Notice of meeting and agenda

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Audit Committee

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

Date: Tuesday, 08 December 2015

Time: 11:00

John Blair
Director of Resources

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, including publication via the internet. The Council will also comply with its statutory obligations under the Data Protection Act 1998 and the Freedom of Information (Scotland) Act 2002.

1 Welcome, introductions and apologies

1.1 Welcome and Apologies

2 Order of business

2.2 Order of Business

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

3 Declaration of interests

3.3 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

4.4 Committee Membership

To note the appointment of Michael Thomas as Independent Member of the Committee

4.5 Minutes of Meeting of 29 September 2015 - For Approval

5 Questions to the Council Leader

6 Motions

7 Reports

8 Private Reports

Further information

If you have any questions about the agenda or meeting arrangements, please contact:

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A copy of the agenda and papers for this meeting will be available for inspection prior to the meeting at the main reception, Midlothian House, Buccleuch Street, Dalkeith.

The agenda, minutes and public reports for this meeting and all main Council committees can be viewed on line by going to www.midlothian.gov.uk.

MINUTES of **MEETING** of the **MIDLOTHIAN COUNCIL AUDIT COMMITTEE** held in the Council Chambers, Midlothian House, Buccleuch Street, Dalkeith on Tuesday, 29 September 2015 at 11.00 am.

Present: - Mr. P Smaill (Independent Chair) and Councillors, Bryant, Muirhead and de Vink.

Apology for Absence: - Councillors Baxter and Milligan.

1 Declarations of Interest

There were no declarations of interest.

2 Minutes

The Minutes of Meeting of 16 June 2015 were approved.

3 Annual Report to Members and the Controller of Audit for the Financial Year ended 31 March 2015

There was submitted the Annual Report to Members and the Controller of Audit for the Financial Year ended 31 March 2015, prepared by the External Auditors, Grant Thornton. The report advised, inter alia, that the external auditors intended to issue an unqualified opinion on the financial statements for the financial year ended 31 March 2015. In addition, the report provided detailed information on Financial Management; Financial sustainability; Governance and Transparency; and Best Value and Value for money. The auditors were heard in amplification of the report.

Decision

(a) To note and approve the Annual report for their interest and to note that this would now be referred to the Council on November 2015;

(b) To note the increase in the Council's cash reserves over the year to 31 March 2015;

(c) To note that the revaluation of the Council's housing stock, had resulted in a reduction in value of £18m;

(d) To note the continued financial challenges faced by the Council for the foreseeable future; and

(e) To record their appreciation of the work undertaken by the Finance Team in assisting the Auditors in the preparation of the report.

4 Financial Statements for the year ended 31 March 2015

With reference to paragraph 4 of the Minutes of 16 June 2015, there was submitted (a) the Midlothian Council Audited Financial Statements for 2014/15 and (b) a draft letter of representation to the External Auditors, in respect of the Statements, prepared by the Head of Finance and Integrated Service Support.

Decision

(i) To approve the Financial statements; and

(ii) To approve the draft letter of representation.

5 Risk Management, Update for 1 April 2015 – 30 June 2015

There was submitted report, dated 16 September 2015, by the Risk Manager, providing the Committee with the 2015/16 quarter 1 update, covering the period 1 April to 30 June 2015.The report highlighted the critical and high corporate risks facing the Council, including the need to produce balanced budgets during periods of financial restraint and a predicted cumulative budget shortfall of £23.344m by 2020/21; Corporate Change and Transition; the Integration of Health and Social Care; and Risk Management Development.

Decision

(a) To note the ongoing systematic review of all Council services; and

(b) To otherwise note the report.

6 Financial Monitoring 2015/2016

There was submitted report dated 22 September 2015 by the Director, Resources, bringing to the Committee's attention reports by the Head of Finance and Integrated Service Support, which had been considered by the Council on 22 September 2015, in relation to:-

Financial Monitoring 2014/15 – General Fund Revenue;
Housing Revenue Account - Revenue Budget and Capital Plan 2014/15;
General Services Capital Plan; and
Financial Strategy 2016/17 to 2020/21.

The Council had noted and approved each of the reports.

Decision

(a) To note that the Financial strategy was predicated on anticipated levels of grant support, which had yet to be confirmed;

(b) To note the impact of pay awards and/or Central Government pay policy on the Council's revenue position;

(c) To note that "spend to save" projects continued to be considered where these could be shown to secure revenue savings;

(d) To note that a settlement from the Council's insurers in respect of the loss of Hopefield Primary School premises following a fire, was anticipated by the end of 2015; and

(e) To otherwise note the reports.

7 Annual Governance Statement

With reference to paragraph of the Minutes of 5 may 2015, there was submitted report, dated 16 September 2015, by the Chief Executive, advising the Committee of a small number of additions to the Annual Governance Statement recommended by the Council's External Auditors, Grant Thornton. The report therefore incorporated a final draft of the Governance Statement which contained the recommended changes.

Decision

To approve, subject to any final changes, the draft Annual Governance Statement as shown in the Appendix hereto.

8 2013/14 Assessment of the Council's Public Performance Reporting

There was submitted report by the Chief Executive, updating the Committee on Audit Scotland's assessment of the Council's Public Performance Reporting (PPR) for 2013/14. The report advised that Audit Scotland placed Midlothian in the top quartile of all Councils in respect of public performance reporting. There remained five areas for improvement , viz:-

- Employees
- Procurement
- Effective use of customer satisfaction information
- Dialogue with the public
- Accessibility

The report therefore incorporated an improvement plan to address the areas for improvement.

Decision

To note the report and approve the associated improvement plan.

(Action: Business Transformation Manager)

9 Audit Scotland Report: Borrowing and Treasury Management in Councils

There was submitted report, dated 8 September 2015, by the Head of Finance and Integrated Service Support, providing the Committee with a summary of an Audit Scotland report: 'Borrowing and treasury management in Councils' and the Council's response in relation to the report's key messages. The report highlighted that the Council complied with all the relevant Treasury

Management and Prudential Codes of Practice and regulations. However,it was important to recognise that Treasury Management decisions involved a significant level of financial risk and the proposals in Audit Scotland's report were designed to strengthen the scrutiny and governance of the Treasury Management function within the Council.

Decision

(a) To note the Audit Scotland report and its recommendations; and

(b) To note that the reporting of Treasury Management activities would be reviewed in the light of Audit Scotland's recommendations.

(Action: Head of Finance and Integrated Service Support)

10 Construction Industry Scheme

There was submitted report, dated 24 August 2015, by the Internal Audit Manager, advising that the Internal audit Unit had reviewed the controls operating over the Construction Industry Scheme following an inspection by HM Revenue and Customs (HMRC). As a result of the inspection, a suspended penalty was applied to the Council.

The review had identified some minor issues which had been addressed and had resulted in recommendations to improve the Council's performance in administering the Construction Industry Scheme, all of which were detailed in the report.

Decision

(a) To approve the recommendations for improvement as outlined in the report; and

(b) To otherwise note the report.

(Action: Heads of Property and Facilities Management and Commercial Operations/ Business Applications manager/Internal Audit Manager)

11 Exclusion of Members of the Public

In view of the nature of the business to be transacted, the Committee agreed that the public be excluded from the meeting during discussion of the undernoted item, as contained in the Addendum hereto, as there might be disclosed information as defined in paragraph 14 of Part I of Schedule 7A to the Local Government (Scotland) Act 1973:-

Internal Audit Report – Review of Controls Operating over Payroll

To note that a number of weaknesses had been identified and to approve a management action plan to address these issues.

The meeting terminated at 12.10 pm.

Appendix
(relative to paragraph 7)

Annual Governance Statement 2014-15 (AGS)

Midlothian Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards. This is to allow public funds and the assets at its disposal to be safeguarded and used efficiently and effectively in pursuit of best value.

Elected Members and senior management are responsible for the governance of the business affairs of Midlothian Council. This includes: setting the strategic direction, vision, culture and values of the Council; establishing appropriate and cost effective systems, processes and internal controls to allow the strategic objectives to be delivered.

In order to achieve this, the Council has developed a Code of Corporate Governance based on the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Society of Local Authority Chief Executives' (SOLACE) framework. The Code was reviewed and updated in 2013. The Council also has a number of officials in statutory posts who monitor governance and the supporting processes during the year. These are the Head of the Paid Service, the Monitoring Officer, the Chief Finance Officer and the Chief Social Work Officer.

Midlothian Council's financial management arrangements conform to the requirements of the CIPFA Statement on the role of the Chief Financial Officer in Local Government.
The governance elements include:
allocating responsibility for maintenance of proper financial records and accounts and for maintaining effective systems of internal control; appointing a Monitoring Officer with responsibility to ensure that the Council, its officers, and its Elected Members, maintain the highest standards of conduct; establishing a scheme of delegated powers; establishing and enforcing a code of conduct for officers; having effective scrutiny and challenge arrangements in place over officer and Council decisions; open and effective recording of Council decisions; risk management processes; whistle blowing and fraud prevention procedures and processes; providing induction and training for Elected Members and Council officers; and encouraging individuals from all sections of the community to engage with the Council.

Each year, using an assurance template, evidence is gathered relating to the governance framework and the level of compliance with the Code of Corporate Governance. This includes all 8 Heads of Service completing a self assessment. Internal Audit checks a sample of the control elements in the Code of Corporate Governance so that each is tested on a three year cycle to determine their effectiveness. Any areas for improvement that are identified through these checks are recorded in the governance improvements section of the AGS below. Furthermore, the assurance elements are, where necessary, discussed with senior management.

The statement has also been informed by the work undertaken by Internal Audit who **following the requirements of the Local Authority Accounts (Scotland) Regulations 2014 conducted an annual review of the effectiveness of the Council's system of internal control. The Internal Audit Manager concluded that based on the work undertaken in 2014/15 by the Internal Audit Section that overall, internal controls had been implemented and were being monitored by management in line with**

Financial Directives, Council Policies and the other key essentials of a robust Internal Control Environment.

The results from these reviews were presented to the May 2015 Audit Committee of the Council along with Annual Governance Statement for approval.

A number of governance improvements were highlighted in the 2013-14 self assessment and progress has been made in 2014-15 on the following:

- having a positive impact on the key priorities of economic recovery and business growth; positive destinations for young people; and early years – getting it right for every Midlothian child;

This action is ongoing with performance monitored through the quarterly performance reports submitted to Cabinet and the Performance and Scrutiny Committee. There has been significant improvement in the Council's positive destinations performance indicator in 2014/15.

- embedding the new management structure and ensuring that appropriate controls and segregations are maintained;

The new management structure was approved by Midlothian Council on 13 May 2014 and implemented by 1 July 2014. Procedures are in place to ensure appropriate controls and segregations are maintained.

- the delivery of the approved financial strategy and mechanisms to ensure that the necessary financial savings are achieved and more efficient processes are introduced at reduced cost;

This action is ongoing and updates are provided through regular reports to Council. Delivering financial sustainability will continue to be a challenge over the coming years.

- continued development of risk management processes by aligning risk assessments with service planning and mitigation of risks associated with delivering the Council's outcomes;

A revised approach to risk management was approved in February 2014. This new approach is being implemented and will continue to be monitored.

- procurement reform arising from the Procurement Reform Bill and new EU Directives;

This action is to be incorporated into the Procurement Improvement Plan and progress will continue to be monitored.

continued compliance with the Public Services Network code of connection requirements;

The 2015/16 PSN Code of Connection has been submitted to the Cabinet Office on 2 April 2015 for approval. Following a positive independent IT Health Check and review of PSN required controls, it is likely that the Council will maintain ongoing PSN compliance.

- responding to the impact of further Welfare Reform changes;

This action is underway but not fully completed.

- the Health and Social Care Integration agenda with the continued establishment of joint services;

The Midlothian Integration Scheme was approved by the Scottish Government on 27 June 2015 and has now been legally constituted with the first Board meeting of

the Integrated Joint Board being held on 20 August 2015. Work is underway to develop a Strategic Plan for Health and Social Care in Midlothian and to determine the financial resources required to support the plan going forward with agreed budgets to be allocated to the Integrated Joint Board by April 2016. Following approval of the Strategic Plan in December 2015 by the Integrated Joint Board it will issue directions to the NHS Lothian and Midlothian Council regarding the delivery of services in 2016-17. The Integrated Joint Board is in the process of developing Financial Regulations and establishing an Audit Committee and reports will continue to be presented to Midlothian Council and the Midlothian Audit Committee on the financial assurance process being undertaken by Management and the reviews of the financial assurance process by the Internal Audit Section of Midlothian Council.

- Safer Communities Board provides the local scrutiny and accountability for Police and Fire & Rescue services in Midlothian as well as the wider strategic role from the Police and Fire Reform (Scotland) Act 2012.

Training workshops have been held during the year with Safer Communities Board and partnership representatives from across the Community Safety and Community Planning partnership who attended on the separate topics of Scrutiny and Challenge, another on reducing reoffending issues and the proposal that the remit of the Community Safety Partnership be adapted to incorporate the new Midlothian Reducing Reoffending Partnership, and a workshop discussion covered Midlothian Policing issues, including a proposed new structure for Policing in Midlothian.

There will be a continuation of training opportunities already provided to the members of the Safer Communities Board, including those participants in the agenda for safeguarding in Midlothian.

Those actions which are underway but which have not yet been fully concluded (ie the Business Transformation Programme; Welfare Reform; Health and Social Care Integration; and Risk Management) will continue to be progressed in 2015/16.

The following areas of improvement have also been identified and are to be progressed in 2015 -16:

- updating the Code of Corporate Governance to allow full compliance with the new International Framework of Good Governance in the Public Sector;
- updating the Council's approach to fraud and corruption to allow full compliance against the new CIPFA code of practice on Managing the Risk of Fraud and Corruption;
- to adopt the recommendations made by Internal Audit on the areas where weaknesses in control have been identified during the year (including Transformation, and Petty Cash); and
- to review any implications of the operation of the Data Protection Act within the Council and to monitor on-going compliance.

The Council has been dealing since September 2013 with a major incident involving gas penetration of carbon dioxide into recently built Council housing stock at Newbyres Crescent, Gorebridge. The Council has worked with various partner bodies in both the public and private sectors throughout this period.

The following actions have been taken or are ongoing to protect the Council's position. In order to protect public health, the tenants of all properties in the

development have been decanted and provided with suitable alternative accommodation.

Following advice from geotechnical engineers, the Council has agreed to demolish and rebuild the properties incorporating appropriate gas protection measures. This action is ongoing.

The Council has instructed a joint report from technical consultants, Fairhursts, and legal advisers, Shepherd and Wedderburn, into potential legal liability emanating from the contractual arrangements and common law duties. The Council is now acting on the basis of their recommendations.

On the basis of the Council's assurance system, and the elements of governance at its disposal, we are satisfied that overall, Midlothian Council's systems of internal control, risk management and governance arrangements are of a satisfactory standard. We are aware of areas where improvements are required and steps will be taken in the forthcoming year to address these areas, allowing the Council to advance its corporate governance arrangements and seek continuous improvement.
Signed:

Leader of the Council / Chief Executive

Midlothian

Audit Committee

Tuesday 8th December 2015

Item No .6

Audit Scotland National Review of Community Planning
Report by Alasdair Mathers, Community Planning & Performance Manager

1 Purpose of Report

This report provides a summary of the results of the national review of Community Planning undertaken by Audit Scotland in 2014, providing a commentary on the Midlothian position relative to each recommendation with recommendations for further action.

2 Background

2.1 Since the publication of the Statement of Ambition by Scottish Government in 2013, Audit Scotland considers that there has been a strong sense of renewed energy nationally and locally to improving Community Planning. In their view Community Planning continues to become more of a shared enterprise, with more active participation by partners and evidence of more shared ownership of the priorities in Single Outcome Agreements (SOAs). However, in their view although many aspects of Community Planning are improving, leadership, scrutiny, and challenge are still inconsistent.

2.2 Audit Scotland comments firstly on the role of the Scottish Government and the National Community Planning Group (NCPG). The report indicated that the NCPG has taken steps to promote the importance of Community Planning across government and in partner organisations. Audit Scotland considered that the NCPG needed to set out what the refocused approach to Community Planning means for the Statement of Ambition, its expectation of CPPs, and how success in implementing these principles will be assessed. Alongside that, it comments that the Scottish Government needs to demonstrate a more systematic approach to implementing its outcomes approach by clarifying the links between longer-term outcomes, its priorities, and performance measures across all policy areas.

2.3 Turning to CPPs, Audit Scotland concludes that many CPPs were still not clear about what they are expected to achieve, and the added value that can be brought through working in partnership. Although SOAs have improved since their introduction by Scottish Government, Audit Scotland considered that many still do not set out the specific improvements CPPs are aiming to achieve. They also consider that many CPPs lack a focus on how Community Planning will improve outcomes for specific communities, and reduce the gap in outcomes between the most and least deprived groups in Scotland. This reflects a wider ambiguity both nationally and locally about the extent to which the focus of Community Planning should be on local needs or about delivering national priorities. Audit Scotland considers that CPPs need to improve their use of local data to help set relevant, targeted priorities for improvement that will address inequalities within specific communities.

2.4 Audit Scotland goes on to note that CPPs are starting to better understand what resources they have available to deliver their SOA. They have begun to identify how partners use their resources, such as money and staff, in particular priority areas or specific communities. But Audit Scotland considered that discussions about targeting these resources at their priorities and shifting them towards preventative activity were still in the early stages. CPPs did not know what a strategic approach to prevention would look like, and in many areas the evidence base for this was underdeveloped. The current pace and scale of activity was contributing to an improved focus on prevention but was, in Audit Scotland's view, unlikely to deliver the radical change in the design and delivery of public services called for by the Christie Commission.

2.5 Audit Scotland considered that there was no coherent national framework for assessing the performance and pace of improvement of CPPs. In their view this meant that there was no overall picture of how individual CPPs are performing, and what progress was being made towards the effective implementation of the Scottish Government's Statement of Ambition. The Scottish Government was starting to use existing performance management and accountability arrangements to monitor the contribution of public bodies to Community Planning. But was not yet consistently holding central government bodies or the NHS to account for their performance within CPPs.

2.6 The Statement of Ambition placed Community Planning at the core of public service reform, but many CPPs were, in Audit Scotland's view, not clear about what their specific role in these reform programmes should be. While some CPPs had a good overview of public service reform in their area, CPP oversight of and engagement with some important aspects of reform, such as the integration of health and social care services, and national reform programmes such as the Early Years Collaborative, remained underdeveloped. Scottish Government guidance was not clear enough about the specific role that CPPs should play in the implementation of public service reforms.

2.7 Audit Scotland made specific recommendations for CPPs:

- strengthen the effectiveness of the leadership, challenge, and scrutiny role at CPP Board level
- streamline local partnership working arrangements and ensure they are aligned with local improvement priorities
- ensure that local Community Planning arrangements are clear about who is responsible for:
- agreeing the priorities of the CPP and SOA
- allocating resources and coordinating activity
- implementing activity
- scrutinising performance and holding partners and others to account for their performance
- work with the new health and social care integration joint boards to develop services that meet the needs of local people and support SOA priorities
- set clearer improvement priorities focused on how they will add most value as a partnership, when updating their SOA
- use local data on the differing needs of their communities to set relevant, targeted priorities for improvement
- start to align and shift partners' resources toward agreed prevention and improvement priorities.

2.8 Progress by Midlothian CPP

The CPP has established a good reputation, as evidenced by feedback from a variety of external partners for effective data gathering and evidence based planning, and for engagement with stakeholders and the communities of Midlothian. The Strategic Assessment process has been used as an example of good practice by Scottish Government, and the local area profiling as a basis for Neighbourhood Planning has been adopted and developed by our neighbouring council East Lothian. Partnership working in Midlothian is also well regarded and the relationships this has developed has supported the introduction of the Integrated Joint Board with few of the public difficulties reported in some other parts of Scotland. Partnership working with the Third Sector is well eastablished, and the level of third sector participation in CPP decision-making structures is also commented on by Scottish Government as good practice.

- **Strengthen the effectiveness of the leadership, challenge and scrutiny role at CPP board level.**
The Board has revised its reporting arrangements to ensure that the half yearly reports it receives now focus on progress the the top three priorities, and the areas where progress is off target. Each thematic partnership identified as owning a top priority has to report on its progress directly to the Board. Every Board meeting now also considers progress reports on the three "approaches" agreed between the partners. Board members lead the annual planning day where the results of the annual Strategic Assessment and public engagement are debated with partners and community representatives. Operational progress reporting is now addressed at the Community Planning Working group, which includes representation from each thematic group and partner agencies. This group regularly reports to the Board through the Chair who is a Board member. Annual public performance reporting is in place.

- **Streamline local partnership working arrangements and ensure they are aligned with local improvement priorities**
The Board has reduced the number of thematic partnerships, merging economy, housing and environment activities together under the title Sustainable Growth Midlothian (SGM). This provides a link between Community Planning and the Local Development planning system, a complex area operating under specific national legislation where nationally links between community and development planning require further consideration. It is also recognised that the environment strand of the CPP's work has been under-resourced to undertake engagement with communities of interest in environmental issues. This will be partly addressed by proposals for revisions to the staffing structure

in the current Council planning service review. The key priority of economic growth is led by the SGM partnership, supported by work in the Improving Opportunities Midlothian (IOM) partnership on employment, lifelong learning, and reducing inequality

IOM leads on positive post school destinations for young people, supported by the Getting it Right for Every Midlothian Child (GIRFEMC) partnership, where raising attainment and supporting children to get the best start in life are key outcomes.

GIRFEMC leads on the final priority of early years, and child poverty reduction, where the IOM group has taken a specific role in the reducing child poverty aspect, given its remit for reducing poverty. This non 'silo working' approach is supported and encouraged by the Community Planning Working Group (CPWG), whose role includes scrutiny of performance and promotion of joint working.

- **ensure that local community planning arrangements are clear about who is responsible for:**
- **agreeing the priorities of the CPP and SOA**
  In Midlothian this is the Single Midlothian Plan, agreed at the Board through the planning cycle of profiling/ Strategic Assessment/public engagement/decision making, and subsequently adopted by the Council as its corporate strategy.

- **allocating resources and coordinating activity**
  In Midlothian coordination is undertaken by the Working Group and the five thematic partnerships reporting to the Board, resource sharing is a normal part of partnership working. The Board considers allocation of additional resources for key priorities, for example the targeting of resources towards the areas of multiple deprivation.

- **implementing activity**
  Implementation is undertaken by the five thematic partnerships, by working groups reporting to them on specific action plans and by individual agencies and staff/community activists and volunteers depending on the activity.

- **scrutinising performance and holding partners and others to account for their performance**
  Accountability and scrutiny is undertaken at a variety of levels, from action planning groups and Neighbourhood Planning groups through thematic groups to the Working Group and up to the Board. The Covalent Performance Management system is used to record and track progress and performance, reporting as indicated above.

- **work with the new health and social care integration joint boards(IJB) to develop services that meet the needs of local people and support SOA priorities**
  The IJB arrangements in Midlothian have been successfully integrated into the CPP structure, with the IJB assuming oversight of the Community Planning work on adult health and care, and in turn reporting to and attending the CPP Board. A full engagement process to develop the required joint health and care plan has been completed. The new plan will be launched on time.

- **set clearer improvement priorities focused on how they will add most value as a partnership, when updating their SOA**
  The CPP will be reviewing the three year outcomes it set itself in 2013 at this year's annual planning event on 22 October. The focus of this event is the outcomes achieved through partnership working in the period 2013-15 as a precursor to agreeing new medium term outcomes (improvement priorities) for the period 2016-19.

- **Use local data on the differing needs of their communities to set relevant, targeted priorities for improvement**
  The completion of 16 Neighbourhood Planning processes over the past five years, based on local data sharing between agencies and with communities, has identified the need for more comprehensive local profiling. Profiles of Mayfield, Gorebridge, Dalkeith/Woodburn, and Penicuik have been completed and further work is underway. The CPP has established an area targeting approach to the three areas including the top 20% geographies in the Scottish Indicators of Multiple Deprivation.

- Start to align and shift partners' resources toward agreed prevention and improvement priorities.
  The CPP has set preventive intervention as one of its three priority approaches, and reports are provided regularly to the Board on activities under this approach. There is room for improvement in tracking the resources being delivered by partners, and further work is required to establish effective systems to do this.

3 Report Implications

3.1 Resource

There are no direct resource implications arising from this report; however the Community Empowerment Act now requires joint resourcing not just of delivery of Community Planning priorities, but of the facilitation of the Board and its sub groups. The Council can now open discussions with key partners to request co-financing of support of the Board, working, and thematic partnership groups.

3.2 Risk

Risk management of Community Planning is embedded in the Covalent risk register, where a number of risks have been identified and risk management arrangements put in place. The national audit report identifies significant common risks across Scotland and the CPP board is embarking on self evaluation work with the Improvement Service which will consider these.

3.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

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

3.4 Key Priorities within the Single Midlothian Plan

The Audit report covers all Community Planning themes, and makes recommendations for improvement that will impact on the Single Midlothian Plan. The new Community Empowerment legislation will require all CPPs to publish a local outcomes improvement plan. Scottish Government has indicated in advance of the statutory guidance due next year that the existing Single Midlothian Plan broadly meets the requirements of the new Act.

3.5 Impact on Performance and Outcomes

One aim of the Audit Scotland review was to increase focus on outcomes in the operation of Community Planning. The Community Empowerment Act further strengthens expectations to demonstrate impact in joint delivery with communities and across partners.

3.6 Adopting a Preventative Approach

The Single Midlothian plan prioritises preventive interventions as one of its three “approaches”, regular reports are made to the CPP Board on progress.

3.7 Involving Communities and Other Stakeholders

The Single Midlothian plan prioritises capacity building and co- production as one of its three “approaches”, regular reports are made to the CPP Board on progress.

3.8 Ensuring Equalities

The Single Midlothian plan is subject to and equality impact assessment process each year.

3.9 Supporting Sustainable Development

The Single Midlothian plan includes Sustainable Growth as one of the five thematic partnerships. The resourcing of sustainability work is part of the current service review of planning within the Council.

3.10 IT Issues

There are no IT issues

4 Summary

The Audit Scotland report made a set of observations and recommendations, which have been outlined in the body of this report, alongside the current position within Midlothian on each of these. Actions are underway to address improvements recommended and to prepare for the implementation of the Community Empowerment Act 2015, due to come into force next year.

5 Recommendations

It is recommended that Audit Committee

1. Note the contents of the Audit Scotland national report and the current assessment of the Midlothian position within this report.

Date: 20 November 2015

Report Contact:
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Background Papers:

Risk Management, Update for 1 July 2015 – 30 September 2015

Report by Chris Lawson, Risk Manager

1 Purpose of Report

The purpose of this report is to provide Audit Committee with the 2015/16 quarter 2 update, covering the period 1 July to 31 September 2015.

2 Background

CORPORATE RISKS

2.1 Audit Committee have requested regular reporting on the Council's Corporate Risks, a headline report is attached as Appendix 1 for information. The format of this report has been updated to reflect the proposed reporting format agreed by the Council's Management Team.

2.2 The headline report indicates the highest risks facing the Council at this time are:

- Balancing Budgets in future years, including the Impact of Budget Reductions and the Financial Strength of Council
- Corporate Change and Transition

2.3 CRITICAL & HIGH CORPORATE RISKS SUMMARY

2.3.1 Balancing Budgets in future years/Impact of Budget Cuts/Financial Strength of Council

The Financial Strategy to 20/21 was approved by Council on 22 September 2015. Other controls remain in place and actions associated with these are being progresses. The Grant settlement for 2016/17 is expected in late December.

2.3.2 Corporate Change and Transition

The 5 transformational strands continue to be monitored through the Programme Boards with regular updates to the Transformation Board and Steering Group. Whilst recognising that the Transformation Programme alone will not deliver the budget gap, Council previously approved the Delivering Excellence framework to respond to the outstanding financial challenge for 2017/18 and the inevitable financial and service challenges the Council will face in future years as a consequence of wider public sector reform and financial outlook.

With a focus on reshaping service delivery as the most sustainable way to address the financial and service challenges, to deliver excellence and maintain service and financial sustainability through a continuing period of public sector constraint. The framework provides a means to refocus the overall approach to service planning, priority setting and resource allocation, whilst also addressing the need to consult and engage with communities. While it is a refocus rather than a fundamentally different approach its success requires a shift in culture and thinking, requiring a more innovative and entrepreneurial approach across the Council, and therefore be underpinned by strong leadership.

2.8 Risk Management Development

2.8.1 Risk Management Group

The Risk Management Group met during Quarter 2 15/16. The focus continues to be on ensuring Service Risk Registers are updated to enable new and emerging risks to be recorded.

Updates at the meeting included a briefing from the Head of Customer & Housing Service advising on the Newbyres Crescent risk, the Carbon Dioxide risk to residents has now been eliminated with all residents being moved out of the affected homes ahead of site demolition.

2.8.2 Corporate Risk Register

In preparation for the review of the Council's Corporate risk register, the Risk Manager has sought to compare the Council's current risks with similar organisations. In seeking to do this, a recently published report published by Zurich Municipal has been utilised as it provides a good picture of the top 10 Corporate Risks facing Local Government at this time; these are as follows:

1. Budget pressure
2. Changes in government policy, legislation & regulation
3. Workforce
4. Business & organisational transformation
5. Working with other organisations
6. Reputational management
7. Social risks
8. Data protection & security
9. Operational risk management (Health & Safety)
10. Environmental challenges

Comparing the Council's Corporate Risk Register against these top 10 risks, 7 of the 10 risk currently feature within Midlothian's Corporate Risk Register. The remaining risks are identified with Service Risk registers, e.g. reputation is considered as part of the assessment process and associate risk rating, Social risk e.g. population change are being identified by services who provide frontline services, Environmental changes is included within the Commercial Operations risk register.

This comparative work will be considered by the Council's Management Team when the Corporate Register is reviewed in-line with the Council's Strategic Objectives.

2.8.3 Risk Management Framework

During this quarter the Risk Manager contributed to the Delivering Excellence program. This work has ensured the consistent use of management assessment tools such as PESTEL, SWOT and Stakeholder Analysis across Delivering Excellence and the new Risk Management Guide.

In support of the Council's Risk Management Policy the following guides have been produced:

- The Risk Management-Process Guide;
- Guide to using covalent to record Risk

The implementation of the Risk Management Guide, which will now follow, will result in changes to the way risk information is presented. At present, risks which have already been realised and future potential risk are recorded within risk registers. The implementation of the risk management guide will see issues logs created. Issues logs will record all those risks which have been realised, whether previously identified as risks or not and the measures being taken now in response.

This will enable the risk registers to become more forward looking, horizon scanning therefore identifying what may impact the organisation in the future; both positive and negative. This should enhance the Council's decision making processes, supporting the evidence based management approach.

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. It appears that the presence of risk is understood and action is being taken to manage and respond to risk on an ongoing basis.

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 the authority 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.

3.6 Involving Communities and Other Stakeholders

Consultation has taken place with Senior Managers responsible for corporate risk management.

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 Corporate Risks.

3.9 IT Issues

No additional issues other than those relating to the Risk Register.

4 Recommendations

Audit Committee is invited to:

Note the 15/16 quarter 2 report on Corporate Risks and consider the current response to the risks highlighted.

Date: 25 November 2015

Report Contact:
Chris Lawson, Risk Manager
Tel No: 3069
chris.lawson@midlothian.gov.uk

Background Papers: **Appendix 1** Corporate Risks Report Quarter 2 2015/16

Brief Headline Report on Corporate Risks

Midlothian

MC01-01 People risks

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-01	Potential sub risk areas include:- 01 - health and safety - duty of care over employees 02 - difficulties recruiting the right staff 03 - retaining quality staff 04 - low skill levels 05 - low morale, especially during change 06 - non compliance with policy and procedure 07 - ageing work force and 08 - high absence rates There is currently a further group of threats that are impacting on the Council and its employees and these are external factors: public sector pay freeze, pension reforms, industrial action, public sector reform, reduction in household incomes, reduced ability to retire, limited job opportunities	Marina Naylor	01 - Main internal controls centre on the approved People Strategy and supporting initiatives and Action Plan. 02 - HR related policies regularly reviewed 03 - Management of external factors that affect staff 04 - Significant stress awareness campaign 05 - Competency Framework 06 - Various initiatives to keep staff informed of change 07 - Absence Monitoring/Reporting. 08 - Health and Safety Risk Management/pro-action to Internal Audit recommendations/use of risk consultants for surveys/updating policies and link to PIs and day-to-day practice/specific improvements underway in driver training, down to casual users 09 - Adoption and management of a BT Project Risk Register, reviewed/updated quarterly 10 - Non-redundancy policy aimed at keeping employee base stable	1	4	✔

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01 -A01-1	Policy Review program	**Q2 15/16**: The Policy review work well underway with key policies being revised e.g. Discipline & Grievance, Attendance Management and Organisational Change.	Marina Naylor	31-Mar-2016	▶
MC01-A01-2	Health & Safety Management Arrangement Development	**Q2 15/16**: Management Arrangement development program is progressing positively with the following arrangements developed: First Aid, Incident Reporting & Investigation, Control of Substances Hazardous to Health, Personal Protective Equipment, Hand Arm Vibration, Smoke Free, Manual Handling & Display Screen Equipment.	Chris Lawson	10-Jul-2016	▶

MC01-02 Governance and Standards in Public Life

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-02	Potential 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	Internal Audit; Elaine Greaves; Alan Turpie	Potential 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	3	4	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01-A02	International Governance Standards	**Q2 15/16**: Working Group to be established to review current governance arrangements against new International Governance standard developed by CIPFA and the International Federation of Accountants.	Alan Turpie	31-Mar-2016	

MC01-04 Internal Control Environment

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-04	Potential risks include:- 01 - Fraud 02 - Waste and 03 - Error caused by inadequate internal control, residual risk and poor governance at macro and micro levels.	Internal Audit; Elaine Greaves	Potential risks include:- 01 - Fraud 02 - Waste and 03 - Error caused by inadequate internal control, residual risk and poor governance at macro and micro levels.	3	3	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01-A04	Audit	**Q2 15/16**: Audit team progressing with 2015/16 Audit Plan to test a range of internal controls as agreed ad approved by Audit Committee.		31-Mar-2016	

MC01-05 Balancing Budgets in future years/Impact of Budget Cuts/Financial Strength of Council

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-05	Potential sub risks include:- 01 - Slow realisation of savings 02 - Improvements to services cannot be financed as a result of budget cuts 03 - Poor collection performance in income streams 04 - Unforseen commitments	Gary Fairley	Potential sub risks include:- 01 - Slow realisation of savings 02 - Improvements to services cannot be financed as a result of budget cuts 03 - Poor collection performance in income streams 04 - Unforseen commitments	4	4	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01-A05-1	Finalise 2016/17 base budget	**Q2 15/16**: The Accountants are completing detailed budget review.	Gary Fairley	15-Dec-2015	
MC01-A05-2	Assess Grant announcement	**Q2 15/16**: This will follow formal announcement.	Gary Fairley	15-Jan-2016	
MC01-A05-3	Consider Savings proposals for 2016/17	**Q2 15/16**: Under consideration by Senior Management Team.	Gary Fairley	18-Dec-2015	

MC01-06 Emergency Planning and Business Continuity Management

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-06	Potential sub risks include:- 01 - Censure through non compliance with the Civil Contingencies Act 02 - Not adequately recovering from the loss of major accommodation (eg secondary school, main offices), computer systems and staff 03 - Not able to respond to a major emergency in the community 04 - 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	Linked action latest note	Assigned to	Due Date	Status
MC01-A06	Preparation for Partership Working	**Q2 15/16**: The Council Emergency Response Plan will be reviewed with a view to the future partnership working in Civil Contingencies.	Chris Lawson	31-Mar-2016	

MC01-07 Corporate Policies and Strategies

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-07	Potential sub risks could include:- 01. Policy may not be aligned to BV 02. Policies may not match aspirations or corporate direction 03. Policies may become out of date 04. Policies not monitored and non compliance exists 05. Strategy misaligned to policy; may not work		Potential sub risks could include:- 01. Policy may not be aligned to BV 02. Policies may not match aspirations or corporate direction 03. Policies may become out of date 04. Policies not monitored and non compliance exists 05. Strategy misaligned to policy; may not work	1	3	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status

MC01-08 Corporate Change and Transition

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-08	Potential sub risks include:- 01 - Delays 02 - Cost creep 03 - Slow benefits realisation and budget savings 04 - Objectives of changes not actually met 05 - Adverse impact on services 06 - Staff morale affected 07 - Government step-in	Nancy Brown	Potential sub risks include:- 01 - Delays 02 - Cost creep 03 - Slow benefits realisation and budget savings 04 - Objectives of changes not actually met 05 - Adverse impact on services 06 - Staff morale affected 07 - Government step-in	4	4	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01-A08	Delivering Excellence	**Q2 15/16**: Heads of Service have been asked by the Chief Executive to set out when their Services are planning to work through the delivering excellence framework.		31-Mar-2017	

MC01-09 Legal and Regulatory Compliance

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-09	The potential sub risks include:-1. A local authority is bound by a plethora of legislation and government regulation: and 2. Ultra vires actions could transpire	Alan Turpie	The potential sub risks include:- 1. A local authority is bound by a plethora of legislation and government regulation: and 2. Ultra vires actions could transpire	3	3	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01-A09	Information Security			31-Mar-2016	

MC01-11 Asset Condition – buildings, vehicles, computer, roads

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-11	Potential risks include insufficient budgets to make a serious impact on deterioration of assets; adverse legacy for the future.Limited funds to make a real difference. For example, in 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.	Gary Fairley	Potential risks include insufficient budgets to make a serious impact on deterioration of assets; adverse legacy for the future.Limited funds to make a real difference. For example, in 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.	3	3	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status

MC01-13 Integration of Health & Social Care

Risk Code	Risk Identification	Ownership Managed by	Risk Control Measures	Likelihood	Impact	Risk Evaluation
MC01-13	The integration of health and social care is one of the Scottish Governments' top priorities and is a key part of planning services for the future. From 20 August 2015 Midlothian Council and NHS Lothian will be working together as a Health and Social Care Partnership governed by the Midlothian Integration Joint Board (IJB). This co-ordinated approach to planning and delivering services across Midlothian aims to achieve the Partnerships vision: “People leading longer and healthier lives by getting the right advice, care, and support, in the right place, at the right time.” The successful operation of the new IJB is key to the on going delivery of adult and social care and in particular further benefits, efficiency and improvement in service through further integration being achieved. The project has been led by the Director of Health & Social Care with support from Council and NHS employees and overseen by the Business Transformation Board within the Council. There is a risk to the delivery of the stated objectives should the IJB not function effectively.	Alison White		3	4	

Related Action Code	Related Action	Linked action latest note	Assigned to	Due Date	Status
MC01-A13-1a	The purpose of Risk Management	**Q2 15/16**: A report was submitted to the IJB on Risk Management highlighting the purpose and importance of the new IJB developing a risk management policy.		31-Mar-2016	
MC01-A13-1b	The purpose of Risk Management	**Q2 15/16**: A workshop on Risk Management is being scheduled for the IJB as part of the induction process.		31-Jan-2016	
MC01-A13-2	IJB Risk Awareness	**Q2 15/16**: Midlothian Council are leading on the development of risk management reporting arrangements between the IJB, the Council and NHS Lothian.		31-Jan-2016	
MC01-A13-3	Develop an IJB risk register	**Q2 15/16**: A draft register has been prepared with input from Midlothian Council and the NHS, this will be updated with input from the IJB following the Risk Management workshop.		31-Mar-2016	

National Fraud Initiative Update 2014/15
Report by Internal Audit Manager

1. Purpose of the Report

The purpose of this report is to update the Audit Committee on the completion of the National Fraud Initiative data matching exercises for 2014/15, and the outcomes of this exercise.

2. Background

2.1 The National Fraud Initiative (NFI) in Scotland is a counter-fraud exercise led by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different financial systems, to identify circumstances (matches) that might suggest the existence of fraud or error.

2.2 Two NFI exercises took place in 2014/15:

- the main data match uploaded in October 2014 which compared a number of datasets; and
- the Council Tax to Referendum Electoral Roll data match which was uploaded in May 2015.

Initial investigation of matches was carried out by staff in the relevant services. Housing Benefit matches were reviewed by the Corporate Fraud Officers and Council Tax matches were sifted by the Corporate Fraud Officers and then referred to Revenues visiting officers for investigation.

3. Outcomes

The NFI exercises for 2014/15 have identified a total of £16,153 in overpaid benefits and discounts. The total for 2012/13 was £38,556

The overpayment totals have been declining in recent years for three reasons:

- the NFI matching process is now run on a regular basis and therefore a number of matches from previous years have already been identified and investigated;
- a movement towards real time information sharing between HM Revenues and Customs and the Department for Work and Pensions(DWP) has led to potential frauds and errors being identified at an earlier stage without the need to wait for the biennial NFI exercise; and
- potential housing benefit frauds from October 2015 are now investigated by the Single Fraud Investigation Service of the DWP. This means that Midlothian Council no longer has

responsibility for these cases and matches. Any therefore that result in recovery are excluded from the above figures.

The following table shows the matches received from the NFI in 2014/15:

Type	No of Matches 2014/15	Cleared No Issue	Errors	Referred for Fraud Investigation	Outcome
Housing Benefit	857	828	3	26	Overpayments identified £8,888 plus 26 cases referred to the DWP for further investigation.
Disabled Parking Blue Badges	120	96	24		24 Blue Badges were cancelled when the match revealed the holders were deceased.
Payroll	147	147			No issues
Residential Care Homes	28	28			No issues
Insurance Claims	13	13			No issues
Personal Budgets	33	33			No issues
Creditors	2,105	2,105			Matches were sampled and no errors were found that had not already been picked up by the controls in place and corrected. The large number of matches is as a result of the volume of creditors' information.
Biennial Exercise Subtotal	3,303	3,250	27	26	
Referendum Electoral Roll	2,770	2,737	33		Overpayments identified £7,265
Total	**6,073**	**5,987**	**60**	**26**	**£16,153**

The majority of matches were resolved by internal checking processes and only a small percentage of matches required referral for investigation.

The next data matching exercise will be comparing the electoral roll in December 2015 to council tax data extracted in November. Work on these matches will start at the beginning of 2016.

4. Report Implications

4.1 Resource

Services have directed resources towards the initial checking of matches identified in the NFI reports. There has been no requirement for additional resources.

4.2 Risk

The NFI is a control that is implemented to identify potential fraud or error. It also provides assurance that if no fraud or error is found, that existing controls are working effectively.

Ensuring that proper arrangements are in place to deal with the resulting NFI matches is critical in ensuring the Council meets its obligations and also provides assurance to Internal and External auditors.

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**
- [x] **None of the above**

4.4 Key Priorities within the Single Midlothian Plan

This report does not address the issues within the Single Midlothian Plan.

4.5 Impact on Performance and Outcomes

Participation in the NFI ensures that fraud or error can be identified as a result of data matching with information from public bodies.

4.6 Adopting a Preventative Approach

Participation in the NFI provides assurance that existing data held is free from fraud or error.

4.7 Involving Communities and Other Stakeholders

The Council’s external auditors Grant Thornton have advised Audit Scotland that they were satisfied with the Council’s arrangements for NFI.

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 invited to note the contents of this report.

Date: 30 November 2015

Report Contact:
Heather Mohieddeen Tel No 0131 271 3126
heather.mohieddeen@midlothian.gov.uk

PROGRESS UPDATE

Report by Graham Herbert, Internal Audit Manager

1. Purpose of Report

The purpose of this report is to provide members of the Audit Committee with:

- a summary of the work undertaken by Internal Audit since April 2015; and
- an update on progress with the current audit plan which was approved by the Audit Committee on 17 March 2015.

2. Detail

The Internal Audit Section has completed the following tasks since April 2015:

Task	Description	Reported to
Annual Governance Statement	Testing a total of 18 of the 54 elements of the Code of Corporate Governance to determine whether these were operating as described. Conclusions were included within the Annual Governance Statement.	Reported to the 5 May Audit Committee.
Statement on Internal Control	An opinion on the internal control environment of the Council by the Internal Audit Manager. This statement was also used to inform the Annual Governance Statement.	Reported to the 5 May Audit Committee.
Public Sector Internal Audit Standards.	Assessment of Internal Audit against the Public Sector Internal Audit Standards.	Reported to the 5 May Audit Committee.
National Fraud Initiative	An update on the results of the data matching exercise to identify circumstances	Reported to the 5 May Audit Committee and the 8 December Audit

	(matches) that might suggest the existence of fraud or error.	Committee.
Cashless Catering	Assessment of the adequacy of controls operating over the Cashless Catering system and whether these controls were consistently applied across sites.	Reported to 5 May Audit Committee.
Internal Audit Charter	Review and update of the Internal Audit Charter.	Reported to 5 May Audit Committee.
Follow up of Recommendations	A review of a sample of recommendations that have been signed off as complete to determine whether they had been implemented satisfactorily.	Reported to 16 June Audit Committee.
Assessment of the Audit Committee	Assessment of the Audit Committee against the Audit Committee Combined Code (2008) and the 2013 Chartered Institute of Public Finance Accountancy (CIPFA) document "Practical Guidance for Local Authorities-Audit Committees".	Reported to 16 June Audit Committee.
Integration of Health and Social Care	This Audit included a review of governance, the proposed allocated budget from Midlothian Council to the Integrated Joint Board, risk registers and project plans.	Reported to 16 June Audit Committee.
Construction Industry Scheme	A review of the controls operating over the Construction Industry Scheme.	Reported to 29 September Audit Committee.
Payroll	To assess the adequacy of the control environment of the Council's payroll arrangements.	Reported to 29 September Audit Committee.
Internal Audit Recommendations	Council performance in closing Internal Audit issues by the	Reported to the 8 December 2015 Audit Committee.

	expected date.	
Commercial Rents	A review of the controls operating over the renting of Council owned commercial property.	Reported to the 8 December 2015 Audit Committee.
House Rents	To review the controls operating over the House Rent System.	Reported to the 8 December 2015 Audit Committee.
Co-ordinated the submission of Audit Scotland National Reports	These are to date: • Overview of Local Government 2015; • Scotland's Public Finances; • School Education; • Procurement; • Audit Scotland borrowing Treasury Management in councils; and • Community Planning	Reported to Audit Committees during the period April to December 2015.
Investigations / consultancies	Support in 4 investigations and 2 consultancy engagements.	N/A
Help Desk	Between the periods of April 2015 to October 2015 Internal Audit has received a total of 26 help desk enquiries.	N/A

The following areas are work in progress:

Task	Description	Progress
Developer Contributions	To review the controls in place over Developer Contributions.	At reporting stage.
Devolved school budgets	To review the processes and controls designed to allow the locally Devolved School Management Scheme to be consistent with the principles laid out in national guidelines	End of field work.
Early Years	To review the provision of external nursery provision.	End of field work
Tendering of	To review the process	End of field work

Contracts	and controls over the tendering of supplier contracts and, for a sample of contracts, to review the level of compliance against the established processes.	
Public Private Partnership Agreements	To review the controls in place over the utilisation of assets held under PPP contracts to ensure best value for the Council.	Planning stage.
Self Directed Support	To review the controls operating over the Social Care (Self-Directed Support) (Scotland) Act 2013 (the Act) which allows users of social services more choice on how to access the service.	Planning stage.
Financial Strategy and Business Transformation	To review the controls designed to allow delivery of the financial strategy and to follow up on the recommendations made in the 2014/15 Business Transformation Internal Audit review.	Planning stage.
Fraud and Corruption Policy	Update of Fraud and Corruption Policy.	At draft stage.
Whistle blowing policy.	Update of Whistle blowing policy.	At draft stage.
Council tax discounts and exemptions	Reviews to identify potential fraudulent applications.	Field work stage.
Audit Committee Integrated Joint Board	Draft SLA / Audit Plan produced	At draft stage

The following Audits from the 2015/16 have not yet commenced:

Task	Description
Welfare Reform	To review the processes and controls put in place to deliver the new Universal Credit payments (which commence on a phased basis from April 2015).
Internal quality assurance of Care at	To review the quality assurance process established by the Council to monitor the

Home Providers	quality of service provided on home care by third party providers.
Purchase Cards and Petty Cash	To follow up on the Audit Report on Petty Cash (completed in March 2015) and to review the controls operating over purchase cards.
Stores	A review of the processes and controls operating over items held in stores.
Business Continuity and civil contingencies	To test the Council's approach to business continuity and the level of compliance against the Civil contingencies legislation.

Impact of the Integration Joint Board

The Joint Integrated Board for Health and Social Care at their meeting on 20 August 2015 recommended and approved that the Internal Audit Manager of Midlothian Council should also be appointed as the Chief Internal Auditor for the Integrated Joint Board. Whilst some resource was set aside for supporting the Integrated Joint Board in the 2015/16 Internal Audit Plan this was not sufficient in relation to the proposed additional allocated responsibilities. This has been estimated at an extra 65 days.

Internal Audit will endeavour to limit the impact of these added responsibilities on the Midlothian Council's Internal Audit Plan and the Audit Committee will be advised if this will lead to a reduction in the number of planned audits.

The following is a list of the additional audits that are planned to be undertaken for the Integrated Joint Board in 2015/16. This plan has not yet been submitted to and approved by the Integrated Joint Board but a paper is being presented to the Board on 10 December 2015.

Task	**Proposed Addition**
Health and Social Care Audit	A review of: • the Strategic plan and planning process; • the financial plan underpinning the strategic plan; and • a review of the financial assurance process undertaken .
Health and Social Care Audit - Planning	Development of a 2015/16 and 2016/17 Internal Audit Plan.
Health and Social Care Audit - Governance	A number of governance related tasks will need to be undertaken to support the Integrated Joint Board Audit and Risk Committee: • an annual review of the Code of Corporate Governance; • a review of 2015/16 Annual Governance Statement; • Internal Audit Managers assessment of internal control;

	• development of a service level agreement between the Integrated Joint Board, Midlothian Internal Audit Section and NHS Lothian Internal Audit Section; and • other support for the Integrated Joint Board Audit and Risk Committee (for example self assessment against best practice codes).

3. Report Implications

3.1 Resource

The Internal Audit Section currently has an experienced member of the team off on maternity leave, has recently been allocated responsibility for corporate fraud team and the management of the National Fraud Initiative and is also now to head up the Audit Service for the Integrated Joint Board.

The Internal Audit Manager will continue to monitor progress against the plan and the impact of these factors on delivery of that plan.

3.2 Risk

There is always a residual risk that investigations and consultancy could overtake risk based reviews and compliance checks on the main financial systems. This risk is being controlled through the introduction of an investigation / consultancy protocol.

Each internal audit assignment examines the control of risk and the perception of risk that the auditee has. 'Risk' is central to each internal audit report. This strengthens the Council's approach to risk management and the internal control system.

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

It is projected that there will be sufficient audits completed to allow the Internal Audit Manager to undertake an assessment of the strength of the internal controls operating within the Council.

3.5 Adopting a Preventative Approach

This report addresses the Council's policy to have a robust internal control environment, management of risk and effective governance.

3.6 Involving Communities and Other Stakeholders

The Internal Audit Plan has been discussed with the Chief Executive, the Corporate Management Team and the Audit Committee (which includes representation from External Audit).

3.7 Ensuring Equalities

For the internal audits completed to date, we found no equalities issues to report on.

3.8 Supporting Sustainable Development

Internal Audit provides an independent assurance function which assists the sustainability of the Council's internal control system, governance and management of risk.

3.9 IT Issues

There are no IT issues as a result of this report.

4. Recommendations

The Audit Committee is requested to:

(1) note the work completed by the Internal Audit Section since April 2015;
(2) note progress with the current plan; and
(3) note that the Internal Audit Manager will update the Audit Committee if there is impact on delivery of the Internal Audit Plan through additional requirements of supporting the Integrated Joint Board.

Date: November 2015
Report Contact: Graham Herbert, Internal Audit
Tel: 0131 271 3517
E-Mail: Graham.Herbert@midlothian.gov.uk

Midlothian

Internal Audit Report

Review of Controls Operating over House Rents

Issued: October 2015

Final

Level of Assurance	**Good** - The control framework is of a good standard with only minor elements of risk identified which are either accepted or being dealt with by management.

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Executive Summary

1.0 Introduction

As at 31st March 2015, the Council owned 6,834 houses and 860 garages and the rent received for 2014/15 was approximately £23.3 million. These properties, and the associated rental charges, are managed through the Capita system.

Midlothian Council continues to make significant investment in affordable housing with 940 Council owned houses being built since 2006. There is an anticipated increase in demand for affordable housing. Midlothian Council undertook a recent review (Housing Need and Demand Assessment) which projected that a total of 5,571 new affordable homes will be required in Midlothian by 2032. This will present the Council with further challenges.

The rents charged for houses are calculated using a points system based on the number of bedrooms and the type of properties. An exception to this general rule is properties used for temporary homeless accommodation which are charged at specific rents. New build properties are also charged at a 25% premium on older stock.

A rent strategy was approved by Midlothian Council in February 2011 which included agreement to increase rents by 6% each year over the period 2011/12 to 2015/16. A consultation on a rent strategy for the period 2016/17 to 2018/19 is currently taking place for an agreed approach to rent setting which will be reported to Cabinet. The average rent in Midlothian is currently £65.51 per week (including temporary homeless accommodation) for a Council House and £11.28 per week (excluding VAT) for a garage.

Rental charges may be paid by a number of methods including cash, cheque, debit or credit card (£2.50 charge for credit cards), direct debit, standing order, direct deduction from benefits, by automated telephone payment system, or through the Midlothian Council website. Payments may also be made through Paypoint/Payzone outlets (including post offices) by cash or by using a rent payment card. 48.75% of customers pay their house rents by direct debit which is the method actively encouraged by the Council. The Council is currently exploring the feasibility of customers being able to view their rent and council tax accounts online.

2.0 Objectives of the Audit

The objective of the audit was to review the adequacy of controls over the house rent system with coverage limited to billing, charging and collection (excluding arrears management).

A copy of the terms of reference for the review is attached at Appendix 2.

3.0 Conclusion

We noted a number of processes and controls that were operating effectively, these included:

- annual rent increase letters were being issued 4 weeks prior to any increase in charges;
- income collected through the cash receipting system was being accurately posted to the house rent system (Capita) and general ledger;
- the housing benefit system (Open Revenues) was being reconciled to the house rent system (Capita);
- new builds were being added to the house rent system accurately and house sales were being removed from the house rent system in a timely and accurate manner;
- the Council offers a wide choice of payment methods to tenants;
- a pending tenancy report is run on a weekly basis to ensure all properties are charged rent; and
- rent collections and other housing statistics are prepared and monitored by management on a regular basis.

A small number of issues were identified during the audit review which included:

- there were a number of credit balances on rent accounts which need to be reviewed and if appropriate refunded to customers;
- there are currently 245 Garages which have not been let for a number of months resulting in lost income to the Council;
- garage site rental charges have not been up-rated every year with the last increase dating to 2011/12;
- testing by Audit identified a small number of errors in figures provided to the Scottish Government on Housing Stock and Rent Collection;
- Discretionary Housing Payment forms did not include the Council's Data Protection Statement;
- rent levels quoted on the Council's website were historic and did not reflect the current charges; and
- testing identified 2 properties (out of 6,908) that had not been included in the automated update for rent increase. The property class code had been incorrectly updated. These 2 properties were not up-rated by 6% in 2013/14 which resulted in a minor loss of revenue.

Given that the control framework is of a good standard with only minor elements of risks identified we have rated the strength of the internal controls over the House Rent system as **Good**. We have rated the strength of the internal controls over House Rents in accordance with the table on page 8.

4.0 Audit Issues and Management Action Plan

4.1 Credit Balances

As at the 3rd March 2015, there were 675 former tenant accounts in credit with a monetary value of £59,805. 57 of these accounts exceeded £250 and 3 accounts exceeded £1,000 (one of which dated back to 2002). Management have indicated that rent statements including credit balances were sent to current tenants in April 2015 but the Council does not proactively review to refund where the customer does not make contact with the Council or is a former tenant. Management have indicated that there are resource limitations within the Arrears Section and as a consequence effort is concentrated on overdue debt recovery rather than refunding credit balances. Under the Tenancy Agreement the agreed rent is set out. Accordingly if for whatever reason there is a surplus, the Council is not entitled to that money (under the contract) and the surplus should therefore be returned.

No	Recommendation	Priority	Manager	Target Date
1	The properties identified with a credit balance should be investigated and a refund made where applicable. <u>Management Comment</u> Management are currently reviewing the number of former tenant accounts in credit and will take action on those exceeding £250. 20 of the 57 accounts have already been cleared. Rent statements for existing tenants with a credit balance will continue to be sent on an annual basis.	Medium	Revenues Manager Operations	31/12/15

4.2 Garages and Garage Sites

<u>4.2.1 Letting performance</u>

The Council owns 860 garages and approximately 500 garage sites (land leased by the Council to customers who erect their own garage) which it rents out to council housing tenants (at a cost of £587 and £52 per annum respectively) and the public generally (at an annual cost of

£704 and £52 respectively). It was noted however that there are significant numbers of these garages and garage sites which are not currently leased and therefore the Council is not obtaining income on these.

It was reported by Management that Midlothian Council, despite local advertising, has a surplus of garage and garage sites for rent; and there is limited demand due to the availability of free parking.

4.2.2 Garage sites

Rents for garage sites have not been increased since 2011/12 and are not subject to regular rent reviews. The Council collects approximately £13,500 per annum through these sites.

4.2.3 Recording of the number of garage sites

The allocation and administration of Council garage sites is managed by the Housing Services team with individual allocation of sites recorded on customer records within the Integra system. Manual files are maintained for each site and it is this manual recording which is used to control the Council stock. We noted however that the list recording the number of garage sites, produced from the manual files, was not up to date and had not been adjusted for the number of sites sold or unavailable through fire damage etc. The Council, therefore at the time of the audit review, did not have an accurate record of the number of garage sites held (500 sites are currently let or available for let rather than the 523 recorded).

No	Recommendation	Priority	Manager	Target Date
2	Management need to review current letting strategies over garages and garage sites with the aim of improving upon the number that are let. Management Comment Management are currently reviewing new advertising strategies and reviewing best practice.	Medium	Housing Services Manager	31/12/15
3	A review of rent charged for garage sites should be undertaken on a regular basis.	Medium	Housing Services Manager	31/12/15
4	Accurate records should be maintained of the number of garage sites under Council	Low	Housing	31/12/15

No	Recommendation	Priority	Manager	Target Date
	ownership. Management Comment The turnover for leasing garage sites is expected to be low. Therefore, management will ensure garage sites are reviewed and updated on an annual basis.		Services Manager	

4.3 A small number of errors were identified in the figures supplied to CIPFA which are used for Scottish Government Returns

On an annual basis, CIPFA sends out a questionnaire to local authorities requesting details of the Councils housing stock and rent collection. A small number of issues were identified by Internal Audit in the CIFPA return reported at the end of 31st March 2014.

4.3.1 Housing stock

The Scottish Government publishes statistics on the total number of houses held by each local authority. The audit found a small number of minor errors. 2 properties were double counted in the CIPFA return. This had occurred through the properties being converted from temporary to permanent accommodation which created two property references for the same properties. We also noted one property that was not handed over to the Council until after the cut off date for the return but was included in the figures.

4.3.2 Purchase schemes included in the public sector housing stock

‘Mortgage to Rent’ is a government established scheme which provides support to home owners who are experiencing difficulty in paying a mortgage or any loan that is secured against their property. The property is purchased by the Council and the home owner will continue to live in the property and pay a monthly rent to the Council. As at 31st March 2014, the Council had 14 ‘Mortgage to Rent’ agreements. The CIPFA guidelines states that dwellings subject to house purchase schemes should be excluded from Council housing stock figures reported as part of the CIPFA return, however it was noted that they had been included in error.

4.3.3 Sheltered dwellings

Within the CIPFA return the Council is also required to report on the number of sheltered dwellings (properties used for the elderly or those with special needs). We noted that due to an administrative error, this had been misreported at 63 rather than 22 on the return.

No	Recommendation	Priority	Manager	Target Date
5	Information reported on the CIFPA returns should be subject to independent checking by a second officer to decrease the risk of error. Management comment Returns will be checked by a second officer prior to dispatch.	Medium	Head of Customer and Housing Services	31/03/16

4.4 Housing Website and Manual Forms

Discretionary Housing Payments (DHP) may be made to claimants to cover any benefit shortfall. Applicants must complete a form in order to receive these payments (DHP form). It was noted however that these forms do not have a Council Data Protection Act statement included and it may not therefore be sufficiently clear to the applicant how the data provided may be used by the Council. In addition, we found that the rent charges published on the Council's website were 2 years out of date.

No	Recommendation	Priority	Manager	Target Date
6	The DHP form should contain a DPA statement.	Medium	Revenues Manager Operations	Complete
7	Rent charges on the Council's website should be updated on an annual basis. Management Comment: Rent charges have been updated for the current year and will be updated on an annual basis going forward.	Low	Housing Services Manager	Complete

4.5 Annual Bulk Up-rating

On an annual basis, rent charges are increased following the Rent Strategy agreed by Midlothian Council and annual rent increase letters are sent out to current tenants in February each year (giving 4 weeks' notice of rent increase). Reconciliations and checks are undertaken to ensure all customer's rent accounts are increased to the correct rate, there are no imbalances or system background failures and annual rent increase letters are sent out in a timely manner. A factor report spreadsheet was established in 2009 by Financial Services to ensure rent charges are updated accurately and this is updated every year by Administration and Systems Control and checked against the rates up-rated on the house rent system. Testing however identified the following:

- not all processing steps are signed off in the annual bulk up-rating to evidence that they have been completed and reviewed. This increases the risk of either processing steps not being undertaken or errors not being detected; and
- we identified 2 properties (out of 6,908) that were not up-rated correctly in 2013/14 and were not treated as standard tenants. It was reported that when rent account charges are increased, the rent charge reason is set to "annual rent increase" on the house rent system. However the two properties class coding was set up incorrectly. The result of this was that the properties were not up-rated by 6%.

No	Recommendation	Priority	Manager	Target Date
8	All processing steps in the annual bulk up-rating should be prepared and reviewed by two members of staff and this should be formally evidenced.	Low	System Group Leader	29/02/16

4.6 House Sales Recorded Incorrectly

38 properties were sold during 2014/15. We noted one minor instance of a house sale being incorrectly updated on Capita as a garage termination. Errors in update to the system may cause corruption to management reporting.

No	Recommendation	Priority	Manager	Target Date
9	House sales should be correctly recorded on the housing system.	Low	System Group Leader	Complete

APPENDIX 1

Definitions of Ratings

Audit Opinion

Level of Control	Reason for the level of Assurance given
Excellent	The control framework is of a high standard with no unacceptable risks identified.
Good	The control framework is of a good standard with only minor elements of risk identified which are either accepted or being dealt with by management.
Average	The overall control framework is of an average standard. Some weaknesses have been identified in the controls and improvements are possible.
Weak	The control framework is weak and requires improvement as significant issues exist with the adequacy and effectiveness of the Internal Control arrangements. These control deficiencies could result in financial loss or reputational damage to the Council.
Poor	The control framework is inadequate or ineffective and the issues identified require immediate attention to prevent financial loss or reputational damage to the Council.

Recommendation Rating

Priority	Risk Definition
High	Legal / regulatory issues would normally be regarded as high risks. Strategic risks would normally be regarded as high risks. Financial impact - £50K plus and / or national press interest
Medium	£5K - £49K and / or local press interest
Low	Under £5K and / or no press interest.

Distribution

- Members of the Audit Committee
- Kenneth Lawrie, Chief Executive
- John Blair, Director, Resources
- Eibhlin McHugh, Director, Health and Social Care
- Kevin Anderson, Head of Customer and Housing
- Gary Fairley, Head of Finance and Integrated Service Support
- Simon Bain, Housing Services Manager
- Jacqui Dougall, Commercial Services Manager
- Mike O'Rourke, Business Applications Manager
- Jane Harvey, Systems Group Leader
- Ken Pike, Revenues Manager Operations
- Grant Thornton, External Auditors

Audit Team

Author: Amber Ahmed, Trainee Auditor
Reviewer: Graham Herbert, Internal Audit Manager

APPENDIX 2

TERMS OF REFERENCE:
Audit Objective The objective of this audit is to review the adequacy of controls over the collection of housing rents during the financial year 14/15 with coverage limited to billing, charging and collection. Scope of Audit The review will focus on the key controls to ensure that: • rent charges and increases for council houses, garages and garage sites are calculated correctly in line with the charging policy set by the Council; • automated interfaces between payment collection systems and the house rent system are accurate and payments are correctly allocated to tenants' accounts; • rent statements and notification of rent charge increases are raised accurately and in a timely manner; • management and financial information, including the risk register, is relevant, accurate and timely; and • access to the house rent system is controlled effectively. The main areas involved in the review will be Revenues, Financial Services and Administration and Systems Control. Excluded from the Scope of the Audit The following areas will not be reviewed as part of this Audit: • Arrears recovery and write off of irrecoverable debt as this is planned for a separate audit; • The allocation of council houses to tenants; • The daily administration involved in tenancy processing; • Void properties; • Properties on special schemes such as 'spend to save'; and • Private leasing scheme properties.

Potential Risks
Key potential risks identified include: • Rent charges are inaccurately calculated or are incorrectly raised, cancelled or applied resulting in poor service to tenants or financial loss to the Council; • Payments are not applied timeously or correctly to tenants' accounts resulting in poor service to tenant or financial loss to the Council; • Incorrect management decisions or reporting due to inaccurate or inadequate records; and • Unauthorised access, amendments to or loss of data due to ineffective controls within the house rents system.
Audit Approach
The audit approach consists of: • fact finding interviews with relevant employees; • review of appropriate documentation which includes any risk reviews that have been conducted and risk registers that are in place; • interrogation of any relevant systems and sample testing as required; • closure meeting with local management to discuss the findings and any recommendations from the review; • draft and final reporting; and • presentation of the final report to the Audit Committee.
Timescales & Reporting
The audit will commence in February 2015 and is expected to be completed by the end of April 2015 and be reported in June 2015. Any issues arising will be communicated directly to local management as they are identified during the course of the audit. A formal audit report will be produced summarising the findings and recommendations of the review and will be presented to the Audit Committee.
Information Requirements
Access to all relevant systems, documentation and employees.

Financial Monitoring 2014/15

Report by John Blair, Director, Resources

1 Purpose of Report

The purpose of this report is to bring to the Committee's attention, the attached reports by the Head of Finance and Integrated Service Support, in relation to Financial Monitoring for 2014/15. The reports specifically relate to

Financial Monitoring 2014/15 – General Fund Revenue;

Housing Revenue Account - Revenue Budget and Capital Plan 2014/15; and

General Services Capital Plan;

2 Background

These reports were considered by the Council on 3 November 2015. The Council noted the position as outlined in each of the reports;

3 Report Implications

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

4 Recommendation

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

Date 9 November 2015

Report Contact:
Name John Ward Tel No 0131 271 3158
john.ward@midlothian.gov.uk

Midlothian

~~Midlothian Council~~
~~Tuesday 3 November 2015~~
~~Item No 20~~

Financial Monitoring 2015/16 – 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 2015/16 and details of the material variances.

2 Background

2.1 Budget Performance

The detailed budget performance figures shown in appendix 1 result in a projected net overspend of £1.363 million which is 0.69% of the revised budget for the year.

Performance against budget has deteriorated by £0.480 million from that reported at quarter 1. 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.

The main areas of variance are outlined below.

<u>Pressures</u>

- Demand led pressures in Children's Services;
- Expenditure pressures in Residential Care Homes for older people;
- Demand led pressures for the Community Care Resource Panel;
- Capacity issues with some external providers for Adult Social Care;
- Waste collection and disposal costs;
- Slippage in planned Transformation Savings.

<u>Favourable Movements</u>

- Council Tax income received;
- Borrowing Costs associated with the General Services Capital Plan and Treasury Management savings;
- Energy costs; and
- Savings in employee costs with vacant posts being held pending service reviews.

2.2 Council Transformation Programme Funding

Council approved utilisation of £5.868 million of General Fund Reserve to fund costs associated with the ongoing transformation programme.

At the report date £2.697 million of this has been applied with future commitments of £0.911 million identified for the remainder of 2015/16 through to 2017/18. This leaves £2.260 million as uncommitted.

2.3 General Fund Reserve

The projected balance on the General Fund as at 31 March 2016 is as follows:

	£ million	£ million
Reserve as at 1 April 2015		21.315
Less earmarked reserves utilised in 2015/16		(5.907)
General Reserve at 1 April 2015		**15.408**
Planned movements in reserves		
Planned Enhancement	2.764	
Supplementary Estimates	(0.122)	
Council Transformation Programme Costs	(0.539)	
One-off costs of VSER	(0.274)	
Workforce Reduction Savings from VSER	0.056	
Financial Discipline	0.416	
Borders Rail	(0.250)	
Other	0.025	
		17.484
Overspend per appendix 1		(1.363)
General Fund Balance at 31 March 2016		**16.121**

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

	£ million
General Fund Balance at 31 March 2016	**16.121**
Earmarked for specific purposes	
Further one-off costs associated with VSER	(0.500)
Budgets earmarked for Council Transformation	(2.260)
General Reserve at 31 March 2016	**13.361**

The uncommitted General Fund Reserve at 31 March 2016 is projected to be £13.361 million. A prudent level of uncommitted reserves is seen to be between 2% and 4% of net expenditure which equates to between approximately £4 million and £8 million. The General Reserve shown is comfortably within this level. However there may be substantial one-off costs associated with further Early Release schemes and the reserve may also be required as a buffer to offset any slippage in the achievement of planned savings.

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 Digital Issues

There are no digital implications arising from this report.

4 Recommendations

It is recommended that Council note the contents of this report.

9th October 2015

Report Contact:
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Background Papers:

MIDLOTHIAN COUNCIL

Appendix 1

GENERAL FUND OVERVIEW 2015/16

Function	**Revised Budget**	**Outturn**	**(Underspend) / Overspend**
	£	**£**	**£**
Management	1,673,312	1,673,312	0
<u>Education Communities and Economy</u>			
Childrens Services	14,842,429	15,392,429	550,000
Communties and Economy	4,849,154	4,669,154	(180,000)
Education	78,335,858	78,157,858	(178,000)
<u>Health and Social Care</u>			
Adult Social Care	38,496,887	39,446,887	950,000
Customer and Housing Services	12,057,398	12,041,398	(16,000)
<u>Resources</u>			
Commercial Services	15,829,947	15,874,947	45,000
Finance and Integrated Service Support	11,672,499	11,972,499	300,000
Properties and Facilities Management	13,392,647	13,335,647	(57,000)
Lothian Valuation Joint Board	555,551	555,551	0
Central Costs	2,842,435	3,103,435	261,000
Non Distributable Costs	1,338,436	1,338,436	0
GENERAL FUND SERVICES NET EXPENDITURE	195,886,553	197,561,553	1,675,000
Loan Charges	7,493,305	7,016,305	(477,000)
Investment Income	(180,285)	(180,285)	0
Council Transformation Programme savings target	(415,000)	0	415,000
Allocations to HRA, Capital Account etc.	(4,877,164)	(4,877,164)	0
	197,907,409	199,520,409	1,613,000
less Funding:			
Scottish Government Grant	154,996,000	154,996,000	0
Council Tax	40,000,000	40,250,000	(250,000)
Utilisation of Reserves	2,911,409	4,274,409	1,363,000

Appendix 2

Financial Monitoring 2015/16 – General Fund Revenue – Material Variances

Education, Communities and Economy

Children's Services

Description of Variance	**Reason for Variance**	**Quarter 1 £000**	**Quarter 2 £000**	**Additional information / Action taken**
Residential and day education placements	Increase in requirement for both residential and secure placements.	591	761	This represents a 21% overspend on the Multi Agency Resource Group Budget of £3.6 million. The group continue to challenge new demand to keep costs under control.
Children with Disabilities	Increased expenditure on taxis and on Direct Payments.	0	95	There are an increased number of people using the direct payment method to pay for their care. Demand for use of taxis has also increased. Work is planned to investigate if there are more efficient ways of delivering transport.
Family Placements	Increase in requirements for placements.	88	35	Demand led. The team are planning to implement new working practices to minimise the length of placements through a variety of methods.
Gross Overspend		**679**	**891**	
Offset by:				
Vacant Posts in Midlothian Residential Services	Posts held vacant due to review of residential services which is due to be completed in September 2015.	(224)	(253)	It has been possible to hold these positions vacant due to a lower number of placements. Recruitment is underway to a new structure.
Employee Vacancies and Performance Factor	Other vacancies throughout the service.	(54)	(86)	Recruitment is underway to these vacant posts.
Other non-material variances	Miscellaneous over and undespends covering the remaining areas of the Childrens Services budget.	(17)	(2)	No impact on frontline service.
Net Overspend		**384**	**550**	

Communities and Economy

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Environmental Health and Trading Standards Shared Services	The shared service arrangement with East Lothian council came to an end on 31st March 2015.	88	88	Cost sharing with East Lothian Council no longer takes place and the service are considering options to address this overspend.
Economic Development	Unbudgeted expenditure for the Leader Programme.	12	12	One-off initial set-up costs in 2015/16. From 2016/17 this programme will be funded through grant income.
Other non-material variances	Miscellaneous over and underspends covering the remaining areas of the Communities and Economies service budget.	50	51	No impact on frontline service provision.
Gross Overspend		**150**	**151**	
Offset by:				
Vacancies and Performance Factor	Vacant posts and part-year vacancies are delivering the performance factor.	(217)	(243)	Recruitment to vacant posts is ongoing and service reviews are taking place which will result in a more efficient staffing establishment.
Building Standards Income	Fee income projections exceed budget due to volume of applications.	(23)	(63)	Conditions in the Housing and Commercial development markets are showing signs of recovery.
Landlord Registrations	Income is projected to be higher than budget.	(19)	(25)	Demand led.
Net Underspend		**(109)**	**(180)**	

Education

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
PPP Contracts	Insurance costs are lower than provided for in the contract which leads to la refund from the contractor.	(67)	(67)	Windfall Income.
	Assumptions regarding the rate of inflation to be applied in 2015/16 were too cautious resulting in a projected underspend for the PPP2 contract.	(30)	(27)	This will be addressed in the 2016/17 budget setting process.
Vacancies and Performance Factor	Vacant posts and part year vacancies within the service are offsetting the performance factor.	(33)	(48)	Recruitment to vacant posts is progressing.
	The Children's Services review has resulted in part year vacancies within the Pathways service.	0	(18)	
Home to School Transport	Current estimates of demand are below that set in the budget.	0	(12)	Work is progressing with the Travel Team to ensure that the information informing development of the 2016/17 budget is accurate and that Home to School Transport is delivered in the most economically efficient way.
Other non-material variances	Miscellaneous over and underspends covering the remaining areas of the Education Service budget.	2	(6)	No impact on frontline service.
Net Underspend		**(128)**	**(178)**	

Health and Social Care

Adult Social Care

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Residential Care Homes for Older People	Projected overspend mainly on staffing costs at Newbyres Village due to the requirement to use locum staff and overtime to cover gaps in the rota.	223	261	The projected overspend in this year is mainly as a result of additional staff on shift over and above the amount allowed for in the budgeted establishment. This includes day, night and activity staff and domestic staff and is a result of the level of needs of the residents. The cost of this is around £200k. This has been partially mitigated by changes made to staffing rotas. There has been a sustained and significant reduction in sickness absence levels at the home. This is a result of successful interventions by management and will be monitored going forward to ensure it is sustained. A review of staffing is underway. Appropriate staffing levels will be addressed as part of this to ensure that the budget reflects the staffing requirements of the home.
Community Care Resource Panel	Assessed needs are currently more than budgeted. The budget is £28 million and is demand led with individual packages of care sometimes in excess of £100k per annum. Projected spend now includes the estimated increased cost within commissioned services in relation to the requirement to pay sleepover shifts at the national minimum wage.	(362)	252	The Resource Panel will continue to allocate resources where a critical or substantial need has been identified. Scrutiny of all applications is ongoing to ensure effective spend to meet assessed needs. Wage pressures for external providers associated with the entitlement to national minimum wage for sleepover shifts have resulted in changes to the rates the Council needs to pay for support overnight and brought with it increased expenditure in 2015/16. Two young people with learning disabilities who have complex needs require support above the normal levels that are provided in order to ensure their safety and wellbeing. Work is ongoing to find more sustainable solutions to these issues.

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Home Care / Rapid Response Team	A projected overspend on employee costs including staff travel and overtime due to the volume of care packages being provided by the Home Care service.	207	174	Packages of care are being held by the reablement team and will transfer to external providers when they have capacity. This has implications as care packages for people being discharged from hospital have to be provided by home care and this is achieved by staff working additional hours. Some of this overspend is being offset by lower resource panel spend on purchased care at home. A recruitment fair involving all providers has been held to encourage more people to work in the care sector. Meetings are in place with providers to address their capacity issues.
Non-achievement of staffing related budget	Planned budget savings from staffing reviews will not take effect until either 2016/17 or 2017/18.	201	201	Timescales for reviews mean savings will not be realised as early as anticipated but are on target for 2016/17 and 2017/18.
Fieldwork Staffing	Non-achievement of performance factor and use of agency staff to cover vacancies.	109	155	There have been staffing changes within this service and also Adult Protection referrals have increased significantly. Due to the demands on the service all posts require to be filled. Use of agency staff will reduce as vacancies are filled. Applicability of a performance factor in this area will be reviewed as part of the 2016/17 budget setting process.
Cherry Road, Community Action Team and Shared Lives	Non-achievement of employee performance factor.	68	93	These are registered services and adequate staffing levels are a requirement of the Care Inspectorate. Cherry Road supports service users with complex needs and appropriate staffing levels must be maintained. Applicability of a performance factor in this area will be reviewed as part of the 2016/17 budget setting process.
Other non material variances	Miscellaneous over and underspends covering the remaining areas of the Adult Social Care budget.	25	53	No impact on frontline service.
Gross Overspend		**471**	**1,189**	

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Offset by:				
Client Income	Contributions from clients towards their care packages are higher than anticipated. The impact of waiving charges for carers will be monitored and reviewed as part of the 2016/17 budget setting process.	(130)	(56)	No impact on frontline service.
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.	(57)	(81)	No impact on frontline service but underspend offsets care and support costs related to protection issues.
Criminal Justice	Previously an element of the Scottish Government funding was used to fund the management and administration of this service.	(43)	0	No impact on frontline service.
Learning and Development	Spend has been constrained to counter pressures elsewhere in the service.	(36)	(102)	No impact on frontline service and offsets cost of essential cover for front-line staff with mandatory training requirements.
Net Overspend		**205**	**950**	

Customer and Housing Services

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Homelessness accommodation	Refurbishment works at Pentland and Midfield House are to take place later than anticipated when the budget was set resulting in savings being delayed. Re-use is expected early in 2016 for Midfield House and April 2016 for Pentland House.	151	209	The budget provided for an average 82 B and B places per week until 1st August and 36 spaces thereafter once Pentland and Midfield House were available for use. Average occupancy is currently 73 places. Action is being taken to reduce this with alternative options being developed across all available tenures.
Gross Overspend		**151**	**209**	
Offset by:				
Council Tax Reduction Scheme	Council Tax Benefits granted are lower than budgeted and are consistent with 2013/14 and 2014/15 positions.	(70)	(113)	Whilst the 2015/16 budget was adjusted to reflect a decreasing trend in expenditure, it is projected that payments will decrease further than originally anticipated. This will be reviewed when setting the 2016/17 budget.
Housing Benefit Overpayment Recoveries	Housing Benefit overpayment recoveries are anticipated to be greater than budgeted.	(53)	(53)	This is consistent with the 2014/15 outturn position and will be reviewed when setting the 2015/16 budget. This will be further reviewed when preparing the 2016/17 budget.
Vacancies and Performance Factor	Vacant posts within the Revenues service.	0	(42)	No impact on frontline service.
Other non material variances	Miscellaneous over and underspends covering the remaining areas of the Customer and Housing Service budget.	(3)	(17)	No impact on frontline service.
Net Overspend / (Underspend)		**25**	**(16)**	

Resources

Commercial Services

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Waste Disposal Charges	The sale price of recyclate has dropped significantly since the budget was prepared.	110	118	During 2014/15 the price per tonne for recyclate reached a peak of £27.20 which was reflected in the average budget price of £20.75. To date in the current financial year the average price has been £9.66. Prices in this market are very volatile.
Trade Waste	Customers are encouraged to reduce residual waste and recycle more. As recycling is charged at a lower price to customers this has led to a drop in income.	0	94	Collection costs are the same for both recyclate and residual waste.
Land Services	A drop in hard landscaping one-off jobs is anticipated as a consequence of an inability to recruit and retain suitable staff.	30	30	Total loss of income is £150k and this is offset by savings in staff costs of £120k. Efforts continue to recruit suitably qualified staff.
Gross Overspend		**140**	**242**	
Offset by:				
Fuel Costs	The budget provided for an average price of £1.12 per litre. The average price to date is £0.86 per litre.	(129)	(147)	Fuel prices have been low during the recent period but can be volatile.
Street Lighting Electricity	The budget provided for an average price of 9.97 pence per kwh. The average price currently being charged is 9.09 pence per kwh.	(50)	(50)	Consumption and the prevailing price will be closely monitored as the year progresses.
Net Overspend / (Underspend)		**(39)**	**45**	

Finance and Integrated Service Support

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Mi-Future	The costs of staff in SWITCH during the year are projected to exceed budget. £66k of the projected variance relates to staff on unfunded placement. The majority of the remainder relates mainly to staff whose placements are at a lower grade than their displaced post.	166	115	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. Since inception 65 people have entered SWITCH. As at 30th September 18 people remain in SWITCH.
Archive facility - the former Hopefield Primary School	The former Hopefield Primary School was being used as an archive and also for other storage until the fire on 17th May. Alternative permanent storage arrangements are still being sought with an anticipated cost of £71k in 2015/16 which is not budgeted.	77	77	No budget was provided as it was anticipated this facility would not be in operational use. Permanent off-site storage costs will be incorporated in the 2016/17 base budget.
Central Postages	The volume and cost of postages exceeds budget.	72	90	Despite changing suppliers and securing better prices the volume and mix of postages continues to exceed budget. Work continues to address this.
Protecting Vulnerable Groups and Public Sector Network disclosure checks	The volume of disclosure checks will exceed budget.	50	50	Work is ongoing to establish the level of retrospective checks still to be undertaken.
Employee Performance Factor	The budgeted employee performance factor is expected to be over achieved.	25	(48)	Delays in recruitment to vacant posts have resulted in a reduction to anticipated staff costs for the year.
Bank Charges	The shift towards electronic payments has led to increased transaction costs.	16	16	A review of bank charges is underway with the aim of negotiating lower rates with service providers.
Net Overspend		**406**	**300**	

Properties and Facilities Management

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional information / Action taken
Bonnyrigg Leisure Centre	Security and Rates costs for the former Leisure Centre.	51	25	Demolition and building works are now underway. A partial refund of rates has been received.
Property costs for former Loanhead Social Work centre	Building is now demolished. Property costs were incurred up to handover date to demolition contractor.	8	8	One-off costs.
Gross Overspend		**59**	**33**	
Offset by:				
Snowsports Income	Tubing party income and consequent impact on cafe.	(90)	(90)	First full year of operation has shown higher than expected income.
Net Underspend		**(31)**	**(57)**	

Other

Description of Variance	Reason for Variance	Quarter 1 £000	Quarter 2 £000	Additional Information / Action taken
Loan Charges	Since setting the 2015/16 budget the cost of borrowing to finance the General Services Capital Plan has reduced due to: (a) Re-phasing of projects which has allowed deferral of long-term borrowing; (b) Reduction in borrowing costs through lower than forecast interest rates; (c) Increase in projected investment returns through utilisation of higher yield investment products, in accordance with investment strategy.	(197)	(477)	Projects that have slipped will now fall into 2016/17 so borrowing costs are only delayed.

Central Costs	Insurance costs – higher than budgeted estimated settlement costs for existing claims. Insurance costs – there has been an increase in premiums as a consequence of claims experience and additional coverage for a certain class of property.	110 72	190 71	Detail of these claims is being reviewed and any mitigating action required will be put in place. This will be reflected as a budget pressure in future years.
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 £165k of this will be achieved.	185	185	Procurement plans are currently being refreshed and this may identify further savings in 2015/16. Contract savings have been made or are planned for 2015/16 which impact on the Capital Account and the Housing Revenue Account.
Transformation Savings - Maximising Attendance	The target of £155k will not been achieved in 2015/16.	155	155	Work continues to generate savings through maximising attendance.
Transformation Savings – Income Maximisation	The Target of £75k will not be achieved in 2015/16.	75	75	Progress towards efficiencies in this area will be consumed into the Delivering Excellence agenda.
Council Tax and Community Charge Income	A continued growth in Band D equivalents results in a higher than budgeted Council Tax yield.	(230)	(250)	The continued growth in Band D equivalents will be factored into Council Tax income budgets for future years.

Housing Revenue Account
Revenue Budget and Capital Plan 2015/16

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 4th October 2015 for the Capital Plan and a projected outturn for both the Housing Revenue Account and Capital Plan for 2015/16.

2 Background

2.1 Revenue Account 2015/16

Since the revision of the Revenue Budget reported to Council on 22nd September 2015 an underspend of £0.497 million is projected for 2015/16 which is shown in Appendix 2.

The underspend is primarily due to delays in the refurbishment of Pentland and Midfield House which will result in a saving of £0.387 million for Housing Support and Caretaker costs.

The cost of borrowing will also be reduced by £0.116 million due to:-

- Rephasing of Phase 2 New Social Housing Programme which has allowed deferral of long-term borrowing;
- Reduction in borrowing costs through lower than forecast interest rates;
- Increase in projected investment returns through utilisation of higher yield investment products, in accordance with the Investment strategy.

The HRA reserve balance is projected to be £24.172 million at 31st March 2016. The longer term financial projections demonstrate that the majority of this will be required to finance existing investment commitments to 2029/30.

2.2 Capital Plan 2015/16

The revision of the Capital Plan reported to Council on 22nd September 2015 allowed for investment of £27.842 million in 2015/16 as shown in Appendix 1. There have been difficulties in gaining access to a number of properties to replace which will result in slippage of the Sanitary Ware Replacement Programme of £2.331 million to be carried forward to 2016/17.

Contaminated land issues and necessary remediation works on New Social Housing Phase 2 sites have resulted in delays within the programme and will result in slippage of £0.832 million to be carried forward to 2016/17.

At this stage there are no material variances to be reported for 2015/16.

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 £24.172 million at 31 March 2016, the longer term financial projections demonstrate that the majority of this will be required to finance existing investment commitments.

However affordability is heavily dependent on the future year's rents strategy, Council on 22nd February 2011 agreed a rent increase of 6% from 2011/12 to 2015/16 and the long term forecast incorporate in the model assumes rent increases in future years of 4%.

Proposals for a revised rental strategy is currently at consultation with tenants; the results will be presented to Council later in the year together with the implications of the options for future new build and investment in existing assets.

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 2015/16 is:

- Capital Expenditure is anticipated to be £24.679 million for the year;
- A net undersend of £0.497 million is projected on the Revenue Account;
- The HRA reserve at 31st March 2016 is projected to be £24.172 million.

5 Recommendations

Council is recommended to note the contents of this report.

Date 8th October 2015

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Background Papers: HRA Capital Plan and Revenue Budget

MIDLOTHIAN COUNCIL

HOUSING REVENUE ACCOUNT 2015/16

Appendix 2

	Revised Budget	Projected Outturn	Variation (Under)/Over
Average No of Houses	**6,833**	**6,833**	**0**
	£000's	**£000's**	**£000's**
Repairs and Maintenance			
General Repairs	5,516	5,516	0
Decant/Compensation	40	46	6
Grounds Maintenance	574	574	0
	6,130	**6,136**	**6**
Administration and Management	4,752	4,752	0
Loan Charges	8,276	8,160	(116)
Other Expenses	2,846	2,459	(387)
TOTAL EXPENDITURE	**22,004**	**21,507**	**(497)**
Rents			
Houses	(23,294)	(23,294)	0
Garages	(504)	(504)	0
Others	(504)	(504)	0
TOTAL RENTS	**(24,302)**	**(24,302)**	**0**
NET EXPENDITURE/(INCOME)	**(2,298)**	**(2,795)**	**(497)**
BALANCE BROUGHT FORWARD	**(21,377)**	**(21,377)**	**0**
BALANCE CARRIED FORWARD	**(23,675)**	**(24,172)**	**(497)**

General Services Capital Plan 2015/16 to 2020/21
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 the projected performance of the General Services Capital Plan against budget for 2015/16.

2. Background

2.1 2015/16 Budget

The Quarter 1 monitoring position for the General Services Capital Plan for 2015/16 was presented to Council on 22 September 2015 and, after accounting for known rephasing of projects, budgeted for expenditure of £23.572 million and funding of £16.581 million, therefore giving a budgeted in-year borrowing requirement of £6.991 million.

2.2 Adjustments to 2015/16 Budget

<u>Expenditure</u>

The budgeted expenditure of £23.572 million, as reported at Quarter 1, has been adjusted as outlined in Tables 1, 2 and 3 below:-

Table 1: New Projects

Project	**Description of amendment to budget**	**Previous Budget £000's**	**Revised Budget £000's**	**Budget Movement £000's**
Stobhill Primary School Footpath	Footpath from existing Arniston Vale development into boundary of primary school	0	22	+22

* Note that this project is fully financed from Developer Contributions.

Table 2: Changes to overall project budgets

Project	**Description of amendment to budget**	**Previous Budget £000's**	**Revised Budget £000's**	**Budget Movement £000's**
Woodburn Family Learning Centre	Inclusion of Digital Services requirements both externally (cabling/infrastructure) and internally (PC's/Laptops, etc)	280	327	+47

* Note that this project is fully financed from the Scottish Government's Early Year's Funding.

Table 3: Rephasing of project budget

Project	Description of amendment to budget	Previous Budget £000's	Revised Budget £000's	Budget Movement £000's
Newbattle High School Preparatory Works	Ongoing costs as a result of delay to construction commencement	723	1,140	+417
Digital Services: Front Office – Device & Interactive Asset Upgrades	Asset replacement – acceleration of roll-out of PC's	150	375	+225
Digital Services: Back Office – Server Replacement	Asset replacement – acceleration of core server infrastructure	50	160	+110
Lasswade High School	Rephasing of MUGA works fully into 2016/17	394	202	-192
New Recycling Facility – Penicuik	Revised report to be presented to Council regarding options for requirement/ replacement/ refurbished facility	315	50	-265
Member's Environmental Improvements	Revised profile of spend based on in-year spend to date	560	280	-280
New Gorebridge North Primary	Rephasing of project start date / revised cashflow projections from contractor	3,402	2,972	-430
New Bilston Primary	Rephasing of project start date / revised cashflow projections from contractor	3,775	2,928	-847
Paradykes & Roslin Preparatory Works / Replacements	Rephasing of project start dates	3,168	1,667	-1,501
Other minor variances		75	133	+58
Total		**12,612**	**9,907**	**-2,705**

This therefore gives a revised budgeted expenditure of £20.936 million for 2015/16.

Funding

In line with this, the budgeted level of funding available to finance the plan has also been adjusted from the Q1 budgeted funding of £16.581 million to £16.865 million, to reflect:-

- An increase of £0.526 million in Other Contributions, reflecting the award from Zero Waste Scotland towards financing of the capital costs associated with the Food Waste Collection roll-out;
- An increase of £0.128 million in Government Grants, reflecting:-
    - The additional £0.047 million utilisation of the Scottish Government's Early Year's Childcare Funding, to fund the additional costs of the Woodburn Family Learning Centre project; and
    - A reduction of £0.081 million in the level of General Capital Grant funding which had been earmarked to fund Public Sector Housing Grants and Contaminated Land;
- A reduction of £0.370 million in the application of developer contributions, reflecting the rephasing of expenditure in the plan.

Borrowing

The budgeted level of borrowing reported at Quarter 1 was £6.991 million. Based on the rephased expenditure and funding levels outlined above, the rephased budgeted borrowing required has reduced to £4.071 million.

2.3 Quarter 2 Projected Performance against Budget

Expenditure

Expenditure to 13 September 2015 is £2.941 million with a projected expenditure outturn of £20.380 million. At this stage it is anticipated that budgets for the projects detailed in Appendix 1 will be fully spent in the current year with the following exceptions:-

Table 4: Adjustment to expenditure budget of projects

Item	Description	Projected (Underspend)/ Overspend £000's
Cornbank, St. Andrew's & Newtongrange Primary School Extensions	Saving as a result of cost and area value engineering	-222
Penicuik Care Home Hub	Saving as a result of competitive tender price	-163
Food Waste Collection	Savings in costs of purchasing new vehicles, internal caddies and external caddies	-127
Burnbrae Primary	Saving as a result of competitive tender price	-44
Total		**-556**

It is therefore expected that there will be a net underspend against budget for the year of £0.556 million.

Funding

Funding received to 13 September 2015 is £5.039 million with a projected total funding available to finance the capital plan in 2015/16 of £16.865 million, in line with the rephased budget.

Borrowing

The rephased budgeted level of borrowing for 2015/16 was £4.071 million. Based on the revised expenditure and funding levels as outlined above, the projected estimate of the level of borrowing required to fund the investment identified in Appendix 1 is £3.515 million, a reduction of £0.556 million. The impact of this on the Council's borrowing costs is reflected in the Financial Monitoring 2015/16 – General Fund Revenue report elsewhere on today's agenda.

2.4 Overall Position 2015/16

Based on the above, the projected performance against budget for 2015/16 is shown in the table below:-

Item	2015/16 Budget At Q1 £000's	Rephased 2015/16 Budget At Q2 £000's	Actual To 13/09/15 £000's	2015/16 Projected Outturn £000's	2015/16 Variance £000's	2015/16 Carry Forward £000's
Expenditure	23,572	20,936	2,941	20,380	-556	2,635
Funding	16,581	16,865	5,039	16,865	0	
Borrowing Required	6,991	4,071	-2,099	3,515	-556	

3. Capital Fund

The Capital Fund at the start of the 2015/16 financial year was £14.853 million. Capital Receipts of £4.198 million are forecast to be received in 2015/16 (£2.167 million to 13/09/15), and will be transferred to the capital fund. This will increase the balance in the Capital Fund to £19.051 million. Officers are currently reviewing the medium to long term strategy for the utilisation of the Capital Fund and will report back in due course.

4. Report Implications

4.1 Resource

The borrowing required to finance the planned investment in 2015/16 is projected to be £3.515 million. The loan charges associated with this borrowing are reported to Council in the Financial Monitoring 2015/16 – General Fund Revenue report presented elsewhere on today's agenda.

4.2 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.

There is also a risk that the wrong projects are prioritised, however there is an additional risk that the revenue budget cannot afford the level of borrowing currently reflected.

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
- [x] Sustainable growth
- [ ] Business transformation and Best Value
- [ ] None of the above

4.4 Impact on Performance and Outcome

There are no issues arising directly from this report.

4.5 Adopting a Preventative Approach

There are no issues arising directly from this report

4.6 Involving Communities and Other Stakeholders

No external consultation has taken place on this report.

4.7 Ensuring Equalities

There are no equalities issues arising directly from this report.

4.8 Supporting Sustainable Development

There are no sustainability issues arising directly from this report.

4.9 IT Issues

There are no IT implications arising from this report.

5 Recommendations

Council is asked to:

a) Note the General Services Capital Plan Quarter 2 monitoring position for 2015/16;
b) Approve the Stobhill Primary School Footpath project as outlined in Table 1 in Section 2.2 to be added to the General Services Capital Plan.

Date 19 October 2015

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Background Papers:
Appendix 1 – Detailed General Services Capital Plan Expenditure 2015/16

Appendix 1

Detailed General Services Capital Plan Expenditure 2015/16

GENERAL SERVICES CAPITAL PLAN 2014/15 to 2017/18	Rephased 2015/16 Budget Q2 £000's	2015/16 Actual to 13/9/15 £000's	2015/16 Projected Outturn £000's	2015/16 Variance £000's	2015/16 Carry Forward £000's
RESOURCES					
Finance & Integrated Service Support					
Front Office - Device & Interactive Asset Upgrades	375	258	375	0	-225
Back Office - Anti Virus Upgrades	0	0	0	0	0
Back Office - Server Replacement	160	41	160	0	-110
Back Office - UPS Devices	10	11	10	0	0
Network Enterprise - Network Internet Connection	0	0	0	0	0
Network Enterprise - Network Assets (Power & Data)	75	0	75	0	0
IGS - Compliance - Data Encryption	0	0	0	0	0
IGS - Compliance - PCI	0	0	0	0	0
Disaster Recovery	0	0	0	0	0
Service Desk - ITMIS Service Improvement	50	0	50	0	0
Midlothian Website Development	5	0	5	0	0
IT Development (Education)	0	0	0	0	0
Committee Management System	15	0	15	0	0
Paperless Meetings	16	0	16	0	0
Business Application Upgrades inc. mobile working	100	16	100	0	0
Commercial Services					
Street Lighting Upgrades	496	325	496	0	0
Street Lighting LED Upgrade (Salix Funded)	200	35	200	0	0
Footway & Footpath Network Upgrades	1,000		1,000	0	0
Road Upgrades	1,521	346	1,521	0	0
A6106 Lugton	30	30	30	0	0
Millerhill Access Road / Site Services	100	13	100	0	0
Beeslack High School Safer Routes to School	0	0	0	0	0
Cycling, Walking & Safer Streets Projects	127	-12	127	0	0
Ironmills Park Steps	28	0	28	0	0
Emily Bing	13	0	13	0	0
New recycling facility - Penicuik	50	0	50	0	265
Waste Collection Vehicles	338	0	338	0	0
Food Waste Collection	653	0	526	-127	0
Vehicle & Plant Replacement Programme	1,484	508	1,484	0	0
Install Geogrid - Barleyknowe Lane	102	0	102	0	0
Bonnyrigg Skate Park	4	0	4	0	0
Newtongrange Wheeled Sports park	39	0	39	0	0
Loanhead Memorial Park	60	19	60	0	0
Riverside Park	26	0	26	0	0
20mph Limits	40	0	40	0	0
Vogrie Car Parking Barriers	33	0	33	0	0
CCTV Upgrade	93	0	93	0	0
Property & Facilities					
Stobhill Depot Upgrade	0	0	0	0	0
Property Upgrades inc. Lighting/Lightning	1,576	137	1,576	0	0
Primary 1-3 Free School Meals	12	1	12	0	0
TOTAL RESOURCES	**8,831**	**1,727**	**8,704**	**-127**	**-70**

EDUCATION, COMMUNITY AND ECONOMY	Rephased 2015/16 Budget Q2	2015/16 Actual to 13/9/15	2015/16 Projected Outturn	2015/16 Variance	2015/16 Carry Forward
Early Years	**£000's**	**£000's**	**£000's**	**£000's**	**£000's**
Woodburn Family Learning Centre	327	0	327	0	-47
Further Early Years Provisions	0	0	0	0	0
Primary					
Burnbrae Primary	67	0	23	-44	0
New Bilston Primary	2,928	75	2,928	0	847
New Gorebridge North Primary	2,972	110	2,972	0	430
Rosewell Primary Extension	104	7	104	0	0
Cornbank Primary Extension	149	-5	24	-125	0
St Andrews Primary Extension	86	-13	5	-81	0
Newtongrange Primary Extension	46	1	30	-16	0
Paradykes & Roslin Primaries Preparatory Works	667	45	667	0	333
Paradykes Primary Replacement	500	0	500	0	868
Roslin Primary Replacement	500	0	500	0	300
Gorebridge Primary School Additional Classroom	12	10	12	0	0
Hopefield Primary School Demolition	0	164		0	0
Hawthornden Primary School Roof	6	6	6	0	0
Stobhill Primary School Footpath	22	22	22	0	0
Secondary					
Lasswade High School inc. 2nd MUGA	202	145	202	0	192
Newbattle High School Preparatory Works	1,140	188	1,140	0	-417
Newbattle High School - Future Extension	0	0	0	0	0
Saltersgate Alterations	159	0	159	0	0
General					
Online Payments for Schools	45	0	45	0	0
Bright Sparks	356	0	356	0	0
PPP1 Land Acquisition	27	0	27	0	0
Children and Families					
Eastfield Children's Unit	3	3	3	0	-3
Woodburn Children's Unit	0	0	0	0	0
Planning & Development					
Environmental Improvements	280	35	280	0	280
Property Asset Management System	9	0	9	0	0
Dalkeith Town Centre (TCRF??)	1	1	1	0	0
TOTAL EDUCATION, COMMUNITY AND ECONOMY	**10,607**	**795**	**10,341**	**-266**	**2,783**
HEALTH AND SOCIAL CARE					
Adult & Social Care					
Care Homes	1	1	1	0	-1
Penicuik Care Home Hub	196	23	33	-163	0
Penicuik Care Home Hub - Fit Out	0	0	0	0	0
Highbank OPH - Adaptations (Phase II)	0	0	0	0	0
Assistive Technology	260	8	260	0	0
Travelling Peoples Site Upgrade	17	0	17	0	0
Customer & Housing Services					
Libraries Cash Management System	-1	-1	-1	0	1
TOTAL HEALTH AND SOCIAL CARE	**473**	**32**	**310**	**-163**	**0**
COUNCIL TRANSFORMATION					
Purchase to Pay	32	8	32	0	0
Property Services Review	43	18	43	0	0
EDRMS	12	6	12	0	0
EWiM	125	125	125	0	-50
EWiM Phase 2	661	229	661	0	0
Online Housing Applications	27	0	27	0	0
Unallocated	125	0	125	0	0
TOTAL COUNCIL TRANSFORMATION	**1,025**	**387**	**1,025**	**0**	**-50**
GENERAL SERVICES CAPITAL PLAN TOTAL	**20,936**	**2,941**	**20,380**	**-556**	**2,663**

Treasury Management Mid-Year Review Report 2015/16
Report by John Blair, Director, Resources

1 Purpose of Report

The purpose of this report is to bring to the Committee's attention, the attached reports by the Head of Finance and Integrated Service Support, in relation to

2 Background

This report was considered by the Council on 3 November 2015. The Council adopted the recommendations contained in the report.

3 Report Implications

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

4 Recommendation

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

Date 9 November 2015

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Treasury Management Mid-Year Review Report 2015/16

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

1 Purpose of Report

The purpose of this report is to inform members of the Treasury Management activity undertaken during the first half of 2015/16, the forecast activity for the second half of 2015/16, and update the Prudential Indicators for 2015/16.

2 Background

Council, on 17 February 2015, approved the Treasury Management and Annual Investment Strategy Statement for the financial year 2015/16.

3. Treasury Activity during first half of 2015/16

The main points arising from treasury activity in the year to 15 October 2015 were:-

- The average interest rate earned on external investments in the period up to 15 October 2015 was 0.85%, exceeding the benchmark rate of 0.73%;
- A 180 day notice account with Santander UK plc was opened on 08 October 2015 with an initial deposit of £14.985 million earning an interest rate of 1.15%, continuing the policy of cash backing reserves, whilst adding value to the portfolio with minimal risk.
- Long-term borrowing of £7.049 million was taken on 27 August 2015 at an interest rate of 2.92% for a 47 year tenor. The borrowing was sourced from PWLB, taking advantage of the Council's successful application for the Project Rate discount of 0.40% from the standard PWLB rates;
- Long term borrowing of £5.031 million matured in the period to 15 October 2015, this being £5.000 million PWLB maturities, £0.013 million PWLB Annuities, and £0.018 million Salix loan;
- No debt rescheduling has been undertaken during the period;

An economic update for the first part of the 2015/16 financial year is included as Appendix 1. PWLB borrowing rates for the first half of the year are outlined in Appendix 2.

The Council's loan and investment portfolio as at 15 October 2015 is shown in tables 1 and 2 overleaf (position at 31 March 2015 also shown for comparison):-

Table 1: Council's Loan Portfolio at 31 March 2015 and 15 October 2015

Loan Type	**31 March 2015**		**15 October 2015**	
	Principal Outstanding £000's	**Weighted Average Rate**	**Principal Outstanding £000's**	**Weighted Average Rate %**
PWLB Annuity	794	8.90%	781	8.90%
PWLB Maturity	177,175	3.99%	179,224	4.01%
LOBO	20,000	4.51%	20,000	4.51%
Temporary Market Loans	36,500	0.37%	28,300	0.32%
Other Loans	236	0.00%	218	0.00%
Total Loans	**234,706**	**3.48%**	**228,524**	**3.61%**
Underlying Borrowing Requirement*	**253,909**		**255,842**	
Internal Borrowing	**19,203**		**27,318**	

* *The Underlying Borrowing Requirement is the Capital Financing Requirement excluding the PPP Liabilities*

Table 2: Council's Investment Portfolio at 31 March 2015 and 15 October 2015

Investment Type	**31 March 2015**		**15 October 2015**	
	Principal Outstanding £000's	**Weighted Average Rate**	**Principal Outstanding £000's**	**Weighted Average Rate %**
Bank Call Accounts	2	0.39%	226	0.25%
Money Market Funds	5,889	0.47%	11,343	0.49%
Bank Notice Accounts	0	0.30%	14,985	1.15%
Bank Fixed Term Deposits	40,000	0.99%	40,000	0.99%
Bank Certificates of Deposit	10,000	0.69%	0	0.00%
Total Investments	**55,891**	**0.88%**	**66,554**	**0.94%**

4. Expected Treasury Activity during second half of 2015/16

<u>Borrowing</u>

Given the capital expenditure forecasts reported elsewhere on today's agenda, and summarised in Section 5 below, there is no requirement to source long-term borrowing to fund capital expenditure in the second half of 2015/16. However, consideration will continue to be given as to whether borrowing now (for capital expenditure in 2016/17 or beyond) to secure historically low PWLB rates offers value compared with forward interest rate projections. Equally, consideration will continue to be given as to whether any forward borrowing opportunities (which would allow the Council to secure loans now, but draw down these lat later dates at interest rates that are significantly less than current market projections, and at the same time eliminate the majority of the cost of carry) offers value compared with forward interest rate projections.

Appendix 3 provides forecasts for interest rates from the Council's Treasury Management advisor, Capita.

As with all long-term borrowing decisions, an option appraisal will be undertaken prior to executing any loan transaction, to ensure that any loans taken offer best value to the Council.

Investments

The Council's current Investment policy, as approved by Council on 17 February 2015, selects investments based on the security, liquidity, and yield (interest rate payable) of an investment product, in that order.

In terms of assessing the security of any counterparty, the Council employs the Capita Credit Scoring Methodology, which utilises credit ratings from the 3 main credit rating agencies (Fitch, Moody's and Standard and Poor's), supplemented with credit watches, outlooks, Credit Default Swap (CDS) spreads (which give early warning of likely changed in credit ratings) and sovereign ratings. This is all wrapped into a weighted scoring system for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested maximum duration for any investment, as shown in Table 3 below:-

Table 3: Capita Credit Scoring: Durational Bands

Capita Colour Code	**Capita Suggested Duration**	**Approved Investment Duration[1]**
Yellow	5 years	6 years
Dark Pink	5 years	6 years
Light Pink	5 years	6 years
Purple	2 years	3 years
Blue	1 year	2 years
Orange	1 year	2 years
Red	6 months	7 months
Green	100 days	100 days
No colour	Not to be used	Not to be used

Counterparties for investment are selected in accordance with the above credit criteria, and investment products with these counterparties are selected to ensure that value can be added to the overall investment portfolio.

The Council's current Investment approach is to broadly cash back its reserves. Useable reserves as at 31 March 2015 were £60.618 million, and are forecast to increase to £67.609 million by 31 March 2016.

The Council currently has deposits totalling £40 million with Lloyds Banking Group and The Royal Bank of Scotland, as shown in Table 4 below:-

[1] Note that the approved durations listed above were 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 7 months, 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.

Table 4: Current Fixed Term Investments

Loan Type	Amount £000's	Start Date	Maturity Date	Interest Rate
Fixed Term Deposit Lloyds Banking Group	20,000	27 Oct 2014	27 Oct 2015	1.00%
Fixed Term Deposit Lloyds Banking Group	10,000	24 Dec 2014	29 Jan 2016	0.92%
Certificate of Deposit Royal Bank of Scotland	10,000	04 Nov 2014	04 Nov 2015	1.05%

At the time of placement of the £20 million and £10 million deposits with Lloyds Banking Group, Lloyds were scored as "Blue" under the Capita credit scoring methodology, reflective of the implied sovereign support for the bank as a result of the UK Government's shareholding. This therefore allowed the Council to place deposits with Lloyds Banking Group for a one year duration.

In the last 12 months, the UK Government has reduced its shareholding in Lloyds Banking Group, with the expectation that this reduction will continue throughout the remainder of this financial year. Whilst the government is still one of the larger, if not the largest, stakeholder, the reduction in shareholding has, and will continue to, leave the government with materially less of an ability to drive processes and policies within the bank than currently. As a result, Capita Asset Services have reviewed the part-nationalised status of Lloyds Banking Group, with the credit status of the bank now being judged solely on its ratings and CDS prices, as with other entities on the suggested Credit List, whereas previously the UK Government's implied support was factored in. This has seen the bank's suggested maximum duration fall from Blue (12 months) to Red (6 months).

Notwithstanding this, table 5 below highlights that Lloyds Banking Group's underlying credit ratings have not been adversely affected in the past year.

Table 5: Lloyds Banking Group Credit Rating

Counterparty	Capita Credit Score Duration	Short Term Ratings (Fitch/ Moody's/ S&P's)	Long-Term Ratings (Fitch/ Moody's/ S&P's)	Viability /Support	Country Sovereign Rating	Max Interest Payable based on Credit Rating
Lloyds Banking Group 24.10.14	Blue 12 months	F1/P-1/A-1	A/A1/A	a-/1	UK/ AA+	1.05%
Lloyds Banking Group 09.10.15	Red 6 months	F1/P-1/A-1	A+/A1/A	a/5	UK/ AA+	0.80%

See Appendix 5 for detail on the credit scoring scale for each credit rating agency.

Whilst the interest rates on offer from Lloyds Banking Group remain at similar levels to those on offer last year (e.g. a 12 month fixed term deposit continues to offer 1.05% interest), the credit scoring methodology outlined above dictates that the Council can no longer invest for a 12 month duration, with the maximum duration available now being a 175 day notice account offering 0.80% interest. Given that the current £30 million of deposits with Lloyds Banking Group matures at the end of October / early November, this reduction in duration and available yield directly impacts on the overall rate of return the Council is able to deliver through its investment portfolio, and therefore presents a challenge for the Council to continue to maximise its investment returns, whilst ensuring that the overriding principle of security of any funds remains paramount.

With that in mind, Council officers have engaged their Treasury Management advisers, Capita, to review the options available to the Council, to ensure a similar level of security of funds whilst at the same time continuing to offer value to the Council's investment portfolio, all within the boundaries of the approved credit scoring methodology. Table 6 below lists a number of these potential investment options available to the Council:-

Table 6: Potential investment options available to the Council

Counterparty	**Capita Suggested Duration**	**Maximum Interest Payable based on Credit Rating**
Lloyds Banking Group	Red (6 months)	0.80%
Santander UK	Red (6 months)	1.15%
Royal Bank of Scotland	Blue (12 months)	n/a
Svenska Handelsbanken	Orange (12 months)	0.93%
Qatar National Bank	Orange (12 months)	1.05%
National Bank of Abu Dhabi	Orange (12 months)	0.94%

The credit ratings (from Fitch, Moody's and Standard & Poors) of each counterparty are reflected in the Capita Suggested Duration in the table above. The credit ratings for Svenska Handelsbanken (a current counterparty of the Council), Qatar National Bank and the National Bank of Abu Dhabi are equivalent to, or higher than, all of the UK counterparties the Council currently have deposits with. Furthermore, all of these counterparties are domiciled within very strong sovereign rated countries.

It is important that Treasury Strategy and Review reports clearly outline to Members the Council's investment policy and the subsequent range of potential counterparties that the Council may therefore transact with, in order that Members can become familiar with the proposed investment policy and attain comfort as to the potential range of counterparties available to the Council for investment.

It is proposed that Council officers, in conjunction with Capita Asset Services, continue to review the range of investment options available to the Council within its stated investment policy 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.

Expected Loan & Investment Portfolio at 31 March 2016

Taking all of the above into account, the expected loan and investment portfolio at 31 March 2015 is shown in Tables 7 and 8 below:-

Table 7: Council's forecast Loan Portfolio at 31 March 2016

Loan Type	**31 March 2016**	
	Principal Outstanding £000's	**Weighted Average Rate**
PWLB Annuity	768	8.90%
PWLB Maturity	179,224	4.01%
LOBO	20,000	4.51%
Temporary Market Loans	36,500	0.33%
Other Loans	400	0.00%
Total Loans	**236,892**	**3.49%**
Underlying Borrowing Requirement	**272,396**	
Internal Borrowing	**35,504**	

*

Table 8: Council's forecast Investment Portfolio at 31 March 2016

Investment Type	**31 March 2016**	
	Principal Outstanding £000's	**Weighted Average Rate**
Bank Call Accounts	0	n/a
Money Market Funds	5,000	0.49%
Bank Notice Accounts	14,985	1.15%
Bank Fixed Term Deposits	25,015	0.92%
Bank Certificates of Deposit	0	n/a
Total Investments	**45,000**	**0.95%**

5. Prudential Indicators 2014/15

The following prudential indicators have been refreshed from those reported to Council on 17 February 2015 in the original Treasury Management and Annual Investment Strategy Statement 2015/16, based on the actual outturn for 2014/15 and the Council's Capital Plans for 2015/16 to 2020/21, and are shown in Table 9 and in graphical form below (see also Appendix 4):-

Table 9: Prudential Indicators 2015/16 – Mid Year Update

Indicator	2015/16 Original Estimate £000's	2015/16 Current Position £000's	2015/16 Revised Estimate £000's
2015/16 Capital Expenditure	75,739	7,895	47,390
2015/16 Required Borrowing	47,304	1,800	25,708
2015/16 Capital Financing Requirement*	358,379	313,142	329,696
2015/16 Underlying Borrowing Requirement**	302,199	255,842	272,396
2015/16 Gross External Borrowing	289,602	228,524	236,892
Authorised Limit – Borrowing	334,101	358,304	358,304
Operational Boundary – Borrowing	302,199	286,018	286,018

** Includes on balance sheet PPP schemes.*
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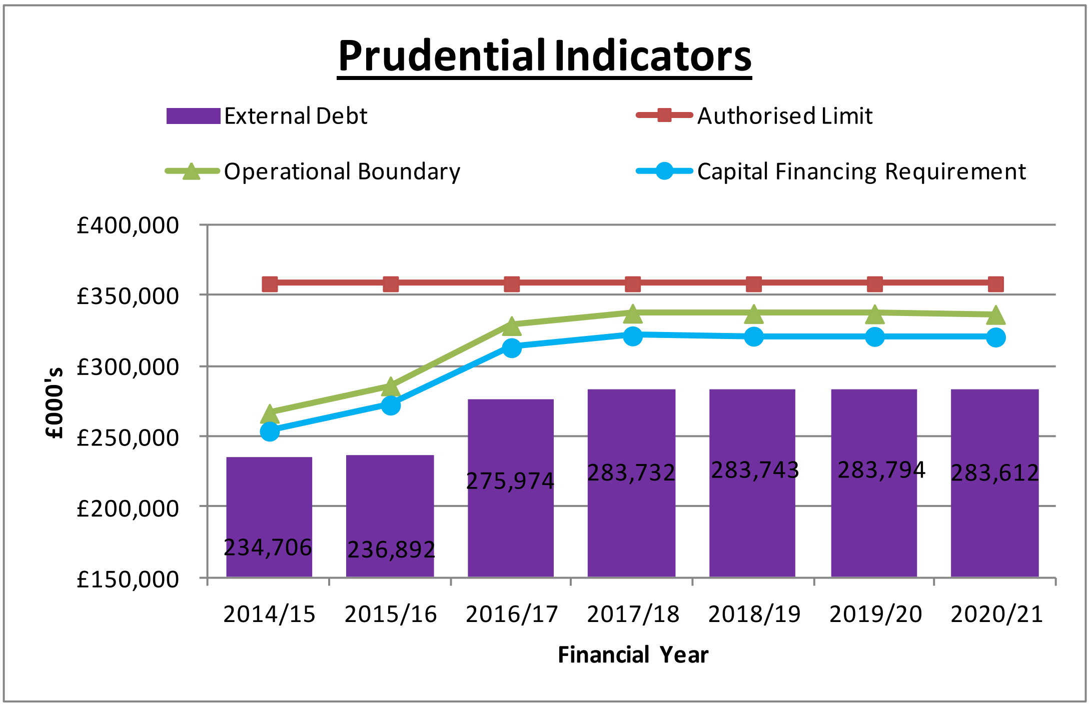

The **Capital Financing Requirement (CFR)** denotes the Council's underlying need to borrow for capital purposes. The CFR includes borrowing arising as a result of the Council's Capital Plans, plus the long-term liability arising from the Council's two PPP contracts. The Underlying Borrowing Requirement 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. This was recommended to be £334.1 million in the Treasury Strategy report presented to Council on 17 February 2015 and subsequently agreed by Council.

Rather than restrict external borrowing in the remainder of 2015/16 to:-

- the expected Underlying Borrowing Requirement for this year (£272.396 million); or
- the Authorised Limit for Borrowing of £334.101 million approved by Council on 17 February 2015;

it is proposed that permission be granted to borrow up to the authorised limit for borrowing of £358.304 million as at 31 March 2021 (as shown in the table below), if market conditions supported 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 2021 remains achievable.

Table 10: Authorised Limit for Borrowing: Calculation

Indicator	**2015/16 Original Estimate £000's**	**2015/16 Revised Estimate £000's**
CFR – General Services (31 March 2021)	120,268	117,295
CFR – HRA (31 March 2021)	194,001	204,760
Unrealised Capital Receipts & Developer Contributions 2015/16	2,785	5,280
Forecast level of Capital Receipts & Developer Contributions 2016/17 to 2020/21	17,047	30,969
Proposed Authorised Limit	**334,101**	**358,304**

6 Report Implications

6.1 Resource

Expenditure from Treasury Management activity i.e. loan charges, is reported in quarterly financial positions to Council, with Quarter 2 monitoring reflected in the Financial Monitoring 2015/16 – General Fund Revenue report elsewhere on today's agenda.

6.2 Risk

As the Council follows the requirements of the CIPFA Code of Practice for Treasury Management, and the Prudential Code, there is a reduced level of risks involved in Treasury Management activities. Those risks that do exist are further controlled through written Treasury Management Practices which define the responsibilities of all staff involved and these have recently been reviewed and updated.

6.3 Single Midlothian Plan and Business Transformation

Themes addresses 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

6.4 Impact on Performance and Outcomes

The strategies 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.

6.5 Adopting a Preventative Approach

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

6.6 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.

6.7 Ensuring Equalities

There are no equality issues arising from this report.

6.8 Supporting Sustainable Development

There are no sustainability issues arising from this report.

6.9 Digital Issues

There are no Digital Services implications arising from this report.

7 Summary

Treasury Management activity during the year to 15 October 2015 has been effective in maximising investment income and minimising borrowing costs within the parameters set by the strategy for the year.

There is no further long-term borrowing forecast for the remainder of 2015/16, reflective of the General Services and HRA capital plans reported elsewhere on today's agenda.

As a result of the revision to the maximum suggested duration for any investment with Lloyds Banking Group, Council officers have explored alternative counterparties and investment products in conjunction with the Council's treasury management advisers, Capita, and an illustration of some of the potential options available for investment is included in Table 6 in Section 4.

The Prudential Indicators have been updated to reflect current capital expenditure and income projections and the extension of the General Services Capital Plan to 2020/21.

8 Recommendations

It is recommended that Council:-

a) Note that the Financial Services team has achieved a better than benchmark return on investments for the period to 15 October 2015;
b) Note the report and the treasury activity undertaken in the period to 15 October 2015, as outlined in Section 3;
c) Note the forecast activity during the second-half of the year as outlined in Section 4, and the illustration of some of the potential options available for investment as outlined in Table 6;
d) Approve the revisions to the Prudential Indicators in Section 5 of this report.

20 October 2015

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Appendices

Appendix 1: Economic Update for first part of 2015/16 financial year
Appendix 2: PWLB Borrowing Rates 1 April 2015 to 30 September 2015
Appendix 3: Capita Asset Services Interest Rate Forecasts
Appendix 4: Prudential Indicators Detail

Appendix 1: Economic Update for first part of 2015/16 financial year

UK

UK GDP growth rates in 2013 of 2.2% and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and the 2015 growth rate is likely to be a leading rate in the G7 again, possibly being equal to that of the US. However, quarter 1 of 2015 was weak at +0.4% though there was a rebound in quarter 2 to +0.7%. The Bank of England's August Inflation Report included a forecast for growth to remain around 2.4 – 2.8% over the next three years. However, the subsequent forward looking Purchasing Manager's Index, (PMI), surveys in both September and early October for the services and manufacturing sectors showed a marked slowdown in the likely future overall rate of GDP growth to about +0.3% in quarter 4 from +0.5% in quarter 3. This is not too surprising given the appreciation of Sterling against the Euro and weak growth in the EU, China and emerging markets creating headwinds for UK exporters. Also, falls in business and consumer confidence in September, due to an increase in concerns for the economic outlook, could also contribute to a dampening of growth through weakening investment and consumer expenditure. For this recovery to become more balanced and sustainable in the longer term, the recovery still needs to move away from dependence on consumer expenditure and the housing market to manufacturing and investment expenditure. The strong growth since 2012 has resulted in unemployment falling quickly over the last few years although it has now ticked up recently after the Chancellor announced in July significant increases planned in the minimum (living) wage over the course of this Parliament.

The MPC has been particularly concerned that the squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of inflation in order to ensure that the recovery will be sustainable. It has therefore been encouraging in 2015 to see wage inflation rising significantly above CPI inflation which slipped back to zero in June and again in August However, with the price of oil taking a fresh downward direction and Iran expected to soon rejoin the world oil market after the impending lifting of sanctions, there could be several more months of low inflation still to come, especially as world commodity prices have generally been depressed by the Chinese economic downturn. The August Bank of England Inflation Report forecast was notably subdued with inflation barely getting back up to the 2% target within the 2-3 year time horizon. Despite average weekly earnings ticking up to 2.9% y/y in the three months ending in July, (as announced in mid-September), this was unlikely to provide ammunition for the MPC to take action to raise Bank Rate soon as labour productivity growth meant that net labour unit costs appeared to be only rising by about 1% y/y. However, at the start of October, statistics came out that annual labour cost growth had actually jumped sharply in quarter 2 from +0.3% to +2.2%: time will tell if this is just a blip or the start of a trend.

There are therefore considerable risks around whether inflation will rise in the near future as strongly and as quickly as previously expected; this will make it more difficult for the central banks of both the US and the UK to raise rates as soon as had previously been expected, especially given the recent major concerns around the slowdown in Chinese growth, the knock on impact on the earnings of emerging countries from falling oil and commodity prices, and the volatility we have seen in equity and bond markets in 2015 so far, which could potentially spill over to impact the real economies rather than just financial markets. On the other hand, there are also concerns around the fact that the central banks of the UK and US have few monetary policy options left to them given that central rates are near to zero and huge QE is already in place. There are therefore arguments that they need to raise rates sooner, rather than later, so as to have ammunition to use if there was a sudden second major financial crisis. But it is hardly likely that they would raise rates until they are sure that growth was securely embedded and 'noflation' was not a significant threat.

The forecast for the first increase in Bank Rate has therefore progressively been pushed back during 2015 from Q4 2015 to Q2 2016 and increases after that will be at a much slower pace, and to much lower levels than prevailed before 2008, as increases in Bank Rate will have a much bigger effect on heavily indebted consumers than they did before 2008.

The Government's revised Budget in July eased the pace of cut backs from achieving a budget surplus in 2018/19 to achieving that in 2019/20.

U.S.

GDP growth in 2014 of 2.4% was followed by first quarter 2015 growth depressed by exceptionally bad winter weather at only +0.6% (annualised). However, growth rebounded very strongly in Q2 to 3.9% (annualised) and strong growth was initially expected going forward. Until the turmoil in financial markets in August caused by fears about the slowdown in Chinese growth, it had been strongly expected that the Fed. might start to increase rates in September. However, the Fed pulled back from that first increase due to global risks which might depress US growth and put downward pressure on inflation, and due to a 20% appreciation of the dollar which has caused the Fed to lower its growth forecasts. Since then the nonfarm payrolls figures for September and revised August, issued on 2 October, were disappointingly weak and confirmed concerns that US growth is likely to significantly weaken. This has pushed back expectations of the first rate increase from 2015 into 2016.

Eurozone

The ECB fired its big bazooka by announcing a massive €1.1 trillion programme of quantitative easing in January 2015 to buy up high credit quality government debt of selected EZ countries. This programme started in March and will run to September 2016. This seems to have already had a beneficial impact in improving confidence and sentiment. There has also been a continuing trend of marginal increases in the GDP growth rate which hit 0.4% in quarter 1 2015 (1.0% y/y) and +0.4%, (1.5% y/y) in Q2 GDP. The ECB has also stated it would extend its QE programme if inflation failed to return to its target of 2% within this initial time period.

Greece. During July, Greece finally capitulated to EU demands to implement a major programme of austerity and is now cooperating fully with EU demands. An €86bn third bailout package has since been agreed though it did nothing to address the unsupportable size of total debt compared to GDP. However, huge damage has been done to the Greek banking system and economy by the resistance of the Syriza Government, elected in January, to EU demands. The surprise general election in September gave the Syriza government a mandate to stay in power to implement austerity measures. However, there are major doubts as to whether the size of cuts and degree of reforms required can be fully implemented and so Greek exit from the euro may only have been delayed by this latest bailout.

China and Japan

Japan is causing considerable concern as the increase in sales tax in April 2014 has suppressed consumer expenditure and growth. In Q2 2015 growth was -1.6% (annualised) after a short burst of strong growth of 4.5% in Q1. During 2015, Japan has been hit hard by the downturn in China. This does not bode well for Japan as the Abe government has already fired its first two arrows to try to stimulate recovery and a rise in inflation from near zero, but has dithered about firing the third, deregulation of protected and inefficient areas of the economy, due to political lobbies which have traditionally been supporters of Abe's party.

As for China, the Government has been very active during 2015 in implementing several stimulus measures to try to ensure the economy hits the growth target of 7% for the current year and to bring some stability after the major fall in the onshore Chinese stock market. Many commentators are concerned that recent growth figures around that figure could have been massaged to hide a downturn to a lower growth figure. There are also major concerns as to the creditworthiness of much bank lending to corporates and local government during the post 2008 credit expansion period and whether the bursting of a bubble in housing prices is drawing nearer. Overall, China is still expected to achieve a growth figure that the EU would be envious of. However, concerns about whether the Chinese cooling of the economy could be heading for a hard landing, and the volatility of the Chinese stock market, have caused major volatility in financial markets in August and September such that confidence is, at best, fragile.

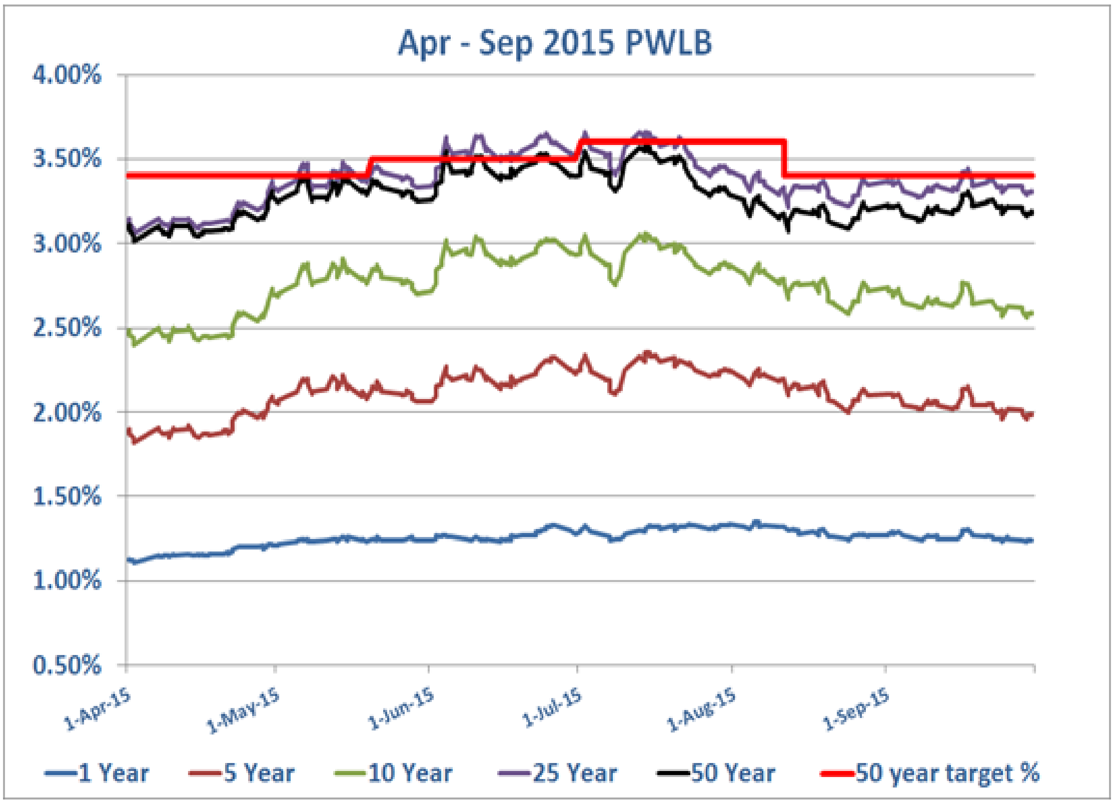
Emerging countries

There are considerable concerns about the vulnerability of some emerging countries and their corporates which are getting caught in a perfect storm. Having borrowed massively in western currency denominated debt since the financial crisis, caused by western investors searching for yield by channelling investment cash away from western economies with dismal growth, depressed bond yields (due to QE), and near zero interest rates, into emerging countries, there is now a strong current flowing to reverse that flow back to those western economies with strong growth and an imminent rise in interest rates and bond yields. This change in investors' strategy and the massive reverse cash flow, has depressed emerging country currencies and, together with a rise in expectations of a start to central interest rate increases in the US and UK, has helped to cause the dollar and sterling to appreciate. In turn, this has made it much more costly for emerging countries to service their western currency denominated debt at a time when their earnings from commodities are depressed. There are also going to be major issues when previously borrowed debt comes to maturity and requires refinancing at much more expensive rates, if available at all.

Corporates (worldwide) heavily involved in mineral extraction and / or the commodities market may also be at risk and this could also cause volatility in equities and safe haven flows to bonds. Financial markets may also be buffeted by sovereign wealth funds of countries highly exposed to falls in commodity prices which, therefore, may have to liquidate investments in order to cover national budget deficits.

Appendix 2: PWLB Borrowing Rates 1 April 2015 to 30 September 2015

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.11%	1.82%	2.40%	3.06%	3.01%
Date	02/04/2015	02/04/2015	02/04/2015	02/04/2015	02/04/2015
High	1.35%	2.35%	3.06%	3.66%	3.58%
Date	05/08/2015	14/07/2015	14/07/2015	02/07/2015	14/07/2015
Average	1.26%	2.12%	2.76%	3.39%	3.29%



Appendix 3: Capita Asset Services Interest Rate Forecasts

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18
Bank rate	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%
5yr PWLB rate	2.40%	2.50%	2.60%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%
10yr PWLB rate	3.00%	3.20%	3.30%	3.40%	3.50%	3.70%	3.80%	3.90%	4.00%	4.10%	4.20%
25yr PWLB rate	3.60%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%
50yr PWLB rate	3.60%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%

Capita Asset Services undertook its last review of interest rate forecasts on 11 August shortly after the quarterly Bank of England Inflation Report. Later in August, fears around the slowdown in China and Japan caused major volatility in equities and bonds and sparked a flight from equities into safe havens like gilts and so caused PWLB rates to fall below the above forecasts for quarter 4 2015. However, there is much volatility in rates as news ebbs and flows in negative or positive ways and news in September in respect of Volkswagen, and other corporates, has compounded downward pressure on equity prices. This latest forecast includes a first increase in Bank Rate in quarter 2 of 2016.

Despite market turbulence since late August causing a sharp downturn in PWLB rates, the overall trend in the longer term will be for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK when economic recovery is firmly established accompanied by rising inflation and consequent increases in Bank Rate, and the eventual unwinding of QE. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

The disappointing US nonfarm payrolls figures and UK PMI services figures at the beginning of October have served to reinforce a trend of increasing concerns that growth is likely to be significantly weaker than had previously been expected. This, therefore, has markedly increased concerns, both in the US and UK, that growth is only being achieved by monetary policy being highly aggressive with central rates at near zero and huge QE in place. In turn, this is also causing an increasing debate as to how realistic it will be for central banks to start on reversing such aggressive monetary policy until such time as strong growth rates are more firmly established and confidence increases that inflation is going to get back to around 2% within a 2-3 year time horizon. Market expectations in October for the first Bank Rate increase have therefore shifted back sharply into the second half of 2016.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
- UK economic growth turns significantly weaker than we currently anticipate.

- Weak growth or recession in the UK's main trading partners - the EU, US and China.
- A resurgence of the Eurozone sovereign debt crisis.
- Recapitalisation of European banks requiring more government financial support.
- Emerging country economies, currencies and corporates destabilised by falling commodity prices and / or the start of Fed. rate increases, causing a flight to safe havens

The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- Uncertainty around the risk of a UK exit from the EU.
- The ECB severely disappointing financial markets with a programme of asset purchases which proves insufficient to significantly stimulate growth in the EZ.
- The commencement by the US Federal Reserve of increases in the Fed. funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

Appendix 4 Prudential Indicators Detail

Prudential Indicator for Capital Expenditure

The table below shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the budget:-

Capital Expenditure by Service	**2015/16 Original Estimate £000's**	**Current Position £000's**	**2015/16 Revised Estimate £000's**
Resources	8,614	1,727	8,704
Education, Community & Economy	27,081	795	10,341
Health & Social Care	457	32	310
Council Transformation	0	387	1,025
HRA	39,587	4,954	27,010
Total	**75,739**	**7,895**	**47,390**

Forecast levels of capital expenditure on:-

- Resources has remained broadly in line with budget, with an acceleration of spend across the Digital Services projects offset by a rephasing of spend for the new recycling facility at Penicuik pending a decision on the depot review;
- Education, Community & Economy has decreased by £16.740 million to account for the rephasing of spend for the new Bilston, Gorebridge North, Paradykes & Roslin Primaries, and the removal of the capital contribution for the new Newbattle Centre;
- Health & Social Care has reduced by £0.147 million to reflect the budget saving for the new Penicuik Care Home hub project;
- HRA has decreased by £12.577 million to reflect the rephasing of the Phase II programme.

Prudential Indicator for the Financing of the Capital Programme & Borrowing

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (principal repayments). This direct borrowing need is also supplemented by maturing debt and other treasury requirements.

Capital Financing	**2015/16 Original Estimate £000's**	**Current Position £000's**	**2015/16 Revised Estimate £000's**
Total Capital Expenditure	**75,739**	**7,895**	**47,390**
Capital Grants	9,537	4,482	10,052
Capital Receipts	1,955	739	2,310
Capital Reserves	6,000	0	0
Developer Contributions	10,828	874	8,630
Other Contributions	115	0	688
Total Financing	**28,435**	**6,095**	**21,680**
Borrowing Required	**47,304**	**1,800**	**25,710**

Total expected financing has reduced from £28.435 million to £21.680 million, reflecting:-

- the removal of the Capital Contribution from the new Newbattle Centre (and therefore the utilisation of £6.0 million of capital fund monies);
- the utilisation of £0.280 million in Early Years Childcare funding to finance the Woodburn Family Learning Centre works;
- a reduction in the level of developer contributions that can be applied to finance the capital plan as a result of the realigning of expenditure on new school projects;
- an increase in the level of “other contributions”, reflecting the £0.526 million grant award from Zero Waste Scotland towards the Food Waste Collection roll-out.