

The City of Edinburgh Council

Statement on the system of internal financial control

1. This statement is provided in respect of the internal financial controls operated by The City of Edinburgh Council. As the Council's designated section 95 officer as defined under the provisions of the Local Government (Scotland) Act 1973, I acknowledge my responsibility for ensuring that an appropriate system of internal financial control is in place and its on-going effectiveness regularly reviewed.
2. The system of control can provide reasonable, but not absolute, assurance that material control weaknesses or irregularities do not exist, and that there is no unacceptable risk of material error, loss, fraud or breach of legislation. Consequently, the Council continually seeks to improve the effectiveness of its systems of internal financial control so that irregularities are either prevented or detected within an acceptable period of time. Tracking of agreed internal audit actions forms a standing item on Corporate Leadership Team (CLT) agendas, with progress in implementation also regularly reported to the Governance, Risk and Best Value Committee. Progress in implementation of recommendations resulting from the external audit process is likewise reported to elected members.
3. In view of successive years' staffing reductions and various resulting changes in responsibilities, previous self-attestation exercises undertaken have been helpful in assessing the extent to which improvements have been embedded within service areas, highlighting a need for further action in some areas to implement and sustain the required controls. This exercise has subsequently been complemented, within the Corporate Services Directorate (where the majority of finance-related controls lie), by quarterly Risk Committee meetings and discussion at the Corporate Services Management Team at which progress in implementation and embedding of agreed actions is also considered.

Independent assessments of the effectiveness of the system of internal financial control

4. The effectiveness of the Council's internal financial control framework as a whole is subject to annual review by its external auditors, with the principal findings of the most recent annual assessment reported to the Governance, Risk and Best Value Committee in October 2023 (as part of the Council's Annual Audit). This assessment did not result in the identification of any significant weaknesses in these systems, albeit scope for improvement in the Council's payroll processes and controls, as well as acknowledged data quality issues within the SWIFT system that will be addressed as part of the system's replacement, were highlighted.
5. As with other systems across the Council, some aspects of the financial control framework have had to be adapted to a continuing home-working environment but with the emphasis consistently being on obtaining assurance in a different way rather than compromising or relaxing existing controls. Specific contingency plans had previously been developed in areas where service continuity is most crucial, including Financial Systems, Procurement, Treasury Management, Council Tax collection,

Benefits Processing, Payroll and Supplier Payments. These plans have worked effectively following enforced and continuing offsite working and performance against a range of key targets in these areas has been maintained.

6. There remain, nonetheless, inherent risks within the Council's activities. Unsuccessful attempts to defraud the Council through a fictitious change of supplier details were made in December 2022, leading to updates in current procedures and refresher training being provided. While no subsequent attempts have been detected, suppliers continue to notify the Council of on-going fraud attempts in the market, reinforcing the importance of staff vigilance, including regular completion of cyber training.

Risks included within Council risk register

7. A number of specific finance- and procurement-related risks linked to the COVID-19 emergency (and corresponding mitigating actions) were identified for inclusion in the Council Incident Management Team (CIMT) Risk Management Plan and actively monitored during 2021/22.
8. While these COVID-specific risks have lessened somewhat, the Financial and Budget Management risk within the Council's Risk Report remains rated as high and outside the Council's current moderate risk appetite. This is mainly due to the cumulative impact of exceptional inflationary and other demand-led pressures alongside reduced resources and limited options identified to deliver recurring savings. The Council also bears a share of the substantial budget gap within the Edinburgh Integration Joint Board (EIJB), having required to provide an additional £19m of support in 2023/24 to achieve overall financial balance, with a further £13m uplift reflected in the Council's "offer" in 2024/25. The adequacy of this latter provision will depend in particular upon delivery of the savings comprising the EIJB's Medium-Term Financial Strategy (MTFS) and effective in-year management of purchasing-led growth.
9. In light of these risks, the Council is developing a Medium-term Financial Plan (MFTP), albeit identification of the specific savings required to bridge future years' gaps remain at a comparatively early stage. Development of tactical savings sufficient to address the immediate 2025/26 gap and a longer-term robust and sustainable programme of change to meet subsequent years' requirements will therefore be a key priority in the coming months, with a progress update being presented to the Finance and Resources Committee on 25 June 2024.

Implementation of Internal Audit recommendations

10. The Finance and Procurement Division has also taken forward, or embedded, a number of specific audit actions during the year. These include those related to improved contract handover and on-going management arrangements for higher-risk contracts, alongside an associated review of Contract Standing Orders where a recent internal audit resulted in an assessment of only limited assurance. Internal audits undertaken in 2022/23 and 2023/24 also resulted in medium- to lower-risk recommendations around (i) expanding and fully updating guidance on accounting for VAT (particularly on supplies made by the Council), (ii) further improving financial systems training and (iii) obtaining improved oversight and consistency across a range of financial models, including

introducing a half-yearly, risk-based peer review. Finance colleagues are also working closely with relevant colleagues elsewhere within Corporate Services in continuing to implement the recommendations of a recent audit in the area of Payment Card Industry (PCI) data security and purchase cards, linked to a wider review of cross-Council arrangements concerning awareness of Fraud and Serious Organised Crime.

Internal audit review of capital, HRA and revenue budget-setting processes

11. A review of the Council's capital budget-setting and management processes undertaken in early 2022 concluded that current arrangements were effective. A report on the procedures and processes for administration of the Transfer of the Management of Development Funding (TMDF) Grants also found these to be effective. More recently, an internal audit examining procedures for Housing Revenue Account budget-setting and monitoring noted a number of positive aspects. In January 2023, the Council's preparations for implementation of the IFRS16 leasing standard (the first such authority in Scotland) were also favourably assessed.
12. The key findings and recommendations arising from a review of the Council's 2023/24 revenue budget-setting process were reported to the Finance and Resources Committee of 20 June 2023 and Finance staff have been working with relevant colleagues in taking forward relevant improvement actions, a number of which were implemented as part of the 2024/25 budget development process. Following planned consideration by the Finance and Resources Committee in June 2024, any further actions arising from the 2024/25 lessons learned review will be implemented with relevant colleagues across the Council.
13. Progress in implementing internal audit actions is regularly considered by the Finance Management Team. As of the time of writing, there are no Finance-led actions where relevant work is not underway, with arrangements to track progress on a regular basis also in place.

Role of Internal Audit

14. The Internal Audit section operates in accordance with the Chartered Institute of Public Finance and Accountancy's United Kingdom Public Sector Internal Audit Standards (PSIAS). The Section undertakes an annual programme based on an agreed audit strategy. The plan is based on formal assessments of risk and audit needs which are reviewed regularly to reflect evolving risks and changes within the Council. During 2023/24, the section reported to the Head of Legal and Assurance. It also has, however, unfettered access to the Chief Executive, Executive Directors, Service Directors (including the Service Director: Finance and Procurement) and elected members of the Council when required.
15. The Head of Internal Audit will present an annual audit opinion on the adequacy and effectiveness of the system of internal control (including financial controls) to the Governance, Risk and Best Value Committee in September 2024. Based on the equivalent 2022/23 opinion, in-year progress reports on audit action implementation and internal audits newly undertaken, this is anticipated to consolidate recent improvements, albeit with further actions still required. The required control

improvements implicit in this opinion will be examined and any corresponding necessary actions as they relate to financial systems implemented as a matter of urgency.

Elements of system of internal financial control

16. The existing system of internal financial control is based on a framework of regular management information, financial rules and regulations, administrative procedures (including segregation of duties), management supervision and a scheme of delegation and accountability. This system of control has been modified, where appropriate, to take account of the impacts of continuing homeworking, although as noted above this has been with a view to obtaining equivalent assurance in a modified way. The system is maintained and developed by Council management and includes:

- **comprehensive budgeting systems;**
- **preparation and regular review of periodic reports that measure actual financial performance against budgeted net expenditure.** Given the unprecedented nature and scale of the financial challenges facing the Council during the pandemic, the frequency of reporting to the Corporate Leadership Team and elected members (through the Leadership and Advisory Panel, Policy and Sustainability Committee and Finance and Resources Committee) was greatly increased, with a focus not only on the immediate in-year position but estimated implications for the budget framework in future years. This reporting frequency was relaxed somewhat in 2022/23 and further in 2023/24, albeit still at an enhanced level relative to pre-COVID periods. A structured programme of at-least quarterly member consideration is in place, with parallel scrutiny by the Governance, Risk and Best Value Committee and an ability for officers to bring forward material or urgent matters for consideration outside these timescales. These arrangements have been assessed to be effective as part of external audit review;
- **agreement of targets against which financial and operational performance can be assessed.** Key amongst these financial targets is the achievement of a balanced Council-wide revenue outturn. Thanks to savings in corporate budgets, a provisional in-year underspend of some £2m was achieved in 2023/24, despite a need to provide over £19m of additional in-year support to the Edinburgh Integration Joint Board (£14m of which related to application of the previous year's underspend). Although in-year savings delivery in 2023/24 reduced to 84%, this reflected an increased reliance on service-based savings relative to recent years. Going forward, however, further actions are required to manage pressures and savings requirements within frontline services' allocated budgets and additional actions supporting this objective are therefore being considered;
- **clearly defined capital and other expenditure guidelines** communicated to services and set out in the Finance Rules which were refreshed in May 2023. The Financial Regulations were also reviewed and minor amendments to their content made in October 2023;
- **a five-year revenue budget framework and ten-year capital strategy** approved by Council in February 2024. The Council's Best Value Assurance Review encouraged the Council, once the recurring impacts of the pandemic became clearer, to continue to look at opportunities to adopt medium- to longer-term financial planning. To this end, work has continued during the year to develop the basis of a Medium-Term Financial Plan (MTFP),

with [a draft strategy](#) presented to the Finance and Resources Committee in February 2024 and a further update to be reported in June.

The draft strategy includes a number of change themes (organisational efficiency, service design and external spend, delivery optimisation and prevention and partnership working) and accompanying values and principles that will underpin the Council's routemap to financial sustainability over the medium to long term. Details of a number of updated assumptions and tactical proposals for 2025/26 will be presented to members in June, with work continuing over the summer to develop further options to bridge the remaining projected funding gap whilst also seeking to provide a degree of resilience against potential further savings requirements resulting from changes in key assumptions or risk factors.

- **formal project management disciplines** as supported and promoted through the Strategy and Communications section, including senior Finance representation on all major project boards and assurance review panels; and
- **formal governance arrangements operated within both subsidiary and associated companies**, complemented by a strengthened Council observer role. Service Level Agreements are also in place for finance-related services provided to a range of external bodies. In recognising the scale of the pandemic's operational and financial impacts on their activities, monthly meetings took place throughout much of the period between 2020 and 2022. While this frequency has subsequently lessened, regular update meetings, particularly with Edinburgh Leisure, continued to take place during 2023/24.

17. My review of the effectiveness of the internal financial control system is informed by:

- **assurance certificates** on internal control received from all Executive Directors of the Council, service areas and relevant service heads;
- **regular senior management-level consideration of progress in implementing internal audit recommendations**, including self-attestation of previous actions where relevant;
- **governance arrangements in place for subsidiary and associated companies** and an on-going assessment of the effectiveness of these arrangements;
- the **work of managers** within the Council;
- the work of **Internal Audit**; and
- **external audit reports**, in particular the independent annual report on the Council's financial statements and internal control framework.

18. The Council's financial management arrangements conform with the governance requirements of the CIPFA Statement on the Role of the Chief Financial Officer (2014) as set out in the Application Note to Delivering Good Governance in Local Government Framework, an opinion confirmed as part of recent external audit scrutiny. Having reviewed the framework, it is therefore my opinion that, as in 2022/23, **although a degree of assurance can be placed upon the adequacy and effectiveness of the Group's systems of internal financial control, further improvements are still required. I would highlight, in particular, the need for (i) some embedding of actions taken in response to previous audit recommendations and (ii) enhanced managerial accountability for financial performance, including full management of pressures, and the active identification of required savings options within service areas, to secure financial sustainability going forward.**

19. I have overseen the improvements put in place in response to Finance-specific recommendations made by internal and external audit work during the year, with a number of actions additionally currently in progress. This said, the extent of change and reduction in overall resources in recent years has reinforced the importance of robust, documented and well-understood procedures for key system controls and, in light of the follow-up audits undertaken by both internal and external audit, a priority continues to be to consolidate these improvements, identify any further required actions and gain necessary assurance by regularly assessing their effectiveness. These arrangements have been thoroughly tested both initially during the COVID pandemic and subsequently amidst continuing home-working and, across the piece, have performed well although there is always room for improvement.

CIPFA Financial Management Code

20. 2023/24 marks the third year of implementation of the requirements of the CIPFA Financial Management (FM) Code. The Code is designed to support good practice and assist councils in demonstrating their financial sustainability and resilience by setting out expected standards of financial management.

A focus has been maintained to embed improvements introduced through recent years' budget processes including:

- maintaining an increased level of unallocated general reserve;
- incorporating explicit revenue budget provision, where practicable, for underlying service pressures including temporary accommodation for homeless households and wider demographic change affecting non-IJB services;
- continuing to reflect the ongoing impacts of the pandemic, particularly for losses of income; and
- earlier publication of the schedule of proposed fees and charges for member consideration.

21. Improvements introduced in 2024/25 or to be introduced for the 2025/26 budget processes include the following:

- development of enhanced scenario planning and sensitivity analysis to illustrate the impact of changes in key planning assumptions and the need to plan for these variations;
- introduction of monthly member briefings, alongside establishment of a cross-party working group to oversee the development of the MTFP; and
- clarification of the process for public engagement on options developed, with a more explicit link and consistency across resource allocation decisions, business plan priorities and views expressed by residents.

22. Further initiatives completed or underway to support my assessment and strengthen financial management arrangements including:
- positive outcomes from Internal Audit reviews of financial management arrangements for both the Council's Capital Investment Programme and Housing Revenue Account;
 - updated [Financial Management guidance](#) being issued to budget managers;
 - approval of business cases and subsequent recruitment of professional accounting staff to recognise additional workload, risk and complexity relating to the Council's Capital Investment Programme and areas of the revenue budget including Housing, Refugee Support and Homelessness. Adequate resourcing of the Finance function will be a prerequisite for continued compliance with the requirements of the FM Code going forward.
23. These steps build on a number of aspects already in place that are conducive to enhancing the Council's longer-term financial sustainability including (i) regular reviews, reported to both CLT and elected members, of revenue and capital budget planning assumptions and (ii) the development of updated, detailed and consistently applied guidance for Finance staff used to assess savings implementation plans and mitigation of service budget pressures. A Financial Management customer survey based on the CIPFA FM Code was also undertaken in 2023 and informed a number of improvement actions.
24. While the above position reflects a number of positive aspects, I have continued to impress upon all elected members and CLT the need for additional savings proposals to be brought forward if the Council's financial sustainability is to be maintained. In my role as Section 95 Officer, I am considering a range of means to reinforce their respective responsibilities in these areas. Given the extent of the financial challenge, both officers and members will need to make increasingly difficult choices about the Council's priorities, including considering service reductions, across all service areas to maintain expenditure in line with available income.
25. In addition to the Council's own activities, I have considered the immediate and potential on-going impacts of the pandemic on major projects within the city, including the Tram Extension and Edinburgh International and Conference Centre (EICC) Hotel project. There has, and continues to be, a need to revisit relevant business cases in light of these significant changes in the external environment and I will therefore keep all under active review in the coming months.
26. Consideration of the FM Code has also highlighted a number of areas where I assess further actions are potentially required going forward, including a need, in some cases, for more systematic options appraisal to be undertaken. In addition, improvements could be made to the effectiveness of current service arrangements in demonstrating value for money, including their contribution to broader Council objectives. Relevant actions will continue to be taken forward with CLT colleagues.

Richard Lloyd-Bithell

Service Director: Finance and Procurement

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