Notice of meeting and agenda

Audit Committee

Venue: **Council Chambers, Midlothian House, Dalkeith, EH22 1DN**

Date: **Tuesday, 21 March 2017**

Time: **11:00**

John Blair
Director, Resources

Contact:
Clerk Name: Janet Ritchie
Clerk Telephone: 0131 271 3158
Clerk Email: janet.ritchie@midlothian.gov.uk

Further Information:

This is a meeting which is open to members of the public.

Audio Recording Notice: Please note that this meeting will be recorded. The recording will be publicly available following the meeting. The Council will comply with its statutory obligations under the Data Protection Act 1998 and the Freedom of Information (Scotland) Act 2002.

1 Welcome, Introductions and Apologies

2 Order of Business

Including notice of new business submitted as urgent for consideration at the end of the meeting.

3 Declarations of Interest

Members should declare any financial and non-financial interests they have in the items of business for consideration, identifying the relevant agenda item and the nature of their interest.

4 Minutes of Previous Meeting

5 Public Reports

6 Private Reports

No private business submitted for discussion

Minute of Meeting

Audit Committee
Tuesday 21 March 2017
Item 4.1

Midlothian

Audit Committee

Date	Time	Venue
Tuesday 13 December 2016	11.00 am	Council Chambers, Midlothian House, Dalkeith, EH22 1DN

Present:

Peter Smaill (Independent Chair)	
Councillor Baxter	Councillor Bryant
Councillor de Vink	Councillor Milligan
Councillor Muirhead	

In attendance:

Stephen Reid	Ernst & Young LLP
Kenneth Lawrie	Chief Executive
John Blair	Director Resources
Mary Smith	Director Education, Communities and Economy
Graham Herbert	Internal Audit Manager
Elaine Greaves	Internal Audit Manager
Chris Lawson	Risk Manager
Heather Mohieddeen	Senior Auditor
James Polanski	Auditor
Amber Ahmed	Auditor
Ian Johnson	Head of Communities and Economy
Kevin Anderson	Head of Housing and Customer Services
Ricky Moffat	Head of Commercial Services
Janet Ritchie	Democratic Services Officer

1. Apologies

1.1 Apologies were received from Councillor Parry and Michael Thomas

2. Order of Business

The order of business was confirmed as outlined in the agenda that had been circulated.

3. Declarations of interest

The Chair declared that he has been adopted as the Conservative Unionist candidate for Midlothian East in the forthcoming local elections in May 2017.

4. Minutes of Previous Meetings

4.1 The minutes of the Audit Committee meeting of 20 September 2016 were approved as a correct record.

4.2 Matters Arising from previous Minutes:

Councillor Byrant referred to section 5.1 for comments with regards to the decision paragraphs (c) the position in relation to bad debt and (d) PPP commitments.

The Director Resources confirmed that with regards to the PPP commitments there is a management team proposal included in the Revenue Budget proposals for the next financial year which has been circulated to Members and with regards to bad debt this is reported routinely within the quarterly financial monitoring.

5. Reports

Report No.	Report Title	Submitted by:
5.1	Midlothian Council External Audit Framework overview	External Auditors, Ernst & Young LLP
Outline of report and summary of discussion		
There was a report submitted to the Audit Committee from the External Auditors dated December 2016 providing details of the evolving focus of the public sector external audit, the external auditor's approach over the term of their appointment and the initial areas of focus for the Council. The annual audit plan will be presented to the Audit Committee in March 2017 upon completion of the initial planning process. Stephen Reid, External Auditor, presented the report to the Committee summarising the audit framework contained within the report. Thereafter responded to questions raised by members of the committee which		

included: • The Accounts Commission's new model for Best Value audits and the work with Audit Scotland to support the review of Best Value at the Council. • The number of Local Authorities that Ernst & Young audit as well as Midlothian Council are: 3 Local Authorities in Scotland, 3 Integrated Joint Boards and 1 Pension Fund and in England approximately 60 Local Authorities. • The External Auditor explained that around significant risk under auditing standards you are required to identify and report on areas which represent a higher likelihood that there could be a material misstatement in the Financial Statement. This would include any risks of management overrides.
Decision
• To note the Report. • To note that a risk assessment would be undertaken and included in the External Auditor's Report to be brought back to the next meeting of the Audit Committee and this could be discussed in more detail from a Midlothian Council perspective.
Action
EY, External Auditors

Report No.	Report Title	Submitted by:
5.2	Risk Management, Update for 1 April 2016 – 30 June 2016	Chris Lawson, Risk Manager
5.3	Risk Management, Update for 1 July – 30 September 2016	Chris Lawson, Risk Manager
Outline of report and summary of discussion		
The Risk Manager presented the 2016/17 quarter 2 and quarter 3 reports to the Audit Committee providing strategic risk management updates for the periods 1 April to 30 June 2016 and 1 July to 30 September 2016. Thereafter responded to questions raised by the Members including: • The geological risk and if a more detailed geological assessment is required. • The risks associated with BREXIT. • The Risk Registers are used by Internal Audit when developing their annual internal audit plan. The Internal Audit Section also undertakes their own assessment of the risks facing Midlothian Council.		
Decision		
To note the quarter 2 and 3 /2016/17 Strategic Risk Profile report and to consider the current response to the risks and opportunities highlighted.		

Report No.	Report Title	Submitted by:
5.4	Maintaining Midlothian's Roads Update Report	Head of Commercial Operations

Outline of report and summary of discussion

The report dated 17 November 2016 was presented to the Audit Committee by the Head of Commercial Operations highlighting some of the key issues raised in the Audit Scotland 'Maintaining Scotland's Roads Update report' published in August this year. The report examines the changes in the condition of the road network since 2011, the current spend on roads maintenance and how the road maintenance service is managed.

Thereafter responded to questions raised by the Committee which included:

- The number of Insurance Claims received with regards to defective roads which was reported as low level in comparison to other Local Authorities,
- The amount spent on the roads network and the reason this is higher than other Councils.
- Guidelines on spending with regards to road repairs.
- Difference on the road deterioration and the weather conditions.
- The quality of Midlothian roads that are used by public transport and how this is monitored.

Decision

- Additional analysis was required on the spending on roads in Midlothian and why it is so expensive per kilometre.
- To otherwise note the Report

Action

Head of Commercial Services

Report No.	Report Title	Submitted by:
5.5	Anti Fraud and Corruption, Anti Bribery and Whistle blowing Policies	Internal Audit Manager

Outline of report and summary of discussion

The report dated 23 November 2016 was presented to the Audit Committee by the Internal Audit Manager on the Anti Fraud and Corruption, Anti Bribery and Whistle blowing Policies. These policies are reviewed regularly by the Internal Audit Section with assistance from Legal and Human Resources and updated with new national guidance as set out in the report. A separate Anti Bribery policy has been created following a recommendation from CIPFA.

Decision

- To Note the Anti Fraud and Corruption, Anti Bribery and Whistle blowing policies.

• To note that the Anti Fraud and Corruption and Anti Bribery policies will be submitted to Cabinet for approval following consultation with the Trade Unions.
Action
Internal Audit Manager

Report No.	Report Title	Submitted by:
5.6	Audit Scotland Report - National Fraud Initiative 2014/15	Internal Audit Manager
Outline of report and summary of discussion		
The Audit Scotland Report – National Fraud Initiative 2014/15 dated 8 November was presented to the Audit Committee by the Senior Auditor. The report provides a summary of how the Audit Scotland report relates to the work undertaken within Midlothian Council; to review the actions taken within Midlothian to address recommendations made in the Audit Scotland Report and to allow the Audit Committee to consider and comment on the draft self assessment questionnaire contained within the Audit Scotland report.		
Decision		
To note the Report.		

Report No.	Report Title	Submitted by:
5.7	Corporate Fraud – Annual Report	Internal Audit Manager
Outline of report and summary of discussion		
The Corporate Fraud Annual Report dated 17 October 2016 was presented by the Senior Auditor providing the Audit Committee with an update on the activities of the Corporate Fraud team over the past year and to seek input from the Audit Committee on areas where this resource could be used further. Thereafter a discussion took place regarding the systems in place to identify fraud and the processes for prosecution.		
Decision		
• To provide an update to the next meeting over the recovery of the 2 Council houses referred to in the report and whether any legal action was considered. • To otherwise note the content of the report.		
Action		
Internal Audit Manager / Head of Housing and Customer Services		

Report No.	Report Title	Submitted by:
5.8	Progress Update Report	Internal Audit Manager

Outline of report and summary of discussion

The Progress Update Report dated 21 November was presented by the Internal Audit Manager providing the Audit Committee with a summary of the work undertaken by the Internal Audit since April 2016 and an update on the progress with the current audit plan which was approved by the Audit Committee on 15 March 2016.

Decision

- To note the work completed by the Internal Audit Section since April 2016.
- To note the progress with the current plan.
- To note the suggested amendment to the audit plan.
- To note that the Internal Audit Manager will continue to provide updates if there is a risk of non delivery of the plan.

Report No.	Report Title	Submitted by:
5.9	Internal Audit Recommendations	Internal Audit Manager

Outline of report and summary of discussion

The Internal Audit Recommendations Report dated 16 November was presented by the Internal Audit Manager informing the Audit Committee of the number of recommendations raised by Internal Audit over the last 4 years and the Council's performance in addressing these issues by the agreed implementation dates.

Thereafter the Head of Communities and Economy responded to a question raised by the Committee which included:

- Developer's contributions and the processes in place in securing the contributions and they are spent appropriately.
- Income lost due to incorrect wording in agreements.
- Explanation of the actions with 0% progress noted which are low priority and are not significant risks.

Decision

- To note the content of the report.
- To note that Internal Audit will continue to monitor for completion of the outstanding issues and will provide reports to the Audit Committee.

Action

Internal Audit Team

Report No.	Report Title	Submitted by:
5.10	Internal Audit Report – Welfare Reform Universal Credits	Internal Audit Manager
Outline of report and summary of discussion		
The Internal Audit Report on Welfare Reform Universal Credits dated November 2016 was presented by the Internal Auditor to the Audit Committee which reviewed the adequacy of the controls in place over the implementation of Universal Credits. Thereafter the Head of Housing and Customer Services responded to concerns raised by the Committee with regards to Housing Benefits overpayments and these are currently not being recovered by the DWP from Universal Credit claimants and the high risk of rent arrears increasing as payments are made directly to claimants rather than the Council and the impact of this on housing.		
Decision		
To note the content of the report.		

Report No.	Report Title	Submitted by:
5.11	Internal Audit Report – Tyne Esk LEADER	Internal Audit Manager
Outline of report and summary of discussion		
The Internal Audit Report Tyne Esk LEADER dated 24 November was presented by the Internal Auditor to the Audit Committee which reviewed the internal controls in place for the administration of the Tyne Esk LEADER Programme. Thereafter the Head of Communities and Economy responded to a question raised by the Committee regarding clarity on the management costs.		
Decision		
To note the content of the Report.		

Report No.	Report Title	Submitted by:
5.12	Financial Monitoring 2016/17 and Financial Strategy 2017/18 to 2021/22	Director Resources
Outline of report and summary of discussion		
The report dated 16 November 2016 was presented to the Audit Committee by the Director Resources bringing to the committee's attention reports presented to Council on 8 November 2016 by the Head of Finance and Integrated Service Support, in relation to Financial Monitoring and Financial Strategy. The report refers to the following reports: • Financial Monitoring 2016/17 – General Fund Revenue • General Services Capital Plan 2016/17 • Housing Revenue Account		

- Financial Strategy 2017/18 to 2021/22
- Treasury Management Mid-Year Review Report

Thereafter the Director Resources responded to questions raised by the Committee on the deposits made with the German bank, 'Heleba'.

Decision

- To provide a link to the Treasury Management Investment Strategy when issuing the minute:
  Treasury Management Investment Strategy 2016/17 and Prudential Indicators – Midlothian Council 8 March 2016.
- To provide a briefing note on the Heleba Investment.
- To otherwise note the reports.

Action

Director Resources

6. Private Reports

No private reports were submitted to this meeting.

The meeting terminated at 12:23 pm

Midlothian Council

Year ending 31 March 2017

Annual Audit Plan

Audit Committee – 21 March 2017

Building a better working world

Public sector audit framework	Pages 3-5

The Code of Audit Practice (the Code) http://www.audit-scotland.gov.uk/report/code-of-audit-practice-2016 sets out the responsibilities of audited bodies, in accordance with statute and other relevant guidance, in respect of the preparation of financial statements.

We issue our audit opinion on the 'truth and fairness' of the Council's financial statements in accordance with management's timetable, and by 30 September 2017.

The nature of public sector audit means that the focus of audit work is broader than just the financial statements of the Council.

We report on the four dimensions of public sector audit as set-out jointly by the Accounts Commission and the Auditor General for Scotland.

Judgements in respect of Best Value are formed from the findings in respect of each of the four dimensions.

Understanding the Council	Pages 6-7

The financial environment for local authorities continues to be challenging. In this context, the Council's priorities set out in Single Midlothian Plan are designed to be responsive to its changing demographic profile.

Our audit approach responds to our understanding of the Council, such as how the Council is supporting service improvement through capital investment, including the programme for building new council houses.

Partnership working is also key, including the embedding of Integration and Social Care through the Midlothian Integration Joint Board.

Financial statements audit	Pages 8-14

Materiality

Planning Materiality for the audit has been determined at £5.0 million, representing 1.75% of estimated gross expenditure. Tolerable Error is set at £2.5 million, being 50% of PM. Our Summary of Audit Differences (SAD) nominal amount, set in line with the Code, is £250,000.

Risk assessment

Significant risks - In line with auditing standards we identify significant risks in respect of fraud in revenue recognition, and in respect of the risk of management override of controls. At this stage of our audit planning, we have not identified any other significant risks which we are required to report to you. We will update our risk assessment as part of our Annual Audit Report.

Inherent risks - The valuation of property, plant and equipment, and also of pension liabilities, are assessed as inherent risks. Management involves specialists in the preparation of these accounting valuations and estimates. We will utilise our own specialists, as appropriate, to support the core audit team in the performance of audit procedures on these balances.

Audit approach

Management has primary responsibility for the prevention and detection of fraud. We design appropriate audit procedures in response to identified fraud risk factors, for the purpose of detecting material misstatements.

There are no significant changes to the Accounting Code of Practice for 2016/17 although a new expenditure and funding analysis is required. We will obtain an understanding of management's readiness to implement the proposed change in accounting for Highways Network Assets as this is technically complex.

We obtain an understanding of your internal control arrangements, both as they apply across the Council, but also in terms of key processes.

We test key controls where appropriate to reduce the extent of substantive testing required. In addition we apply data analytics to capture and analyse whole populations of financial data.

We liaise with internal audit to ensure our approach takes account of risks identified and findings reported.

In respect of the Council's group financial statements, based on the 2015/16 financial statements and our knowledge of the business, we have scoped Midlothian Integration Joint Board into our group audit work. We have also been appointed as external auditor to the Integration Joint Board.

Wider scope audit framework	Pages 15-17

The wider scope audit as set out in the Code plays a key role in the public sector audit framework in Scotland. As part of this, as the appointed auditor, we contribute to the Local Area Network Shared Risk Assessment.

We have identified two wider scope audit focus area in respect of financial management and financial sustainability. Our Annual Audit Report will contain the findings from our work performed over these areas. Our Annual Audit Report, and those in subsequent years, will contain the core findings making up the BVAR report when this is formally scheduled by the Accounts Commission.

The specifics of the work to be undertaken in respect of the other audit dimensions, and in response to the Accounts Commission's strategic priorities, will be communicated on completion of the current risk assessment, and from input gained from senior management.

The quality of self-evaluation by the Council is considered a key aspect to demonstrating Best Value. We will pay particular attention to the effectiveness of the Midlothian's self-assessment.

Other audit responsibilities	Pages 18-19

We will include in our reporting to you any significant findings or issues in respect of the Council's arrangements for Following the Public Pound, publication of Statutory Performance Information or participation in the National Fraud Initiative.

We will report to you on the certification of various grant claims and the Council's Whole of Government Accounts.

Team, fees and deliverables	Pages 20-22

Stephen Reid is your audit engagement partner, supported principally by Keith Macpherson and John Boyd.

We have agreed an auditor remuneration fee element of £140,080. This results in a total audit fee, inclusive of pooled costs, central performance audit and Best Value costs and central support costs, of £225,820 (*2015/16 actual*: £241,760).

Appendices	Pages 23-27

We confirm our independence to act as your external auditor.

We provide you with details of the key communications we are required to provide you with in accordance with Auditing Standards.

About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Midlothian Council (the Council) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

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

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

Complaints

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

1. Public sector audit framework

1. Public Sector Audit Framework

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as Midlothian Council's (the Council) external auditor for the five year period 2016/17 to 2020/21.

We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; relevant Auditing Standards and applicable Practice Notes issued by the Auditing Practices Board; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Plan, prepared for the benefit of Council management and the Audit Committee, sets out our proposed audit approach for the audit of the financial year ending 31 March 2017, in accordance with the responsibilities placed on us through the public sector audit framework in Scotland.

Financial statements audit

The Council's responsibilities

The Council is responsible for the preparation of the financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation. The Code also sets out the Council's responsibilities for maintaining accounting records and supporting working papers that have been prepared to an acceptable professional standard.

The Council is also required to prepare and publish, along with the financial statements, an annual governance statement, management commentary and a remuneration report that are consistent with the disclosures within the financial statements.

Management, with the oversight of the Audit Committee, should ensure communication of relevant information to users about the Council and its financial performance.

Our responsibilities

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

- whether they give a true and fair view of the financial position of the Council and its group as at 31 March 2017 and its expenditure and income for the year then ended; and
- whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2016/17 Code of Practice on Local Authority Accounting in the United Kingdom.

We also review and report on the consistency of the other information prepared and published by the Council along with its financial statements.

The Local Authority Accounts (Scotland) Regulations 2014 (the Regulations)

In accordance with the Regulations 2014, the signed unaudited annual financial statements should be submitted to the external auditor no later than 30 June 2017. Furthermore, the unaudited annual financial statements should be considered by an appropriate committee of the Council by 31 August 2017.

The Regulations also set out the requirements for approval of the audited financial statements. The Council, or relevant committee, is required to approve the audited annual financial statements for signature no later than 30 September 2017. In making their consideration, the Regulations require elected members to have regard to any report made, or advice provided by the proper office of the Council and the auditor.

To support elected members in discharging these responsibilities, we will report to elected members the findings of our audit in our Annual Audit Report.

Key messages

The Code of Audit Practice (the Code) http://www.audit-scotland.gov.uk/report/code-of-audit-practice-2016 sets out the responsibilities of audited bodies, in accordance with statute and other relevant guidance, in respect of the preparation of financial statements.

We issue our audit opinion on the 'truth and fairness' of the Council's financial statements in accordance with management's timetable, and by 30 September 2017.

Together the Accounts Commission and the Auditor General for Scotland agreed the four dimensions set out in the Code which comprise the wider scope audit for public sector in Scotland. These are:

- financial sustainability;
- financial management;
- governance and transparency; and
- value for money.

In local government, audit work over the four dimensions leads to an overall assessment of Best Value.

Wider scope audit

The Council's responsibilities

The Code sets out the broader responsibilities of the Council in respect of ensuring proper financial stewardship of public funds. In particular the Council should establish proper arrangements:

- for ensuring the proper conduct of its affairs, including the legality of activities and transactions and for monitoring the adequacy and effectiveness of these arrangements;
- for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct;
- to ensure that their financial position is soundly based having regard to, for example, balances and reserves including strategies about levels held and their future use and how they plan to deal with uncertainty in the medium and longer term; and
- for securing Best Value in accordance with the Council's statutory duty, including the preparation and publication of performance information in accordance with directions issued by the Accounts Commission.

Our responsibilities

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

Financial management	Financial sustainability	Governance and transparency	Value for money
We conclude on the effectiveness of financial management arrangements. This includes considering whether there is sufficient financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively.	We consider the medium and longer term outlook to determine if planning is effective to support service delivery. This will focus on the arrangements to develop viable and sustainable financial plans.	We review the adequacy of governance arrangements. In particular, we consider and report on; whether these are appropriate and operating effectively and that there is effective scrutiny, challenge and transparency on decision-making.	We consider whether value for money can be demonstrated in the use of resources. This includes the extent to which there is an alignment between spend, outputs and outcomes delivered and that there is a clear focus on improvement.

Key messages

The nature of public sector audit means that the focus of audit work is broader than just the financial statements of the Council.

We report on the four dimensions of public sector audit as set-out jointly by the Accounts Commission and the Auditor General for Scotland.

Judgements in respect of Best Value are formed from the findings in respect of each of the four dimensions.

2. Understanding the Council

2. Understanding the Council

In accordance with the principles of the Code, our audit work is designed to be proportionate and risk based. It is based on an understanding of the strategic environment in which the Council operates.

Through our knowledge and experience, plus our assessment of how the wider environment impacts on individual local authorities, we tailor our approach to risk assessment.

Through discussion with senior management, and from review of corporate planning documents, we develop an understanding of your priorities and the specific challenges which the Council faces.

Strategic context

The Council continues to operate in a challenging environment. There has been continued pressure on the local government finance settlement in recent years. Changes in population demographics across Scotland increases the need and demand for certain services. Management of both cost and demand pressures while maintaining and improving local government services is therefore highly challenging.

Audit Scotland's Financial Overview 2015/16 highlights that while the financial health of local government was generally good in 2015/16, there is a variation in the extent to which demand and cost pressures affect individual councils and also to the extent to which councils are prepared for tougher times ahead.

Social work and social care remains a pressure point. Net spending on this service area has increased by 8.6% since 2011/12. 2016/17 represents the first full year of operation of integration authorities, established to take forward the Scottish Government's programme of reform in respect of Integration of Health and Social Care.

The uncertainty of Brexit, within a broader geo-political environment, also has the ability to affect financial markets. This may result in significant changes, and volatility, in financial assets and liabilities of local authorities.

Understanding the Council's priorities

The council, and its community planning partners, have integrated the Single Outcome Agreement (SOA), Midlothian Community Plan and Midlothian Council Corporate Strategy into a single document: the Single Midlothian Plan. The Single Midlothian Plan includes five overarching thematic groups which support the achievement of outcomes. The themes are:

- Adult Health, Care – Responding to growing demand for the adult social care and health services.
- Community Safety – Ensuring Midlothian is a safe place to live, work and grow up in.
- Getting it Right for Every Midlothian Child – Improving outcomes for children, young people and their families.
- Improving Opportunities for People in Midlothian – Creating opportunities for all and reducing inequalities.
- Sustainable Growth and Housing – Growing the local economy by supporting business growth and responding to growing demand for housing in a sustainable environment.

The 2016/17 Single Midlothian Plan includes the Council's top three priorities for 2016-19. These are: Reducing the gap in learning outcomes; reducing the gap in health outcomes; and reducing the gap in economic circumstances. Delivery of these priorities will represent a significant challenge given cost and demand pressures faced by the Council.

Key messages

The financial environment for local authorities continues to be challenging. In this context, the Council's priorities set out in the Single Midlothian Plan are designed to be responsive to its changing demographic profile.

Our audit approach responds to our understanding of the Council, such as how the Council is supporting service improvement through capital investment, including the further phase of new council homes. Partnership working is also key, including the embedding of Integration and Social Care through the Midlothian Integration Joint Board.

3. Financial statements audit

3. Financial statements audit

We provide an opinion on the financial statements as to whether they give a true and fair view of the financial position of the Council, and its group, and whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2016/17 Code of Practice on Local Authority Accounting in the United Kingdom. We also review and report on the consistency of the other information prepared and published by the Council along with its financial statements.

We undertake our financial statements audit work in accordance with the four phases of EY's Global Audit Methodology: *Planning*; *Identification and assessment of risk*; *Design and execution of our response to those risks*; and *Conclude and communicate*.

Planning our audit work

Initial planning, independence and quality assurance

Our initial planning for any audit engagement includes client and engagement acceptance, which includes our documentation of the service requirements. We did not identify any specific audit risks arising from these procedures.

Part of these procedures are designed to ensure compliance with all relevant ethical standards, including independence which we assess for both EY as a firm and the individuals assigned to the audit. We set out more information on our independence in Appendix A.

We identify the team with primary responsibility for performance of the audit. Stephen Reid is the audit partner-in-charge.

Materiality

In accordance with ISA 320 we apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion. Materiality is the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. We determine:

- Planning materiality (PM) – this is set for the financial statements as a whole, and is used to set the scope for our audit. We have determined this to be £5.0 million, representing 1.75% of estimated gross expenditure.
- Tolerable Error (TE) – materiality at an individual account balance, which is set so as to reduce to an acceptably low level that the aggregate of uncorrected and undetected misstatements exceeds PM. We have set this at 50% of PM, being £2.5 million, based on our initial risk assessment at the Council.
- Summary of Audit Differences (SAD) Nominal amount – this is the amount below which misstatements, whether individually or accumulated with other misstatements, would not have a material effect on the financial statements. The Code requires that auditors report at no more than £250,000.

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

The amount we consider material at the end of the audit may differ from our initial determination. At the end of the audit we will form, and report to you, our final opinion by reference to all matters that could be significant to users of the financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

Key messages

Planning Materiality for the audit has been determined at £5.0 million, representing 1.75% of estimated gross expenditure.

Tolerable Error is set at £2.5 million, being 50% of PM.

Our SAD nominal amount, set in line with the Code, is £250,000.

We outline our initial assessment of the financial statement risks facing the Council, identified through our knowledge of the environment in which the Council operates; discussion with those charged with governance and officers; and through handover and transition arrangements with your previous auditor.

Our risk assessment is ongoing throughout the conduct of our audit and we will report to you any notable changes in our risk assessment during the course of our work.

Risk assessment includes the requirement to consider whether the financial statements as a whole are free of material misstatements whether caused by fraud or error.

Financial statement risks

Auditing standards require us to consider whether any of the risks identified are 'significant' risks to our audit of the Council and the group. Financial statement significant risks are defined as those with a higher likelihood of occurrence and, if they were to occur, a higher magnitude of impact which could result in a material misstatement of the financial statements.

We are required to perform specific procedures over those risks. These include the identification and testing of the design and implementation of key controls designed to address the risks plus performance of additional substantive procedures in response to the specific risk. We are also required to specifically highlight these significant risks to 'those charged with governance' i.e. the Audit Committee.

Significant risks (including fraud risks)	Our audit approach
Risk of fraud in revenue recognition	
Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. We rebut the risk of improper recognition of revenue in respect of core grant funding from the Scottish Government, as well as in respect of council tax and non-domestic rate income.	We will: ► Review and test revenue and expenditure recognition policies. ► Review and discuss with management any accounting estimates on revenue or expenditure recognition for evidence of bias. ► Develop a testing strategy to test material revenue and expenditure streams. ► Review and test revenue cut-off around the year end.
Risk of management override	
As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement. We also consider the potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.	Our approach will focus on: ► Testing the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. ► Reviewing accounting estimates for evidence of management bias, including management's retrospective consideration of prior year estimates. ► Evaluating the business rationale for any significant unusual transactions. ► Reviewing capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised.

Key messages

Significant risks:

In line with auditing standards we identify significant risks in respect of fraud in revenue recognition, and in respect of the risk of management override of controls.

At this stage of our audit planning, we have not identified any other significant financial statement risks. We will confirm our updated risk assessment as part of our Annual Audit Report.

Our risk assessment is ongoing throughout the conduct of our audit and we will report to you any notable changes in our risk assessment during the course of our work.

Risk assessment includes the inherent risk relating to the susceptibility of a transaction, disclosure or account balance in the financial statements to material misstatement. These inherent risks are broader in nature than significant risks, but require tailored audit procedures to be performed.

In accordance with Auditing Standards, we perform specific procedures on opening balances as this is the first year of our audit.

Other financial statement risks – inherent risks	Our audit approach
Valuation of property, plant and equipment	
The Council's property portfolio totals £0.6 billion as at 31 March 2016, with the major elements of this being in respect of Council Dwellings, Other Land and Buildings and Infrastructure assets. Given the size of this balance and the fact that a number of assumptions are made in the valuation, we assign a higher inherent risk to property, plant and equipment. We do not, however, at the planning stage have any specific concerns over management's approach to property valuations. **New fixed asset register** During 2016/17, the Council is replacing the existing fixed asset application, Logotech, with a Capita based platform. It is important that asset valuations and balances are transitioned completely and accurately to the new platform and that the application appropriately records property, plant and equipment transactions.	For the valuation of property, plant and equipment, our approach will focus on: ► Analysis of the source data and inquiries as to the procedures used by management's specialist to establish whether the source date is complete. ► Assessment of the reasonableness of the assumptions and methods used, including their compliance with the Accounting Code of Practice. ► Consideration of the appropriateness of the timing of when the specialist carried out the work. ► Assessment of whether the substance of the specialist's findings are properly reflected in the financial statements. For the new fixed asset register, our approach will focus on: ► Reviewing the reconciliation between the new and old asset registers to confirm completeness and accuracy of the data migration. ► Testing of the new application to ensure that fixed asset transactions including: depreciation, additions and disposals have been correctly reflected on the register/
Valuation of pension liabilities	
The net pension liabilities on the Balance Sheet arising from participation in the Lothian Pension Fund were £68 million. Following the result of the EU Referendum in June 2016, we saw significant changes in certain economic assumptions used in the valuation of pension liabilities. We anticipate that, in particular, with discount rates being much lower than as at 31 March 2016, the Council will experience a significant increase in the net pension liabilities at the upcoming year end.	Our audit approach will focus on: ► Analysis of the payroll and pensions source data and making inquiries as to the procedures used by management's specialist to establish whether the source date is relevant and reliable. ► Assessment, using EY pensions specialists, of the reasonableness of the assumptions and methods used. ► Assessment of whether the substance of the specialist's findings are properly reflected in the financial statements.

First year audit procedures

As a first year audit, we also have additional procedures to perform in respect of opening balances. We follow Audit Scotland's protocol for handover from previous auditors and have already held discussions with your former external auditor.

Key messages

Inherent risks:

The valuation of property, plant and equipment, and also of pension liabilities, are assessed as inherent risks. Management involves specialists in the preparation of these accounting valuations and estimates.

We will utilise our own specialists, as appropriate, to support the core audit team in the performance of audit procedures on these balances.

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. We assess the fraud risk factors affecting the audit of the financial statements.

We remain aware of changes to the Accounting Code of Practice which impact on the preparation of financial statements. Our aim is to discuss such changes with finance and senior management in advance, to assist in the smooth conduct of the audit.

Responsibilities in respect of fraud and error

Management has primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. As auditors, we approach each engagement with a questioning mind that accepts the possibility that a material misstatement due to fraud could occur, and design the appropriate procedures to consider such risk.

Based on the requirements of auditing standards our approach will focus on:

- Identifying fraud risks during the planning stages.
- Enquiry of management about risks of fraud and the controls to address those risks.
- Understanding the oversight given by those charged with governance of management's processes over fraud.
- Consideration of the effectiveness of management's controls designed to address the risk of fraud.
- Determining an appropriate strategy to address any identified risks of fraud.
- Performing mandatory procedures regardless of specifically identified risks.

Highways Network Assets (HNA)

In November 2016, CIPFA/LASAAC approved the postponement of the full implementation of the move to measuring Highways Network Assets at depreciated replacement cost until 2017/18, at the earliest. This resulted in a late change to the current Accounting Code of Practice to remove the requirement for 2016/17.

The purpose of the change is intended to be threefold: to improve management of HNA, to reflect the requirements of IFRS, and to go towards the removal of the audit qualification on the Whole of Government Accounts (WGA).

While there is no requirement on the Council to change their accounting for 2016/17, we will engage with the finance and estates teams to understand the Council's state of readiness to implement what represents a major change to the financial reporting framework.

Changes to the Accounting Code of Practice in 2016/17

We will engage with management to consider their assessment and incorporation of changes to the 2016/17 Accounting Code. Principal amongst these is the introduction of a new expenditure and funding analysis to enable greater transparency and linkage to the management commentary on the performance of the Council. In addition, the comprehensive income and expenditure statements will now provide a service analysis in line with the basis of the Council's operational structure.

Key messages

Management has primary responsibility for the prevention and detection of fraud. We design appropriate audit procedures in response to identified fraud risk factors, for the purpose of detecting material misstatements.

There are no significant changes to the Accounting Code of Practice for 2016/17 although a new expenditure and funding analysis is required. We will obtain an understanding of management's readiness to implement the proposed change in accounting for Highways Network Assets as this is technically complex.

Our approach is designed to develop an audit strategy that is responsive to the Council's risks of material misstatement for transactions and account balances in the financial statements.

In addition, we plan and perform certain general audit procedures on every audit to address areas that are not directly related to financial statement account assertions.

Examples of such procedures include aspects of audit work which are not directly related to the financial statements, such as compliance with applicable laws and regulations, litigation and claims and related parties.

Overview of audit approach

We determine which accounts, disclosures and relevant assertions could contain risks of material misstatement based on our understanding of the business, understanding of entity-level controls and our determination of planning materiality.

We establish an understanding of the five components of internal control, as they apply within the Council: control environment; risk assessment, monitoring; information and communication; and control activities. In particular we understand those controls which operate across the organisation and establish the tone and culture of the organisation, rather than addressing specific transactions entered into by the Council.

Processes

Our initial assessment of the key processes across the Council has identified the following key processes where we will seek to test key controls, both manual and those which are dependent on IT systems:

- Expenditure approval and creditors payments.
- Payroll.
- Cash receipting and payments.
- Accounts receivable.

Data analytics

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular covering journal entries, payroll and expenditure. These tools:

- Help identify specific exceptions and anomalies to direct more traditional substantive audit tests.
- Give greater likelihood of identifying errors than random sampling techniques.

We have held initial planning discussions with your IT and systems accountants to agree the practicalities of data provision.

Internal audit

We will review internal audit plans and the results of their work, including the discussion of audit findings at the Audit Committee and management's response to findings.

As this is the first year of our appointed, our assessment of internal audit will be more detailed to enable greater reliance on the work of internal audit to be integrated into our audit in subsequent years. In particular, where necessary, we will provide comment to the internal audit manager to ensure audit sample sizes meet our own requirements for the extent of audit testing over key controls. We will consider the impact of the ongoing Internal Audit Service review as well as Internal Audit's self-assessment against the Public Sector Internal Audit standards.

Key messages

We obtain an understanding of your internal control arrangements, both as they apply across the Council, but also in terms of key processes.

We test key controls where appropriate to reduce the extent of substantive testing required. In addition we apply data analytics to capture and analyse whole populations of financial data.

We liaise with internal audit to ensure our approach takes account of risks identified and findings reported.

The Accounting Code of Practice requires local authorities to prepare group accounts to take account of the assets and liabilities, income and expenditure, and cashflows of the authority and its subsidiary undertakings, as well as the investments that may be held in associates or joint ventures.

Our audit methodology requires us to understand the various components which make up the group boundary, and to determine which components should be included in the scope of the group audit, and the work to be performed on those components.

Audit process overview (*cont.*)

Use of specialists

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. We expect to use EY specialists in the following areas:

- *Valuation of property, plant and equipment:* The Council's land and buildings are subject to a rolling programme of revaluation, using either internal or external experts. We focus our audit work on the revaluations undertaken within the financial year and involve EY valuations specialists as appropriate, depending on the extent and complexity of the assets valued.
- *Valuation of pension liabilities:* The Council uses actuarial specialists to obtain a valuation of the share of the pension assets and liabilities in the Lothian Pension Fund. We utilise EY pensions team to review the actuarial assumptions adopted in the financial statements.

Management may use their own specialists in these, and other, areas of the preparation of the financial statements, for example in the valuation of certain financial instruments.

Group financial statements

For the purposes of consolidation and incorporation into the group financial statements, the Council has assessed that due to the small value of transactions for Pacfici Shelf 826 and the small share of net assets of Lothian Valuation Joint Board in 2015-16 it was considered unnecessary to provide a full set of group accounts.

The Midlothian Integration Joint Board was not material to the 2015/16 financial statements, however, this will change in 2016/17. We have been appointed as auditor to the Midlothian Integration Joint Board and will report separately on our audit of that entity.

On the grounds of materiality, the Midlothian Integration Joint Board has been scoped into the group financial statements audit.

Key messages

In respect of the Council's group financial statements, based on the 2015/16 financial statements and our knowledge of the business, we have scoped Midlothian Integration Joint Board into our group audit work. We are the appointed auditor of the Integration Joint Board and so our work will be aligned to that required for the group audit.

4. Wider scope audit work

Together the Accounts Commission and the Auditor General for Scotland agreed the four dimensions set out in the Code which comprise the wider scope audit for public sector in Scotland. These are: financial sustainability, financial management, governance and transparency, and value for money.

In local government, the Accounts Commission has also agreed its five Strategic Audit Priorities, which should be incorporated in audit planning.

Our annual audit work in respect of the wider scope audit, and the judgements and conclusions reached in these areas, contribute to the overall assessment and assurance on Best Value. This will draw on wider evidence or assurance gained through the Local Area Network's shared risk assessment.

Wider scope audit work - context

In undertaking our work in respect of the four audit dimensions, we draw your attention to the Accounts Commission's recently published Strategic Audit Priorities, being:

- The clarity of council priorities and quality of long-term planning to achieve these.
- How effectively councils are evaluating and implementing options for significant changes in delivering services.
- How effectively councils are ensuring members and officers have the right knowledge, skills and time to lead and manage delivery of the council priorities.
- How effectively councils are involving citizens in decisions about services.
- The quality of council public performance reporting to help citizens gauge improvement.

Shared Risk Assessment (SRA)

As your external auditor we participate in the Local Area Network (LAN). The LAN brings together representatives from across different scrutiny bodies to agree a Shared Risk Assessment (SRA) for each local authority. The SRA informs the local scrutiny plan ensuring that for any risks identified there is an appropriate scrutiny response.

Our audit planning activity will both inform and build upon the SRA for the Council, ensuring that there is a co-ordinated approach to assurance activity.

At the time of preparation of this report, the work of the Local Area Network (LAN) in preparing the SRA for the Council, together with the Local Scrutiny Plan setting the scrutiny response, has not yet been completed. Working with the LAN lead, held by the Care Commission, we will update the Council on this on completion.

Best Value Assurance Report

Under the new approach to Best Value auditing in local government, the Controller of Audit will provide a Best Value Assurance Report (BVAR) for each council at least once in a five year period. Midlothian Council has not been selected as one of six councils to be subject to a BVAR report in the first year of the new arrangements. We will be in discussion with management as the timetable for future local authority BVAR work becomes more certain.

In practice, it is expected that the content of the BVAR will be drawn principally from the findings of our audit as reported through our Annual Audit Reports up until that point. This report will also include conclusions drawn from any work performed by other scrutiny bodies as a result of the SRA, or through integrated working with Audit Scotland.

Key messages

The wider scope audit as set out in the Code plays a key role in the public sector audit framework in Scotland. As part of this, as the appointed auditor, we contribute to the Local Area Network Shared Risk Assessment.

Our Annual Audit Report, and those in subsequent years, will contain the core findings making up the BVAR report when this is formally scheduled by the Accounts Commission.

Audit work in respect of the four dimensions is designed to be proportionate and risk based.

The Code sets out an expectation that 'significant' risks identified through our planning process that relate to the wider scope dimensions will be communicated with you.

To distinguish between the definition of significant risks to the audit of the financial statements, as set out in Auditing Standards and to which the concept of materiality applies, we refer in our report to 'Wider Scope Audit Focus Areas'. While we undertake work across the dimensions of public audit on an annual basis, the focus areas will represent the issues where we direct most of our audit effort.

Wider scope audit risks

The Code requires us to undertake work in respect of each of the four dimensions on an annual basis. Where we identify, however, specific higher risk areas in relation to any of these dimensions, the Code requires us to communicate these to you.

Wider Scope Audit Focus Areas	Our audit approach
Financial sustainability	
The Local Scrutiny Plan for the Council for 2016/17 included financial sustainability as an area of continuing focus by scrutiny bodies. In the 2017/18, the Financial Strategy reported to Council in February 2017, estimated the budget gap through to 2021/22 as £30.498 million. With significant savings required to balance the budget going forward, we have identified this as a wider scope audit focus area for the first year of our audit.	Our approach will focus on: ► The effectiveness of the financial planning systems and identifying and addressing risks to financial sustainability across shorter and longer terms. ► Whether the Council can demonstrate the affordability and effectiveness of funding and investment decisions that it has made. ► The appropriateness of the arrangements to address identified funding gaps and whether the body can demonstrate that these arrangements are working.
Financial management	
For 2016/17, the Council is forecasting a net overspend of over £1.7 million. This is due to demand on services exceeding expectation as well as slippages in the transformational savings programme. The Council has recognised the financial pressures faced in the current years. In order to effectively manage these challenges, it is essential that the Council has effective budgetary processes and robust internal controls that operate effectively. We have therefore identified this as a wider scope audit focus area for the first year of our audit.	Our approach will focus on: ► whether the audited body has arrangements to ensure systems of internal control are operating effectively ► whether the body can demonstrate the effectiveness of the budgetary control system in communicating accurate and timely financial performance ► how the audited body has assured itself that its financial capacity and skills are appropriate ► whether the body has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

Other aspects of the wider scope audit

- **Governance and Transparency** - Members and officers are responsible for establishing robust governance arrangements. This includes ensuring effective systems of internal control, including arrangements to safeguard public money, and compliance with applicable laws and regulations.
- **Value for Money** – this dimension is focused on how the Council effectively utilises its resources and the arrangements in place to continually improve services.

Key messages

We have identified one wider scope audit focus area in respect of financial sustainability and financial management. The specifics of the work to be undertaken in respect of the other audit dimensions, and in response to the Accounts Commission's strategic priorities, will be communicated on completion of the current risk assessment, and from input gained from senior management.

The quality of self-evaluation by the Council is considered a key aspect to demonstrating Best Value. We will pay particular attention to the effectiveness of Midlothian's self-assessment.

5. Other audit responsibilities

5. Other audit responsibilities

Under the terms of our appointment, our role and responsibilities extend beyond the audit of the financial statements and the wider scope audit dimensions.

There a number of further areas of audit activity that we will cover over the term of our appointment. These include our responsibilities in relation to Following the Public Pound, Statutory Performance Information, the National Fraud Initiative and the impact of national studies undertaken by Audit Scotland.

In addition, a number of other assurance activities are included in the terms of our appointment. These include the certification of certain grant claims and the Council's Whole of Government Accounts return.

Following the Public Pound

Local Authorities have a statutory responsibility to comply with the Accounts Commission / COSLA Code of Guidance on Funding External Bodies and Following the Public Pound (the FtPP Code). The principles of the FtPP Code are embedded into the new approach to auditing Best Value. As part of our risk based planning approach we will consider the Council's arrangements to comply with the FtPP Code.

Over our five year appointment, Audit Scotland undertake performance audits across authorities for which we will be required to provide supporting information. During 2017, Audit Scotland will be undertaking a performance audit relating to Arms Length Organisations (ALEOs).

We link this work directly to that undertaken to support the conclusions on the Governance and Transparency audit dimension.

Statutory Performance Information

Local authorities have a responsibility, under their Best Value duty, to report performance to the public. One of the Accounts Commission's Strategic Audit priorities is 'the quality of council public performance reporting to help citizens gauge improvement'.

Consequently, over the term of our appointment, we will focus on the Council's performance reporting arrangements and integrate this with our wider planning activity.

National Fraud Initiative and fraud returns

All local authorities are required to participate in the National Fraud Initiative (NFI). NFI involves the collection of data from various entities including authorities to identify potential irregularities for investigation. Authorities are required to participate through both initial data submission and investigation of identified matches. We are required to monitor and report on the Council's participation in NFI. We are also required to report on any frauds identified at the Council.

Audit Scotland – National Study Programme

Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission. Audit Scotland ask us to ensure that local government bodies review the national studies relevant to them, which may also include joint studies under the remit of the Auditor General for Scotland, at a committee level and act on them accordingly.

Other assurance activity

Under the terms of our appointment we are required to undertake a number of other areas of audit activity. These include certifying authorities Whole of Government Accounts returns as well as certifying any applicable grant claims and returns such as the non-domestic rates return and housing benefits subsidy claim.

Key messages

We will include in our reporting to you any significant findings or issues in respect of the Council's arrangements for Following the Public Pound, publication of Statutory Performance Information or participation in the National Fraud Initiative.

We will report to you on the certification of various grant claims and the Council's Whole of Government Accounts.

6. Team, fees and deliverables

6. Team, fees and deliverables

We identify an audit team with the relevant skills and experience. All member of our core team have several years experience in the audit of local government.

The audit fee is determined in line with Audit Scotland's fee setting arrangements, set out in recent communications to all audited bodies in line with their publication on '*Our Approach to setting audit fees*'

(http://www.audit-scotland.gov.uk/uploads/docs/um/audit_fee_approach.pdf).

Audit team

The engagement team is led by Stephen Reid, who is one of three partners leading EY's Government and Public Sector practice in the UK. Stephen is supported by Keith Macpherson, our Head of Government & Public Sector Audit in Scotland, whose primary role is to set the direction and consistency of our audit work across our audit portfolio, in particular in respect of the wider scope audit. John Boyd will be the manager for the financial statements audit.

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2016/17 Audit fee

The expected fee for each body, set by Audit Scotland, assumes that it has sound governance arrangements in place and operating effectively throughout the year, prepares comprehensive and accurate draft financial statements and meets the agreed timetable for the audit. It also assumes there is no major change in respect of the scope of work in the year.

Expected Fee Element	2016/17	2015/16*
Auditor remuneration	£136,670	n/a
Pooled costs	£11,900	n/a
Performance audit and Best Value (Audit Scotland)	£65,680	n/a
Audit support costs	£8,160	n/a
Total expected fee	**£222,410**	**£225,170**

* The breakdown of the prior year fee into these components is not available from Audit Scotland.

The auditor remuneration element of the fee can be increased by up to 10% dependent on circumstances in the audited body. For 2016/17, we have agreed an auditor remuneration element of £140,080 (2.5% above the expected level).

This reflects additional audit work required over the Council's implementation of the new fixed asset register, given the inherent risk around the sizeable property, plant and equipment balances.

On this basis, the total audit fee will be £225,820, compared to actual agreed fees payable in the prior year with the previous auditor of £241,760 (6% reduction).

Key messages

Stephen Reid is your audit engagement partner, supported principally by Keith Macpherson and John Boyd.

We have agreed an auditor remuneration fee element of £140,080. This results in a total audit fee, inclusive of pooled costs, central performance audit and Best Value costs and central support costs, of £225,820 (*2015/16 actual*: £241,760).

We agree a timetable with management, in line with the Council's internal reporting requirements, and in accordance with Audit Scotland's planning guidance.

There are a number of deliverables required during the year, as set out in the table.

As part of our transparency to you, and to allow you to assess the performance of your external auditor, we will report to you annually on how we have performed against the timetable for audit deliverables.

Timeline and deliverables

Audit activity	Deliverables
Planning: September – December 2016	
► Introductory meetings with senior management ► Handover discussions with outgoing auditor ► Review of Audit Scotland planning guidance ► Review of Council documentation	1. Welcome to EY, presented to Audit Committee, 20/9/2016 2. External Audit Framework, presented to Audit Committee, 13/12/2016
Identification and assessment of risks: January – March 2017	
► Onsite fieldwork, documentation and walkthrough of key accounting processes ► Testing of key financial controls as appropriate ► Participation in LAN Shared Risk Assessment ► Scoping of Best Value work for the year	3. Annual Audit Plan, presented to Audit Committee, 21/3/2017 4. Submit Accounts Commission current issues return to Audit Scotland (this submission is required quarterly) 5. Letter to Chief Executive setting out scope of proposed Best Value work 6. Local Scrutiny Plan (communicated by the LAN lead)
Design and execute response to risks: April – August 2017	
► Understanding of Council's response to results from National Fraud Initiative (NFI) ► Performance of Best Value fieldwork (May – July) ► Commencement of year-end substantive audit fieldwork on unaudited accounts (from June) ► Education Maintenance Allowance (EMA) grant claim testing	7. Submit any fraud returns to Audit Scotland by 26/5/2017 8. Interim management report, presented to Audit Committee, 9. Submit NFI return to Audit Scotland by 30/6/2017 10. Submit certified EMA return by 31/7/2017
Conclude and communicate: September – November 2017	
► Conclude on results of audit procedures ► Audit clearance meeting with senior management, and report findings to those charged with governance ► Issue opinion on the Council's financial statements ► Criminal Justice Social Work (CJSW) return testing / Whole of Government Accounts testing / Non-domestic rates return testing / housing benefits subsidies claim testing ► Finalise Best Value Assurance Report for Accounts Commission	11. Certify CJSW claim – by 29/9/2017 (tbc) 12. Annual Audit Report – to Audit Committee (date tbc) 13. Certify Annual Accounts – by 30/9/2017 14. Submit WGA assurance statement to NAO by 2/10/2017 (tbc) 15. Submit Best Value Data Return to Audit Scotland by 2/10/2017 16. Submit Non-Domestic Rates return by 9/10/2017 (tbc) 17. Submit Housing benefit subsidies claim to DWP by 30/11/2017

Appendices

A – Auditor Independence

B – Required Communications

A. Independence

The APB Ethical Standards and ISA (UK and Ireland) 260 'Communication of audit matters with those charged with governance', requires us to communicate with you on a timely basis on all significant facts and matters that bear on our independence and objectivity.

The Ethical Standards require that we do this formally both at the planning stage and at the conclusion of the audit, as well as during the audit if appropriate.

The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communication	
Planning stage	**Final stage**
► The principal threats, if any, to objectivity and independence identified by EY including consideration of all relationships between you, your affiliates and directors and us. ► The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality Review. ► The overall assessment of threats and safeguards. ► Information about the general policies and process within EY to maintain objectivity and independence.	► A written disclosure of relationships (including the provision of non-audit services) that bear on our objectivity and independence, the threats to our independence that these create, any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed. ► Details of non-audit services provided and the fees charged in relation thereto. ► Written confirmation that we are independent. ► Details of any inconsistencies between APB Ethical Standards, Audit Scotland's Terms of Appointment and your policy for the supply of non-audit services by EY and any apparent breach of that policy. ► An opportunity to discuss auditor independence issues.

During the course of the audit we must also communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of our safeguards, for example when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future contracted services, and details of any written proposal to provide non-audit services;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period are disclosed, analysed in appropriate categories.

Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including any principal threats. However we have adopted the safeguards below to mitigate these threats along with the reasons why they are considered to be effective.

Self-interest threats

A self-interest threat arises when EY has financial or other interests in your entity. Examples include where we have an investment in your entity; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with the Council.

At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services, and we will comply with the policies that the Council has approved and that are in compliance with Audit Scotland's Terms of Appointment. At the time of our appointment, we disclosed to Audit Scotland ongoing work from our infrastructure advisory team, in particular in respect of the long running Midlothian Zero Waste project and the fact that it had not yet reached financial close by the start of the 2016/17 financial year. Audit Scotland were satisfied that appropriate safeguards were in place around this work. To date, total non-audit fees earned in 2016/17 are circa £35,000.

Self-interest threats (cont.)

A self-interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to the Council. We confirm that no member of our audit engagement team, including those from other service lines, is in this position, in compliance with Ethical Standard 4.

There are no self-interest threats at the date of this report.

Self-review threats

Self-review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no other self-review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of your entity. Management threats may also arise during the provision of a non-audit service where management is required to make judgements or decisions based on that work.

There are no management threats at the date of this report.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

The 2016/17 audit year is the first year that Stephen Reid has led the audit of the Council. We assessed this relationship prior to the commencement of the audit period and concluded that there are no considerations that compromise, or could be perceived to compromise, Stephen Reid's independence or objectivity.

Overall Assessment

Overall we therefore confirm that EY is independent and the objectivity and independence of Stephen Reid, the Audit Engagement Partner and the audit engagement team have not been compromised.

B. Communications

EY has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained. Details of the key policies and processes within EY for maintaining objectivity and independence can be found in our annual Transparency Report, which the firm is required to publish by law. The most recent version of this report is for the year ended June 2016 and can be found here:

http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2016

There are certain additional communications that we must provide to the Audit Committee, which are set out below.

Required communication	Reference
Planning and audit approach ► Communication of the planned scope and timing of the audit including any limitations.	► Annual Audit Plan
Significant findings from the audit ► Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ► Significant difficulties, if any, encountered during the audit ► Significant matters, if any, arising from the audit that were discussed with management ► Written representations that we are seeking ► Expected modifications to the audit report ► Other matters if any, significant to the oversight of the financial reporting process ► Findings and issues regarding the opening balances on initial audits	► Annual Audit Report
Misstatements ► Uncorrected misstatements and their effect on our audit opinion ► The effect of uncorrected misstatements related to prior periods ► A request that any uncorrected misstatement be corrected ► In writing, corrected misstatements that are significant	► Annual Audit Report
Fraud ► Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity ► Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ► A discussion of any other matters related to fraud	► Annual Audit Plan ► Annual Audit Report
Related parties Significant matters arising during the audit in connection with the entity's related parties including, when applicable: ► Non-disclosure by management ► Inappropriate authorisation and approval of transactions ► Disagreement over disclosures ► Non-compliance with laws and regulations ► Difficulty in identifying the party that ultimately controls the entity	► Annual Audit Report
External confirmations ► Management's refusal for us to request confirmations ► Inability to obtain relevant and reliable audit evidence from other procedures	► Annual Audit Report

B. Communications (cont.)

Required communication	Reference
Significant deficiencies in internal controls identified during the audit	► Annual Audit Report
Consideration of laws and regulations ► Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ► Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	► Annual Audit Report
Independence Communication of all significant facts and matters that bear on EY's objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: ► The principal threats, and any safeguards adopted and their effectiveness ► An overall assessment of threats and safeguards ► Information about the general policies and process within the firm to maintain objectivity and independence	► Annual Audit Plan ► Annual Audit Report
Going concern Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: ► Whether the events or conditions constitute a material uncertainty ► Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ► The adequacy of related disclosures in the financial statements	► Annual Audit Report
Group audits ► An overview of the type of work to be performed on the financial information of the components, and of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components ► Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work ► Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted ► Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements	► Annual Audit Report
Fee information and confirmation of additional certification work ► Details of the audit fee ► Summary of additional audit certification work undertaken	► Annual Audit Plan ► Annual Audit Report

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Risk Management, Update for 1 October 2016 – 31 December 2016

Report by Chris Lawson, Risk Manager

1 Purpose of Report

The purpose of this report is to provide Audit Committee with the 2016/17 quarter 3 strategic risk management update, covering the period 1 October to 31 December 2016.

2 Background

Corporate Risks

2.1 Audit Committee has requested regular reporting on the Council's Strategic Risks. The Strategic Risk Profile report for quarter 3 is attached as Appendix 1. This report reflects the Current Issues, Future Strategic Risk, and Opportunities facing the Council as Q3 2016/17.

2.2 Following the announced Scottish Government Grant settlement for 2017/18 in the second half of December 2016 the impact of this settlement was assessed by the Head of Finance and Integrated Service Support and reported to the Council. In respect of 2017/18 the initial assessment of the grant settlement indicated that the budget shortfall for 2017/18 would increase to £12.880 million as set out in the December Council report.

The impact this has had on Council General Fund Reserves has been significant as detailed below.

Balancing the Budget in future years has been re-assessed during quarter 3 as 'Critical' given the scale of the financial challenge facing the Council.

2.3 Welfare reform has an increased Strategic Risk Profile as the Council prepares for the full implementation of Universal Credit from 22 March 2017.

2.4 A further addition has an increased the Strategic Risk Profile this quarter, 'the Scottish Abuse Inquiry' has been incorporated. This was reported to Council on 27 September 2016. This potential risk has been widely reported in the national media as the Scottish Government progresses with the enquiry on a nationwide basis and more locally the subject has been reported in local media.

2.5 Strategic Risk Profile Summary

The Top Strategic Issues are as set out in the following table.

Top Issues	Likelihood	Impact	Score	Evaluation
Balancing budget 2017/18	5	5	25	Critical
Welfare Reform	5	4	20	High
Review of Pay and Grading	4	4	16	High
Corporate change and transition	3	4	12	Medium
Integration of Health and Social Care	3	4	12	Medium

The key Strategic Risks for the Council are tabled below.

Strategic Risks	Likelihood	Impact	Score	Evaluation
Balancing budget in future years	5	5	25	Critical
The Change Program	3	5	15	High
Scottish Abuse Inquiry	4	5	20	High
People risk	3	4	12	Medium
Integration of health and social care	3	4	12	Medium
Governance and standards	3	4	12	Medium
Legal and regulatory compliance	3	3	9	Medium
Working with other to deliver outcomes	3	3	9	Medium
Asset condition	3	3	9	Medium
Climate change	3	3	9	Medium
Internal control environment	3	3	9	Medium
Emergency planning and business continuity	2	4	8	Low
Corporate policies and strategies	2	3	6	Low

The Strategic Opportunities for the Council are:-

Strategic Opportunities	Likelihood	Impact	Score	Evaluation
Shawfair	5	4	20	High
Borders rail	5	4	20	High
Easter Bush - Penicuik	5	4	20	High
City deal	3	5	15	Medium

2.6 Strategic Issues – Rated Critical and High

2.6.1 Balancing Budgets 2017/18

On 20 December 2016 Council was provided with an updated assessment of projected budgets shortfalls through to 2021/22, with an update on the Scottish Government Grant settlement for 2017/18.

In respect of 2017/18 the initial assessment of the grant settlement had indicated that the budget shortfall for 2017/18 would increase to £12.880 million from the previously reported sum of £10.018 million.

In order to achieve a balanced budget for 2017/18 the Council will utilise £5.965 million of reserves, leaving a contingency level of General Fund Reserves of £3.413 million. This is below the £8 million level set out in the Reserves Strategy approved by Council on 8 November 2016 and equates to 1.7% of projected net expenditure for 2017/18.

2.6.2 Welfare Reform

Universal Credit Live Service was introduced in Midlothian for newly unemployed single claimants, with or without housing costs from 27 April 2015. Universal Credit Full Service is being rolled out in Midlothian on 22 March 2017. The Universal Credit Programme will close gateways for legacy benefits, so existing benefits will no longer be eligible as Universal Credit rolls out and there are plans for the migration of those remaining claimants on current benefit types once the digital rollout is complete for all of Great Britain.

Awareness, advice and assistance is being provided by the Council. The projected outcomes are based on local data and evidence in conjunction anecdotal information resulting in speculative scenarios. Monthly meetings are taking place via the Midlothian Operational Delivery Group to plan Universal Credit implementation.

2.6.3 Review of Pay and Grading

There are Consequences to not fully implementing the review and concerns regarding what the Council will 'look like' if the cultural change required does not follow. This might result in higher employee relationship issues, because there is uncertainty regarding what behaviours are expected and what boundaries the organisation works within. There is a risk if the 'pay and grading review' is not implemented in full, the vision of 'A Great Place to Grow' and the Council values including respect, collaboration, pride and ownership will not be embedded.

The challenge facing the Council is to ensure the delivery of the 'give and the get', the give from the Council in terms of the new pay and grading model in return for improvements in flexibility "the "get". This will be actively supported by the Council's People Strategy.

2.7 Strategic Risks – Rated Critical/High

2.7.1 Balancing budget in future years

The Council's Financial Strategies core objective is to secure the Council's continued financial sustainability during what is and will continue to be an extended period of significant financial constraint coupled with increasing service demands and increasing customer expectations.

In response to these challenges the Council has set out a Financial Strategy covering the period to 2021. In order to ensure the Services provided meet the needs of service users and are as efficient as possible the Council are implementing A Change Program, incorporating the Delivering Excellence framework for service review and redesign is expected to bring forward savings options in addition to ensuring service user needs are achieved.

A report was provided to February Council setting out the 2017/18 Budget for approval.

2.7.2 The Change Program

The strands of work that will continue to be necessary to address the projected budget shortfalls represent a change programme, encompassing:-

- The Delivering Excellence programme;
- The delivery of savings approved in 2016/17 and 2017/18; and the continued control over expenditure;
- The Transformation Programme;
- The EWiM programme;
- An updated Capital Strategy and Reserves Strategy;
- Operational savings encompassing financial discipline measures;
- The development of further savings options for 2018/19 and beyond.

2.7.3 Strategic Opportunities

2.7.4 Shawfair

The Shawfair development with its new rail link provides a major incentive for house builders, employers, retailers and commercial interests; including opportunities to secure a low carbon community through a district heating scheme from the Zero Waste facility currently being constructed.

2.7.5 Borders Rail

The Borders Rail provides the opportunity to support the regeneration of priority communities of Midlothian, through which the railway passes.

The line provides ready access to education/training at Edinburgh College, Borders College and Queen Margaret University with improved access to the labour markets in Edinburgh and the Borders. The Railway has also acted as a catalyst for housing growth in Midlothian.

2.7.6 Easter Bush

Easter Bush offers fast growing opportunities in Science Technology Engineering and Mathematics (STEM), with opportunities to link directly with Education. Maximising partnership links between schools the University sector and the Bush will all support STEM opportunities.

2.7.7 City Deal

Midlothian Council is part of the South East Scotland Region City Deal bid for funding to Scottish and UK Governments.
The purpose of which is to support the acceleration of economic growth through investment in infrastructure/ housing/ skills and innovation. Detailed discussion and negotiation are underway with UK Government and Scottish Government Officials with work progressing towards a City Deal sign off in 2017.

3 Report Implications

3.1 Resource

There are no direct resource implications in this report although individual risks will have associated resource implications which are considered within the Risk Registers.

3.2 Risk

Corporate Risks are generally those that impact on all parts of the Council and the strategic priorities of the Council. It appears that the presence of risk is understood and action is being taken to manage and respond to risk on an ongoing basis by officers.

The risks referred to in this report are articulated within the Strategic Risk Profile attached as Appendix 1.

3.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☒ Adult health, care and housing
☒ Getting it right for every Midlothian child
☒ Improving opportunities in Midlothian
☒ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

3.4 Impact on Performance and Outcomes

The purpose of the Council's risk management approach is to support a level of risk awareness, to inform decision making and support the Council to deliver on its key outcomes by highlighting and taking steps to mitigate potential disruption to delivery of services.

3.5 Adopting a Preventative Approach

The Risk Management approach being taken by the Council is founded on a preventative approach to managing risks where appropriate and more generally greater risk awareness.

3.6 Involving Communities and Other Stakeholders

Consultation has taken place with Senior Managers responsible for leading responses to key Strategic Issues, Risk and Opportunities.

3.7 Ensuring Equalities

There are no direct equalities issues arising from this report.

3.8 Supporting Sustainable Development

Senior Managers must ensure the sustainability of the Council, which entails identifying, understanding and managing Strategic and Service level Issues, Risks and Opportunities.

3.9 IT Issues

No additional issues other than those relating to the Strategic Risk Profile.

4 Recommendations

Audit Committee is invited to:

Note the quarter 3 2016/17 Strategic Risk Profile report and consider the current response to the risks and opportunities highlighted.

Date: 16 February 2017

Report Contact:
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Background Papers: **Appendix 1** Strategic Risks Profile Quarter 3 2016/17

Appendix 1

Strategic Risk Profile

Midlothian

ISSUES

SRP.IR.01 Balancing budget 2017/18

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.IR.01	Risk cause **The reduced level of grant settlement offered to Midlothian Council and budgetary pressures including:** **Pay inflation, Pension reform, Demographics, Service demand.** Risk event **Council on 7 February 2017 will need to set a balanced budget for 2017-18** Risk effect **There is a gap between expenditure and funding which will require the utilisation of reserves. The structural deficit remains to be addressed in 2018/19.**	**Gary Fairley**	**1. Financial Strategy.** **2. The reserves position can accommodate the short term utilisation**	**5**	**5**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.IA.01.01	**Financial Strategy**	Q3 16/17: **The immediate focus for the next Council will be on longer term financial planning.**	**Gary Fairley**	**30-Jun-2017**	
SRP.IA.01.02	**Financial Strategy**	Q3 16/17: 1. **Council approving a budget on 7 February 2017 for 2017/18.**	**Gary Fairley**	**07-Feb-2017**	

SRP.IR.02 The Change Programme

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.IR.02	Risk cause **Change programme that doesn't address the budget shortfall;** **The Change Programme does not achieve the projected savings** Risk event **Delayed progress in applying various strands of the Change Programme including the Delivering Excellence framework.** Risk effect **Slow or delayed proposals/savings arising from service redesign. Potentially further eroding reserves or requiring short term service reductions which impact on the Council's ability to deliver against its priorities.**	**Ricky *Moffat; Garry *Sheret; Kevin Anderson; Gary Fairley; Ian Johnson; Joan Tranent; Grace Vickers; Alison White**	**1. Change Programme including Delivering Excellence framework** **2. Delivering Excellence Management Tools to support the application of the framework** **3. Senior Leadership Group developing the longer term Change Programme for the new Council.**	**3**	**5**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.IA.02.01	**Developing and implementing a Change Programme to ensure long term financial sustainability.**	Q3 16/17: **Senior Leadership Group action in preparation for the new Council.**	**Ricky *Moffat; Garry *Sheret; Kevin Anderson; Gary Fairley; Ian Johnson; Joan Tranent; Grace Vickers; Alison White**	**30-Jun-2017**	

SRP.IR.03 Integration of Health & Social Care

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.IR.03	Risk cause **IJB not having enough flexibility to make changes** **Unbalanced budget set for IJB.** **Savings targets sought from Adult Services to contribute to Council budget saving 2017/18 by MLC are challenging..** Risk event **Uncertainty on final financial settlement for IJB** Risk effect **Impact the IJB's ability to govern and deliver on strategic plan.**	**Eibhlin McHugh**	**IJB Strategic Plan setting out key transformational activity to shift the demands on services and improve outcomes for people of Midlothian.**	**3**	**4**	

SRP.IR.05 Review of Pay & Grading

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.IR.05	Risk cause **Investment to reduce in-work poverty need to improve flexibility, productivity and service quality.** **Many current policies and terms and conditions, including pay arrangements have been constructed around a Monday - Friday, 9 - 5 working week, with many services requiring to deliver services 7 days a week beyond 9-5.** Risk event **Council does not see improvements in productivity and flexibility across the workforce. Council services are not competitive against the voluntary 3rd or private sector.** Risk effect **Investment in pay and grading not translating into positive productivity gains for the Council.**	**Gary Fairley**	**1. Investing in our Workforce Project Board focussed on securing the gains.** **2. Governance on the 4 strands of work from Council: Life Long Learning, Policy, Pay, Non Financial Benefits.** **3. Launch of new People Policies on 1st March 2017.** **4. Communications plan to ensure all employees know what is changing and how this will impact them and service delivery.**	**4**	**4**	

Related Action Code	Related Action	Related action latest note	**Managed By**	Due Date	Status
SRP.IA.05.02	**Launch of new People MAnagement Policies on 1st March 2017.**	Q3 16/17: **Consultation with the Trades Unions are on going - linked to changes in Council**	**Gary Fairley**	**01-Mar-2017**	

RISKS

SRP.RR.01 Balancing Budgets in future years/Impact of Budget Cuts/Financial Strength of Council

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.01	Risk cause **Future Scottish Government grant settlements are expected to result in cash reductions.** **Policy decisions by UK & Scottish Governments which are not fully funded.** **Non or delayed savings from planned activities.** **Future year pay award settlements and implications of living wage increases.** **Inflation, interest rates, tax, income levels, service demand.** Risk event **Reduced grant settlement.** **Policies decisions at Government level not fully funded to Council's.** **Delay in project to achieve savings.** **Cost pressures exceeding budget estimates.** Risk effect **Gap in Council budget between budget commitments/ pressures and funding level and inadequate options presented to appraise this, resulting in a structural deficit.**	**Gary Fairley**	**1. The Financial Strategy to 2021-22** **2. Development of a Change Programme including the Delivering Excellence framework developed for the new Council Administration.** **3. Maintaining a level of reserves to deal with unforeseen or one off cost pressures.**	**5**	**5**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.RA.01.01	**Developing and implementing a Change Programme to ensure the long term financial sustainability.**	Q3 16/17**: 1. Update Financial Strategy report presented to an early meeting of the next Council; and 2. Senior Leadership Group action in preparation for the new Council.**		**30-Jun-2017**	

SRP.RR.02 The Change Programme

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.02	Risk cause **Reduced resources** **Leadership fit for the future** **Lack of clarity or clear compelling vision for the future** **Delay or shortfall in securing savings** Risk event **Slow benefits realisation and budget savings** Risk effect **Objectives of changes not actually met** **Adverse impact on services** **Staff morale affected Government step-in**	**Gary Fairley**	**1. Financial Strategy and Change Programme** **2. Leadership from Executive Team and Senior Leadership Group.** **2. Appropriated governance in place across the Change Programme.** **3. Links between Change Programme and Workforce Plans** **4. Resilience planning.** **5. Senior Leadership Group regularly considering Change Programme and budget position.**	**4**	**4**	

Related Action Code	Related Action	Related action latest note	**Managed By**	Due Date	Status
SRP.RA-02.01	**Developing and implementing a Change Programme to ensure the long term financial sustainability.**	Q3 16/17: **Update Financial Strategy report presented to an early meeting of the next Council; and Senior Leadership Group action in preparation for the new Council.**	**Gary Fairley**	**31-Mar-2017**	

SRP.RR.03 Legal and Regulatory Compliance

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.03	Risk cause **Current or new legislation applying to Midlothian Council** Risk event **Council and or Services not identifying all applicable legislation impacting Council activities and Service requirements.** Risk effect **Council failing to meet its statutory obligations resulting in a potential negative impact for service users or employees. Reputational impact of not meeting statutory obligations.**	**Ricky *Moffat; Garry *Sheret; Kevin Anderson; Gary Fairley; Ian Johnson; Joan Tranent; Grace Vickers; Alison White**	**1. Directors and Heads of Service responsible for identifying applicable legislation and propose Council or Service responses to CMT and Cabinet/Council as required.** **2. Annual Assurance Statement.** **3. Internal Audit testing of internal controls as part of risk based audit plan.** **4. External Audit.** **5. Statutory Inspection.**	**3**	**3**	

Related Action Code	Related Action	Related action latest note	**Managed By**	Due Date	Status
SRP.RA.03.01	**Legal & Regulatory Compliance**	Q3 16/17: **Heads of Service ensuring compliance with statutory obligations and making CMT, Cabinet/Council aware as required.**	**Ricky *Moffat; Garry *Sheret; Kevin Anderson; Gary Fairley; Ian Johnson; Joan Tranent; Grace Vickers; Alison White**	**31-Mar-2017**	

SRP.RR.04 People risks

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.04	Risk cause **HR Policies and Employee Terms & Conditions not creating adequate flexibility to meet service needs and or employee desires.** **Employees not suitably qualified or developed for the roles required of them.** **Statutory health and safety - duty of care over services users and employees not met.** **Organisational transformation activities not informed by all key stakeholders** **Ageing work force** **Employees unclear on expected behaviours.** Risk event **Employees required to undertake tasks they are not competent to.**	**Chris Lawson; Marina Naylor**	**01 - Main internal controls centre on the approved People Strategy and supporting initiatives and Action Plan.** **02 - People Management policies reviewed as part of wider review of pay and grading** **03 - Making performance matter** **04 - A range of initiatives to keep staff informed of change (In brief, Staff Magazine, Espresso Sessions for Managers on new People Management Policies)** **05 - Absence Monitoring/Reporting.** **06 - Health and Safety Management Arrangements** **07 - Comprehensive range of Health & Safety Management & Assessment based development opportunities for line managers** **08 - Risk Management/pro- active action to Internal Audit recommendations/use of risk consultants for surveys.** **09 - Use of Health & Safety Management Information System to enhance information transfer and organisational effieiency**	**3**	**4**	

	Statutorily driven health and safety protective arrangements for service users and employees not implemented correctly. **Employees not engaged/consulted as part of organisational transformation.** **Experienced employees leaving the organisation** **Unacceptable behaviours demonstrated by employees** Risk effect **Negative impact on outcomes for customers/service users.** **Difficulties recruiting the right staff** **Challenges retaining quality staff** **Service users and employees exposed to hazards where statutory requirements exist.** **low skill levels** **low morale, especially during change** **non compliance with policy and procedure** **high absence rates** **Lose of experience in service areas. 'A Great Place to Grow' our values including respect ,collaboration, pride and ownership not realised**		**10 - Non-redundancy policy supported by SWITCH and Organisational Change Policy**			

Related Action Code	Related Action	Related action latest note	**Managed By**	Due Date	Status
MC01 -A01-1	**Policy Review program**	Q2 16/17: **The Policy review work is linked to the review of Pay & Grading for Non-Teaching staff has been prepared with Trade Union Consultation on going. Initial implementation of the new Policies is expected to take place over November and December 2016.**	**Marina Naylor**	**31-Dec-2016**	
MC01-A01-2	**Health & Safety Management Arrangement Development**	Q3 16/17: **The Management Arrangement development program is nearing completion. A suite of 16 Management Arrangements were presented to CMT for formal approval in Q3. The development of the complete suite of arrangements is expected to be completed during Q4.**	**Chris Lawson**	**31-Mar-2017**	

SRP.RR.05 Working with others to deliver outcomes

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.05	Risk cause **Partners not engaged or focused to deliver specific outcomes.** **Public Sector Reform Agenda.** Risk event **Partners prioritising activity in areas not inline with delivery of defined outcomes.** **Community groups afforded legal right to make case to operate vacant properties for community use.** Risk effect **Delivery of outcomes delayed or not achieved** **Officer time to support the assessment of unsustainable business cases.**	**John *Blair; Mary *Smith; Eibhlin McHugh**	**1. Key partners engaged in planning and delivery of Service outcomes, e.g.** **Midlothian Community Planning Partnership have developed a Single Midlothian Plan.** **Midlothian Integrated Joint Board (Adult & Social Care Integration) have developed and Strategic Plan.** **2. Approved integration scheme.** **3. Service Directions in Place.**	**3**	**3**	

SRP.RR.06 Information Security

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.06	Risk cause **General Data Protection Regulation is a new piece of legislation currently being formulated by the European Commission. It is expected to be agreed in the first part of 2016 with a two year lead in period.** Risk event **The Regulation has been agreed with implementation due on 25 May 2018.** Risk effect **The Regulations will bring about a number of requirements on the Council including mandatory reporting of all data breaches, appointment of a Data Protection Officer and the potential for fines ranging to 4% of turnover or 20million Euros which ever is greater.**	**Ian Wragg**	**1. Information Management Group** **2. Public Sector Network Compliance.** **3. Meta Compliance** **4. Information Management, awareness raising program (Private-i)** **5. General Data Protection Regulation Project Plan.**	**3**	**5**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.RA.06.02	**Preparing for next PSN Assessment**	Q3 16/17: **Final activity to secure positive reassessment and continued connection to the Public Sector Network.**	**Phil Timoney**	**30-Apr-2017**	
SRP.RA.06.03	**GDPR Project Plan**	Q3 16/17: **General Dat Protection Regulation - Project Plan to be reported to CMT.**	**Phil Timoney**	**30-Apr-2017**	

SRP.RR.07 Integration of Health & Social Care

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.07	Risk cause **The nature of many of the Services provided under the banner of Health & Social Care are demand led. Rising numbers of people requiring care and support together arising from demographic make up and improvements in treatment increase the number of people in receipt of long term care packages.** Risk event **Unless the focus and balance of care shifts from acute treatment the costs of providing these services will continue to rise and not provide the best possible outcomes for individuals.** Risk effect **The reactive demand led service may become financially unsustainable.**	**Alison White**	**Midlothian IJB Strategic Plan - focussed on rebalancing care.** **Transformation Change Program** **Strategic Core Group Oversight**	**3**	**4**	

SRP.RR.08 Asset Condition – buildings, vehicles, roads and Digital assets/networks

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.08	Risk cause **Many of the assets the Council own by their nature are in a position of on going deterioration through their normal use, e.g. roads - normal wear and tear, street lights and vehicles & buildings used to deliver services.** Risk event **Many assets will deteriorate under normal conditions although buildings, roads and street lights as an example can be damaged during more extreme weather events or as a result of a lack of maintenance.** Risk effect **In the case of Roads Services there is a real risk of increased potholes and insurance claims, reduced skid resistance leading to higher accident potential and building up of higher costs in the future. In respect of vehicles, increased breakdowns, service failures, greater maintenance inevitable, higher short-term hire costs. In terms of property, health and safety issues arise, failure to meet current standards and higher running costs. There is also the risk of two-tier accommodation, some high quality, some low.**	**Ricky *Moffat; Garry *Sheret; Gary Fairley**	**1. There is provision in place within the capital plan for investment in the asset base.** **2. Asset register** **3. Conditional Survey** **4. Understanding of future asset needs** **5. Asset Strategy.** **6. Roads asset management plan** **7. Land register** **8. Vehicle maintenance schedules.** **9. Capital program - investment in estate.** **10. On going monitoring of properties by: Maintenance Surveyors, Facilities Management and Property Users.** **11. Updated Digital Strategy and Digital Learning Strategy going to Council on 7th February 2017.** **12. Asset management plans for office and school digital devices** **13. Network Strategy**	**3**	**3**	

SRP.RR.09 Emergency Planning and Business Continuity Management

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.09	Risk cause **The Council not preparing Emergency Plans and testing arrangements to respond to Civil Contingencies Incidents** Risk event **There are a wide range of potential events the Council may be expected to respond to e.g. Severe weather incident, Pandemic, Utility disruption etc.** Risk effect **Censure through non compliance with the Civil Contingencies Act** **Not adequately recovering from the loss of major accommodation (eg secondary school, main offices), computer systems and staff** **Not able to respond to a major emergency in the community** **Fatal Accident Inquiries**	**Chris Lawson**	**Potential sub risks include:-** **01 – Civil Contingencies Risk Register used to highlight key risks and record response,** **- Council's plans developed and maintained in response to identified risks,** **- Contingency Planning Group support development, peer review and roll out of plans.** **02 – Establishment based incident response plans in place and maintained locally.** **03 – Emergency response plan setting out general approach to respond to a major emergency inline with key partner organisations.** **04 – As part of the Council's Emergency response plan the importance of recording decisions made and information available at the time is highlighted as this would be scrutinised in the event of an FAI.**	**2**	**4**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.RA.09.02	**Development of Emergency Planning Improvement Plan**	Q3 16/17: **Civil Contingencies Risk Register revised to assist the prioritising of a new forward program of Contingency Plan Reviews and Development to meet the needs of Midlothian Council.**	**Chris Lawson**	**31-Mar-2017**	

SRP.RR.10 Governance and Standards in Public Life

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.10	Risk cause **Code of conduct for Members and employees actions falling short of International Standards.** Risk event **Failure in openness, accountability, clarity.** Risk effect **Service, partnerships and project outcomes not achieved** **Non compliance with conduct standards and reduction in standards in public life**	**Alan Turpie**	**<u>Potential</u> sub risks include:-** **01 Macro governance at the top – failure in openness, accountability, clarity;** **02 Micro governance in services, partnerships and projects and outcomes not achieved** **03 Non compliance with codes of conduct and reduction in standards in public life** **04 Annual Assurance Statement.**	**3**	**4**	

Related Action Code	Related Action	Related action latest note	**Managed By**	Due Date	Status
SRP.RA.10.02	**International Governance Standards**	Q3 16/17: **Current governance standards being reviewed in-line with new CIPFA/SOLACE Guide. Due to be reported to CMT in advance of reporting to May 2017 Audit Committee.**	**Alan Turpie**	**31-May-2017**	

SRP.RR.11 Corporate Policies and Strategies

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.11	Risk cause **Policies may not be match the aspirations of the Council's Strategic priorities or cultural perspective.** Risk event **Policies not monitored may become out of date** **Policies not reviewed to ensure alignment with strategic priorities.** Risk effect **Policies not monitored could result in non compliance with legislation** **Policies not align to strategic priorities will inhibit the rather than support implementation of strategic priorities.**	**Ricky *Moffat; Garry *Sheret; Kevin Anderson; Gary Fairley; Ian Johnson; Joan Tranent; Grace Vickers; Alison White**	**1. Single Midlothian Plan providing overarching direction** **2. Service plans aligned to Single Midlothian Plan.** **3. Leadership team to ensure correct approaches are adopted to get the right results.**	**2**	**3**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.RA.11.01	**HR Policy Review**	Q3 16/17: **HR - People Policies being overhauled as part of Pay & Grading review, ongoing review thereafter. New People policies being implemented**	**Marina Naylor**	**01-Mar-2017**	
SRP.RA.11.02	**Developing a policy overview**	Q3 16/17**: Service review of Business Transformation, Performance Management, Quality and Scrutiny teams to incorporate to enhance capacity for oversight for corporate policies and strategies**	**Gary Fairley**	**01-May-2017**	

SRP.RR.12 Internal Control Environment

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.12	Risk cause **Work procedures/process inadvertently create the capacity for fraud and waste to occur.** **Internal Controls requiring more time, effort or cost than the risk being managed.** Risk event **Persons exploiting opportunities to commit fraud** **Waste and errors** Risk effect **Waste and loss** **Risks over managed with risk controls costing more than the potential loss being managed.**	**Ricky *Moffat; Garry *Sheret; Kevin Anderson; Gary Fairley; Ian Johnson; Joan Tranent; Grace Vickers; Alison White**	**1. Services have been prompted to consider fraud and waste within Service Risk Registers.** **2. Risk Management Guide, provides direction on the need to balance time, effort and cost against benefit of risk controls.** **3. Internal Audit examine internal control arrangements based largely on the risk registers.**	**3**	**3**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.RA.12.01	**Annual Audit Plan**	Q3 16/17**: Audit team progressing with 2016/17 Audit Plan to test a range of internal controls as agreed and approved by Audit Committee.**	**Internal Audit**	**31-Mar-2017**	

SRP.RR.13 Climate Change

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.13	Risk cause **Council Services not adequately engaged, resourced or directed to fulfil the requirements of the Climate Change Act** Risk event **Council Services not responding to the Climate Change Act with sufficient pace.** Risk effect **Council failing to meet its obligation under the Climate Change (Scotland) Act 2009 and incurring the associated reputational damage.**	**Ian Johnson**	**1. Voluntary reporting on compliance with the climate change duties (this will be a statutory requirement from 30 November 2016 onwards).** **2. Council Carbon Management Plan** **3. Approval of a Corporate Climate Change and sustainable development action plan 2016/17**	**3**	**3**	

Related Action Code	Related Action	Related action latest note	Managed By	Due Date	Status
SRP.RA.13.01	**Adaptive Planning**	Q3 16/17: **Adaptive planning proposal to be brought forward to CMT.**	**Ian Johnson**	**31-Mar-2017**	

SRP.RR.14 Scottish Abuse Inquiry

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.RR.14	Risk Cause: **Midlothian Council and its legacy organisations, predating the creation of Midlothian Council in 1996, have been involved in the provision of care of children going back to living memory. During this time there is the likelihood that the care children received fell below standards of care now in place. There is the further potential the some people in the care of Midlothian Council and its legacy organisations were subject to abuse by those who where employed to care for them.** Risk Event: **The Scottish Government began an Inquiry into cases of Child Abuse occurring prior to 17 December 2014, the intention of this enquiry is to identify historic case of abuse which have to date gone unreported.** Risk Effect: **If the inquiry finds historic cases of abuse in Midlothian this could damage the reputation of the Council and could place doubt in the eyes of the public as to the safety of these currently in care. There is significant scope for a substantial financial impact arising from claims of historic abuse. Some existing employees may be affected by the inquiry and subsequent claims of abuse.**	**Joan Tranent**	**The Council have set up an Abuse Enquiry Project Team to support the Council to prepare for information requests to support the Inquiry.** **The Project Team have established a Project Plan covering:** **1. Residential establishments, List D Schools and Foster Carers: identifying Children's homes, Foster Carers and any List D Schools in Midlothian over the last 100 years and researching historic records.** **2. Record Audit: reviewing the Council's existing paper and electronic recordkeeping systems to identify relevant records and map them to** **residential establishments. This also includes, where possible, noting the Council's historic recordkeeping policies, such as retention schedules.** **3. Cataloguing/Indexing: checking and updating existing recordkeeping systems for accuracy and consistency, enabling effective information** **retrieval when requested by the Inquiry.** **4. Ascertaining the succession and insurance position in relation to potential historic child abuse claims.** **5. Ascertaining and agreeing Midlothian Council's legal position/ approach in dealing with the potential historic child abuse claims.**	**4**	**5**	

1 OPPORTUNITIES

SRP.OP.01 Shawfair

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.OP.01	**The Shawfair development with its new Rail link provides a major incentive for house builders, employer's retail and commercial interests including opportunities to secure a low carbon community through district heating from Zero Waste.**	**Ian Johnson**	**1. Shawfair Development Group.** **2. Legal agreement with developers** **3. Secured developer contributions (Section 75)** **4. Plan for entire community:** **5. Business and industrial provision, including small business incubator space.** **6. Circa 4000 new homes** **7. A school campus comprising Early Years, Nursery, Primary, Secondary & Life Long Learning provision** **8. New Primary schools**	**5**	**4**	

SRP.OP.02 Borders Rail

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.OP.02	**Regeneration of priority communities of Midlothian through which the railway passes.** **The line provides ready access to education/training at Edinburgh College, Borders College and Queen Margaret University with improved access to the labour markets in Edinburgh and the Borders. Also a catalyst for housing growth.** **Ensuring Midlothian secures appropriate levels of Blueprint funding.**	**Ian Johnson**	**1. Designated Project Manager post.** **2. Maximising the Impact: A blueprint for the Future - published by the blueprint group involving Scottish Government,** **Scottish Borders, Midlothian and City of Edinburgh Council, Transport Scotland, Scottish Enterprise and Visit Scotland. The** **document sets out the ambitions of the partners to realise the full potential of the new Railway.** **3. Dedicated Inward Investment Co-ordinator post** **4. Dedicated Tourism Development post.** **5. Timely submission of bids for approval by the Blueprint Group.**	**5**	**4**	

SRP.OP.03 Easter Bush - Penicuik

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.OP.03	**Fast Growing opportunities in Science Technology Engineering and Mathematics (STEM) with opportunities to link with education. Partnership links to schools and university sector at the Bush to promote STEM.** **Link to City Deal**	**Ian Johnson**	**1. Planning in place around creating Secondary Schools as centres for excellence linked to specialisms including STEM.** **2. Land allocated for expansion.** **3. Easter Bush Development Board.** **4. Troubleshooting issues - Roads Access - tackling road access through proposal in the Local Plan.**	**5**	**4**	

SRP.OP.04 City Deal

Risk Code	Risk Identification	Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
SRP.OP.04	**South East Scotland Region City Deal - a bid for funding to Scottish and UK Governments to accelerate economic growth through investment in infrastructure/ housing/ skills and innovation.**	**Ian Johnson**	**1. Key projects identified.** **2. Consortium submission made, including Midlothian Council in September 2015 with and update in December 2015.** **3. Heads of terms agreed by consortium for discussion with Scottish and UK Government Officials.**	**3**	**5**	

Related Action Code	Related Action	Related action latest note	**Managed By**	Due Date	Status
SRP.OA.05.01	**City Deal submission**	Q3 16/17: **Detailed discussion and negotiation with UK Government and Scottish Government Officials towards a City Deal sign off in 2017.**	**Ian Johnson**	**31-Dec-2017**	

Business Transformation Programme - Update report February 2017

Report by Kenneth Lawrie, Chief Executive

1 Purpose of Report

The purpose of this report is to present the Business Transformation Programme – update report to Audit Committee.

2 Background

2.1 The Business Transformation Programme, Follow-up Review Report produced by Internal Audit and reported to Audit Committee in September 2016 noted the following recommendation with a target date of 31 December 2016:

'An annual update report summarising the work of Business Transformation should be produced and submitted to BTB, BTSG, Audit Committee and Council. This should summarise the active business transformational work streams, transformation funded projects, benefits realised and transformation savings'

2.2 The report attached as Appendix 1 is a response to the outstanding recommendation. Members should note that as the first annual report this looks back over a number of years to provide some background to the programme.

3 Report Development

3.1 The report has been drafted using input from various sources including existing information available in the regular reporting requirements for Business Transformation governance and also from key officers involved in the various strands.

3.2 Prior to presentation to Audit Committee the report was presented to and considered by a senior officers group and Business Transformation Steering Group.

3.3 It is recognised given the scale of the future financial challenge that it will be necessary to robustly track savings and performance across the full scope of the transformation programme and all other work programmes contributing to the delivery of the financial strategy. The annual report will be an important element of that approach.

4.1 Resource

There are no direct resource implications arising out of this report.

4.2 Risk

The report responds to issues and risks previously identified in a review carried out by Internal Audit.

4.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☐ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☐ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

4.4 Key Priorities within the Single Midlothian Plan

Although this report does not relate directly to the key priorities within the Single Midlothian Plan, ensuring an appropriate focus on transformation activity and programmes ensures effective use of resources to support the Council's objectives.

4.5 Impact on Performance and Outcomes

The Council's performance and outcomes will be improved by delivery of an effective Transformation Programme.

4.6 Adopting a Preventative Approach

Having a robust Transformation Programme contributes to safeguarding the Council's financial resources and delivery of services.

4.7 Involving Communities and Other Stakeholders

As the report is an internally driven requirement development has required engagement with relevant officers.

4.8 Ensuring Equalities

There are no equalities issues with regard to this report.

4.9 Supporting Sustainable Development

A robust transformation programme reduces the risk of threats to sustainable development.

4.10 IT Issues

There are no IT issues with regard to this report.

5 Summary

The Business Transformation Programme Update Report has been developed to respond to an outstanding Internal Audit recommendation and should enhance ongoing reporting and monitoring.

6 Recommendations

The Audit Committee is invited to:

1. Note and Consider the report

Appendix 1 –
Transformation Programme Update Report – February 2017

Date 14th February 2017

Report Contacts:
Nancy Brown
Transformation Programme Manager

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Tel No 0131 271 3444

Transforming the way we work

Midlothian Council
Business Transformation Programme – Update Report February 2017

Introduction

This report provides a snapshot of the Business Transformation Programme to date. This is in line with the recommendations of Internal Audit's review of September 2016. To date the Transformation Programme has played an important role in driving improvement in Midlothian in line with the Council's ambitious agenda, whilst also generating significant savings to enable the Council to meet its budget challenges.

It is recognised given the scale of the future financial challenge faced by the Council, as set out in the Financial Strategy, that it will be increasingly vital to robustly track savings and performance across the full scope of the Transformation Programme and all other work programmes contributing to the delivery of the Financial Strategy. An annual report in respect of this will be an essential part of providing the Audit Committee and the Council with the necessary assurances about the progress and direction of this work and it is intended to further develop this report in future years to meet that need.

Our Transformational Aims...

...and Outcomes

Review and transform Midlothian Council services to ensure they are effective, efficient and economically viable and achieve the best outcomes for the people of Midlothian.

Provide a modern, consistent, reliable and efficient service to customers, including maximising self service and interactive service delivery though all available channels.

Work with our key partners to deliver and commission shared and collaborative services and products to facilitate savings, improvement, efficiency and innovation.

Work with our communities to build confidence and capacity.

Develop a supported, engaged and high performing workforce.

Provide a modern, flexible, efficient and cost effective workplace for employees that facilitate effective and efficient working practices, improves service delivery and acts as a catalyst for culture change.

OUR TRANSFORMATION PROGRAMME JOURNEY

Midlothian Council, along with all local authorities, has experienced and will continue to experience significant challenges. The Council continues to face unprecedented challenge as a result of constrained funding combined with demographic cost pressures and a number of additional national and local challenges including welfare reform and significant differences in social and economic equality across Midlothian. By adopting a Transformation approach, we have become more efficient and at the same time we have delivered changes resulting in improvements to the way we work, the services we deliver and the quality of life experienced by local people. These changes are evidenced in the delivery of new affordable homes, new schools, improved recycling rates, improved positive destinations for school leavers and the arrival of the Borders railway. In addition we have successfully delivered significant changes and improvements in services to protect children and vulnerable adults

In response to the changing context the Transformation Programme has been subject to regular review and change. The initial programme approved in February 2010 and the original Business Transformation Strategy 2010-2015 approved in June 2010 identified six key components and associated work streams of: Service Reviews; Asset Management; Organisational Review; Customer Services; Shared Services and Procurement. The programme was further developed with a revised strategy and programme presented to Council in May 2013 which reaffirmed the governance structure and requirements supporting the following transformation strands:

- Business Services (including Procurement, Purchase to Pay, EDRMS and HR Transactions)
- Customer Services (including Telephony, Customer Satisfaction, Complaints Handling and Customer Care)
- Effective Working in Midlothian (Asset Rationalisation including fit for purpose buildings and work spaces and effective working practices)
- Integrated Service Support (including Services Support, Performance Management and Management Structure)
- People (including Culture, Recognition, Working Lives, Management Development, Performance and Development and Mi-Future)

- Systems Reviews (using Systems Thinking methodology to support whole system reviews in Children's Services and Housing and Homelessness)
- Partnership Working (joint initiatives with East Lothian Council)

Following further review and rationalisation of the above strands the programme identified for the period 2014-17 was revised as shown in Figure 1 and this resulted in there being eight key strands for transformation, with a number of early activities being transitioned to business as usual/ongoing projects with responsibility for delivery transferring to the appropriate Head of Service/Service area.

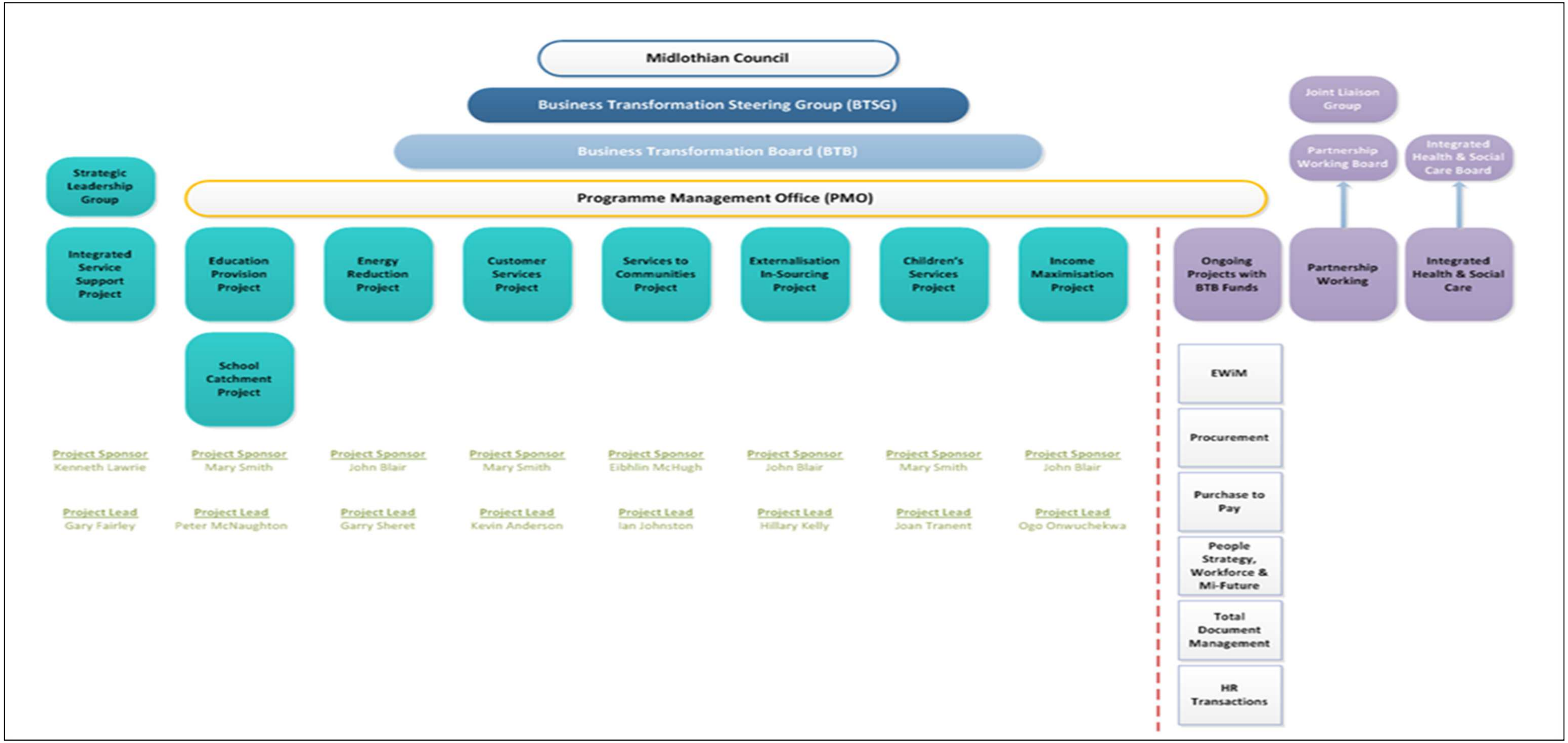


Figure 1: Council Transformation Model 2013/14

To provide more visibility and rigour to the financial savings identified for the Transformation Programme the Head of Finance and Integrated Service Support, in introducing a Financial Strategy and regular reporting for members, incorporated an update on the financial position for the programme within the Financial Strategy Report to Council on 4 February 2014. In addition, whilst no longer key strands within transformation, the importance of the need to deliver against the financials for Asset Management and Workforce are also incorporated within the Financial Strategy report and ongoing updates.

In Grant Thornton's External Audit Report presented to Council in December 2014, the following was recommended:

'As one of the smaller councils in Scotland, Midlothian has limited capacity to support significant transformation programmes. There are currently 8 work streams supported by the Council's transformation team and reported to the Business Transformation Steering Group, but not all of the work streams would be considered transformational. We recommend that the transformation program is streamlined to focus support and resources on the areas that will have the biggest impact on the Council's priorities and savings.'

In acknowledging this issue and following agreement with the Business Transformation Board and the Strategic Leadership Group three of the non-transformational strands (Externalisation/Insourcing, Energy, and Income Maximisation) were transitioned out of the Transformation Program and into the Delivering Excellence Framework approach (July 2015) for the appropriate officers to progress. In line with the auditor's feedback the shift in the programme over the last year has allowed a refocus on the areas of high impact, cost and true reshape of key services and the number of transformational strands to reduce to five as shown in Figure 2.

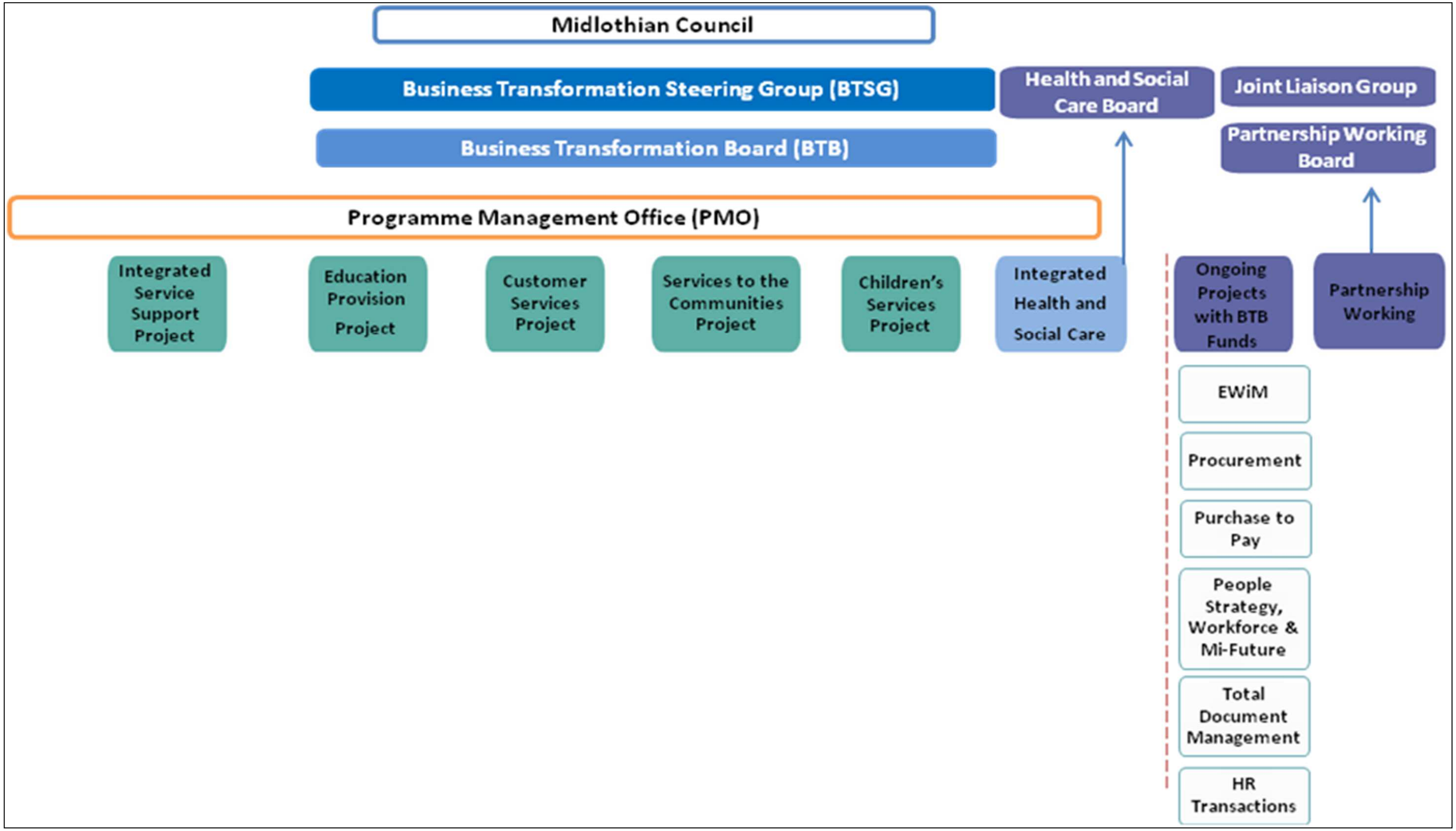


Figure 2: Council Transformation Model as at 2015/16

Financial position

Delivery of the financial savings element of the programme has been and will continue to be a key contributor to the wider change programme aimed at addressing the projected budget shortfalls. An overview of the targeted and achieved savings is shown in Table 1. Savings achieved to date (31/3/17) total £12.310 million which equates to 6.3% of the 2016/17 budgeted net expenditure.

Table 1: Transformational Savings

Financial Year	Saving Category	Target	Achieved	Variance
		£m	£m	£m
2011/12 & 2012/13	Transformation Programme	7.592	5.735	-1.857
2013/14	Transformation Programme	1.199	1.737	0.538
2014/15	Transformation Programme	1.995	1,952	-0.043
2015/16	Transformation Programme	1.721	1,730	0.009
2016/17 (Q3 Projection))	Transformation Programme	1.659	1.156	-0.503
Totals		14.166	12.310	-1.856

Council has approved utilisation of £7.718 million of General Fund Reserves to fund costs associated with the ongoing transformation programme. At this time £3.287 million of this has been applied with future commitments of £0.593 million identified for 2017/18 and 2018/19. This leaves £3.838 million as uncommitted.

Table 2: Business Transformation Funding

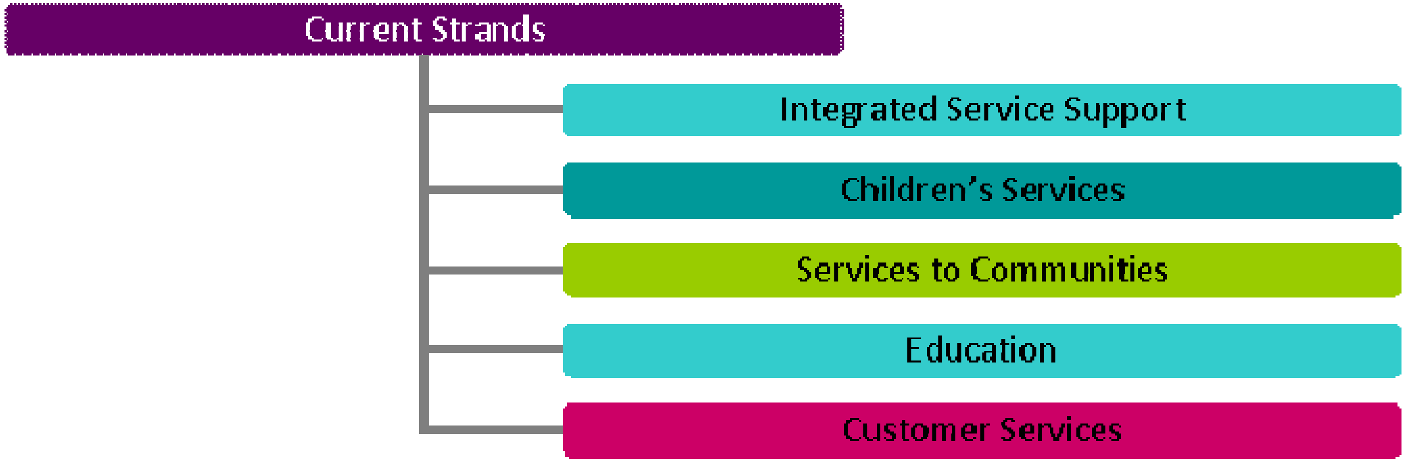
Activity	Approved Funding	Projected spend to 31/3/17	Funding Remaining
Programme Management	151,318	151,318	0
Programme Facilitation	291,987	326,889	-34,902
Systems Thinking	130,140	119,580	10,560
Customer Services	337,651	321,651	16,000
IT Support	468,000	115,845	352,155
People Strategy and Organisational Review	833,342	835,419	-2,077
Shared Services	113,478	113,478	0
Procurement	144,000	144,000	0
Asset Management	10,300	10,300	0
Purchase to Pay	40,000	40,000	0
EWiM	150,000	150,000	0
Externalisation / Insourcing	10,000	10,000	0
Income Maximisation	151,446	151,446	0
Service Reviews			
Secondary School Management	60,061	60,061	0
Property Services Mobile Working	72,260	72,260	0
Arts, Creativity, Regeneration and CLD	19,796	19,796	0
Older Peoples Services	125,500	44,638	80,862
Childrens Services	55,900	55,900	0
Community care - Internal and Shared Services	30,000	0	30,000
Mobile and Flexible working	33,400	33,400	0
TDM	258,000	258,000	0
Family Resilience Project	85,602	85,602	0
Schools Review	148,000	148,000	0
Renewable Energy	160,000	20,000	140,000
Total	3,880,180	3,287,582	592,598

Financial position for each of the current strand of transformation is detailed later in the report.

A shift in our programme over the last year has responded to the need to refocus the programme and strands on areas of high impact and cost and the need to reshape key services.

This is as a result of a number of factors including

- Grant reductions and prospects for future years financial resources
- Current spending pressures
- New spending commitments
- Demographic and cost pressures
- Risk of non delivery of saving targets



The latter part of 2016 saw Integrated Health and Social Care appearing within the transformation Section of the Financial Strategy with savings of £1.550 million set for 2017/18 (note this activity has always been visible to BTB/BTSG)

Successes from the Programme enablers include:

People and Organisational Development – People Strategy

A key enabler to support the organisation through change, focusing on having the right people, with the right skills, working in the right way.

Achievements through this enabler include the development of smarter working policies for:

- Promotion and support of flexible working;
- Promoting Midlothian as an employer of choice and improving the employment deal;
- Ensuring we have a workforce profile that adapts as the organisation changes; and
- An Investing in Our Workforce strategy to reshape the relationship with employees

Digital Foundation – Digital Strategy

A number of smarter working initiatives have been piloted during 2015/16, testing new technology that can assist our transformational activity.

These new ways of working help the Council to adopt new and modern working practices and underpins a great deal of transformation across the council. Examples include the introduction of multi functional printing, scanning and copying devices (removing traditional table top printers) and end to end transactions processing through Purchase to Pay

Transformational toolkit/Resources

Our Transformation Team work with managers across the organisation to support, build organisational strength and capacity to manage change. The team deploy a range of skills and our toolkit includes:

- Project Management
- Coaching and Mentoring
- Change methodology
- Business Case development
- Information Analysis

Transformation Officers deploy a variety of tools and techniques across a range of activities in their wider Council support role and all are accredited with the nationally recognised Systems Thinking methodology, a core tool applied within the transformation strands.

In addition to supporting the wider transformation and change agenda, a key focus of the Transformation Unit, and in particular the Programme Management Office (PMO), is to provide appropriate assurance around delivery of the Transformation Programme and the supporting governance framework. See page 18 for programme assurance.

Transformation Strand Case Studies

Customer Services

The 2015-18 Customer Service Strategy sets out our commitment to:

- Listen, engage and involve our customers in the future design of our services.
- Improve customer access and deliver services locally.
- Introduce new services and change the way we do things.
- Work in partnership with others and delivering services from co-localities.

Through significant service redesign our customer service teams, identified channel shift efficiencies, telephony integration, automation of applications and transactions and customer service asset rationalisation we are meeting the challenge of transforming our service. Since the project commenced we have:

- Realigned our customer service functions (libraries, customer service points, contact centre, and registration services) and created service flexibility and resilience through the implementation of phase 1 of the Customer Service staffing review.
- Developed and launched of a new responsive Council website to improve customer accessibility and functionality.
- Secured funding for the upgrade and extension of free public WiFi provision across libraries, our mobile library and right across our hub buildings.
- Signed up to the Digital Participation Charter, along with other organisations as part of a national initiative to promote digital participation and basic digital skills.
- Launched our new mobile library service into communities across Midlothian and established a shared service arrangement with our neighbours in East Lothian.
- Established the Mayfield Library and Customer Hub creating a place where we offer frontline services and support locally within the community.

- Delivered an automated contact portal for external switchboard calls and moved our main switchboard number to our customer contact centre to offer first time resolution, reduce the double handling of enquiries, and ensure distribution of calls across all available customer service advisors.
- Designed new library and customer service provision for inclusion in the new fit-for-purpose community hub buildings at Loanhead Paradykes and Newbattle. Working in partnership with our colleagues in schools, leisure, health and early years, our new service will be open in Paradykes later in 2017 and in Newbattle later in 2018.
- Carried out a range of projects and activities to extend services to our wide range of different users groups including:
  - Extended funding for our Bibliotherapy services
  - Supporting the Macmillan Living Well in Midlothian project with dedicated space provided at Lasswade Library.
  - Secured funding to work in partnership with Creative Scotland to increase access to film resources for communities across Midlothian.
  - Extended funding for our Connect Online digital support services in partnership with Volunteer Midlothian to provide a range of digital learning opportunities.
  - The launch of Codling Clubs (computer programming) for primary aged children in our libraries across Midlothian.
  - Secured funding from the Scottish Library and Information Council, for the development of 3D printing services, the launch of Appiness – a digital project for under 5s and their parents and the commitment to ensuring that every child is a library member from birth.

Listening to our customers is fundamental to the continued redesign of our services. The feedback from the 'Choices for Change' public consultation for Libraries and Customer Service, will inform future proposals on the rationalisation of library opening hours, alternative models of service delivery, and how best we can deliver core services locally.

Target Savings 31.3.17(£)	£350,000	Delivered Savings 31.3.17 (£)	£240,000

Children's Services

Our vision is to improve families' lives by giving them the support they need, when they need it. We support children, young people and their families to manage a number of difficulties and traumas so that they can fulfil their potential and experience fulfilling and positive lives.

We have recently undertaken a 'whole system' review of children's services, taking the opportunity to re-build the foundation of our service provision by re-directing resources to provide earlier levels of support, reducing demand for and minimising the high costs incurred and improving outcomes for the children and young people involved.

There is significant evidence that responding at an earlier point of intervention prevents situations escalating and often results in more positive outcomes for families. In response to this and to the feedback shared, we have introduced three Early Intervention and Prevention teams, consisting of social workers and practitioners. Early engagement, underpinned by the Getting It Right First Time principles, ensures that children have the best start in life and families get the right support when it is needed.

Working with education services, we hope to be able to re-invest money into our own local infrastructure so that we can ensure we have the skills, experience and capacity to meet the needs of those children and young people who struggle to be educated within our mainstream provisions. We also have an ongoing fostering campaign to recruit more local foster carers so that we do not have to use external carers who often live a long way away from Midlothian. Our vision moving forward is to prevent children and young people being placed in external foster placements and meet their needs within Midlothian.

Target Savings 31.3.17(£)	£950,000	Delivered Savings 31,3,17 (£)	£1.986m

Integrated Service Support

The integrated service support project sets out to consolidate key support services, review and challenge service delivery and priorities as well as management arrangements and ensure appropriate spans of control through layers and specialism's. With the aim to deliver service improvements and achieve cost efficiencies by eliminating duplication and silo working and support the delivery of service 'enablers' and services across the council.

Key successes include:

- Key support functions merged across all 3 Directorates
- Creation of a 'fit for purpose' Finance and Integrated Service Support Management team
- Creation of Workforce Profiles across the organisation
- New entry level jobs created for school and college leavers (positive destinations recruitment)
- Team succession planning and career paths strengthened

Target Savings 31.3.17 (£)	£2.340 million	Delivered Savings 31.3.17 (£)	£1.858 million

Education

The Councils aspirations for Education are high. A key priority will be to continue to make sure our youngster progress to positive destinations after leaving school. The latest position highlights that 95.1% of school leavers have gone on to further education, jobs or volunteering. The figures are 1.7% above last year's Midlothian figures and 1.8% above the national average with Midlothian Council now ranking joint 4th when comparing performance across the 32 local authorities. In comparison in 2008/9 only 78.4% of school leavers had a positive destination.

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Our delivery of world class education is a priority. We aim to review and streamline processes and structures to appropriately utilise education staff across all of our schools. We want to ensure we deliver the most cost effective pre-school provision giving children access to a wider curriculum and educational experiences. A new preferred pre-school provision model has been delivered with a minimum annual saving of £368,000.

A review of the secondary provision will move away from an age/stage basis to organising opportunities that create pathways that enable young people to pursue their choices. The principals of the models of delivery have been developed and all six secondary schools will move to the new timetabling model which will be implemented over the next two years.

A strategy for Midlothian's learning estate which plans for new schools in Midlothian for the next 10 to 20 years will be developed and support the implementation of the Local Development Plan. It is proposed the strategy is submitted to Council in summer 2017. The work to review and rationalise the schools estate and catchment areas is complex and involves contributions from many services across the organisation. In order to make this flow as well as possible establishment of a School Estate Planning Group has been

Target Savings 31.3.17 (£)	£1.044 million	Delivered Savings 31.3.17 (£)	£947,000

Services to Communities

This strand of transformation was agreed in 3 phases:

Phase 1. A new transparent approach to awarding grants was successfully introduced in 2015/16 with £300k savings delivered to date rising to £500k in 2017/18.

Phase 2. A streamlined and focused review of structures within Lifelong Learning and Communities teams has provided an good foundation for resources to be deployed across Midlothian but with emphasis on those areas of priority and higher levels of inequality

Phase 3. Development of an approach to focus on the 3 priority areas (Woodburn/Dalkeith, Mayfield/Easthouses and Gorebridge) that will build strong communities where individuals and families have opportunities to improve their health and wellbeing, achieve their aspirations through education and employment, feel safe, and can play an active part in their local community.

Alongside this, it is recognised that local people are often best placed to support each other and take positive action to improve their area. Individual residents can take action that has a significant impact on their family, friends and neighbours, from volunteering with a local group, improving their own health and wellbeing, or just by being neighbourly.

Each of the 3 Priority areas has Neighbourhood plans and local action plans (developed with local people). At a strategic level, regeneration work progresses on improving Town Centre regeneration and investment in physical condition of premises.

Target Savings 31.3.17 (£)	£300,000	Delivered Savings 31.3.17 (£)	£300,000

Integrated Health and Social Care

Whilst Integrated Health and Social Care is not a formal strand of the Transformation Programme, the governance framework in terms of reporting to the Board and the Strategic Group is a mechanism used to ensure awareness of the current position of the integration agenda.

Integration of Health and Social Care in Midlothian went live in April 2016 when the Midlothian strategic commissioning plan for 2016-19 came into effect. This signalled a very significant change, delivering sustainable health and social care services for the future that focus on people's needs.

The new integrated arrangement is responsible for delivering a range of nationally agreed outcomes that apply to adult health and social care across Scotland. These include:

Improving adult health and social care services

Delivering more services in community settings

Reducing inequalities

Improving health and care outcomes for local people.

The regular Transformation updates focus on the foundations of progress on governance and not in relation to change/improvement initiatives planned (these are reported to Integrated Joint Board)To date the following arrangements have been put in place:

- Integrated Joint Board established
- User/Carer Collaborative in place
- New Public Partnership Forum arrangements agreed
- Joint Management Team in place/ Revised Senior Management Structures under consideration
- Interim Professional Leadership for AHPs agreed
- Risk, performance and communication frameworks agreed

Managing the programme - Programme assurance

A key focus of the Transformation team, and in particular the Programme Management Office, has been to provide appropriate assurance around delivery of the Transformation Programme ensuring that projects are delivering to time, cost and quality, that the information being reported about the programme is correct.

Following an Annual Health Check and internal audit, some of the key ways in which we have improved our approach to providing assurance around the delivery of the Transformation Programme include;

- Developing and implementing strategies, processes and tools to ensure a consistent and effective approach to managing risks and realising benefits across the Transformation Programme
- Evaluating whether the right projects are being taken forward within the Transformation Programme, assuring that those projects are supported by robust business cases and appropriate governance arrangements
- Improving project and programme level monitoring and reporting to ensure the right information is collected and clear and accurate view on delivery progress is provided. In turn, providing Business Transformation Board and Steering Group with the assurance that Programme is on track to achieve its objectives and where appropriate identify areas where further support is required.
- As part of our commitment to continuous improvement, we will focus over the forthcoming months on continuing to work with key stakeholders to identify where strengthening assurance arrangements can enhance delivery of the Transformation Programme

Our evolving change agenda – Delivering Excellence

This annual report sets out the significant progress that is being made in the area of transformation across the council, and there is still so much more for us to do. Moving to a more agile and responsive approach to the delivery of change and service transformation will ensure that the council continues to identify and act on opportunities for continuous improvement, service efficiency and transformation across all areas of the council.

Our employees are key to the successful delivery of the new transformation programme, and as such the development to shape and lead transformation projects has never been more critical. All staff will be expected to work in new and different ways, will have the tools for the job and will know what is expected of them. A programme of cultural change and different ways of working across the council will be essential as the council moves forward on this next phase of Transformation. Areas of focus for change will include:

1. Delivery of our services in new and effective ways, using the most up to date thinking, the joining of complimentary services and effective partnership working to provide better outcomes for our customers.

2. Helping our customers and communities to become and remain independent by understanding needs and by providing appropriate responses.

3. Reviewing our commissioned services and securing the best deals possible through; ensuring effective contract management.

4. Continuing our changes to become a more modern council, improving our use of digital approaches, improving access to information and increasing our self-service offering for customers where it makes sense to do so.

5. Shaping structures, resources and ways of working, to reflect a lean and effective model that; remains responsive to the challenges and priorities ahead.

6. Maximising income generation by reviewing our charging models to help generate a contribution that protects front line services.

Next Steps

The latest Financial Strategy report to Council sets out the longer term projected budget shortfalls for the period 2017/18 to 2021/2022 and the contribution change activity will have in reduceing the projected shortfalls. This includes further savings across the strands of the transformation programme of £2.791 million in 2017/18 rising to £5.437 million by 2021/22 . Taken together with the savings delivered to date set out earlier in this report overall savings for the transformation programme are expected to be in the region of £17.8 million, or 9% of net expenditure.

Whilst the existing and planned change programme go some way to addressing the projected budget shortfalls there is still more to be done to move from longer term financial projectios to the development and agreement of a longer term financial plan which sets out the actions to balance future years budgets.

As the organisation evolves, the need for a more flexibly designed Change Programme becomes essential. The introduction of Delivering Excellence will help us to ensure the programme is realistic and achievable whilst still ultimately ensuring that the associated benefits (both financial and non-financial) in supporting the delivery of the Financial Strategy are achieved.

Midlothian

Internal Audit Plan 2017/18
Report by Internal Audit Manager

1. Purpose of the Report

The purpose of this report is to:

- present the draft Internal Audit plan for 2017/18;
- explain how the plan was developed; and
- seek Audit Committee comments on the draft plan.

2. Background

Risk Based Plan

The Public Sector Internal Audit Standards require the Internal Audit Manager to develop a risk based audit plan which sets out the priorities for the internal audit activity during the year. These priorities need to be consistent with the Council's goals. In order to achieve this requirement, the 2017/18 plan has been developed following a review of:

1. Midlothian Council's priority themes and objectives;
2. Midlothian Council's risk management framework including operational, project and strategic risk registers which detail the key risks, their likelihood and potential impact as well as detailing controls and residual risk;
3. Midlothian Council's quarterly Performance reporting to the Performance Review and Scrutiny Committee;
4. any budgeted overspends;
5. the previous year's annual governance statement and any issues raised;
6. the impact of national issues (eg economic factors or the introduction of new legislation);
7. the impact of local issues (eg corporate or service action plans and issues raised by external assurance bodies);
8. the available audit resource and skills;
9. the need for specialist skills, where they are not available already;
10. staff development and training;
11. an assessment of the time needed for the management of the Internal Audit Service (eg audit planning, development of the annual audit opinion, attendance at meetings, the appraisal process, the updating of relevant audit policies and procedures);
12. the need to establish a contingency for consultancy, ad hoc reviews or fraud investigations;
13. the balance of coverage required so External Audit can place reliance on Internal Audit's work;
14. the need to undertake periodic reviews of core financial and operational systems in line with Internal Audit's three year strategy;

15. Internal Audit's own knowledge and experience through previous internal audits, consultancy work and investigations (including follow up reviews of recommendations raised);
16. input received from senior management (all Heads of Service) and the Corporate Management Team; and
17. work undertaken by other assurance providers.

The Audit Plan has been developed using the process detailed in the Audit Charter approved by the Audit Committee on 10 May 2016.

Internal Audit has developed its own Audit Universe and scored all elements on a high, medium or low basis. This universe has then been used to derive the Audit Plan.

The plan is fluid and can be adapted to accommodate any escalation of risks coming to light through the risk management process or any change in Internal Audit resource.

Key areas and Internal Audit Manager's opinion on governance, risk management and controls

The Internal Audit Manager is required to deliver an annual internal audit opinion on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control. In order to allow the Internal Audit Manager to form an opinion, the audit plan needs to be sufficiently broad to cover key areas over a regular cycle and for this reason a number of core processes and systems are reviewed on a regular basis.

Consultancy and Help Desk

Some audit resource is set aside for consultancy engagements based on the engagement's potential to improve management of risk, add value and improve Council operations.

Time is also made available to assist with requests for Internal Audit assistance through the operation of a help desk facility. This is used to support Council Services who are looking for advice or support on risk or control related issues.

Corporate Fraud

The 2017/18 plan provides resource for Corporate Fraud. This resource will be used to help identify and / or investigate any suspected internal or external fraud, specific audits on vulnerabilities to fraud, Council tax investigations, reviewing of NFI matches and the provision of fraud awareness training to management and employees.

Reporting Calendar

Appendix 2 shows the timing of likely reports to individual Audit Committees for information.

3. Proposed Internal Audit Plan

Appendix 1 details the audits and reviews Internal Audit plan to deliver against the available number of days.

Conclusion

The above approach is aimed at allowing audit resource to be allocated to high risk areas in the Council but also allows the Audit Manager to conclude on the governance, risk management and controls more generally.

4. Report Implications

4.1 Resource

The Internal Audit Section has an FTE of 3.7 and an additional 2 FTE fraud officers. After deduction for holidays, sickness, training, management and administration this equates to a total of 1058 days available for auditing.

The Internal Audit Section is currently undergoing a Service review. This may have an impact on available resource to deliver against the 2017/18 plan.

4.2 Risk

Each Internal Audit assignment is risk-based and tests the service's management of risk. The requirement to provide resource to the Midlothian IJB and the need to undertake some audits annually may impact on the Internal Audit strategy to review all key Council processes and systems on a 3 year cycle.

4.3 Single Midlothian Plan

Themes addressed in this report:

☒ Community safety
☒ Adult health, care and housing
☒ Getting it right for every Midlothian child
☒ Improving opportunities in Midlothian
☒ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

4.4 Key Priorities within the Single Midlothian Plan

Midlothian Council and its Community Planning Partners include the following areas as key priorities under the Single Midlothian Plan:

- Reducing the gap in learning outcomes
- Reducing the gap in health outcomes
- Reducing the gap in economic circumstances

Audits within the 2017/18 plan include reviews of these areas.

4.5 Impact on Performance and Outcomes

The Internal Audit plan assists the Council in improving its performance and outcomes.

4.6 Adopting a Preventative Approach

Specific audits within the 2017/18 plan will include assessments on when a preventative approach can be adopted.

4.7 Involving Communities and Other Stakeholders

The Internal Audit Plan has been discussed with Heads of Service, the Section 95 Officer and the Corporate Management Team. The plan has also been discussed with EY (the Council's external auditors).

4.8 Ensuring Equalities

There are no equalities issues with regard to this report.

4.9 Supporting Sustainable Development

There are no sustainability issues with regard to this report.

4.10 IT Issues

There are no IT issues with regard to this report.

5. Recommendations

The Audit Committee is therefore asked to:

a) note that 80 days have been set aside for Health and Social Care within the plan but that the proposed audits and time allocated may change following input from the Midlothian Integration Joint Board Audit and Risk Committee; and
b) to otherwise review and comment on the proposed Internal Audit plan for 2017/18.

Date:	**22 February 2017**
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Internal Audit Plan: 2017/18 **Appendix 1**

Audit Reviews									
Ref	**Strategic Risk/Risk Based/Core System (S/ R/C or N/A)**	**Auditable Unit**	**Priority (H/M)**	**Total Number of Days**	**Q1**	**Q2**	**Q3**	**Q4**	**Comments**
1	S	Tyne Esk Leader Grant Fund	M	25		✓			Annual requirement to review the controls in place to deliver the Tyne Esk Leader Grant Fund and to undertake compliance related work as defined by the Service Level Agreement.
2	S	Construction Industry Scheme	M	10	✓				Annual requirement to undertake a review in this area to test that the scheme rules are being complied with as required by HM Revenues and Customs.
3	S and R	Children and Young People's Act – Named Person	H	30				✓	The Children and Young People's Act requires all children to have a named person. The audit will review the controls in place which allow the Council to implement this legislation. Postponed from 2016/17 as implementation delayed.
4	S	Climate Change Reporting	M	25			✓		This is a strategic risk for the Council. The audit will review the reporting arrangements to the Scottish Government.

Ref	Strategic Risk/Risk Based/Core System (S/ R/C or N/A)	Auditable Unit	Priority (H/M)	Total Number of Days	Q1	Q2	Q3	Q4	Comments
5	S	Highways Network Assets	M	30			✓		Requirement to review compliance with the new CIPFA Code of Practice on the Highways Network Asset.
6	S	Follow up of the 2016/17 Audit of Financial Strategy and Delivering Excellence	H	25				✓	Follow up review of the 2016/17 Audit of Financial Strategy and Delivering Excellence to determine progress with Internal Audit recommendations.
7	S and R	Pupil Equity Funding	H	40			✓		Additional ring fenced funding of £2.27M provided to help close poverty related attainment gap in schools. Review of controls over this funding.
8	S and R	Social Care Budget Planning Project	H	40		✓			To provide assurance over the Social Care Budget Planning Project currently underway.
9	R	Waste	H	40		✓			Review of controls over collection and disposal of waste. Residual waste currently being land-filled without any secondary treatment - residual waste contract currently out to tender.
10	R and C	Bank and Cash	M	40			✓		To review the controls over the collection, banking and accounting for income including online payments and compliance with PCI requirements. Postponed from 2016/17 due to the implementation of a new till / management reporting system in Leisure Services.

Ref	Strategic Risk/Risk Based/Core System (S/ R/C or N/A)	Auditable Unit	Priority (H/M)	Total Number of Days	Q1	Q2	Q3	Q4	Comments
11	R	Complaints	M	30	✓				Performance reports highlight that performance indicators are off target for all Services. To include a review of controls operating over FOI requests.
12	R	Council Owned Care Homes	H	30		✓			To review controls over the management of Council owned care homes.
13	C	Payroll	M	30				✓	Core system with significant value of payments. Scope to include controls over Electronic Payments.
14	C	Treasury Management	M	30	✓				Core system. To test controls over policies and practices, strategies and reporting and compliance with the Treasury Management Code of Practice.

Corporate Fraud Reviews									
Ref	**Strategic Risk/Risk Based/Core System (S/ R/C or N/A)**	**Auditable Unit**	**Priority (H/M)**	**Total Number of Days**	**Q1**	**Q2**	**Q3**	**Q4**	**Comments**
1	S	Vetting of Employees	H	30	✓				Action from Integrity Group. Review of vetting of new / existing employees to ensure that references obtained, PVG and Disclosure Scotland checks undertaken, membership of bodies maintained (eg SSSC), secondary employments and any convictions are disclosed.
2	R	Insurance Claims	H	15				✓	Review of controls to prevent insurance frauds particularly those below the Council's excess level.
3	R	Contract Compliance – Building Maintenance Services	H	15			✓		For a sample of contracts, check a sample of invoices to ensure that contract conditions are being adhered to.
4	R	Subletting of Council Owned Properties	H	30		✓			Local data match of Council tax system to house rents system to identify potential subletting of Council houses.
5	R and C	Council Tax Reduction Scheme and Discounts and Exemptions	M	50	✓	✓	✓	✓	Investigations for Council tax reduction scheme and discounts and exemptions to determine whether these reductions are claimed legitimately.

Ref	Strategic Risk/Risk Based/Core System (S/ R/C or N/A)	Auditable Unit	Priority (H/M)	Total Number of Days	Q1	Q2	Q3	Q4	Comments
6	C	National Fraud Initiative	M	55	✓	✓	✓	✓	To co-ordinate the NFI exercise, review and investigate matches and produce reports for the Audit Committee on the outcomes from these matches.
7	R	Fraud Awareness Training	M	10	✓	✓	✓	✓	A budget is set aside to allow fraud awareness training to be provided by the Corporate Fraud team to Council management and employees.

Annual Audit Work									
Ref	**Strategic Risk/Risk Based/Core System (S/ R/C or N/A)**	**Auditable Unit**	**Priority (H/M)**	**Total Number of Days**	**Q1**	**Q2**	**Q3**	**Q4**	**Comments**
1	R and C	Recommendation follow up Reviews	H	35		✓		✓	2 reviews are undertaken. The first notes performance against closing issues by the agreed due date while the second includes a sample check on the adequacy of actions taken against issues which are flagged as closed.

Ref	Strategic Risk/Risk Based/Core System (S/ R/C or N/A)	Auditable Unit	Priority (H/M)	Total Number of Days	Q1	Q2	Q3	Q4	Comments
2	R and C	Review of Corporate Governance	M	10				✓	Internal Audit each year tests a sample of the key elements in the Code of Corporate Governance to determine whether these are operating as described. The results from this testing are included in the Annual Governance Statement.
3	R and C	Annual Assessment of Internal Controls	M	10				✓	Internal Audit each year prepares an annual report for the Audit Committee summarising the work undertaken by the Internal Audit Section and forming an opinion on the adequacy of the control environment within the Council.
4	N/A	Assessment of Internal Audit against PSIAS and of the Audit Committee against the CIPFA code.	M	15				✓	Each year the Internal Audit Section undertakes a self assessment against the Public Sector Internal Audit Standards and reports its findings to the Audit Committee. This year there will also be an external assessment. In addition assistance is provided to the Chair of the Audit Committee in undertaking an assessment of the Audit Committee against the CIPFA guidance.
5	R	Consultancy (4 at 30 days each)	H	120	✓	✓	✓	✓	Time is set aside in the plan to undertake any consultancy work / emerging risks.
6	R	Investigations (3 at 30 days)	H	90	✓	✓	✓	✓	Time is set aside in the plan to undertake any investigations.

Ref	Strategic Risk/Risk Based/Core System (S/ R/C or N/A)	Auditable Unit	Priority (H/M)	Total Number of Days	Q1	Q2	Q3	Q4	Comments
7	R	Help Desk Enquiry system	H	34	✓	✓	✓	✓	Internal Audit has a help desk facility where guidance and advice is given to management on internal controls. The help desk is also used to manage any enquiries received through the whistle blowing facilities offered by the Council.
8	N/A	Administration of Audit Scotland Reports	M	4	✓	✓	✓	✓	Internal Audit co-ordinates submission of Audit Scotland Reports to the Audit Committee.
9	N/A	Support for the Risk Management and Integrity Groups	M	15	✓	✓	✓	✓	Internal Audit attends and provides support to the Risk Management Group and the Integrity Group.
10	R and C	Audit reviews and support for the Integration Joint Board	H	80	✓	✓	✓	✓	This time relates to three scheduled audits for the Integration Joint Board and all related support work.
11	N/A	Planning for 2018/19	M	15				✓	Time is set aside to allow for the development of the 2018/19 internal audit plan.

Key:

S – Strategic Risk Based Audit

R – Risk Based Audit

C – Core Process or Systems Audit

AUDIT COMMITTEE - REPORTING CALENDAR **Appendix 2**

The following sets out the proposed timetable for submission of standard reports to the Audit Committee. This does not include:

- Internal Audit and External Audit reports on individual assignments;
- Audit Scotland National Reports; and
- Reports from external scrutiny bodies where governance, risk and internal controls have been examined.

These reports will be presented when work is completed.

The Reports listed below are expected to be delivered according to the following timetable but some are provisional dates:

Area	Assigned to	September	December	March	May	June
Governance						
Council's Annual Governance Statement	Legal Services Manager				✓	
Review of Council's Code of Corporate Governance	Legal Services Manager				✓	
Internal Audit Assessment of Annual Governance Statement and review of the Council's Code of Corporate Governance	Internal Audit Manager				✓	
Audit Committee Chair Report to Council (including assessment of Audit Committee against the CIPFA Audit Committee Practical Guidance for Local Authorities 2013)	Audit Committee Chair					✓
Assessment of Internal Audit against the Public Sector Internal Audit Standards	Internal Audit Manager				✓	

Area	Assigned to	September	December	March	May	June
Review and approval of the Internal Audit Charter (following any changes)	Internal Audit Manager				✓	
Internal Audit						
Internal Audit Plan	Internal Audit Manager			✓		
Progress Reports with Current year's plan	Internal Audit Manager		✓			
Follow up on adequacy of actions taken on Internal Audit Recommendations	Internal Audit Manager					✓
Number of recommendations made by Internal Audit and percentage reported as complete by management	Internal Audit Manager		✓			
Internal Audit Manager's Annual Assurance Statement	Internal Audit Manager				✓	
External Audit						
Annual plan	EY			✓		
ISA 260 - External Audit Report to those charged with Governance	EY	✓				
Risk Management						
Review of risk registers - reporting of critical and high risks	Risk, Safety Health & Civil Contingencies Manager	✓ Quarter 1	✓ Quarter 2	✓ Quarter 3		✓ Quarter 4
Risk, Safety Health & Civil Contingencies Manager's Annual report on Risk Management Control	Risk, Safety Health & Civil Contingencies Manager					✓

Area	Assigned to	September	December	March	May	June
Fraud and Corruption						
National Fraud Initiative Report	Internal Audit Manager	✓				✓
Corporate Fraud Annual Report	Internal Audit Manager		✓			
Finance						
Treasury Management Reports (Provisional date)	Head of Finance and Integrated Service Support			✓		✓
Financial Monitoring Reports (Provisional date)	Head of Finance and Integrated Service Support	✓ Quarter 1	✓ Quarter 2	✓ Quarter 3		✓ Quarter 4
Number of Reports per meeting		**4**	**5**	**5**	**6**	**7**

Midlothian

Audit Scotland Report: Local government in Scotland: Financial Overview 2015/16 (Audit Scotland, March 2017)

Report by: Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of the Report

To provide Audit Committee with a summary of the Audit Scotland report, 'Local government in Scotland: Financial Overview 2015/16' and the Council's position in relation to the report's findings. Link to the full report here:

http://www.audit-scotland.gov.uk/report/local-government-in-scotland-financial-overview-201516

2 Background

2.1 Each year the Accounts Commission produces an overview of issues that have arisen from their local authority audits. For 2015/16 these will be encompassed in two reports. The first report assists Councils in identifying and planning for pressures they may face during 2017/18 and the report explores Councils financial and service performance and their journey of improving outcomes for service users and communities.

2.2 Local government in Scotland: Financial Overview 2015/16 was published by the Accounts Commission in November 2016. The report provides a high-level, independent view of Councils financial performance and position in 2015/16. It is aimed primarily at Councillors and senior council officers as a source of information and to support them in their complex and demanding roles. It is in two parts:

- Part 1 focuses on Councils income and expenditure in 2015/16 and trends over time; and
- Part 2 comments on the financial outlook of Councils at the end of 2015/16 and outlines important factors to be considered in assessing future spending plans.

2.3 The report is the first of the Account's Commission new overview outputs. It tells the strategic financial story for local government in Scotland in 2015/16, another challenging year for Councils. Overall, Councils responded well by controlling their spending and have also increased reserves and reduced debt. Scottish Government funding has fallen in real terms in recent years and, although there was a small annual real-terms increase in 2015/16, it fell again in 2016/17. Councils also continue to face cost pressures, including increasing pension costs and wage inflation. The Accounts Commission recognise Councils have been making difficult decisions when setting their budgets and that this has required a disciplined approach to delivering savings. This disciplined approach must continue throughout this 2017 election year, as significant challenges lie ahead and Councils need to be well placed to meet them.

2.4 In anticipation of reductions in future Scottish Government funding, most Councils have continued to increase their reserves. Councils must consider how and when reserves are used to support services, in line with their financial plans and reserves policies, as they can only be used once and relying on them is not sustainable. All Councils have identified future funding gaps that will need to be addressed through making savings or using reserves. How well placed individual Councils are to address these funding gaps is a combination of the relative size of the funding gap, the reserves they hold, and their ability to identify and make savings and to service debt.

2.5 Financial scrutiny and transparency in financial reporting are themes that recur throughout the report. Under the new *Code of Audit Practice 2016*, auditors will comment on the financial sustainability of Councils. It is important that all Councils have long-term financial strategies in place that support their strategic priorities, underpinned by more detailed financial plans and indicative budgets that cover the next three to five years. These will help Councillors and officers assess the impact of approved spending on their current and future financial position.

2.6 New Approach to Overview Reporting

This year, the Accounts Commission have developed an approach to overview reporting for local government into a series of outputs throughout the year. The Accounts Commission will examine the performance of Council services and the challenges facing Councils in their upcoming overview report in March 2017, but hope that the links between good financial and service performance remain clear.

2.7 It is hoped that the report and the supplementary information prove to be informative and help shed light on the complex nature of local government finances. The Accounts Commission welcome feedback and will use this to inform their approach to overview reporting in future years.

2.8 The key messages identified in the 2015/16 report include:

- The overall financial health of local government was generally good in 2015/16 and there was a slight increase in overall reserves and a reduction in overall debt. Auditors did not raise concerns about the immediate financial position of Scotland's Councils and, for the fifth year in a row, issued unqualified opinions on Councils accounts.

- Significant challenges for local government finance lie ahead. Councils' budgets are under increasing pressure from a long-term decline in grant funding from the Scottish Government which is expected to continue to fall in future, rising demand for services and increasing costs, such as pensions. There is variation in how these pressures are affecting individual Councils, with some overspending their total budgets or budgets for individual services such as social care. It is important that Councils have effective budgetary control arrangements in place to minimise unplanned budget variances that can affect their financial position.

- Councils need to change the way they work to deal with the financial challenges they face. All Councils face future funding gaps that require further savings or a greater use of their reserves. There is variation in how well placed Councils are to address these gaps.

- Councils spent £19.5 billion in 2015/16. Spending on providing services remains lower than in 2011/12, but is increasing in key services, most noticeably in social care because of rising demand from an ageing population. Many Councils overspent their social care budgets and this poses a risk to their longer-term financial position. Councils need to ensure budgets reflect true spending patterns so that the impact of current spending on their financial position is clearly understood.

- Over and above growing demands on services, Councils need to manage other financial pressures such as increasing pension costs and wage inflation. It is essential that Councils have long-term financial strategies and plans in place that align with their priorities and are supported by medium-term financial plans and budget forecasts.

- Long-term financial strategies must be in place to ensure Council spending is aligned with priorities, and supported by medium-term financial plans and budget forecasts. Even where the Scottish Government only provides Councils with one-year financial settlements, this does not diminish the importance of medium and longer-term financial planning. This is necessary to allow Councillors and officers to assess and scrutinise the impact of approved spending on future budgets and the sustainability of their Council's financial position.

3 Self-Assessment Tool

The Accounts Commission has produced a Self-assessment tool for Councillors which is attached at the end of this report as Appendix 1.

The self-assessment brings together a number of potential questions for Councillors related to Local government in Scotland: Financial Overview 2015/16 designed to help Councillors identify how well informed they are about each area and to highlight areas where they may wish to ask further questions and to help them better understand Council's financial position and to scrutinise financial performance. The questions are included in Appendix 1 and also included as a link on the following Audit Scotland website:

http://www.audit-scotland.gov.uk/report/local-government-in-scotland-financial-overview-201516

4 Report Implications

4.1 Resource

There are no additional resource implications.

4.2 Risk

Whilst there are no additional direct risks associated with this report, the Audit Scotland Report – Local government in Scotland: Financial Overview 2015/16 does ask members to consider the wider scrutiny and performance management and risk elements associated with their role.

4.3 Single Midlothian Plan

Themes addressed in this report:

☐ Community safety
☐ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☐ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

4.4 Key Priorities within Single Midlothian Plan

Midlothian Council and its Community Planning Partners have made a commitment to treat the following areas as key priorities under the Single Midlothian Plan:-

- Early years and reducing child poverty
- Economic Growth and Business Support
- Positive destinations for young people

This report does not directly impact Midlothian Council's key priorities but a key message within the Audit Scotland Report does make reference to the need for clear priorities.

4.5 Impact on Performance and Outcomes

The report does not directly impact Midlothian Council's and wider partners performance and outcomes but it does stress the need to ensure consideration is given to the wider strategic planning and objectives as part of the council's response to Audit Scotland's finding noted in their report.

4.6 Adopting a Preventative Approach

This report does not directly impact actions and plans in place to adopt a preventative approach.

4.7 Involving Communities and Other Stakeholders

This report does not directly relate to involving communities but the Audit Scotland Report does emphasise the need to address the requirements in the Community Empowerment (Scotland) Act 2015.

4.8 Ensuring Equalities
This report does not recommend any change to policy or practice and therefore does not require and Equalities Impact Assessment.

4.9 Supporting Sustainable Development
The recommendations in this report support Midlothian Council's position in relation to Audit Scotland's findings for the wider overview of Local government in Scotland: Financial Overview 2015/16 and therefore support ongoing sustainable development.

4.10 IT Issues
There are no IT issues arising from this report at this time.

5 Recommendations

The Committee is asked to note the Audit Scotland report and the position of Midlothian Council in relation to the report's recommendations.

Appendix 1: Local government financial overview 2015/16 - Self-assessment tool for Councillors

Date: 02 March 2017
Report Contact: Gary Fairley **Tel No: 0131 271 3110**
gary.fairley@midlothian.gov.uk

Background Papers:

Accounts Commission - Local government in Scotland: Financial Overview 2015/16 – (November 2016)

Self-assessment tool for Councillors

Code of Audit Practice 2016

Appendix 1

SUPPLEMENT 1

Prepared by Audit Scotland | November 2016

Local government financial overview 2015/16

Self-assessment tool for councillors

ACCOUNTS COMMISSION

This self-assessment brings together a number of potential questions for councillors related to *Local government in Scotland: Financial overview 2015/16*. It is designed to help councillors identify how well informed they are about each area and to highlight areas where they may wish to ask further questions.

We have also included a high-level guide to the main service expenditure on an accounting basis (as identified in the accounts) and on a funding basis (as used for budgeting purposes).

	How well informed am I?	
Questions for councillors to consider	**What do I know?**	**Do I need to ask further questions?**
Annual accounts and financial transparency (paragraphs 10 to 12)		
• Does the management commentary of our annual accounts provide a clear and easily understandable account of the council's finances?		
Funding and income (paragraphs 13 to 25)		
• How do you consider potential changes to income streams and their impact on spending and services as part of medium and long-term planning?		
• Is income from fees and charges clearly reported?		
• What increases in fees and charges are planned and how will these affect our citizens? Do you consider local economic impacts?		

How well informed am I?		
Questions for councillors to consider	**What do I know?**	**Do I need to ask further questions?**
• How do your fees and charges compare to other councils?		
Capital investment (paragraphs 26 to 28)		
• Is your capital investment programme appropriately funded?		
• Do you know what slippage there has been in capital projects and why? Are you assured that appropriate action is being taken?		
Council budgeting (paragraphs 37 to 42)		
• Do service budgets reflect your priorities?		
• Are potential overspends highlighted to you as they occur and before year-end?		
• Are there services where you are consistently over or under spending against your budget? Are such variances adequately explained?		
Council workforces (paragraphs 43 to 45)		
• Are exit packages supported by business cases setting out the total estimated costs and savings?		
Reserves (paragraphs 46 to 49)		
• Do you know what levels of reserves are needed, and why?		
• Do you think reserves are being used effectively?		
Debt (paragraphs 50 to 62)		
• Are there clear links between the capital programme and our treasury management strategy?		

Cont.

How well informed am I?		
Questions for councillors to consider	**What do I know?**	**Do I need to ask further questions?**
• Do you know what the implications that different types of borrowing options have on future revenue budgets?		
• Do you know the split in debt between General Fund and HRA (where applicable)? Is this reported within your management commentary?		
• Do you know how debt repayments affect what money is available to spend on services?		
Financial strategies and plans (paragraphs 72 to 77)		
• Do you have a long-term financial strategy covering five to ten years?		
• Are there clear links between the financial strategy and the vision for the future?		
• Is the long-term financial strategy supported by detailed plans covering a minimum of three years?		
• Do financial plans set out the implications of different levels of income, spending and activity?		
• Is there a clear link between the council's revenue plans and the budget information you are asked to approve?		
Funding gaps, savings and service transformation (paragraphs 78 to 87)		
• Do financial plans identify the differences between income and expenditure for the next three years?		
• Do you know the actions being taken to close the funding gap?		
• Do you know what plans there are to redesign services and deliver savings?		

Cont.

How well informed am I?		
Questions for councillors to consider	**What do I know?**	**Do I need to ask further questions?**
• Are savings plans realistic within agreed timescales?		
• Are all savings clearly identified and categorised as recurring or non-recurring (ie, one-off) savings?		
• Is the council reliant on non-recurring savings?		
• Do you know what will happen to the reserves if savings are not made?		
Scrutiny considerations (paragraph 88 to 89)		
• Do you feel you have the knowledge and expertise to scrutinise your finances effectively?		

The differences between financial information presented on a funding and an accounting basis

Council accounts show spending on services on an accounting basis which is higher than the amounts council's budget to spend

1. Councils prepare their annual accounts based on International Financial Reporting Standards. These are the same standards followed by large private sector companies and they set out the principles and rules that apply for accounting. The Code of Practice on Local Authority Accounting in the United Kingdom, published annually by CIPFA, interprets how these standards are to be applied to councils.

2. Some spending on services recorded in the accounts does not need to be funded from available resources in the year. Conversely some of the things that councils do need to fund in the year, by statute and regulation, are not required to be treated as spending by companies. Councils set their budgets on the basis of what needs to be funded in the year. This means they budget for the amounts they need to either pay or to set aside.

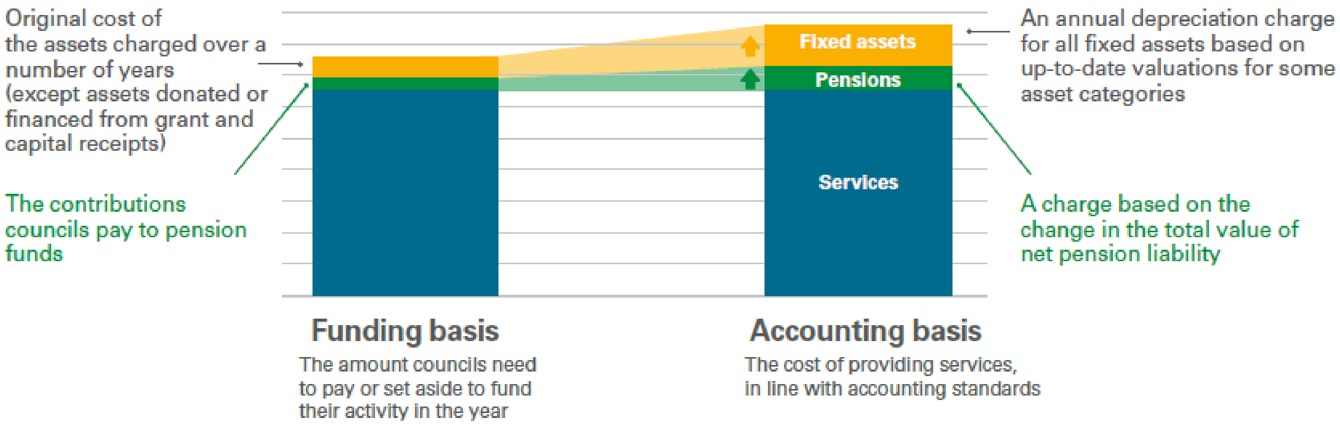
3. Councils' annual accounts include details of the adjustments necessary to get from an accounting basis to a funding basis. However, this complex area is not always well explained. Councils have found it difficult to link the figures in the annual accounts with those in budget reports. The Exhibit 1 (page 5) overleaf shows the main differences between service expenditure on an accounting basis (as identified in the accounts) and on a funding basis (as used for budgeting purposes).

4. From 2016/17, councils will be required to include an expenditure funding analysis showing more clearly the differences between the figures in the accounts and those that officers and members will be more familiar with from budget reports. The Commission welcomes this development as it is hoped this will present figures councillors are more familiar with and therefore make the accounts more useful at a local level and improve scrutiny of the accounts.

Exhibit 1

The main differences between a funding basis and an accounting basis

The main differences are in respect of pensions and fixed assets.



Source: Audit Scotland

Audit Committee
Tuesday 21 March 2017
Item No. 5.7

Financial Monitoring 2016/17 and Financial Strategy 2017/18 to 2021/22

Report by John Blair, Director, Resources

1 Purpose of Report

The purpose of this report is to bring to the Committee's attention to the reports presented to Council on 7 February 2017 by the Head of Finance and Integrated Service Support, in relation to Financial Monitoring and Financial Strategy. The reports are available on the Council website and can be accessed using the link below and specifically relate to:

Audit Committee Meeting – 21 March 2017

- **Financial Monitoring 2016/17 – General Fund Revenue**
- **General Services Capital Plan 2016/17**
- **Housing Revenue Account**
- **Financial Strategy 2017/18 to 2021/22**
- **Treasury Management Mid-Year Review Report**

2 Background

These reports were considered by the Council on 21 February 2017 as detailed above.

3 Report Implications

These remain unchanged from those highlighted in the Head of Finance and Integrated Service Support's reports.

4 Recommendations

The Committee is invited to scrutinise for its interest the reports by the Head of Finance and Integrated Service Support.

Date: 9 March 2017

Report Contact:
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Midlothian Council
7th February 2017

Financial Monitoring 2016/17 – General Fund Revenue

Report by Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of Report

The purpose of this report is to provide Council with information on performance against revenue budget in 2016/17 and details of the material variances.

2 Background

2.1 Budget Performance

The detailed budget performance figures shown in appendix 1 result in a net overspend of £1.771 million which is 0.88% of the revised budget for the year. This is a deterioration of £0.275 million on the quarter 2 position reported to Council on 8th November.

The main areas of variance are outlined below:

Pressures

- Demand led pressures in Adult Social Care, particularly the Community Care Resource Panel and in Home Care packages. They are currently projected to overspend by £1.646 million which is £0.081 million less than reported at quarter 2. Projections of spend in this area can be very volatile given the fluidity of demand and potential high value of individual packages of care;
- Running costs for Care Homes for Older people of £0.180 million;
- Slippage in the opening of Pentland House which has put additional pressure on Bed and Breakfast budgets for Homeless clients. An overspend of £0.411 million is currently projected;
- Loan charges are currently projected to be £0.264 million over budget due to less slippage in the General Services Capital Plan than anticipated;
- Achievement of Council Transformation Targets for procurement savings and for tactical reductions in contracted hours has slipped and is projected to overspend by £0.400 million.

Favourable Movements

- Demand for Residential and Day Care placements for children is lower than budgeted and some high value placements are now being provided in a different way. Spend in this area is now projected to be £0.956 million less than the budget of £3.900 million but is very volatile in its nature;
- A continued growth of properties in Midlothian will generate an improvement on budget of £0.600 million for Council Tax Income.

Detailed information on material variances is contained in appendix 2 which identifies each variance, explains why it happened, outlines what action is being taken to control variances and details the impact of that action.

2.2 Council Transformation Programme

Council approved utilisation of £7.718 million of General Fund Reserve to fund costs associated with the ongoing transformation programme.

At the report date £3.287 million of this has been applied with future commitments of £0.593 million identified for 2017/18 and 2018/19. This leaves £3.838 million as uncommitted.

2.3 General Fund Reserve

The projected balance on the General Fund as at 31 March 2017 is as follows:

	£ million	£ million
Reserve as at 1 April 2016		24.625
Less earmarked reserves utilised in 2016/17		(5.947)
General Reserve at 1 April 2016		**18.678**
Planned movements in reserves		
Planned Utilisation	(2.668)	
Supplementary Estimates	(0.605)	
Council Transformation Programme Costs	(0.337)	
One-off costs of VSER	(0.042)	
Other	(0.012)	
		(3.664)
Overspend per appendix 1		(1.771)
General Fund Balance at 31 March 2017		**13.243**

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

	£ million
General Fund Balance at 31 March 2017	**13.243**
Earmarked for specific purposes	
Approved contingency level of General Fund Reserve	(8.000)
Budgets earmarked for Council Transformation	(3.838)
Borders Rail Economic Development Opportunities	(0.027)
Available General Reserve at 31 March 2017	**1.378**

The uncommitted General Fund Reserve at 31 March 2017 is £9.378 million of which £8 million is earmarked as a contingency in the context of the continuing challenging financial outlook, the uncertainty associated with future years grant settlements, pay awards, the economic impact of Brexit and also the potential costs to come from the historic child abuse enquiry. This leaves the remaining £1.378 million as uncommitted.

3 Report Implications

3.1 Resource

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

3.2 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 minimises 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 remedial action is taken where possible. The primary purpose of this report is to provide information on historic performance, however the material variances detailed in appendix 2 highlight that the financial management and budgetary control arrangements require continual review and enhancement if financial risk is to be effectively mitigated.

3.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☐ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☒ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

3.4 Impact on Performance and Outcomes

The decisions taken to balance the budget will have fundamental implications for service performance and outcomes. The Council's Transformation Programme aims to minimise the impact on priority services.

3.5 Adopting a Preventative Approach

The proposals in this report do not directly impact on the adoption of a preventative approach.

3.6 Involving Communities and Other Stakeholders

No consultation was required.

3.7 Ensuring Equalities

There are no equality implications arising directly from this report.

3.8 Supporting Sustainable Development

There are no sustainability issues arising from this report.

3.9 IT Issues

There are no IT implications arising from this report.

4 Recommendations

It is recommended that Council note the contents of this report and consider the financial position in the context of the Financial Strategy for 2017/18 to 2021/22.

20th January 2017

Report Contact:
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Background Papers:

MIDLOTHIAN COUNCIL

Appendix 1

GENERAL FUND OVERVIEW 2016/17

Function	**Revised Budget** £	**Outturn** £	**(Underspend) / Overspend** £
Management	1,634,240	1,634,240	0
Education Communities and Economy			
Childrens Services	15,598,780	14,857,780	(741,000)
Communties and Economy	4,672,846	4,841,846	169,000
Education	83,748,489	83,825,489	77,000
Health and Social Care			
Adult Social Care	38,713,731	40,121,731	1,408,000
Customer and Housing Services	12,242,933	12,266,933	24,000
Resources			
Commercial Services	16,359,583	16,365,583	6,000
Finance and Integrated Service Support	12,576,663	12,846,663	270,000
Properties and Facilities Management	13,983,055	14,314,055	331,000
Lothian Valuation Joint Board	555,551	555,551	0
Central Costs	625,574	788,574	163,000
Non Distributable Costs	1,338,436	1,338,436	0
GENERAL FUND SERVICES NET EXPENDITURE	202,049,881	203,756,881	1,707,000
Loan Charges	6,582,639	6,846,639	264,000
Investment Income	(300,475)	(300,475)	0
Council Transformation Programme savings target	(2,104,873)	(1,704,873)	400,000
Allocations to HRA, Capital Account etc.	(4,781,596)	(4,781,596)	0
	201,445,576	203,816,576	2,371,000
less Funding:			
Scottish Government Grant	151,516,000	151,516,000	0
Council Tax	40,600,000	41,200,000	(600,000)
Utilisation of Reserves	9,329,576	11,100,576	1,771,000

Appendix 2

Financial Monitoring 2016/17 – General Fund Revenue – Material Variances

Education, Communities and Economy

Children's Services

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Children's services review interim staffing position	Ongoing Children's Services Review. At the same time the service is experiencing higher than average levels of maternity leave which is adding to the requirement for temporary staff which has been met using agency workers.	267	267	314	The service is in the process of implementing its new structure. In order to move towards the new structure it has employed supernumerary staff and used high levels of agency staff. These actions have been taken in order to minimise permanent post holders being displaced by the review and to ensure the right people are in post for the new structure.
Other non-material variances	Miscellaneous over and underspends covering the remaining areas of the Children's Services budget.	11	11	(7)	No impact on frontline service.
Gross Overspend		**278**	**278**	**307**	
Offset by:					
Residential and Day Education Placements	The requirement for residential placements is lower than anticipated and provided for in the budget. Demand for new placements was low for the first half of the 2016 calendar year.	(912)	(1,003)	(956)	This represents a 25% underspend on the Multi Agency Resource Group budget of £3.9 million. The group continue to challenge new demand to keep costs under control and has recently been successful in its work to progress children in secure placements to allow them to move to other forms of care.
Family Placements	Slippage in plans for the usage of additional Scottish Government Grant.	(174)	(174)	(92)	A part time team leader and two social workers have been recruited to develop the kinship care service service. Between quarter 2 and quarter 3 forecast expenditure on inter-agency adoption fees increased by £30k.
Net Underspend		**(808)**	**(899)**	**(741)**	

Communities and Economy

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Building Standards Income	There was an artificially high level of income received in 2015/16 as a result of changes to Building Regulations in October 2015. This created a high level of application activity before the new regulations came into force. As a result the numbers and related fee income of warrants in 2016/17 are lower than budgeted.	84	84	94	The income received for Building Warrants is highly variable and is influenced by the timings of building works.
Planning Income	Applications for planning consent are lower than budgeted.	64	64	66	The income received for planning applications is highly variable and is influenced by the timing of major developments.
Landlord Registration income	Fewer registrations are due to be renewed in 2016/17 than budgeted.	25	25	20	Registrations run in a three year cycle.
Other non-material variances	Miscellaneous over and underspends covering the remaining areas of the Communities and Economy budget.	17	17	13	No impact on frontline service.
Gross Overspend		**190**	**190**	**193**	
Offset by:					
Staffing Costs	Posts remaining vacant across the service for longer than planned.	0	0	(24)	
Net Overspend		**190**	**190**	**169**	

Education

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Lifelong Learning and Employability Income	The Skill Development Scotland Employability Fund has been reduced nationally by 40%. As a consequence Midlothian's funding was significantly reduced for 2016/17.	167	167	171	The 2017/18 budget reflects the up to date position in relation to projects.
Vacancies and Performance Factor	Non achievement of employee performance factor.	36	36	36	
Gross Overspend		**203**	**203**	**207**	
Offset by:					
PPP Contracts	Insurance costs are lower than provided for in the contract which leads to a refund from the contractor. Contractual refund of funding paid to cover reparation of malicious damage that was not utilised.	(67) (17)	(67) (17)	(83) (38)	Windfall Income. Deductions for PPP1 have increased between quarter 2 and quarter 3. This has been addressed in the 2017/18 budget setting process.
Other non-material variances	Miscellaneous over and underspends covering the remaining areas of the Education Service budget.	(9)	(9)	(9)	No impact on frontline service.
Net Overspend		**110**	**110**	**77**	

Health and Social Care

Adult Social Care

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Community Care Resource Panel	Assessed needs are currently more than budgeted. The budget is £30 million, demand led and subject to demographic pressures. Individual packages of care sometimes in excess of £100k per annum and as a consequence projections in this area can be volatile.	497	1,453	1,503	An underlying over-commitment of around £900k at the start of the financial year has been partially addressed through the review of high cost packages. A review team is in place and a programme of care package reviews are now underway. The impact of this work will be seen more in 2017/18 when there will be a full year impact from the savings.
Home Care / Midlothian Enhanced Rapid Response and Intervention Team (MERRIT)	Additional employee costs due to the volume of care packages being provided.	254	274	332	The service continues to prioritise hospital discharges. There have been additional complexities associated with moving packages of care to external providers and during this transitional period the costs falling on the internal home care service have been higher.
Care Homes for Older People	Projected overspend on running costs, including cleaning materials and first aid supplies, at both Highbank and Newbyres. Projected overspend on staffing costs to cover gaps in the rota.	108 120	83 144	82 98	Additional supply costs associated with increased complexity of residents. The 2017/18 budget has been reviewed to address this. Sickness absence levels at Highbank have been high particularly at the start of the financial year. Managers are working closely with HR to address this issue and improvements have been seen. The development of the Locum bureau will be taken forward to ensure that when extra staff are required this can be done in the most cost effective manner.
Gross Overspend		**979**	**1.954**	**2,015**	
Offset by:					
Service User Income	Contributions from service users towards their care packages are higher than anticipated.	0	0	(189)	Review team work has contributed to an increase in chargeable income.

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Public Protection	Scottish Government funding provided specifically for Adult Support and Protection requirements. Some spend relevant to this funding is in the form of care packages and is met from the Resource Panel budget.	(150)	(140)	(134)	No impact on frontline service but underspend offsets care and support costs related to protection issues.
Learning and Development	Spend continues to be constrained to counter pressures elsewhere in the service.	(128)	(102)	(134)	No impact on frontline service and offsets cost of essential cover for front-line staff with mandatory training requirements.
Joint Equipment Store and Aids and Adaptations	Demand is currently less than budgeted but spend level tends to vary over the course of the year.	(79)	(124)	(97)	No impact on frontline service.
Other non-material variances	Miscellaneous over and underspends covering the remaining areas of the Adult Social Care budget.	(44)	(100)	(53)	No impact on frontline service.
Net Overspend		**578**	**1,488**	**1,408**	

Customer and Housing Services

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Homelessness accommodation	Specialist treatment required in the conversion works to re-use Pentland House has led to delays in the project, with completion now targeted for 1st April 2017. The saving against the Bed and Breakfast budget will therefore not be made.	229	390	411	The budget provided for an average 82 B and B places per week until 1st August 2016 and 36 spaces thereafter once Pentland House was available for use. Average occupancy is currently 85 places. The Polton Centre will be available for use from mid-January and the impact of this is reflected in the projected overspend.
Other non material variances	Miscellaneous over and underspends covering the remaining areas of the Customer and Housing Services.	13	11	50	No impact on frontline service.
Gross Overspend		**242**	**401**	**461**	
Offset by:					
Housing Benefit Subsidy	It is anticipated that income will be higher than budgeted for.	(193)	(163)	(155)	The 2016/17 budget was set based on the experience of previous years. However, in 2016/17 the subsidy receivable is now anticipated to be higher.
Customer Services Staffing	Customer Services is currently under review so current vacancies are being held until the review runs its course.	(123)	(131)	(168)	It is anticipated that vacancies will be filled once the review reaches its later stages.
Revenues Service Vacancies	Vacancies in the Revenues Processing Team that were unfilled for a period or remain unfilled in addition to some maternity savings.	(43)	(68)	(114)	No impact on frontline service. Vacant posts are being retained pending resource requirements for full service commencement of universal credit in April 2017 becoming clearer.
Net Overspend / (Underspend)		**(117)**	**39**	**24**	

Resources

Commercial Services

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Waste Disposal Charges	Movement in tonnage and price.	119	119	239	Market conditions in the recycling market have resulted in issues with disposing of recyclate. A report to Council on 9th February 2016 covered this in more detail and efforts continue to resolve the situation. Whilst the longer term outcome remains uncertain there is a risk that in-year and future year projected costs may vary considerably.
Fleet Repairs	The cost of vehicle parts and repairs carried out by third parties are expected to exceed budget.	0	0	141	An element of repairs to the Councils fleet requires to be completed externally due to specialist skills.
Burials Income	Income from lairs and interments is lower than anticipated at this stage in the year.	90	71	35	The number of burials varies throughout the year.
Zero Waste	Procurement and transition costs for the Zero Waste project exceeds the remaining budget	0	33	33	An update was provided to Council on 8th November 2016 and the 2017/18 budget was adjusted accordingly.
Taxi-cards	The taxi-card scheme was closed to new entrants in 2015/16 but usage by remaining participants is higher than budgeted.	26	26	18	
Gross Overspend		**235**	**249**	**466**	
Offset by:					
Land Services chargeable income	Income is expected to exceed budget due to additional income from work undertaken on capital projects.	0	0	(107)	One-off income in 2016/17.
Street Lighting Electricity	Spend is lower than at the same point last year.	0	(82)	(84)	Conversion to LED lighting leads to lower consumption but this is offset by growth from new Housing Developments.
Staff Vacancies	Vacancies across the service have exceeded the performance factor.	(76)	(52)	(50)	This predominantly relates to Waste Services due to changes in the service provided and delays in recruiting to new posts.

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Fuel Costs	Waste Services vehicles have lower fuel usage than was anticipated when setting the budget.	(68)	(68)	(114)	This will be reflected in future years budgets.
Bus Shelter maintenance	Expenditure on bus shelter maintenance is largely reactive with lower demand to date in 2016/17.	0	0	(61)	The 2017/18 budget has been reviewed.
Other non-material variances	Miscellaneous variances covering the remaining areas of the service.	16	(6)	(44)	No impact on frontline service.
Net Overspend		**107**	**41**	**6**	

Finance and Integrated Service Support

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Mi-Future	The costs of staff in SWITCH during the year are projected to exceed budget.	130	133	130	6 months budget is moved to Switch with displaced employees. The Mi-Future team continues to work towards a satisfactory resolution for each employee in SWITCH and when compared to severance costs SWITCH remains a cost effective solution. As at 30th November 2016 there were 16 people in SWITCH on placements, some of whom are funded by services.
Telephone costs	The council's telephone budget has been centralised and current costs exceed budget. There is also demand led pressures relating to growth in the school estate.	0	0	64	A tender process is underway which may contribute to reducing costs.
Central Postages	The volume and cost of postages exceeds budget of £122k.	49	45	40	Despite changing suppliers and securing better prices the volume and mix of postages continues to exceed budget. Work continues to address this by reducing postage volumes, avoiding all unnecessary postage costs and maximising compliance with contractual requirements.

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
External Legal fees	Continuing costs associated with residual equal pay claims and a higher than anticipated incidence of children's permanence cases.	0	0	28	The residual legal issues related to Equal Pay claims are expected to be concluded in 2017/18 with no further costs anticipated.
Photocopying	Costs associated with the new centralised Council wide contract are greater than estimated due to higher than anticipated volume of use. The budget is £129k.	33	33	18	A review of activity is underway with the aim of minimising volumes and reducing reliance on paper in accordance with EWiM principles.
Bank Charges	The shift towards electronic payments has led to increased transaction costs.	24	23	24	A review of bank charges is underway with the aim of negotiating lower rates with service providers.
Occupational Health	A change to the external provider has resulted in an unexpected cost. The budget is £86k. This cost has now been mitigated.	15	13	0	The previous provider was very competitive but is no longer operating. Budgets for future years will be revised to incorporate the new terms.
Other non-material variances	Miscellaneous variances covering the remaining areas of the service.	0	0	(34)	No impact on frontline service.
Gross Overspend		**251**	**247**	**270**	

Properties and Facilities Management

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Property Costs for EWiM phase 2	Slippage in planned building closures and disposals resulted in unbudgeted costs.	0	0	192	Disposal of Dundas Building has been postponed pending determination of plans for the adjacent site. Eskdaill Court and Jarnac Court remain occupied pending long term decisions on Dalkeith Town Centre and conversion of Eskdaill court.
Catering – food costs	The unit cost of meals provided is increasing due to market pressures. There has also been an increase in demand.	0	0	93	Menus are reviewed regularly to maintain economy, maximise nutritional value and to minimise waste.
Energy Costs	The price mix between standing charges and for consumption has changed for electricity supply.	0	41	41	Standing charges have increased.

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional information / Action taken
Loanhead Leisure Centre – loss of income	Loanhead Leisure Centre will close temporarily in January 2017 before re-opening as part of the new Loanhead Community Hub in August 2017.	34	38	50	Work is ongoing to identify alternative locations for various activities and classes currently held at the centre.
Gross Overspend		**34**	**79**	**376**	
Offset by:					
Catering Staffing	Difficulty recruiting to vacant posts.	(30)	(45)	(45)	Efforts continue to recruit to vacant posts targeting entry level applicants where appropriate.
Net Overspend		**4**	**34**	**331**	

Other

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Quarter 3 £000	Additional Information / Action taken
Loan Charges	The 2016/17 budget provided for planned slippage in the General Services Capital Plan. To date slippage has been less than planned.	283	283	264	
Central Costs	Insurance costs – an increase in the likely settlement costs of existing claims.	112	163	163	Detail of these claims is being reviewed and any mitigating action required will be put in place. A review of likely settlement costs since quarter 1 gave rise to increased exposure to one high value claim.
Transformation Savings - Procurement	A target of £350k for procurement savings was set for 2015/16 which mainly reflected slippage in targeted savings for previous years. It is projected that £200k of this will be achieved.	150	150	250	Procurement plans are currently being refreshed and this may identify further savings in 2016/17. Contract savings have been made or are planned for 2016/17 which impact on the Capital Account and the Housing Revenue Account.
Transformation Savings – Tactical Reductions in contracted hours	The target of £150k will not been achieved in 2016/17	150	150	150	Progress in taking forward a voluntary reduction in hours initiative and promoting flexible retirement options have been delayed because of the focus on low pay. Work in the remainder of the year is expected to deliver a part year saving.

Council Tax Income	A continued growth in Band D equivalents results in a higher than budgeted Council Tax yield.	(452)	(500)	(600)	The continued growth in Band D equivalents has been factored into Council Tax income budgets for future years.

General Services Capital Plan 2016/17 to 2021/22
Report by Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of Report

The purpose of this report is to provide Council with:-

- An update of the General Services Capital Plan incorporating new projects approved since the previous report to Council on 08 November 2016 (Section 2.1/2.2);
- Information on further additions to the Capital Plan for approval (Section 2.3);
- Information on the projected performance of the General Services Capital Plan against budget for 2016/17 (Section 3);
- Forecast expenditure and income for the General Services Capital Plan for 2017/18 through to 2021/22 (Section 4);
- Update Council on the projected balance on the Capital Fund (Section 5) and the projected balance on debt outstanding (Section 6).

2 Update of General Services Capital Plan for rephasing and new projects approved

2.1 Rephasing

The General Services Capital Plan presented to Council on 27 September 2016 allowed, over the period 2016/17 to 2021/22, for expenditure of £128.072 million, funding of £77.213 million, and a total borrowing requirement of £50.859 million, phased as shown in table 1 below:-

Table 1: General Services Capital Plan as approved 27 September 2016

Item	2016/17 Budget £000's	2017/18 Budget £000's	2018/19 Budget £000's	2019/20 Budget £000's	2020/21 Budget £000's	2021/22 Budget £000's	Total Budget £000's
Expenditure	35,953	22,867	22,867	21,869	14,072	10,444	**128,072**
Funding	13,994	13,791	15,579	15,501	10,494	7,854	**77,213**
Borrowing Required	**21,959**	**9,076**	**7,288**	**6,368**	**3,578**	**2,590**	**50,859**

The General Services Capital Plan Q2 Monitoring for 2016/17 was presented to Council on 08 November 2016 and reported:-

- New projects already approved of £0.250 million;
- New projects for approval of £0.565 million;
- New additional funding of £0.366 million;
- Net rephasing from 2016/17 to 2017/18 of £0.165 million expenditure and £0.462 million funding.

This revised the overall levels of expenditure, funding and borrowing required over the period 2016/17 to 2021/22 as shown in table 2.

Table 2: General Services Capital Plan revised per Q2 Monitoring Report

Item	2016/17 Budget £000's	2017/18 Budget £000's	2018/19 Budget £000's	2019/20 Budget £000's	2020/21 Budget £000's	2021/22 Budget £000's	Total Budget £000's
Expenditure	36,605	23,032	22,867	21,869	14,072	10,444	**128,889**
Funding	13,898	14,253	15,579	15,501	10,494	7,854	**77,579**
Borrowing Required	**22,707**	**8,779**	**7,288**	**6,368**	**3,578**	**2,590**	**51,310**

2.2 Approved Projects

Since the report to Council on 08 November 2016, the following projects have received approval by Council for inclusion in the General Services Capital Plan.

- **Gore Glen Bing**: Excavation of heated areas and removal of burning material at Gore Glen Bing. £0.270 million budget approved by Council 20 December 2016. Part funded through utilisation of £0.086 million of the existing provision for Contaminated Land;
- **Purchase of 49 Abbey Road, Dalkeith**: Land purchase to provide for extension of King's Park Primary. £0.215 million budget approved by Council 20 December 2016;
- **Purchase of 31 Jarnac Court**: Purchase of existing shop at 31 Jarnac Court to provide Disability Discrimination Act access to the upper floor (Council owned offices). £0.205 million budget approved by Council 20 December 2016;
- **Grass Cutting Machinery**: Investment in rotary cutting machinery of £0.120 million, approved by Council 20 December 2016 as part of Choices for Change Savings Proposals.

2.3 Projects presented for approval

Since the report to Council on 08 November 2016, the following new projects are being presented for inclusion in the plan:-

- **King George V Park Outdoor Fitness Trail**: Introduction of a fitness trail with new outdoor fitness equipment at King George V Park in Bonnyrigg. £0.021 million budget recommended by CMT 23 November 2016 on the basis that it is ~~,~~fully funded by external contributions from Tesco, Bank of Scotland and Environmental funds raised by Bonnyrigg & Lasswade Community Council;
- **Hillend Freestyle Jump Slope**: Replacement and redevelopment of the existing Snowflex surface to bring facility up to national/international standard. £0.208 million budget recommended by CMT 18 January 2017, part funded by £0.104 million contribution from Sportscotland;
- **Beeslack Community High School 3G Pitch**: Installation of new 3G pitch to replace existing 2G pitch. £0.360 million budget, fully funded through contributions from Sportscotland, Penicuik Athletic Youth

Football Club, Army Covenant, Beeslack Community Fund, Beeslack High School, & a Midlothian Council education contribution;

- **Saltersgate Alterations Phase II**: Further internal alterations to Dalkeith Schools Community Campus to keep the physical environment of the school suitable for the needs of the pupils. £0.254 million budget recommended by CMT 19 October 2016;
- **Cycling, Walking & Safer Streets**: Installation of lighting columns on the Bonnyrigg Bypass to Gorton Road. £0.127 million budget (£0.050 million falling in 2016/17) fully funded by Sustrans contribution;
- **Cycling, Walking & Safer Streets**: Widening of existing footpath to become "shared use" pedestrian/cycleway and conversion of existing puffin crossing to a toucan crossing, adjacent to the B6482, complementing the existing and proposed cycling facilities at the Newbattle Centre. £0.084 million budget fully funded by Sustrans contribution;
- **Marc Building Alterations**: Alterations to kitchen space, toilets and cleaners stores. £0.018 million budget fully funded by external contributions from Grassy Riggs, MVA, Marc (White Goods) and Member's Environmental Funds.

The inclusion of these projects revises the overall levels of expenditure, funding and borrowing required over the period 2016/17 to 2021/22 as shown in table 3 below.

Table 3: General Services Capital Plan including Projects Approved / for Approval

Item	2016/17 Budget £000's	2017/18 Budget £000's	2018/19 Budget £000's	2019/20 Budget £000's	2020/21 Budget £000's	2021/22 Budget £000's	Total Budget £000's
Expenditure	38,206	23,313	22,867	21,869	14,072	10,444	**130,771**
Funding	14,537	14,414	15,579	15,501	10,494	7,854	**78,379**
Borrowing Required	**23,669**	**8,899**	**7,288**	**6,368**	**3,578**	**2,590**	**52,392**

3. 2016/17 Projection against budget

3.1 2016/17 Budget

The 2016/17 capital plan budget of £38.206 million for 2016/17, as reported above, has been rephased to £34.604 million to account for updated expenditure profiles provided in the period, as shown in the table below:-

Table 4: Rephasing of project budgets

Project	Description of amendment to budget	Previous Budget £000's	Revised Budget £000's	Budget Movement £000's
EWiM Phase III: New Depot at Hopefield	Revised programme of works provided	1,631	28	-1,603
Stobhill Depot Upgrade	Rephasing based on actual expenditure to date	569	100	-469
Hopefield Primary School	Related to development of accommodation schedule brief	500	100	-400
Digital Services inc. Website upgrade	Various	2,273	1,934	-339
Property Upgrades	Rephasing based on actual expenditure to date	1,884	1,550	-334
Assistive Technology	Less equipment that envisaged has been purchased. Ongoing requirement of £0.150 million to be reviewed.	355	75	-280
Borders Rail – Economic Development Projects	Reflects timing of projects coming forward	250	0	-250
New Bilston & GoreGlen Primary Schools	Refinement of final contractual & project payments	8,104	7,861	-243
Member's Environmental Funds	Revised estimate based on current & previous year's expenditure	140	70	-70
Loanhead Centre & Roslin Primary School	Acceleration of build by both contractors	12,410	12,780	+370
Other	Minor variances	1,512	1,528	+16
Total		**29,628**	**26,026**	**-3,602**

In line with this, the expected level of funding available to finance the plan has also been rephased and totals £14.152 million, a decrease of £0.368 million which reflects the additional £0.104 million capital grant no longer required for the Public Sector Housing Grant scheme, reduction in the application of developer contributions due to rephasing of expenditure on new primary school projects of £0.490 million.

This reduces the projected in-year borrowing requirement from £23.669 million to £20.452 million. The projected performance against budget for 2016/17 is shown in table 5 below:-

Table 5: General Services Capital Plan Projected Performance against Budget 2016/17 – as at Quarter 3

Item	2016/17 Budget £000's	2016/17 Rephased Budget £000's	Actual To Period 9 £000's	2016/17 Projected Outturn £000's	2016/17 Variance £000's	2016/17 Carry Forward £000's
Expenditure	38,206	34,604	16,858	34,702	+98	-3,602
Funding	14,537	14,152	7,955	14,152	0	
Borrowing Required	**23,669**	**20,452**	**8,903**	**20,550**	**+98**	

3.2 Expenditure

Expenditure to date is £16.858 million with a projected expenditure outturn of £34.702 million. At this stage it is anticipated that budgets for the projects detailed in Appendix 2 will be fully spent in the current year with the following exceptions:-

Table 6: Adjustment to expenditure budget of projects

Item	Description	Projected (Underspend)/ Overspend £000's
Millerhill Access Road / Site Services	Final settlement payment to Scottish Water Horizons.	+15
Digital Services: Back Office Server Replacement	Costs associated with upgrade of backup server within schools, to mitigate risk of service failure, were higher than expected.	+19
Waste Service Review Collection Vehicles	Additional costs due to price inflation on purchase costs (*as reported at Quarter 2*)	+64
Total		**+98**

It is therefore expected that there will be a net overspend against budget for the year of £0.098 million.

3.3 Funding

The funding available to finance the Capital Plan in 2016/17 is expected to total £14.152 million, in line with the rephased budget. Funding of £7.955 million has been received to date.

3.4 Borrowing

The budgeted level of borrowing for 2016/17 is £20.452 million. Based on the forecast expenditure and funding levels, the revised estimate of the level of borrowing required to fund the investment identified in Table 5 is £20.550 million, an increase of £0.098 million. The impact on the Council's borrowing costs is reflected in the Financial Monitoring 2016/17 General Fund Revenue and Financial Strategy 2017/18 to 2021/22 reports elsewhere on today's agenda.

4. Capital Plan 2017/18 to 2021/22

4.1 Expenditure

In the report to Council on 27 September 2016, it was noted that work had been undertaken to progress the development of full asset management plans and the associated investment requirements for the Council's core asset bases. At that stage, provisions sums were included within the General Services Capital Plan for the Council's core asset bases of Property, Roads, Street Lighting, Footway & Footpaths, Vehicles and Digital Services equipment

Whilst this work is currently still ongoing, for the purposes of forward planning the following revised provisional sums are proposed for inclusion within the General Services Capital Plan. These provisions will be subject to further review and refinement with final requirements presented to Council in due course.

Table 7: Core Asset Bases: Asset Management Plans Additional Investment Requirements

Asset strand	Provisional Additional Investment Requirement 2017/18 to 2021/22 £000's		Notes	Indicative Plan Received/ Costed
	Sep 2016	Feb 2017		
Vehicle & Plant Replacement Programme	10,274	10,446	Variable annual profile over period 2017/18 to 2021/22	Yes
Road Upgrades	4,000	6,200	Annual budget of £1.5 million plus additional £0.2 million in 2017/18	No
Street Lighting Upgrades	4,000	4,000	Annual budget of £1 million	No
Property Upgrades	4,000	4,000	Annual budget of £1 million	No
Footways & Footpaths	2,500	2,500	Annual budget of £0.5 million	No
Digital Services	8,759	8,759	Variable annual profile over period 2017/18 to 2021/22	Yes
Total	**33,533**	**35,905**		

Expenditure forecasts have been rephased based on the most recent project information available.

Based on the new projects as presented in Sections 2.1, 2.2 and 2.3, and the revised levels of investment requirements in the Council's six core asset bases as shown in Table 7 above, the forecast level of expenditure over the life of the plan is forecast to increase from £128.072 million to £133.629 million, an increase of £5.557 million. This includes £0.657 million of "unallocated" capital expenditure (see Section 6 below and Appendices 1 and 2).

Council will also be aware that there are a number of projects associated with the development of the Council's Learning Estate Strategy which will have significant investment requirements which will not be met by developer contributions. These will be reflected in the plan as they come forward and the wider implications for borrowing, the cap on debt outstanding and the funding required to support that borrowing will need to be considered as the strategy is developed.

4.2 Funding

The planning assumption for the level of General Capital Grant funding from the Scottish Government over the life of the plan was £45.247 million, as reported to Council in the *General Services Capital Plan 2016/17 to 2021/22* report on 27 September 2016. The Local Government Finance (Scotland) Settlement 2016-17 (Finance Circular 9/2016) issued on 15 December 2016 provides for an increase in the level of General Capital Grant in 2017/18 compared to the previous planning assumption.

The indications are that Scottish Government will set out a two year settlement in December 2017 covering the years 2018/19 and 2019/20. In advance of this and future year settlements, the planning assumption included in the General Services Capital Plan is that the level of General Capital Grant funding beyond 2017/18 will remain cash flat at 2017/18 levels.

As such the forecast level of General Capital Grant funding from the Scottish Government over the life of the plan is projected to increase from £45.247 million as reported to Council on 27 September 2016 to £51.896 million, an increase of £6.649 million.

This funding continues to include the re-profiling reduction of £1.763 million applied in the 2016/17 capital grant allocation for Midlothian, albeit that this will now be paid over the period 2018-20 as opposed to the previous indication that this would be paid over the period 2017-2020.

In line with revised levels of expenditure, the forecast level of developer contributions that can be applied to finance the plan has been reprofiled and has reduced from £15.612 to £15.078, a reduction of £0.534 million. This also reflects more accurate estimates of the proportion of new primary school facilities that are eligible for developer contribution funding.

In addition, the level of other contributions available to finance the plan has increased from £4.355 million (per 27 September 2016 report) to £5.472 million, an increase of £1.117 million. This reflects the additional funding contributions as reported in Sections 2.1, 2.2. and 2.3.

Overall, the funding available to finance the planned expenditure has increased from £77.213 million to £84.447 million, an increase of £7.233 million. A more detailed breakdown is shown in Appendix 1.

4.3 Borrowing

As a result of the revised expenditure and funding forecasts as reported in Sections 2.1 to 2.5, the forecast level of borrowing over the period 2016/17 to 2021/22 has decreased from £50.859 million to £49.183 million.

Table 8: General Services Capital Plan 2016/17 to 2021/22

Item	**2016/17 Budget £000's**	**2017/18 Budget £000's**	**2018/19 Budget £000's**	**2019/20 Budget £000's**	**2020/21 Budget £000's**	**2021/22 Budget £000's**	**Total Budget £000's**
Expenditure	34,702	24,263	22,744	19,849	20,576	11,495	**133,629**
Funding	14,152	14,320	16,220	17,470	12,626	9,659	**84,447**
Borrowing Required	**20,550**	**9,944**	**6,523**	**2,379**	**7,950**	**1,836**	**49,183**

More details are provided in Appendix 1.

5. Capital Fund

The Capital Fund at the start of the 2016/17 financial year was £15.378 million. Capital Receipts of £5.178 million are forecast to be received in 2016/17 (£0.343 million to Period 9), and will be transferred to the capital Fund. This will increase the balance in the Capital Fund to £20.556 million as at 31 March 2017.

Council, on 27 September 2016, approved the medium to long-term strategy for the Capital Fund, specifically, to maintain the current arrangements for crediting all capital receipts for the disposal of assets to the Capital Fund, and for £12.000 million to be earmarked from the Capital Fund for the Edinburgh and South East Scotland City Region Deal.

The projected balance on the Capital Fund at 31 March 2022, inclusive of the release of £12.000 million City Deal funding, is £26.338 million.

6 Overall Cap on Debt Outstanding

The projected level of debt outstanding, based on the expenditure and income assumptions outlined in Table 8, and net of any forward funded projects, is shown in Table 9 below:-

Table 9: Debt outstanding net of any forward funded projects

Item	**2016/17 Budget £000's**	**2017/18 Budget £000's**	**2018/19 Budget £000's**	**2019/20 Budget £000's**	**2020/21 Budget £000's**	**2021/22 Budget £000's**
Debt Outstanding 01 April	99,959	116,877	122,939	125,504	124,023	128,067
Borrowing arising from Capital Plan	20,550	9,944	6,523	2,379	7,950	1,836
Debt Repayments	-3,632	-3,882	-3,958	-3,860	-3,906	-3,980
Debt Outstanding 31 March	**116,877**	**122,939**	**125,504**	**124,023**	**128,067**	**125,923**
Less: Net debt on Forward Funded projects	-5,434	-6,865	-6,819	-5,161	-3,109	-1,923
Debt Outstanding 31 March exc. Forward Funded projects	**111,443**	**116,074**	**118,685**	**118,862**	**124,958**	**124,000**
Agreed Cap	**124,000**	**124,000**	**124,000**	**124,000**	**124,000**	**124,000**
Headroom	**12,557**	**7,926**	**5,315**	**5,138**	**-958**	**0**

The previous Council approved cap on debt outstanding is £124.000 million, net of the debt outstanding on any projects that are forward funded (e.g. where the Council build the asset and recover monies from e.g. developers).

As can be noted from the table above, the overall level of debt outstanding (net of forward funded projects) is projected to temporarily exceed this cap in the year ended 31 March 2021 but remain back within this revised cap of £124.000 million as at 31 March 2022.

Based on the current expenditure and funding assumptions, there remains limited headroom within the cap (£0.657 million of "unallocated" capital expenditure over the life of the capital plan, phased in full in 2021/22 – see Appendix 1) and therefore any new investment requirements being brought forward over the life of the plan will require to be evaluated to ensure the appropriate prioritisation of projects to ensure that the overall level of debt outstanding remains within the £124.000 million cap. The loan charges presented to Council in the Financial Strategy report elsewhere on today's agenda are based on the overall level of debt outstanding remaining within the cap of £124.000 million as at 31 March 2022 as noted in Table 9 above, and exclude the impact of any net capital expenditure presented in reports elsewhere on today's agenda.

As a result, any capital expenditure that results in the level of debt outstanding rising above this £124.000 million cap will result in a corresponding increase in the level of loan charges that are included in the Financial Strategy 2017/18 to 2021/22 report also presented on today's agenda.

It is proposed that over the course of the spring, officers shall continue to review the level of the cap, the additional investment requirements arising from the developing asset management plans, the Emerging Learning Estate projects, and the prioritisation of any new projects, and bring a report back to Council in June 2017 setting out options and their implications.

7. Report Implications

7.1 Resource

The borrowing required to finance the planned investment in 2016/17 to 2021/22 is currently £49.183 million. The loan charges associated with this borrowing are reported to Council in the Financial Monitoring 2016/17 General Fund Revenue and Financial Strategy 2017/18 to 2021/22 reports presented elsewhere on today's agenda.

7.2 Risk

The inherent risk in the Capital Plan is that projects will cost more than estimated thus resulting in additional borrowing. The monitoring procedures ensure that significant variations are reported at an early stage so that remedial action can be taken to mitigate this risk.

As noted in Section 6, there is limited headroom within the £124.000 million cap on the level of debt outstanding, this headroom existing only in 2021/22, and therefore limited headroom for any additional capital expenditure that will not result in additional loan charges. This risk is exacerbated through the need for more fully developed asset management plans, with only provisional sums for the Council's 6 core asset bases (Property, Roads, Street Lighting, Footway & Footpaths, Vehicles and Digital Services equipment) currently included in the capital plan. In order to mitigate this risk it is proposed that over the course of the spring, officers review the level of the cap, the additional investment requirements arising from the developing asset management plans, the emerging Learning Estate Strategy, and the prioritisation of any new projects, to ensure that the overall level of debt outstanding remains affordable.

7.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

- ☐ Community safety
- ☐ Adult health, care and housing
- ☐ Getting it right for every Midlothian child
- ☐ Improving opportunities in Midlothian
- ☒ Sustainable growth

☐ Business transformation and Best Value
☐ None of the above

7.4 Impact on Performance and Outcome

There are no issues arising directly from this report.

7.5 Adopting a Preventative Approach

There are no issues arising directly from this report

7.6 Involving Communities and Other Stakeholders

No external consultation has taken place on this report.

7.7 Ensuring Equalities

There are no equalities issues arising directly from this report.

7.8 Supporting Sustainable Development

There are no sustainability issues arising directly from this report.

7.9 Digital Services Issues

There are no Digital Services implications arising from this report.

8 Recommendations

Council is asked to:

a) Note the General Services Capital Plan Quarter 3 monitoring position for 2016/17;
b) Approve the projects as outlined in Section 2.3 to be added to the General Services Capital Plan;
c) Approve the allocated expenditure and funding in the General Services Capital Plan 2016/17 to 2021/22 (as shown in appendices 1 and 2);
d) Note that based on the current forecasts and provisional sums, that the level of debt outstanding is forecast to be £124.000 million at 31 March 2022;

Date 27 January 2017

Report Contact:
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Background Papers:
Appendix 1 – Summary General Services Capital Plan 2016/17 to 2021/22
Appendix 2 – Detailed General Services Capital Plan Expenditure 2016/17 to 2021/22

Appendix 1

General Services Capital Plan 2016/17 to 2021/22

GENERAL SERVICES CAPITAL PLAN 2016/17 to 2021/22	2016/17 Budget £'000	2017/18 Budget £'000	2018/19 Budget £'000	2019/20 Budget £'000	2020/21 Budget £'000	2021/22 Budget £'000	Total Budget £'000
EXPENDITURE							
Resources	11,073	7,871	13,159	12,143	17,807	10,116	**72,169**
Education, Community & Economy	23,293	15,820	5,535	1,556	519	519	**47,243**
Health & Social Care	127	452	150	150	150	203	**1,232**
Council Transformation	208	120	3,900	6,000	2,100	0	**12,328**
Unallocated	0	0	0	0	0	657	**657**
Total Approved Expenditure	34,702	24,263	22,744	19,849	20,576	11,495	**133,629**
FUNDING							
Government Grants	7,386	8,854	9,355	9,355	8,473	8,473	**51,896**
Receipts from Sales transferred to Capital Fund	5,178	6,682	0	8,700	0	0	**20,560**
Transfer from Capital Fund to Capital Plan	-5,178	-6,682	3,900	-2,700	2,100	0	**-8,560**
Developer Contributions	3,485	3,469	2,771	2,115	2,052	1,186	**15,078**
Other Contributions	3,281	1,996	195	0	0	0	**5,472**
Total Available Funding	14,152	14,320	16,220	17,470	12,626	9,659	**84,447**
Approved Borrowing Required	**20,550**	**9,944**	**6,523**	**2,379**	**7,950**	**1,836**	**49,183**

Appendix 2

Detailed General Services Capital Plan Expenditure 2016/17 to 2021/22

GENERAL SERVICES CAPITAL PLAN	2016/17	2017/1	2018/19	2019/2	2020/2	2021/2	Total
2016/17 to 2021/22	Budget	Budget	Budget	Budget	Budget	Budget	Spend
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
RESOURCES							
Customer Services							
Front Office - Device & Interactive Asset Upgrades	481	265	143	0	0	0	**889**
Back Office - Anti Virus Upgrades	0	0	49	26	0	0	**75**
Back Office - Server Replacement	194	0	0	0	0	0	**194**
Back Office - UPS Devices	1	0	0	0	0	0	**1**
Network Enterprise - Network Assets (Power & Data)	157	81	44	0	0	0	**282**
IGS - Compliance - Data Encryption	0	0	15	8	0	0	**23**
IGS - Compliance - PCI	39	0	0	0	0	0	**39**
Disaster Recovery	0	0	0	0	26	14	**40**
Service Desk - ITMIS Service Improvement	64	86	0	0	0	0	**150**
Committee Management System	3	0	0	0	0	0	**3**
Paperless Meetings	16	0	0	0	0	0	**16**
Business Application Upgrades inc. mobile working	19	120	0	0	0	0	**139**
Interactive White Board Replacement	652	161	0	0	0	0	**813**
SWAN Programme	208	350	0	0	0	0	**558**
New GoreGlen & Bilston Digital Assets	147	0	0	0	0	0	**147**
Digital Services Asset Management Plan	0	0	1,645	2,496	2,355	2,264	**8,759**
Commercial Operations							
Street Lighting Upgrades	728	650	1,000	1,000	1,000	1,350	**5,728**
Street Lighting LED Upgrade (Salix Funded)	0	0	0	0	0	0	**0**
Footway & Footpath Network Upgrades	1,122	325	500	500	500	675	**3,622**
Road Upgrades	1,524	1,105	1,570	1,500	1,500	2,025	**9,224**
Millerhill Access Road / Site Services	15	0	0	0	0	0	**15**
Zero Waste Capital Contribution	0	0	0	0	7,380	0	**7,380**
Cycling, Walking & Safer Streets Projects	242	187	167	102	94	122	**913**
Ironmills Park Steps	185	0	0	0	0	0	**185**
Emily Bing	13	0	0	0	0	0	**13**
New recycling facility - Penicuik	281	0	0	0	0	0	**281**
Waste Collection Vehicles	204	361	195	0	0	0	**760**
Vehicle & Plant Replacement Programme	1,523	2,181	2,343	1,707	2,957	2,226	**12,938**
Electric Vehicles - Powerpoint Installation	73	0	0	0	0	0	**73**
Grass Cutting Machinery	0	78	42	0	0	0	**120**
Install Geogrid - Barleyknowe Lane	68	0	0	0	0	0	**68**
Loanhead Memorial Park	5	0	0	0	0	0	**5**
20mph Limits	12	28	0	0	0	0	**40**
Vogrie Car Parking Barriers	33	0	0	0	0	0	**33**
CCTV Upgrades	30	0	0	0	0	0	**30**
Mayfield Park Amenities	81	0	0	0	0	0	**81**
King George V Park Outdoor Fitness Equipment	21	0	0	0	0	0	**21**
Gore Glen Bing	270	0	0	0	0	0	**270**
Property & Facilities							
Stobhill Depot Upgrade	100	469	0	0	0	0	**569**
New Depot: EWiM Phase III	28	421	4,448	3,804	994	91	**9,786**
Straiton Bing Site Investigation	70	0	0	0	0	0	**70**
Property Upgrades inc. Lighting/Lightning	1,550	1,002	1,000	1,000	1,000	1,350	**6,902**
Purchase of 7 Eskdaill Court, Dalkeith	285	0	0	0	0	0	**285**
Purchase of 49 Abbey Road, Dalkeith	215	0	0	0	0	0	**215**
Purchase of 31 Jarnac Court, Dalkeith	205	0	0	0	0	0	**205**
Hillend Freestyle Jump Slope Upgrade	208	0	0	0	0	0	**208**
Primary 1-3 Free School Meals	3	0	0	0	0	0	**3**
TOTAL RESOURCES	**11,073**	**7,871**	**13,159**	**12,143**	**17,807**	**10,116**	**72,169**

EDUCATION, COMMUNITY AND ECONOMY	2016/17 Budget £'000	2017/18 Budget £'000	2018/19 Budget £'000	2019/20 Budget £'000	2020/21 Budget £'000	2021/22 Budget £'000	Total Spend £'000
Early Years							
Woodburn Family Learning Centre	180	0	0	0	0	0	**180**
Gorebridge Development Trust (EYG Funded)	100	0	0	0	0	0	**100**
Gorebridge Development Trust	116	0	0	0	0	0	**116**
Gorebridge Development Trust (EYG Funded)	70	0	0	0	0	0	**70**
Further Early Years Provisions	0	0	519	519	519	519	**2,078**
Primary							
New Bilston Primary	3,414	213	0	0	0	0	**3,627**
New Gorebridge North Primary	4,447	179	0	0	0	0	**4,626**
Cornbank Primary Extension	19	0	0	0	0	0	**19**
St Andrews Primary Extension	-18	0	0	0	0	0	**-18**
Newtongrange Primary Extension	20	0	0	0	0	0	**20**
Paradykes & Roslin Primaries Preparatory Works	436	0	0	0	0	0	**436**
Paradykes Primary Replacement	8,562	6,130	232	0	0	0	**14,924**
Roslin Primary Replacement	3,782	2,927	109	0	0	0	**6,818**
Former Hopefield Primary School	100	4,838	3,977	855	0	0	**9,769**
Inspiring Learning Spaces	310	0	0	0	0	0	**310**
Secondary							
Lasswade High School inc. 2nd MUGA	479	384	154	0	0	0	**1,017**
Newbattle High School Preparatory Works	395	407	544	182	0	0	**1,528**
Beeslack Community High School Pitch	360	0	0	0	0	0	**360**
General							
Online Payments for Schools	45	0	0	0	0	0	**45**
PPP1 Land Acquisition	27	0	0	0	0	0	**27**
Saltersgate Alterations Phase II	254	0	0	0	0	0	**254**
Children and Families							
Planning & Development							
Environmental Improvements	70	491	0	0	0	0	**561**
Borders Rail - Economic Development Projects	0	250	0	0	0	0	**250**
Property Asset Management System	6	0	0	0	0	0	**6**
East High Street Public Realm & Burns Monument	120	0	0	0	0	0	**120**
TOTAL EDUCATION, COMMUNITY AND ECONOMY	**23,293**	**15,820**	**5,535**	**1,556**	**519**	**519**	**47,243**
HEALTH AND SOCIAL CARE							
Adult & Social Care							
Assistive Technology	75	377	150	150	150	203	**1,105**
Travelling Peoples Site Upgrade	17	0	0	0	0	0	**17**
Homecare	35	75	0	0	0	0	**110**
Customer & Housing Services							
TOTAL HEALTH AND SOCIAL CARE	**127**	**452**	**150**	**150**	**150**	**203**	**1,232**
COUNCIL TRANSFORMATION							
Purchase to Pay	21	0	0	0	0	0	**21**
Online Housing Applications	27	0	0	0	0	0	**27**
Corporate Telephony Services Upgrade	9	0	0	0	0	0	**9**
EWiM - Buccleuch House Ground Floor	33	0	0	0	0	0	**33**
Website Upgrade	119	120	0	0	0	0	**239**
City Deal	0	0	3,900	6,000	2,100	0	**12,000**
TOTAL COUNCIL TRANSFORMATION	**208**	**120**	**3,900**	**6,000**	**2,100**	**0**	**12,328**
UNALLOCATED							
Unallocated	0	0	0	0	0	657	**657**
TOTAL UNALLOCATED	**0**	**0**	**0**	**0**	**0**	**657**	**657**
GENERAL SERVICES CAPITAL PLAN TOTAL	**34,702**	**24,263**	**22,744**	**19,849**	**20,576**	**11,495**	**133,629**

Midlothian Council
7th February 2017

Housing Revenue Account
Revenue Budget and Capital Plan 2016/17

Report by Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of Report

The purpose of this report is to provide Council with a summary of expenditure and income to 16th December 2016 for the Capital Plan and a projected outturn for both the Housing Revenue Account (HRA) and Capital Plan for 2016/17.

2 Background

2.1 Capital Plan 2016/17

The revision of the Capital Plan reported to Council on 27th September 2016 allowed for investment of £22.449 million in 2016/17 as shown in Appendix 1. £4 million will be required to be carried forward to 2017/18 due to:-

- Issues with site investigations and various remediation works, due to external factors out with our control, will result in slippage of £3 million for New Social Housing;
- Difficulties in gaining access to a number of properties to carry out works will result in slippage of the Sanitary Ware Replacement Programme of £0.300 million;
- General slippage in the Energy Efficiency Programme of £0.700 million;

Offset by:-

- Developer Contributions of £1 million which are now anticipated to be received in 2017/18.

There were no material variances reported to Council 8th November 2016, however it is now anticipated that there will be a net underspend of £0.056 million against the revised budget of £18.449 million principally due to:-

- A fall in the number of Mortgage to Rent cases being presented resulting in a projected underpsend of £0.103 million offset by a reduction in subsidy received of £0.034 million;
- The removal of asbestos and repairs to boilers at Midfield House has resulted in a projected overspend of £0.040 million;

This is offset by an increase in Capital Receipts of £6.195 million due to:-

- Further Affordable Housing Contribution's being awarded from Scottish Government of £3.332 million for Phase 2 and Phase 3 for New Social Housing;
- Right to Buy sales have increased more than anticipated due to the termination of the scheme resulting in an increase in receipts of £3.077 million;
- Some of the properties bought back will not be awarded grant funding as they will be used as temporary accommodation rather than affordable housing resulting in a shortfall of £0.180 million.

The variations on capital expenditure and receipts including carry forwards will result in a reduction of borrowing required of £6.251 million for the year.

2.2 Revenue Account 2016/17

The underspend reported to Council on the 8th November 16 was £0.290 million. This has increased slightly by £0.011 million to £0.301 million, as shown in Appendix 2.

The HRA reserve balance is projected to be £29.214 million at 31st March 2017. The longer term financial projections demonstrate that the majority of this will be required to finance existing investment commitments to 2030/31.

3 Report Implications

3.1 Resource

There are no direct resource implications arising from this report.

3.2 Risk

The principal risks are around the issue of affordability, ensuring that the investment in new build and the existing stock can be made without having to impose unacceptable increases on weekly rents.

Whilst the HRA reserve balance is projected to be £29.214 million at 31 March 2017, the longer term financial projections demonstrate that the majority of this will be required to finance existing investment commitments.

3.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☒ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☒ Sustainable growth

☐ Business transformation and Best Value
☐ None of the above

3.4 Impact on Performance and Outcomes

This report links to the Corporate Priority 1a. “Provide quality, affordable housing including increasing homelessness accommodation”.

3.5 Adopting a Preventative Approach
There are no issues arising directly from this report.

3.6 Involving Communities and Other Stakeholders

No external consultation has taken place on this report.

3.7 Ensuring Equalities

There are no equality issues arising directly from this report.

3.8 Supporting Sustainable Development
There are no sustainability issues arising from this report.

3.9 IT Issues
There are no IT issues arising directly from this report.

4 Summary

The summarised financial performance for 2016/17 is:

- Capital Expenditure is anticipated to be £18.393 million for the year;
- A net undersend of £0.301 million is projected on the Revenue Account;
- The HRA reserve at 31st March 2017 is projected to be £29.214 million.

5 Recommendations

Council is recommended to note the contents of this report.

Date 16th January 2017

Report Contact:
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Background Papers: HRA Capital Plan and Revenue Budget

MIDLOTHIAN COUNCIL

Appendix 1

HOUSING REVENUE ACCOUNT CAPITAL PLAN 2016/17

	Approved Budget 2016/17	Carry Forward to 2017/18	Revised Budget 2016/17	Actuals to Date	Projected Outturn	Variation (Under)/Over
	£'000	£'000	£'000	£'000	£'000	£'000
FUNDING						
Net Receipts from Sales	2,155	0	2,155	3,761	5,232	3,077
Grants						
-Incentivising New Build	764	0	764	1,556	4,096	3,332
-Mortgage to Rent	168	0	168	74	134	(34)
-Buy Backs Funding	300	0	300	0	120	(180)
Council Tax on Second Homes	118	0	118	0	118	0
Developer Contributions	1,000	1,000	0	0	0	0
Borrowing Required	17,944	3,000	14,944	5,171	8,693	(6,251)
TOTAL AVAILABLE FUNDING	22,449	4,000	18,449	10,562	18,393	(56)

APPROVED EXPENDITURE	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
New Build Houses Phase 1	162	0	162	(140)	162	0
New Build Houses Phase 2	13,019	3,000	10,019	5,714	10,019	0
Buy Backs	1,603	0	1,603	672	1,603	0
Aids & Adaptations	300	0	300	214	300	0
Energy Assistance	1,000	700	300	103	300	0
Homelessness - Mortgage to Rent	303	0	303	117	200	(103)
Homelessness - Pentland House Refurbishment	472	0	472	44	472	0
Homelessness - Midfield House Refurbishment	39	0	39	69	79	40
Environmental Works - McNeill Terrace	0	0	0	7	7	7
Scottish Housing Quality Standard						
-Upgrade Central Heating Systems	650	0	650	529	650	0
-Kitchen Replacement Programme	201	0	201	37	201	0
-Sanitary Ware Replacement Programme	950	300	650	420	650	0
-SHQS Repairs	3,750	0	3,750	2,776	3,750	0
Total Expenditure	22,449	4,000	18,449	10,562	18,393	(56)

MIDLOTHIAN COUNCIL

HOUSING REVENUE ACCOUNT 2016/17

Appendix 2

	Revised Budget	Projected Outturn	Variation (Under)/Over
Average No of Houses	**6,864**	**6,845**	**(19)**
	£000's	**£000's**	**£000's**
Repairs and Maintenance			
General Repairs	5,400	5,364	(36)
Decant/Compensation	40	40	0
Grounds Maintenance	574	574	0
	6,014	**5,978**	**(36)**
Administration and Management	4,842	4,842	0
Loan Charges	8,649	8,582	(67)
Other Expenses	2,492	2,270	(222)
TOTAL EXPENDITURE	**21,997**	**21,672**	**(325)**
Rents			
Houses	24,882	24,758	124
Garages	529	529	0
Others	586	686	(100)
TOTAL RENTS	**25,997**	**25,973**	**24**
NET EXPENDITURE/(INCOME)	**(4,000)**	**(4,301)**	**(301)**
BALANCE BROUGHT FORWARD	**(24,913)**	**(24,913)**	**0**
BALANCE CARRIED FORWARD	**(28,913)**	**(29,214)**	**(301)**

Midlothian Council
Tuesday 07 February 2017

Financial Strategy 2017/18 to 2021/22 – Revised Report

Report by Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of Report

This report replaces the previous Financial Strategy 2017/18 to 2021/22 report dated 31 January 2017 and incorporates the implications of the additional grant funding for 2017/18 announced by Scottish Government on 2 February 2017.

This report provides Council with an update on the Financial Strategy encompassing the years 2017/18 to 2021/22. It sets out recommendations to enable Council to set Council Tax and to determine a budget for 2017/18.

It also includes:-

- An update on Scottish Government Grant;
- Updated budget projections for 2017/18 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios for later years;
- An update on the resources to be provided to the Midlothian Integration Joint Board in 2017/18;
- An update on the strands of the change programme;
- The resultant 2017/18 service budgets;
- An update on reserves.

2 Background

The core objective of the Financial Strategy is that of securing the Council's continued financial sustainability during an ongoing period of substantial financial constraint coupled with continuing service demand pressures and increasing customer expectations.

On 20 December 2016 Council was provided with an updated assessment of projected budgets shortfalls through to 2021/22 together with a verbal update on the recently announced Scottish Government Grant settlement for 2017/18. In respect of 2017/18 the initial assessment of the grant settlement had indicated that the budget shortfall for 2017/18 would increase to £12.880 million from that set out in the report.

Encompassing the savings targets for the change programme and incorporating the full 3% per annum increase in Council Tax resulted in a remaining budget gap to be addressed for 2017/18 of £4.080 million.

3 Scottish Government Grant Settlement

The Scottish Government's draft budget for 2017/18 was published on 15 December 2016 together with Finance Circular 9/2016 which set out the grant settlement package being offered to Council's and included the individual grant figures for each Council. Alongside these the Cabinet Secretary for Finance and the Constitution set out further details of the terms of the settlement in a letter to the COSLA President and Council Leaders (A copy of which was circulated as part of the Administration motion on 20 December 2016 in respect of the Financial Strategy 2017/18 to 2021/22).

At a national level the settlement represented a reduction of £349 million or 3.6% in core revenue funding for Councils. The full funding package set out in the finance circular incorporates an additional specific grant of £120 million for the Attainment Scotland Fund for schools to support closing the attainment gap. This will be distributed to schools based on pupils registered for Free School Meals and at the time of writing there is limited information on the conditions and constraints associated with the fund. Accordingly the projections set out later in this report presume that these resources will be committed towards additional spending.

Integrated Joint Boards will receive an additional £107 million allocated from the Health budget. This additional funding is provided to meet the full year costs of the joint aspiration to deliver the Living Wage for social care workers, sleepovers and sustainability (£100 million) and removal of social care charges for those in receipt of war pensions and pre-implementation work in respect of the new carers legislation pressures (£7 million). To reflect this additional support Councils are able to adjust their allocations to Integration Authorities in 2017-18 by up to their share of £80 million below the level of budget agreed with their Integration Authority for 2016-17.

In a departure from what had previously been indicated by Government the additional income estimated at £111 million as a result of the Council Tax reforms will be available in full to be spent in the Council area it was collected.

The settlement package requires Councils to maintain the overall pupil/teacher ratio at 2016-17 levels (13.7) and secure places for all probationers who require one under the teacher induction scheme.

The package provides flexibility to increase Council Tax by up to 3%.

On 2 February 2017 the Finance Secretary confirmed, as part of an agreement with the Scottish Green party to support the passage of the budget bill, that Councils would benefit from an additional £130 million revenue and £30 million capital funding for them to spend at their discretion on local priorities. For Midlothian this equates to an additional £2.115 million revenue grant and £0.458 million capital grant.

Earlier projections of the budget shortfall for 2017/18 had been based on a £1.000 million grant reduction together with a reduction in the core grant funding in respect of the monies raised by Council Tax reform. It is now estimated that for 2017/18 Midlothian will receive a total funding package of £153.022 million of which £3.330 million is ring fenced, £2.273 million for the Attainment Scotland Fund and £1.057 for Community Justice. This leaves a core grant allocation of £149.692 million. This core grant allocation is approximately £2.000 million less than the equivalent sum for 2016/17.

At its meeting on 20 December 2016 Council agreed note the terms of the settlement as set out in the letter from the Cabinet Secretary for Finance and the Constitution and agree that the Leader of the Council write to the Cabinet Secretary confirming Midlothian Council's agreement to the offer and accepting the full package of measures and benefits.

It is now estimated that the impact of the revised settlement would reduce the budget shortfall for 2017/18 by £0.358 million from that set out in the report on 20 December 2016.

The 2018/19 to 2021/22 year grant projections set out later in this report have also been reassessed from those presented on 20 December 2016 to reflect the impact of the original 2017/18 settlement and are based on a central planning assumption that reductions in grant at a similar level to the original 2017/18 settlement will continue (a 3.6% reduction at a national level, offset by the impact of the relative growth in the Midlothian population).

It is stressed that the grant settlement figures for 2018/19 to 2021/22 set out table 1 are projections, the actual figures being dependant on future budget decisions taken by Government. However they do provide Council with an assessment of the impact of the grant settlement on the Council's financial position. Critically they highlight the extent of the challenge ahead for the term of the next Council and the extent to which service provision will have to be transformed.

4 Council Tax

The budget shortfalls set out in table 1 are based on the current Band D Council Tax of £1,210 and reflect the additional income from an increase in the number of properties, the changes to discounts on second homes and the anticipated income generated by the reform of Council Tax.

As indicated earlier the funding package set out in Finance Circular 9/2016 means that the additional income arising from reform will be available in full to be spent in the Council area it was collected. The package also provides flexibility to increase Council Tax by up to 3%.

For Midlothian a 3% increase is estimated to generate £1.254 million for 2017/18 rising to £1.334 million by 2021/22 and would result in Band D Council Tax rising to £1,246 in 2017/18 and to £1,403 by 2021/22. Given the grant prospects and budget shortfalls set out in this report it is recommended that Council apply the full 3% increase in 2017/18 to contribute to reducing the projected budget shortfalls.

Appendix 1 sets out the proposed Council Tax levels for 2017/18 based on the recommended 3% increase.

5 Cost of Services

The assessment of the projected cost of services for 2017/18 to 2021/22 set out in this report reflects the latest information available.

The projected cost of services for 2017/18 has increased from that set out in the update provided to Council on 20 December 2016. This is attributable to the grant settlement, and the other cost pressures as detailed in table 3. These changes increase the projected budget shortfall for 2017/18 to £12.431 million, an increase of £1.351 million from the shortfall set out in the previous report.

Table 2 provides an analysis of the principal year on year budget changes which include the following key assumptions and cost drivers:

- Pay inflation averaging 1.4% for Local Government Workers and 1% for Teachers and Chief Officials in 2017/18. Thereafter 1% per annum for all groups. Since the last report the provision for 2017/18 has been increased by £350,000 to reflect our current best estimate of the likely impact.
- The cost of the Review of Pay and Grading and subsequent incremental pay progression;
- The impact of Pension Reform and anticipated changes in the Council's contribution towards employee pensions costs;
- Provision for the Apprenticeship Levy which is 0.5% of the pay bill and equates to £0.480 million. Previous projections were based on this cost being offset by additional grant or other funding from Government. However there is no provision in the grant settlement and the most recent indication from COSLA officials is that there is now unlikely to be any other funding provided to Councils to offset the impact of the levy.
- Provision for the Devolved School Management allocation to schools based on the indicative pupil numbers and the requirement to maintain the pupil teacher ratio.
- The additional cost, revised since the last report, of delivering the statutory 25 hours of teacher contact each week in primary schools;
- Contractual inflation linked to existing contractual conditions, many of which mirror pay inflation assumptions;
- An initial provision for future years costs of maintain pay levels for procured care services at or above the living wage;
- The impact of current demand for services;
- The demographic impact on the future demand for services;
- Borrowing costs related to capital investment decisions based on future interest rate forecasts provided by the Council's Treasury Advisers;
- Any new government policy requiring budgetary growth will be fully funded through increased Scottish Government grant;
- Council Tax income continues to grow in line with previous trends and planned future housing growth.

The 2017/18 budget shortfall and projections for later years reflecting the assumptions set out in sections 3 to 5 are therefore as follows:-

Table 1: Budget Shortfalls 2017/18 to 2021/22– 7 February 2017

	2017/18	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m	£m
Cost of Services	205.573	212.448	220.653	228.351	235.924
Less: Council Tax	(43.450)	(44.100)	(44.750)	(45.400)	(46.050)
Less: Scottish Government Grant	(149.692)	(145.708)	(142.118)	(138.618)	(135.205)
Budget Shortfall	**12.431**	**22.640**	**33.785**	**44.333**	**54.669**

The budget shortfall in 2017/18 equates 6% of the net cost of services and the projections indicate this could rise to 23% by 2021/22.

As Council is aware, significant elements of the budget are either fixed or are challenging to change for a number of reasons including:-

- Historic decisions, for example, loan charges and unitary charge contractual payments;
- Specific conditions, for example the maintenance of the teacher pupil ratio; and
- Growing demand for services through demographic pressures.

These elements of the budget equate to £112 million in 2017/18 and are projected to rise to £140 million by 2021/22. Consequently the budget shortfall expressed as a percentage of the remainder of the budget equates to 13% for 2017/18 and has the potential to rise to 57% by 2021/22.

Whilst the projected cost of service provision, Council Tax and Scottish Government grant has been projected forward for 2018/19 to 2021/22 these are very much indicative projections based on the assumptions set out in sections 3 to 5 and will inevitable change over the period.

The main purpose of the projections is to provide Council with an assessment of the key factors which influence income and expenditure and the overall impact these may have on the Council's financial position for future years. Critically they highlight the extent of the challenge ahead for the term of the next Council and the extent to which service provision will have to be transformed.

Again it is stressed that the cost of services set out in table 1 above and the analysis set out in table 2 and 3 for 2018/19 to 20121/22 are projections based on an analysis of a range of information sources. The projections and planning assumptions on which they are based will be updated and reported to Council as new information becomes available.

Members should note that the projections are based on the continuation of the existing service delivery and funding arrangements for Local Government both of which Scottish Government has indicated its intention to review during the term of the current Parliament.

The budget shortfalls set out in table 1 arise for the following reasons:

Table 2: Analysis of Shortfalls – 7 February 2017

	2017/18	2018/19	2019/20	2020/21	2021/22
	£m	**£m**	**£m**	**£m**	**£m**
Opening Shortfall / (surplus)	**2.668**	**12.431**	**22.640**	**33.785**	**44.333**
Pay Inflation and Progression	2.700	1.893	2.344	2.297	2.451
Pensions Reform	0.350	0.000	0.000	0.000	0.000
Pension Contributions	0.000	0.450	0.450	0.450	0.000
Apprenticeship Levy	0.500	0.000	0.000	0.000	0.000
Contractual Inflation	0.465	0.547	0.637	0.571	0.652
Demographics: Care	1.120	1.040	1.040	1.040	1.040
Demographics: School Rolls	2.098	2.260	2.770	2.798	3.083
Demographics: Thorough Care	0.600	0.000	0.000	0.000	0.000
25 Hours in Primary Schools	0.300	0.090	0.000	0.000	0.000
Demand pressures: Children	0.000	0.324	0.024	0.024	0.024
School Estate Investment	0.311	0.381	1.126	0.033	0.036
Waste Disposal Costs	0.320	0.213	(0.285)	0.125	0.125
Non Domestic Rates	0.128	0.132	0.135	0.138	1.142
Borrowing Costs	0.997	(0.003)	(0.089)	0.123	(0.007)
Scottish Government Grant	2.342	3.466	3.590	3.500	3.413
Council Tax Income	(2.850)	(0.650)	(0.650)	(0.650)	(0.650)
Other Movements	0.382	0.066	0.053	0.099	(0.973)
Totals	**12.431**	**22.640**	**33.785**	**44.333**	**54.669**

The principal movement from the figures set out in the 20 December 2016 report are as follows.

Table 3: Movement from 20 December 2016 to 7 February 2017

	2017/18	2018/19	2019/20	2020/21	2021/22
	£m	**£m**	**£m**	**£m**	**£m**
Shortfall 20 December 2016	**11.080**	**18.867**	**27.422**	**35.470**	**43.393**
Grant Settlement	(0.358)	2.108	4.698	7.198	9.611
Apprenticeship Levy	0.480	0.480	0.480	0.480	0.480
Pay Inflation	0.350	0.350	0.350	0.350	0.350
Additional Cost of 25 hours in Primary Schools	0.140	0.140	0.140	0.140	0.140
Other movements reflecting current service provision	0.739	0.695	0.695	0.695	0.695
Shortfall 7 February 2016	**12.431**	**22.640**	**33.785**	**44.333**	**54.669**

6 Sensitivity Analysis

Given the level of uncertainty for future year grant settlements and outstanding pay awards table 4 provides a sensitivity analysis reflecting the potential impact of different scenarios/outcomes for these two key aspects of the budget.

Scenario 1. This is a more optimistic scenario which continues to assume a 1% pay award in each of the years but with cash flat grant settlements. Otherwise all other assumptions remain as set out in section 3.

Scenario 2. Is a more pessimistic scenario which assumes a 2% pay award and reducing grant income as set out in section 2.

Table 4: Sensitivity Analysis – 7 February 2017

	2018/19 £m	2019/20 £m	2020/21 £m	2021/22 £m
Scenario 1				
Central Assumption	22.640	33.785	44.333	54.669
Cash Flat Government Grant	(3.466)	(7.056)	(10.556)	(13.969)
Amended Shortfall	**19.174**	**26.729**	**33.777**	**40.700**
Scenario 2				
Central Assumption	22.640	33.785	44.333	54.669
Revised Pay Award Assumption	1.893	4.237	6.534	8.895
Amended Shortfall	**24.533**	**38.022**	**50.867**	**63.564**

These scenarios help to demonstrate the significance of the impact that changes from the central planning assumption for either government grant or pay inflation have on the projected budget shortfalls.

7 Midlothian Integration Joint Board

The 2017/18 budget as set out in appendix 2 provides for an allocation to the Integrated Joint Board (IJB) for 2017/18 of £37.510 million. This represents a net increase of £0.424 million from the 2016/17 allocation.

The provisions set out in the grant settlement package would allow Council to reduce its allocation to the IJB by a maximum of £1.160 million. However given the demographic and other cost pressures projected for Heath and Social Care such a reduction may not be feasible without a reassessment of the Services delegated to the IJB and as such it is unlikely that the IJB would agree to the reduced allocation. Consequently the reduction is not reflected in the IJB allocation however the feasibility of part or all of the reduction being achieved will be raised with the Chief Officer and Chief Financial Officer of the IJB.

The Chief Officer and Chief Financial Officer of the IJB are currently supporting the IJB to develop its 2017/18 Financial Plan and the Directions it will issue to the Council and NHS Lothian within the context of the indicative allocations from the Council and NHS Lothian.

Subject to Council determining its budget for 2017/18 it is recommended that Council approve the allocation of £37.510 million to the Midlothian Integrated Joint Board for 2017/18 in respect of delegated services, noting that the feasibility of part or all of the £1.160 million reduction being applied will be raised with the Chief Officer and Chief Financial Officer.

8 Change Programme

The strands of work that will continue to be necessary to address the projected budget shortfalls represent a change programme, encompassing:-

- The Delivering Excellence programme;
- The delivery of savings approved in 2016/17 and 2017/18; and the continued control over expenditure;
- The Transformation Programme;
- The EWiM programme;
- An updated Capital Strategy and Reserves Strategy;
- Operational savings encompassing financial discipline measures;
- The development of further savings options for 2018/19 and beyond.

8.1 Delivering Excellence

The Delivering Excellence framework supports the repositioning of services to ensure they have a greater emphasis on and achieve better outcomes for those most disadvantaged and vulnerable in the community. The framework focuses on reshaping service delivery as the most sustainable way to address the financial and service challenges and maintain financial sustainability.

The framework sets out an approach that provides the means to:

- Realise savings of the scale and magnitude required and to continue to deliver high quality services by engaging staff, partners, stakeholders and citizens to determine the nature of service delivery, the level of service standards and the method of delivering these services;
- To perform successfully in this environment, the Council will require to forward plan for the period beyond known financial settlements, to prioritise the services to be delivered and to clearly identify those services which will no longer be funded or indeed provided or may be provided through alternative mechanisms or approaches; and
- To ensure that there is achievement of the outcomes and priorities of the Council and Community Planning Partners.

The savings proposals presented to Council on 20 December 2016 emerged from the focussed Delivering Excellence activity which has taken place over the earlier part of the year. In addition to identifying savings proposals to reduce the 2017/18 budget gap it has also identified key transformational activities which it is anticipated can generate savings in future years. These are summarised in table 5, or where they relate to the existing transformation programme they have been reflected in table 6 included in section 8.2 – Transformation Programme.

As each strand is developed proposals will be presented to the Business Transformation Steering Group for their consideration and direction and then to Council.

Table 5: Delivering Excellence – Emerging Projects – 7 February 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Asset Management	0.078	0.500	2.650	2.650
Waste Services	0.400	0.400	0.400	0.400
Destination Hillend	0.000	1.000	1.000	1.000
Others	0.070	0.284	0.284	0.284
Totals	**0.548**	**2.184**	**4.334**	**4.334**

8.2 Transformation Programme

The existing Transformation Programme remains a major focus with a continued drive towards delivering on the agreed outcomes and targets. The future year's savings targets incorporated in the Financial Strategy are derived from those set out in the Council's Transformation Programme update reports to Business Transformation Steering Group (BTSG) revised to incorporate the transformational activity as outlined in section 8.1 and are set out in table 6 below.

Table 6: Council Transformation Programme Savings – 7 February 2017

	2017/18	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m	£m
Children's Services	0.532	0.806	0.867	0.867	0.867
Services to Communities	0.200	1.050	1.050	1.050	1.050
Education	0.329	0.755	0.790	0.790	0.790
Customer Service	0.175	0.175	0.175	0.175	0.175
Health & Social Care	1.555	2.555	2.555	2.555	2.555
Totals	**2.791**	**5.341**	**5.437**	**5.437**	**5.437**

The savings targets set out in table 6 exclude those already reflected in the 2016/17 approved budget and are predicated on the outcomes of the reviews and any subsequent decisions taken by Council and so remain indicative.

8.3 Asset Management

The position remains as reported on 28 June 2016.

8.4 Capital Strategy and Reserves Strategy

A separate report is on today's agenda setting out the latest projection of the General Services Capital plan. An update on General Fund Reserves is set out in section 11 of this report.

The £0.458 million of additional capital grant funding will increase the headroom reported in the General Services Capital plan report elsewhere on today's agenda. However it does not have a material impact on the recommendations set out in that report nor does it have a material impact on the Treasury Management and Investment Strategy report.

The impact of the additional capital grant will be reflected in the next General Service Capital Plan report to Council in June 2017.

8.5 Operational Savings

The budget projections set out in tables 1 and 2 already reflect the operational savings reported in previous year's budgets.

As reported on 20 December 2016 further operational savings have been identified by the Strategic Leadership Group. These total £2.021 million in 2017/18 rising to £3.139 million by 2021/22.

8.6 Savings

On 20 December 2016 Council approved a range of savings proposals. These total £2.115 million in 2017/18 rising to £4.121 million by 2021/22.

On 1 February Scottish Government announced the school level pupil equity funding (Attainment Scotland fund) allocations together with draft national operational guidance. It is clear from that guidance that the decision of Council on 20 December 2016 in respect of Music Tuition, "to ensure that funding for this is directed from the recently announced schools' attainment funding", would not be achievable and accordingly the savings reduce to £1.995 million in 2017/18 and £4.001 million by 2021/22.

8.7 Fees and Charges

The position remains as reported on 20 December 2016.

8.8 Summary of Financial Strategy

The updated projections incorporating the impact of the various strands of the Financial Strategy and the full 3% per annum increases in Council Tax are set out in table 7 below. The change programme set out above reduces the remaining budget gap for 2017/18 to £3.970million.

As part of the development and consideration of the proposals recommended by the Strategic Leadership Group all Heads of Service have provided assurance to me, as Section 95 Officer, that the savings proposals incorporated in 2017/18 are achievable. It is stressed however that ultimately the achievement of savings will also be dependent on decisions taken by Council.

In order to achieve a balanced budget for 2017/18 it will be necessary to utilise £3.970 million of reserves. While this will result in a level of contingent reserves below the level previously recommended it is considered a practical response to the financial position against the alternative of developing and bring forward additional savings proposals for immediate implementation without the opportunity for further consultation.

Table 7: Financial Strategy 2017/18 to 2021/22 – 7 February 2017

	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	2021/22 £m
Budget Shortfall Table 1	**12.431**	**22.640**	**33.785**	**44.333**	**54.669**
Less: Change Programme					
Delivering Excellence 8.1	-	(0.548)	(2.184)	(4.334)	(4.334)
Transformation Programme 8.2	(2.791)	(5.341)	(5.437)	(5.437)	(5.437)
Asset Management 8.3	0.000	0.000	(0.288)	(0.288)	(0.288)
Operational Savings 8.5	(2.021)	(3.029)	(3.139)	(3.139)	(3.139)
Savings Options 8.6	(1.995)	(2.283)	(2.531)	(3.391)	(4.001)
Fees and Charges 8.7	(0.100)	(0.180)	(0.240)	(0.280)	(0.300)
Less:					
Council Tax Increase	(1.254)	(2.528)	(3.823)	(5.138)	(6.472)
Council Tax on Second Homes	(0.300)	(0.250)	(0.200)	(0.200)	(0.200)
Utilisation of Reserves	(3.970)	-	-	-	-
Remaining Budget Gap	**-**	**8.481**	**15.943**	**22.126**	**30.498**

9 Governance and Timetable

Each element of the Financial Strategy continues to have clear governance in place to ensure the timely delivery of the work stream, with proposals being reported through Business Transformation Steering Group and then to Council as appropriate.

Members are reminded that Council has a duty as set out in Section 93 of the Local Government Finance Act 1992 (as amended) to set its Council Tax and a balanced budget for the following financial year commencing 1 April by 11 March.

Accordingly the budget timetable, agreed by Council on 28 June 2016, provides for Council to set Council Tax and determine a budget for 2017/18 at today's meeting.

Furthermore members are also reminded that in terms of Section 112 of the Local Government Finance Act 1992 (as amended) it is an offence to participate in any vote in respect of setting Council Tax where the member has unpaid Council Tax. Members are required to disclose the fact this section of the act applies to them and not vote on any question with respect to the matter.

10 Focussing Resources to Key Priorities

The Financial Strategy is designed to ensure that available resources are as far as possible targeted on delivery of improved outcomes, particularly against the key priorities of:-

- Reducing the gap in learning outcomes
- Reducing the gap in health outcomes
- Reducing the gap in economic circumstances

The Midlothian Community Planning Partnership continues to prioritise the available resources towards the delivery of the partnerships key priorities and the Financial Strategy sets out for partners the parameters the Council is working within and provides a means to better facilitate the sharing of budget and resource planning information.

The Change Programme, incorporating the Delivering Excellence framework and Transformation Programme, is central to ensuring that resources are directed towards the priorities set out in the Midlothian Single Plan. The development activity for the 2017/18 budget has ensured that as far as possible the resultant budget, reflecting the savings outlined in section 10, will be focussed on delivery of the Council's key priorities.

Recognising the impact of continued substantial financial constrain and the projected remaining budget gaps set out in table 7 the Strategic Leadership Group is engaged in developing further options for change so that these can be considered early in the term of the next Council.

11 Reserves

The projected position for General Fund Reserves is set out in the Financial Monitoring 2016/17 – General Fund Revenue report also on today's agenda.

As indicated in section 8 to balance the 2017/18 budget it will be necessary to utilise £3.970 million of General Fund Reserves which would reduce the contingency level of General Fund Reserves to £5.408 million.

At £5.408 million the contingency is below the £8 million level set out in the Reserves Strategy approved by Council on 8 November 2016 and equates to 2.7% of projected net expenditure for 2017/18. It still provides a level of contingency against unforeseen events or financial risks.

Table 8 summarises the General Fund reserve position.

Table 8: Available General Fund Reserve 31 March 2017 – 7 February 2017

	£million
General Fund Balance at 31 March 2017	**13.243**
Earmarked for specific purposes	
• Earmarked for Council Transformation	(3.838)
• Borders Rail Economic Development Opportunities	(0.027)
Proposed Utilisation in 2017/18	(3.970)
Available Contingent Reserve at 31 March 2017	**5.408**

In addition the unallocated balance on the Capital Fund at 31 March 2017 is projected to be £8.556 million, equivalent to 4.3% of projected net revenue expenditure.

12 Report Implications

12.1 Resources

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

12.2 Risk

Within any financial projections, there are a number of inherent assumptions in arriving at figures and budget provisions and therefore risks that may be faced if costs change or new pressures emerge. The following key risks and issues are highlighted in the context of this report:

- The economic outlook and decision by Scottish Government on future years grant settlements and grant distribution;
- Given the nature of the savings options incorporated in the budget proposals the increase risk of non-delivery or late delivery of planned savings, including those arising from reductions in the staffing establishment;
- The risk to service provision and service users associated with a continued decline in available resources to fund services.
- Outstanding pay award settlements and the implications of the National Living Wage for external service providers;
- Actual school rolls for the 2017/18 academic term exceeding those provided for in the budget;
- The impact of the wider economic climate on range of factors including: inflation, interest rates, employment, tax and income levels and service demands;
- Cost pressures, particularly demographic demand, exceeding budget estimates;
- The impact of Universal Credit, and potential pension changes;
- The costs of implementation of national policies varying from the resources provided by Government; and
- Unplanned capital investment requirements and associated cost.

The Financial Strategy aims to mitigate a number of these risks by setting out the key assumptions on which forward plans are based, and through the Change Programme activities, setting out the early identification of future saving proposals.

12.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☐ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☒ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

12.4 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 budget projections indicate that in 2021/22 the Council will have available in the region of £180 million for the provision of services and the pursuit of key outcomes as set out in the Single Midlothian Plan

12.5 Adopting a Preventative Approach

Whilst the proposals in this report do not directly impact on the adoption of a preventative approach, an effective Financial Strategy in turn allows resources to be prioritised to support prevention.

12.6 Involving Communities and Other Stakeholders

Shaping our Future, the consultation strand of the Delivering Excellence framework, has been a key aspect of informing the community and other stakeholders of the financial and service challenges and included consultation on a range of options as the change programme developed.

In addition, there continues to be engagement with the recognised Trade Unions on the Council's financial position and service challenges.

12.7 Ensuring Equalities

Whilst the financial strategy and the supporting proposals have been developed within the context of ensuring that resources are directed towards key priorities, Midlothian Council is committed to the ethos of the Equality Act 2010 and has considered the interests of the most vulnerable in our communities through equality impact assessment for all the budget proposals.

An updated EQIA encompassing the revenue budget for 2017/18 as set out in table 7 is attached as appendix 3.

12.8 Supporting Sustainable Development

There are no direct sustainability issues arising from this report.

12.9 IT Issues

There are no direct IT implications arising from this report.

13 Summary

This report sets out recommendations to enable Council to set Council Tax and to determine a budget for 2017/18.

It also provides:-

- An update on Scottish Government Grant;
- Updated budget projections for 2017/18 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios for later years;
- An update on the resources to be provided to the Midlothian Integration Joint Board in 2017/18;
- An update on the strands of the Change Programme;
- The resultant 2017/18 service budget analysis;

- An update on reserves.

14 Recommendations

Council is recommended to:-

a) In line with the provisions of the Grant Settlement package set a Band D Council Tax of £1,246 for 2017/18 as set out in appendix 1;

b) Note the updated projected cost of services, key assumptions and resultant budget shortfalls as set out in section 3;

c) Note the continuing uncertainties and the potential impact as outlined in the differing scenarios as set out in section 6;

d) Approve the 2017/18 service budget analysis as set out in appendix 2, including the utilisation of £3.970 million of reserves.

e) Approve the allocation of £37.510 million to the Midlothian Integrated Joint Board for 2017/18 in respect of delegated services, noting that the feasibility of part or all of the £1.160 million reduction being applied will be raised with the Chief Officer and Chief Financial Officer of the IJB.

a) Note that the Strategic Leadership Group is engaged in developing further options for change so that these can be considered early in the term of the next Council.

b) In considering the recommendations also consider the contents of the draft EQIA set out in appendix 3;

c) Otherwise note the contents of the report.

Date 3 February 2017

Report Contact:
Gary Fairley Tel No 0131 271 3110
gary.fairley@midlothian.gov.uk

APPENDIX 1

MIDLOTHIAN COUNCIL

Council Tax for Financial Year 2017/18

This statement gives details of the 2017/18 Council Tax payable in respect of a chargeable dwelling in each of the valuation bands specified in Section 74(2) of the Local Government Finance Act 1992 determined in accordance with Section 74(1) of the Act (as amended)
Based on Band D Council Tax of £1,246.

Band	Range of Values From £	To £	Band D Proportion	Council Tax £
A	-	27,000	240/360	830.66
B	27,001	35,000	280/360	969.11
C	35,001	45,000	320/360	1,107.55
D	45,001	58,000	360/360	1,246.00
E	58,001	80,000	473/360	1,637.10
F	80,001	106,000	585/360	2,024.75
G	106,001	212,000	705/360	2,440.08
H	212,001	upward	882/360	3,052.70

MIDLOTHIAN COUNCIL Appendix 2

REVENUE BUDGET 2017/18 SUMMARY

Service Function	**Budget 2017/18 £**
Management and Members	1,603,944
Education Communities and Economy	
Childrens Services	14,542,843
Communties and Economy	3,987,437
Education	85,143,974
Health and Social Care	
Adult Social Care	37,509,783
Customer and Housing Services	11,578,657
Resources	
Commercial Services	15,472,619
Finance and Integrated Service Support	11,736,179
Properties and Facilities Management	12,949,607
Lothian Valuation Joint Board	555,551
Centrally Held Budget Provisions	1,591,000
Non Distributable Costs	1,338,436
GENERAL FUND SERVICES NET EXPENDITURE	198,010,030
Loan Charges	7,406,000
Investment Income	(300,475)
Council Transformation Programme savings targets	(1,667,125)
Allocations to HRA, Capital Account etc.	(4,782,000)
NET EXPENDITURE	**198,666,430**
Utilisation of Reserves	3,970,430
Scottish Government Grant	149,692,000
Council Tax	45,004,000
TOTAL FUNDING	**198,666,430**

Appendix 3

Overview Equality Impact Assessment (EqIA)

on

Midlothian Council

Budget

2017/18

31 January 2017

Midlothian Council

Equality Impact Assessment (EqIA) on Midlothian Council Budget 2017/18

Budget Proposal: Operational Policy Council Tax	 As set out in appendices to Council report 20/12/16 A 3% increase as set out in report 07/02/17
Directorate and service area	List as detailed above

Overview of Budget Investment through the Financial Strategy	The core objective of the Financial Strategy 2017/18 to 2021/22 is that of securing the Council's continued financial sustainability during what is expected to be an ongoing period of financial constraint coupled with continuing service demand pressures and increasing customer expectations.
Completion Date	31 January 2017
Lead officer	Gary Fairley

Aims and Objectives

The public sector continues to face significant service delivery challenges due to reduced income streams, funding constraints, inflationary cost pressures and additional legislative burdens. Demand for public services in Midlothian continues to increase as a consequence of changes in the size and profile of the county's population with greater numbers of young and older people, those in poor economic situations, and those with disabilities be they physical, sensory, mental health or learning disabilities. The Council must continue to prioritise expenditure on public services which prevent negative outcomes for those within its communities whilst securing maximum benefit from all available resources. Accordingly, it is prudent that significant savings and cuts are made over the coming years and projected budget shortfalls stemmed. This will allow the Council to maintain its financial sustainability and also to ensure that all within its communities, irrespective of protected characteristics, (age, disability, gender re-assignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex, and sexual orientation plus in Midlothian poor socio-economic circumstances), are not unlawfully discriminated against, and that equality of opportunity and advancement of good relations in upheld between those who have a protected characteristic and those who do not.

1. Does the proposed budget affect people? Yes ☒ No ☐

2. What is/are the reason(s) for your proposed Council Tax Increase, budget savings and use of reserves?

On 7 February 2017 Council will be provided with an updated assessment of projected budgets shortfalls through to 2021/22 which, based on the assumptions set out in that report, projected a budget shortfall for 2017/18 of £14.546 million rising to £56.784 million . Encompassing the savings targets for the change programme and the recommended 3% per annum increase in Council Tax resulted in a use of reserves in 2017/18 £5.965 million for 2017/18 and a potential budget gap by 2021/22 of £32.493 million.

Scottish Government grant accounts for 80% of external funding. As in previous years the prospects for and the timing of future years grant settlements have been a major factor which dominated the financial projections set out in the Financial Strategy 2017/18 to 2021/22. The Grant Settlement, which was published on the 15 December 2016 resulted in a reduction of core grant funding which increased the budget gap from that previously projected by £1.8 million in 2017/18. In addition since the December report additional budget provision has also been made for pay awards, the provision of 25 hours class contact and the unfunded costs of the Apprenticeship Levy. While these national policy initiatives will all benefit minority groups they do however increase the budget gap.

In addition whilst the grant settlement was only for 2017/18 it will have an impact on medium term plans and as such will significantly influence the timing of and the extent to which Council has to reshape and reduce service budgets in order to maintain financial sustainability.

3. Impact

Which of the protected characteristics* will the proposed budget savings have an impact upon?

Equality Target Group*	**Positive Impact**	**Negative Impact**	**Relevant evidence/ information**
Age			Overall Grid in Appendix 1 attached.
Disability			
Gender Reassignment			
Marriage & Civil Partnership			
Pregnancy and maternity			
Race			
Religion or Belief			
Sex			
Sexual Orientation			

4. Overall Impact of Budget

Each budget proposal which was presented in December 2016 was subjected to an Equality Impact Assessment. The overall grid (Appendix 1) details the protected characteristics which are considered to be most likely to be affected in a potentially negative way. The overall grid includes the currently non-enacted 10th protected characteristic of socio-economic deprivation which Midlothian Council voluntarily considers. It is understood that this 10th protected characteristic will be enacted in 2017 by the Scottish Government.

In no proposal area has any unlawful negative impact been identified, and where possible reduction/removal of services will be monitored to establish the actual affect to those within our communities.

5. How will the implementation of proposed budget savings be communicated to those affected by any changes?

Information will be available on the Council's web site and communicated to affected businesses/customers/service users by letter, email, etc. In addition, information documents, as required, can and will be made available in different formats and languages on request. If an individual or group require this information in another language or format, then they should email equalities@midlothian.gov.uk or telephone the Equality, Diversity & Human Rights Officer on 0131 271 3658.

6. How will you monitor the impact of the changes proposed? When is the budget due to be reviewed?

Changes will be monitored through Covalent, the council's performance management system, discussion groups and forums, fees and charges income, and various other methods detailed in the individual equality impact assessments.

The overall budget is reviewed on an annual basis.

7. Please use the space below to detail any other matters arising from the Equality Impact Assessment (EqIA) process.

   If available, mitigating actions for each of the proposals have been outlined in the individual equality impact assessments.

   Where no mitigating actions are possible it is considered that any negative effects are not unlawful and are justifiable on a benchmarking/inflationary basis.

   Midlothian Council is committed to the ethos of the Equality Act 2010 and has considered this through equality impact assessment of all its budget proposals. For proposals being decided upon on 20 December 2016 the relevant Equality Impact Assessments have been published as legislation requires and this overall EQIA encompasses these decisions, the increase in Council Tax and the resultant 2017/18 service budgets.

Please send an electronic copy of completed forms to lesley.crozier@midlothian.gov.uk

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

		Protected Characteristics									
Service	**Budget Proposals**	**Age**	**Disability**	**Gender re-assignment**	**Marriage & Civil Partnership**	**Pregnancy & Maternity**	**Race**	**Religion or belief**	**Sex**	**Sexual Orientation**	**Socio-economic deprivation**
Council Tax	Increase 3% or £36 per annum for Band D of. to £1,246										√
Commercial Operations											
	Service Review - operational proposal										
Roads											
	Review Spending on Roads Maintenance Capitalising saving for 2017/18 only - policy proposal	√	√								√
	Review Winter Maintenance Spend - policy proposal	√	√								√
	Review Flood Prevention Work - policy proposal	√	√								√
Waste											
	Increase Trade Waste Charges - policy proposal										√
Land & Countryside Services											
	Cease direct provision of the Garden Assistance Programme - policy proposal	√	√								√
	Review the financial contribution to the Pentland Hills - policy										√

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

Service	Budget Proposals	Protected Characteristics									
		Age	Disability	Gender re-assignment	Marriage & Civil Partnership	Pregnancy & Maternity	Race	Religion or belief	Sex	Sexual Orientation	Socio-economic deprivation
	proposal										
	Review grass cutting standards - policy proposal										√
	Review number of football pitches - policy proposal	√	√								
	Review Christmas light funding - policy proposal	√				√					
	Review providing hanging baskets, planters and flower beds - policy proposal										
	Explore Closure Vogrie golf course - policy proposal										
	Reduce play area & right of way budgets - operational proposal	√	√			√					√
Travel & Fleet Services											
	Review travel arrangements for Grey Fleet - policy proposal		√								√
	Reduce bus shelter maintenance - operational proposal	√	√			√	√				√
	Increase sale of Health & Safety training courses - operational proposal										
Communities and Economy											

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

		Protected Characteristics									
Service	**Budget Proposals**	**Age**	**Disability**	**Gender re-assignment**	**Marriage & Civil Partnership**	**Pregnancy & Maternity**	**Race**	**Religion or belief**	**Sex**	**Sexual Orientation**	**Socio-economic deprivation**
	Merger of Communities & Economic Development Teams - operational proposal										√
	Cease funding from the Midlothian Business Partnership - policy proposal	√	√						√		√
	Charging for Section 75 Legal Agreement Monitoring - policy proposal										√
Customer & Housing Services											
	Revenues Service Review 2017 - operational proposal										
Education											
	Reduce central curriculum budget - operational proposal								√		√
	Reduce central training budget - operational proposal										√
	Reduce budgets Devolved to School Management (DSM) - policy proposal	√							√		√
	Review of Inclusion Policy - policy proposal	√	√								√
	Mini Service Reviews within Education - operational proposal										

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

Service	Budget Proposals	Protected Characteristics									
		Age	Disability	Gender re-assignment	Marriage & Civil Partnership	Pregnancy & Maternity	Race	Religion or belief	Sex	Sexual Orientation	Socio-economic deprivation
Finance											
	Review 1 - BT/Q&S/PPT - operational proposal										
	Vacant Posts (Grade 4 - 8) - Freeze (Business Services) - operational proposal										
	Vacant Posts Balance - operational proposal										
	Rationalisation of Support Services (OD/HR) - operational proposal										
	Rationalisation of Support Services (E&R) - operational proposal										
	Removal of Vacant Material Planner Post(Procurement & Stores) - operational proposal										
	Consolidate Stores (Fleet) - operational proposal										
	Technology Changes: Digital Services & Supplies - operational proposal										
	Procurement Rebates SXL Contracts - operational proposal										
	Internalise Arrears Court actions - Customer & Housing Services (Legal Services) - operational proposal										
	Amend Treasury Strategy as a consequence of BREXIT - operational proposal										
	F&ISS Review - Staff Reduction Target of 7% - operational proposal										

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

Service	Budget Proposals	Protected Characteristics									
		Age	**Disability**	**Gender re-assignment**	**Marriage & Civil Partnership**	**Pregnancy & Maternity**	**Race**	**Religion or belief**	**Sex**	**Sexual Orientation**	**Socio-economic deprivation**
Legal Services											
	Curators' Fees - policy proposal										
	Legal Fees - Licensing - policy proposal	√	√								√
Property & Facilities Management											
Catering											
	Review kitchen staff due to dropping numbers at Dalkeith Campus - operational proposal	√	√						√		√
	Increase school meals by 15 pence - policy proposal – amended to 10p										
	Reduce P1 - P3 free fruit to once a week - policy proposal										√
	Reduce waste in plates/cutlery - operational proposal										
	Increase vending/trolley prices - operational proposal		√								√
	Review public toilet provision - policy proposal – amended reduced saving	√	√			√					
Facilities											
	Merge janitorial S & L staff in Hubs - operational proposal										

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

Service	Budget Proposals	Protected Characteristics									
		Age	Disability	Gender re-assignment	Marriage & Civil Partnership	Pregnancy & Maternity	Race	Religion or belief	Sex	Sexual Orientation	Socio-economic deprivation
	Review FM Officers from two to one (dependent on shared primary school janitors) - operational proposal	√	√								√
Building Services											
Sport & Leisure											
	Review Sport & Leisure staffing - operational proposal	√	√						√		√
	Reduce opening hours during low usage periods at leisure centres - policy proposal	√	√						√		√
	Introduce soft play at Penicuik Centre - operational proposal										
	Increase Sport and Leisure charges by 10% - policy proposal	√	√				√		√		√
PPP Management											
	Maximise use of contractual entitlement in PPP core hours - operational proposal	√	√								
	Review of PPP Contracts - policy proposal										
Property Assets											
	Introduce Energy Management Systems to control heating / power use remotely - operational proposal										
	Mini service review - operational proposal	√	√						√		√
	Reduce drainage charging by utilising soakaways / SUDS ponds -	√	√				√		√		√

		Protected Characteristics									
Service	**Budget Proposals**	**Age**	**Disability**	**Gender re-assignment**	**Marriage & Civil Partnership**	**Pregnancy & Maternity**	**Race**	**Religion or belief**	**Sex**	**Sexual Orientation**	**Socio-economic deprivation**
	operational proposal										
	Review water metering arrangements to downsize meters, reducing charges - operational proposal	√	√				√		√		√
	SALEX funding for energy saving initiatives eg lighting, pool covers etc - operational proposal	√	√				√		√		√
EWIM											
	Independent Stores partnership renting new depot space - operational proposal	√	√				√		√		√
	Bespoke joinery through Independent Stores - operational proposal	√	√				√		√		√
	Property & Facilities Management Service Review - operational proposal										
	Staff consolidation due to reduced locations at new depot - operational proposal	√	√				√		√		√
	Earlier closure of Penicuik Town Hall and Library HQ - operational proposal	√	√				√		√		√
	Creation of IJB Hub at St Andrew's Street - operational proposal	√	√				√		√		√
Children's Services											
	Review of Family Support Staff (2%)	√	√				√		√		√

APPENDIX 1 - OVERVIEW EQUALITY ASSESSMENT GRID

Service	**Budget Proposals**	**Protected Characteristics**									
		Age	**Disability**	**Gender re-assignment**	**Marriage & Civil Partnership**	**Pregnancy & Maternity**	**Race**	**Religion or belief**	**Sex**	**Sexual Orientation**	**Socio-economic deprivation**
	Reduction in purchase of external foster care placements - policy proposal	√									√
	Multi-Agency Resource Group (MARG) - policy proposal	√									√
Health & Social Care	Increase Income from Charges - policy proposal	√	√	√			√		√	√	√

Treasury Management and Investment Strategy 2017/18 & Prudential Indicators

Report by Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of Report

The purpose of the report is to seek the agreement of Council to the Treasury Management and Annual Investment Strategies for 2017/18 and the Prudential and Treasury indicators contained therein.

2 Treasury Management & Investment Strategy 2017/18

2.1 Current Loan and Investment Portfolio

The Council's current loan and investment portfolio, as at 27 January 2017, is shown in tables 1 and 2 below:-

Table 1: Current Loan Portfolio as at 27 January 2017

Loan Type	Principal Outstanding £000's	Weighted Average Rate
PWLB Annuity	739	8.90%
PWLB Maturity	197,224	3.77%
LOBO	20,000	4.51%
Temporary Market Loans	36,000	0.25%
Other Loans	357	0.00%
Total Loans	**254,320**	**3.34%**

Table 2: Current Investment Portfolio as at 27 January 2017

Investment Type	Principal Outstanding £000's	Weighted Average Rate
Bank Call Accounts	0	n/a
Money Market Funds	17,941	0.30%
Bank Notice Accounts	64,985	0.85%
Total Investments	**82,926**	**0.73%**

2.2 Borrowing Requirement 2016/17 to 2021/22

The Council's capital plans contain projections of capital expenditure and income over the forthcoming financial years. Any expenditure not financed directly by income, requires funding through borrowing.

The projected borrowing requirement arising from the Council's Capital Plans, and the maturing long-term loans that require to be refinanced, over the period 2016/17 to 2021/22 is shown in table 3 below:-

Table 3: Total Borrowing Requirement over the period 2016/17 to 2021/22

	2016/17 £000's	2017/18 £000's	2018/19 £000's	2019/20 £000's	2020/21 £000's	2021/22 £000's	Total £000's
Capital Expenditure							
General Services	34,702	24,263	22,744	19,849	20,576	11,495	**133,629**
HRA	18,393	41,945	27,095	19,434	6,711	5,758	**119,336**
Total Capital Expenditure	**53,095**	**66,208**	**49,839**	**39,283**	**27,287**	**17,253**	**252,965**
Total Available Financing	-23,851	-15,608	-16,513	-17,765	-12,923	-9,960	**-96,620**
Principal Debt Repayments	-7,293	-7,927	-8,883	-9,531	-10,299	-10,863	**-54,796**
Capital Expenditure less available Financing	**21,951**	**42,673**	**24,443**	**11,987**	**4,065**	**-3,570**	**101,549**
Maturing Loans	2,090	10,271	10,452	9,131	9,142	1,394	**42,480**
Total Borrowing Requirement	**24,041**	**52,944**	**34,895**	**21,118**	**13,207**	**-2,176**	**144,029**
Borrowing secured	-20,000	-10,000	-10,000	0	0	0	-40,000
Total Remaining Borrowing Requirement	**4,041**	**42,944**	**24,895**	**21,118**	**13,207**	**-2,176**	**104,029**

2.3 Borrowing Strategy for remainder of 2016/17 and 2017/18

Long-term borrowing rates from the Debt Management Office's (DMO) Public Works Loans Board (PWLB) are currently sitting at, or close to, historical lows. Whilst the Council has already secured the majority of its borrowing requirement for financial year 2016/17, as can been noted from Table 3 above the Council has a significant borrowing requirement across the forthcoming 2 financial years (2017/18 and 2018/19).

Part of this borrowing requirement has already been secured through two forward dealt loans. This involved the Council committing to draw down two £10 million loans at fixed interest rates that were priced against historically low borrowing rates, with minimal cost of carry and allowed the Council to hedge against future borrowing rate movements, thereby representing an extremely viable alternative to traditional PWLB borrowing and adding certainty to the Council's loan portfolio. The first of these two loans is to be drawn on 29 June 2017 and the second on 15 November 2018, with these dates matched to two £10 million PWLB loans maturing on the same dates.

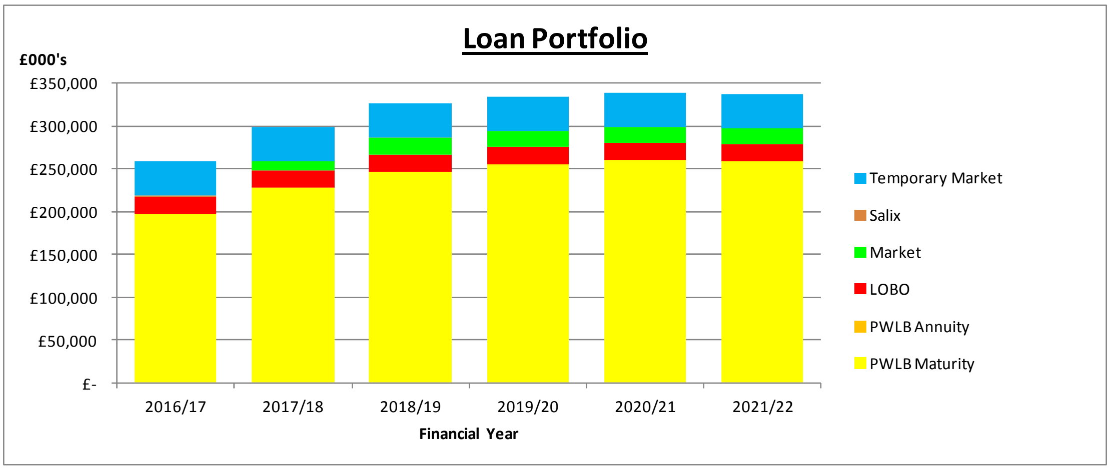
It is expected that the majority of the remaining borrowing requirement to fund capital expenditure incurred in 2017/18 and 2018/19 shall be sourced from PWLB. However, the opportunity continues to exist to consider further loans on a 'forward dealing' basis, and officers will continue to explore the viability of these loans throughout the remainder of 2016/17 and into 2017/18.

In addition to the longer-term element of the borrowing portfolio as noted above, the current low Bank of England base rate level of 0.25% and the expectation that base rate will not rise markedly in the short-medium term, means that continued utilisation of an element of temporary borrowing within the Council's overall loan portfolio (current level of £36.0 million as at 27 January 2017 at an average borrowing rate of 0.25% as shown in Table 1) would continue to provide a cost-effective solution to the Council. The quantum of this will continue to be assessed against the backdrop of potential long term costs if the opportunity is missed to take PWLB loans at historically low medium-long term rates, particularly given the projected gradual rise in PWLB rates.

Officers will ensure that any loans taken are drawn to match the existing maturity and projected capital expenditure profiles as closely as possible, that proposed interest rates continue to sit below forward interest rate projections, and that the overall borrowing remains within the Authorised Limit of £384.042 million proposed below.

Any other borrowing undertaken in advance of need would be supported by a business case which will appraise the anticipated savings in borrowing costs (from expected increases in rates later in the year / in forthcoming years) against the carrying cost associated with borrowing in advance of need.

The Council's projected loan portfolio over the period 2016/17 to 2021/22 is shown in graphical format below.



2.3 Investment Strategy

The investment environment remains challenging, with the continued scrutiny over the creditworthiness of counterparties resulting in an ever tighter counterparty list. At the same time, the low 0.25% Bank of England base rate dictates low returns of typically sub 1% for a 12 month fixed term deposit.

The position on potential investment opportunities remains broadly as reported to Council in the Treasury Management Mid-Year Update report on 08 November 2016.

£40.000 million of the Council's investments are held in fixed term deposits which mature in late March / early April 2017 and £24.985 million in bank notice accounts (with the notice period equating to broadly 6 months). Council officers, in conjunction with Capita Asset

Services will continue to review the range of investment options available to the Council, within the proposed Permitted Investments included as Appendix 1, in order to select only the most creditworthy counterparties to ensure the security of Council funds, and from that list select the range of investment products that offer best value to the Council's investment portfolio.

3 Prudential Indicators

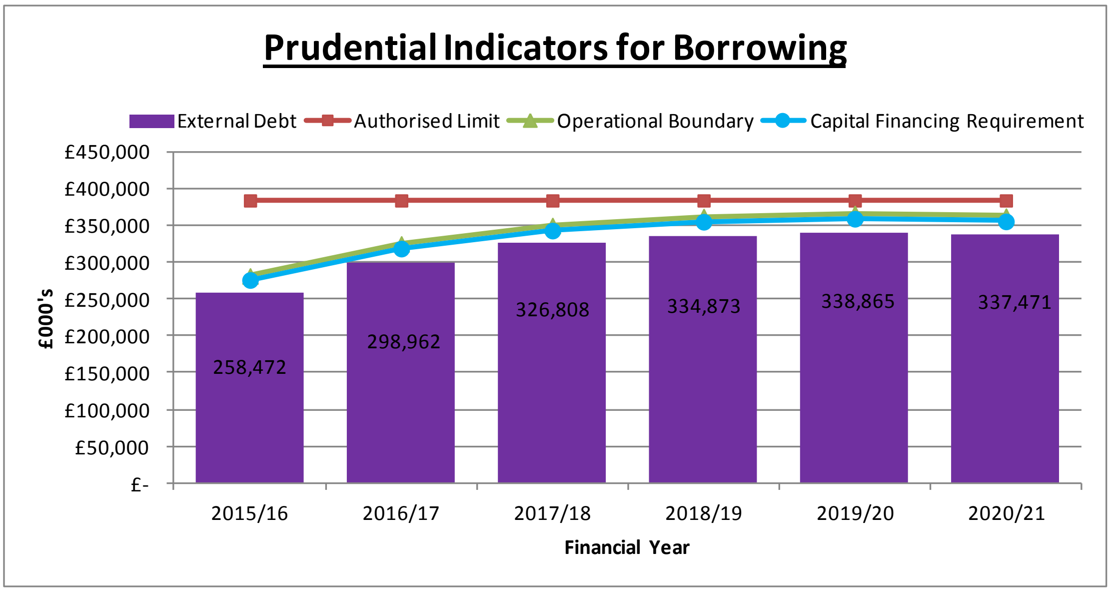
Prudential Code for Capital Finance in Local Authorities

The Prudential Code for Capital Finance in Local Authorities requires that Councils can demonstrate that their Capital Plans are affordable, prudent and sustainable, taking into account the financial provisions made in current and future revenue budgets; and that Treasury Management decisions are taken in accordance with good practice.

The Prudential Indicators that Councils need to consider relate to both actual, historic outcomes, and future estimated outcomes (covering the same period as the Council's Capital Plans), as follows:-

- Original indicators and actual outcomes for 2015/16;
- Revised estimates of the 2016/17 indicators; and
- Estimates of indicators for 2017/18 to 2021/22.

The Prudential Indicators required by the Code are listed individually in Appendix 2. The key indicators relating to external borrowing are shown in graphical format below.



The **Capital Financing Requirement (CFR)** denotes the Council's underlying need to borrow for capital purposes. The CFR includes borrowing arising as a result of the Council's Capital Plans, plus the long-term liability arising from the Council's two PPP contracts. The Underlying Borrowing Requirement strips out the latter of these (long-term liability arising from the two PPP contracts) from the CFR.

The **Authorised Limit for Borrowing** represents the limit beyond which borrowing is prohibited, and needs to be set and revised by

Members. It is the expected maximum borrowing need with some headroom for unexpected movements.

The Authorised Limit for Borrowing has been calculated by taking the maximum value of the CFR over the next 5 financial years (2017/18 to 2021/22), with the total forecast level of capital receipts and developer contributions added back to this figure (given the inherent uncertainty regarding the timing and value of these receipts/contributions). This is shown in table 4 below.

Table 4: Authorised Limit for Borrowing: Calculation

Authorised Limit	**Amount £000's**
CFR – General Services (31 March 2021)	128,063
CFR – HRA (31 March 2021)	231,089
Unrealised Capital Receipts & Developer Contributions 2016/17	10,105
Forecast level of Capital Receipts & Developer Contributions 2017/18 to 2021/22	14,785
Proposed Authorised Limit	**384,042**

Council is therefore asked to approve an adjustment to the authorised limit for borrowing to £384.042million, if market conditions support this action. This would have the effect of securing lower costs for future years but care would be taken to ensure that the cost of carry from borrowing early is minimized and that the maturity structure of all debt is sufficiently robust to ensure that the CFR at 31 March 2022 remains achievable.

The authorised limit therefore reflects a level of borrowing which, while not desired, could be afforded but is not sustainable.

Statutory repayment of loans fund advances

Under Finance Circular 7/2016, Council is now required to set out its policy for the statutory repayment of loans fund advances prior to the start of each financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years.

A variety of options are provided to Councils so long as a prudent provision is made each year. The Council is recommended to approve the following policy on the repayment of loans fund advances:-

- For loans fund advances made before 1 April 2016, the policy will be to maintain the practice of previous years and apply what is termed "the Statutory Method", with all loans fund advances being repaid by the annuity method.
- For loans fund advances made after 1 April 2016, the policy for the repayment of loans advances is proposed to continue to operate under the "Statutory Method" – i.e. loans fund

advances will be repaid by the annuity method. This annuity rate that is proposed to be applied to the loans fund repayments is based on historic interest rates and is currently 3.20%.

Under current legislation, the Statutory Method i.e. the annuity approach can be applied up to and including 31 March 2021, at which point consideration will need to be given to a number of alternative methods, with the broad aim to ensure that repayment periods are 'reasonably commensurate with the period and pattern of the benefits provided to the community from capital expenditure'. Officers will review the impact of this on loan charges from 31 March 2021 and report back to Council in due course.

4. Report Implications

4.1 Resources

There are no direct resource implications arising from this report.

4.2 Risk

The strategies outlined in this report are designed to improve the overall risk management of Treasury activity. Providing the limits outlined in the strategies are observed they will enhance the controls already in place in the Treasury Management Practices within which the treasury function operates.

The Prudential Indicators contained in Appendix 2 improve the overall risk management of Capital Investment and Treasury Management.

4.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☐ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☐ Sustainable growth
☐ Business transformation and Best Value
☒ None of the above

4.4 Impact on Performance and Outcomes

The strategies to be adopted are an integral part of the corporate aim to achieve Best Value as they seek to minimise the cost of borrowing by exercising prudent debt management and investment. This in turn helps to ensure that the Council's capital expenditure is sustainable in revenue terms.

4.5 Adopting a Preventative Approach

The proposals in this report do not directly impact on the adoption of a preventative approach.

4.6 Involving Communities and Other Stakeholders

Although no external consultation has taken place, cognisance has been taken of professional advice obtained from Capita Asset Services, the Council's appointed Treasury Consultants.

4.7 Ensuring Equalities

There are no equality issues arising from this report.

4.8 Supporting Sustainable Development

There are no sustainability issues arising from this report.

4.9 Digital Issues

There are no IT issues arising from this report.

5 Summary

The Treasury Management and Investment Strategies outlined in this document, and in the detailed document that has been placed in the Member's Library / uploaded to the Council's Committee Management System, have been formulated to comply with the revised Codes of Practice and relevant Regulations and provide the framework for achieving best value in the management of the Council's borrowing and investment portfolios.

6 Recommendations

It is recommended that the Council

a) Approve the Treasury Management and Investment Strategy for the 2017/18 financial year, as detailed in Section 2 of this report;
b) Approve the list of Permitted Investments outlined in Appendix 1;
c) Adopt the Prudential Indicators contained in Appendix 2 of this report;
d) Approve an adjustment to the Authorised Limit for Borrowing to £384.042 million (as shown in Section 3) if market conditions indicate that this is prudent;
e) Note that the policy to repay loans fund advances made before 1 April 2016 will be to continue to use the 'Statutory annuity method';
f) Approve the policy for the statutory repayment of loans fund advances made from 1 April 2016 to be the 'Statutory annuity method' and that the current annuity rate applied is 3.20%.

Date:- 31 January 2017

Report Contact:-
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Background Papers:-

Appendix 1:- Permitted Investments
Appendix 2:- Prudential Indicators
Appendix 3:- Treasury Management & Annual Investment Strategy Statement – 2017/18 Detailed – placed in Member's Lounge / uploaded to Committee Management System

Permitted Investments Appendix 1

The Council uses the Capita creditworthiness service. This utilises credit ratings from the three main credit rating agencies – Fitch, Moody's and Standard & Poors, along with credit watches, outlooks, CDS spreads and country sovereign ratings in a weighted scoring system with an end product of a series of colour coded bands which indicate the relative creditworthiness of counterparties for investment.

These colour codes are used by the Council to determine the maximum suggested duration for investment with that counterparty. These are as follows:-

Capita Colour Code	Maximum Suggested Duration for Investment
Yellow	6 years*
Dark Pink	6 years**
Light Pink	6 years**
Purple	3 years
Blue	2 years***
Orange	2 years
Red	8 months
Green	120 days
No colour	Not to be used

* *Note the yellow colour category is for:- UK Government Debt, or its equivalent, constant NAV Money Market Funds (MMF's), and collateralised deposits where the collateral is UK Government Debt*

** *Dark Pink for Enhanced MMF's with a credit score of 1.25; Light Pink for Enhanced MMF's with a credit score of 1.5*

*** *Only applies to nationalised or semi-nationalised UK banks*

**** *The Green Limit was formerly for 3 months but the Financial Conduct Authority set (in July 2013) a requirement for qualifying deposits for bank liquidity buffers of a minimum of 95 days so the Green Limit has been slightly extended to accommodate this regulatory change*

Note that the maximum suggested durations listed above have been extended by 1 year (when compared to the suggested maximum durations provided by Capita) for the Yellow, Dark Pink, Light Pink, Purple, Blue and Orange categories, to allow flexibility around these durations on the margins e.g. the placement of a 13 month fixed term deposit for a counterparty rated Orange or Blue. Equally, the maximum suggested duration for the Red category has been extended by a month to 8 months, and the maximum duration for the Green category has been extended by 20 days to 120 days, on the same basis. A thorough appraisal of the additional risk involved in extending the duration of any deposit (marginally) beyond the maximum suggested by Capita, against any enhanced value to the portfolio, will be undertaken prior to the placement of any deposit.

1.1 Deposits

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
Debt Management Agency Deposit Facility	--	Term	No	**100%**	**6 months**
Term deposits – local authorities	--	Term	No	**100%**	**2 years**
Call accounts – banks and building societies	Green	Instant	No	**100%**	**1 day**
Term deposits / Notice Accounts – banks and building societies	Yellow Purple Blue Orange Red Green No Colour	Term	No	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 8 mths** **Up to 120 days** **Not for use**
Fixed term deposits with variable rate and variable maturities: - Structured deposits	Yellow Purple Blue Orange Red Green No Colour	Term	No	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 8 mths** **Up to 120 days** **Not for use**

1.2 Deposits with counterparties currently in receipt of government support / ownership

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
UK nationalised banks – Call accounts	Blue	Instant	No	**100%**	**1 day**
UK nationalised banks – Term Deposits / Notice Accounts	Blue	Term	No	**100%**	**2 years**
UK nationalised banks – Fixed term deposits with variable rate and variable maturities: - Structured deposits	Blue	Term	No	**100%**	**2 years**
Non-UK(high sovereign rated country) nationalised banks – Call accounts	Green	Instant	No	**100%**	**1 day**
Non-UK (high sovereign rated country) nationalised banks:- Term Deposits / Notice Accounts	Yellow Purple Blue Orange Red Green No Colour	Term	No	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 8 mths** **Up to 120 days** **Not for use**
Non-UK (high sovereign rated country) nationalised banks:- Fixed term deposits with variable rate and variable maturities: - Structured deposits	Yellow Purple Blue Orange Red Green No Colour	Term	No	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 8 mths** **Up to 120 days** **Not for use**

If forward deposits are made, the forward period plus the deal period equate to the maximum maturity period.

1.3 Collective investment schemes structured as Open Ended Investment Companies (OEICs)

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
Government Liquidity Funds	AAA	Instant	No	**100%**	**1 day**
Money Market Funds	AAA	Instant	No	**100%**	**1 day**
Enhanced Money Market / Cash Funds with a credit score of 1.25	AAA	T+1 to T+5	Yes	**100%**	**1 day**
Enhanced Money Market / Cash Funds with a credit score of 1.5	AAA	T+1 to T+5	Yes	**100%**	**1 week**
Bond Funds	AAA	T+2 or longer	Yes	**50%**	**2 days**
Gilt Funds	AAA	T+2 or longer	Yes	**50%**	**2 days**

1.4 Securities issued or guaranteed by governments

Investment Category	* Minimum Credit Criteria	Liquidity risk	Market risk	Max %?£m of total investments	Max. maturity period
Treasury Bills	UK sovereign rating	Sale T+1	Yes	**100%**	**50 years**
UK Government Gilts	UK sovereign rating	Sale T+1	Yes	**100%**	**50 years**
Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government e.g. National Rail	UK sovereign rating	Sale T+3	Yes	**100%**	**50 years**
Sovereign bond issues (other than the UK govt)	AAA (or state your criteria if different)	Sale T+1	Yes	**100%**	**50 years**
Bonds issued by multilateral development banks	AAA (or state your criteria if different)	Sale T+1	Yes	**10)%**	**50 years**

1.5 Securities issued by corporate organisations

Investment Category	* Minimum Credit Criteria	Liquidity risk	Market risk	Max % of total investments	Max. maturity period
Certificates of deposit issued by banks and building societies	Yellow Purple Blue Orange Red Green No Colour	Sale T+1	Yes	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 7 mths** **Up to 100 days** **Not for use**
Commercial paper other	Yellow Purple Blue Orange Red Green No Colour	Sale T+0	Yes	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 7 mths** **Up to 100 days** **Not for use**
Floating rate notes	Yellow Purple Blue Orange Red Green No Colour	Sale T+0	Yes	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 7 mths** **Up to 100 days** **Not for use**
Corporate Bonds other	Yellow Purple Blue Orange Red Green No Colour	Sale T+3	Yes	**100%**	**Up to 6 yrs** **Up to 3 yrs** **Up to 2 yrs** **Up to 2 yrs** **Up to 7 mths** **Up to 100 days** **Not for use**

1.6 Other

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
Local authority mortgage guarantee scheme.	Blue	Term	No	**50%**	**5 years**
Loans to Third Parties	n/a	Term	No	**£25m**	**20 years**
Subordinated Debt Subscription to Newbattle Centre SPV	n/a	Term	No	**£1m**	**27 years**
Property Funds	n/a	T+4	Yes	**50%**	**15 years**

Prudential Indicators Appendix 2

1. Prudential Indicators for Affordability

1.1 Estimates of Ratio of Financing Costs to Net Revenue Stream

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Ratio of Financing Costs to Net Revenue Stream								
%	2015/16	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	Original	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
General Services	**3.86%**	**3.69%**	3.57%	3.86%	3.86%	3.71%	3.70%	3.74%
HRA	**36.37%**	**35.00%**	34.35%	35.40%	38.16%	39.00%	41.57%	42.23%

1.2 Estimates of the Incremental Impact of Investment Decisions on Council Tax and Rents

This indicator shows the change in Council Tax and Rents necessary to support increased spending on the capital account year on year. This is achieved by taking the difference between:-

- the capital plans used to calculate last years' prudential indicators; and
- the current capital plans.

The loan charges on that difference are then expressed as the change to Council Tax or Rents which would be necessary to support those charges.

Incremental Impact of Capital Investment Decisions on Council Tax and Housing Rent Levels								
	2015/16	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	Original	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
General Services	**£ 7.95**	**£ (1.53)**	£ (2.07)	£ 2.86	£ 3.81	£ 3.25	£ 1.58	£ 4.49
HRA	**£ 0.32**	**£ (0.08)**	£ (1.61)	£ (1.72)	£ 2.98	£ 2.06	£ 0.97	£ 0.21

The figures in 1.1 and 1.2 above are based on the latest Capital Plans presented to Council.

1.3 HRA Ratios

The following indicator identifies the ratio of overall debt on the HRA account compared to annual house rent revenue.

HRA Debt as a % of Gross Revenue							
	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
HRA debt £000's	£ 154,065	£ 159,097	£ 195,708	£ 217,586	£ 231,054	£ 231,074	£ 229,648
HRA revenues £000's	£ 23,257	£ 24,882	£ 26,712	£ 28,644	£ 30,700	£ 31,083	£ 31,789
Ratio of debt to revenues %	662%	639%	733%	760%	753%	743%	722%

The following indicator identifies the ratio of overall debt on the HRA account per HRA dwelling.

HRA Debt per Dwelling							
	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
HRA debt £000's	£ 154,065	£ 159,097	£ 195,708	£ 217,586	£ 231,054	£ 231,074	£ 229,648
Number of HRA dwellings	6,833	6,864	6,992	7,179	7,301	7,304	7,307
Debt per dwelling £	£ 22,547	£ 23,178	£ 27,990	£ 30,309	£ 31,647	£ 31,637	£ 31,428

2. Prudential Indicators for Capital Expenditure

2.1 Estimated Capital Expenditure

This indicator shows the gross capital spend included in the relevant capital plans.

Capital Expenditure	2015/16 Actual £000's	2016/17 Estimate £000's	2017/18 Estimate £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's
General Services							
Resources	£ 7,941	£ 11,073	£ 7,871	£ 13,159	£ 12,143	£ 17,807	£ 10,116
Education, Community & Economy	£ 9,772	£ 23,293	£ 15,820	£ 5,535	£ 1,556	£ 519	£ 519
Health & Social Care	£ 85	£ 127	£ 452	£ 150	£ 150	£ 150	£ 203
Business Transformation	£ 1,074	£ 208	£ 120	£ 3,900	£ 6,000	£ 2,100	£ -
Unallocated		£ -	£ -	£ -	£ -	£ -	£ 657
Total General Services	**£ 18,872**	**£ 34,701**	**£ 24,263**	**£ 22,744**	**£ 19,849**	**£ 20,576**	**£ 11,495**
Total HRA	**£ 12,859**	**£ 18,393**	**£ 41,945**	**£ 27,095**	**£ 19,434**	**£ 6,711**	**£ 5,758**
Combined Total	**£ 31,731**	**£ 53,094**	**£ 66,208**	**£ 49,839**	**£ 39,283**	**£ 27,287**	**£ 17,253**

2.2 Financing of Capital Expenditure

This indicator shows how the Capital Expenditure forecasts are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital Expenditure and Available Financing	2015/16 Actual £000's	2016/17 Estimate £000's	2017/18 Estimate £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's
Capital Expenditure							
General Services	£18,872	£34,701	£ 24,263	£22,744	£19,849	£20,576	£11,495
HRA	£12,859	£18,393	£ 41,945	£27,095	£19,434	£ 6,711	£ 5,758
Total	**£31,731**	**£53,094**	**£ 66,208**	**£49,839**	**£39,283**	**£27,287**	**£17,253**
Financed by:							
Capital receipts	£ 1,843	£ 5,232	£ -	£ -	£ -	£ -	£ -
Capital grants	£11,481	£11,735	£ 9,022	£ 9,523	£ 9,523	£ 8,641	£ 8,641
Capital reserves	£ -	£ -	£ -	£ 3,900	£ 6,000	£ 2,100	£ -
Developer/Other Contributions	£11,089	£ 6,884	£ 6,586	£ 3,090	£ 2,242	£ 2,182	£ 1,319
Net financing need for the year	**£ 7,318**	**£29,243**	**£ 50,600**	**£33,326**	**£21,518**	**£14,364**	**£ 7,293**

2.3 Estimated Capital Financing Requirement

This indicator measures the Council's maximum underlying need to borrow for capital purposes and other long term liabilities over the next three years.

Capital Financing Requirement (CFR)	2015/16 Actual £000's	2016/17 Estimate £000's	2017/18 Estimate £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's
Capital Financing Requirement							
CFR – General Services	£ 99,959	£ 116,877	£ 122,939	£ 125,503	£ 124,020	£ 128,063	£ 125,919
CFR – HRA	£ 154,065	£ 159,097	£ 195,708	£ 217,588	£ 231,058	£ 231,089	£ 229,675
CFR – PFI Schemes	£ 56,180	£ 54,972	£ 53,659	£ 52,233	£ 50,683	£ 48,998	£ 47,167
Total CFR	**£ 310,204**	**£ 330,946**	**£ 372,306**	**£ 395,324**	**£ 405,761**	**£ 408,150**	**£ 402,761**
Movement in CFR	**£ (1,006)**	**£ 20,742**	**£ 41,360**	**£ 23,018**	**£ 10,437**	**£ 2,389**	**£ (5,389)**
Movement in CFR represented by							
Net financing need for the year (previous table)	£ 7,318	£ 29,243	£ 50,600	£ 33,326	£ 21,518	£ 14,364	£ 7,293
Less Scheduled Debt Amortisation	£ (7,204)	£ (7,293)	£ (7,927)	£ (8,882)	£ (9,531)	£ (10,290)	£ (10,851)
Less PFI Finance Lease Principal Payments	£ (1,120)	£ (1,208)	£ (1,313)	£ (1,426)	£ (1,550)	£ (1,685)	£ (1,831)
Movement in CFR	**£ (1,006)**	**£ 20,742**	**£ 41,360**	**£ 23,018**	**£ 10,437**	**£ 2,389**	**£ (5,389)**

3. Prudential Indicators for Prudence

3.1 Net Borrowing Requirement

This indicator shows the amount of external borrowing required to finance the current debt outstanding on capital projects.

Net Borrowing Requirement	2015/16 Actual £000's	2016/17 Estimate £000's	2017/18 Estimate £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's
External Debt							
Debt at 1 April	£ 234,706	£ 237,272	£ 258,472	£ 298,962	£ 326,808	£ 334,873	£ 338,865
Actual/Expected change in Debt	£ 2,566	£ 21,200	£ 40,490	£ 27,846	£ 8,065	£ 3,992	£ (1,394)
Other long-term liabilities (OLTL)	£ 57,300	£ 56,180	£ 54,972	£ 53,659	£ 52,233	£ 50,683	£ 48,998
Actual/Expected change in OLTL	£ (1,120)	£ (1,208)	£ (1,313)	£ (1,426)	£ (1,550)	£ (1,685)	£ (1,832)
Actual/Expected Gross Debt at 31 March	**£ 293,452**	**£ 313,444**	**£ 352,621**	**£ 379,041**	**£ 385,556**	**£ 387,863**	**£ 384,637**
The Capital Financing Requirement	**£ 310,204**	**£ 330,946**	**£ 372,306**	**£ 395,324**	**£ 405,761**	**£ 408,150**	**£ 402,761**
Under / (over) borrowing	**£ 16,752**	**£ 17,502**	**£ 19,685**	**£ 16,283**	**£ 20,205**	**£ 20,287**	**£ 18,124**
Investments							
Cash & Cash Equivalents	£ 13,355	£ 10,000	£ 10,000	£ 10,000	£ 10,000	£ 10,000	£ 10,000
Short-Term Investments	£ 54,985	£ 64,985	£ 64,985	£ 64,985	£ 64,985	£ 64,985	£ 60,000
Total Investments	**£ 68,340**	**£ 74,985**	**£ 74,985**	**£ 74,985**	**£ 74,985**	**£ 74,985**	**£ 70,000**

4. Prudential Indicators for External Debt

4.1 Operational Boundary

This is the limit beyond which external debt is not normally expected to exceed and will be the focus of day to day treasury management. Typically, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

For this Council:-

- the Operational Boundary for Borrowing has been calculated to equate directly to the value of the CFR for General Services and HRA combined, over each of the next 5 financial years (2016/17 to 2021/22); and
- the Operational Boundary for Other Long-Term Liabilities has been calculated to equate directly to the in-year CFR for Other Long-Term Liabilities, given the known contractual provisions for the repayment of debt within the Council's two PPP agreements.

Table 10: Operational Boundary

	2016/17 Estimate £000's	2017/18 Estimate £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's
Operational Boundary - Borrowing	£ 275,974	£ 318,647	£ 343,091	£ 355,078	£ 359,152	£ 355,594
Operational Boundary - Other long term liabilities	£ 54,972	£ 53,659	£ 52,233	£ 50,683	£ 48,998	£ 47,167
Total	**£ 330,946**	**£ 372,306**	**£ 395,324**	**£ 405,761**	**£ 408,150**	**£ 402,761**

Should the Operational Boundary be breached, for example as a result of a decision taken to borrow in advance (should market conditions indicate that it is prudent to do so), this will be reported to Council at the next available opportunity.

4.2 Authorised Limit of Total External Debt

This indicator sets the limit for total external debt.

In an active Treasury Management policy it is sometimes prudent to borrow in advance of need if interest rates are expected to rise.

In order to continue to service the ongoing external debt and finance the current capital programmes the Council needs to increase its external borrowing to £384.042 million by 31 March 2022. Within the Capital Plans, there are assumptions regarding capital receipts and developer contributions which when applied to the Council's capital plans reduce the Council's borrowing requirements. However, the realisation of these capital receipts and developer contributions carry inherent uncertainty around both the timing and value of each receipt/contribution, given that they are largely dependent upon economic and market activity which are outwith the Council's control. Therefore, in order to calculate the Authorised Limit for Borrowing, these capital receipts and developer contributions have been added to the Capital Financing Requirement, to give the Council flexibility to fully borrow in advance of need (if market conditions support this action) should these receipts and contributions be unable to be realised in the short term. This therefore reflects a level of borrowing which, while not desired, could be afforded but is not sustainable.

Council is therefore asked to approve that, rather than restrict borrowing to £275.974 million for 2016/17, £318.647 million for 2017/18, £343.091 million for 2018/19, £355.078 million for 2019/20, £359.152 million for 2020/21 and £355.594 million for 2021/22, that permission be granted to borrow up to the 2021/22 Authorised Limit for borrowing of £384.042 million as shown in the table below), if market conditions support this action.

Adopting this approach will secure lower costs for future years but care will be taken to ensure that the cost of carry is minimised and that the maturity structure of all debt is sufficiently robust to ensure that the Capital Financing Requirement at 31 March 2022 remains achievable.

Authorised Limit						
	2016/17 Estimate £000's	2017/18 Estimate £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's
Authorised Limit - Borrowing	£ 384,042	£ 384,042	£ 384,042	£ 384,042	£ 384,042	£ 384,042
Authorised Limit - Other long term liabilities	£ 54,972	£ 53,659	£ 52,233	£ 50,683	£ 48,998	£ 47,167
Total Debt	**£ 439,014**	**£ 437,701**	**£ 436,275**	**£ 434,725**	**£ 433,040**	**£ 431,209**

Reconciliation of calculation of Authorised Limit for borrowing:-

Reconciliation of Authorised Limit for Borrowing	
	£000's
CFR - General Services at 31 March 2021	£ 128,063
CFR - HRA at 31 March 2021	£ 231,089
Capital Receipts 2016/17 unrealised to date	£ 6,306
Capital Receipts 2017/18 to 2021/22	£ -
Developer/Other Contributions 2016/17 Unrealised to date	£ 3,799
Developer/Other Contributions 2017/18 to 2021/22	£ 14,785
Authorised Limit for Borrowing	**£ 384,042**

5. Prudential Indicators for Treasury Management

5.1 Adoption of the CIPFA Treasury Management Code of Practice

The adoption of CIPFA's *Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes* is an indication of a clear, integrated and prudent approach to Treasury Management.

5.2 Upper limits on Fixed and Variable Interest Rates

This indicator limits the amount of external debt that may be held at fixed or variable rates. These limits are proposed to be as follows:-

Upper Limits on Exposure to Fixed and Variable Interest Rates 2017/18	
Interest rate exposures	**Upper Limit**
Limits on fixed interest rates based on gross debt	100.00%
Limits on variable interest rates based on gross debt	30.00%
Limits on fixed interest rates based on investments	100.00%
Limits on variable interest rates based on investments	100.00%

5.3 Maturity Structure of Borrowing

This indicator sets the upper and lower limits of the time scales within which external debt may be held.

The Treasury Management Code of Practice now requires that LOBO's with a call date in the next 12 months are classified as short-term borrowing rather than longer-term (10 year+) borrowing.

In addition, the Code also recommends that where an authority's debt is typically very long term (i.e. for a period of greater than 10 years), that authorities should break down the period in excess of 10 years into several ranges, for example 10 to 20 years, 20 to 30 years, etc.

With the above in mind, the proposed upper and lower limits for each maturity band are shown below, with the overall aim to ensure a spreading approach to avoid a cluster of high value loans maturing/requiring refinancing within a short period of time.

Maturity Structure of Borrowing 2017/18		
Maturity structure of fixed interest rate borrowing 2017/18	**Lower**	**Upper**
Under 12 months	0.00%	50.00%
12 months to 2 years	0.00%	50.00%
2 years to 5 years	0.00%	50.00%
5 years to 10 years	0.00%	50.00%
10 years to 20 years	0.00%	50.00%
20 years to 30 years	0.00%	50.00%
30 years to 40 years	0.00%	50.00%
40 years to 50 years	0.00%	50.00%
50 years and above	0.00%	50.00%
Maturity structure of variable interest rate borrowing 2017/18	**Lower**	**Upper**
Under 12 months	0.00%	30.00%
12 months to 2 years	0.00%	30.00%
2 years to 5 years	0.00%	30.00%
5 years to 10 years	0.00%	30.00%
10 years to 20 years	0.00%	30.00%
20 years to 30 years	0.00%	30.00%
30 years to 40 years	0.00%	30.00%
40 years to 50 years	0.00%	30.00%
50 years and above	0.00%	30.00%

5.4 Total Principal Sums Invested for Periods Longer than 364 Days

This indicator relates to the total level of investments held for periods longer than 364 days.

Principal Sums Invested for > 364 Days		
Limit		£50m

The current strategy as outlined in the body of these reports is to cash-back the Council's balance sheet reserves. It is expected that the majority of this will be in the form of 12 month fixed term deposits and/or certificates of deposit. The limit for prinicipal sums invested for > 364 days has been set at £50m to give the Council flexibility to extend the duration of such deposits on the margins, to e.g. 366 days or 13/14 months. As noted in the Investment Strategy section of this report, a thorough appraisal of the additional risk involved in extending the duration of any deposit (marginally) beyond the maximum suggested by Capita, against any enhanced value to the portfolio, will be undertaken prior to the placement of any deposit.