Item: 3

Monitoring and Audit Committee: 5 February 2026.

Audit Report to those charged with Governance.

Report by Director of Enterprise and Resources.

ORKNEY ISLANDS COUNCIL

1. Overview

1.1. On 25 September 2025, the Chair advised that, as Members had only received the Audit Report to those charged with Governance the previous day, the status of which was incomplete, that the Monitoring and Audit Committee could not scrutinise the report.

1.2. Following assurance from KPMG that the completed Annual Audit Report would be submitted to an additional meeting of the Monitoring and Audit Committee to be held prior to 31 October 2025, the Committee thereafter noted the draft audit report, the draft Annual Audit Report to the Council and the Auditor General for Scotland and Orkney Island's Council's Letter of Representation to KPMG in connection with its audit of the financial statements of Orkney Islands Council for the year ended 31 March 2025.

1.3. KPMG, the Council's external auditors, have concluded their audit of the Orkney Islands Council Annual Accounts for the year ended 31 March 2025.

1.4. KPMG has provided an unqualified certificate on the Annual Accounts for the year ended 31 March 2025.

1.5. The draft audit certificate states that the financial statements have been properly prepared in accordance with applicable law, accounting standards and other reporting requirements.

1.6. During the audit, it was noted that two Management Review Controls (MRCs) were not identified. These MRCs are considered by Management to be impractical for a Council the size of Orkney Islands Council to implement.

1.7. No further weaknesses in the accounting and internal control systems were identified during the audit. However, a number of disclosure misstatements and other minor presentation and typographical changes were identified within the financial statements, which have been adjusted in the final accounts.

2. Recommendations

2.1. It is recommended that members of the Committee:

i. Note KPMG's independent auditor's report in respect of the audit of Orkney Islands Council's Annual Accounts for 2024/25, attached as Appendix 1 to this report, in accordance with the International Standard on Auditing 260.

ii. Approve Orkney Island's Council's Letter of Representation to KPMG in connection with its audit of the financial statements of Orkney Islands Council for the year ended 31 March 2025, attached as Appendix 2 to this report.

iii. Scrutinise the Annual Audit Report to the Council and the Auditor General for Scotland, attached as Appendix 3 to this report.

3. Main audit output

3.1. The main outputs from the audit report are as follows:

- An unqualified opinion on the truth and fairness of the statutory accounts as at 31 March 2025.
- One low level recommendation on the wider scope audit in respect of the Council's Strategic Planning and Performance Framework (p37, appendix 3).
- Four adjusted differences (p51, appendix 3):
    - Correction of split between long and short term borrowings.
    - Correction of classification between long and short term debtors.
    - Correction of classification for decommissioning provision.
    - Correction of depreciation charges charged in year of revaluation of HRA properties.
- Presentational changes, casting and additional disclosures (p51, appendix 3).
- Confirmation of two unadjusted audit differences (p52, appendix 3):
    - Timing issue between actual and expected returns in specific class of pension fund investments.
    - Disagreement in respect of valuation of area of land.

For Further Information please contact:
Erik Knight, Head of Finance, extension 2127, Email: Erik.Knight@orkney.gov.uk.

Implications of Report

1. **Financial** The audit fee payable to KPMG for the audit work is £242,810 for financial year 2023/2024 (compared to £238,260 for the previous year).
2. **Legal** None directly relating to the recommendations in the report.
3. **Corporate Governance** In terms of the Scheme of Administration, review of the Annual Audit Report to Elected Members, including the audit certificate, from External Audit, is referred to the Monitoring and Audit Committee.
4. **Human Resources** No direct HR implications.
5. **Equalities** N/A.
6. **Island Communities Impact** N/A.
7. **Links to Council Plan:** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Council Plan strategic priorities:
   ☒Growing our economy.
   ☒Strengthening our Communities.
   ☒Developing our Infrastructure.
   ☒Transforming our Council.
8. **Links to Local Outcomes Improvement Plan:** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Local Outcomes Improvement Plan priorities:
   ☒Cost of Living.
   ☒Sustainable Development.
   ☒Local Equality.
   ☒Improving Population Health.
9. **Environmental and Climate Risk** N/A
10. **Risk** An annual audit provides reassurance that the Annual Accounts have been prepared in accordance with International Financial Reporting Standards, and reduces the risk of material misstatement.
11. **Procurement** N/A
12. **Health and Safety** N/A
13. **Property and Assets** N/A
14. **Information Technology** N/A
15. **Cost of Living** N/A

List of Background Papers

Monitoring and Audit Committee, 03 April 2025, External Audit Plan 2024/25.
Monitoring and Audit Committee, 28 August 2025, Draft Annual Accounts 2024/25.
Monitoring and Audit Committee, 25 September 2025, Annual Audit Report.

Appendices

Appendix 1: DRAFT Independent Auditors Report.

Appendix 2: Orkney Islands Council's Letter of Representation to KPMG.

Appendix 3: DRAFT KPMG's Annual Audit Report to the Council and the Accounts Commission.

Independent auditor's report to the members of Orkney Islands Council and the Accounts Commission

Reporting on the audit of the financial statements

Opinion on financial statements

We certify that we have audited the financial statements in the annual accounts of Orkney Islands Council and its Group for the year ended 31 March 2025 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Group and Council Comprehensive Income and Expenditure Statements, Group and Council Balance Sheets, Group and Council Movement in Reserves Statement, Group and Council Cash Flow Statements, the Council Tax Income Account, the Non-domestic Rates Income Account, the Housing Revenue Account, the Harbour Authority Account, the UHI Orkney Account and notes to the financial statements, including material accounting policy information. The financial reporting framework that has been applied in their preparation is applicable law and UK adopted international accounting standards, as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2024/25 (the 2024/25 Code).

In our opinion the accompanying financial statements:

- give a true and fair view of the state of affairs of the Council and its Group as at 31 March 2025 and of the income and expenditure of the Council and its Group for the year then ended;
- have been properly prepared in accordance with UK adopted international accounting standards, as interpreted and adapted by the 2024/25 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Basis for opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)), as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report. We were appointed by the Accounts Commission on 18 May 2022. Our period of appointment is five years, covering 2022/23 to 2026/27. We are independent of the Council and its Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. Non-audit services prohibited by the Ethical Standard were not provided to the Council. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern basis of accounting

We have concluded that the use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the ability of the Council and its Group to continue to adopt the going concern basis of accounting for a period of at least twelve months from when the financial statements are authorised for issue.

These conclusions are not intended to, nor do they, provide assurance on the current or future financial sustainability of the Council and its Group. However, we report on the Council's arrangements for financial sustainability in a separate Annual Audit Report available from the Audit Scotland website.

Risks of material misstatement

We report in our Annual Audit Report the most significant assessed risks of material misstatement that we identified and our judgements thereon.

Responsibilities of the Corporate Director for Enterprise and Sustainable Regeneration and Monitoring and Audit Committee for the financial statements

As explained more fully in the Statement of Responsibilities, the Director for Enterprise and Sustainable Regeneration is responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Director for Enterprise and Sustainable Regeneration determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Corporate Director of Enterprise and Sustainable Regeneration is responsible for assessing the ability of the Council and its Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless there is an intention to discontinue the operations of the Council and its Group.

The Monitoring and Audit Committee is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decisions of users taken on the basis of these financial statements.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities outlined above to detect material misstatements in respect of irregularities, including fraud. Procedures include:

- using our understanding of the local government sector to identify that the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003 are significant in the context of the Council and its Group;
- inquiring of the Corporate Director of Enterprise and Sustainable Regeneration as to other laws or regulations that may be expected to have a fundamental effect on the operations of the Council and its Group;
- inquiring of the Corporate Director of Enterprise and Sustainable Regeneration concerning the policies and procedures of the Council and its Group regarding compliance with the applicable legal and regulatory framework;
- discussions among our audit team on the susceptibility of the financial statements to material misstatement, including how fraud might occur; and
- considering whether the audit team collectively has the appropriate competence and capabilities to identify or recognise non-compliance with laws and regulations.

The extent to which our procedures are capable of detecting irregularities, including fraud, is affected by the inherent difficulty in detecting irregularities, the effectiveness of the Council's controls, and the nature, timing and extent of the audit procedures performed.

Irregularities that result from fraud are inherently more difficult to detect than irregularities that result from error as fraud may involve collusion, intentional omissions, misrepresentations, or the override of internal control. The capability of the audit to detect fraud and other irregularities depends on factors such as the skilfulness of the perpetrator, the frequency and extent of manipulation, the degree of collusion involved, the relative size of individual amounts manipulated, and the seniority of those individuals involved.

A further description of the auditor's responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Reporting on other requirements

Opinion prescribed by the Accounts Commission on the audited parts of the Remuneration Report

We have audited the parts of the Remuneration Report described as audited. In our opinion, the audited parts of the Remuneration Report have been properly

prepared in accordance with The Local Authority Accounts (Scotland) Regulations 2014.

Other information

The Corporate Director of Enterprise and Sustainable Regeneration is responsible for the other information in the annual accounts. The other information comprises the Management Commentary, Annual Governance Statement, Statement of Responsibilities and the unaudited parts of the Remuneration Report.

Our responsibility is to read all the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except on the Management Commentary and Annual Governance Statement to the extent explicitly stated in the following opinions prescribed by the Accounts Commission.

Opinions prescribed by the Accounts Commission on the Management Commentary and Annual Governance Statement

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with statutory guidance issued under the Local Government in Scotland Act 2003; and

- the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016).

Matters on which we are required to report by exception

We are required by the Accounts Commission to report to you if, in our opinion:

- adequate accounting records have not been kept; or

- the financial statements and the audited parts of the Remuneration Report are not in agreement with the accounting records; or

- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Conclusions on wider scope responsibilities

In addition to our responsibilities for the annual accounts, our conclusions on the wider scope responsibilities specified in the Code of Audit Practice, including those in respect of Best Value, are set out in our Annual Audit Report.

Use of our report

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 108 of the Code of Audit Practice, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

ENTERPRISE AND RESOURCES
Director: Gareth O Waterson BAcc CA
Council Offices, Kirkwall, Orkney, KW15 1NY

Tel: (01856) 873535 Website: www.orkney.gov.uk
Email: gareth.waterson@orkney.gov.uk

If telephoning, please ask for Gareth Waterson on extension 2521

13 January 2026

KPMG LLP
319 St Vincent Street
Glasgow
G2 5AS

Dear Sirs

Letter of Representation 2024-25

This representation letter is provided in connection with your audit of the financial statements of Orkney Islands Council ("the Council"), for the year ended 31st March 2025 for the purpose of expressing an opinion:

i. as to whether these financial statements, in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2024-25 give a true and fair view of the state of the Council's affairs as at 31st March 2025 and of the Council and Group's income and expenditure for the financial year then ended;

ii. whether the Council and Group financial statements have been properly prepared in accordance with UK adopted international accounting standards, as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2024-25; and

iii. whether the financial statements have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

These financial statements comprise the following: Group and Council Comprehensive Income and Expenditure Statements, Group and Council Balance Sheets, Group and Council Movement in Reserves Statement, Group and Council Cash Flow Statements, the Council Tax Income Account, the Non-domestic Rates Income Account, the Housing Revenue Account the Harbour Authority Account, the UHI Orkney Account and notes to the financial statements, including significant accounting policies..

I confirm that the representations it makes in this letter are in accordance with the definitions set out in the Appendix to this letter.

I confirm that, to the best of my knowledge and belief, having made such inquiries as I considered necessary for the purpose of appropriately informing myself:

Financial statements

1. I have fulfilled my responsibilities, as set out in the terms of the audit engagement letter dated 18 March 2022, for the preparation of financial statements that:

   i. give a true and fair view of the state of the Council and Group's own affairs as at the end of its financial year and of the Council and Group's own income and expenditure for that financial year;
   ii. have been properly prepared in accordance with UK adopted international accounting standards, as interpreted, and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2024-25; and
   iii. have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

   The financial statements have been prepared on a going concern basis.

2. The methods, the data and the significant assumptions used by me in making accounting estimates and their related disclosures are appropriate to achieve recognition, measurement or disclosure that is reasonable in the context of the applicable financial reporting framework.

3. All events subsequent to the date of the financial statements and for which IAS 10 *Events after the reporting period* requires adjustment or disclosure have been adjusted or disclosed.

4. The effects of uncorrected misstatements are immaterial, both individually and in aggregate, to the financial statements as a whole. A list of the uncorrected misstatements is included in Appendix 2.

Information provided

5. I have provided you with:

   - access to all information of which I am aware, that is relevant to the preparation of the financial statements, such as records, documentation and other matters;
   - additional information that you have requested from me for the purpose of the audit; and
   - unrestricted access to persons within the Council from whom you determined it necessary to obtain audit evidence.

6. All transactions have been recorded in the accounting records and are reflected in the financial statements.

7. I confirm the following:

   I have disclosed to you the results of my assessment of the risk that the financial statements may be materially misstated as a result of fraud.

   Included in the Appendix to this letter are the definitions of fraud, including misstatements arising from fraudulent financial reporting and from misappropriation of assets.

8. I have disclosed to you all information in relation to:

   a) Fraud or suspected fraud that I am aware of and that affects the Council and involves:
      - management;
      - employees who have significant roles in internal control; or
      - others where the fraud could have a material effect on the financial statements; and
   b) allegations of fraud, or suspected fraud, affecting the Council's financial statements communicated by employees, former employees, analysts, regulators or others.

   In respect of the above, I acknowledge my responsibility for such internal control as I determine necessary for the preparation of financial statements that are free from material misstatement, whether due to fraud or error. In particular, I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

9. I have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.

10. I have disclosed to you and have appropriately accounted for and/or disclosed in the financial statements, in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.

11. I have disclosed to you the identity of the Council's related parties and all the related party relationships and transactions of which I am aware. All related party relationships and transactions have been appropriately accounted for and disclosed in accordance with IAS 24 *Related Party Disclosures.*

    Included in the Appendix to this letter are the definitions of both a related party and a related party transaction as I understand them and as defined in IAS 24.

12. I confirm that:

    - The financial statements disclose all of the key risk factors, assumptions made and uncertainties surrounding the Council's ability to continue as a going concern as required to provide a true and fair view and to comply with IAS 1 *Presentation of Financial Statements*.
    - No material events or conditions exist that may cast significant doubt on the ability of the Council to continue as a going concern.

13 On the basis of the process established by us and having made appropriate enquiries, we are satisfied that the actuarial assumptions underlying the valuation of defined benefit obligations are consistent with our knowledge of the business and are in accordance with the requirements of IAS 19 *Employee Benefits*.

We further confirm that:

a) all significant retirement benefits, including any arrangements that are:
- statutory, contractual or implicit in the employer's actions;
- arise in the UK and the Republic of Ireland or overseas;
- funded or unfunded; and
- approved or unapproved,
- have been identified and properly accounted for; and

b) all plan amendments, curtailments and settlements have been identified and properly accounted for

This letter was tabled and agreed at the meeting of the Monitoring and Audit Committee on 5 February 2026.

Yours faithfully

Gareth Waterson BAcc CA
Director of Enterprise and Resources

Appendix 1 Letter of Representation to Orkney Islands Council: Definitions

Financial Statements

IAS 1.10 states that "a complete set of financial statements comprises:

- a statement of financial position as at the end of the period;
- a statement of profit or loss and other comprehensive income for the period;
- a statement of changes in equity for the period;
- a statement of cash flows for the period;
- notes, comprising a summary of significant accounting policies and other explanatory information;
- comparative information in respect of the preceding period as specified in IAS 1 paragraphs 38 and 38A; and
- a statement of financial position as at the beginning of the preceding period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements in accordance with IAS 1 paragraphs 40A-40D.

An entity may use titles for the statements other than those used in this Standard. For example, an entity may use the title 'statement of comprehensive income' instead of 'statement of profit or loss and other comprehensive income'."

Additionally, the financial statements contain the Council's Statement of Financial Position, Statement of Movement in Reserves and related notes.

Material Matters

Certain representations in this letter are described as being limited to matters that are material.

IAS 1.7 and IAS 8.5 state that:

"Material omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor."

Fraud

Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users.

Misappropriation of assets involves the theft of an entity's assets. It is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorisation.

Error

An error is an unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

- was available when financial statements for those periods were authorised for issue; and
- could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

Management

For the purposes of this letter, references to “management” should be read as “management and, where appropriate, those charged with governance”.

Related Party and Related Party Transaction

Related party:

A related party is a person or entity that is related to the entity that is preparing its financial statements (referred to in IAS 24 *Related Party Disclosures* as the “reporting entity”).

1. A person or a close member of that person’s family is related to a reporting entity if that person:
    - has control or joint control over the reporting entity;
    - has significant influence over the reporting entity; or
    - is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.

2. An entity is related to a reporting entity if any of the following conditions applies:

    - The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
    - One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
    - Both entities are joint ventures of the same third party.
    - One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
    - The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.
    - The entity is controlled, or jointly controlled by a person identified in (a).
    - A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
    - The entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity.

A reporting entity is exempt from the disclosure requirements of IAS 24.18 in relation to related party transactions and outstanding balances, including commitments, with:

- a government that has control or joint control of, or significant influence over the reporting entity; and
- another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity.

Related party transaction:

A transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged.

Appendix 2 – Uncorrected misstatements

2,715

Unadjusted audit differences (£'000s)

No	Detail	CIES Dr/(Cr)	Balance Sheet Dr/(Cr)	Comments
1	Dr Pension Assets		2,023	Being the additional rate of return between the Actual Rate of Return and the Estimated Rate of Return by the Actuary as at 31.3.2025
	Cr Rate of Return	(2,023)		
	Dr MIRS	2,023		
	Cr Pension Reserve		(2,023)	
2	Dr Investment Properties		2,715	Being the valuation of development land
	Cr Income and Expenditure	(2,715)		
	Dr MIRS	2,715		
	Cr Capital Adjustment Acc		(2,715)	

Appendix 3

KPMG

Orkney Islands Council

Annual Audit Report - Monitoring and Audit Committee

DRAFT

15 January 2026

Key contacts

Your key contacts in connection with this report are:

Michael Wilkie
Partner
Tel: 07795 370106
Michael.Wilkie@kpmg.co.uk

Matthew Moore
Senior Manager
Tel: 07468 369807
Matthew.moore@kpmg.co.uk

Taimoor Alam
Manager
Tel: 07731 348596
Taimoor.alam@kpmg.co.uk

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Introduction

Purpose of this report

The Accounts Commission has appointed KPMG LLP as auditor of Orkney Islands Council (the Council) under part VII of the Local Government (Scotland) Act 1973 ("the Act"). The period of appointment is 2022-23 to 2026-27, inclusive.

Our annual audit report is designed to summarise our opinions and conclusions on significant issues arising from our audit. It is addressed to both those charged with governance at the Council and the Controller of Audit. The scope and nature of our audit are set out in our audit strategy document dated 3 April 2025.

Audit Scotland's Code of Audit Practice ("the Code") sets out the wider dimensions of public sector audit which involves not only the audit of the financial statements but also consideration of wider scope areas. The reports incorporates both aspects of the Code.

Accountable officer responsibilities

The Code sets out Orkney Islands Council's responsibilities in respect of:

- corporate governance;
- financial statements and related reports;
- standards of conduct for prevention and detection of fraud and error
- financial position; and
- Best Value.

Auditor responsibilities

This report reflects our overall responsibility to carry out an audit in accordance with our statutory responsibilities under the Act and in accordance with International Standards on Auditing (UK) issued by the Financial Reporting Council and the Code.

How we have delivered audit quality

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. We consider risks to the quality of our audit in our engagement risk assessment and planning discussions.

We define 'audit quality' as being the outcome when audits are:

– **Executed consistently**, in line with the requirements and intent of **applicable professional standards** within a strong **system of quality controls** and

– All of our related activities are undertaken in an environment of the utmost level of **objectivity**, **independence**, **ethics** and **integrity**.

External auditors do not act as a substitute for the Council's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

Introduction

Limitations on work performed

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's Code of Audit Practice ("the auditing Code").

This report is for the benefit of Orkney Islands Council and is made available to Audit Scotland and the Controller of Audit (together "the Beneficiaries").This report has not been designed to be of benefit to anyone except the Beneficiaries. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we may have been aware that others might read this report. We have prepared this report for the benefit of the Beneficiaries alone.

Nothing in this report constitutes an opinion on a valuation or legal advice. We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scoping and purpose section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries 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 Beneficiary'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, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries.

Status of our audit

Our audit testing is complete

Subject to approval of the financial statements by the Monitoring and Audit Committee, receipt of the signed representation letter and finalisation procedures, we expect to issue an unmodified audit opinion.

Audit Conclusions

Audit opinion

We expect to issue an unqualified opinion on the truth and fairness of the state of the Council's affairs as at 31 March 2025, and of the results for the year then ended. There are no matters identified, to date, on which we are required to report by exception.

Financial reporting framework, legislation and other reporting requirements

The Council is required to prepare its annual accounts in accordance with International Financial Reporting Standards, as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2024-25 ("the CIPFA Code"), and in accordance with the Local Authority Accounts (Scotland) Regulations 2014. We expect to confirm that the annual accounts have been prepared in accordance with the CIPFA Code and relevant legislation.

Statutory reports

We have not identified any circumstances, based on work performed till date, to notify the Controller of Audit that indicate a statutory report may be required.

Other communications

We did not encounter any significant difficulties during the audit. There were no other significant matters arising from the audit that were discussed, or subject to correspondence with management that have not been included within this report. There are no other matters arising from the audit, that, in our professional judgement, are significant to the oversight of the financial reporting process.

Materiality - Group and Council

Total group expenditure*
£248m
(PY - £208m**)
Total council expenditure*
£241m
(PY - £201m**)

Group materiality
£5.5m, 2.2% of total expenditure
(PY £4.2m, 2% of total expenditure)

Council materiality
£5.3m, 2.2% of expenditure
(PY £4.1m, 2% of total expenditure)

*Based on 2024-25 draft financial statements.

**Based on 2022-23 financial statements.

Group: £275k
Council: £265k

Misstatements reported to the Audit Committee

Group: £4.1m
Council: £4.0m

Procedure designed to detect individual errors at this level

Group: £5.5m
Council: £5.3m

Materiality for the financial statements as a whole

Our materiality levels

We determined materiality for the consolidated financial statements at a level which could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. We used a benchmark of gross expenditure which we consider to be appropriate as it reflects the scale of the Group/Council's services and we consider this most clearly reflects the interests of users of the Group/Council's accounts. To respond to aggregation risk from individually immaterial misstatements, we design our procedures to detect misstatements at a lower level of performance materiality. We also adjust this level further downwards for items that may be of specific interest to users for qualitative reasons. We also adjust this level further downwards for items that may be of specific interest to users for qualitative reasons, such as information in the remuneration report.

We have updated the updated materiality levels, based on the 2024-25 draft financial statements, since the last indicative audit plan.

Our audit findings

Significant audit risks	Risk Change since planning	Findings (Pages 9-14)
1 Retirement Benefit Obligations	No change	We have identified that there was not a Management Review Control (MRC) to address the significant audit risk. Audit difference was identified, which has not been adjusted by management (appendix 3).
2 Valuation of Land and Buildings and Investment Properties	No change	We have identified that there was not a Management Review Control (MRC) to address the significant audit risk. With respect to HRA properties we used KPMG valuers to support our challenge of the Council's approach and assumptions. With respect to investment properties there is one unadjusted misstatement (appendix 3).
3 Fraud risk from expenditure recognition (completeness of expenditure)	No change	We did not identify any issues in relation to fraud risk from expenditure recognition.
4 Management override of controls	No change	We have not identified any instances of management override of controls based on work performed till date.
Other focus area	**Change since planning**	**Findings**
IFRS 16 Leases	No change	We did not identify any reportable issues in relation to initial application of IFRS 16.

Please refer to page 15 for key accounting estimates

Our audit findings

Control Recommendations

There is one low grade recommendation arising in the current year in respect of the Wider Scope of public audit, related to the strategic planning and performance framework. **Page 37**

There is one recommendation arising from our Best Value Thematic review, aligned with a prior year Wider Scope recommendation. This is related to the identified financial pressures within the Council. **Page 32**

While consistent with a number of organisations, we continue to be required to recommend implantation of management review controls related to pension assumptions and valuations. **Pages 10/12**

Audit Misstatements

There are four adjusted audit misstatements, mainly related to balance sheet classification and the application of depreciation. In addition there were some presentational amendments. **Page 51**

There are two unadjusted audit misstatements. One unavoidably arises due to the timing of the preparation of draft accounts and the other relates to a difference in professional opinion. **Page 52**

Wider Scope and Best Value (Pages 18-32)

The Code of Audit Practice sets out four areas that constitute the wider scope of public audit in Scotland: financial sustainability; financial management; vision, leadership and governance; and use of resources to improve outcomes.

In addition to wider-scope, we are required to report on Best Value as prescribed by the Accounts Commission.

Audit Risks and our audit approach

1 Retirement benefit Obligations

Significant Audit risk

Risk: An inappropriate amount is estimated and recorded for the defined benefit obligation

The valuation of the Local Government Pension Scheme (Orkney Pension Fund) relies on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the Council's overall valuation.

There are financial assumptions and demographic assumptions used in the calculation of the Council's valuation, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Council's employees, and should be based on appropriate data. The basis of the assumptions should be derived on a consistent basis year to year, or updated to reflect any changes.

There is a risk that the assumptions and methodology used in the valuation of the Council's pension obligation are not reasonable. This could have a material impact to net pension liability accounted for in the financial statements.

Pension Funds in surplus pose an additional risk to Councils, as the entity will need to assess the level of surplus that it can recognise. This will need to be assessed each year, and the conclusion can change from one year to the next based on facts and circumstances for each participation.

Our response

We performed the following procedures designed to specifically address the significant risk associated with the valuation:

Control design:

- We evaluated the design and implementation of controls in place for management to review the LGPS valuation and the appropriateness of assumptions used.

Assessing the actuarial expert's credentials:

- We evaluated the competency and objectivity of the Scheme actuaries, Hymans Robertson, to confirm their qualifications and the basis for their calculations.

Input assessment:

- We reviewed the input from the Council into the calculation of the LGPS valuation; and
- We agreed the data provided by the audited entity to the Scheme Administrator for use within the calculation of the scheme valuation.

Audit Risks and our audit approach

1 Retirement benefit Obligations (continued)

Assessing methodology and benchmarking assumptions:

- We challenged, with the support of our own actuarial specialists, the key assumptions applied, being the discount rate, inflation rate, salary increases and mortality/life expectancy against externally derived data where appropriate; and
- We confirmed that the accounting treatment and entries applied by the Authority are in line with the requirements of the Code.

Assessing transparency:

- Disclosures: We considered the adequacy of the disclosures concerning the key judgements and degree of estimation involved in arriving at the valuation, in addition to disclosures regarding the sensitivity of the Authority's defined benefit obligation to these assumptions.

Assessing the recognised Surplus:

- We have considered the level of surplus that the Council has recognised and ensured that the asset recognised met the requirements of the CIPFA code for Local Authority Accounting in 2024-25, and current actuarial interpretation of the Code.

Our findings

Our work is complete for this significant risk.

Our actuarial specialists have evaluated the assumptions applied in measuring the defined benefit liabilities and have found these to be balanced, while remaining within actuaries' acceptable range. More detail is available on Page 15.

In assessing the Net pension Liability that has been recognised in the financial statements one misstatement was identified between the actual rate of return on assets achieved and the value the Actuary estimated in their report. This misstatement has not been corrected, see unadjusted misstatement – Appendix 3.

Auditing Standards requires where we have identified a significant audit risk, for management to have a review control in place (MRC) to respond to the risk. The threshold set for an effective Management Review Control is a high one, with various criteria that must be met including creating an independent expectation around amounts estimated. While we acknowledge that putting such a control in place would be impractical for a Council of your size, under Audit Standards we communicate to you that we have not identified such a MRC that is designed and implemented in such a way to provide the level of precision, response, investigation, and follow up needed by the Auditing Standards. **It is recommended.**

Audit Risks and our audit approach

2- Valuation of land and buildings,

Investment Properties

Significant Audit risk

Risk: The carrying amount of revalued Land & Buildings, and Investment Properties differs materially from the fair value

The value of the Council's Other Land and Buildings at 31 March 2024 was £338.5m, and Investment Property was £19.2m

The Code requires that Land and Buildings and Investment Properties are subject to revaluation and their year end carrying value should reflect the fair value at that date.

Any asset valuation carries with it risks of estimation uncertainty. The size of the land and buildings balance relative to our expected materiality means that the risk of a material difference between carrying value and fair value is increased.

Our response

We performed the following procedures designed to specifically address the significant risk associated with the valuation:

Control design:

- We evaluated the design and implementation of controls in place for management to review the valuation and the appropriateness of assumptions used.

Assessing the valuer's credentials:

- We critically assessed the independence, objectivity and expertise of Orkney and Shetland Joint Valuation Board, the valuers used in developing the valuation of the Council's properties at 31 March 2025; and
- We inspected the instructions issued to the valuers for the valuation of land and buildings to verify they are appropriate to produce a valuation consistent with the requirements of the Code.

Input assessment:

- We compared the accuracy of the data provided to the valuers for the development of the valuation to underlying information, such as floor plans, and to previous valuations, challenging management where variances were identified.

Assessing methodology and benchmarking assumptions:

- We challenged the appropriateness of the valuation of land and buildings; including any material movements from the previous valuation. We challenged key assumptions within the valuation, including the use of relevant indices and assumptions around physical and functional obsolescence;

Audit Risks and our audit approach

2 Valuation of land buildings (continued)

- We performed inquiries of the valuers in order to verify the methodology that was used in preparing the valuation and whether it was consistent with the requirements of the Royal Institute of Chartered Surveyors (RICS) Red Book and the Code; and
- We agreed the calculations performed of the movements in value of land and buildings and verified that these had been accurately accounted for in line with the requirements of the Code.

Assessing transparency:

- Disclosures: We considered the adequacy of the disclosures concerning the key judgements and degree of estimation involved in arriving at the valuation.

Our findings

We have completed our work in relation to valuation of DRC, HRA and investment properties.

Auditing Standards requires where we have identified a significant audit risk, for management to have a review control in place (MRC) to respond to the risk. The threshold set for an effective Management Review Control is a high one, with various criteria that must be met including creating an independent expectation around amounts estimated. While we acknowledge that putting such a control in place would be impractical for a Council of your size, under Audit Standards we communicate to you that we have not identified such a MRC that is designed and implemented in such a way to provide the level of precision, response, investigation, and follow up needed by the Auditing Standards. **It is recommended.**

Audit Risks and our audit approach

3 Fraud risk from expenditure recognition – cut off of expenditure

Significant Audit risk

Risk: Liabilities and related expenses for purchases of goods or services are not complete.

Under ISA 240 there is a presumed risk that income may be misstated due to improper recognition of income. This requirement is modified by Practice Note 10, issued by the FRC, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

In our audit plan reported to you in April 2025, we outlined that we intended to rebut the presumed risk of fraudulent revenue recognition, as we considered that there are limited incentives and opportunities to manipulate the way income is recognised in a material way. We continue to rebut this presumed risk. We also reported that we had not at the planning stage of our audit rebutted the risk around expenditure recognition, and noted that this was most likely to occur through the completeness of recognition of expenditure.

Following completion of all our risk assessment activities, we have concluded there is a significant risk in respect expenditure recognition in the incorrect accounting period (cut-off) risk over the completeness (understatement) of accrued expenditure and payables.

Our response

We performed the following procedures designed to specifically address the significant risk:

- We evaluated the design and implementation of the controls in place for manual expenditure accruals;
- We performed a search for unrecorded liabilities by selecting a sample of expenditure items paid from the Council's bank accounts in the period following year-end, and confirming that those relating to 2024/25 expenditure was accrued appropriately at year- end.
- We tested purchase transactions close to the year end to confirm that they are recorded in the correct period.

Our findings

We have not identified any fraudulent expenditure recognition during our testing. We have not identified any material misstatements from our completed procedures.

Auditing Standards requires where we have identified a significant audit risk, for management to have a review control in place (MRC) to respond to the risk. We have not identified such a MRC that is designed and implemented in such a way to provide the level of precision, response, investigation, and follow up needed by the Auditing Standards. However, the Council has a number of year end processes including a journal approval process which authorises the year end accruals as they are entered into the General Ledger; and budgetary controls that assist in identifying unusual or unexpected variances from budget. Management considers these arrangements are sufficient to address the Council face.

Audit Risks and our audit approach

4 Management override of controls Significant Audit risk

Risk: Liabilities Professional standards require us to communicate the fraud risk from management override of controls as significant.

Professional standards require us to communicate the fraud risk from management override of controls as significant.

Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

We have not identified any specific additional risks of management override relating to this audit.

Our response

- Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we evaluated the design and implementation and, where appropriate, tested the operating effectiveness of the controls in place for the approval of manual journals posted to the general ledger to ensure that they are appropriate;
- We analysed all journals through the year and focused our testing on those with a higher risk, such as journals with unusual expenditure code combinations;
- We assessed the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates;
- We reviewed the appropriateness of the accounting for significant transactions that are outside the Council's normal course of business, or are otherwise unusual; and
- We assessed the controls in place for the identification of related party relationships and tested the completeness of the related parties identified. We verified that these have been appropriately disclosed within the financial statements.

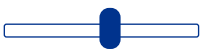
Our findings

- We identified 24 journal entries and post closing journal meeting our high-risk criteria
- We evaluated accounting estimates and did not identify any indicators of management bias. See page 15 to 16 for further discussion.
- Our examination did not identify any inappropriate entries.
- We did not identify any significant unusual transactions, based on work performed.
- We did not identify any issues from our related parties testing, based on work performed.

Key accounting estimates – Overview

Our view of management judgement

Our views on management judgements with respect to accounting estimates are based solely on the work performed in the context of our audit of the financial statements as a whole. We express no assurance on individual financial statement captions. Cautious means a smaller asset or bigger liability; optimistic is the reverse.

Asset/ liability class	Our view of management judgement	Balance (£m)	YoY change (£m)	Our view of disclosure of judgements & estimates	Further comments
	Cautious – Neutral – Optimistic			Needs improvement – Neutral – Best practice	
Liabilities LGPS Defined Benefit Obligation		**£-4.3m (2023-24 £141m)**	**-£145.3m**		KPMG actuaries have reviewed the actuarial valuation for the Orkney Pension Fund, considered the disclosure implications and compared the actuarial valuation to our internal benchmarks. Overall we consider the assumptions adopted to be balanced.

We reviewed the approach to valuation of land and buildings. We concur with management's assessment with one exception in which there is a difference in professional opinion related to a piece of land (appendix 3, p52).

Other estimates

We have also reviewed the following non-significant estimates as part of our audit work

- Depreciation

Group involvement – significant component audits

Involvement in group components

The Council management have assessed on the basis of materiality and significant influence that the Group financial statements are made up of the following components:

We have assessed from a Group perspective the following:

- Orkney Islands Council (Parent) (**significant**);
- Orkney Integration Joint Board (**not significant**);
- Orkney Ferries Limited **(non-significant – testing of defined benefit obligation balance);**
- Pickaquoy Centre Trust **(non-significant)**; and
- Hammers Hill Energy Limited **(non-significant).**

We performed testing of specific balances for Orkney Ferries Limited and we have performed risk assessment procedures over the remaining components in order to confirm that there were not material balances within the other entities that could cause a material error and did not identify any exceptions.

We did not identify any errors as a result of the procedures set out above based on work performed.

Other matters

Annual report

The Local Authority Accounts (Scotland) Regulations 2014 require the inclusion of a management commentary within the annual accounts, similar to the Companies Act requirements for listed entity financial statements. The requirements are outlined in the Local Government finance circular 5/2015.

We are required to read the management commentary and express an opinion as to whether it is consistent with the information provided in the annual accounts. We also review the contents of the management commentary against the guidance contained in the local government finance circular 5/2015.

We have considered the accounts and annual report and provided feedback to management who have addressed our observations.

Independence and Objectivity

ISA 260 also requires us to make an annual declaration that we are in a position of sufficient independence and objectivity to act as your auditors, which we completed at planning and no further work or matters have arisen since then.

Audit Fees

The base fee for the audit was £242,810 (2023/24: £238,260).

We have not completed any non-audit work at the Council during the year.

Wider Scope and Best Value

Financial Management

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

2024/25 budget and performance

In March, 2024 the Council agreed its 2024/25 budget based on the recommendation from the Policy and Resources Committee. General fund revenue budget was set at £112.3 million.

When setting the budget and Council Tax levels for 2024/25, the Council delegated powers to the Head of Finance, in consultation with the Corporate Director for Enterprise and Sustainable Regeneration and the Chief Executive, to revise the General Fund revenue budget for financial year 2024/25 in respect of any change to the estimated funding levels.

Following above a detailed budget was presented to the Policy and Resources Committee dated 17 June 2024 and was recommended for approval to the Council.

The final revised amount of the budget after taking into account the adjustments throughout the year, as reported in the annual financial statements, amounted to £115.1 million.Actual expenditure was £114.3 million. Major variances have been analysed as follows:

Orkney Health & Care – The continuation of recruitment pressures has resulted in the ongoing requirement to use agency staff to cover essential posts, which costs a premium.

Roads and Transport – Winter maintenance costs, surface treatment and patching for 2024/25 were high. Annual costs of maintaining airfield runways and general infrastructure were also high.

Other Services – Underspend on loan charges due to slippage on the planned delivery of the capital programme and the current programme of approved projects nearing completion. Increased interest on revenue balances.

The annual accounts provide a reconciliation between the planned and actual surplus/deficit, including the accounting adjustments to arrive at the amount of surplus as per the financial statements.

The Council continues to incur significant capital investment with £17.2 million being spent in 2024-25. Funding of capital expenditure mainly included £0.5 million from capital receipts, £9.7 million of grants with the balance of £6.9 million being met through internal funding and borrowing.

The Council reported an underspend of £0.3 million due to the expenditure not meeting the profile assumed in the capital programme. Capital outrun reports were presented periodically to the Policy and Resources Committee.

Wider Scope and Best Value

2025/26 budget

On 4 March 2025, when setting the budget and Council Tax levels for 2025/26, the Council delegated powers to the Head of Finance, in consultation with the Corporate Director for Enterprise and Sustainable Regeneration and the Chief Executive, to prepare and distribute a detailed budget incorporating all the budget adjustments agreed by the Council, and any settlement updates and/or clarifications unknown on 25 February 2025. General fund revenue budget was set at £119.2 million.

The approved budget exceeds the previous budget by £6.9 million and includes use of Strategic Reserve Fund amounting up to £20 million.

Budget Monitoring

Periodic revenue expenditure monitoring reports are presented to Individual Service committees. Additionally annual expenditure monitoring reports are presented to the Policy and Resources Committee.

Internal controls

As part of our audit, we identify and assess the key internal controls relevant to our audit. Our objective is to plan and seek assurance, where relevant, that the body has controls around recording and processing transactions to provide a sound basis for the preparation of the financial statements. Overall financial systems of internal control operated effectively, with the exception of the control weaknesses identified in the relevant section of this report.

Internal Audit

Internal Audit charter for 2024/25 was presented to the Monitoring and Audit Committee dated 6 June 2024 and was approved.

The annual report and opinion for 2024/25 was presented to the committee dated 28th August 2025 and noted that the Council has a framework of controls in place that provides adequate assurance regarding the organisation's governance framework, internal controls, and the management of key risks.

75% of the planned audits were reported as complete. Of the completed audits limited opinion was expressed in relation to two audits.

The report notes that throughout the previous financial year a common theme had emerged, which is non-compliance with the Council's Financial Regulations and Contract Standing Orders. It further notes that action was taken by the Head of Finance and the Head of Corporate Governance to raise awareness and improve compliance with these policies, and this has reduced both the instances of non-compliance identified and also the severity of the types of breaches. During 2024/25 only 4 instances were identified, 3 of which were minor in nature.

The report further notes that at the financial year end there were 25 (PY:32) recommendations which were past the agreed target date for completion. Of these 2 were high priority, 12 were medium and 11 were low priority.

Wider Scope and Best Value

Financial Management (continued)

Fraud prevention mechanisms

The Council is responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption. Furthermore, it is responsible for ensuring that its affairs are managed in accordance with proper standards of conduct by putting effective arrangements in place.

There are established procedures for preventing and detecting any breaches of these standards including any instances of corruption enacted through the anti fraud and corruption policy and whistleblowing policy.

The National Fraud Initiative (NFI) is a counter-fraud exercise across the UK public sector which aims to prevent and detect fraud. We note that the Council recognised the need for and participates in the initiative.

Financial regulations

The standing financial regulations are comprehensive and available on the website for public access. The regulations were reviewed by the Policy and Resource Committee dated 18th June 2024.

Going Concern

The Council's Group Accounts have been prepared on a "going concern" basis as it is expected that future local government finance settlements, aligned with the budget process, which drives through efficiency savings, will provide sufficient resources to finance future liabilities.

Conclusion

- Council has established budget setting and monitoring systems is in place.
- An established Internal Audit system is in place.

Wider Scope and Best Value

Financial Sustainability

Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

Medium term financial strategy (MTFS)

The Council's latest financial strategy update covers the period 2025/26 to 2029/30. The plan with the latest update was presented to the Policy and Resources Committee, and recommended to the Council for approval, dated 17 June 2025.

The strategy identifies the following key financial risk areas faced by the Council over the medium term:

Level and reduction in real terms of Scottish Government funding.

- Pay awards.
- General inflation.
- Economies of scale.
- Level of competition / choice.
- Demographics, in particular ageing population.
- Investment return volatility.
- Housing shortages.
- Recruitment and retention.
- Increasing levels of demand.
- Increased cost of borrowing.

Strategy notes that the potential funding gap faced by the Council may amount to £27.1 million over the period covered by the MTFS and recognises the need for delivering savings to achieve financial balance.

The projections produced contain several assumptions which are considered most likely by the Council:

- Staff costs – 2% to 3% annual increase over the forecast period
- Budget uplifts – 2% increase on annual basis.
- CPI on charges – 2% annual increase
- Council tax – 2% annual increase

The Medium-Term Financial Strategy includes an analysis of best and worst case scenarios as part of the financial planning. The risks associated with the assumptions in the MTFS include forecast error, economic performance (including inflation assumptions), changes to Scottish Government spending, political pressure, and demand-led need. The best and worst case scenario result in a funding gap to rise to £24.4 million and £27 million respectively by 2029/2030.

Wider Scope and Best Value

Financial Sustainability (continued)

The MTFS currently proposes to bridge the funding gap through contributions from Strategic Reserves Fund, County Fund Contribution and new charges, efficiencies and transformation. Planned new charges, efficiencies and transformation amount to £40.8 million over the period of the MTFS.

The amounts currently identified on account of requisite amounts above, amount to £793k and £2.8 million for 2026/27 and 2027/8. In order to balance the projected 2026/27 budget, based on the MTFS assumptions, the Council will have to identify additional funding, charges or efficiencies of £3.1 million. For 2027/28 £6.3 would have to be found.

We noted as part of the previous year audit that although the strategy has identified the options available to bridge the gap, detailed plans at operational/service level are required to be developed and implemented to ensure achievement. The 2024/25 budget as well the medium term strategy identify the use of reserves to bridge the funding gap however pressures on investment returns and strategic reserve fund and falling general fund balances make this approach untenable on an ongoing basis.

We recommended that the Council needs to continue to develop specific plans to bridge the gap in a sustainable manner.

Prior year recommendation

As part of prior year audit we noted that the Island Communities Impact Assessment was not carried out as part of MTFS development as it was considered unlikely to have an impact by the Council. We recommended that the Council should review the applicability of this assessment as part of the development of all plans, ensuring it is completed in respect of service redesign arising from the MTFS. The latest approved MTFS notes that the strategy being reviewed has been assessed as being unlikely to have an effect on an island community which is significantly different from its effect on other communities (including other island communities) in Orkney, accordingly a full Island Communities Impact Assessment has not been undertaken.

The Council plan identifies securing a new fleet of green ferries as one of the biggest challenges, under the developing our infrastructure theme, in light of the ageing fleet. Further associated performance measures and action points have been identified as part of the Council plan and Council delivery plan respectively. The Scottish Government has agreed to the further funding of a business case to investigate replacing Orkney's internal ferry fleet.

Wider Scope and Best Value

Financial Sustainability (continued)

This now requires the Council to build an agreed business case for ferry replacement, providing the resources required for work to scope out options and to carry out physical investigative works around Orkney's pier and harbours infrastructure including assessment of the impact on the future budgets and the medium term financial strategy. The latest update, provided to the Policy and Resource Committee, in June 2025 noted ongoing dialogue with Scottish Government and funding supplied to conduct design work on both potential future ferries and port infrastructure.

Capital Projections

As part of our previous year audit we noted that the Council has a capital programme in place. We further noted that the 2021/22 Annual Audit report recommended minimisation of recurring capital slippage which continues to occur in 2022/23. The Council delivery plan, which is a key document in relation to implementation of the Council plan, identifies the action plan in relation to capital program under the theme of "Developing our Infrastructure". The action plan identifies the objective to finalize and approve the new capital program in 2024/25 along with the monitoring of the current capital programme.

Slippage continued to occur in 2023/24. A report, titled "Review of Capital Programme: Capital Slippage", was presented to the Policy and Resource Committee dated 18th June 2024. The report noted that The Council has seen slippage in the delivery of capital projects for a number of years. The report recommended the amendment to the capital programme through consideration of the redeployment of a number of project budgets.

An update on capital slippage and a revised Capital Project Appraisal process has been developed through working with the Finance team in partnership with whom a review of the programme has been done, with projects which cannot progress at present being recommended for removal from the programme by Policy and Resources Committee in June 2024, which reduces artificial items of slippage.

The updated Capital Strategy and updated Capital Project Appraisal process were presented to Policy and Resources Committee in November 2024 and subsequently approved by the Council.

Reserves Strategy

The General Fund Reserves Strategy was reviewed by the Policy and Resources Committee in February 2025, in the context of setting revenue budget for 2025/26.

Wider Scope and Best Value

Financial Sustainability (continued)

Strategic Reserve Fund (SRF)

The purpose of the Strategic Reserve Fund is to provide for the benefit of Orkney and its inhabitants including the development of one-off strategic capital projects. The Strategic Reserve Fund is also supporting the level of General Fund Services as part of an agreed Medium Term Financial Strategy. For the financial year 2024-25 £20m from the Strategic Reserve Fund was used as a funding source to supplement the General Fund Services revenue budget. The approved contributions from the Strategic Reserve Fund for 2024/25 together with indicative budgets for 2025/26 and 2026/27, were set at at £20m, £18m and £15m respectively. The draw on reserves was set at £18.5m as part of detailed revenue budgets presented to the Policy and Resources Committee in June 2025.

The currently approved medium term financial strategy assumes SRF contribution amounting to £52.4 million and £4million on account of SRF contribution and Advance SRF re Wind Farm over the next five years.

One of the key principles of the medium term financial strategy is to ensure sustainable use of strategic reserves keeping in view the fund's commitment in relation to long term decline and potential decommissioning cost to the Council of the Flotta Oil terminal.

While there is a level that can be utilised, overuse of strategic reserve fund, as previously noted, is not sustainable as part of the longer-term financial plans and strategy. We recommend that the Council should carry out detailed analysis to develop a strategy in relation to sustainable use of the strategic reserve fund taking into account the long term commitments/plans of the Council which are expected to be settled/implemented through the use of the fund balance.

Prior year Recommendation

Conclusion

- MTFS is in place and takes into account scenario analysis and planning.
- Options to bridge the identified funding gaps have been identified as part of the MTFS.
- The 2025/26 budget as well the medium term financial strategy identify the use of reserves to bridge the funding gap however pressures on investment returns and strategic reserve fund and falling general fund balances make this approach untenable in the medium term.
- The Council has a capital programme in place.
- The Council has a reserves strategy in place.
- The Council should carry out detailed analysis to develop a strategy in relation to sustainable use of the strategic reserve fund taking into account the long term commitments/plans of the Council which are expected to be settled/implemented through the use of the fund balance.

Wider Scope and Best Value

Vision, leadership and Governance

Vision, leadership and governance is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

The governance framework is the system by which the Council leads, directs and controls its functions and relates to the community and other stakeholders. It includes the systems, processes, cultures and values through which the Council strives to adhere to the principles of good governance of openness, inclusivity, integrity and accountability. The Council's corporate governance is underpinned by the CIPFA/Solace Framework 'Delivering Good Governance in Local Government'. A revised edition of the Framework was published in early 2016 and the Local Code of Corporate Governance was updated to reflect the 2016 edition of the Framework. The Council adopted the revised Local Code of Corporate Governance in 2017. Review was carried out and revisions to the code were approved in October 2022. The updated code is published on the Council's website for public access. The Council has adopted a code of conduct for its employees and councillors which has been published on the website for awareness and public access. Arrangements are in place to ensure Members and officers are supported by appropriate learning and development.

Strategy

The overarching strategic vision of the Council is detailed in the Council's Plan which sets out the key outcomes the Council is committed to delivering with its partners. The plan extends for 5 years from 2023 to 2028. The plan is available for public's access on the Council's website. The Council plan is accompanied by a delivery plan. This Delivery Plan complements and supports Orkney Islands Council's strategic plan for the current Council term. The Delivery Plan describes some of the projects, services and policies which will progress priorities of the Council plan and achieve tangible outcomes for Orkney. The Council's Performance Management Framework sets out the process for monitoring performance against the strategic objectives. Priorities under the strategic plan are aimed to be delivered through service delivery plans.

Involvement of Stakeholders

Consultation relating to this plan was carried out in two stages. As part of the first stage the Council conducted a consultation exercise under the banner 'Orkney Matters'. This exercise included a questionnaire, a series of online meetings, and dedicated sessions for schools and community groups, which used art to engage with people less likely to respond through regular channels. The second stage was a public consultation on the draft plan itself before the plan was finalised

Wider Scope and Best Value

Vision, Leadership and Governance (continued)

The Council acknowledges the vulnerabilities of the remote communities like the ferry-linked isles as part of the development of the Council plan and have community specific performance measures and actions plans as part of the Council plan and Council delivery plan respectively.

Equalities Impact Assessment and Island Communities Impact Assessment were carried out as part of the development of the plan and presented for consideration along with the presentation of the Council plan for approval to the Policy and Resources Committee.

Setting and reporting of operational performance

In order to monitor and review progress the Council plan lays out performance measures and specified targets for each theme, to be achieved by the conclusion of the Council plan, which includes the three priority themes and the overall theme of transforming the Council. Some performance measures and targets are taken from the Orkney Partnership's Community Plan and some are taken from the Local Government Benchmarking Framework (LGBF).

Governance statement

As part of our audit process we review the Annual Governance Statement in the annual report and accounts. Governance statement is reviewed and approved by the relevant committees of Council ahead of being published as part of the annual accounts. The arrangements are appropriate and operated effectively during 2024/25.

Standing Orders, Schemes of Delegation and Financial Regulations

The Council operates within an established procedural framework. The roles and responsibilities of Elected Members and officers are defined within the Council's Standing Orders and Scheme of Administration, Contract Standing Orders, Scheme of Delegation and Financial Regulations. These are subject to regular review.

Risk Management

In order to manage and monitor its risks, the Council has an approved risk management strategy. Revised risk management policy and strategy 2024 - 26 was approved in October 2024.

Wider Scope and Best Value

Vision, Leadership and Governance (continued)

The policy requires the review and maintenance of risk registers. Corporate risk registers were presented to the Policy and Resources Committee periodically.

Scrutiny, challenge and transparency

Status of progress of audit recommendations and action points are regularly reported and considered by the Audit Committee. Committee minutes and related documents are available on the website for public scrutiny. The Council maintains a website where users can find further wide range of information about the Council including documents relating to strategies, policies and performance.

Alternative models of Governance

A reported titled “Alternative models of Governance” was presented to the Policy and Resources Committee dated 19th September 2023. Purpose of the report was to consider the scope of work, together with the resources required, to explore options for alternative models of governance that would provide greater fiscal security and economic opportunity for the Islands of Orkney. This was in pursuance of a notice of motion on alternative governance arrangement presented to the Council on 4 July 2023.

A progress update was provided to the Policy and Resources Committee on 17th June 2025. The Committee resolved to recommend that the Council should focus on engagement with the Scottish Government, COSLA and NHS Orkney in advancing the Single Authority Model agenda as set out in the current Programme for Government and supported by specific grant funding as the most likely option to ultimately progress to Stage 2 of the project.

Conclusion

- Council has effective strategic planning in place.
- Directorate Delivery plans have been developed.
- Governance arrangements are appropriate and operated effectively.
- Arrangements are in place in relation to security, challenge and transparency.

Wider Scope and Best Value

Use of resources to improve outcomes

Audited bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities. This includes demonstrating economy, efficiency, and effectiveness through the use of financial and other resources and reporting performance against outcomes.

The Council's Strategic Planning and Performance Framework describes the elements that make up the Council's strategic planning and performance arrangements, and its role in the strategic planning and performance arrangements of the Orkney Partnership. The framework goes on to describe the Council's arrangements for service and corporate self-assessment, service planning, workforce planning, and the management of risk, performance and business continuity. This was set in 2019 and needs to be updated to align with the new Council plan.

Recommendation one

Public Performance Reporting is a requirement carried out largely through the Council's Public Performance Reporting (PPR) webpages of the Council's website. The PPR webpages contain a wide variety of performance reports, for example, the Council's Annual Performance Report and Council Plan Monitoring Reports.

The Council's Annual Performance Reports are structured around Council priorities, and use various measures to show how well the Council performed during particular years. The annual performance reports for 2023/24 and earlier years are available for public access on the Council's website. The performance report reports achievement against the action points identified in the Council delivery plan aimed towards satisfaction of the key themes identified in the Council plan 2023-28 and best value.

This is based on performance reporting, against the delivery plan, reported to the Policy and Resources Committee on a periodic basis based on the following status categories:

- BLUE = Completed.
- RED = Overdue/Significant underperformance with a medium to high risk of failure to meet the target.
- AMBER = Minor underperformance, with a low risk of failure to meet the target.
- GREEN = On target.

The Council Plan 2023 to 2028 also lists performance measures in order to monitor and review progress on the delivery of the strategic priorities. This report provides the most recent data and status for each performance measure listed under each strategic priority as either:

- RED = The performance measure is experiencing significant underperformance, with a medium to high risk of failure to meet its target.
- AMBER = The performance measure is experiencing minor underperformance, with a low risk of failure to meet its target.
- GREEN = The performance measure is likely to meet or exceed its target.

Wider Scope and Best Value

Use of resources to improve outcomes (continued)

The Local Government Benchmarking Framework (LGBF) brings together a wide range of information about how all Scottish Councils perform in delivering services to local communities. The LGBF assists Councils in benchmarking their performance in key areas and creates opportunities to identify and share good practice. The link to LGBF performance is provided on the Council's website as well as the annual accounts, which allows visualization of the Council's performance by service areas and indicators.

Taking into account all indicators, as per the latest published data the Council's performance has improved or stayed the same as compared to the prior year and base year in relation to 54% and 55% of the indicators. The percentage of indicators in top 2 quartile reduced from 54% to 53%.

The lowest percentages in relation to indicators in the top 2 performance quartiles related to cost indicators, corporate services and tackling climate change categories i.e. 30%, 21% and 0% respectively. Performance against cost indicators has improved as compared to base year.

A detailed report was presented to the Policy and Resource Committee, dated 17th June 2025 to provide an overview of performance in relation to LGBF and to scrutinise the performance against measures specific to Orkney Council.

Conclusion

Performance management arrangements provide a sound base for improvement.

Wider Scope and Best Value

The Publication of Information (Standards of Performance) Direction 2021 Statutory Performance Indicators

The Accounts Commission issued a new Statutory Performance Information (SPIs) Direction in December 2021 which applies for the three years from 2022/23.

Direction requires a Council to report its:

- performance in improving local public services (including those provided with its partners and communities), and progress against agreed desired outcomes (SPI 1). The Commission expects this reporting to allow comparison both over time and with other similar bodies (drawing on Local Government Benchmarking Framework and/or other benchmarking activities).
- own assessment and audit, scrutiny, and inspection body assessments of how it is performing against its duty of Best Value, and how it has responded to these assessments (SPI 2).

Details of how the Council complies with requirements of SP1, along with the related recommendations, are included in the “Use of resources to improve outcomes” slide.

The Council has a system in place to report regular updates in relation to the achievement of strategic objectives to the Service Committees and the Policy and Resources Committee in the form of monitoring of the Council delivery plan. The latest reporting is accessible through accessing the minutes of the relevant committees.

Progress against action pointes emanating from external and internal assessments is reported to and monitored by the Policy and Resources Committee and are accessible by public through the minutes of the meetings of the relevant committee. The Council Plan 2023-28 was published for consultation, which also included the performance measures mapped against the desired outcomes and key themes. This enabled the respondents to consider and comment on the meaningfulness of the performance indicators. The plan was updated in light of the responses and presented to the Policy and Resources Committee dated 21 February 2023. The Council has made arrangements related to self-evaluation of services.

Conclusion

Council has made arrangements to comply with the SPI Directions.

Wider Scope and Best Value

Best Value

Local government bodies have a duty under the Local Government in Scotland Act 2003 to make arrangements which secure Best Value. Best Value is continuous improvement in the performance of the body's functions.

Under the new Code of Audit Practice, the audit of Best Value in Councils is fully integrated within the annual audit work performed by appointed auditors and their teams. Auditors are required to evaluate and report on the performance of Councils in meeting their Best Value duties.

There are the following four aspects to auditors' work:

- Follow-up and risk-based work.
- Service improvement and reporting.
- Thematic reviews.
- Contributing to Controller of Audit reports.

Thematic reviews

Auditors are required to report on Best Value or related themes prescribed by the Accounts Commission. The thematic work for 2024/25 is on the subject of service transformation. In carrying out the overview, auditors are required to answer the following questions:

- To what extent does the council have clear plans for transformation that link to its priorities and support long-term financial sustainability?
- To what extent do the council's programme management arrangements facilitate effective oversight of its transformation plans?
- To what extent are communities and partners involved in the development and delivery of the council's plans for transformation?
- To what extent has the council considered the impact of its transformation activity, including on vulnerable or protected groups?

Wider Scope and Best Value

Best Value (continued)

As required by guidance we issue a separate management report.

Some of the key messages are:

- The council's plans for transformation are embedded within its key plans and strategies and align with its corporate priorities. It does not have an overarching transformation programme, but 'transforming our council' is a key theme underlying its plans.
- The council's transformation projects vary in scale, and it is clear how it will address its funding gaps/ contribute to the financial sustainability of the Council. However, the Council needs to consider projects to generate further cost savings/income generation required to address the financial challenge identified as part of the financial strategy.
- The Council faces challenges including sufficient staffing capacity to deliver its transformation ambitions.

There is one improvement action which relates to the need for the Council to consider additional schemes to generate cost savings or generate income in order to meet the financial challenge identified as part of the medium-term financial strategy. This aligns with the prior year wider scope recommendation (page 44) in respect of which management has provided an update.

Appendices

Appendix one

Mandatory communications

Type		Statement
Our draft management representation letter		We do not expect to request any specific representations in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2025.
Adjusted audit differences		Refer Appendix Three
Unadjusted audit differences		Refer appendix Three.
Related parties		There were no significant matters that arose during the audit in connection with the entity's related parties.
Other matters warranting attention by the Audit and Risk Committee		There were no matters to report arising from the audit that, in our professional judgment, are significant to the oversight of the financial reporting process.
Control deficiencies		We communicate to management in this report all deficiencies in internal control over financial reporting of a lesser magnitude than significant deficiencies identified during the audit that had not previously been communicated in writing.
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts		No actual or suspected fraud involving group management, employees with significant roles in internal control, or where fraud results in a material misstatement in the financial statements was identified during the audit.

Appendix one

Mandatory communications

Type		Statement
Significant difficulties		No significant difficulties were encountered during the audit.
Modifications to auditor's report		None expected.
Disagreements with management or scope limitations		The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit.
Other information		No material inconsistencies were identified relating to other information in the Management Commentary. The Commentary is fair, balanced and comprehensive, and complies with the requirements of the Code.
Breaches of independence		No matters to report. The engagement team have complied with relevant ethical requirements regarding independence.
Accounting practices		Over the course of our audit, we have evaluated the appropriateness of the Council's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate.
Significant matters discussed or subject to correspondence with management		The significant matters arising from the audit were discussed, or subject to correspondence, with management.

Appendix two

Recommendations followed up and raised

We have followed up the recommendations raised in the prior years. Below is a table of the actions and implementation. We have disclosed below the prior year recommendations with the current management response.

Priority rating for recommendations					
❶	**Priority one:** issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	❷	**Priority two:** issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸	**Priority three:** issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

Appendix two

Recommendations Current year (Wider Scope)

#	Risk	Issue, Impact and Recommendation	Management response
1	3	The Council's Strategic Planning and Performance Framework was set in 2019. There has been updates to the Council Plana and underlying delivery, directorate and service plans. There is a risk that the framework is outdated and not aligned to the most recent planning documents. **Recommendation:** We recommend that the framework is reviewed and updated on a periodic basis.	The framework is already under review to ensure it remains fit for purpose and is up to date and aligned with current planning and performance requirements. While a draft has been developed it will be finalised after the management restructure is fully implemented and the mid-term review of the Council Plan is complete. The current framework has been checked and is still an appropriate model while the full refresh is being completed.

Appendix two

Recommendations 2023-24 Financial Statements

#	Risk	Issue, Impact and Recommendation	Management response PY	Position as at September 2025
1	❷	We challenged management in respect of the Beacon valuation compared to market sales evidence for certain categories, and the approach to Beacon valuations in general. We undertook additional risk assessment procedures and concluded there was no risk of material misstatement. We identified a control weakness related to the evidence supplied by the Council Valuer to support some of the judgements made. **Recommendation** We recommend that management discuss with the valuer: - the approach to Beacon categories (consistency of property type in each Beacon) - how market sales evidence is considered in respect of each Beacon - how property valuations have been adjusted for the social rental compared to market price	**Response** Management to meet with valuer prior to commencement of 2024/25 valuation process **Officer Responsible** Service Manager Corporate Finance **Date** 31 March 2025	The Head of Finance and officers from the Corporate Finance team met with the Council's valuer on 12 March 2025, to discuss the valuations required for the Council's asset as at 31 March 2025 under the rolling programme of revaluations. We also asked the Valuer to undertake a review of the Beacon valuations he uses to revalue the Housing Revenue dwellings, which required revaluation at the end of 2024/25. This review took place and the Valuer concluded that the Beacons used were still relevant and no changes were required. The Head of Finance was content to accept the Valuer's professional judgement and the review carried out.

Appendix two

Recommendations 2023-24 Financial Statements

#	Risk	Issue, Impact and Recommendation	Management response PY	Position as at September 2025
2	❷	The Council's development plan was not reflected in the approach to valuations of certain investment properties. This contributed to the adjusted audit misstatement where development land included in the development plan was valued as agricultural land. **Recommendation** We recommend that management review the development plan alongside the valuation of land and buildings as part of the closedown procedures and share the same with the appointed valuer.	**Response** Where relevant, the Development Plan will be considered as part of the information drawn upon for the valuation of land and buildings. **Officer Responsible** Service Manager Corporate Finance **Date** 31 March 2025	The Head of Finance and officers from the Corporate Finance team met with the Council's valuer on 12 March 2025, to discuss the valuations required for the Council's asset as at 31 March 2025. Investment properties are re-valued every year to ensure the carrying value reflects current market values. The Head of Finance advised the Council's valuer that the Orkney Islands Council Local Development Plan should be taken into consideration when carrying out these valuations. The Head of Finance is content to accept the Valuer's professional judgement for investment property valuations.

Appendix two

Recommendations 2023-24 (Wider Scope)

#	Risk	Issue, Impact and Recommendation	Management response PY	Position as at September 2025
3	1	Internal audit noted non-compliance with the Council's Financial Regulations and Contract Standing Orders. There is a risk of improper use of resources and public money. **Recommendation:** We recommend root cause analysis is undertaken and corrective actions are put in place to ensure compliance with the relevant regulations.	The Council's Contract Standing Orders were updated in March 2024 and financial regulations were updated and approved at Policy and Resources Committee on 18th June 2024. This was circulated to all OIC staff by the Communications team on the 03rd July 2024. The Head of Finance and the Head of Legal and Governance reminded officers of the importance of adhering to the Financial Regulations and the Contract Standing Orders. This is reinforced by the Procurement Team who endeavour to ensure policies are followed by officers. The Corporate Leadership Team and Senior Management Teams will ensure it is applied. In addition, in April 2024, training in respect of the updated Contract Standing Orders was delivered by the Service Manager (Procurement) to officers within the Council who have authority for exercising procurement functions, in order to further enhance compliance."	The financial regulations are now highlighted within budget training and circulated to budget holders. This is now business as usual. The Internal Audit Internal Audit Annual Report and Opinion, reported to M&A in 28 August 2025, noted improved compliance with the financial regulations and contract standing orders.

Appendix two

Recommendations 2023-24 (Wider Scope)

#	Risk	Issue, Impact and Recommendation	Management response PY	Position as at September 2025
4	1	The Council's Medium-Term Financial Strategy and the Long-Term Financial Plan are not updated to reflect recent performance, current assumptions, efficiency targets, and Strategic Reserve Fund draws. There is a risk of outdated financial plans **Recommendation:** We recommend that the Council's Medium-Term Financial Strategy and the Long-Term Financial Plan are updated to reflect recent performance, current assumptions, efficiency targets and Strategic Reserve Fund draws.	It is acknowledged this an outstanding strategy and plan but it is difficult to predict when funding levels are set annually by the Scottish Government. Also in a time of political and economic climate the landscape is changing frequently and therefore at present any strategy and plans are very quickly outdated.	The Medium Term Strategy was approved in June 2025 for the period 2025/26 to 2029/30. Due to the continued economic and political uncertainty no longer term plan has been approved due to plans being outdated very quickly.

Appendix two

Recommendations 2022-23 (Financial Statements) follow up

#	Risk	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
5	2	In August 2022, Audit Scotland issued updated guidance in regards to the accounting of Infrastructure assets. Councils which did not meet this requirement could utilise two statutory overrides. For management to meet this requirement they will need to carry out a retrospective review of the methodology used to account for the infrastructure assets and update the methodology accordingly to ensure compliance with the guidance. This did not impact upon our planned audit approach	The Council continued to make use of the Scottish Government statutory override in the preparation of the annual accounts for 2023/24. The Council awaits further guidance on this from CIPFA/LASAAC.	No further guidance has been issued by CIPFA/LASAAC so the Council continued to make use of the Scottish Government statutory override in the annual accounts for financial year 2024/25. This recommendation is considered complete until such time as the statutory override is withdrawn.

Appendix two

Recommendations 22-23 (Wider scope)

#	Risk	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
6	3	The anti-fraud policy notes that it is subject to review every three years. However, it was last reviewed and updated in 2019. There is a risk of obsolete and out of date policies and procedures. **Recommendation:** We recommend timely review and update of all policy and procedures documents	The anti-fraud policy has been updated and reviewed by the Corporate Director of Enterprise and Sustainable Regeneration, the Head of Finance and the Chief Internal Auditor. The updated policy will be presented to Policy and Resources Committee in November 2024.	The Council's revised and updated Corporate Anti-Fraud Policy was presented and approved by Policy and Resources Committee on 27 November 2024.

Appendix two

Recommendations 22-23 (Wider scope)

#	Risk	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
7	1	MTFS identifies the options available to bridge the identified funding gap. However, detailed plans at operational/service level are required to be developed and implemented to ensure achievement. There is a risk of inability to achieve financial balance. **Recommendation:** We recommend that the Council should continue to develop detailed service level medium terms plans to bridge the gap ina sustainable manner	As part of the development of a transformation portfolio to feed into the MTFS, Corporate Directors have commenced the initial identification of savings and income generation towards the Service targets as set by the Policy and Resources Committee in February 2024. A series of seminars for elected members is underway to go through proposals for each service area in detail with a consolidation session planned in November 2024 ahead of formal budget setting in Feb 2025. In-progress	There has been a Charging Officer Working Group on proposed charging changes as part of the budget setting for 2026/27. The savings template for 2024/25 is being refreshed and will be submitted as part of a series of seminars prior to budget setting for 2026/27 in March. On-going lobbying of Scottish Government, and other funding bodies, for specific funding streams and in general funding – for example the review of SINA being undertaken as part of 2026/27 settlement work by COSLA and Scottish Government.

Appendix two

Recommendations 22-23 (Wider scope)

#	Risk	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
8	2	The Council recognises that overuse of strategic reserve fund is not sustainable as part of the longer term financial plans and strategy. There is a risk of financial imbalance and depleted reserves. **Recommendation:** We recommend that the Council should carry out detailed analysis to develop a strategy in relation to sustainable use of the strategic reserve fund taking into account the long-term commitments/plans of the Council which are expected to be settled/implemented through the use of the fund balance. It should determine a floor with a clear rationale and a policy/process for the approval of use of the fund.	Partially complete. Updated and revised Reserve Fund Investment Strategy is presented to Investment Sub-committee on 18 September.	The updated and revised Investment Strategy recognised the continued draw on reserves until financial year 2027/28. The new strategy was approved by Members on 18 September 2024 and work has been ongoing throughout financial year 2024/25 to implement the new strategy, recognising that movements out of and into new investment classes should be carried out at the most beneficial time to maximise gains and minimise transitional transaction costs.

Appendix two

Recommendations 22-23 (Wider scope)

#	Risk	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
9	3	The policy requires the review and maintenance of risk registers (corporate and directorate). Corporate risk registers were presented to the Policy and Resources Committee periodically however directorate risk registers were last presented in June 2021. Additionally the internal audit report on corporate governance and risk management, dated 26th January 2023, identified action points for improvement. There is a risk of ineffective risk management. **Recommendation:** We recommend that risk management strategy should be implemented without exception.	The Corporate Risk Register was considered in June 2024 by Policy and Resources Committee. An updated Risk Management Plan and Strategy is going to be considered by Policy & Resources on 24 September. Directorate Risk Registers are the responsibility of the different Corporate Directors. Each Directorate has submitted a Directorate Delivery Plan to the relevant Committee and these will be reported on 6- monthly which will include a review of the Risk Register for the service. The NSI Directorate Delivery Plan and Risk Register was considered by D&I committee in March 2024 and is under review at the moment to make sure all mitigating actions are progressing as planned. The SPBS was considered at Policy and Resources in November 2023 and is reviewed by the service regularly and Policy and Resources Committee 6 monthly. The ESR Directorate Delivery Plan and Risk Register was considered by Development and Infrastructure Committee in March 2024. The ELH Risk Register was considered by the Education, Leisure and Housing Committee in June 2024 and the Directorate Delivery Plan by the same Committee in September 2024.	The revised Risk Management Policy and Strategy for 2024 -2026 was approved by Policy and Resources Committee on 24 September 2024.

Appendix two

Recommendations raised Best Value Thematic report – 22-23

#	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
10	**Stakeholder engagement** The Council used to operate a citizens panel under the title of Orkney Opinions. While there are other engagement activities including aspects of good practice, there is a risk that citizens do not have opportunity for engagement with the Council through a regular structured way throughout the year. A project to review the approach to Community Consultation and Engagement is underway and includes actions to consider engagement methods. We recommend the Council ensures that it considers, as part of this project, how ad hoc and in-year consultation is carried out effectively and that it seeks stakeholder views on the proposed and implemented approach.	The Community Engagement Project team continues to progress Phase one, involving selection of a suitable digital engagement platform, engagement with young people and Orkney Matters 2. Orkney Matters 2 meetings began in May and will conclude in October. An arts outreach programme connected with Orkney Matters 2 will begin in August and once this is concluded, work will begin on compiling a full report and analysis on the findings. The review of the citizenship panel forms part of the second phase of the project.	This project has progressed within phase one. The review of the citizenship panel remains within phase two as previously noted. The Community Engagement Project Team has reviewed progress against the delivery plan. The project has temporarily paused while the management restructure is fully implemented. The project will be reinitiated once this is complete and the project team will progress this workstream as part of the updated delivery plan.

Appendix two

Recommendations raised Best Value Thematic report – 22-23

#	Issue, Impact and Recommendation	Position as at September 2024	Position as at September 2025
11	**Equality performance measures** Indicators in the Council plan include a number in relation to reducing inequality. The Council presented on Equality Outcomes 2023-2027 to Policy and Resources Committee in September 2023 and Work is ongoing to develop associated KPIs and delivery plan. Until these are completed, there is a risk of inability to monitor and achieve inequality related objectives and outcome. We recommend development / highlighting of specific inequality related performance measures and delivery plan is set a target date and monitored.	The Delivery Plan for the Equality Outcomes has been drafted and agreed with relevant lead officers across the Council. The Delivery Plan will be published on the Council website and the first progress and performance monitoring report on it will be presented to Policy and Resources Committee in November 2024.	An annual report is provided to Policy and Resources Committee on progress with Equality, Diversity and Inclusion priorities. This incorporates the progress against the priority actions identified in our Equality Outcomes Delivery Plans. The first report went to Policy and Resources Committee in November 2024 and the second is on the agenda for the meeting of 23 September 2025. This now falls within business as usual.

Appendix two

Recommendations raised Best Value Thematic report – 22-23

#	Issue, Impact and Recommendation	Position at September 2024	Position at September 2025
12	**Climate change** The objectives outlined in the previous carbon management programme have not yet been achieved. The council is working on developing the new climate related strategy and associated plans which will then need incorporating into other strategies. Until this is completed there is a risk of the Council plans and strategies not aligned to support the achievement of the climate related objectives and outcomes in a timely manner. The Council should expedite its ongoing development of climate related strategies and associated action and delivery plans. This should include incorporation of the impacts of the identified climate related initiatives in the future budgets and the medium-term financial plan.	The Officer Working Group to support strategy development and co-ordination is now up and running with progress being made as planned, through smaller task themed sub-groups. The external consultant to support the development of the OIC Climate Work programme including developing indicative Council transition pathways towards net zero has been appointed (August 2024) and work with them has started. A report on Climate Change and Net Zero will be considered by Policy & Resources on 24 September, this includes an overview of the Council's developing strategic approach to Climate Change and an updated vision statement for members consideration. The Annual Report for Scottish Government on how the Council is fulfilling its climate change duties will be considered at the November cycle of meetings.	In relation to the Carbon Management Programme work has been progressing including joint working between the council's energy and climate teams. This includes working with the Islands Centre for Net Zero regarding funding which could include additional staff resources. To deliver the Strategy; work on the baseline study has been ongoing with the consultancy team during 2025. This is nearing conclusion with a report on the first taskings scheduled to the November meeting of the Council's P&R Committee. The annual report to the Scottish Government on how the Council is fulfilling its duties will also be reported to the November P&R Committee. The other plans are proceeding in line with the Council Corporate Delivery Plan.

Appendix two

Recommendations raised Best Value Thematic report – 22-23

#	Issue, Impact and Recommendation	Position at September 2024	Position at September 2025
14	**Impact assessments** Equalities Impact Assessment and Island Communities Impact Assessment were carried out as part of the development of the Council plan. However, these have not been published on the designated section of the website (alongside older assessments) but rather with the associated committee meeting reports were they were considered. There is a risk that stakeholders cannot readily access the latest assessments. We recommend that the Council add a note to this effect on the website and consider how assessments can be most readily accessed / overviewed by the public.	The approach has been considered including benchmarking against other Councils. A new unified area for impact assessments is being developed and will be completed by December 2024.	A dedicated section has been added to the Orkney Islands Council website that outlines our approach to Impact Assessments; both Equality Impact Assessments and Island Communities Impact Assessments and provides guidance on how to find them. This can be found at: https://www.orkney.gov.uk/your-council/equality-diversity-and-inclusion/impact-assessments/ As noted on the webpage, EqIAs are published alongside the relevant committee meeting reports where they were considered. This ensures they are available in context and aligned with the decision-making process. Impact Assessments can also now be searched for by typing IA into the search bar on the home page and this search can be tailored by including a policy or document title.

Appendix three

Audit Differences

Adjusted audit differences (£'000s)

Under UK auditing standards (ISA (UK) 260) we are required to provide the Audit and Risk Committee with a summary of adjusted audit differences (including disclosures) in excess of £265,000 identified during the course of our audit. The adjustments below have been included in the financial statements.

Adjusted audit differences (£'000s) – Financial Statements (Council and Group)

Detail	CIES Dr/(Cr)	Balance Sheet Dr/(Cr)	Comments
Long term Borrowings	-	10,000	Being the correction of the maturity of borrowings
Short Term Borrowings	-	(10,000)	
Long term debtors	-	3,243	Being the correction of the classification of long term debtors
Long Term investments	-	(3,243)	
Provisions non- current	-	(41,341)	Being the correction of the maturity of decommissioning provision
Provisions current	-	41,341	
Depreciation (CIES)	(1,093)	-	Being the correction of depreciation in respect of HRA properties
Accumulated Depreciation	-	1,093	
Gain on Revaluation (CIES)	(2,637)	-	
Land and Building (Gain in NBV of assets)	-	2,637	
Capital Adjustment Account	-	(1,093)	
General Fund	-	3,730	
Revaluation Reserve	-	(2,637)	

In addition to above following change has been agreed for disclosures:

- Update to related parties note in relation to transactions with Orkney Ferries Limited.
- Presentational changes in respect of pension disclosures, include those related to pension asset ceiling.
- Casting and other internal consistency points.
- Disclosure updates regarding the term of provisions and related party balances with explanatory notes added, regarding the prior year.

Appendix three

Audit Differences

Under UK auditing standards (ISA (UK) 260) we are required to provide the Audit Committee with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements.

Unadjusted audit differences (£'000s)

No	Detail	CIES Dr/(Cr)	Balance Sheet Dr/(Cr)	Comments
1	Dr Pension Assets		2,023	Being the additional rate of return between the Actual Rate of Return and the Estimated Rate of Return by the Actuary as at 31.3.2025
	Cr Rate of Return	(2,023)		
	Dr MIRS	2,023		
	Cr Pension Reserve		(2,023)	
2	Dr Investment Properties		2,715	Being the valuation of development land
	Cr Income and Expenditure	(2,715)		
	Dr MIRS	2,715		
	Cr Capital Adjustment Acc		(2,715)	

The first difference above, relates to the difference between the estimated and actual rate of return arose between the preparation of the draft and audited accounts and could not have been known by management when preparing the draft. This is a common difference arising in the sector which needs annual consideration for potential adjustment alongside other unadjusted differences.

The second difference also arose in the prior period, when it was adjusted, and relates to a difference in professional opinion regarding the valuation of certain land held by the Council.

Taken together, these exceed our performance materiality but are below our overall materiality.

Appendix four

Confirmation of Independence

We confirm that, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and that the objectivity of the Partner and audit staff is not impaired.

To the Audit Committee members

Assessment of our objectivity and independence as auditor of the Orkney Islands Council.

Professional ethical standards require us to provide to you with a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- General procedures to safeguard independence and objectivity;
- Independence and objectivity considerations relating to the provision of non-audit services; and
- Independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard.

As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Communications
- Internal accountability
- Risk management
- Independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

Independence and objectivity considerations relating to the provision of non-audit services

Summary of non-audit services

We have not provided any non-audit services in year.

Confirmation of Independence (continued)

We have considered the fees charged to the Council for professional services provided during the reporting period. Total fees charged can be analysed as follows:

Entity	2024/25	2023/24
Auditor Remuneration	£230,170	£220,890
Pooled Costs	£5,780	£8,050
PABV Contribution	£46,960	£49,800
Sectoral Cap Adjustment	-£40,100	-£40,480
TOTAL AUDIT FEES (Incl VAT)	**£242,810**	**£238,260**

Source: Audit Scotland

Application of the FRC Ethical Standard 2019

We communicated to you previously the effect of the application of the FRC Ethical Standard 2019. That standard became effective for the first period commencing on or after 15 March 2020, except for the restrictions on non-audit and additional services that became effective immediately at that date, subject to grandfathering provisions.

We confirm that as at 15 March 2020 we were not providing any non-audit or additional services that required to be grandfathered.

Confirmation of audit independence

We confirm that as of the date of this letter, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the partner and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

Yours faithfully

KPMG LLP

Appendix five

KPMG's Audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.

- To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework.
- Responsibility for quality starts at the top through our governance structures as the UK Board is supported by the Audit Oversight Committee, and accountability is reinforced through the complete chain of command in all our teams.

Appendix five (continued)

Commitment to continuous improvement

- Comprehensive effective monitoring processes
- Significant investment in technology to achieve consistency and enhance audits
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

Association with the right entities

- Select clients within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management

Performance of effective & efficient audits

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching, including the second line of defence model
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Insightful, open and honest two way communications

Clear standards & robust audit tools

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- KPMG Clara incorporating monitoring capabilities at engagement level
- Independence policies

Commitment to technical excellence & quality service delivery

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights

Recruitment, development & assignment of appropriately qualified personnel

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members employed KPMG specialists and specific team members

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