

Minute of Meeting

Audit Committee
Monday 24 February 2025
Item No 4.1



Audit Committee

Date	Time	Venue
Monday 25 November 2024	11am	Council Chambers/Hybrid

Present:

Councillor McEwan (Chair)
Councillor McCall
Councillor Bowen

In Attendance:

Councillor Pottinger (virtual)	
Councillor Scott (virtual)	
Councillor Winchester (virtual)	
Dr Grace Vickers	Chief Executive
Kevin Anderson	Executive Director Place
Morag Barrow	Director of Health & Social Care: Midlothian HSCP Chief Officer to Midlothian IJB
David Gladwin	Chief Financial Officer and Section 95 Officer
Saty Kaur	Chief Officer Corporate Solutions
Derek Oliver	Chief Officer Place
Duncan Stainbank	Chief Internal Auditor
Michelle Strong	Education Chief Operating Officer

Gary Thomson	Senior Finance Business Partner
Alan Turpie	Legal and Governance Manager and Monitoring Officer
Patricia Fraser	Audit Scotland
Claire Gardiner	Audit Director, Audit Scotland
Lisa Young	Acting Senior Business Partner
Iina Jaara	Democratic Services Team Leader
Maria Perez	Democratic Services Officer

1. Welcome and Apologies for Absence

The Chair welcomed everyone to the meeting of the Audit Committee.

Apologies were received from Councillor Milligan.

2. Order of Business

The order of business was as detailed in the agenda.

3. Declarations of interest

No declarations of interest were intimated at this stage of the proceedings.

4. Minute of Previous Meeting

4.1 Minutes of the previous meeting held 30 September 2024 were submitted and approved as the correct record. Minutes were moved by Councillor McCall and seconded by Councillor Bowen.

4.2 The Action Log was submitted and noted.

5. Public Reports

Report No.	Report Title	Submitted by:
5.1	Annual Audit Report to Members and the Controller of Audit – year ended 31 March 2024	Audit Scotland
Outline of report and summary of discussion		
<p>The Audit Director presented the report for noting.</p> <p>Audit Scotland completed two reports on the 2023-2024 accounts, including the Independent Auditor's report and the Annual Audit Report.</p> <p>The Audit Director referred to the International Standards in Auditing (ISA) 580 letter which is required by audit standards and discussed the financial statements' audit work. The Audit Director stated that the report provides an unmodified opinion on the annual accounts and in that regard everything is satisfactory.</p>		

The purpose of the Annual Audit Report's role is to highlight significant audit matters and unadjusted errors. The Audit Director stated that there are no errors for the financial year audited.

Appendix B in the report contains the Chief Financial Officer and Section 95's letter of representation which offers assurance on the matters of fraud, liability and any non-compliance with rules and regulations. The Audit Director asked the Elected Members to confirm if this letter aligns with their understanding of fraud or non-compliance.

Elected Members thanked the Audit Director for the reports and praised the good financial management shown by the Chief Financial Officer and Section 95's team.

The Audit Director explained that the Annual Audit Report concludes Audit Scotland's involvement for the financial year 2023-2024. Audit Scotland confirmed they had complied with ethical standards and remained independent. The Audit Director highlighted the following parts in the report:

Section 1- The Audit Director confirmed Audit Scotland is issuing an unmodified opinion.

Exhibit 1 highlights a materiality increase from planning which is linked to increased gross expenditure rather than an increase in the percentages applied or the benchmark used.

Exhibit 2 points out seven significant audit matters for the Elected Members' attention. These issues or errors have been discussed with management. The first three issues relate to non-current assets, and these have been highlighted to the Finance Team and Valuer:

- Condition ratings (received post year-end) led to the Valuer making adjustment on the value of Council buildings and resulted in an adjustment of £19 million in the accounts.
- Valuation process used for Council dwellings. While Audit Scotland found no material error, they recommend the Valuer considers rent yield factor for next valuation
- Two mixed use properties in which the majority use had not been reflected in the choice of the Building Cost Information Service code. This resulted in an adjustment of £1 million.

The Audit Director also highlighted holiday pay accrual and explained that the absence rates applied had an error which was corrected resulting in a £3 million adjustment.

Exhibits 3 and 4 in the report highlight risks identified during the audit process but in all instances Audit Scotland is satisfied these risks will not result in material misstatement in the annual accounts.

Sections 2 to 5 in the report flag that appropriate and effective financial arrangements are in place, and that the Council ended the financial year with a small budget underspend of £0.1 million. The report also identified some areas in

which controls could be strengthened. These are not seen by Audit Scotland as weaknesses but as areas for improvement.

The report also highlighted reserves diminished in year, and that the Council made use of the financial flexibilities around service concessions in year which has impacted the opening balance of reserves by moving it upwards by £20 million.

In terms of financial sustainability, the Council's Medium Term Financial Strategy has identified a budget gap of £20 million. The Audit Director stated that Midlothian Council is not underestimating the risk and is taking appropriate action to address sustainability.

The Audit Director stated that there is an effective governance and performance framework in place, summarised by the Best Value Report brought to this Committee in September 2024. The Workforce Strategy recommendations made in the Best Value Report are in the process of being implemented. The Audit Director thanked the Finance Team for their hard work and cooperation during the audit process.

Elected Members expressed their satisfaction with the findings of the Audit Scotland report and thanked all those involved.

The report was moved by Councillor McCall and seconded by Councillor Bowen.

Decision

The Audit Committee approved the recommendations in the report.

Report No.	Report Title	Submitted by:
5.2	Annual Accounts for the year ended 31 March 2024	Chief Financial Officer and Section 95 Officer

Outline of report and summary of discussion

The Chief Financial Officer and Section 95 Officer presented the report for decision.

The Chief Financial Officer and Section 95 Officer noted that the draft annual accounts had been submitted to the Audit Committee on 24 June 2024 and passed to Audit Scotland. The Committee is asked to approve the audited annual accounts. It is a governance requirement for the annual accounts to be approved prior to the Chief Financial Officer and Section 95 Officer, Chief Executive and Council Leader signing them so that Audit Scotland can issue the audit certificate.

During the last 5 months Audit Scotland carried out an extensive audit and issued an unmodified opinion.

The Audit Director already addressed some areas of accounts that required adjustment which are also listed in section 3.2 of the Chief Financial Officer and Section 95's report:

- The error in the unused annual leave calculation has been amended, resulting in changes to the comprehensive income and expenditure account, increased creditor balance and increased statutory reserve for employee benefits. This is a non-cash adjustment.
- In terms of accounting for non-current assets, the draft annual accounts were prepared with information available at the time. There was an asset condition survey carried out simultaneously, and after the findings of this survey were released, the decreased value of some assets resulted on a reduction of £19.5 million pounds.
- Other adjustments have been made in the valuation methodology of mixed-use properties and housing stock discount factor but in either case these are non-cash adjustments and Council reserves were not affected.

The Chief Financial Officer and Section 95 Officer noted the challenging financial landscape and the difficulty to justify investing in additional resources. This mismatch between demand, focus, expectations of auditors and the need to provide resource allocations by Councils has been observed at a national level.

The third adjustment impacts the value of Midlothian Energy Limited, in which the Council holds a 50% share consolidated in group accounts. Again, this has not resulted in a change to reserves.

Finally, the Scottish Government changes to non-domestic rates have resulted in some adjustments to the creditor accounts. This has not impacted cash reserves. In response to feedback received from Audit Scotland and Elected Members, there have been other minor adjustments to the annual accounts.

The Chief Financial Officer and Section 95 Officer noted that Audit Scotland found the papers provided to be of good standard and that colleagues in the Council had worked well with auditors during the audit process.

The Chief Financial Officer and Section 95 Officer highlighted reserve sustainability which along with the budget gap are the main challenges noted in the report. Members were reminded that the usable reserves in March 2023 had £33 million in the Housing Revenue Account to support the Council's housebuilding program. The Capital Fund had £17 million earmarked to support capital investment. Midlothian's growth is putting pressure on this fund as new infrastructure is required. Another £4 million was earmarked for repairs and renewals as part of the Public Private Partnership (PPP) accounting regime. The General Fund had £46 million, most of which was either cross-year flexibility or to be released in the coming years to support recurring expenditure whilst longer-term sustainable change is made.

Planned utilisation of reserves leaves the Council with £9 million of non-earmarked reserves, which have decreased to £6.8 million reflecting the pressures of the current financial year. The Chief Financial Officer and Section 95 Officer warned that Council reserves are getting close to the minimum 2% figure of £4.8 million.

Elected Members asked whether retrofitting a property affects the value of the asset, and in that case whether re-evaluation is needed. The Chief Financial Officer and Section 95 Officer confirmed that investment in assets is reflected in the value of those assets.

Councillor McCall moved to approve the 2023-2024 audited annual accounts, Councillor Bowen seconded the motion.

Decision

The Audit Committee approved the audited annual accounts for the financial year ending 31 March 2024 for signature in light of the appointed auditor's report.

Report No.	Report Title	Submitted by:
5.3	Treasury Management Mid-Year review 2024/2025	Chief Financial Officer and Section 95 Officer
Outline of report and summary of discussion		
<p>The Chief Financial Officer and Section 95 Officer presented the report for noting. The report informs Elected Members of treasury management activity undertaken during the first half of 2024/2025 and the forecast activity for the second half of 2024/2025 in accordance with the Treasury Management and Annual Investment Strategy approved by Council on 27 February 2024. Elected Members are invited to comment on this report which is to be presented to Council on 17 December 2024.</p>		

Section 3 of the report provides background information on the role of the Audit Committee in treasury management.

Section 4 provides a summary of the economic environment of the first half of this financial year.

Section 5 describes the main areas of treasury activity.

The position on 31 March 2024 showed an under borrowed position of £60.9 million which had increased to £67.8 million by 30 September 2024. The Council took advantage of low interest rates in August to secure two £10 million loans for a 4-5 year period. A further £10 million was borrowed last week under the same rationale, with the additional risk mitigation that it would allow the Council not to rely on internal borrowing. Table 2 on page 184 shows information on the Council's funds on deposits showing little variation between the deposit values on 31 March and 30 September 2024.

Section 6.6.1 provides an update on economic conditions post-UK budget showing an increase in inflationary pressures and section 6.6.2 shows expected treasury activity for the second half of the financial year 2024/2025. Through effective treasury decisions the Council avoided the need to borrow during the period of high interest rates. The Chief Financial Officer and Section 95 Officer stressed the need to not overly rely on internal borrowing and added that the Finance Team will continue to explore favourable borrowing opportunities.

Section 8 shows Midlothian's performance indicators compared to other Local Authorities. Data on other Local Authorities' loan fund rate is provided for comparison and illustrates the financial benefits of the current treasury management strategy for Midlothian Council.

Elected Members congratulated the Chief Financial Officer and Section 95 Officer for their probity and efficient bookkeeping.

Councillor McCall moved to adopt the recommendations in the report, seconded by Councillor Bowen.

Decision

The Audit Committee noted the recommendations set out in the report.

Report No.	Report Title	Submitted by:
5.4	Internal Audit Work to October 2024	Chief Internal Auditor
Outline of report and summary of discussion		
<p>The Chief Internal Auditor presented the report for decision. The report informs Members of the recent work carried out by the Internal Audit Team and the findings and actions agreed by management to improve internal controls and governance arrangements.</p>		
<p>The Chief Internal Auditor highlighted that final assurance reports have been completed for Attainment Scotland Funding and Midlothian Energy Limited which show that risk management, governance and controls are reasonable. Midlothian</p>		

Energy Limited is a 50/50 joint venture established in 2020 between Vattenfall and Midlothian Council to provide low carbon heating and eventually other energy solutions. Key agreements including a shareholders' agreement and concession agreement are in place between both organisations.

The internal audit work on Midlothian Energy Limited has identified the following areas for improvement:

- Although financial extracts are provided to Midlothian Energy Limited, full management accounts as required by the shareholders agreement are not being provided.
- There is no separate risk register for approved projects approved or an overall risk register for Midlothian Energy Limited and no separate risk management policy.

The Chief Internal Auditor advised that page 215 in the report contains the Attainment Scotland Funding summary. The Attainment Scotland Funding is distributed from the Scottish Government to Local Authorities and is composed of funds from Pupil Equity, Strategic Equity and Care Experienced Young People Funding. Midlothian Council fully allocates Pupil Equity Funds to schools. The report highlights that there are processes and governance in line with Council procedures and national guidance. However, some issues were identified, and the report recommends that they are addressed, and management have agreed to complete by March 2025:

- Schools have not provided an annual audit report of the use of their school fund since the pandemic.
- Transfers from Pupil Equity Funds to schools increased significantly over the past two years and processes have not yet been established for schools to formally report on their use of the Pupil Equity Funding.
- There is no service level agreement for the use of Pupil Equity Funds for play therapy in primary school settings.
- The Care Experienced Young People Fund does not have a service level agreement for their provider of art therapy supplies

Elected Members thanked the Chief Internal Auditor for the report. Councillor McCall recommended the adoption of this report and Councillor Bowen seconded this motion.

Decision

The Audit Committee approved the recommendations set out in the report.

Report No.	Report Title	Submitted by:
5.5	Follow-Up Review of Completed Internal Audit Recommendations and Progress Update	Chief Internal Auditor
Outline of report and summary of discussion		
<p>The Chief Internal Auditor presented the report for decision. The report updates Elected Members on the results of the internal audit follow-up review including a sample check on the adequacy of new internal controls for internal audit recommendations which were marked as completed by management in the period April 2023 to March 2024. The report also updates Elected Members on the status of the implementation by management of recommendations from Internal Audit Reports.</p> <p>From a sample of 33 recommendations, 22 have been completed in a satisfactory manner, 7 have been partially completed and 4 are yet to be completed. Of the 7 partially completed recommendations 5 are low rated and the remaining 2 are medium rated, and all are to be taken to finalisation by management.</p> <p>Of the 4 not yet completed recommendations, 2 are medium rated and 2 are low rated. One of the partially completed recommendations has been confirmed as closed since the completion of this report brings the number of partially completed recommendations down to 6 which will be monitored until completion by management and internal audit within the Council.</p> <p>Appendix 1 on page 221 provides a list of recommendations which are past their target dates.</p> <p>The Chief Internal Auditor summarised that the report shows management are taking appropriate steps to implement recommendations made by the Internal Audit Report however competing priorities sometimes delays this process.</p> <p>Elected Members pointed out that Appendix 1 in the report needs to be updated as some of the action owners have left Midlothian Council. The Chief Internal Auditor advised this would be updated.</p> <p>Councillor McCall recommended the adoption of this report with the above amendment and Councillor Bowen seconded this recommendation.</p>		
Decision		
The Audit Committee accepted the recommendations set out in the report.		
Action		
Chief Internal Auditor to update Appendix 1 in report with the correct overdue action owners.		

Report No.	Report Title	Submitted by:
5.6	Audit Scotland Report: The National Fraud Initiative in Scotland 2024	Chief Internal Auditor
Outline of report and summary of discussion		
<p>The Chief Internal Auditor presented the report for noting. The report informs Elected Members of Audit Scotland’s National Fraud Initiative 2024. Midlothian Council continues to be involved in the National Fraud initiative which involved 110 public sector bodies and takes place every two years.</p> <p>The report highlights the following key findings:</p> <ul style="list-style-type: none"> • £21.5 million in fraud and payment errors across the Scottish public sector, increasing from £14.9 million in 2021. Although savings have increased from £4.5 million to £5.7 million similar to the 2018/19 savings, some of the other increases in savings and notional outcome estimates are due in part to methodology changes. • £4.5 million was saved through Council tax discounts by removing ineligible claims, £1.2 million through housing benefit overpayments and £1.5 million from preserved occupational pensions where the claimant has passed away. <p>Th Chief Internal Auditor explained that these findings were included in the Annual Fraud Report presented to the Audit Committee in June 2024. The findings showed £444,000 in fraud and payment errors from Midlothian Council which are included within National Fraud Initiative results. The Council’s Counter Fraud Team is working together with the National Fraud Initiative and further matches for the new exercise will be available in December 2024.</p> <p>Elected Members asked if it is possible to carry out recovery actions on discovering overpayment of a deceased person’s pension. The Chief Officer Corporate Solutions advised that there is a process to recover monies from a deceased person’s estate and the decision whether to carry out recovery is made on a case-by-case basis. This recovery process would not apply for pensions because these are not administered by the Council.</p> <p>Elected Members asked if artificial intelligence is used to identify fraud. The Chief Internal Auditor stated that there is continuous improvement in the data and joint working with the Department of Work and Pensions, but that there is no artificial intelligence involved in the process.</p> <p>Elected Members noted that the number of applicants taken off the housing list has increased and asked whether the Council has the correct information. The Chief Internal Auditor stated that individuals were removed after a data matching exercise. The Executive Director Place advised that the last data review process took place during the pandemic and a new review is due. They advised that matching is done based on applicants’ declarations and if any individuals are removed from the housing list this is due to their circumstances being inconsistent with this declaration.</p>		

Councillor McCall moved to adopt the recommendations in the report, and Councillor Bowen seconded this recommendation.

Decision

The Audit Committee noted the recommendations set out in the report.

6. Private Reports

No items for discussion.

7. Date of Next Meeting

The next meeting will be held on Monday 24 February 2025 at 11:00am.

The meeting ended at 11.54am.