

Financial Monitoring 2022/23 – General Fund Revenue**Report by David Gladwin, Acting Chief Financial Officer****Report for Decision****1 Recommendations**

Council is recommended to:

- a) Approve the use of Capital Receipts Flexibility of £0.397 million as laid out in section 3.17 of this report;
- b) Approve the earmarking of £2m of the £9.877m General Reserve to invest in projects to support delivery of the Transformation Blueprint with authority to release this funding delegated to the Business Transformation Steering Group (BTSG) as laid out in section 5.2 of this report; and otherwise
- c) Note the contents of this report.

2 Purpose of Report / Executive Summary

- 2.1 The purpose of this report is to provide Council with information on performance against service revenue budgets in 2022/23 and to provide commentary on areas of material variance against budget. The budget performance figures as shown in appendix 1 result in a net underspend of £11.631 million. This is a £10.039 million improvement on the projected position at quarter 3 although £7.565 million relates to the one-off positions on VAT and Servitude income and also unbudgeted Waste third party income as explained in sections 3.3 to 3.8 below.
- 2.2 The most notable factors in the remaining favourable movement of £2.474 million are a further upside in loan charges and vacant posts, lower spend in educational settings and higher than anticipated distribution of previously undistributed Scottish Government Grant. Whilst very difficult to quantify, the moratorium on non-essential spend will also be significant. The underspend, excluding one-off's, is 1.51% of the revised budget.
- 2.3 The General Fund balance at 31st March 2023 is £34.194 million, of which £17.477 million is earmarked for specific use and a further £6.839 million relates to VAT claims leaving a non-earmarked General Fund balance of £9.877 million, of which Council are asked to earmark a further £2 million to support Transformation Blueprint work,

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3 Background

- 3.1 This report encompasses all performance against revenue budget for General Fund services including additional costs incurred and lost income as a consequence of the Covid-19 pandemic.
- 3.2 In response to the immediate and challenging financial outlook the Chief Executive introduced a moratorium on non-essential spend and a freeze on non-essential vacancies. The financial impact is reflected in this report.

Value Added Tax (VAT) on Leisure services

- 3.3 The Council has two claims with HMRC for overpaid VAT on sporting activities. These date back to around 2009 and have been the subject of ongoing legal debate until March 2023 when HMRC announced in Revenue and Customs Brief 3 (2023) that Local Authorities' leisure services are "provided under a statutory framework and can be treated as non-business for VAT purposes". In simple terms, for every £1 collected previously, an element for VAT was paid over to HMRC. Updated guidance allows the Council to retain the whole £1 and to reclaim VAT previously paid over to HMRC.
- 3.4 The two claims relate to:
 - the period from August 2006 to March 2023; and
 - the period from January 1981 to December 1989 (known as the Fleming period).
- 3.5 The cumulative value of the claims is £6.279 million. Once HMRC have finalised their review, interest will be added to each claim and a fee is payable to KPMG who have acted on behalf of the Council. The estimated net impact amounts to £6.839 million and that figure is included in the 2022/23 accounts.
- 3.6 As the claims are not yet settled by HMRC the Council has not received any cash. However, there is now enough certainty that cash will be received to necessitate accounting for income due in 2022/23. Until final settlement is received income will remain set-aside in the General Fund Balance. Once everything is finalised a full report will be presented to Council.

2022/23 one-off variances against budget

- 3.7 Council Officers from Midlothian and the City of Edinburgh Council (CEC), as part of the joint management and monitoring arrangements for the waste plant at Millerhill, have been working through calculations for third party income due. In financial year 2022/23 £0.879 million of unbudgeted income was paid to Midlothian. Income projections for future years are included in Medium Term Financial Strategy (MTFS) projections.
- 3.8 A one-off receipt of income of £0.573 million was received in respect of agreed legal right of access (servitude) across Midlothian Council land.

Performance against budget

3.9 The other main areas of variance against service budget for the year are:

Overspends

- There remains £0.671 million of MTFS cost reductions to be finalised mainly relating to Management Reviews across Place (£0.305 million), Sport & Leisure (£0.166 million) and also including a review of the Council's Creative Arts service (£0.200 million). Clearly the pandemic has impacted on progress with these but they are all now at implementation stage. These cost pressures are fully mitigated by the holding of vacancies pending completion of reviews;
- The volume and value of school pupil transport invoices was considerably higher than projected giving rise to an overspend of £0.738 million. An urgent root and branch review of the service is underway and is incorporated into the Transformation Blueprint;
- Sport and Leisure income remains lower in 2022/23 than budgeted by £0.628 million but is moving much closer to pre-covid levels. The income shortfall is fully offset by reduced running costs in leisure facilities;
- Additional budget of £1.058 million was provided by Council early in 22/23 to cover energy price increases. Continued price inflation during the year gave rise to a further £0.484 million of cost in excess of budget;
- Costs of vehicle repairs mainly relating to external works exceeds budget by £0.319 million. A service review is underway;
- Costs of software and licencing due to increased cyber security measures and a continued move to cloud-based software gives rise to an overspend of £0.303 million. Ongoing digital costs have been provided for in the MTFS;
- Insurance costs are over budget by £0.285 million due to provisions made for new or reopened claims on the Council. Whilst no individual claim is of particularly high value the volume of individual claims is higher than is customary. Council officers and loss adjusters review each claim with oversight by the Risk and Resilience Group;
- Council run cafes and the outside catering service have reopened after a long period of closure. Business is considerably slower than experienced pre-pandemic and may not fully recover leading to an overspend of £0.186 million. Management are reviewing the offering;
- Fuel purchase costs for the Council's fleet are £0.131 million in excess of budget. Supply costs increased considerably in the earlier part of the year although have now returned close to budgeted levels;

- Customer income from the Trade Waste service is lower than provided for in the budget. The customer base is contracting and management are reviewing the implications of this. The overspend is £0.113 million;
- Whilst the majority of the winter period required a normal level of emergency response the adverse winter conditions in December resulted in an overspend for Winter Maintenance of £0.103 million.

Underspends

- Significantly higher surplus cashflow than expected linked to lower than planned spend on Capital Programmes alongside a continued higher interest rate environment provided opportunity to generate a significantly higher return on short term deposits in 22/23 than was anticipated when the budget was set. Approved methodology for allocating Loan Charges between General Fund and Housing Revenue Account results in the majority of this upside benefitting the General Fund. There is an underspend of £1.812 million;
- Costs across the spectrum of learning settings for children and young people are lower than provided for in the budget mainly due to lower pupil numbers thus giving rise to a positive variance of £0.854 million;
- Waste disposal costs are lower than budgeted by £0.383 million. Lower volumes are being found in domestic waste streams possibly as an impact of household behaviours seen during Covid starting to unwind;
- Income from charges for Building Warrants exceeds budget by £0.348 million. Building Regulations changed in December 2022 and this may have prompted an influx of applications prior to the change;
- Focus on progressing the Residential Streets capital programme and weather conditions on the latter part of the financial year contributed to an underspend against the Roads Maintenance budget. External customer income in excess of budget for services provided brings the combined underspend to £0.347 million;
- When the budget was set the Council share of undistributed Scottish Government Grant was estimated. Actual distribution, most notably for Discretionary Housing Payments, was slightly higher. Total distributed Scottish Government Grant amounts to £195.436 million;
- The cost of residential, day education and family placements for children was £0.230 million less than budget with a continued push to recruit foster carers;
- Savings continue to accrue from the avoidance of use of Bed and Breakfast accommodation for homeless clients with an in-

year underspend of £0.183 million. The ongoing implications are reflected in the MTFS.

Covid Costs

- 3.10 Covid related funding provided to the Council by the Scottish Government alongside other funding streams aligned to Covid recovery were carried forward from 2021/22 to 2022/23. Funding continues to be applied in-year to match costs as applicable. The planning assumption remains that funding will be required in future years to mitigate the continued impact of the pandemic and to support increased service costs across Midlothian.
- 3.11 The main draw on the Covid budget during 2022/23 was funding for enhanced cleaning measures in sport and leisure facilities, schools and council offices put in place during the pandemic. Total supported spend was £0.927 million.

Pay + National Insurance

- 3.12 The 2022/23 pay claims for the Scottish Joint Council (SJC) bargaining group were settled during quarter 3. The agreed offer represents:
- For those on the Local Government Living Wage and pay scale point (SCP) 19 to 24 and undifferentiated 5% or a £2,000 uplift (calculated on a nominal 36 hour working week), whichever is larger;
 - A 10.2% increase for the lowest paid. For SCP 38 (£24,984) a 7.7% increase (£1,925) and for SCP 52 (£30,212) a 6.37% increase (£1,925); and
 - An undifferentiated 5% or a £1,925 uplift (calculated on a nominal 36 hour working week), whichever is larger, capped for those currently earning £60,000 or more at a £3,000 uplift (based on a 37 hour working week).

It is estimated that this equates to a 7.23% increase in the Council's SJC paybill.

- 3.13 The Scottish Negotiating Committee of Teachers (SNCT) settled on a flat offer of 7%. Payments to Teachers were made in April with costs accounted for in 2022/23.

Funding

- 3.14 A pay increase of 2.5% was provided for in the 2022/23 base budget. The Scottish Government have provided additional funding for 3.73% of the increased cost:
- £140m revenue funding nationally of which £2.401m flowed to Midlothian as part of general revenue funding;
 - £120.6 million of Capital Funding (Capital Flexibilities) of which £2.069 million flowed to Midlothian as a capital grant. A one-off flexibility option to allow capital grant to fund in-year revenue expenditure was developed with Scottish Government and CoSLA officials and has now been approved by Scottish Government Ministers.

- 3.15 The remaining 1% equated to £2.057 million and linked into ongoing national discussions around funding flexibilities. Progress with deliverable options available for Councils was very limited. The Scottish Government / CoSLA planning assumption was that there would be an option(s) that works for all Councils.
- 3.16 Council Officers reviewed areas of the available budget to fund pay. In the absence of workable funding flexibilities the following areas were used to fully fund costs:
- Employers National Insurance Savings;
 - Capital Receipts Flexibility;
 - One-off in-year savings; and
 - A review of 2021/22 budgets carried forward to 2022/23.

Capital Receipts Flexibility

- 3.17 Council previously approved the use of a financial flexibility permitting the use of capital receipts to fund projects designed to transform service delivery or reduce costs. Capital Receipts in 2021/22 of £0.554 million were set aside for this purpose. For the flexibility to apply funding must have been utilised by 31st March 2023.
- 3.18 There are very specific criteria set out in Scottish Government Finance Circular 7/2022 including:
- Expenditure must be non-recurring on a transformation / service redesign project where up-front costs generate ongoing savings or reduce demand;
 - Expenditure includes the set up and implementation costs of any new processes or arrangements, but not the ongoing revenue costs; and
 - A meeting of full Council must be provided with costs and benefits associated with individual projects eligible for this flexibility and provide formal approval.
- 3.19 A number of different areas of transformational work were initially considered appropriate for consideration:
- Client Travel Review;
 - Sport and Leisure Review;
 - Local by Default;
 - Commercialisation;
 - School week / curriculum review;
 - Climate Change;
 - Building Maintenance Review; and
 - Customer Services Project.

- 3.20 The projects outlined in Table 1 below were those that met eligibility conditions. Council are therefore asked to approve use of the capital receipts flexibility to fund these.

Table 1: Eligible Capital Receipts Flexibility Funded Projects

Project	Project Description / Benefits	2022/23 Cost (£)
Building Maintenance Review	Radical service redesign and modernisation of all processes within the Building Maintenance Service with the purpose of raising the business efficiency and effectiveness at all levels across the organisation.	137,067.14
Customer Services Project	In 2022/23 the multi-year project developed and delivered new FOI, Registrar and Contact Us modules. These all provide significant service enhancement and efficiency.	193,993.13
School Week Transformation	Drive transformational change in the design and delivery of the curriculum within secondary schools taking into account national development and digital solutions.	40,509.16
Climate Change – Zero Carbon	External support to develop the Council's ambition to make the Council's activities net carbon zero by 2030.	25,925.00
	Total	397,494.43

- 3.21 Approval of the use of Capital Receipts to fund costs shown in table 1 releases budget to fund pay as covered in sections 3.14 to 3.16 above.
- 3.22 In accordance with conditions of Finance Circular 7/2022 the unused value of £156,045.57 is added to the Capital Fund.

4 Delegation of resources to Midlothian Integration Joint Board

- 4.1 The approved budget provided for the allocation of £56.438 million to the Midlothian Integration Joint Board (MIJB) for the provision of delegated services. Minor technical adjustments to this allocation during the year to date increases the allocation to £56.611 million.
- 4.2 In accordance with the Integration Scheme the MIJB is required to deliver delegated services within the budget allocations from the Council and NHS Lothian and where any overspend is projected to put in place a recovery plan to address that. As a last resort the integration scheme allows for the MIJB to seek additional financial support from its partners, either by way of an additional budget allocation or by "brokerage" (provision of additional resources in a year which are repaid in the following year).
- 4.3 The MIJB financial position for 2022/23 will be reported to the MIJB Board on Thursday 22nd June. Outturn figures show an in-year underspend so there will be no requirement for an additional budget allocation from the Council.
- 4.4 Financial Monitoring reports covering all of the MIJB activity are presented to the Integration Joint Board and are available on the committee management section of the Council website:-

[Midlothian Integration Joint Board \(cmis.uk.com\)](https://cmis.uk.com)

5 General Fund Reserve

5.1 The balance on the General Fund as at 31 March 2023 is as follows:

	£ million	£ million
General Fund Reserve at 1 April 2022		32.432
<i>Planned movements in reserves</i>		
Application of Budgets carried forward from 2021/22 for use in 2022/23	(19.923)	
Funding of Corporate Solution for 2022/23 Budget	(4.689)	
Supplementary Estimate for Inflationary Pressures	(1.395)	
Supplementary Estimate for costs of the additional public holiday	(0.030)	
Other movements	0.027	
		(26.010)
Application of Business Transformation Funding to support service re-design		(0.268)
Underspend per appendix 1		11.631
In year budgets carried forward for use in 2023/24		16.409
General Fund Balance at 31 March 2023		34.194

An element of the General Fund is earmarked for specific purposes and this is shown below:

	£ million
General Fund Balance at 31 March 2023	34.194
<i>Earmarked for specific purposes</i>	
Budgets carried forward and earmarked for use in 2023/24	(15.243)
Set aside to balance 23/24 budget	(1.166)
To support Council Transformation	(1.069)
General Reserve at 31 March 2023	16.716
VAT Windfall not yet settled	(6.839)
Revised General Reserve at 31 March 2023	9.877

5.2 The Midlothian Council Transformation Blueprint presented to Council later on today's agenda incorporates MTFS projections of a budget gap of £29.121 million to 2028/29 and lays out the transformation themes and detailed projects within to tackle the financial challenge. Success in delivering change at pace will depend on significant up-front investment and some ongoing enabling costs. To create an initial fund for this it is recommended that Council earmark £2 million of the £9.877 million General Reserve and delegate governance to release these funds to BTSG.

- 5.3 The Reserves Strategy approved by Council on 12th February 2019 requires Council to maintain an adequate level of General Reserve to provide a contingency for unforeseen or unplanned costs. In the financial context at that time Council approved the adoption of 2% of the approved budgeted net expenditure (excluding resources delegated to the IJB) to be considered a minimum. This now equates to £4.178 million. Council also agreed that where projections indicate that should the 2% minimum General Reserve balance be breached an immediate recovery plan be implemented to recover the position, failing which, the next available budget would need to provide for the reinstatement of reserve position.
- 5.4 The General Reserve, excluding windfall VAT income, of £7.877 million (assuming Council approve earmarking of £2m to support the transformation blueprint) is well above the minimum set in the Reserves Strategy but will only remain that way if there is no further adverse performance against budget or any draw on reserves. Critically, it must also be viewed in the context of Council reaching a position of ongoing financial sustainability. The latest projected budget gap to 2028/29 is £29.121 million as laid out in the Transformation Blueprint.

6 Report Implications (Resource, Digital and Risk)

6.1 Resource

Performance against budget set out in this report presents the final position for the year. Work continues across the council to reduce overspends and to progress at pace delivery of approved savings.

Whilst this report deals with financial issues there are no financial implications arising directly from it.

6.2 Digital

Increased reliance and investment in digital solutions and digital first solutions will be a key element of future plans.

6.3 Risk

Section 95 of the Local Government (Scotland) Act 1973 requires all Local Authorities in Scotland to have adequate systems and controls in place to ensure the proper administration of their financial affairs.

The assessment of performance against budgets by services is underpinned by comprehensive financial management and budgetary control arrangements. These arrangements are central to the mitigation of financial risk.

Ensuring that adequate systems and controls are in place reduces the risk of significant variances arising, and where they do arise they help to ensure that they are identified and reported on and that appropriate and robust remedial action is taken. The primary purpose of this report

is to provide an assessment of performance against budget for the full year. The material variances detailed in the report highlight that the financial management and budgetary control arrangements require continual review and enhancement if financial risk is to be effectively mitigated during the year.

There are a some areas where effective forecasting of spend against budget is hindered due to incomplete service information which in previous years has resulted in previously unreported or significantly adjusted variances at the financial year end. Financial Management CMT continues to consider these areas and supports actions to address the underlying issues and mitigate the risk associated with them.

The financial projections are predicated on new burdens, including those arising from the Government's 100 day commitments to be fully funded. The position with outstanding pay awards and the potential for unfunded costs arising presents a significant risk to the Council's financial position.

The Council recognises the potential for compensation claims deriving from Scottish Government's Limitation (Childhood Abuse) (Scotland) Act 2017 which removes the three year time limit on claims of child abuse. Some claims will be historic and relate to Lothian Regional Council, Midlothian District Council or their predecessors and some will date post reorganisation and relate to Midlothian Council, and so presents a risk that would further reduce reserves from those currently projected. Further financial obligations may also arise as the implications associate with the The United Nations Convention on the Rights of the Child (Incorporation) (Scotland) Bill, which has yet to secure Royal Assent , are more fully understood.

6.4 Ensuring Equalities

As changes to existing plans are developed the assessment of the impact of these proposals in relation to their impact on equalities and human rights will be carried out. This will help to ensure wherever possible that there are no negative impacts on equality groups or potential for infringement of individuals' human rights from the any of the proposals.

6.5 Additional Report Implications

Appendix A – Report Implications
Appendix B – Financial Tables

APPENDIX A – Report Implications

A.1 Key Priorities within the Single Midlothian Plan

The existing financial plans support the delivery of the key priorities in the single Midlothian Plan. As the impact on the Council of the pandemic and recovery continues to unfold over the financial year any changes in the availability and allocation of resources will need to be considered in parallel to the actions proposed to continue to delivery key priorities.

A.2 Key Drivers for Change

Key drivers addressed in this report:

- ☒ Holistic Working
- ☒ Hub and Spoke
- ☒ Modern
- ☒ Sustainable
- ☒ Transformational
- ☒ Preventative
- ☒ Asset-based
- ☒ Continuous Improvement
- ☒ One size fits one
- ☐ None of the above

A.3 Key Delivery Streams

Key delivery streams addressed in this report:

- ☒ One Council Working with you, for you
- ☒ Preventative and Sustainable
- ☒ Efficient and Modern
- ☒ Innovative and Ambitious
- ☐ None of the above

A.4 Delivering Best Value

The report does not directly impact on Delivering Best Value.

A.5 Involving Communities and Other Stakeholders

The development of the Medium Term Financial Strategy reflected a community consultation exercise carried out in 2019 which has also helped shape the drafting of the “Midlothian Promise” and the early development of the Council’s Longer Term Financial Strategy.

In addition there is continues engagement with the recognised Trade Unions on the financial position.

A.6 Impact on Performance and Outcomes

The Financial Strategy facilitates decision on how Council allocates and uses its available resources and as such has fundamental implications for service performance and outcomes. The financial consequences of the pandemic will impact on the availability and allocation of resources in pursuit of key outcomes as set out in the Single Midlothian Plan for both the immediate and longer term and therefore the ability of the Council to continue to deliver services in a financial sustainable manner.

A.7 Adopting a Preventative Approach

Maintaining the effectiveness of the Financial Strategy will support the prioritisation of resources to support prevention.

A.8 Supporting Sustainable Development

There are no direct sustainability issues arising from this report and we will work to mitigate as far as feasible any sustainability issues which arise as a consequence of any of the changes to existing plans.