiations were still continuing among some councils into 1996/97 and beyond as to how the closing balances of the former authorities should be allocated among the relevant successor authorities. There was therefore uncertainty about the accuracy of the opening balances included within some of the 1996/97 accounts. Of the 24 sets of accounts which were qualified, covering 34 individual matters, most references were to the uncertainty relating to the balances inherited from the former authorities.

7.2 Two items in particular featured in most auditors' reports. The first of these relates to a change in the method of calculating the cost of financing assets. Most authorities changed their method of debt repayment from equal annual instalments to the annuity method. Those authorities which switched to the annuity method were able to generate significant "savings" in 1996/97 and achieve a more favourable year end financial position than they otherwise would have done. This is because the annuity method reduces the level of repayments in the short to medium term but leads to higher repayments in later years.

7.3 The second matter relates to the new system for local authority capital accounting. This requires capital assets to be included on the balance sheet on the basis of valuation which reflects the type of asset and for capital charges to be made to the service revenue account at a level which represents the real cost of using the asset.

The balance sheet provisions came into effect on 31 March 1995 and the revenue implications applied from 1996/97.

7.4 The maintenance of an accurate register of fixed assets is a fundamental component of the system and forms the basis on which capital charges are calculated. Some councils experienced difficulties in maintaining up-to-date registers in 1996/97, mainly due to the quality of the information available from the outgoing councils or the failure by the new councils to incorporate assets inherited at reorganisation. Some councils need to ensure that their approach to asset recognition in the accounts and the calculation of depreciation charges accords more closely with practice required by the Accounting Code of Practice.

7.5 Several councils decided that it was unnecessary to charge depreciation. Some auditors expressed concerns about whether the level of maintenance of properties was sufficient to justify a policy of non-depreciation. To satisfy auditors councils need to maintain records which demonstrate that the condition of their assets has been maintained by regular repair.

8. INTERNAL AUDIT

8.1 Internal audit is an important tool by which management monitors its control procedures and is a key element of any effective internal control environment. External auditors undertake regular assessment of the work of internal audit. From this they can assess whether the internal control mechanisms are being adequately monitored from within the authority and the extent to which they can rely on the work of internal audit, thus facilitating the efficient deployment of both internal and external audit resources.

8.2 Many auditors reported deficiencies in the arrangements which the new councils had established for internal audit. The most recurring concerns related to the lack of resources available for internal audit. While councils' staff structures had generally made provision for adequately resourced internal audit units, in practice many internal audit departments were not fully staffed during 1996/97. In addition, during the year many internal audit staff spent a significant amount of time on non-audit related duties. This occurred, typically, where internal audit staff were seconded to cover staff shortages in the finance department or other departments of the council.

8.3 Auditors drew attention to the need for internal audit departments to prepare long term plans, setting out the areas to be reviewed, and to develop or have access to specialist skills in areas such as computer audit. Where audit plans had been drawn up, the range of work planned had not always been completed with the result that the external auditors were unable to place reliance on the work of internal audit.

8.4 In its Stewardship Report the Commission indicated that it regarded the adoption and implementation of audit committee principles as an important step in raising standards of corporate governance. The functions of an Audit Committee are:

- to review with management the adequacy of the internal control systems
- to review with management the adequacy of policies and practices to ensure compliance with relevant statutes, directions, guidance and policies
- to review with management compliance with relevant standards or codes of corporate governance
- to review with management the financial statements
- to ensure that the internal audit function is properly resourced and has appropriate standing within the council
- to review the activities of the internal audit function
- to manage all aspects of the council's relationships with the external auditors.

8.5 It is encouraging to note that, despite the poor performance of some internal audit sections in their first year, some councils had taken early action to incorporate audit committee principles within their overall management arrangements.

9. COMPUTER AUDIT

9.1 During the year most councils' computer systems were in a transitional stage with new systems being introduced. Audit work undertaken during the year embraced an overview of councils' arrangements for the provision of computer services and the appraisal of operational controls. The issues which featured most frequently in auditors' reports included the need:

- to develop an overall strategy for computer services which supports achievement of the corporate business objectives, together with individual IT strategies at departmental level
- for documented standards and procedures at all locations where IT facilities are available, including security
- to develop, document and test continuity / disaster recovery plans
- for service level agreements for the provision of central IT services to individual departments.

10. FOLLOWING THE PUBLIC POUND

10.1 In May 1996 COSLA and the Accounts Commission issued joint guidance to councils, setting out the practice which they should adopt when giving significant financial assistance to other bodies. Auditors are expected to review, on a regular basis, whether councils are observing the guidance in practice.

10.2 Work undertaken by auditors in 1996/97 identified the following areas where the guidance in the Code was not being fully observed:

- absence of formal arrangements covering, for example, applications for financial assistance or agreements where assistance has been granted
- failure to set conditions regarding the objectives to be achieved by the recipient body
- inadequate monitoring of performance of recipient organisations
- failure to obtain audited accounts in respect of recipient bodies
- absence of regular reports back to the council
- inadequate insurance cover for officers involved in external organisations.

10.3 The purpose of the Code is to ensure that there are adequate safeguards in place when external organisations receive financial assistance from public funds and for holding recipient organisations accountable for the proper use of the assistance granted. It is clear from auditors' reports that some councils need to take more effective action to ensure that the guidance laid down in the Code is complied with fully.

11. HOUSING AND COUNCIL TAX BENEFITS

11.1 During 1996/97 the Commission continued to promote the importance of sound arrangements for the administration of Housing and Council Tax Benefits and to encourage auditors to devote adequate resources to the review of these arrangements. This was in line with the drive by central government to reduce the level of fraudulent payments within the benefits system.

11.2 A high proportion of auditors' reports referred to inadequacies in many councils' arrangements for benefit administration and, in particular, for tackling fraud. The following specific matters were referred to:

- the absence of a formal policy for dealing with fraud
- no formal instructions or training for staff on how to detect or follow up fraud
- poor maintenance of benefit records
- the need to increase the level of checking
- inadequate fraud investigation procedures.

11.3 The impetus to improve the standard of benefit administration has been increased by the formation of the Benefit Fraud Inspectorate to undertake a programme of detailed inspections. The Commission's auditors work closely with the Inspectorate, with both organisations sharing information and findings from the separate work which they carry out.

11.4 There are clear expectations on councils to improve significantly the quality of benefit administration. Auditors will continue to monitor councils' performance on an annual basis to assess whether the necessary improvements are being achieved.

12. DIRECT LABOUR AND DIRECT SERVICE ORGANISATIONS

12.1 In many cases local government reorganisation brought together DLO/DSOs from different authorities. This required many councils to engage in a major exercise of rationalisation to harmonise conditions of service, working practices, management information systems, prices and other matters. Rationalisation was often undertaken at the same time as resources were being devoted to the preparation of tenders for contracts that were approaching termination.

12.2 Auditors' reports highlighted a range of weaknesses in the management of DLO/DSOs, including:

- no regular monitoring of the financial position
- unsatisfactory procedures for recharging work
- inadequate control over day works
- unacceptable bases for allocating central administration costs
- accrued expenditure not identified
- limited checking by client departments.

12.3 In many cases rationalisation resulted in a reduction in staffing and the incurrence of redundancy costs. As these are a charge to trading accounts they impacted on the financial performance of the DLO/DSOs concerned. In 1996/97 a number of DLO/DSOs did not achieve their financial performance targets and, in many cases, this was attributable solely to the impact of redundancy costs.

12.4 The one-off effects of rationalisation and redundancies meant that 1996/97 was an untypical year, from which it was difficult to draw general conclusions about underlying financial performance.

12.5 In 1997/98 a few councils incurred very substantial deficits. I prepared individual reports on two councils and an overview of the performance and management arrangements of all DLO/DSOs.

13. SPECIFIC ISSUES

In addition to issues which were common to a number of councils the following specific matters arose at individual councils and, in my opinion, warrant reference in this report.

13.1 Aberdeenshire Council

In September 1996 I submitted a report under section 102(2) of the Local Government (Scotland) Act 1973 highlighting weaknesses in the manner in which the former Gordon District Council had arrived at and implemented a decision to construct an archaeological visitor centre known as Archaeolink. I recommended certain action that Aberdeenshire Council, as the successor authority, should take in relation to the ongoing management of the centre.

In 1996/97 the Council gave financial assistance totalling £88,000 to meet the deficit arising from the running costs of the centre. In their report the auditors identified the action which the Council had taken to monitor the ongoing financial performance of the centre and the level of financial support provided by the Council. Under the improved arrangements the cost of any services provided by the Council to the Archaeolink Trust, which operates the centre, will be fully recharged to the Trust and shown clearly in the Council's accounts.

13.2 Dumfries and Galloway Council

In 1996/97 Dumfries and Galloway Council made financial contributions of £4.5 million and £8 million pounds to the Crichton Trust and the Crichton Endowment Trust respectively. The contributions were designed to provide funding for the development and maintenance of the Crichton site. This is a large area close to Dumfries that was previously owned and used by the Health Service. The Council considered that the site had excellent development potential and the funding arrangements were to facilitate that objective.

The auditor of the Council questioned whether the Council had legal powers for the contribution to the Endowment Trust. The Council sought counsel's opinion on the matter and was advised that it was unlikely that the Council had the necessary statutory powers.

In view of counsel's opinion, the Council sought to recover the contribution of £8 million from the Endowment Trust. The Trust has agreed in principle to the repayment of the contribution and is now engaged in discussions with the Council regarding the amount which should be repaid. This issue has been ongoing for some time and the auditor has been awaiting its resolution before concluding the 1996/97 audit. The manner in which it is resolved will determine whether I require to prepare a separate report on this matter.

13.3 East Dunbartonshire Council

The auditors of East Dunbartonshire Council were unable to complete the audit of the 1996/97 accounts until June 1999. The delay reflects the difficulties which the auditors faced in obtaining a final balanced set of accounts.

The first version of the accounts was received on 7 November 1997 but did not include a number of required disclosures, including notes to the accounts and opening balances. As a result of audit work a significant number of adjustments were identified; these were discussed with the authority on 1 May 1998. A revised version of the accounts, incorporating the necessary adjustments and disclosures was not received until 15 October 1998. This version required further amendment to comply with the Accounting Code of Practice and to adjust capital accounting balances. A final set of accounts, of an acceptable standard, was received on 19 March 1999.

Even allowing for the particular difficulties which arose in 1996/97 as a consequence of local government re-organisation, this is a wholly unacceptable time-scale for the production of accounts It is imperative that, in future, accounts are presented for audit by the new statutory date of 30 June in a complete, balanced and fully compliant form, supported by the necessary working papers and reconciliations.

East Dunbartonshire was one of the councils which was subject to inspection by the Benefit Fraud Inspectorate. The detailed report which followed the exercise highlighted a number of significant weaknesses, including a general lack of management control, no internal security checks, an absence of internal audit of benefit payments and inadequate procedures for the receipt and accounting for direct payments of rent arrears received from the Benefits Agency.

The inspection also revealed the absence of a clearly defined counter-fraud policy, no controls to measure the effectiveness or quality of the fraud investigation process and a failure to act on data to target fraudulent activity.

The Council must act quickly and positively to address all the findings arising from the inspection.

13.4 Fife Council

In March 1997 Fife Council placed an order for goods and services to the value of £60,000, excluding VAT, with a computer company. Payment was made following receipt of an invoice from the company but before any goods or services had been received.

An investigation by the internal audit department concluded that, at the time payment was made and for a considerable period thereafter, it was unclear what had been ordered and paid for. Approximately ten months after payment had been made and without any goods having been received by the Council the supplier went into liquidation.

Subsequently the Council received software licences which apparently formed part of the original order, at no extra cost. In his 1997/98 report the auditor indicated that the Council has still to recover the full value of the loss and that he is continuing to monitor the position to assess the eventual outcome.

This incident highlights the risk of making payments in advance. It should be a fundamental principle of all councils that payment is not released until the goods or services have been received.

Inverclyde Council

The audit of Inverclyde Council was not completed and reported on until 31 May 1999. This reflects the difficulties which the auditors had in obtaining an acceptable set of accounts supported by adequate subsidiary records.

The original accounts were presented for audit in September 1997 but were subject to extensive amendment over the succeeding two years to correct errors and incorrect accounting practice. During this period the auditors faced considerable difficulties in completing their audit work due to the poor quality of the supporting documentation, a lack of a transparent audit trail and an absence of bank reconciliations. These problems were due, in part, to the operation of two financial ledgers throughout the year and the difficulties in managing information flows from these systems.

The auditors expressed significant concerns about the standard of financial control which operated during the year. In addition to the areas already referred to these included:

- non-compliance with the Accounting Code of Practice
- weaknesses in processing and accounting for DLO/DSO information.
- aspects of housing and council tax benefit administration
- insufficient evidence to support fixed asset valuations.

The last issue resulted in the accounts being qualified. A further qualification arose because the surplus for the year in the consolidated revenue account was materially understated as a result of certain transactions being treated as movements in reserves instead of being reflected in the revenue account.

Overall the audit revealed a poor standard of financial administration and control requiring immediate and positive action by the Council. The comments in the auditors' 1997/98 report, receipt of which is imminent, will influence the nature of my follow up action in respect of this Council.

14. VALUE FOR MONEY

14.1 Introduction

The Accounts Commission has a statutory duty to carry out studies of value for money in the provision of services by audited bodies. During 1996/97, five topics were reviewed locally by auditors as part of the follow up of national studies:

- Council tax collection
- Emergency repairs to council houses
- Management of school property risks
- Management of road safety defects
- Trade refuse.

The first four of these studies were based on central development work carried out by the Commission's Local Government Studies Directorate. The work on trade refuse was based on an audit guide developed by District Audit for England and Wales. With the exception of trade refuse, the results of these studies are published separately. The main issues covered by each are set out below.

14.2 Council Tax Collection

By the end of 1996/97, the first year of the new councils, about 87% of the council tax (net of council tax benefit) due that year had been collected. Much of the council tax uncollected by the end of the financial year will be collected in subsequent years, but early collection improves cash flow and the amount ultimately collected.

Collection levels vary significantly among councils. Some of the difference in collection levels is due to social deprivation and other factors outwith the control of authorities, and some of it is due to the collection practices adopted by councils. In particular, there is scope in some councils to:

- improve the take up of council tax benefit
- bring forward the instalment dates to earlier in the month

- increase the take-up of direct debit as a method of paying council tax
- undertake regular checks of properties to ensure continued entitlement to discounts or exemptions
- improve IT systems, to increase the accuracy of records
- tighten the procedure for recovery of council tax debt.

The overview audit was undertaken in all councils. To date, auditors have submitted local reports to 18 authorities, in most cases containing action plans to improve collection levels. A national report, '*Council tax collection*', was published in February 1998.

As part of the 1998/99 audit, auditors will be reviewing the progress made by councils in implementing their action plans and the improvements achieved.

14.3 Emergency Repairs to Council Houses

There is a very wide variation among councils in the percentage of repairs to council dwellings that are classed as emergencies, from about 1% to 60%. Control of the level of emergency repairs is important, because they are more expensive than normal repairs. The Commission undertook a study in 1996, and then auditors reviewed 23 councils as part of the 1996/97 audit. The report of the findings and recommendations, '*Emergency repairs to council houses*', was published in May 1998.

The audits showed that a significant minority of jobs should not have been undertaken as emergencies. Some councils could save around 15% of their emergency repairs bill by, for example, ensuring that less urgent repairs are not treated as emergencies and introducing fixed prices for each type of repair rather than paying contractors at an hourly rate. In total, councils spent £33 million in 1996/97 on emergency repairs to council houses. Savings of up to £1.3 million across Scotland may be possible if councils reduce the levels of over-categorisation, and other savings may be made from using fixed prices for each type of repair.

14.4 School Property Risk Management

In January 1997, the Commission published its report on property risk management in schools, "*A Safer Place*". Schools suffer many types of property risk, but the most significant are crime-related, including fire-raising, vandalism and theft, costing education authorities £18 million a year. By investing £4 million a year in crime prevention packages in schools over a period of four years, councils could reduce their losses from property crime by £5 million a year. Following the report, a handbook was issued to all schools in Scotland giving guidance on best practice in implementing property risk management.

Local audits were undertaken in 17 councils. Generally, councils are taking steps to improve security in schools, making use of a specific grant for that purpose made available by the Government.

14.5 Road Safety Defects

In 1996, the Commission published a report, *A Costly Trip*, following its national review of authorities' management of road safety defects. The review found that as many as seven out of ten public liability claims against Scottish local authorities were claims for "tripping" and "pothole" accidents caused by footway and carriageway defects. Over a three-year period, these claims had amounted to £10 million.

Local follow-up audits were undertaken in 20 councils. These have resulted in auditors agreeing a plan of action to be taken by councils to improve their performance. Key areas for councils to improve include:

- adopting a systematic approach to inspecting roads for safety defects by:
- adopting a formal safety inspection policy
- inspecting specific risk areas more frequently
- providing training and issuing guidelines to inspectors
- setting appropriate target repair times, ensuring that repairs to dangerous defects are completed without undue delay
- identifying areas with the highest incidence of claims, and taking action to reduce the number of claims.

- making better use of management information by:
- making good use of IT for recording defects
- using a database to determine trends in claims
- informing service departments of outcomes of claims.

The work has enabled the Commission to produce a benchmark of council performance. More than one claim received a year per 1,000 population should be of concern to councils. In some councils the ratio is almost twice that.

14.6 Trade Refuse

Trade refuse is commercial waste from shops and businesses. Councils charge for collecting trade refuse, generating income worth over £14 million a year. Landfill tax was introduced on 1 October 1996. It is a charge levied on all waste that is disposed of at landfill sites. It will lead to an increase in the cost of trade refuse services.

The research for the audit guide was undertaken by District Audit in England and Wales, and the audit guide was then applied in Scotland. Of the 23 councils reviewed, only two operated a trading account for trade refuse. Consequently, most councils do not know whether their trade refuse service is operating at profit or a loss. On examination, it was found that most councils make a loss. Charges for trade refuse collection vary considerably among councils. Some councils are having to harmonise widely differing charges levied by the former district councils within their area. Illegal dumping of trade refuse is a problem for many councils.

15. MANAGEMENT ARRANGEMENTS OVERVIEW

15.1 In 1996/97, the Commission introduced a new approach to the audit of management arrangements in Scottish councils based on self assessment, action planning and continuous improvement. The management arrangements audit covered “strategy, planning and budgetary control” activity undertaken by councils at corporate level and within individual services.

15.2 The areas addressed by the audit were councils' arrangements for:

- setting direction
- strategic analysis
- implementing policy
- checking progress
- continuous improvement
- budgetary control.

15.3 The auditors' task was to review a council's self assessment of the arrangements currently in place and action plans for improvement, sample check evidence, and agree action plans to address key areas for improvement.

A review of a sample of audit returns found that in 1996/97:

- about a quarter of councils had already developed a sound management framework for corporate and service planning
- about a quarter required to make substantial progress in establishing and embedding basic elements of a sound management framework
- the remaining councils had some core processes and systems in place, but these required to be extended and integrated within the organisation.

All councils agreed action plans with their auditors to improve various aspects of their management arrangements. Progress in delivering these actions will be audited.

15.4 A more detailed review of the findings from the management arrangements audit and the Commission's recommendations for councils can be found in '*Planning for Success - a review of the audit of Management Arrangements in Scottish Councils in 1997*'.

16. CONCLUSION

16.1 The first year of the new system of local government was undoubtedly a difficult period for all new councils. The finance function, in common with most other services, faced major problems in simultaneously having to wind up the affairs of the former authorities and set up financial regimes for the new councils. Frequently the work load had to be undertaken with fewer and, in some cases, less experienced staff.

16.2 In my view, it is the joint responsibility of elected members, the chief executive and the director / head of finance of each council to ensure that high standards of corporate governance and financial stewardship are achieved. It is clear from the 1996/97 audit reports that more required to be done to improve standards of governance and stewardship in many councils. Many councils were unable to establish satisfactory accounting and financial control arrangements in their first year of operation. Accounts were produced which were not of an acceptable standard or were not adequately supported by subsidiary records, and there were failures to establish basic control procedures. One of the most common and most concerning features was the widespread absence of proper bank reconciliations. These are a fundamental control which provide a measure of assurance about the integrity of the financial records. In the absence of proper reconciliations there remains the possibility that differences, even if small in amount, may be masking errors or untoward transactions within the accounts.

16.3 In some cases the absence of adequate controls was exacerbated by an inadequate level of internal audit activity. While internal audit can never be a substitute for a satisfactory system of internal control it can partially compensate by undertaking a high level of testing. Where this does not happen an authority is at risk from error or fraud remaining undetected. It is essential that councils take early and effective remedial action to redress any weaknesses that still remain in their accounting and internal audit arrangements.

16.4 The work undertaken by auditors on the housing benefit system, together with the findings from inspections carried out by the Benefit Fraud Inspecorate, indicate that the standard of housing benefit administration is inadequate in some authorities. Councils must tackle this issue by effecting improvements in their benefits system and by ensuring that they are subjected to a level of examination by internal audit that provides a reasonable chance of detecting errors or frauds that have occurred.

16.5 This report provides an overview of the main issues which have arisen from the 1996/97 audits. Currently, the audits of 21 of the 32 councils for 1997/98 have been completed. It is my intention to produce an overview report on the 1997/98 financial year in early course.

ROBERT W BLACK
Controller of Audit
13 July 1999