

REPORT TO: Audit and Governance Committee

MEETING DATE: 20 May 2014

BY: Depute Chief Executive - Resources & People Services

SUBJECT: Internal Audit Report – Trading Operations

1 PURPOSE

- 1.1 To inform the Audit and Governance Committee of the recently issued audit report on Trading Operations.

2 RECOMMENDATION

- 2.1 That the Audit and Governance Committee note the contents of the Executive Summary and Action Plan for Trading Operations.

3 BACKGROUND

- 3.1 A review of Trading Operations was undertaken as part of the audit plan for 2013/14.
- 3.2 The main objective of the audit was to ensure that the Council's Trading Operations comply with statutory requirements.
- 3.3 The main findings from our audit work are outlined in the attached report.

4 POLICY IMPLICATIONS

- 4.1 None

5 EQUALITIES IMPACT ASSESSMENT

- 5.1 This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.

6 RESOURCE IMPLICATIONS

6.1 Financial - None

6.2 Personnel - None

6.3 Other - None

7 BACKGROUND PAPERS

7.1 None

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EAST LoTHIAN COUNCIL – INTERNAL AUDIT TRADING OPERATIONS

1. EXECUTIVE SUMMARY

1.1 Introduction

As part of the Audit Plan for 2013/14 a review was undertaken of the Council's Trading Operations. A summary of our main findings is outlined below.

1.2 Key Findings

- 1.2.1 The Local Government in Scotland Act 2003 brought a formal end to Compulsory Competitive Tendering (CCT) ending the prescriptive regime which had been in place since 1980. The 2003 Act sets out the statutory duty of Best Value, the requirement for Local Authorities to maintain Statutory Trading Accounts for Significant Trading Operations (STOs) and the requirement for STOs to break even over a three year rolling period.
- 1.2.2 The determination of trading operations is a matter for individual Councils and each Council is expected to structure the delivery of its services in order to achieve Best Value.
- 1.2.3 We note that the status of the Council's STOs was last reviewed in August 2012. The Council had five STOs up until 2011/12 – Property Maintenance, Road Services, Facilities Services, Older Peoples Care Homes Service and the Domiciliary Care Service. The report to Council of 28 August 2012 recommended that Council approve the cessation of the Older Peoples Care Homes Service and the Domiciliary Care Service as STOs.
- 1.2.4 East Lothian Council currently operates three STOs: Property Maintenance, Road Services and Facilities Services (which includes Catering, Janitorial and Building Cleaning Services) and maintains Trading Accounts for each of the STOs. For the three years ended 31 March 2013 each of the Council's STOs had met the statutory financial target of breaking even.
- 1.2.5 The Chartered Institute of Public Finance and Accountancy (CIPFA) and Local Authority (Scotland) Accounts Advisory Committee (LASAAC) provide guidance to Councils in respect of determining the appropriate identification and treatment of STOs. The guidance states that the determination of trading operations is a matter for individual Councils but that it should be based on consideration of whether a service meets both of the following criteria:
- the service is provided in a competitive environment, i.e. service users have discretion to procure services from an alternative provider; and
 - the service is provided on a basis other than a straightforward recharge of costs, i.e. users take the service on the basis of quoted lump sums, fixed periodical charges, or rates, or a combination of these.

- 1.2.6 In addition to the fundamental tests of competitive environment and charging, the guidance emphasises the importance of applying a test of significance based on financial and non-financial criteria. Only trading operations which are regarded as significant will need to be classed as STOs.
- 1.2.7 Our review has highlighted that in 2013/14 the vast majority of income generated by each of the Council's STOs was from the provision of services to internal clients within the Council. Income generated from external clients was not significant.
- 1.2.8 We reviewed the charging arrangements within all three services currently operating as STOs and we note that:
- for Property Maintenance charging is based on a Schedule of Rates;
 - for Road Services charging is based on an hourly labour charge out rate and agreed mark-up on costs for materials, hired plant and sub-contractors;
 - for Facilities Services a number of charging methods are used including historical contract charges/contract payments and the recharging of costs.
- 1.2.9 We note that the original guidance issued by CIPFA/LASAAC has been modified and that revised guidance was approved in June 2013. The revised guidance states that identification of STOs should focus only on those services or activities which are external to the local authority and which are not statutory in nature. Externally provided services should be separated out and any cross-subsidisation identified.
- 1.2.10 The revised CIPFA/LASAAC guidance narrows down the services which may be classified as STOs – internal services may still be accounted for as trading operations, but they may not be relevant trading operations for the purposes of the STO review.
- 1.2.11 We note that the Council may choose to demonstrate Best Value by continuing to operate Trading Accounts, however this can be achieved without the services operating as STOs or being subject to the statutory requirement to break even over a cumulative three year period.

1.3 Summary

In view of the revised CIPFA/LASAAC guidance issued in June 2013, the Council now has the opportunity to undertake a review of all its services to determine which services (if any) require to be categorised as STOs.

Our review has identified one recommendation which is included in the attached action plan.

Mala Garden
Internal Audit Manager

May 2014

ACTION PLAN

PARA REF	RECOMMENDATION	GRADE	RESPONSIBLE OFFICER	AGREED ACTION	RISK ACCEPTED/ MANAGED	AGREED DATE OF COMPLETION
1.4	Management should undertake a review of the Council's Significant Trading Operations and ensure compliance with the CIPFA/LASAAC Guidance.	Medium	Head of Council Resources/Service Manager – Business Finance	Agreed		September 2014

Grading of Recommendations

In order to assist Management in using our reports, we categorise our recommendations according to their level of priority as follows:

Level	Definition
High	Recommendations which are fundamental to the system and upon which Management should take immediate action.
Medium	Recommendations which will improve the efficiency and effectiveness of the existing controls.
Low	Recommendations concerning minor issues that are not critical, but which may prevent attainment of best practice and/or operational efficiency.