



Agenda Item 4

Report to Members and the Controller of Audit on the 2021/22 Audit

Falkirk Council

Title: Report to Members and the Controller of Audit on the 2021/22 Audit

Meeting: Audit Committee

Date: 27 October 2022

Submitted By: Director of Transformation, Communities & Corporate Services

1. Purpose of Report

- 1.1 The purpose of this report is to present the outcome of the 2021/22 Annual Audit and to provide a summary of the key points arising from the Auditor's Annual Report.

2. Recommendations

2.1 The Committee is asked to:-

- (1) Note the Annual Audit Report for 2021/22.**
- (2) Note the action plan appended to the Annual Audit Report.**
- (3) Consider and recommend to Council that the Audited Annual Accounts of the Council to March 2022 are approved.**

3. Background

- 3.1 The Council's appointed auditors, Ernst & Young, are required to communicate matters relating to the audit of the Financial Statements (the Accounts) to those charged with governance of the organisation. The appropriate body to consider governance within Falkirk Council is the Audit Committee.
- 3.2 The Local Authority Accounts (Scotland) Regulations 2014 require the Council to submit annual accounts to our External Auditor no later than 30 June following the financial year to which the accounts relate. Following the audit process a local authority, or Committee of that authority must meet to consider the audited Annual Accounts and approve these accounts for signature.
- 3.2 In accordance with the Council's Standing Orders, the Audit Committee is asked to review the audited Annual Accounts and recommend approval to the Council.
- 3.4 Ernst & Young are in attendance at today's meeting and will present their report to the Audit Committee. Ernst & Young have also prepared an action plan which requires management responses. This forms part of their Annual Audit Report at Appendix D.

4. Considerations

4.1 Audit of Financial Statements

- 4.1.1 The audit process formally commenced at the beginning of July. The unaudited accounts were considered by the Audit Committee on the 22 August 2022.
- 4.1.2 Ernst & Young have now completed their audit of the financial statements and the Auditor's Certificate is free from qualification. Copies of the accounts will be sent to interested parties, posted on the Council's website and their availability advertised in the local press.
- 4.1.3 Since presenting the unaudited accounts to Audit Committee in August, there were two compensating adjustments that overstated the expenditure and income of both Children's and Social Work Adult Services. These have both been corrected and had no net effect on the Council's overall net position.
- 4.1.4 In addition, the net pension liability for the unaudited accounts was based on provisional figures provided by the Actuary. These have been updated to reflect the final Actuarial report. This has no impact on the Council's General Fund balances.

4.2 Wider scope – Approach to Best Value

- 4.2.1 The annual report notes that the Code of Audit Practice details four dimensions within the wider scope audit for the public sector in Scotland. These are financial management, financial sustainability, governance and transparency and value for money. These have been assessed by Ernst & Young.
- 4.2.2 Member's will also be aware that the Council was subject to a Best Value Assurance Review during 2021. In February 2022, the Council agreed a strategic Action Plan addressing the findings and recommendations. The auditors noted that progress has been made and a number of important steps have been taken. The Auditor does, however, highlight the need to assess the impact of the changes flowing from this. The Council will be subject to a follow up review in 2023.

Financial Sustainability

- 4.2.3 With regard to financial sustainability, the report notes the acute financial challenge and the need to find and deliver savings of £69m over the next four years and the risk and uncertainty outside the Council's control which could impact its ability to deliver services. The auditors note the establishment of the Financial Strategy Group as important and emphasize the need for elected Members to have oversight of progress on the delivery of savings, including transformational savings.

Financial Management

- 4.2.4 As in prior years the auditor's report notes the Council continues to demonstrate good financial control over the budget. Good progress was made

to address vacancies within internal audit and responsiveness to audit queries generally improved.

- 4.2.5 The reduced capacity of the Finance Team has been noted in previous years and the auditor notes that the Council has financial capacity below the level they expect from councils of a similar size. The outstanding assessment against the CIPFA Financial Management Code will be used to review the capacity of the Finance Team to meet its obligations. Going forward, there is also a need for the team to establish good working relationships with the new Auditors who will take on this role from later in October 2022.

Governance and Transparency

- 4.2.6 The auditor comments that the key features of good governance are in place. The report notes that given the change in the composition of the Council's Audit Committee that there is an opportunity to review arrangements against best practice. The report notes two incidents that have been disclosed to the Health and Safety Executive. The auditor also noted that while improvements have been made to whistle blowing arrangements, work to review such arrangements need to continue.

Value for Money

- 4.2.7 The report notes that the Council has reviewed its arrangements for performance monitoring, improvement and self-assessment as part of the Council's response to the Best Value Audit. It is noted that further work is needed to make performance information easily accessible and understandable. Service performance in comparison with other Council's was weaker in some areas but performed well in others, particularly in Education.

Other Matters

- 4.2.8 The report also draws attention to additional audit work beyond that usually expected, primarily relating to whistleblowing allegations and additional procedures in respect of infrastructure assets. A fee variation will be discussed to recognise the additional time spent.

5. Consultation

- 5.1 No consultation is required on this report. The approved accounts and auditor's report will be made available on the Council's website.

6. Implications

Financial

- 6.1 There are no direct financial implications as a result of the recommendations in this report.

Resources

- 6.2 There are no direct resource implications as a result of the recommendations in this report.

Legal

- 6.3 There are no legal implications as a result of the recommendations in this report.

Risk

- 6.4 There are no risks as a result of the recommendations in this report.

Equalities

- 6.5 There are no equality implications as a result of the recommendations in this report.

Sustainability/Environmental Impact

- 6.6 There are no sustainability/environmental implications as a result of the recommendations in this report.

7. Conclusions

- 7.1 The audit of the Council's annual accounts for 2021/22 will be formally concluded following the approval of the audited accounts. The action plan arising from the audit process has been prepared and will be monitored to ensure completion.

Director of Transformation, Communities & Corporate Services

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Date: 13 October 2022

Appendices

- Appendix 1 Ernst & Young's report – 2021/22 Annual audit report to Members and the Controller of Audit.
Appendix 2 Proposed Audit opinion and letter of representation by Ernst & Young.
Appendix 3 Annual Accounts 2021/22

List of Background Papers:

The following papers were relied on in the preparation of this report in terms of the Local Government (Scotland) Act 1973:

- None

Falkirk Council

**Annual Audit Report to Members
and the Controller of Audit - year
ended 31 March 2022**

October 2022

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About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Falkirk Council (the Council) for financial years 2016/17 to 2021/22. As a result of the impact of Covid-19 our appointment was extended by a further 12 months to include the financial year 2021/22. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice. This report is for the benefit of the Council and is made available to the Accounts Commission, the Controller of Audit and Audit Scotland. This report has not been designed to be of benefit to anyone except the recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

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If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Hywel Ball, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Executive Summary: Key Conclusions from our 2021/22 audit

[We have issued an unqualified audit opinion on the Council and Group 2021/22 financial statements.]

We continued to review and update our risk assessment throughout the audit, including the materiality level applied. During the year, a national issue emerged in relation to the valuation of infrastructure assets. As a result, this was treated as a significant risk. No changes were required to the level of materiality that we applied.

Financial Statements

[We have concluded our audit of the Council's financial statements for the year ended 31 March 2022.] Three adjustments have been made to the financial statements since the publication of the unaudited financial statements in June 2022. We identified a further 5 unadjusted differences that we are required to communicate in Appendix E. The draft financial statements and supporting working papers were provided on time and were of a good quality, although some of the adjustments identified during the audit should have been addressed by management during quality review processes. We worked with management to make a number of enhancements to the financial statements, in particular to ensure that they better reflect recent good practice guidance from Audit Scotland around the disclosures.

We concluded that the other information subject to audit, including the applicable parts of the Remuneration Report and the Annual Governance Statement were appropriate. We were satisfied that the Annual Governance Statement reflects the requirements of the *Delivering Good Governance Framework*, and changes to the presentation of the statement were an improvement on prior years.

Best Value Follow Up

In January 2022, the Accounts Commission published Falkirk Council's Best Value Assurance Report (BVAR). The report concluded that the Council had demonstrated improvement in performance in some key services but that overall the pace and depth of improvement since the previous Best Value audit report in 2018 had not been sufficient to achieve the level of transformational change needed to address future budget gaps.

Since the publication of the report, significant work has been undertaken to respond to the key messages. Local government elections mean that there have been changes in the political make up of the Council, and 15 new councillors were elected. Changes of this type offer an opportunity to reset and establish new ways of working, but the changing financial environment means that the budget gap facing the Council is now stark.

Over a number of years, we have noted that the Council has found it difficult to build the consensus needed to make unpalatable political decisions. As a result, budgets have been balanced using non-recurring measures and any easy budget options have now been exhausted. The Council has recently agreed to replace Budget Working Groups with a new cross-party forum, a Financial Strategy Group. The group will give elected members the opportunity to work together to find political solutions that best protect the Council's priorities and commitments.

Wider Scope

We summarise the conclusions we reached in response to our work on the wider scope dimensions below.

Financial Sustainability



The Council's Financial Strategy outlines the need to deliver savings of £69 million by 2027; a further increase in the budget gap to be bridged. In order to deliver a balanced budget, challenging decisions on service priorities and expenditure commitments will be required, along with careful evaluation of any new spending commitments.

The Council of the Future transformation programme is now expected to deliver £10 million of savings from Wave 3 of the project. The programme has been further rationalised to ensure it is more realistic. Planned changes to governance arrangements, including the establishment of the Financial Strategy Group, must allow elected members to continue to scrutinise the achievement of COTF savings.

Our assessment of red reflects the level of savings required over a short period of time, along with the degree of risk and uncertainty outside the Council's control which could impact its ability to deliver services.

Financial Management



The Council continues to demonstrate good financial management arrangements and control of the in-year budget, including understanding of the ongoing impact of Covid-19 and other financial pressures. The Council initially budgeted to use £2 million of reserves in 2021/22, but this was not required as a result of underspends against budget, and the use of financial flexibilities.

The Council reports that it delivered £4.86 million (96%) of planned savings in 2021/22. Savings in 2022/23 will be more challenging as a result of inflationary and service demand pressures. The Council has taken important steps towards the development of a realistic and affordable capital programme. We do, however, note that the Council has highlighted, like many in the sector, that key priorities such as the ambition to achieve net zero carbon emissions by 2030, may be unaffordable in the short to medium term.

Governance & Transparency



The key features of good governance remain in place at the Council.

The composition of the Council's Audit Committee has significantly changed and there is an opportunity to review arrangements against revised best practice, ensuring that the scrutiny needs of the Council are met.

The Council has disclosed two accidents which have been investigated by the Health and Safety Executive (HSE). The HSE is considering further action and an action plan is in place to address the weaknesses identified. We have also drawn attention to a series of whistleblowing allegations over the last three years. While improvements have been made to the whistleblowing reporting arrangements to Audit Committee, we consider that underlying cultural issues have not been fully addressed.

Value for Money



The Council has reviewed its arrangements for performance monitoring, improvement and self-assessment as part of its response to the Best Value Assurance Report. Its analysis of the 2020/21 Local Government Benchmarking Framework notes that performance declined against prior year but remains higher than national averages for 50% of the indicators. The Falkirk Performs website continues to be developed but further work is needed to make performance information easily accessible and understandable.

While we note that performance reporting remains a developing area, reports are generally heavily narrative based, resulting in performance being harder to readily interpret.

Work is required to finalise future success measures targets to report performance against the Council Plan.

Best Value Strategic Action Plan

In February 2022, the Council agreed a Strategic Action Plan to respond to the recommendations within the BVAR. A number of important steps have been taken to respond to the challenges outlined in the report, including:

- ▶ A comprehensive induction programme for elected members, complemented by external support on equalities and on collaborative leadership;
- ▶ The development of the new Council Plan, based on elected member engagement and drawing on the views of communities. This is supported by the critical Financial Strategy and Workforce Plan;
- ▶ Review of the Council of the Future Transformation programme; and
- ▶ A review of the affordability of the current capital programme.

The Accounts Commission has signalled that the Council will be visited early in the next programme of Best Value reviews, likely to be in 2023. While the Council has made good progress against the planned actions, it is too early to assess whether elected members and officers will work together effectively enough to meet the scale of the financial challenge. We understand that a further update report will be considered by the Executive in December 2022 which will report on the Council's assessment of impact to date. This will remain a key area of focus for the Council's incoming external auditor, and the future Best Value audit.



Introduction

As a result of the impact of Covid-19, Audit Scotland and the Accounts Commission agreed to extend our appointment as external auditor of the Council to 2021/22.

Purpose of this report

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as the external auditor of Falkirk Council ("the Council"). Our appointment term was extended by a further 12 months, to financial year 2021/22. We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Report is intended to summarise the key findings and conclusions from our audit work. It is addressed to both members of the Council and the Controller of Audit, and presented to those charged with governance. This report is provided to Audit Scotland and will be published on their website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the Council. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our Annual Audit Plan.

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, our observations around where the Council employs best practice and where practices can be improved. We use these insights to form our audit recommendations to support the Council in improving its practices around financial management and control, as well as around key aspects of the wider scope dimensions of audit. Such areas we have identified are highlighted throughout this report together with our judgements and conclusions regarding arrangements, and where relevant recommendations and actions agreed with management. We also report on the progress made by management in implementing previously agreed recommendations.

Our independence

We confirm that we have undertaken client and engagement continuance procedures, which include our assessment of our continuing independence to act as external auditor. Further information is available in Appendix B.

We remain satisfied that the values reported to you in our Annual Audit Plan for planning materiality, performance materiality and our audit threshold for reporting differences remain appropriate.

Scope and Responsibilities

The Code sets out the responsibilities of both the Council and the auditor (summarised in Appendix A). We outlined these in our Annual Audit Plan, which was presented to the Council's Audit Committee in March 2022.

Our review and reassessment of materiality

Our Annual Audit Plan explained that our audit procedures would be performed using a materiality of £12.2 million. We considered whether any change to our materiality was required, including factors such as the continuing response to the pandemic and the Council's 2021/22 financial performance. We remained satisfied that the materiality values reported within our Annual Audit Plan were appropriate.

Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations. Factors which we consider include the perspectives and expectations of users of the financial statements as well as our risk assessment as to the likelihood of material misstatements arising in the financial statements.

Overall Materiality	Tolerable Error	Nominal amount
£12.2 million	£9.1 million	£250,000
2% of the Council's net expenditure	Materiality at an individual account level	Level that we will report to committee

As outlined in our Annual Audit Plan, based on considerations around the expectations of financial statement users and qualitative factors, we apply lower materiality levels to the audit of the Remuneration Report and Related Party Transactions.

Financial statement audit

We are responsible for conducting an audit of the Council's financial statements. We provide an opinion as to:

- ▶ whether they give a true and fair view of the financial position of the Group and Council as at 31 March 2022 and its expenditure and income for the year then ended; and
- ▶ whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2021/22 Code of Practice on Local Authority Accounting in the United Kingdom.

We also review and report on the consistency of the other information prepared and published along with the financial statements. Our findings are summarised in Section 2 of this report.

Wider Scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider scope public audit:

- ▶ Financial management;
- ▶ Financial sustainability;
- ▶ Governance and transparency; and
- ▶ Value for money.

Our findings are summarised in Section 3 of this report.

Best Value

Our wider scope audit work, and the judgements and conclusions reached in these areas, contribute to our overall assessment and assurance on the Council's achievement of Best Value. We outline our findings and assessment for 2021/22 on page 41.

Going Concern

In accordance with the CIPFA Code of Practice on Local Authority Accounting in the UK, the Council prepares its financial statements on a going concern basis unless informed by the Scottish Government of the intention for dissolution without transfer of services or function to another entity.

Under a revised auditing standard, ISA 570, we are required to undertake greater challenge of management's assessment of going concern, including testing of the adequacy of the supporting evidence we obtained. The Council has concluded that there are no material uncertainties around its going concern status, however it has continued to include enhanced disclosures around its future financial position in the financial statements to reflect the impact of Covid-19 and inflationary pressures. We have no matters to report in respect of our work around going concern or the conclusions reached by the Council.



Financial Statements audit

Introduction

The annual financial statements provide the Council with an opportunity to demonstrate accountability for the resources that it has the power to direct, and report on its overall performance in the application of those resources during the year.

This section of our report summarises the audit work undertaken to support our audit opinion, including our conclusions in response to the significant and other risks identified in our Annual Audit Plan.

The plan highlighted two areas that we identified as a significant risk of material misstatement or fraud risk:

- ▶ the risk of fraud in revenue and expenditure recognition (significant risk); and
- ▶ misstatements due to fraud or error (fraud risk).

Compliance with Regulation

The draft financial statements were submitted for audit in line with planned timescales. The inspection notice was published in accordance with requirements.

The Local Authority Accounts (Scotland) Regulations 2014 set out the statutory requirements on the Council to prepare financial statements, ensure their availability for public inspection and consideration by the Council or a committee with an audit or governance remit. The Council complied with the regulations and the normal timescale concerning preparation, publication and approval of its annual financial statements. We received the unaudited financial statements by 30 June 2022.

The inspection notice was published by the Council in line with the requirements of the Regulations. No objections were received in relation to the financial statements.

Preparation of the Financial Statements

The unaudited financial statements prepared by management were to a generally good standard and were materially compliant with the Code and required disclosures. As part of the audit process, we worked with management and the finance team to make amendments and enhancements to the presentation. Our focus included consideration of the appropriateness of the disclosures related to the ongoing impact of Covid-19 and recovery activities, including in the management commentary, governance statement and financial statements notes.

Recommendation 1: As part of the preparation process to develop the draft financial statements, the Council should develop a quality assurance process. This should include consideration of recent good practice guidance in relation to the management commentary and key financial disclosures.

This year we worked with management to consider guidance from Audit Scotland issued to local government bodies, following a review of the related parties disclosed within the 2020/21 financial statements of 30 Scottish councils. The disclosures of related parties were chosen for a good practice review because of potential impact of the relationships in understanding the financial statements, along with indications that the quality of disclosures were variable. Following our review and discussions with management, a number of enhancements were made to further align them with identified areas of good practice.

Group financial statements

The Council has identified and accounted for the following interests in other entities within its group financial statements:

- ▶ Falkirk Community Trust;
- ▶ Falkirk Community Stadium Limited;
- ▶ Central Scotland Valuation Joint Board; and
- ▶ Falkirk Integration Joint Board.

No matters were identified as a result of our review of the group consolidation arrangements within the financial statements. Falkirk Integration Joint Board (IJB) is the only entity in scope for our group audit arrangements. All required audit work was provided by the IJB audit team to the Council audit team in line with timeframes agreed and with no exceptions or reportable matters noted.

[Audit Status]

Our audit work is substantially complete with the following areas of work ongoing:

- ▶ *The conclusion of audit procedures in response to a whistleblowing allegation*
- ▶ *Finalisation of the Manager and Partner review; and*
- ▶ *Subsequent events procedures.]*

Audit Outcomes

We identified 7 audit differences arising from the audit, which have been summarised in the relevant sections of this report. Three have been adjusted by management in the finalised financial statements and four remain unadjusted on the grounds of materiality. Our overall audit opinion is summarised on the following page.