

# Notice of Meeting and Agenda



## Audit Committee

**Venue:** Virtual Meeting,

**Date:** Monday, 22 June 2020

**Time:** 11:00

**Executive Director : Place**

**Contact:**

Clerk Name: Janet Ritchie

Clerk Telephone: 0131 271 3158

Clerk Email: [janet.ritchie@midlothian.gov.uk](mailto:janet.ritchie@midlothian.gov.uk)

**Further Information:**

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## **1 Welcome, Introductions and Apologies**

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## **2 Order of Business**

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

## **3 Declaration of Interest**

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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 Minute of Previous Meeting**

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**4.1** Minute of meeting of 10 March 2020 submitted for approval 5 - 12

**4.2** Action Log 13 - 14

## **5 Public Reports**

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**5.1** Internal Audit Work to March 2020 - Report by Chief Internal Auditor 15 - 20

**5.2** Internal Audit Annual Assurance Report 2019/20 - Report by Chief Internal Auditor 21 - 30

**5.3** Annual Governance Statement 2019/20 - Report by Chief Executive 31 - 40

**5.4** Counter Fraud Annual Report 2019/20 - Report by Chief Internal Auditor 41 - 60

**5.5** External Audit Plan Addendum – Report by E.Y. External Auditors (To Follow)

**5.6** Annual Treasury Management Report 2019/20 - Report by Chief Officer Corporate Solutions 61 - 94

**5.7** Financial Statement 2019/20 - Report by Chief Officer, Corporate Solutions 95 - 98

**5.8** Audit Committee Annual Report 2019/20 - Report by Chair of Audit Committee 99 - 116

## **6 Private Reports**

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No items for discussion

**7 Date of Next Meeting**

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To be confirmed



# Minute of Meeting

Audit Committee  
Monday 22 June 2020  
Item No: 4.1



## Audit Committee

Date	Time	Venue
Tuesday 10 March 2020	11.00am	Council Chambers, Midlothian House, Dalkeith, EH22 1DN

### Present:

Mike Ramsay (Independent Chair)
Councillor Hardie
Councillor Milligan
Councillor Muirhead
Councillor Smail
Councillor Alexander (Substitute)
Councillor Cassidy (Substitute)

### In attendance:

Grace Vickers	Chief Executive
Kevin Anderson	Executive Director Place
Joan Tranent	Chief Officer, Children's Services, Partnerships and Communities
Alison White	Head of Adult Health and Social Care
Gary Fairley	Chief Officer Corporate Solutions
Alan Turpie	Legal Services Manager/Monitoring Officer
Grace Scanlin	External Auditor, EY
Jill Stacey	Chief Internal Auditor
Chris Lawson	Waste, Risk and Resilience Manager
Janet R Ritchie	Democratic Services Officer

## 1. Welcome and Apologies

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The Chair, Mike Ramsay welcomed everyone to the meeting, following which there was a round of introductions.

Apologies were received from Councillor Baird, Councillor Parry and the Independent Member, Mr Peter de Vink.

## 2. Order of Business

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The order of business was confirmed as that outlined in the Agenda.

## 3. Declarations of interest

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No declarations of interest were received.

## 4. Minutes of Previous Meetings

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4.1 The minute of the meeting of 28 January 2020 was submitted and approved as a correct record having been proposed by Councillor Smaill, seconded by Councillor Murihead.

4.2 The Action log was submitted and the following agreed:

- 1) 'Internal Audit Recommendations' - Two follow-up reports per year to Audit Committee as per approved Internal Audit Annual Plan – Noted.
- 2) 'Treasury Management and Investment Strategy 2020/21 & Prudential Indicators – Strategy was approved by full Council on 11 February 2020 - Closed.

## 5. Public Reports

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Report No.	Report Title	Presented by:
5.1	Midlothian Council Annual Audit Plan - Report by External Auditors	Stephen Reid and Grace Scanlin, External Auditors, EY
Outline of report and summary of discussion		
<p>The External Auditors submitted their Annual Audit Plan 2019/20. Stephen Reid External Auditor advised the Committee that prior to presenting this report they would provide a short slide presentation on 'Audit market reform and revised auditing standards and guidance' to inform the Committee of the audit reform which was currently taking place now and likely to take place over the next 5 years.</p> <p>He further advised that over the last 2 years there has been a number of significant corporate failures and as a result of that a number of reviews had been launched into the role of Audit, the role of Directors in companies and also into the responsibilities of Audit Committees and other governance Committees within corporate environments.</p>		

Mr Reid presented the following slides which are appended to this minute:

- Next steps regarding the key regulatory and independent reviews – January 2020.
- Potential outcomes of regulatory reviews – January 2020
- CMA four key recommendations: potential implications
- Brydon recommendations
- Board considerations

Mr Reid then presented the External Annual Audit Plan advising the Committee that this Annual Audit Plan prepared for the benefit of Council management and the Audit Committee, sets out their proposed audit approach for the audit of the financial year ending 31 March 2020, the fourth year of their appointment. In preparing this plan, they had updated their understanding of the Council through planning discussions with management, review of relevant documentation and committee reports, and their general understanding of the environment in which the Council is currently operating. He went on to explain that their responsibilities fell into two main areas, one in respect of the financial statements and the other in respect of their responsibility around the wider-scope public sector audit dimensions and highlighted some key sections from the Report.

Thereafter the External Auditors responded to questions and comments raised by members of the Committee.

#### Decision

The Audit Committee noted the content of the report.

Report No.	Report Title	Presented by:
5.2	Audit Scotland City Region Deal and Growth Deals	Ian Johnson, Head of Major Projects
Outline of report and summary of discussion		
<p>Mr Johnson provided the committee with a brief update on City Deal advising that the Edinburgh and South East Scotland City Region Deal is one of a number of City Region and Growth deals in Scotland and across the UK. The aim of these was to grow the economy of the region in an inclusive way so that all parts of the region benefits. The City Region Deal for this region was signed in August 2018 and will be a 15 year programme. He provided further information on the Council partners and regional partners, details of the total expenditure to the programme, the number of key elements and the Governance structure.</p> <p>Mr Johnson highlighted that the Audit Scotland report provides an early assessment of City Region and Growth Deals in Scotland, rather than the performance of individual Deals. He advised that the Audit Scotland report went to the Joint Committee on 6 March 2020 and that the recommendations were approved.</p>		

Mr Johnson also updated the Committee on the Audit Scotland recommendations and the comments which were relevant to Midlothian.

Thereafter he responded to questions and comments from the Members of the Committee.

#### Decision

The Audit Committee noted the contents of the Report.

Report No.	Report Title	Presented by:
5.3	Risk Management Update 1 October 2019 – 31 December 2019.	Chris Lawson, Waste, Risk and Resilience Manager
Outline of presentation and summary of discussion		
<p>The Risk Manager presented a report dated 25 February 2020 providing the Audit Committee with the 2019/20 Quarter 3 Strategic Risk Management update, covering the period 1 October 2019 to 31 December 2019. The Strategic Risk Profile sought to provide a strategic look at the current issues and future risks and opportunities facing the Council.</p> <p>The Risk Manager highlighted the main sections contained within the report and responded to questions raised by members of the committee which included:</p> <ul style="list-style-type: none"><li>• The motion raised at Council regarding Climate emergency.</li><li>• Financial sustainability for future years being a medium risk and how the scoring of risks interpretation differs from the External Auditor's report.</li></ul> <p>Mr Lawson provided feedback on both issues explaining that work is already underway for quarter 4 regarding Climate change and that with regards to the motion that went to council more work will take place to reflect this.</p> <p>With regards to the Financial sustainability he advised that this was a risk that had sat higher in the risk register but in the last year there had been significant efforts undertaken to manage the Council's longer term financial position and significant work underway in terms of the Medium Term Financial Strategy. He further advised that this will continue to be monitored and as the work of the Medium Term Financial Strategy develops the position will continue to be reflected on the risk register.</p>		
Decision		
Audit Committee noted the quarter 3 2019/20 Strategic Risk Profile report and considered the current response to the issues, risks and opportunities highlighted.		



Report No.	Report Title	Presented by:
5.4	Internal Audit Work to February 2020	Jill Stacey, Chief Internal Auditor
<b>Outline of presentation and summary of discussion</b>		
<p>The purpose of this report was to provide members of the Audit Committee with details of the recent work carried out by Internal Audit and the findings and recommended audit actions agreed by Management to improve internal controls and governance arrangements.</p> <p>Internal Audit issued final assurance reports on the following subjects:</p> <ul style="list-style-type: none"> <li>• Procurement and Management of Contracts</li> <li>• Change and Transformation Programme</li> <li>• Business Planning, Budget Setting and Monitoring</li> </ul> <p>An Executive Summary of the final Internal Audit assurance report issued, including audit objective, findings, good practice and recommendations (where appropriate), and the Chief Internal Auditor's independent and objective opinion on the adequacy of the control environment and governance arrangements within each audit area, is shown in Appendix 1.</p> <p>The Chief Internal Auditor presented the report highlighting the main sections contained within the report and provided the Committee with a brief update of each individual audit report during which the members of the committee raised questions and comments relating to each of these.</p> <p>Several Members had raised concerns regarding the value of the 22 expired contracts and the responsibility of management to ensure these contracts are retendered. After a lengthy discussion regarding Procurement and Contract management it was agreed that a detailed report would be prepared regarding these 22 expired contracts. It was also highlighted that Officers were continuing to look at different approaches to improve services and opportunities to work jointly with other local authorities and that discussions were taking place with Scottish Borders in particular with regards to Procurement and Contract management.</p> <p>In responding to questions regarding the savings which had not been achieved, Officers highlighted that after a large piece of work with the finance team, savings which were not realistic were identified and robust recovery plans were put in place. In addition to this, a Budget Monitoring Board was set up which included Chief Officers and Accountants and that they worked closely together to ensure the projects could deliver the agreed savings. Officers also gave further assurances that the 2020/21 Budget set on 11 February 2020 was more robust than in previous years and the expectation is that services will deliver within budget. Further clarity was provided on the slippage in previous years which impacted on the transformation savings and that the Medium Term Financial Strategy related to the 2020/21 budget onwards. Officers also stressed that the assurance reports were completed in November 2019 and that considerable improvements had been put in place since then.</p>		

Decision
<p>The Audit Committee;</p> <ul style="list-style-type: none"> <li>a) Noted the final assurance reports issued in the period from 1 January to 20 February 2020 associated with the delivery of the approved Internal Audit Annual Plan 2019/20; and</li> <li>b) Acknowledged the assurance provided on internal controls and governance arrangements in place for the areas covered by this Internal Audit work.</li> <li>c) Noted that a detailed report would be provided to Members on the 22 expired contracts.</li> </ul>
Action
Legal Services Manager

Report No.	Report Title	Presented by:
5.5	Internal Audit Charter	Jill Stacey, Chief Internal Auditor
Outline of presentation and summary of discussion		
<p>There was a report submitted dated 12 February 2020 which provided the Audit Committee with the updated Internal Audit Charter for approval that defines the terms of reference for the Internal Audit function to carry out its role to enable the Chief Internal Auditor to prepare annual opinions on the adequacy of the overall control environment for Midlothian Council, and for Midlothian Health and Social Care Integration Joint Board.</p> <p>The Chief Internal Auditor presented this report highlighting the main sections contained within the report and advised that Appendix 1 details the Internal Audit Charter and provided a brief overview of this.</p>		
Decision		
<p>The Audit Committee:</p> <ul style="list-style-type: none"> <li>• Noted the changes outlined in this report.</li> <li>• Approved the revised Internal Audit Charter shown at Appendix 1.</li> <li>• Noted that the Internal Audit Charter will be reviewed annually.</li> </ul>		

Report No.	Report Title	Presented by:
5.6	Internal Audit Strategy and Annual Plan 2020/21	Jill Stacey, Chief Internal Auditor
Outline of presentation and summary of discussion		
<p>There was a report submitted dated 13 February 2020 the purpose of which was to gain approval to the proposed Internal Audit Strategy and Annual Plan 2020/21 to enable the Chief Internal Auditor to prepare annual opinions on the adequacy of</p>		

the overall control environment for Midlothian Council and Midlothian Health and Social Care Integration Joint Board.

The Chief Internal Auditor presented this report highlighting the main sections contained within the report and advised that Appendix 1 details the Internal Audit Strategy and Appendix 2 details Midlothian Council Internal Audit Annual Plan 2020/21.

Thereafter the Chief Internal Auditor responded to questions and comments raised by the Committee.

#### **Decision**

The Audit Committee approved the Internal Audit Strategy (Appendix 1) and the Annual Plan 2020/21 (Appendix 2).

## **6. Private Reports**

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No private reports were submitted.

## **7. Date of Next Meeting**

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The next meeting will be held on Tuesday 22 June 2020 at 11 am

The meeting terminated at 12.50 pm



# Actions Log

Audit Committee  
Monday 22 June 2020  
Item No: 4.2



No	Subject	Date	Action	Action Owner	Expected completion date	Comments
1	Internal Audit Recommendations	03/12/2019	Internal Audit will continue to monitor for completion the outstanding recommendations and will provide update reports to the Audit Committee.	Chief Internal Auditor	June 2020	Two follow-up reports per year to Audit Committee as per approved Internal Audit Annual Plan
2	Internal Audit Work	10/03/2020	Noted that a detailed report would be provided to Members on the 22 expired contracts	Legal Services Manager	September 2020	
3						
4						



**Internal Audit Work to March 2020**  
**Report by Chief Internal Auditor****1. Purpose of the Report**

The purpose of this report is to provide members of the Audit Committee with details of the recent work carried out by Internal Audit and the findings and recommended audit actions agreed by Management to improve internal controls and governance arrangements.

**2. Progress Report**

- 2.1 The Internal Audit Annual Plan 2019/20 was approved by the Audit Committee on 12 March 2019. Internal Audit has carried out the following work in the period from 21 February to 31 March 2020 associated with the delivery of the Plan to meet its objective of providing an opinion on the efficacy of the Council's risk management, internal control and governance.
- 2.2 The MLC Internal Audit function conforms to the professional standards as set out in Public Sector Internal Audit Standards (PSIAS) (2017) including the production of this report to communicate the results of the reviews.
- 2.3 Internal Audit issued final assurance reports on the following subject:
- Community Empowerment
- 2.4 An Executive Summary of the final Internal Audit assurance report issued, including audit objective, findings, good practice and recommendations (where appropriate), and the Chief Internal Auditor's independent and objective opinion on the adequacy of the control environment and governance arrangements within each audit area, is shown in Appendix 1.

The definitions for Internal Audit assurance categories are as follows:

Level	Definition
Comprehensive assurance	Sound risk, control, and governance systems are in place. These should be effective in mitigating risks to the achievement of objectives. Some improvements in a few, relatively minor, areas may be required.
Substantial assurance	Largely satisfactory risk, control, and governance systems are in place. There is, however, some scope for improvement as current arrangements could undermine the achievement of objectives or leave them vulnerable to error or misuse.
Limited assurance	Risk, control, and governance systems have some satisfactory aspects. There are, however, some significant weaknesses likely to undermine the achievement of objectives and leave them vulnerable to an unacceptable risk of error or misuse.
No assurance	The systems for risk, control, and governance are ineffectively designed and operated. Objectives are not being achieved and the risk of serious error or misuse is unacceptable. Significant improvements are required.

## Other Internal Audit Assurance Work in Progress

- 2.5 Internal Audit issued a draft assurance report on the following subject and were awaiting Management Responses at the time that the Covid-19 emergency response put extraordinary pressures on Management to deliver business critical services:

- ICT Operational Processes

Internal Audit also completed the audit fieldwork for the following and drafted the reports though these were not issued for the same reason above:

- Leisure Management Booking System
- Information Governance – Records Management

These three audits will be pending until there is Management capacity post-Covid-19 emergency response to conclude to final report stage.

- 2.6 On request by Chief Executive and Strategic Covid-19 Locality Support Manager an agile Internal Audit was carried out on the arrangements in place to administer food grants and localised partnership grants to community groups on behalf of Scottish Government. Reasonable assurance can be provided on the adequacy of the internal controls and governance arrangements in place. Some suggestions were made for Management consideration in further phases.

## Recommendations

- 2.7 Recommendations in reports are suggested changes to existing procedures or processes to improve the controls or to introduce controls where none exist. The grading of each recommendation reflects the risk assessment of non-implementation, being the product of the likelihood of the risk materialising and its impact:

<b>High:</b> Significant weaknesses in existing controls, leaving the Council or Service open to error, fraud, financial loss or reputational damage, where the risk is sufficiently high to require immediate action within one month of formally raising the issue. Added to the relevant Risk Register and included in the relevant Assurance Statement.
<b>Medium:</b> Substantial weaknesses in existing controls, leaving the Council or Service open to medium risk of error, fraud, financial loss or reputational damage requiring reasonably urgent action within three months of formally raising the issue.
<b>Low:</b> Moderate weaknesses in existing controls, leaving the Council or Service open to low risk of error, fraud, financial loss or reputational damage requiring action within six months of formally raising the issue to improve efficiency, effectiveness and economy of operations or which otherwise require to be brought to attention of senior management.
Outwith the report, Internal Audit informs operational managers about other matters as part of continuous improvement.

- 2.8 The table below summarises the number of Internal Audit recommendations made during 2019/20:

	2019/20 Number of Recs
High	0
Medium	0
Low	0
<b>Sub-total reported this period</b>	<b>0</b>
Previously reported	48
<b>Total</b>	<b>48</b>
Recommendations agreed with action plan	48
Not agreed; risk accepted	0
<b>Total</b>	<b>48</b>



### **3. Report Implications**

#### **3.1 Resource**

Resource implications of implementing Internal Audit recommendations are considered as part of the audit process to ensure these are reasonable and proportionate to the risks.

#### **3.2 Risk**

The PSIAS require Internal Audit to evaluate the effectiveness of the Council's Risk Management arrangements and contribute to improvements in the process. At the start of each audit engagement, to capture potential areas of risk and uncertainty more fully, key stakeholders have been consulted and risk registers have been considered. During each audit engagement the management of risk has been tested.

It is anticipated that improvements in the management and mitigation of risks will arise as a direct result of Management implementing the Internal Audit recommendations made. If audit recommendations are not implemented, there is a greater risk of financial loss and/or reduced operational efficiency and effectiveness, and Management may not be able to demonstrate improvement in internal control and governance arrangements, and effective management of risks.

#### **3.3 Single Midlothian Plan**

Themes addressed in this report:

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

#### **3.4 Key Priorities within the Single Midlothian Plan**

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

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

#### **3.5 Impact on Performance and Outcomes**

The Findings and Recommendations from Internal Audit work during the year assists the Council in improving its performance and outcomes.

### **3.6 Adopting a Preventative Approach**

Internal Audit assurance work includes assessments on when a preventative approach can be adopted.

### **3.7 Involving Communities and Other Stakeholders**

This report has been presented to the Corporate Management Team (SRG 3 June 2020) to outline the key messages of assurance and areas of improvement. Executive Directors, Chief Officers and Service Managers relevant to the area audited have agreed the final Internal Audit reports as set out in the relevant Executive Summary within Appendix 1.

### **3.8 Ensuring Equalities**

There are no equalities issues with regard to this report.

### **3.9 Supporting Sustainable Development**

There are no sustainability issues with regard to this report.

### **3.10 IT Issues**

There are no IT issues with regard to this report.

## **4. Recommendations**

The Audit Committee is asked to:

- a) Note the final assurance reports issued in the period from 21 February to 31 March 2020 associated with the delivery of the approved Internal Audit Annual Plan 2019/20; and
- b) Acknowledge the assurance provided on internal controls and governance arrangements in place for the areas covered by this Internal Audit work.

**Date:** 14 May 2020  
**Report Authors:** Jill Stacey, Chief Internal Auditor  
**E-Mail:** [Jill.Stacey@midlothian.gov.uk](mailto:Jill.Stacey@midlothian.gov.uk)

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
<p>Subject: Community Empowerment</p> <p>Category: Assurance</p> <p>Date issued: 5 March 2020 Draft; 17 March 2020 Final</p> <p>Level of Assurance: Substantial</p>	<p>The purpose of the review was to review the implementation of the requirements of the Community Empowerment (Scotland) Act 2015.</p> <p>The requirements of the Act broadly fall into 3 parts:</p> <ul style="list-style-type: none"> <li>• powers of Scottish Ministers to make future regulations,</li> <li>• the duty of the Community Planning Partnership (CPP) to prepare and publish a local outcomes improvement plan (LOIP) which sets out the local outcomes which will prioritise for improvement as well as produce locality plans at a more local level for areas experiencing particular disadvantage; and</li> <li>• the grant of various specified opportunities and rights to the citizens of Midlothian.</li> </ul> <p>Success in implementing the requirements of the Act and for the community to obtain the Act's intended benefits depends upon: partners encouraging and facilitating community participation and building the capacity of the community; and the ambitions of the community. This will take time given the small numbers of community volunteers and the Council's limited resources, the latter being only one of the CPP partners.</p> <p>The Community Planning Partnership (CPP) has prepared and published a local outcomes improvement plan (LOIP) - 'The Single Midlothian Plan' and locality plans following consultation with the community.</p> <p>Good progress has been made with implementing the other requirements of the Act.</p> <p>Reporting requirements are set out in the Community Empowerment Act (Parts 2, 3 and 5) which stipulates the frequency, content and publication of reports. Reports have been produced and published in accordance with the legislation.</p> <p>Internal Audit considers that the level of assurance we are able to give is Substantial Assurance (Largely satisfactory risk, control, and governance systems are in place. There is, however, some scope for improvement as current arrangements could undermine the achievement of objectives). Management are working on actions to address two issues. We made no recommendations.</p>	0	0	0	Management have confirmed the factual accuracy of the report and accepted the report findings.



**Internal Audit Annual Assurance Report 2019/20**  
**Report by Chief Internal Auditor****1. Purpose of the Report**

- 1.1 The purpose of this report is to present to the Audit Committee the Internal Audit Annual Assurance Report for the year to 31 March 2020 which includes the Chief Internal Auditor's independent assurance opinion on the adequacy of Midlothian Council's overall control environment.

**2. Background**

- 2.1 The Local Authority Accounts (Scotland) Regulations 2014 that came into force on 10 October 2014 require a local authority to operate a professional and objective internal auditing service. This service must be provided in accordance with recognised standards and practices in relation to internal auditing. Recognised standards and practices are those set out in the *Public Sector Internal Audit Standards: Applying the IIA International Standards to the UK Public Sector* (PSIAS). The standards require internal audit to have suitable operational independence from the organisation.
- 2.2 The Public Sector Internal Audit Standards (PSIAS) 2017 require that: "The chief audit executive [MLC's Chief Internal Auditor] must deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement. The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control. The annual report must incorporate:
- the opinion;
  - a summary of the work that supports the opinion; and
  - a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme."
- 2.3 The Terms of Reference of the Midlothian Council Audit Committee states:
1. The Audit Committee is a key component of Midlothian Council's corporate governance. It provides an independent and high-level focus on the audit, assurance and reporting arrangements that underpin good governance and financial standards.
  2. The purpose of the Audit Committee is to provide independent assurance to Elected Members of the adequacy of the risk management framework and the internal control environment. It

provides independent review of Midlothian Council's governance, risk management and control frameworks, and oversees the financial reporting and annual governance processes. It oversees Internal and External Audit, helping to ensure efficient and effective assurance arrangements are in place.

### **3. Internal Audit Annual Assurance Report 2019/20**

- 3.1 The Internal Audit Annual Assurance Report 2019/20, at Appendix 1, includes the Chief Internal Auditor's independent and objective opinion regarding the adequacy and effectiveness of internal control within Midlothian Council to fulfil the statutory role of Internal Audit, provides details of the Internal Audit activity that supports the opinion and of the performance during the year, and summarises the outcomes of assessments of the Internal Audit service against the Public Sector Internal Audit Standards.
- 3.2 The Internal Audit Annual Assurance Report 2019/20 provides assurances in relation to the Council's corporate governance framework that is a key component in underpinning delivery of the corporate priorities within the Single Midlothian Plan and has been used to inform the Annual Governance Statement 2019/20.

### **4. Report Implications**

#### **4.1 Resource**

The Internal Audit function reports directly to the Chief Executive (operationally) and the Audit Committee (functionally). Staff resources have been adversely affected during the year, mostly notably due the continued deployment of Internal Audit and Counter Fraud resources to the ongoing counter fraud activity and in March 2020 due to the Council's emergency response associated with COVID-19. This has had an impact on the delivery of the Internal Audit planned work which is reflected in the Internal Audit Annual Assurance Report 2019/20 (Appendix 1).

There is a commitment by Midlothian Council to provide Internal Audit resources to the Midlothian Health and Social Care Integration Joint Board (MIJB) and audit work was undertaken during the year to meet that commitment. A separate annual assurance report will be presented to MIJB Audit and Risk Committee and MIJB to fulfil that role.

#### **4.2 Risk**

The PSIAS require Internal Audit to evaluate the effectiveness of the Council's Risk Management arrangements and contribute to improvements in the process. Each Internal Audit engagement has been risk-based and, where appropriate, has tested the specific Service's management of risk.

Internal Audit provides assurance to the Corporate Management Team and the Audit Committee on the adequacy and effectiveness of internal controls and governance within the Council, including risk

management, and to highlight good practice and recommend improvements. Key components of the audit planning process include a clear understanding of the Council's functions, associated risks, and range and breadth of audit areas for inclusion within the Annual Plan.

Improvements in internal controls and governance arrangements can be demonstrated through Management-initiated actions complemented by the implementation of Audit recommendations.

It is anticipated that further improvements in the management and mitigation of risks will arise as a direct result of Management implementing the Internal Audit recommendations made during the year or outstanding from previous years which will enable Management to demonstrate further improvement in internal controls and governance arrangements.

Delivery of the Internal Audit services in conformance with the PSIAS will enable the Council to meet the requirements of the Local Authority Accounts (Scotland) Regulations 2014 to consider the findings of assessments as part of the consideration of the system of internal control required by regulation 5.

#### **4.3 Single Midlothian Plan**

Themes addressed in this report:

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

#### **4.4 Key Priorities within the Single Midlothian Plan**

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

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

#### **4.5 Impact on Performance and Outcomes**

The Findings and Recommendations from Internal Audit work during the year assists the Council in improving its performance and outcomes.

#### **4.6 Adopting a Preventative Approach**

Internal Audit assurance work includes assessments on when a preventative approach can be adopted.

#### **4.7 Involving Communities and Other Stakeholders**

The Internal Audit Annual Assurance Report 2019/20 has been presented to senior management at an SRG meeting on 3 June 2020 (comprising Chief Executive, Executive Directors, Chief Officers and Heads of Service) to outline the key messages of assurance and areas of improvement, and have been advised to take this into account when completing their annual self-evaluation and assurance process for the Council's Annual Governance Statement 2019/20.

#### **4.8 Ensuring Equalities**

There are no equalities issues with regard to this report.

#### **4.9 Supporting Sustainable Development**

There are no sustainability issues with regard to this report.

#### **4.10 IT Issues**

There are no IT issues with regard to this report.

### **5. Recommendations**

The Audit Committee is therefore asked to consider the Internal Audit Annual Assurance Report 2019/20 (Appendix 1), and assurances contained therein, and to provide any commentary thereon.

**Date:** 14 May 2020  
**Report Authors:** Jill Stacey, Chief Internal Auditor  
**E-Mail:** [Jill.Stacey@midlothian.gov.uk](mailto:Jill.Stacey@midlothian.gov.uk)



## **Chief Internal Auditor's Annual Assurance Report and Opinion 2019/20 for Midlothian Council**

### **1 Introduction**

- 1.1 It is Management's responsibility to design and maintain proper risk management, governance and internal control processes and systems to ensure probity in systems and operations, including the prevention, detection and resolution of fraud and irregularities. Management is also responsible for checking that the arrangements and controls are operating effectively. These are known as the first and second lines of defence which are not fixed but evolve as the Council changes.
- 1.2 Internal Audit, as the third line of defence, is an independent appraisal function established for the review of the internal control system as a service to Midlothian Council. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources and the management of risk.
- 1.3 The Internal Audit activity adds value to the organisation (and its stakeholders) when it considers strategies, objectives, and risks; strives to offer ways to enhance governance, risk management and control processes; and objectively provides relevant assurance.
- 1.4 The Objectives of Internal Audit are set out in its Charter: "As part of Midlothian Council's system of corporate governance, Internal Audit's purpose is to support the Council in its activities designed to achieve its declared objectives and to do so:
- In support of the Council's vision, values and priorities.
  - As a contribution to the Council's corporate management of risk.
  - As an aid to ensuring that the Council and its elected members, employees and contracted third parties are operating within the law and relevant regulations.
  - As a contribution towards establishing and maintaining a culture of honesty, integrity, openness, accountability and transparency throughout the Council in all its activities and transactions.
  - As a contribution towards ensuring that financial statements and other published information are accurate and reliable."
- 1.5 The Public Sector Internal Audit Standards (PSIAS) (2017) requires that:
- "The chief audit executive must deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement.
- The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.
- The annual report must incorporate:
- the opinion;
  - a summary of the work that supports the opinion; and
  - a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme."
- 1.6 This Annual Assurance Report provides the annual internal audit opinion to fulfil the statutory role of Internal Audit and summarises the work carried out by Internal Audit during the year to 31 March 2020 that underpins the opinion in accordance with the Internal Audit Charter, Strategy and Annual Plan. The report also states the outcomes of assessments of the Internal Audit service against the PSIAS.

## **2 Opinion on the systems of Internal Control, Risk Management and Governance**

- 2.1 My opinion is that, based on our reviews, risk assessments and knowledge, the systems of internal control and governance are generally adequate with improvements having been made during the year. The implementation of further Audit recommendations as part of a culture of continuous improvement is of importance particularly relating to the strategic governance arrangements that underpin procurement and contract management, financial management, workforce development, and delivery of change and transformation.
- 2.2 The Council's Local Code of Corporate Governance (approved December 2017) complies with the CIPFA/SOLACE Framework 'Delivering Good Governance in Local Government' (2016). The Local Code has been updated as part of Internal Audit's assessment of internal control and governance to include comprehensive evidence against each of the seven principles of good governance and sub-principles. The updated Local Code will require approval by Council to ensure this key document continues to be relevant and complete to reflect the appropriate framework for effective governance of the Council's affairs and facilitate the exercise of its functions to deliver best value.
- 2.3 The Council recognises that Risk Management is an integral part of all activities and has Corporate and Service Risk Registers in place which are subject to regular review by those Managers who are allocated the responsibilities for managing individual risks. The Audit Committee received reports from the Risk Manager each quarter outlining corporate risks and mitigations to fulfil its oversight role to monitor the effective development and operation of risk management in the Council, though Members were not aware of when the Risk Management Policy and Strategy were most recently reviewed and scrutinised.
- 2.4 The Financial Regulations (approved July 2012), and associated policies, procedures and guidelines need to be reviewed, updated and developed, as appropriate, to reflect changes arising from organisation structures and systems and then be kept under regular review.
- 2.5 Improvements over the Council's capital planning arrangements are required to apply the Accounts Commission good practice guide 'Major capital investment in Councils'. A long term Capital Investment Strategy is in place. The Capital Plan and Asset Management Board (CPAMB) agreed to subject new Capital projects >£1M to a gateway review. The timeframes of the underlying Asset Strategies require aligning and Asset Management Plans require updating before projects can be effectively prioritised. The CPAMB should focus on its roles and responsibilities within its terms of reference to provide more effective scrutiny and challenge for capital planning, ensuring that projects included in the plan fit with strategic priorities and are affordable and realistically deliverable within stated timescales.
- 2.6 Further improvements in internal control, risk management and governance have been agreed by Management as highlighted in Internal Audit reports and recommendations made during the year or outstanding from previous years.
- 2.7 The significant incident which commenced in late March 2020 in response to the Covid-19 pandemic tested how well the risk management framework is operating. There were examples of innovations, new business processes and solutions, and new technology being embraced in order to deliver services to the community in the Council's role as Category 1 responder to carry out the following three essential functions: Caring for the Vulnerable; Liaising with Resilience Partners; and Supporting Economic Recovery. This was achieved using amended governance arrangements, new ways of decision-making, leadership and implementation including virtual meetings, conference calls, and systems remote access. Internal Audit were suitably informed of or engaged in changes in governance and internal controls. It will be important for the Council, at the appropriate time, to carry out a post-incident review and highlight any lessons learned.

### 3 Internal Audit Annual Plan 2019/20 Delivery

- 3.1 Internal Audit staff resources had been adversely affected during the first half of the year, mostly notably due the continued deployment, over and above the Plan Days, of Internal Audit resources to the ongoing corporate fraud investigations. This had reduced Internal Audit output during the first half of the year. The continuation of the Interim Internal Auditor to offset the full deployment of the two Fraud and Audit Officers on investigations and other corporate fraud work (non-Internal Audit work) in the second half of the year has enabled the completion of delayed work at the half year and the remaining planned audit work with one exception. In March 2020, due to the Council's emergency response associated with COVID-19 pandemic and adherence to national guidelines, the whole team were working from home. This has had a minor impact on the delivery of the Internal Audit planned work mainly due to the time of year.
- 3.2 The following Audit from the 2019/20 Audit Plan has not been carried out as a result of a request by Management to delay due to the Council's Covid-19 emergency response:
- Automated Invoice Payments (Deferred to 2020/21 though Internal Audit staff undertook training in early March 2020 on the system-based authorisation controls, including segregation of duties, and security controls over payments).
- 3.3 The range and breadth of Internal Audit work that has been performed during the year, which is listed below, is sufficient to inform the Internal Audit assurance on the systems of internal control, governance arrangements and risk management. For one audit marked^ the draft report was issued and Management Responses were awaited and for two audits marked\* the draft reports were not issued; these will be pending until there is Management capacity, post-Covid-19 incident, to conclude to the finalisation of reports:

#### **Strategic and Risk Based Audits**

- 3.4 To provide assurance on the internal controls, risk management and governance arrangements in place to ensure efficient and effective use of assets and resources and achievement of strategic objectives, reviews included:
- Change and Transformation Programme (Monitor implementation of improvements to the governance and accountability arrangements for the change and transformation programme including processes for benefit (financial and other) identification, tracking and realisation).
  - Business Planning, Budget Setting and Monitoring (Evaluate the implementation of improvements to ensure that budgets set for 2019/20 are sustainable and based on realistic plans, and that appropriate scrutiny and challenge is undertaken on revenue budget monitoring reports to enable service delivery within approved budget).
  - Workforce Planning (Follow-up on implementation of previous recommendations to improve workforce strategy and planning processes to provide skills, knowledge and competency requirements for service delivery to meet the Council's objectives).
  - Procurement and Management of Contracts (Review the processes and internal controls relating to the procurement journey to ensure these adequately address the key risks, and assess compliance with the procurement framework and adequacy of contract monitoring arrangements).
  - Information Governance – Records Management (Review the Information Governance framework, specifically on the theme of Records Management i.e. Plan and actions to comply with good practice)\*
  - Capital Investment (High level review of the established control framework and governance arrangements in place to plan Capital Investment projects).

### **Core Process / System Audits**

- 3.5 To provide assurance on the internal controls in place and perform substantive testing of transactions to ensure completeness and accuracy of data in core systems, reviews included:
- Leisure Management Booking System (Evaluate the income management controls on Leisure Management online booking systems to ensure income is accurately collected)\*
  - Attendance Management (Assess the controls in place to manage sickness absence across the Council, including compliance with policy and procedures, which underpin the effective use of resources).
  - Social Care Income Charging, Billing and Collection (Review the mechanisms in place to raise charges for Social Care clients in a timely manner and the process of collection and recovery of those charges, including the reliance upon various elements, namely: Care Plan, Funding, Contract, and Financial Assessment).
  - Asset Registers (Review of systems, processes and controls that are in place to ensure complete and accurate records of all Property, Fleet, and IT assets that underpin Asset Management Plans to deliver Council's strategies, plans and priorities).
  - Environmental Health (Review the business practices and ways of working within Environmental Health to ensure that regulatory obligations are met and risks are appropriately managed).

### **Assurance Audits Carried Forward from 2018/19**

- 3.6 To provide assurance on the internal controls in place, reviews included:
- Community Empowerment (Review the implementation of the requirements of the Community Empowerment (Scotland) Act 2015).
  - ICT Operational Processes (Evaluate the change / incident / problem management operational controls to ensure they are designed appropriately and that all parties are adhering to them. Assess response to Audit Scotland report May 2017 "Principles for a digital future: Lessons learned from public sector ICT projects")^
  - Commercial Rents (Assess internal financial controls and governance arrangements linked to Corporate priorities, including estate management).
  - Electronic Payment Systems (Review of security and authorisation controls, including segregation of duties).

### **Legislative and Other Compliance Audits**

- 3.7 To test compliance with the terms of the funders' service level agreements or other requirements as part of the wider assurance framework, reviews included:
- EU Funded Programme Tyne Esk LEADER (Annual requirement to review the controls in place to deliver the EU Funded Programme Tyne Esk LEADER and to undertake compliance related work as defined by the Service Level Agreement).

### **Consultancy**

- 3.8 In its 'critical friend' role provide an independent view and challenge at various forums including Business Transformation Board, Capital Planning and Asset Management Board, Learning Estate Strategy Board, Information Management Group, and Early Learning and Childcare Expansion Working Group, taking into consideration the findings from Internal Audit or external assurance work. On request by corporate Management, in response to concerns raised by third parties, carried out Internal Audit Consultancy work to ascertain the key timelines and current status in relation to school estate and housing developments.

### Other Audit Work

3.9 During the year resources were deployed in undertaking the following other audit work relating to the whole Council:

- Annual Assessment of Internal Controls and Governance (Prepare this annual assurance report for Management and the Audit Committee summarising the work undertaken by Internal Audit during the year and forming the statutory opinion on adequacy of the Council's arrangements for risk management, governance and internal control. Test a sample of the key elements in the Local Code of Corporate Governance to determine whether these are operating as described).
- Assessment of Internal Audit against PSIAS (Undertake an annual self-assessment of the Internal Audit service against the Public Sector Internal Audit Standards (PSIAS) and report its findings to Management and the Audit Committee).
- Assessment of the Audit Committee against CIPFA Guidance (Provide assistance to the Chair in undertaking an assessment of the Audit Committee against the CIPFA Audit Committees Practical Guidance for Local Authorities and Police 2018 Edition).
- Recommendation Follow-Up Reviews (Two reviews were undertaken. The first included a sample check of Audit Recommendations which are flagged as closed, to check that they have been implemented and to ensure that the new controls had the desired effect on improving internal controls, risk management and governance; and the second assessed performance against closing Audit Recommendations by the agreed due date).
- Internal Audit Help Desk Enquiry System (Provide guidance and advice on request to Management and Staff on internal controls and governance).
- Administration of Audit Scotland Reports (Monitor publication of Audit Scotland reports and co-ordinate submission by Management of Audit Scotland Reports to the Audit Committee or other Committee as relevant).
- Support for the Risk Management, Serious Organised Crime and Integrity Groups (Attend and provide support in the form of relevant Internal Audit and Counter Fraud updates and advice to the Groups to fulfil their roles).
- Attendance at MLC Boards / Committees (Prepare for and attend Audit Committee meetings and other Boards/Committees as relevant).
- Planning for 2020/21 (Review and update the Internal Audit Charter and Strategy, and develop and consult on proposed coverage of the Internal Audit Annual Plan for 2020/21 for Midlothian Council).

### Investigations

3.10 The most significant activity related to ongoing corporate fraud investigations which required the continued deployment of staff resources greater than the Plan. It is important that these complex and specialist investigations are carried out by specialist fraud investigators, with supervision by the Principal Internal Auditor and Chief Internal Auditor. The outcomes of corporate fraud activity and the Council's participation in the National Fraud Initiative will be included in the Counter Fraud Annual Report 2019/20. The Internal Audit role, in accordance with the Internal Audit Charter, is to ascertain whether there are any internal control weaknesses that are contributory factors in the occurrence of fraud and to make recommendations for the improvement of internal controls.

### **Non MLC Work**

- 3.11 The MLC Internal Audit team has carried out assurance work during the year for the Midlothian Integration Joint Board (MIJB) based on a plan approved by MIJB Audit and Risk Committee in March 2019. An annual assurance report, including audit opinion on the adequacy of the MIJB's arrangements for risk management, governance and control of the delegated resources, will be presented to MIJB Audit and Risk Committee then to MIJB in due course.

## **4 Public Sector Internal Audit Standards and Quality Assurance & Improvement Plan**

- 4.1 The professional standards as set out in Public Sector Internal Audit Standards (PSIAS) effective 1 April 2013 (updated 2017) include:
- Definition of Internal Auditing;
  - Code of Ethics;
  - Attribute Standards (Purpose, Authority and Responsibility; Independence and Objectivity; Proficiency and Due Professional Care; Quality Assurance and Improvement Programme);
  - Performance Standards (Managing the Internal Audit Activity; Nature of Work; Engagement Planning; Performing the Engagement; Communicating Results; Monitoring Progress; Communicating the Acceptance of Risks).
- 4.2 A self-assessment of Internal Audit practices against the Standards was carried out in 2019/20 (in March 2020), as required by the PSIAS, taking into account the progress with implementation of the improvement actions arising from the previous year's self-assessment, as set out within the Quality Assurance and Improvement Programme (QAIP).
- 4.3 The 2019/20 self-assessment has indicated Internal Audit 'Fully Conforms' with the requirements within the 13 Assessment Areas of the Definition of Internal Auditing, the Code of Ethics, Attribute Standards and Performance Standards. The minor improvement actions in the QAIP arising from the self-assessment are as follows: (1) Internal Audit Charter to include: the PSIAS Mission Statement; a high level reference to statutory officers; and the requirement for the CAE to hold a professional qualification; (2) archive electronic audit files in line with retention policy and record in register (3) streamline audit engagement planning and performing using new templates for audit work files to facilitate more concise reporting; and (4) update Audit Manual to reflect new operating arrangements.
- 4.4 PSIAS requires the self-assessment to be subject to an External Quality Assessment (EQA) each five years, by appropriately qualified and independent reviewers. To achieve this, an "EQA Peer Review Framework" was developed by the Scottish Local Authorities Chief Internal Auditors Group (SLACIAG), with Midlothian Council's first EQA in March 2018. SLACIAG has refined its "EQA Peer Review Framework" based on lessons learned and a programme for the second phase has been finalised, with Midlothian Council's EQA expected before or during 2023 to meet the requirements.

**Jill Stacey BA (Hons) ACMA CGMA**  
**Chief Internal Auditor**  
**14 May 2020**



## **Annual Governance Statement 2019/20**

### **Report by Chief Executive**

#### **1. Purpose of the Report**

The purpose of this report is to propose that the Audit Committee considers and approves the Annual Governance Statement that will be published in the Council's Statement of Accounts 2019/20.

#### **2. Background**

Midlothian Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

The Council's Local Code of Corporate Governance, which is consistent with the principles and recommendations of the CIPFA/SOLACE Framework 'Delivering Good Governance in Local Government' and the supporting guidance notes for Scottish authorities (2016), was approved by Council in December 2017.

Fundamentally Corporate Governance is about openness, integrity and accountability. It comprises the systems and processes, and cultures and values by which the authority is directed and controlled and through which it accounts to, engages with and, where appropriate, leads its communities.

The CIPFA/SOLACE Framework urges local authorities to review the effectiveness of their existing governance arrangements against their Local Code, and prepare a governance statement and report compliance on an annual basis.

The Audit Committee is integral to overseeing independent and objective assurance and monitoring improvements in internal control and governance.<sup>1</sup> Its Terms of Reference includes 'To review the Annual Governance Statement prior to approval and consider whether it properly reflects the risk environment and supporting assurances'.

#### **3. Annual Assurance Process 2019/20**

In February and March 2020 the Internal Audit function has undertaken the annual self-assessment of the effectiveness of internal control and governance arrangements and compliance against the Local Code for the year ended 31 March 2020. The Chief Internal Auditor led on this process as part of HIA<sup>2</sup> role to be champion for sound governance.

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<sup>1</sup> CIPFA guidance note for local authorities 'Audit Committees' (2018)

<sup>2</sup> CIPFA 'the role of the head of internal audit in public service organisations' (2019)

The Internal Audit function has considered examples of evidence such as systems, processes and documentation to demonstrate compliance with the Framework's seven core principles of good governance, supporting principles and a range of specific requirements as set out in the Local Code. A revised Local Code of Corporate Governance will be presented for approval in due course.

Progress with implementation of actions regarding previously identified improvement areas of governance has also been evaluated.

The Annual Governance Statement 2019/20 at Appendix 1, in compliance with the CIPFA/SOLACE Framework, provides details of the Council's Governance Framework, the annual Review of Framework undertaken, Improvement Areas of Governance, and overall opinion.

It is the Chief Executive's opinion that, although there are areas of work to be completed for full compliance with the Local Code, the overall governance arrangements of the Council have improved during the year and are considered adequate.

The Annual Governance Statement 2019/20 is informed by the assessment of compliance against the Local Code, Internal Audit annual opinion and recommendations, comments and recommendations made by External Auditors and other external scrutiny bodies and inspection agencies, and findings and recommendations within the Accounts Commission's Best Value Assurance Report for Midlothian Council (published July 2019).

In light of the Covid-19 emergency response by the Council commencing in March 2020, the written assurance statements from the Directors and Chief Officers/Heads of Service were not obtained. The significant and recent change in the Senior Leadership structure was a factor in this decision as part of the annual assurance process. The intention is to issue the toolkits later in 2020 to be used for self-assessment of governance on a continuous basis for 2020/21 annual assurance process.

## **4. Report Implications**

### **4.1 Resource**

The overall aim of the CIPFA/SOLACE Framework 'Delivering Good Governance in Local Government' (2016), on which Midlothian Council's Local Code of Corporate Governance is framed, is to ensure that: resources are directed in accordance with agreed policy and according to priorities; there is sound and inclusive decision making; and there is clear accountability for the use of those resources in order to achieve desired outcomes for service users and communities.

Core principle of good governance "E. Developing the entity's capacity, including the capability of its leadership and the individuals within it" is included within the CIPFA/SOLACE Framework. Workforce and elected member development are a key part of the good governance framework within the Council's Local Code of Corporate Governance.



## 4.2 Risk

The Annual Governance Statement 2019/20 details areas where additional work would further enhance the internal control environment, or improve risk management and corporate governance arrangements. The review and update of the Local Code of Corporate Governance will ensure that internal controls, risk management and other governance arrangements reflect the arrangements in place on an evidence-basis.

Core principle of good governance “F. Managing risks and performance through robust internal control and strong public financial management” is included within the CIPFA/SOLACE Framework. Midlothian Council’s evidence of systems, processes and documentation to demonstrate local compliance with this core principle of good governance is set out in its updated Local Code of Corporate Governance.

## 4.3 Single Midlothian Plan

Themes addressed in this report:

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

## 4.4 Key Priorities within the Single Midlothian Plan

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

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

## 4.5 Impact on Performance and Outcomes

The annual self-assessment and the identification of improvement actions as evidenced through the Annual Governance Statement 2019/20 are designed to enhance the internal control environment, and risk management and corporate governance arrangements. This demonstrates the core principle of good governance “G. Implementing good practices in transparency, reporting, and audit to deliver effective accountability” included within the CIPFA/SOLACE Framework.

## 4.6 Adopting a Preventative Approach

Core principle of good governance “D. Determining the interventions necessary to optimise the achievement of the intended outcomes” is included within the CIPFA/SOLACE Framework. Prevention and detection internal controls and governance arrangements are a key part of the good governance framework within the Council’s Local Code of Corporate Governance.

#### **4.7 Involving Communities and Other Stakeholders**

Core principle of good governance “B. Ensuring openness and comprehensive stakeholder engagement” is included within the CIPFA/SOLACE Framework. Midlothian Council’s evidence of systems, processes and documentation to demonstrate local compliance with this core principle of good governance is set out in its Local Code of Corporate Governance.

#### **4.8 Ensuring Equalities**

The application of equalities legislation within practices is set out in Midlothian Council’s Local Code of Corporate Governance to demonstrate compliance of core principle of good governance “A. Behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law” which is included within the CIPFA/SOLACE Framework.

#### **4.9 Supporting Sustainable Development**

Core principle of good governance “C. Defining outcomes in terms of sustainable economic, social, and environmental benefits” is included within the CIPFA/SOLACE Framework. Midlothian Council’s evidence of systems, processes and documentation to demonstrate local compliance with this core principle of good governance is set out in its Local Code of Corporate Governance.

#### **4.10 IT Issues**

There are no IT issues with regard to this report.

### **5. Recommendations**

The Audit Committee is therefore asked to:

- a) Consider the details of the Annual Governance Statement 2019/20 at Appendix 1 to ensure it reflects the risk environment and governance in place to achieve objectives, and acknowledge the actions identified by Management to improve internal controls and governance arrangements; and
- b) Approve that it be published in the Council’s Statement of Accounts 2019/20.

**Date:** 13 May 2020  
**Report Authors:** Jill Stacey, Chief Internal Auditor  
**E-Mail:** [Jill.Stacey@midlothian.gov.uk](mailto:Jill.Stacey@midlothian.gov.uk)

## **Annual Governance Statement 2019/20**

### **Introduction**

The Annual Governance Statement explains how the Council has complied with the terms of the CIPFA/SOLACE Framework (2016) for the year ended 31 March 2020, sets out the Council's governance arrangements and systems of internal control, and reports on their effectiveness. The statement also covers relevant governance matters as they affect those entities included as part of the Council's Group Accounts.

### **Scope of Responsibility**

Midlothian Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for. The Council also has a statutory duty of Best Value under the Local Government in Scotland Act 2003 to make arrangements to secure continuous improvement and performance, while maintaining an appropriate balance between quality and cost; and in making these arrangements and securing that balance, to have regard to economy, efficiency and effectiveness.

In discharging this overall responsibility, elected members and senior officers are responsible for putting in place proper arrangements for the governance of Midlothian Council's affairs and facilitating the exercise of its functions in a timely, inclusive, open, honest and accountable manner. This includes setting the strategic direction, vision, culture and values of the Council, effective operation of corporate systems, processes and internal controls, engaging with and, where appropriate, lead communities, monitoring whether strategic objectives have been achieved and services delivered cost effectively, and ensuring that appropriate arrangements are in place for the management of risk.

The system can only provide reasonable and not absolute assurance of effectiveness.

### **Framework for Good Governance**

The overall aim of the CIPFA/SOLACE Framework 'Delivering Good Governance in Local Government' (Spring 2016) is to ensure that: resources are directed in accordance with agreed policy and according to priorities; there is sound and inclusive decision making; and there is clear accountability for the use of those resources in order to achieve desired outcomes for service users and communities.

The CIPFA/SOLACE defines the seven core principles of good governance, namely:

- A. Behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law;
- B. Ensuring openness and comprehensive stakeholder engagement;
- C. Defining outcomes in terms of sustainable economic, social, and environmental benefits;
- D. Determining the interventions necessary to optimise the achievement of the intended outcomes;
- E. Developing the entity's capacity, including the capability of its leadership and the individuals within it;
- F. Managing risks and performance through robust internal control and strong public financial management; and
- G. Implementing good practices in transparency, reporting, and audit to deliver effective accountability.

The Council's Local Code of Corporate Governance, which is consistent with the principles and recommendations of the CIPFA/SOLACE Framework and the supporting guidance notes for Scottish authorities (November 2016), was approved by Council in December 2017.

### **The Council's Governance Framework**

The key elements of the Council's governance arrangements, as set out in the Council's Local Code of Corporate Governance, include:

#### **A. Behaving with integrity, demonstrating strong commitment to ethical values, and respecting rule of law**

The roles and responsibilities of elected members and officers and the processes to govern the conduct of the Council's business are defined in standing orders and scheme of delegation for officers, scheme of administration, and financial regulations.

Codes of conduct are in place for, and define the high ethical values and standards of behaviour expected from, elected members and officers to make sure that public business is conducted with fairness and integrity.

The Monitoring Officer is responsible for ensuring that agreed procedures are followed and that all applicable statutes and regulations are complied with. The Standards Committee is responsible for dealing with matters relating to conduct and ethical standards.

The Council seeks feedback from the public through its complaints and comments procedures for Corporate and Social Work (statutory) service areas, responds to the outcomes, as appropriate, and reports the results annually.

Professional advice on the discharge of statutory social work duties is provided to the Council by the Head of Adult Health and Social Care (Chief Social Work Officer). The CSWO promotes values and standards of professional practice and acts as the 'agency decision maker' taking final decisions on a range of social work matters including adoption, secure accommodation, guardianship, etc. The CSWO reports annually on the statutory work undertaken, regulation and inspection, workforce issues and significant social policy themes.

## **B. Ensuring openness and comprehensive stakeholder engagement**

Council meetings are held in public unless there are good reasons for not doing so on the grounds of confidentiality.

Unless confidential, decisions made by Council or other Committees are documented in the public domain. All decisions are explicit about the criteria, rationale and considerations used. The impact and consequences of all decisions are clearly set out.

The Council seeks community views on a wide range of issues and undertakes regular consultation and engagement with citizens and service users, including the Council's 'Shaping Our Future' plans, using a range of consultation and engagement methods adopted across Services.

## **C. Defining outcomes in terms of sustainable economic, social, and environmental benefits**

The Council's vision, strategic objectives and priorities are set out in the Single Midlothian Plan developed through the Community Planning Partnership (of which the Council is a partner). The Council Change and Transformation programme and individual Service Plans outline how Midlothian Council will deliver its contribution to the Single Midlothian Plan.

Asset management planning (which is being developed) and capital investment is structured to consider and balance the combined economic, social and environmental impact of policies and plans when taking decisions about service provision. The Council fully supports community empowerment and recognises the importance of building community capacity and volunteering as a key factor in building stronger, safer, and supportive communities.

Implications are considered during the decision making process within the standard report template covering Resources, Risk, Single Midlothian Plan and Key Priorities, Impact on Performance and Outcomes, Adopting a Preventative Approach, Involving Communities and Other Stakeholders, Ensuring Equalities, Supporting Sustainable Development, and IT issues.

## **D. Determining the interventions necessary to optimise the achievement of the intended outcomes**

Decision makers receive detailed information indicating how intended outcomes would be achieved together with the risks, financial and other implications associated with the proposals, by way of the compulsory sections of the Committee report template.

In determining how services and other courses of action should be planned and delivered the Council is increasingly engaging with internal and external stakeholders. The Council fosters effective relationships, collaborative working and contractual arrangements with other public, private, and voluntary organisations in delivering services that meet the needs of the local community including the achievement of 'social value' (community benefits) through service planning and commissioning.

## **E. Developing the entity's capacity, including the capability of its leadership and the individuals within it**

The corporate management structure (March 2020) consists of the Chief Executive, two Executive Directors and Joint Director Health and Social Care, and six Chief Officers/Heads of Service. The roles of officers are defined in agreed job descriptions. Staff performance is reviewed on an annual basis in accordance with the 'Making Performance Matter' (MPM) process in place during the year.

The Chief Executive is responsible and accountable to the Council for all aspects of management including promoting sound governance, providing quality information/support to inform decision making and scrutiny, supporting other statutory officers, and building relationships with all Councillors.

The Elected Members Induction Programme is periodically supplemented by training events, seminars and briefings. Members appointed to certain committees have also received specific training related to the responsibilities on these committees e.g. licensing, planning, audit.

#### **F. Managing risks and performance through robust internal control & strong public financial management**

The Council has overall responsibility for directing and controlling the organisation. The Cabinet is the principal decision-making committee of the Council. The Performance Review and Scrutiny Committee is responsible for reviewing performance against policy objectives and commenting on decisions and policies and their impact.

The Council has a risk management policy and approach whose main priorities are the robust systems of identification, evaluation and control of risks which threaten the Council's ability to meet its objectives to deliver services to the public.

The Chief Officer Corporate Solutions (the Section 95 officer) is responsible for the proper administration of all aspects of the Council's financial affairs including ensuring appropriate advice is given to the Council on all financial matters.

The Council's system of internal financial control is based on a framework of financial regulations, regular management information, administrative procedures (including segregation of duties), management supervision and a system of delegation and accountability.

The Council has an approved strategy to tackling fraud, theft, corruption and crime, as an integral part of protecting public finances, safeguarding assets, and delivering services effectively.

A Medium Term Financial Strategy has been developed and approved by Council, and plans for revenue (5-year) and capital (10-year) based on strategic priorities are developed, led by the Corporate Management Team, and approved by Council in February each year.

Revenue and Capital Budget Monitoring reports are presented to the Council on a quarterly basis for monitoring and control purposes including the annual outturn. The Management Commentary in the Statement of Accounts provides financial and other performance information regarding the operation of the Council, its wider achievements and areas for development.

#### **G. Implementing good practices in transparency, reporting, & audit to deliver effective accountability**

The independent and objective audit opinion of the Chief Internal Auditor (Chief Audit Executive) is stated within the Internal Audit Annual Assurance Report 2019/20. This is based on work carried out by an in-house and shared services team in conformance with the Public Sector Internal Audit Standards to fulfil statutory Internal Audit provision.

The Council responds to the findings and recommendations of Internal Audit, External Audit, Scrutiny and Inspection bodies including associated Action Plans for improvement. The Audit Committee is integral to overseeing independent and objective assurance and monitoring improvements in internal control and governance.

Quarterly Performance Reports were presented to the Performance, Review and Scrutiny Committee for monitoring the achievement of strategic priorities and key performance indicators.

The Annual Accounts and Report for 2019/20, setting out the financial position in accordance with relevant accounting regulations, are being prepared.

#### **Review of Adequacy and Effectiveness of the Council's Governance Framework**

An annual review of the adequacy and effectiveness of its overall governance framework is carried out. The output is this Annual Governance Statement which is presented to the Audit Committee.

The review was informed by assurances from: Internal Audit annual opinion and recommendations; comments and recommendations made by External Auditors and other external scrutiny bodies and inspection agencies; and findings and recommendations within the Accounts Commission's Best Value Assurance Report for Midlothian Council (published July 2019).

In light of the Covid-19 emergency response by the Council commencing in March 2020 and the significant change in the Senior Leadership Team, only the written assurance statements from the



Directors and Chief Officers/Heads of Service were obtained. The self-assessment toolkits will be issued later in 2020 to be used on a continuous basis for 2020/21 annual assurance process.

### **Improvement Areas of Governance**

The collective review activity outlined above has identified the following areas where improvement in governance arrangements can be made to enhance compliance with the Council's Local Code of Corporate Governance and to demonstrate Best Value, including financial sustainability, financial management and service transformation.

The Council at its meeting on 20 August 2019 approved the "Best Value Assurance Report: Midlothian Council Action Plan", following its consideration by the Corporate Management Team on 17 July 2019, to address the recommendations (1-8 below) in order to demonstrate Best Value. Progress has been made on improvement actions though these are not yet fully implemented:

- 1) As a matter of urgency, officers and elected members work together to develop and agree the medium term financial strategy and progress the council's transformation plans.
- 2) Develop and sustain more constructive relationships between members and between members and officers. Implement effective cross party governance arrangements to ensure that it delivers the medium term financial strategy and transformation plans.
- 3) Ensure that workforce planning reflects the medium term financial strategy
- 4) Undertake a review of its capital programme, to ensure that the timeframes for delivery are achieved going forward and that monitoring and reporting mechanisms are enhanced to drive more accurate analysis and planning around capital work.
- 5) Continue to implement financial planning arrangements to address budget gaps, underpinned by robust financial budgeting and monitoring arrangements.
- 6) Refine its vision in light of the outcome of consultation work through the Services with Communities transformation workstream and to ensure that it focuses its activity most effectively.
- 7) Ensure elected members exercise appropriate scrutiny at all times, take ownership for personal development plans and take up relevant training opportunities.
- 8) Continue to build on positive elements of community empowerment: Increase community ownership of local neighbourhood plans and work with communities to improve how they monitor progress.

In addition, other improvement actions (9-12 below) have been agreed during the year that are not specifically covered by the above in order to enhance compliance with the Council's Local Code of Corporate Governance:

- 9) Strengthen resource capacity and skills in the Procurement function to better support Service Managers to comply with the Council's procurement strategy and procedures, and to undertake contract monitoring to demonstrate delivery of value for money.
- 10) Enhance the Performance Management Framework through the full application of appropriate and proportionate self-assessment processes in all Council services as a self-evaluation tool to demonstrate achievement of Best Value.
- 11) Review and update the Financial Regulations and policies, procedures and guidelines of the key financial planning, management and administration processes linked to the Financial Regulations to reflect changes arising from organisation structures and systems.
- 12) Provide ongoing leadership training for officers relating to their roles and responsibilities to apply procedures and practices with a focus on new or refreshed policies.

These actions to enhance the governance arrangements in 2020/21 will be driven and monitored by the Corporate Management Team on a regular basis in order to inform the next annual review. Internal Audit work planned in 2020/21 is designed to test improvements and compliance.

### **Conclusion and Opinion on Assurance**

The conclusion from the review activity outlined above and our opinion is that reasonable assurance can be placed upon the adequacy and effectiveness of Midlothian Council's systems of internal control and governance. Although areas for further improvement have been identified, the annual review demonstrates sufficient evidence that the Council's Local Code of Corporate Governance is operating effectively and that the Council complies with that Local Code in most respects to meet its principal objectives. Systems are in place to regularly review and improve governance arrangements and the system of internal control.

## Covid-19 Response

The above assurance opinion reflects the assessment of governance in place during normal operations in 2019/20 prior to the significant Covid-19 pandemic response in late March 2020. The latter clearly had an impact on business as usual in the delivery of services. The Council moved to Critical Service delivery at 15.30 on Friday 20 March 2020. This means that as a Category 1 responder the Council carries out the following three essential functions: Caring for the Vulnerable; Liaising with Resilience Partners; and Supporting Economic Recovery.

The Council's Standing Order 19.2, i.e. decision-making responsibility delegated to the Chief Executive in consultation with the Leader, was utilised on a temporary basis during the Covid-19 pandemic incident as a more agile way of decision-making for urgent decisions within its governance arrangements. All formal Council and Committee meetings had been cancelled for an indefinite period, thus ensuring the safety of officers, elected members and the community.

New innovations, business processes, and technology solutions have been embraced in order for the Council to deliver services to the community in its Category 1 responder role, and in particular for new areas of activity as part of the national response with funding provided by UK and Scottish Government as relevant. For example, Non Domestic Rates reliefs including the Business Grants Scheme (Administered by City of Edinburgh Council on behalf of MLC), Hardship Fund, Scottish Welfare Fund, Food Fund, Supporting Communities Fund, and Third Sector Resilience Fund.

The logistics of delivering services in a radically different way, in order to keep staff safe, and adhere to social distancing and self-isolation measures at the same time, has meant significant changes in when and where services are provided, deployment of a large number of staff who do not deliver critical services to undertake alternative duties, rapidly modernised IT support, and significant partnership working across the community. This was achieved using amended governance arrangements, new ways of decision-making, leadership and implementation including daily Corporate Incident Management Team virtual meetings, conference calls, and systems remote access, weekly updates to Group Leaders, Chief Executive daily message to all staff and Elected Members, and a range of wellbeing supports.

Initial work is underway on assessing the financial impact on the Council and the longer term disruption and consequences arising from the Covid-19 pandemic. The Council will, at the appropriate time, carry out a Covid-19 pandemic response formal review, highlight any lessons learned, and implement associated improvements. It should be noted that a reflective approach has been applied to improve practices during the response phase on a continuous basis.

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Grace Vickers  
Chief Executive  
mm 2020

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Derek Milligan  
Leader of the Council  
mm 2020





**Counter Fraud Annual Report 2019/20**  
**Report by the Chief Internal Auditor****1 Purpose of Report**

The purpose of this report is to provide an update to the Audit Committee on the Council's counter fraud responsibilities and the activities of the Corporate Fraud team over the past year as part of the arrangements to tackling fraud at the Council, and to propose a revised Counter Fraud Policy Statement and Strategy for Council approval.

**2 Background**

- 2.1 The Council is committed to minimising the risk of loss due to fraud, theft or corruption and to taking appropriate action against those who attempt to defraud the Council, whether from within the authority or from outside, as set out within its counter fraud and corruption policy and strategy.
- 2.2 The primary responsibility for the prevention, detection and investigation of fraud rests with Management, supported by the corporate Fraud & Audit Officers. Internal Audit provides advice and independent assurance on the effectiveness of processes put in place by Management.
- 2.3 Part of the Audit Committee's role is to review the assessment of fraud risks and potential harm to the Council from fraud and corruption, and to monitor the counter fraud strategy, actions and resources.

**3 Corporate Fraud Team Activity**

- 3.1 The 2019/20 planned Corporate Fraud activity was approved by this Committee in March 2019. The Plan Days for Corporate Fraud activity was increased from the previous year 2018/19 of 210 days (equivalent to staff resources of 1.0 FTE) to 305 days (equivalent to staff resources of 1.5 FTE), to reflect the actual corporate fraud resources deployed on fraud investigations during the previous year in order to carry out ongoing fraud activity anticipated in 2019/20. The staff resource relates to the two Fraud & Audit Officers, plus some management and supervision provided by the Principal Internal Auditor and the Chief Internal Auditor. The actual corporate fraud resources deployed during 2019/20 was 455 days, broadly equivalent to 2.1 FTE (i.e. utilising the two Fraud & Audit Officers full time and greater than planned management and supervision by the Principal Internal Auditor and the Chief Internal Auditor).
- 3.2 For the second consecutive year significantly more staff resources have been deployed during the year than planned on corporate fraud activity, mostly notably due to the deployment to the ongoing fraud investigation activity and responses to fraud enquiries which have increased in volume, some of which have been received through the whistleblowing

mechanisms. This has had an impact on the delivery of some of the Counter Fraud planned work with the following not being carried out:

- a) Compliance testing of Licensing;
- b) Data Match of Council Tax Reduction Scheme, Discounts and Exemptions; and
- c) Fraud Awareness Training.

The planned Data Match associated with the Council's participation in the National Fraud Initiative was carried out in line with the Plan and the outcomes are included within this report.

- 3.3 It has been calculated, using Audit Scotland guidance (where relevant), that as a result of Corporate Fraud Team activity on other corporate fraud enquiries a total savings value of £103,164 has been identified during 2019/20. These are detailed in Appendix 1. Areas of work undertaken by the Team and the value identified during 2019/20 are detailed below.
- 3.4 As specialist investigators, the Team has continued to be involved in the recovery action that is ongoing under the Roads Contract Management Investigation, which in addition has involved input from the Principal Internal Auditor. In addition £3,438 Income was recovered for Midlothian Council as a result of additional work carried out under the review of Invoices from the Roads Investigation.
- 3.5 The Corporate Fraud Team continues to deal with enquiries from the Midlothian Council website page "Report a possible crime, fraud or similar concern" or the anonymous telephone reporting line or secure email address which are all available to staff or the public for whistleblowing purposes. Investigations have been carried in response to 15 referrals from various sources that raised concerns of corporate fraud, bribery or corruption. Initial fact-finding responses are followed by intelligence gathering and investigations. If substantiated, appropriate action is taken in accordance with the Council's policies and procedures, for example, disciplinary or contract management action. Where criminal activity is suspected, referrals have been made to Police Scotland; there are 3 criminal investigations that are ongoing. The value of these fraud, bribery or corruption cases has not yet been verified due to the ongoing nature of the investigations.
- 3.6 The Team has received notifications from Housing Officers during the year to detect and investigate potential subletting or abandonment of Council owned properties. As a result of this, 23 allegations of potential tenancy fraud were investigated; one of which resulted in the return of a property to the housing stock which was subsequently made available to those in genuine need. For each of the houses identified the calculation, according to Audit Scotland guidance, is £93,000 over 4 years.
- 3.7 The Corporate Fraud Team responded to 12 notifications of alleged fraud associated with Council Tax Discounts and Exemptions during the year to determine whether these discounts and exemptions are claimed legitimately, including Council Tax Reduction Scheme (CTRS) and Single Person Discount (SPD). One referral from Housing relating to an undeclared person residing in the property, was investigated and subsequently referred to the Single Fraud Investigation Service (SFIS) of the Department for Work and Pensions (DWP) to interview the Tenant.

This resulted in identification of overpayments of Housing Benefit (£6,907) and Council Tax Reduction and Single Persons Discount (£3,257). Although planned compliance testing of CTRS was not carried out during the year, as stated in 3.2, the above indicates that reactive CTRS counter fraud work was undertaken relating to this area of fraud risk.

- 3.8 A member of the Corporate Fraud team acts as the Single Point of Contact for Midlothian Council with Police Scotland for Serious and Organised Crime Groups. During the year, 12 enquiries were received from Police Scotland and information was provided to them under section 21 (paras 2 & 3) of the Data Protection Act 2018. One enquiry subsequently resulted in a further allegation being referred to SFIS of the DWP to investigate. The outcome is not yet known. The Fraud & Audit Officers are members of the Council's Serious Organised Crime (SOC) Group, relating to Serious and Organised Crime and Counter Terrorism.
- 3.9 The Fraud & Audit Officers are members of the Scottish Local Authority Investigators Group (SLAIG) to represent Midlothian Council. They attend SLAIG's quarterly meetings as a forum for sharing best practice across Councils and the wider public sector, thus ensuring their knowledge of emerging fraud risks and issues is up to date.
- 3.10 Midlothian Council continues to participate in the National Fraud Initiative (NFI) which is a UK wide counter-fraud exercise led by the Cabinet Office and Audit Scotland. It uses data analytic techniques to compare information about individuals held by different public bodies, and on different systems, to identify circumstances (data matches) that might suggest the existence of fraud or error. The Principal Internal Auditor acts as the Council's Key Contact for NFI and the Corporate Fraud Team has coordinated the submission of the required data sets from various Council systems and responded to the data matches received to date with input from relevant Services across the Council. The outcomes from Midlothian Council's participation in the National Fraud Initiative 2018/2019, shown in Appendix 2, total £83,088.
- 3.11 In conclusion, the Corporate Fraud Team has been successful in achieving the above outcomes during 2019/20 and making best use of resources to support Midlothian Council's objectives. Tackling fraud is an ongoing process as the Council's internal and external operating environment changes.

#### **4 Review of Counter Fraud Management Arrangements**

- 4.1 In light of the significant fraud investigations that have occurred within Midlothian Council in recent years, noting that these have aspects that are still ongoing, it is relevant to conduct a review of counter fraud management arrangements in place and to make improvements.
- 4.2 The new Senior Leadership Structure provides the ideal opportunity for re-establishing a counter fraud culture which is fundamental to ensuring an effective response to fraud, theft, corruption or crime. The leadership part played by Corporate Management Team and Operational Management is key to establishing counter fraud behaviours within the organisation, its partners, suppliers and customers.

- 4.3 A revised Counter Fraud Policy Statement (Appendix 3) and Counter Fraud Strategy (Appendix 4) is included for consideration and endorsement by the Audit Committee for full Council approval.
- 4.4 Midlothian Council is committed to creating a great place to grow supported by the 9 drivers for change:



- 4.5 Implementing the 9 drivers for change in practice is applicable to the Council's arrangements for tackling fraud as set out in the Counter Fraud Policy Statement (Appendix 3) and Counter Fraud Strategy (Appendix 4). The shift from the left-hand column to the right hand column is an intrinsic part of the proposed change in approach and culture for the Council for tackling fraud and corruption. For example:
- (a) The formal establishment of an Integrity Group with a Terms of Reference (Appendix 5) shifting from silo-based working to more holistic working in multi-disciplinary forums to tackle fraud in a consistent and collaborative way across the Council;
  - (b) A focus on enhancing fraud prevention and detection to improve Midlothian Council's resilience to the threat of fraud and corruption, and ensure these are embedded preventative practices;
  - (c) Applying the minimum standard within the CIPFA Code of Practice on 'Managing the Risk of Fraud and Corruption (2014)' for counter fraud policy, strategy and other practices, and adopting the CIPFA Counter Fraud Maturity Model as a means of self-assessment moving forward will enable continuous improvement to be evaluated, managed and evidenced; and
  - (d) Use of a blend of toolkits such as fraud vulnerability assessments and e-learning packages that can be tailored to specific Services.
- 4.6 It is important that associated policies, procedures and guidelines across the Council are regularly reviewed and updated, as appropriate, as this will ensure that they keep pace with best practice in relation to fraud and corruption prevention and detection, to ensure their continued relevance and effectiveness.
- 4.6 An assessment has been carried out during 2019/20 of the Council's counter policy framework against best practice, the CIPFA Counter Fraud guidance, as set out in the table below:

<b>The CIPFA Counter Fraud guidance states the minimum policy framework will include:</b>	<b>Associated Policies across the Council (latest approved date and responsible officer in brackets):</b>
<ul style="list-style-type: none"> <li>Counter Fraud Policy</li> </ul>	<ul style="list-style-type: none"> <li>Anti-Fraud Policy and Strategy (December 2016; Chief Internal Auditor)</li> </ul>
<ul style="list-style-type: none"> <li>Whistleblowing Policy</li> </ul>	<ul style="list-style-type: none"> <li>Whistle Blowing – Public Interest Disclosure Policy (August 2017; Chief Internal Auditor/HR Manager)</li> </ul>
<ul style="list-style-type: none"> <li>Anti-Money Laundering Policy</li> </ul>	<ul style="list-style-type: none"> <li>Anti-Money Laundering Policy (October 2019; s95 Officer)</li> </ul>
<ul style="list-style-type: none"> <li>Anti-Bribery &amp; Corruption Policy</li> </ul>	<ul style="list-style-type: none"> <li>Anti-Bribery Policy (December 2016; s95 Officer)</li> </ul>
<ul style="list-style-type: none"> <li>Gifts &amp; Hospitality Policy and register</li> </ul>	<ul style="list-style-type: none"> <li>Gifts &amp; Hospitality Policy and register (March 2019; HR Manager)</li> </ul>
<ul style="list-style-type: none"> <li>Conflict of Interest Policy and register</li> </ul>	<ul style="list-style-type: none"> <li>Outside Employment and Other Interests Policy (April 2019; HR Manager)</li> </ul>
<ul style="list-style-type: none"> <li>Codes of Conduct and Ethics</li> </ul>	<ul style="list-style-type: none"> <li>Employee Code of Conduct (2019; HR Manager)</li> </ul>
<ul style="list-style-type: none"> <li>Information Security Policy</li> </ul>	<ul style="list-style-type: none"> <li>Information Security Policy (October 2017; Information Governance / Security Services Lead)</li> </ul>
<ul style="list-style-type: none"> <li>Cyber Security Policy</li> </ul>	<ul style="list-style-type: none"> <li>Information Security Policy incorporates the subset of cyber security policy (October 2017; Information Governance / Security Services Lead)</li> </ul>

- 4.7 The Corporate Fraud Annual Plan 2020/21 (Appendix 6) sets out the planned Corporate Fraud activity to support the change in approach and culture for the Council for tackling fraud and corruption to deliver the revised Counter Fraud Strategy which requires additional resources as set out below.

## **5 Report Implications**

### **5.1 Resource**

The actual corporate fraud resources deployed during 2019/20 was 455 days, broadly equivalent to 2.1 FTE i.e. utilising the two Fraud & Audit Officers full time and greater than planned management and supervision by the Principal Internal Auditor and the Chief Internal Auditor. This was higher than the current approved establishment which is 50% of each of the two Fraud & Audit Officers (1 FTE Corporate Fraud Team), who are Accredited Counter Fraud Specialist officers.

The new counter fraud policy and strategy with a focus on prevention will also require more fraud staff resources than is within the current approved establishment. It is therefore proposed to have 2 FTE Corporate Fraud Officers with the 1 FTE Audit resource being retained to deliver planned Internal Audit activity approved by the Audit Committee in March 2020. These additional costs arising from enhanced fraud risk mitigation within the Council will have to be considered and prioritised against other pressures in the revenue budget. A Service Review will be undertaken in collaboration with HR.

## **5.2 Risk**

The report sets out primary responsibility for the prevention, detection and investigation of fraud that rests with Management, and directly addresses fraud risk and outcomes arising from work undertaken by the Corporate Fraud Team in collaboration with other Services to reduce the risks within the Council.

## **5.3 Single Midlothian Plan and Business Transformation**

Themes indirectly 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

## **5.4 Key Priorities within the Single Midlothian Plan**

Although this report does not relate directly to the key priorities within the Single Midlothian Plan (Reducing the gap in learning outcomes; Reducing the gap in health outcomes; and Reducing the gap in economic circumstances) by preventing and detecting fraud, additional resources might be available to support the Council's objectives. Any loss of funds due to fraud and corruption might impact on the ability of Midlothian Council to achieve its priorities.

## **5.5 Impact on Performance and Outcomes**

The Findings and Recommendations from Internal Audit and Corporate Fraud work during the year assists the Council in improving its performance and outcomes which are designed to maintain and / or enhance fraud prevention and detection controls.

## **5.6 Adopting a Preventative Approach**

Having a robust fraud prevention and investigation service contributes to safeguarding the Council's financial resources, for delivery of services, as part of protecting the public purse. A focus on enhancing fraud prevention and detection to improve Midlothian Council's resilience to the threat of fraud and corruption, and ensure these are embedded preventative practices are specific changes associated with the proposed Counter Fraud Strategy (2020).

## **5.7 Involving Communities and Other Stakeholders**

This Counter Fraud Annual Report 2019/20 has been presented to the Corporate Management Team (SRG 3 June 2020 comprising Chief Executive, Executive Directors, and Chief Officers/Heads of Service) who play a key leadership role along with Operational Management in establishing counter fraud behaviours within the organisation, its partners, suppliers and customers.



This report outlines outcomes arising from work undertaken by the Corporate Fraud Team, some of which arose from whistleblowing received from those within communities or other stakeholders.

## **5.8 Ensuring Equalities**

There are no equalities issues with regard to this report.

## **5.9 Supporting Sustainable Development**

There are no sustainability issues with regard to this report.

## **5.10 IT Issues**

There are no IT issues with regard to this report.

## **6 Recommendations**

The Audit Committee is therefore asked to:

- a) Consider the counter fraud work undertaken by the Corporate Fraud Team during the year to 31 March 2020 (Appendix 1), in support of Management and the delivery of the Council's anti-fraud and corruption policy and strategy;
- b) Note the Outcomes of Midlothian Council's participation in the National Fraud Initiative 2018/2019 (Appendix 2);
- c) Endorse the revised Counter Fraud Policy Statement (Appendix 3) and Counter Fraud Strategy (Appendix 4) for full Council approval, and endorse the proposal to have 2 FTE Corporate Fraud Officers to deliver the revised Counter Fraud Strategy which requires additional resources;
- d) Approve the Terms of Reference for the new Integrity Group (Appendix 5); and
- e) Approve the Corporate Fraud Annual Plan 2020/21 (Appendix 6) which is based on the proposal to have 2 FTE Corporate Fraud Officers to deliver the revised Counter Fraud Strategy.

**Date:** 15 May 2020

**Report Authors:** Jill Stacey, Chief Internal Auditor  
Elaine Greaves, Principal Internal Auditor

**E-Mail:** [Jill.Stacey@midlothian.gov.uk](mailto:Jill.Stacey@midlothian.gov.uk)  
[Elaine.Greaves@midlothian.gov.uk](mailto:Elaine.Greaves@midlothian.gov.uk)

## Appendix 1 – Outcomes from Corporate Fraud Team activity on other corporate fraud enquiries in 2019/20

Type of Referral	No of Referrals	Web	Telephone	Email	No with Fraud Detected	£ value Fraud Detected	Comments
Corporate Fraud (Internal)	15	5	7	3			Investigations in response to referrals from various sources. Disciplinary or other action taken, as appropriate. Referrals made to Police Scotland for 3 criminal investigations that are ongoing. Value not yet verified.  £3,438 was recovered associated with the review of Invoices from the Roads Investigation. Other recovery action currently ongoing under the Roads Investigation.
Housing Tenancy Fraud	23	1	3	19	1	£93,000	23 referrals resulting in investigations which recovered 1 Council house and return to available housing stock. Value per Audit Scotland guidance (£93,000 over 4 years each).
Council Tax Discounts & Exemptions, CTRS / SPD	12	4	5	3	1	£10,164	1 investigation relating to an undeclared person residing in the property subsequently referred to DWP SFIS to interview the Tenant. This resulted in overpayments of Housing Benefit (£6,907) and Council Tax Reduction & Single Persons Discount (£3,257).
DPA/SOCG enquiries	12			12			12 enquiries received from Police Scotland. 1 enquiry subsequently resulted in a further allegation being referred to DWP SFIS to investigate. The outcome is not yet known.
Other	5	3		2			Investigations resulting in referrals being submitted to external partners and internal services including Health & Safety Executive, Trading Standards, Planning, and Environmental Health.
<b>Total</b>	<b>67</b>	<b>13</b>	<b>15</b>	<b>39</b>		<b>£103,164</b>	



**Appendix 2** – Outcomes from Midlothian Council’s participation in The National Fraud Initiative 2018/2019 (to 04/04/2020)

Type	No of Matches in 2018/2019	No of matches reviewed	Fraud or Errors Detected	Outcome (overpayment)	Estimated Savings	Total Savings	Comments
Council Tax (SPD)	3667	613	51*	£8,958	£40,814	£49,771	Previous years NFI matches excluded.
Housing Benefit	422	55	2*	£999	£2,532	£3,531	*2 of the 51 SPD cases also had HB element.
Council Tax Reduction (CTRS)	517	224	3	£2,729	£1,757	£4,486	Previous years NFI matches excluded.
Payroll	154	85					Previous years matches excluded. No issues found.
Disabled Parking Blue Badges	92	92	44		£25,300	£25,300	44 badges had not been cancelled.
Housing Tenants	563	509					No issues found.
Residential Care Homes	34	34					No issues found.
Personal Budgets	7	6	1	£4,629	£74,246		Awaiting outcome of DWP SFIS investigation (notional figures input as per NFI guidance)
Creditors	3,054	591					The large number of matches is as a result of the volume of creditors’ information.
<b>Total Savings</b>						<b>£83,088</b>	



## COUNTER FRAUD POLICY STATEMENT

### Introduction

The size and nature of the services provided by Midlothian Council (MLC), as with other large organisations, puts the Council at risk of loss due to fraud, theft or corruption. The aim of this policy is to communicate why effective and robust counter fraud arrangements should be in place to ensure the Council's ongoing resilience to the threats of fraud and corruption. This policy will be supported by the Counter Fraud Strategy, which describes the approach that will be adopted by MLC to tackle fraud, to ensure that MLC, nor its stakeholders, are exposed to an unknown, unmanaged or unacceptable degree of fraud risk by protecting themselves in an appropriate way.

Tackling fraud is an integral part of protecting public finances. The harm caused by fraud, however, is not just financial. Fraud damages local people and communities, damages the Council's reputation and undermines trust in public services. Every pound lost through fraud cannot be spent on providing and delivering quality services that people rely on and which they pay their taxes to get, therefore it is important to have a strong counter-fraud culture and effective counter-fraud measures embedded within its business processes and governance arrangements.

The changing and increasingly complex environment in which the Council operates, and the complexity of policies, procedures, processes, systems, customer interfaces, legislative requirements, partnerships and joint working arrangements and relationships with other organisations that enable the Council to deliver its services, is happening against a backdrop of depressed economic activity in which the fraud risk tends to increase.

Management are committed to minimising fraud risk and at the same time taking appropriate actions against those who attempt to defraud the Council, whether from within the authority or from outside. Refinements to the Council's approach to tackling fraud include a focus on enhanced fraud prevention and detection to improve its resilience to fraud.

### Roles and responsibilities

There is an expectation and obligation that all individuals and organisations associated with the Council will act with honesty and integrity, are aware of and adhere to the procedures and practices in place to prevent fraud, theft or corruption when performing their roles, and utilise the whistleblowing process online to report any concerns. The Council will continue to support its people to develop the appropriate skills and competencies so as to enable them to tackle fraud effectively, with a focus on enhanced fraud prevention and detection tools and management arrangements.

#### Corporate Management Team (CMT)

CMT will act as counter fraud champions, tackling fraud from the top down, allocating sufficient resources proportionate to the level of fraud risk to ensure that income is maximised and assets are safeguarded, and fostering a strong counter fraud culture.

#### Senior Management

Senior management will: identify fraud and corruption risks; ensure that they understand and apply the counter fraud policy requirements within their own service provision procedures and practices to embed counter fraud in the Council's culture and working practices; take action to prevent, detect and investigate fraud; periodically highlight to staff the importance of behaving with integrity; support internal and external audits; and carry out a periodic review of the efficacy of their counter fraud arrangements.

#### Chief Officer Corporate Solutions

The Chief Officer Corporate Solutions is designated by Council as the officer responsible for the administration of the Council's financial affairs in terms of Section 95 of the Local Government (Scotland) Act 1973.

### Integrity Group

The Integrity Group will support the Management across the Council with counter fraud management by: overseeing the review of the counter fraud policy framework in line with best practice; highlighting emerging fraud and corruption risks, threats, vulnerabilities; agreeing fraud and corruption mitigation actions; raising awareness of bribery, fraud and corruption in the Council as a method of prevention; meeting during the course of fraud investigations with the aim to take corrective action, minimise losses and help prevent further frauds; and coordinating with Serious Organised Crime (SOC) Group.

### Corporate Fraud Team

The Corporate Fraud Team will support the counter fraud management by: supporting the Integrity Group; leading on the implementation of identified improvement actions; carrying out fraud vulnerability assessments with Service Managers; monitoring that the fraud prevention, detection and investigation processes and procedures are followed; offering advice, guidance, training and support; and conducting fraud investigations.

### Internal Audit

Internal Audit will review the effectiveness of controls put in place by Management to manage the risk of fraud. Full details of its roles are set out in the Internal Audit Charter.

### Audit Committee

The Audit Committee will oversee the adequacy and effectiveness of the Council's internal controls, review the assessment of fraud risks and monitor the counter fraud strategy, actions and resources.

### Elected Members

Elected Members need to be aware of and adhere to the procedures and practices in place to prevent fraud, theft or corruption when performing their roles, and support the Public to utilise the whistleblowing process online to report any concerns.

## **Counter Fraud process**

Tackling fraud is not a one-off exercise; it is a continuous process across all parts of the Council because the service delivery processes it underpins are continuous. Tackling fraud is an integral part of good governance within the Council and demonstrates effective financial stewardship and strong public financial management.

## **Reporting**

Reporting will include an annual report by the Integrity Group to CMT and the Audit Committee on the corporate fraud activity and outcomes. The Annual Governance Statement to CMT and the Audit Committee will include a statement on the efficacy of counter fraud arrangements.

## **Budget**

One of the five key principles in the CIPFA Code of Practice on Managing the Risk of Fraud and Corruption is to provide resources to implement the strategy. The two previous years indicates resources of at least 2.0 FTE Corporate Fraud Officers in conducting fraud investigations. The refocus from a reactive to a proactive strategy on prevention and detection will require the equivalent corporate fraud resources. Any additional costs within Services arising from enhanced counter fraud risk mitigation will have to be considered and prioritised against other pressures in the revenue budget.

## **Quality Assurance**

This policy will be subject to document control, version control, be reviewed at least annually, and be revised to reflect changes in legislation, counter fraud best practice, and significant changes in corporate governance.

## **Review**

Counter Fraud policies and procedures will be reviewed on a regular basis to ensure their continued relevance and effectiveness.

## COUNTER FRAUD STRATEGY

The size and nature of the Council's services, as with other large organisations, puts the Council at risk of loss due to fraud, theft or corruption. Management are committed to minimising this risk and at the same time taking appropriate action against those who attempt to defraud the Council, whether from within the authority or from outside. Refinements to the Council's approach to tackling fraud include a focus on enhancing fraud prevention and detection to improve its resilience to the threat of fraud and corruption.

The Council's strategy, which is based upon the national counter fraud standard CIPFA's Code of Practice on 'Managing the Risk of Fraud and Corruption' published in December 2014, is built around the following:

### ***Counter fraud and corruption culture***

The Council expects its employees and elected members to act within the law and the high standards of integrity, honesty and openness, which are reflected in the Council's Code of Conduct internal codes, rules and procedures. The Council also expects that all outside individuals and organisations, including service users, partners, suppliers, and contractors will act to the same standards.

### ***Plans and policies***

Service specific plans, policies, procedures, processes and guidelines must contain detailed information on how to prevent or reduce the Council's vulnerability to fraud, theft or corruption as part of their Service provision to ensure that income is maximised and assets are safeguarded.

The Integrity Group, chaired by the Executive Director Place and supported by the Chief Internal Auditor and the Corporate Fraud team, must oversee the review and update of associated policies, procedures and guidelines across the Council by the responsible owner. The CIPFA Counter Fraud guidance states as a minimum the policy framework should include: Counter Fraud Policy; Whistleblowing Policy; Anti Money Laundering Policy; Anti-Bribery & Corruption Policy; Gifts & Hospitality Policy and register; Conflict of Interest Policy and register; Codes of Conduct and Ethics; Information Security Policy; and Cyber Security Policy.

### ***Deter and detect***

The Council will focus on enhanced fraud prevention and detection in accordance with the Scottish Government's cross sector counter fraud strategy 'Protecting Public Resources in Scotland: The strategic approach of fighting fraud, bribery and corruption' launched in June 2015 and measure progress against the CIPFA Counter Fraud Maturity Model.

Management will continuously monitor and review the internal control systems which include financial regulations, scheme of delegation, standing orders, data security, codes of conduct, protocols, practices, guidelines and training, to ensure that fraud prevention and detection procedures are effective and robust, and that risk mitigating actions are in place.

In addition Management will continue to identify those areas, existing or new, which are vulnerable to fraud, theft or corruption and will use a standard assessment method to assess the effectiveness of the controls in place. The Corporate Fraud team will assist Service Managers to make those fraud vulnerability assessments and to carry out annual reviews. The Corporate Fraud Annual Plan will include compliance testing to check the efficacy of internal controls. Service Managers must co-operate with compliance checks and ensure that vulnerabilities within processes are addressed.

A proactive approach to fraud detection will be followed, including enhanced use of techniques such as data matching and intelligence sharing with partner organisations within the provisions of the General Data Protection Regulations. Positive publicity about the successful detection or prevention of a fraud will play a key part in deterring others.

The Council will continue to work with other organisations to manage its fraud risks and share best practice through participation in counter fraud forums at local and national levels. This will include the Scottish Local Authorities Investigators Group (SLAIG) and the NHS's Counter Fraud Service (CFS). There will be further joint working in countering fraud in particular in response to the risks from organised crime which can commit fraud across the public sector, embedding the principles of the "Letting Our Communities Flourish" strategy. The Council will continue to participate in the National Fraud Initiative (NFI) in Scotland as active detection and prosecution of fraudsters is a vital deterrent to others contemplating defrauding the public purse.

### ***Training and awareness***

To have effective counter fraud, theft or corruption controls the Council recognises that it must provide awareness and training programmes for counter fraud prevention and detection techniques. General fraud awareness for all members of staff will mainly be done through the use of E Learning modules and will focus on the key message that compliance with Council policies, processes and procedures are designed to keep employees and the organisation safe. More specific training and case studies, based on fraud vulnerability assessments, will be targeted to appropriate Service Managers and their staff.

In its communications with employees and elected members the Council will incorporate the key message that internal control systems to counter fraud, theft or corruption are designed both to safeguard assets and to protect their integrity if challenged.

In the Council's dealings with outside individuals and organisations it will ensure that they are aware of the Council's stance towards tackling fraud, theft or corruption. The Council will encourage the reporting of suspected fraud, theft or corruption through confidential reporting or whistleblowing arrangements to the Corporate Fraud team and reassure those who fear reprisals that it will protect their rights.

### ***Action***

All actual or suspected cases of fraud, theft or corruption should be reported to the Corporate Fraud team (anonymously if desired) by email [CounterFraud@midlothian.gov.uk](mailto:CounterFraud@midlothian.gov.uk) or telephone 0131 271 3572 / 3573 or via the Council's website "[Report/ Fraud, corruption and whistleblowing](#)". The Corporate Fraud team will conduct fraud investigations in accordance with legislation and standard operating procedures. The Integrity Group will meet during the course of fraud investigations with the aim to take corrective action, minimise losses and help prevent further frauds.

## **Investigations**

Anyone suspected of fraudulent behaviour will be treated fairly and courteously within the principles of Article 6 and Article 8 of the Human Rights Act 1998. All investigations will be strictly confidential and intelligence or evidence will be gathered to a standard that would be admissible in court and held securely. Investigators will not carry out directed surveillance without proper authorisation as detailed in Regulation of Investigatory Powers (Scotland) Act 2000 and the Council's code of practice.

Where initial investigations identify evidence of criminality, the matter will be reported to Police Scotland and the Council will co-operate fully with any Police investigation.

Where investigations reveal evidence of fraudulent or dishonest behaviour, corrupt practice or theft by a member of staff, appropriate steps will be taken including disciplinary action in accordance with the HR policies.

Steps will also be taken to recover losses resulting from fraud, theft or corruption including the recovery of assets and money, which may involve joint working with public sector partners.

## **Monitoring and Review**

Internal Audit will continue to review the efficacy of counter fraud internal controls put in place by Management and provide independent assurance over fraud risk management, strategy and activities.

The Audit Committee will oversee the adequacy and effectiveness of the Council's systems of internal financial control and framework of internal control through scrutiny of annual reports on the assessment of fraud risks and the monitoring of the counter fraud strategy, actions and resources.

This strategy will be reviewed annually.







## **INTEGRITY GROUP**

### **TERMS OF REFERENCE**

#### **INTRODUCTION**

Tackling fraud is an integral part of protecting public finances. The harm caused by fraud, however, is not just financial. Fraud damages local people and communities, damages the Council's reputation and undermines trust in public services. Every pound lost through fraud cannot be spent on providing and delivering quality services that people rely on and which they pay their taxes to get, therefore it is important to have a strong counter-fraud culture and effective counter-fraud measures embedded within its business processes and governance arrangements.

#### **PURPOSE**

The purpose of the Integrity Group is to improve the Council's resilience to fraud, corruption, theft and crime (including cybercrime and money laundering).

#### **REPORTING ARRANGEMENTS**

The Integrity Group will be accountable to the Corporate Management Team and the S95 Finance Officer (Chief Officer Corporate Solutions), and annually will provide assurance to CMT and the S95 Finance Officer, and to the Audit Committee.

#### **RESPONSIBILITIES**

It is Management's responsibility to design and maintain proper risk management, governance and internal control processes and systems to ensure probity in systems and operations, and mitigation of risks, including the prevention, detection and resolution of fraud and irregularities. Management is also responsible for checking that the arrangements and controls are operating effectively and obtaining assurances from internal compliance, risk, inspection, quality, and control functions. These are known as the first and second lines of defence.

In supporting Management across the whole of the Council to fulfil their responsibilities, the Integrity Group will:

1. Review the level of compliance against the CIPFA code on Managing the Risk of Fraud and Corruption.
2. Assist with developing, reviewing and updating the policies and procedures to mitigate the risk of fraud, corruption, theft and crime (including cybercrime and money laundering), for example, Whistleblowing, Conflicts of Interest, Gifts and Hospitality. Ensure these are communicated effectively throughout the Council.
3. Highlight emerging risks, threats, vulnerabilities and related fraud, corruption, theft and crime (including cybercrime and money laundering) opportunities through our engagement with national forums to share intelligence and best practice.
4. Receive, consider and monitor organisational vulnerability alerts or fraud flags, including those identified via various internal and external sources.

5. Agree appropriate actions to mitigate the risks of fraud, corruption, theft and crime (including cybercrime and money laundering), identifying sustainable preventative measures.
6. Raise awareness of risks and potential implications of bribery, fraud, corruption, theft and crime (including cybercrime and money laundering) in the Council as a method of prevention.
7. Meet during the course of fraud investigations with the aim to take corrective action, minimise losses and help prevent further frauds.
8. Develop an Annual Plan to focus the activity of the Corporate Fraud resources and to target areas where there is a higher risk of fraud.
9. Report annually on corporate fraud activity and outcomes for presentation to CMT (including S95 Finance Officer) and the Audit Committee, or more frequently to CMT or S95 Finance Officer if required for case management.

## **MEMBERSHIP**

To be effective the Group will comprise of members with specific roles and responsibilities associated with these risks and complementary skill sets that will guide and inform decision making. In addition, it will also allow activities to be better coordinated when multiple teams are involved in the investigation process.

The following post holders will be members of the Integrity Group:

- Executive Director (Chair)
- Chief Internal Auditor
- Service Reps CO/HOS
- Procurement Manager
- Human Resources Manager
- Legal Services Manager (and Monitoring Officer)
- Financial Services Manager
- Corporate Fraud Officers
- Information Governance/Security Services Lead

The Chair acts as the coordinator between the Integrity Group and the Serious Organised Crime (SOC) Group (through the existing quarterly meetings).

The Group has the authority to co-opt members or invite other Managers for certain agenda items.

Directorates can send more than one delegate if they see the need in consultation with the Chair.

## **FREQUENCY OF MEETINGS**

The Group is scheduled to meet on a quarterly basis and individuals who cannot attend are requested to send a deputy.

Fraud response meetings will be arranged in response to allegations of fraud. Relevant personnel from the Membership of the Integrity Group will be invited dependent on the nature of the fraud allegation.

Ref	Category	Activity	Number of Days	Commentary
1.	Compliance	Contract Management	130	Testing of governance and internal controls in place over Contract Management arrangements with third parties to determine whether there is compliance with procurement rules and Management monitoring is adequate.
2.	Compliance	Corporate Fraud Enquiries	65	Respond to whistleblowing notifications.
3.	Data Match	Council Tax Reduction Scheme, Discounts and Exemptions	30	Data analytics on Council Tax Reduction Scheme, Discounts and Exemptions to determine whether these reductions are claimed legitimately.
4.	Data Match	National Fraud Initiative	75	Co-ordinate the NFI exercise across Council services, review and investigate data matches, and periodically produce reports on the outcomes. New data sets proposed by Cabinet Office associated with support funding to businesses re Covid-19 response.
5.	Other	Corporate Fraud Policy Framework	18	Support the Integrity Group with monitoring of policies and procedures review, update and communication. Assist with the self-assessment of compliance against the CIPFA code on Managing the Risk of Fraud and Corruption.
6.	Other	Fraud Vulnerability Assessments	55	Support operational Service Managers to assess fraud risks and put in place appropriate controls within processes and practices.
7.	Other	Fraud Awareness Training	33	Develop and deliver fraud awareness training modules (either face-to-face or via e-learning) to Management and Staff.
Corporate Fraud Total			406	



## **Annual Treasury Management Report 2019/20**

**Report by Gary Fairley, Chief Officer, Corporate Solutions**

### **Covering Report**

#### **1 Purpose of Report**

A draft of the Annual Treasury Management Report 2019/20 report is being presented today to Audit Committee.

The CIPFA Treasury Management Code of Practice 2017 requires that all Treasury Management reports are presented to an appropriate body for adequate scrutiny prior to being presented to full Council for approval. For Midlothian Council, this body is Audit Committee.

The report is presented in draft and as such any comments on this report from Audit Committee shall be included in the final report to Council.

The purpose of the report is to note the Treasury Management Annual Report for 2019/20.



## **Annual Treasury Management Report 2019/20**

**Report by Gary Fairley, Chief Officer, Corporate Solutions**

**Report for Decision**

### **1 Recommendations**

It is recommended that the Council

- a) note the Treasury Management Annual Report for 2019/20.

### **2 Purpose of Report/Executive Summary**

The purpose of the report is to inform members of the Treasury Management activity undertaken in 2019/20 and the year-end position.

**Date: 8 June 2020**

**Report Contact:**

**Gary Thomson, Senior Accountant**

**[gary.thomson@midlothian.gov.uk](mailto:gary.thomson@midlothian.gov.uk)**

**0131-271-3230**

### 3 Background

The main points arising from treasury activity in 2019/20 were:

- Total new long term borrowing taken in the year amounted to £50.000 million, comprising the following:-
  - Two £10.000 million maturity loans from PWLB, both drawn on 25 September 2019, with loan tenors of 20 years and 50 years respectively, and at interest rates of 1.76% and 1.68% respectively;
  - Two £15.000 million maturity loans from PWLB, both drawn on 12 March 2020, with loan tenors of 39.5 years and 48.5 years respectively, and at interest rates of 2.36% and 2.32% respectively;
- Total long term borrowing maturing in the year amounted to £9.201 million, comprising the following:-
  - One £8.400 million Maturity Loan with PWLB matured on 14 December 2019 (original tenor 8 years at an interest rate of 2.77%), refinanced by the PWLB borrowing undertaken on 25 September 2019;
  - £0.037 million of PWLB Annuities of various tenors and interest rates;
  - £0.633 million of Annuity and EIP loans from Deutsche Pfandbrief bank, and £0.131 million of Salix interest free loans.
- Three new long term investments were placed, which continue the strategy of cash backing the Council's reserves, as follows:-
  - £10.000 million placed on deposit with Rushmoor Borough Council, for an 18 month period at an interest rate of 1.15%, deposit date 22 July 2019 and maturity date 22 January 2021;
  - £15.000 million placed on deposit with Wokingham Borough Council, for a 36 month period at an interest rate of 1.60%, deposit date 25 March 2020 and maturity date 24 March 2023;
  - £15.000 million placed on deposit with Medway Council, for a 24 month period at an interest rate of 1.80%, deposit date 30 March 2020 and maturity date 30 March 2022;
- The average rate of interest paid on external debt was 3.44% in 2019/20, down from 3.62% in 2018/19 and reflecting the historically low interest rates secured on longer-term PWLB borrowing in 2019/20;
- The average rate of return on investments was 1.15% in 2019/20, exceeding the benchmark of 0.80% for the sixteenth year in succession;
- The pooled internal loans fund rate for General Fund and HRA decreased from 3.12% in 2018/19 (4<sup>th</sup> lowest in mainland Scotland – see Appendix 1) to 2.95% in 2019/20, which is again



expected to be one of the lowest when benchmarked against all mainland Authorities in Scotland;

- Were the pooled internal loans fund rate to have equated to the Scottish weighted average of 3.81%, this would have generated loan charges in 2019/20 of £19.0 million. The Council's actual 2019/20 loan charges for General Services and HRA were £16.4 million, representing a cash saving (compared to the Scotland average) of £2.6 million in 2019/20;
- The appointment of interest between HRA and General Fund was changed in 2017/18, with the HRA charged interest at the weighted average interest rate on the Council's long-term debt, removing interest rate risk for the HRA to support the long-term rent setting strategy. The interest charged to the General Fund provides support to the Council's medium term financial strategy and capital plans. This methodology was retained in 2019/20.
- No debt rescheduling was undertaken during 2019/20.

A detailed report "*Annual Treasury Management Review 2019/20*" on the activity during 2019/20 is attached as Appendix 2.

The Treasury Portfolio at the start and end of the financial year is shown in Tables 1 and 2 below.

Table 1: Loan Portfolio at 1 April 2019 and 31 March 2020

<b>Loan Type</b>	<b>Principal Outstanding 1 Apr 2019 £000's</b>	<b>Principal Outstanding 31 Mar 2020 £000's</b>	<b>Movement £000's</b>
PWLB Annuity	674	637	-37
PWLB Maturity	187,224	228,824	+41,600
LOBO	20,000	20,000	0
Forward Starting Loans	19,464	18,831	-633
Temporary Market Loans	9,000	0	-9,000
Salix Loans	916	785	-131
<b>Total Loans</b>	<b>237,279</b>	<b>269,077</b>	<b>+31,798</b>

Table 2: Investment Portfolio 1 April 2018 and 31 March 2019

<b>Investment Type</b>	<b>Principal Outstanding 1 Apr 2019 £000's</b>	<b>Principal Outstanding 31 Mar 2020 £000's</b>	<b>Movement £000's</b>
Bank Call Accounts	0	11,476	+11,476
Money Market Funds	9,767	14,901	+5,134
Bank Notice Accounts	49,985	14,985	-35,000
Bank Fixed Term Deposit Accounts	0	30,000	+30,000
Other Local Authorities	15,000	40,000	+25,000
<b>Total Investments</b>	<b>74,752</b>	<b>111,363</b>	<b>+36,611</b>

#### **4. Other Issues**

The Code recommends that Treasury reports are presented to and scrutinised by Audit Committee in advance of being considered by Council.

The report is being presented to Audit Committee on 22 June 2020 and to Council at the next meeting of Council thereafter, and will be updated to reflect any comments that the Audit Committee have.

### **5 Report Implications (Resource, Digital and Risk)**

#### **5.1 Resource**

Treasury Management activity during the year has been effective in minimising the cost of borrowing and maximising investment income within the parameters set by the strategy for the year.

Although benefits from Treasury Management activity continue to accrue there are no direct financial implications or other resource issues arising from this report.

The loan charges associated with Capital Expenditure and Treasury Management activity during 2019/20 are reported in the Financial Monitoring 2019/20 – General Fund Revenue report elsewhere on today's agenda.

#### **5.2 Digital**

None.

#### **5.3 Risk**

As the Council follows the requirements of CIPFA Code of Practice and the Prudential Code this minimises the risks involved in Treasury Management activities place. For those risks that do exist there are robust and effective controls in place to further mitigate the level of risks. These include further written Treasury Management Practices, which define the responsibilities of all staff involved.

#### **5.4 Ensuring Equalities (if required a separate IIA must be completed)**

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

#### **5.5 Additional Report Implications**

See Appendix A

#### **Appendices:-**

**Appendix 1: Loans Fund Rate Comparison with other Scottish Local Authorities**

**Appendix 2: Annual Treasury Management Review 2019/20**

**Appendix 3: Investment Benchmarking Analysis 2019/20**

## **APPENDIX A – Report Implications**

### **A.1 Key Priorities within the Single Midlothian Plan**

Not applicable

### **A.2 Key Drivers for Change**

Key drivers addressed in this report:

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

### **A.3 Key Delivery Streams**

Key delivery streams addressed in this report:

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

### **A.4 Delivering Best Value**

The report does not directly impact on Delivering Best Value.

### **A.5 Involving Communities and Other Stakeholders**

Although no external consultation has taken place, cognisance has been taken of professional advice obtained from Link Asset Services, the Council's appointed Treasury Consultants.

### **A.6 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.

### **A.7 Adopting a Preventative Approach**

Not applicable.

### **A.8 Supporting Sustainable Development**

Not applicable.

## Appendix 1:-

### Loans Fund Pooled Rate Comparison 2018/19

Authority	2018/19
West Dunbartonshire	2.770%
Dumfries & Galloway	3.050%
Perth & Kinross	3.055%
<b>Midlothian</b>	<b>3.120%</b>
Aberdeenshire	3.270%
East Lothian	3.270%
North Lanarkshire	3.540%
Inverclyde	3.650%
Fife	3.670%
Dundee City	3.695%
East Dunbartonshire	3.720%
Falkirk	3.740%
Argyll & Bute	3.800%
Aberdeen City	3.820%
West Lothian	3.860%
East Renfrewshire	3.880%
South Lanarkshire	3.940%
Glasgow City	4.000%
Highland	4.010%
South Ayrshire	4.010%
North Ayrshire	4.090%
Scottish Borders	4.100%
Renfrewshire	4.110%
East Ayrshire	4.150%
Stirling	4.160%
Moray	4.190%
Angus	4.350%
Edinburgh City	4.660%
Clackmannanshire	4.915%

The Pooled Loans Fund Rate combines the interest paid by the Council on money borrowed, with the interest earned by the Council on money invested, along with other charges such as internal interest allowed, premiums written off and treasury-related expenses to arrive at a weighted average “loans fund rate” figure for each authority, as noted in the final column above.

## **Appendix 2**

# **Annual Treasury Management Review 2019/20**

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Midlothian Council  
June 2020

## Contents

- 1 The Council's Capital Expenditure and Financing 2019/20
- 2 The Council's overall borrowing need
- 3 Treasury Position as at 31 March 2020
- 4 The Strategy for 2019/20
- 5 The Economy and Interest Rates
- 6 Borrowing Rates in 2019/20
- 7 Borrowing Outturn for 2019/20
- 8 Investment Rates in 2019/20
- 9 Investment Outturn for 2019/20
- 10 Performance Measurement
- 11 Conclusion

This Council is required by regulations issued under the Local Government in Scotland Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2019/20. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

During 2019/20 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 12/02/2019);
- a mid-year, (minimum), treasury update report (Council 12/11/2019);
- an annual review following the end of the year describing the activity compared to the strategy, (this report);

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they are reported to the full Council.



# 1. The Council's Capital Expenditure and Financing 2019/20

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

<b>Table 1: Capital Expenditure + Financing</b>			
	<b>2018/19</b>	<b>2019/20</b>	<b>2019/20</b>
	<b>Actual</b>	<b>Budget</b>	<b>Actual</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>
<b>General Fund</b>			
Capital Expenditure	18,209	45,373	30,978
Available Funding	18,045	25,051	26,062
<b>Borrowing Required</b>	<b>164</b>	<b>20,322</b>	<b>4,916</b>
<b>HRA</b>			
Capital Expenditure	14,718	54,519	24,936
Available Funding	11,086	5,507	11,951
<b>Borrowing Required</b>	<b>3,632</b>	<b>49,012</b>	<b>12,985</b>
<b>General Fund and HRA</b>			
Capital Expenditure	32,927	99,892	55,914
Available Funding	29,131	30,558	38,013
<b>Borrowing Required</b>	<b>3,796</b>	<b>69,334</b>	<b>17,901</b>

## 2. The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and what resources have been used to pay for the capital spend. It represents the 2019/20 unfinanced capital expenditure (see above table), plus prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLb] or the money markets), or utilising temporary cash resources within the Council.

**Reducing the CFR** – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Scheduled Debt Amortisation (or loans repayment), to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

- the application of additional capital financing resources (such as unapplied capital receipts); or
- charging more than the minimum loan repayment each year through an additional revenue charge.

The Council's CFR for the year is shown below, and represents a key prudential indicator.

Table 2: Council's Capital Financing Requirement			
CFR:	31-Mar-19	2019/20	31-Mar-20
	Actual	Budget	Actual
	£000	£000	£000
Opening balance	£ 280,214	£ 284,964	£ 274,582
Add Borrowing Required	£ 3,797	£ 69,334	£ 17,900
Less scheduled debt amortisation	£ (9,429)	£ (8,241)	£ (9,098)
Closing balance	£ 274,582	£ 325,196	£ 283,384

Borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.

**Gross borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2018/19) plus the estimates of any additional capital financing requirement for the current (2019/20) and next three financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2019/20. The table below highlights the Council's gross borrowing position against the CFR (excluding PFI schemes). The Council has complied with this prudential indicator.

<b>Table 3: Council's Gross Borrowing Position</b>			
	<b>31-Mar-19</b>	<b>2019/20</b>	<b>31-Mar-20</b>
	<b>Actual</b>	<b>Budget</b>	<b>Actual</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>
<b>Gross Borrowing</b>	£ 237,279	£ 290,770	£ 269,077
<b>CFR</b>	£ 274,582	£ 325,196	£ 283,384

**The authorised limit** – this Council has kept within its authorised external borrowing limit as shown by the table below. Once this has been set, the Council does not have the power to borrow above this level.

**The operational boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

<b>Table 4: Gross Borrowing against Authorised Limit / Operational Boundary</b>	
	<b>2019/20</b>
Authorised limit - borrowing	£524,349
Operational boundary - borrowing	£346,056
Maximum gross borrowing position	£248,652
Average gross borrowing position	£234,727

### 3. Treasury Position as at 31 March 2020

The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the Purpose section of this report, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2019/20 the Council's treasury (excluding borrowing by PFI and finance leases) position was as follows:

Table 5: Treasury Position						
	31 March 2019 Principal	Rate/ Return	Average Life (Yrs)	31 March 2020 Principal	Rate/ Return	Average Life (Yrs)
<b>Debt</b>						
<b>Fixed Rate Debt</b>						
PWLB	£ 187,899	3.75%	27.27	£ 229,462	3.43%	30.27
Market	£ 34,380	2.32%	23.20	£ 24,616	2.89%	30.70
<b>Total Fixed Rate Debt</b>	<b>£ 222,279</b>	<b>3.53%</b>	<b>26.64</b>	<b>£ 254,078</b>	<b>3.38%</b>	<b>30.31</b>
<b>Variable Rate Debt</b>						
PWLB	£ -	n/a	n/a	£ -	n/a	n/a
Market	£ 15,000	4.63%	31.71	£ 15,000	4.63%	31.71
<b>Total Variable Rate Debt</b>	<b>£ 15,000</b>	<b>4.63%</b>	<b>32.71</b>	<b>£ 15,000</b>	<b>4.63%</b>	<b>32.71</b>
<b>Total debt/gross borrowing</b>	<b>£ 237,279</b>	<b>3.47%</b>	<b>27.02</b>	<b>£ 269,078</b>	<b>3.47%</b>	<b>30.45</b>
<b>CFR</b>	<b>£ 274,879</b>			<b>£ 283,384</b>		
<b>Over/ (under) borrowing</b>	<b>£ (37,600)</b>			<b>£ (14,306)</b>		
<b>Investments</b>						
<b>Fixed Rate Investments</b>						
In House	£ 15,000	1.70%	1.0000	£ 70,000	1.43%	1.71
With Managers	£ -	n/a	n/a	£ -	n/a	n/a
<b>Total Fixed Rate Investments</b>	<b>£ 15,000</b>	<b>1.70%</b>	<b>1.00</b>	<b>£ 70,000</b>	<b>1.43%</b>	<b>1.71</b>
<b>Variable Rate Investments</b>						
In House	£ 59,751	0.96%	0.41	£ 26,378	0.59%	0.18
With Managers	£ -	n/a	n/a	£ -	n/a	n/a
<b>Total Variable Rate Investments</b>	<b>£ 59,751</b>	<b>0.96%</b>	<b>0.41</b>	<b>£ 26,378</b>	<b>0.59%</b>	<b>0.18</b>
<b>Total Investments</b>	<b>£ 74,751</b>	<b>1.11%</b>	<b>0.53</b>	<b>£ 96,378</b>	<b>1.20%</b>	<b>1.29</b>
<b>Net Borrowing</b>	<b>£ 162,528</b>			<b>£ 172,700</b>		

The maturity structure of the debt portfolio was as follows:

<b>Table 6: Maturity Structure of Debt Portfolio</b>						
	<b>31-Mar-19</b>		<b>2019/20</b>	<b>31-Mar-20</b>		
	<b>Actual</b>		<b>Original Limits</b>	<b>Actual</b>		
	<b>£000</b>	<b>%</b>	<b>%</b>	<b>£000</b>	<b>%</b>	
<b>Under 12 months</b>	£ 18,263	8%	0% to 50%	£ 9,230	3%	
<b>12 months to 2 years</b>	£ 9,266	4%	0% to 50%	£ 1,490	1%	
<b>2 years to 5 years</b>	£ 3,827	2%	0% to 50%	£ 3,720	1%	
<b>5 years to 10 years</b>	£ 5,509	2%	0% to 50%	£ 14,560	5%	
<b>10 years to 20 years</b>	£ 62,653	26%	0% to 50%	£ 63,229	23%	
<b>20 years to 30 years</b>	£ 15,179	6%	0% to 50%	£ 14,265	5%	
<b>30 years to 40 years</b>	£ 75,534	32%	0% to 50%	£ 90,534	34%	
<b>40 years to 50 years</b>	£ 42,048	18%	0% to 50%	£ 67,049	25%	
<b>50 years and above</b>	£ 5,000	2%	0% to 50%	£ 5,000	2%	
<b>Total</b>	<b>£ 237,279</b>	<b>100%</b>		<b>£ 269,077</b>	<b>100%</b>	

The maturity structure of the investment portfolio was as follows:

<b>Table 7: Maturity Structure of Investment Portfolio</b>		
	<b>31-Mar-19</b>	<b>31-Mar-20</b>
	<b>£000</b>	<b>£000</b>
<b>Investments</b>		
Under 1 Year	£ 74,751	£ 81,363
Over 1 Year	£ -	£ 30,000
<b>Total</b>	<b>£ 74,751</b>	<b>£ 111,363</b>

The exposure to fixed and variable interest rates on debt was as follows:-

<b>Table 8: Fixed/Variable Interest Rate Exposure of Debt Portfolio</b>						
	<b>31-Mar-19</b>		<b>2019/20</b>	<b>31-Mar-20</b>		
	<b>Actual</b>		<b>Original Limits</b>	<b>Actual</b>		
	<b>£000</b>	<b>%</b>	<b>%</b>	<b>£000</b>	<b>%</b>	
<b>Fixed Interest Rate Exposure</b>	£222,279	92%	0% to 100%	£ 254,077	94%	
<b>Variable Interest Rate Exposure</b>	£ 15,000	6%	0% to 30%	£ 15,000	6%	
<b>Total</b>	<b>£ 237,279</b>	<b>98%</b>		<b>£ 269,077</b>	<b>100%</b>	

## 4. The Strategy for 2019/20

During 2019-20, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure.

A cost of carry remained during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. the Chief Officer, Corporate Solutions therefore monitored interest rates in financial markets and adopted a pragmatic strategy to take new long term borrowings based on the low interest rate environment and the Council's capital plans over the current and forthcoming financial years.

Interest rate forecasts expected only gradual rises in medium and longer term fixed borrowing rates during 2019/20 and the two subsequent financial years.

Link Asset Services Interest Rate View 5.8.19											
	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25
3 Month LIBID	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20
6 Month LIBID	0.80	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40
12 Month LIBID	1.00	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60
5yr PWLB Rate	1.20	1.30	1.50	1.60	1.70	1.70	1.80	1.90	2.00	2.00	2.10
10yr PWLB Rate	1.50	1.60	1.80	1.90	2.00	2.00	2.10	2.20	2.30	2.30	2.40
25yr PWLB Rate	2.10	2.30	2.40	2.50	2.60	2.70	2.70	2.80	2.90	3.00	3.00
50yr PWLB Rate	2.00	2.20	2.30	2.40	2.50	2.60	2.60	2.70	2.80	2.90	2.90

Link Asset Services Interest Rate View 31.3.20								
	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 Month LIBID	0.45	0.40	0.35	0.30	0.30	0.30	0.30	0.30
6 Month LIBID	0.60	0.55	0.50	0.45	0.40	0.40	0.40	0.40
12 Month LIBID	0.75	0.70	0.65	0.60	0.55	0.55	0.55	0.55
5yr PWLB Rate	1.90	1.90	1.90	2.00	2.00	2.00	2.10	2.10
10yr PWLB Rate	2.10	2.10	2.10	2.20	2.20	2.20	2.30	2.30
25yr PWLB Rate	2.50	2.50	2.50	2.60	2.60	2.60	2.70	2.70
50yr PWLB Rate	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50

Investment returns remained low during 2019/20. The expectation for interest rates within the treasury management strategy for 2019/20 was that Bank Rate would stay at 0.75% during 2019/20 as it was not expected that the MPC would be able to deliver on an increase in Bank Rate until the Brexit issue was finally settled. However, there was an expectation that Bank Rate would rise after that issue was settled, but would only rise to 1.0% during 2020.

Rising concerns over the possibility that the UK could leave the EU at the end of October 2019 caused longer term investment rates to be on a falling trend for most of April to September. They then rose after the end of October deadline was rejected by the Commons but fell back again in January before recovering again after the 31 January departure of the UK from the EU. When the coronavirus outbreak hit the UK in February/March, rates initially plunged but then rose sharply back up again due to a shortage of liquidity in financial markets. As longer term rates were significantly higher than shorter term rates during the year, value was therefore sought by placing longer term investments where cash balances were sufficient to allow this.

While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

## 5. The Economy and Interest Rates

**UK. Brexit.** The main issue in 2019 was the repeated battles in the House of Commons to agree on one way forward for the UK over the issue of Brexit. This resulted in the resignation of Theresa May as the leader of the Conservative minority Government and the election of Boris Johnson as the new leader, on a platform of taking the UK out of the EU on 31 October 2019. The House of Commons duly frustrated that renewed effort and so a general election in December settled the matter once and for all by a decisive victory for the Conservative Party: that then enabled the UK to leave the EU on 31 January 2020. However, this still leaves much uncertainty as to whether there will be a reasonable trade deal achieved by the target deadline of the end of 2020. It is also unclear as to whether the coronavirus outbreak may yet impact on this deadline; however, the second and third rounds of negotiations have already had to be cancelled due to the virus.

Economic growth in 2019 has been very volatile with quarter 1 unexpectedly strong at 0.5%, quarter 2 down at -0.2%, quarter 3 bouncing back up to +0.5% and quarter 4 flat at 0.0%, +1.1% y/y. 2020 started with optimistic business surveys pointing to an upswing in growth after the ending of political uncertainty as a result of the decisive result of the general election in December settled the Brexit issue. However, the three monthly GDP statistics in January were disappointing, being stuck at 0.0% growth. Since then, the whole world has changed as a result of the coronavirus outbreak. It now looks likely that the closedown of whole sections of the economy will result in a fall in GDP of at least 15% in quarter two. What is uncertain, however, is the extent of the damage that will be done to businesses by the end of the lock down period, when the end of the lock down will occur, whether there could be a second wave of the outbreak, how soon a vaccine will be created and then how quickly it can be administered to the population. This leaves huge uncertainties as to how quickly the economy will recover.

After the Monetary Policy Committee raised Bank Rate from 0.5% to 0.75% in August 2018, Brexit uncertainty caused the MPC to sit on its hands and to do nothing until March 2020; at this point it was abundantly clear that the coronavirus outbreak posed a huge threat to the economy of the UK. Two emergency cuts in Bank Rate from 0.75% occurred in March, first to 0.25% and then to 0.10%. These cuts were accompanied by an increase in quantitative easing (QE), essentially the purchases of gilts (mainly) by the Bank of England of £200bn. The Government and the Bank were also very concerned to stop people losing their jobs during this lock down period. Accordingly, the Government introduced various schemes to subsidise both employed and self-employed jobs for three months while the country is locked down. It also put in place a raft of other measures to help businesses access loans from their banks, (with the Government providing guarantees to the banks against losses), to tide them over the lock down period when some firms may have little or no income. However, at the time of writing, this leaves open a question as to whether some firms will be solvent, even if they take out such loans, and some may also choose to close as there is, and will be, insufficient demand for their services. At the time of writing, this is a rapidly evolving situation so there may



be further measures to come from the Bank and the Government in April and beyond. The measures to support jobs and businesses already taken by the Government will result in a huge increase in the annual budget deficit in 2020/21 from 2%, to nearly 11%. The ratio of debt to GDP is also likely to increase from 80% to around 105%. In the Budget in March, the Government also announced a large increase in spending on infrastructure; this will also help the economy to recover once the lock down is ended. Provided the coronavirus outbreak is brought under control relatively swiftly, and the lock down is eased, then it is hoped that there would be a sharp recovery, but one that would take a prolonged time to fully recover previous lost momentum.

Inflation has posed little concern for the MPC during the last year, being mainly between 1.5 – 2.0%. It is also not going to be an issue for the near future as the world economy will be heading into a recession which is already causing a glut in the supply of oil which has fallen sharply in price. Other prices will also be under downward pressure while wage inflation has also been on a downward path over the last half year and is likely to continue that trend in the current environment. While inflation could even turn negative in the Eurozone, this is currently not likely in the UK.

Employment had been growing healthily through the last year but it is obviously heading for a big hit in March – April 2020. The good news over the last year is that wage inflation has been significantly higher than CPI inflation which means that consumer real spending power had been increasing and so will have provided support to GDP growth. However, while people cannot leave their homes to do non-food shopping, retail sales will also take a big hit.

**USA.** Growth in quarter 1 of 2019 was strong at 3.1% but growth fell back to 2.0% in quarter 2 and 2.1% in quarters 3 and 4. The slowdown in economic growth resulted in the Fed cutting rates from 2.25-2.50% by 0.25% in each of July, September and October. Once coronavirus started to impact the US in a big way, the Fed took decisive action by cutting rates twice by 0.50%, and then 1.00%, in March, all the way down to 0.00 – 0.25%. Near the end of March, Congress agreed a \$2trn stimulus package (worth about 10% of GDP) and new lending facilities announced by the Fed which could channel up to \$6trn in temporary financing to consumers and firms over the coming months. Nearly half of the first figure is made up of permanent fiscal transfers to households and firms, including cash payments of \$1,200 to individuals.

The loans for small businesses, which convert into grants if firms use them to maintain their payroll, will cost \$367bn and 100% of the cost of lost wages for four months will also be covered. In addition there will be \$500bn of funding from the Treasury's Exchange Stabilization Fund which will provide loans for hard-hit industries, including \$50bn for airlines.

However, all this will not stop the US falling into a sharp recession in quarter 2 of 2020; some estimates are that growth could fall by as much as 40%. The first two weeks in March of initial jobless claims have already hit a total of 10 million and look headed for a total of 15 million by the end of March.

**EUROZONE.** The annual rate of GDP growth has been steadily falling, from 1.8% in 2018 to only 0.9% y/y in quarter 4 in 2019. The European Central Bank

(ECB) ended its programme of quantitative easing purchases of debt in December 2018, which meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by purchases of debt. However, the downturn in EZ growth, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), prompted the ECB to take new measures to stimulate growth. At its March 2019 meeting it announced a third round of TLTROs; this provided banks with cheap two year maturity borrowing every three months from September 2019 until March 2021. However, since then, the downturn in EZ and world growth has gathered momentum so at its meeting in September 2019, it cut its deposit rate further into negative territory, from -0.4% to -0.5% and announced a resumption of quantitative easing purchases of debt to start in November at €20bn per month, a relatively small amount, plus more TLTRO measures. Once coronavirus started having a major impact in Europe, the ECB took action in March 2020 to expand its QE operations and other measures to help promote expansion of credit and economic growth. What is currently missing is a coordinated EU response of fiscal action by all national governments to protect jobs, support businesses directly and promote economic growth by expanding government expenditure on e.g. infrastructure; action is therefore likely to be patchy.

**CHINA.** Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium-term risks have also been increasing. The major feature of 2019 was the trade war with the US. However, this has been eclipsed by being the first country to be hit by the coronavirus outbreak; this resulted in a lock down of the country and a major contraction of economic activity in February-March 2020. While it appears that China has put a lid on the virus by the end of March, these are still early days to be confident and it is clear that the economy is going to take some time to recover its previous rate of growth. Ongoing economic issues remain, in needing to make major progress to eliminate excess industrial capacity and to switch investment from property construction and infrastructure to consumer goods production. It also needs to address the level of non-performing loans in the banking and credit systems.

**JAPAN** has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It appears to have missed much of the domestic impact from coronavirus in 2019-20 but the virus is at an early stage there.

**WORLD GROWTH.** The trade war between the US and China on tariffs was a major concern to financial markets and was depressing worldwide growth during 2019, as any downturn in China would spill over into impacting countries supplying raw materials to China. Concerns were particularly focused on the synchronised general weakening of growth in the major economies of the world. These concerns resulted in government bond yields in the developed world falling significantly during 2019. In 2020, coronavirus is the big issue which is going to sweep around the world and have a major impact in causing a world recession in growth in 2020.

## 6. Borrowing Rates in 2019/20

PWLB rates are based on, and are determined by, gilt (UK Government bonds) yields through H.M.Treasury determining a specified margin to add to gilt yields. There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels. The context for that was heightened expectations that the US could have been heading for a recession in 2020, and a general background of a downturn in world economic growth, especially due to fears around the impact of the trade war between the US and China, together with inflation generally at low levels in most countries and expected to remain subdued; these conditions were conducive to very low bond yields. While inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. We have therefore seen, over the last year, many bond yields up to 10 years in the Eurozone turn negative. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. The other side of this coin is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.

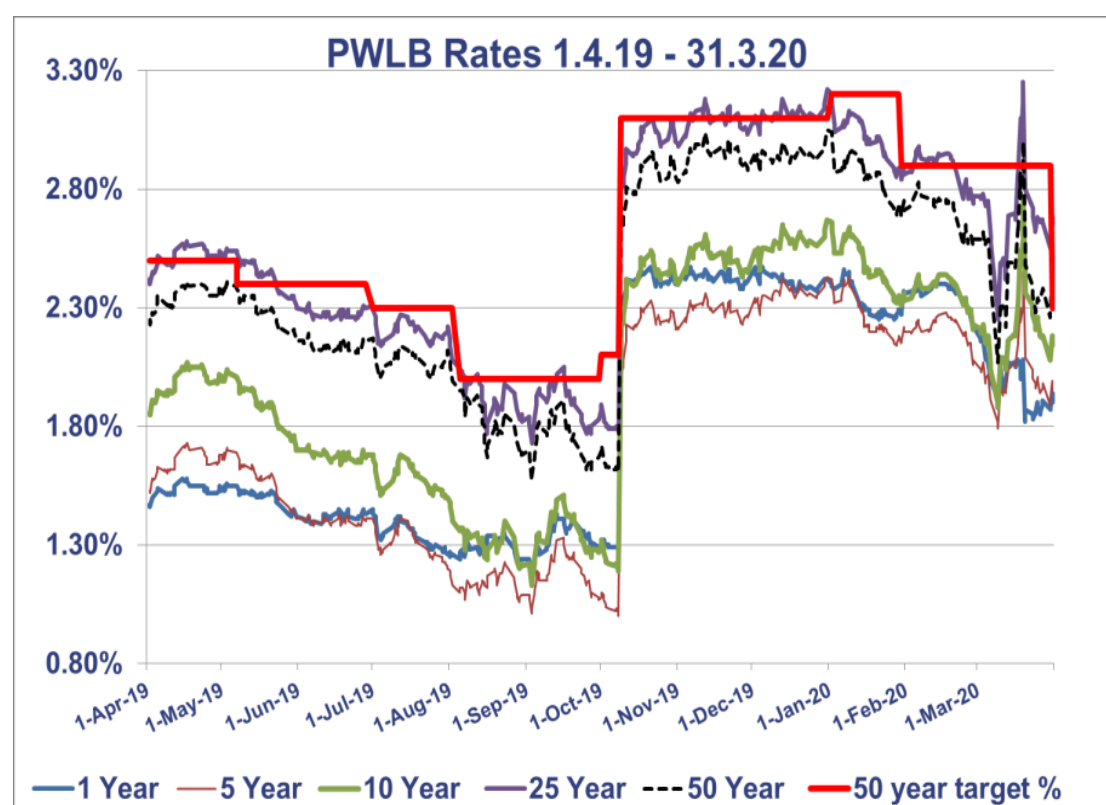
Gilt yields were on a generally falling trend during the last year up until the coronavirus crisis hit western economies. Since then, gilt yields have fallen sharply to unprecedented lows as investors have panicked in selling shares in anticipation of impending recessions in western economies, and moved cash into safe haven assets i.e. government bonds. However, major western central banks also started quantitative easing purchases of government bonds which will act to maintain downward pressure on government bond yields at a time when there is going to be a huge and quick expansion of government expenditure financed by issuing government bonds; (this would normally cause bond yields to rise). At the close of the day on 31 March, all gilt yields from 1 to 5 years were between 0.12 – 0.20% while even 25-year yields were at only 0.83%.

However, HM Treasury has imposed two changes in the margins over gilt yields for PWLB rates in 2019-20 without any prior warning; the first on 9 October 2019, added an additional 1% margin over gilts to all PWLB rates. That increase was then partially reversed for some forms of borrowing on 11 March 2020, at the same time as the Government announced in the Budget a programme of increased spending on infrastructure expenditure. It is clear that the Treasury intends to put a stop to local authorities borrowing money from the PWLB to purchase commercial property if the aim is solely to generate an income stream.

Following the changes on 11 March 2020 in margins over gilt yields, the current situation is as follows: -

- PWLB Standard Rate is gilt plus 200 basis points (G+200bps)
- PWLB Certainty Rate is gilt plus 180 basis points (G+180bps)
- PWLB HRA Standard Rate is gilt plus 100 basis points (G+100bps)
- PWLB HRA Certainty Rate is gilt plus 80bps (G+80bps)
- Local Infrastructure Rate is gilt plus 60bps (G+60bps)

There is likely to be little upward movement in PWLB rates over the next two years as it will take national economies a prolonged period to recover all the momentum they will lose in the sharp recession that will be caused during the coronavirus shut down period. Inflation is also likely to be very low during this period and could even turn negative in some major western economies during 2020-21.



	1 Year	5 Year	10 Year	25 Year	50 Year
01/04/2019	1.46%	1.52%	1.84%	2.41%	2.24%
31/03/2020	1.90%	1.95%	2.14%	2.65%	2.39%
Low	1.17%	1.00%	1.13%	1.73%	1.57%
Date	03/09/2019	08/10/2019	03/09/2019	03/09/2019	03/09/2019
High	2.47%	2.45%	2.76%	3.25%	3.05%
Date	21/10/2019	19/03/2020	19/03/2020	19/03/2020	31/12/2019
Average	1.83%	1.77%	2.00%	2.56%	2.40%

**Short-dated market money:-** sourced from other UK public bodies, rates fluctuated throughout the year from 0.15%-0.80% for 1 to 12 month maturities.

## 7. Borrowing Outturn for 2019/20

### New Treasury Borrowing:-

New loans were drawn to fund the net unfinanced capital expenditure and naturally maturing debt.

The loans drawn were:-

Table 9: New Loans Taken in Financial Year 2019/20						
Lender	Date Taken	Principal £000's	Interest Rate	Fixed/ Variable	Maturity Date	Term (Yrs)
PWLB Maturity	25 Sep 2019	£ 10,000	1.76%	Fixed	25 Sep 1939	20.00
PWLB Maturity	25 Sep 2019	£ 10,000	1.68%	Fixed	25 Sep 2069	50.00
PWLB Maturity	12 Mar 2020	£ 15,000	2.36%	Fixed	12 Sep 2059	39.50
PWLB Maturity	12 Mar 2020	£ 15,000	2.32%	Fixed	12 Sep 2068	48.50
Market	Various	£ 26,500	0.23%-0.82%	Variable interest rate	Various	0.09-0.18
<b>Total</b>		<b>£ 76,500</b>				

### Maturing Debt:-

The following table gives details of treasury debt maturing during the year:-

Table 10: Maturing Debt in Financial Year 2019/20						
Lender	Date Repaid	Principal £000's	Interest Rate	Fixed/ Variable	Date Originally Taken	Original Term (Yrs)
PWLB	14 Dec 2019	£ 8,400	2.77%	Fixed	14 Dec 2011	8.00
Salix	Various	£ 131	0.00%	Fixed	Various	7-8 years
Deutsche Pfandbriefbank	Various	£ 357	2.63%	Fixed	29 Jun 2017	28.00
Deutsche Pfandbriefbank	Various	£ 276	2.73%	Fixed	15 Nov 2018	25.50
Market	Various	£ 35,500	0.23%-0.82%	Variable interest rate	Various	0.09-0.18
<b>Total</b>		<b>£ 44,664</b>				

### Rescheduling:-

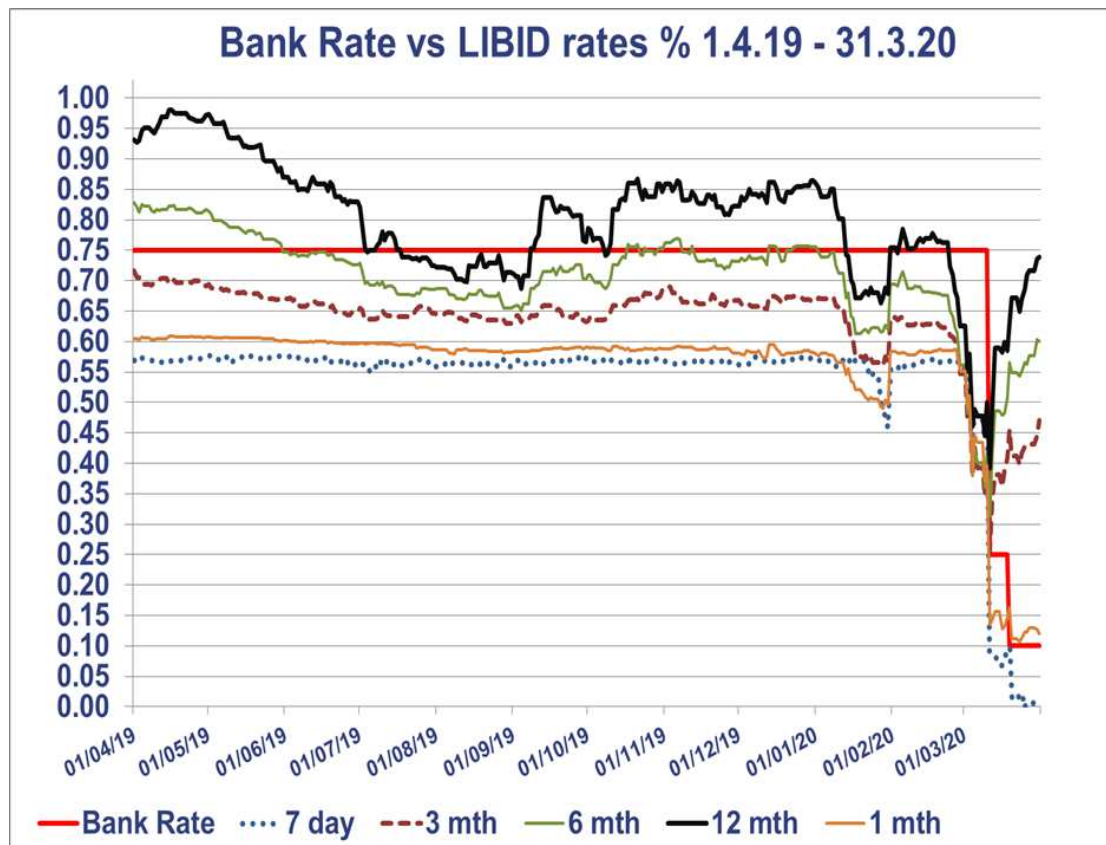
No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

### Summary of debt transactions:-

The average interest rate payable on external debt decreased from 3.62% at the start of 2019/20 to 3.44% at the end of 2019/20. The average life of debt within the loan portfolio lengthened from 26.96 years to 30.33 years.

## 8. Investment Rates in 2019/20

Money market fund rates started the year between 0.31%-0.78%, trending at base rate levels throughout the year, and mirroring the decreases in bank rate, with a slight lag due to the longer durational element of money market fund portfolios.



## 9. Investment Outturn for 2019/20

### **Investment Policy:-**

The Council's investment policy is governed by Scottish Government Investment Regulations, which have been implemented in the annual investment strategy approved by the Council on 12 February 2019. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

### **Investments held by the Council:-**

The Council maintained an average balance of £86.727 million of internally managed funds. The internally managed funds earned an average rate of return of 1.15%. The comparable performance indicator is the average 12-month LIBID un-compounded rate, which was 0.80%.



## 10. Performance Measurement

One of the key requirements in the Code is the formal introduction of performance measurement relating to investments, debt and capital financing activities.

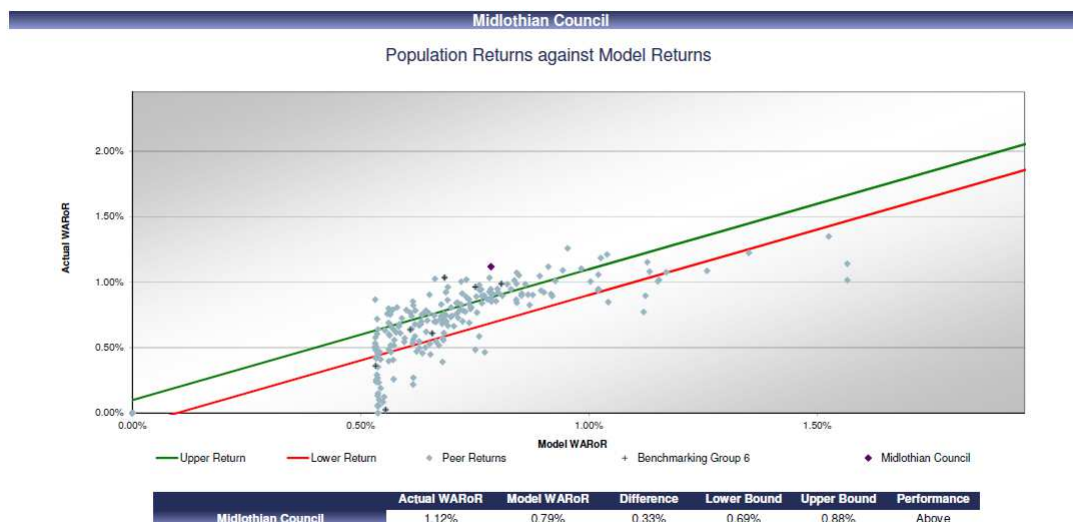
### Loans Fund Rate

Combining the interest paid (earned) on external debt (investments) with charges for premiums written off and internal interest allowed into an average Loans Fund Rate, Midlothian's result of 3.12% for 2018/19 was the fourth lowest Loans Fund Rate amongst all mainland authorities in Scotland (see Appendix 1).

The comparative Loans Fund Rate for 2019/20, of 2.95%, is once again expected to be one of the lowest when benchmarked against all mainland authorities in Scotland (note that at present, these benchmark figures are not yet available).

### Investment Benchmarking

The Council participates in the Scottish Investment Benchmarking Group set up by its Treasury Management Consultants, Capita. This service provided by Capita provides benchmarking data to authorities for reporting and monitoring purposes, by measuring the security, liquidity and yield within an individual authority portfolio. Based on the Council's investments as at 31 March 2020, the Weighted Average Rate of Return (WARoR) on investments of 1.12% against other authorities is shown in the graph below:-



*\* Models for 30 June 2019, 30 September 2019 and 31 December 2019 are attached as Appendix 3.*

As can be seen from the above graph, Midlothian is performing above the Capita model benchmarks (red to green lines), and is achieving one of the highest Weighted Average Rates of Return (WARoR) for the Weighted Average



Credit Risk held, not only amongst peer Councils within the Benchmarking Group but also amongst the population of authorities across the UK.

### **Debt Performance**

Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide. In this respect, the relevant figures for Midlothian are incorporated in the table in Section 3.

## 11. Conclusion

The Council's overall cost of borrowing continues to benefit significantly from proactive Treasury Management activity.

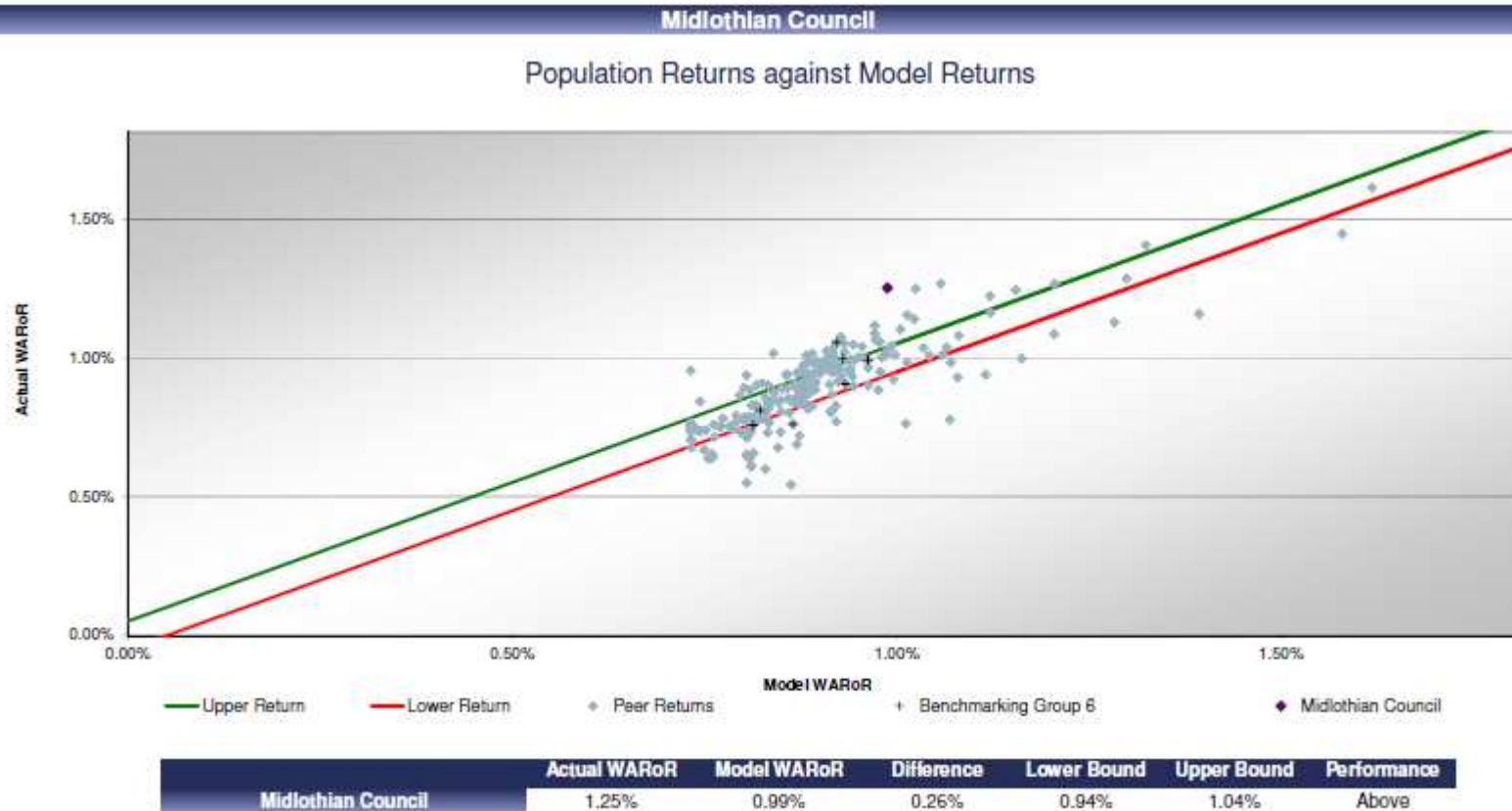
The cost of long term borrowing has been maintained by taking up opportunities to borrow from the PWLB at low interest rates.

A better than average return on investments has been achieved for the sixteenth consecutive year and Midlothian continues to perform above the Link model benchmarks and is achieving one of the highest Weighted Average Rates of Return (WARoR) for the Weighted Average Credit Risk held, not only amongst peer Councils within the Benchmarking Group but also amongst the population of authorities across the UK.

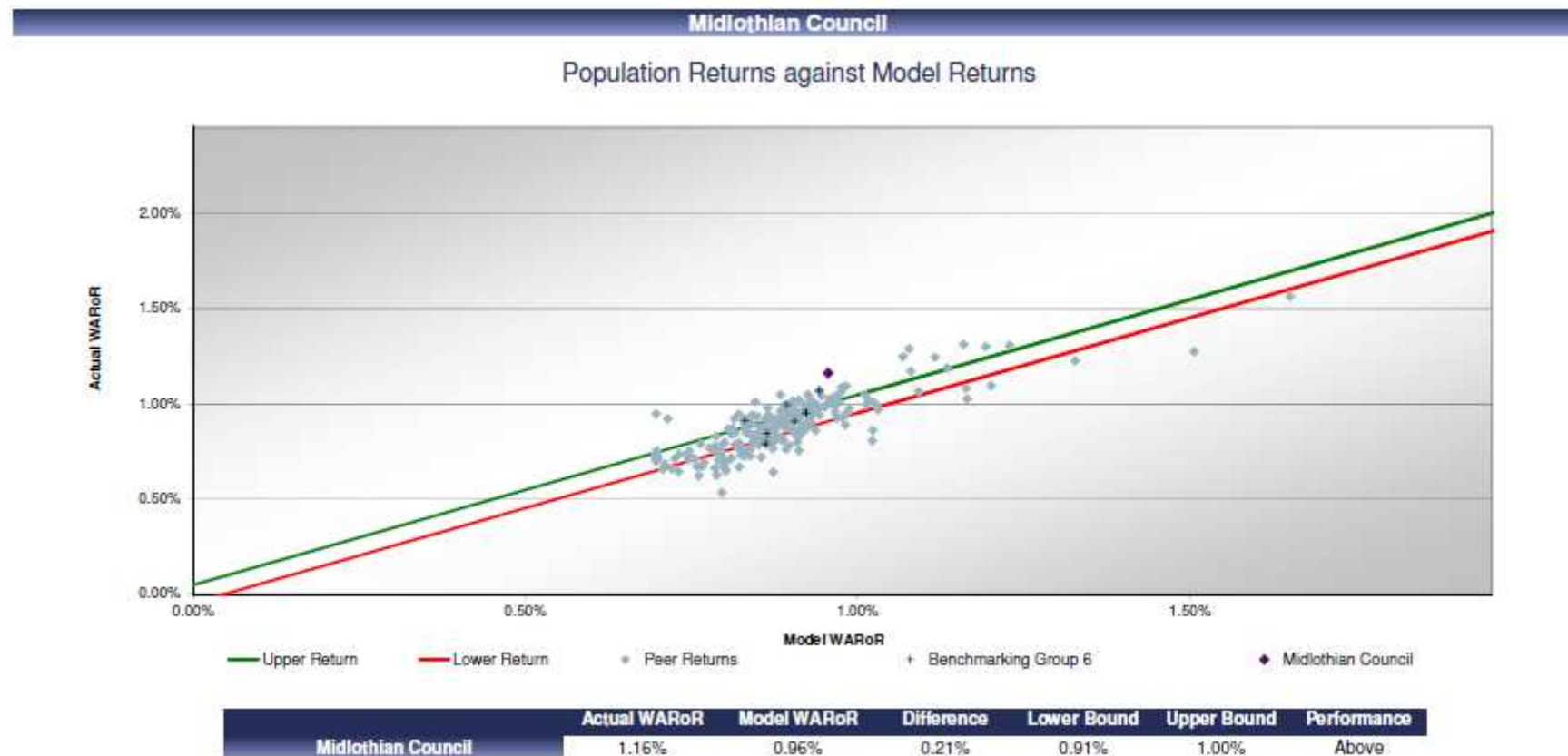
Overall Midlothian's Loans Fund Rate of 2.95% for the year is expected to be one of the lowest when benchmarked against all mainland Authorities in Scotland.

## Appendix 3

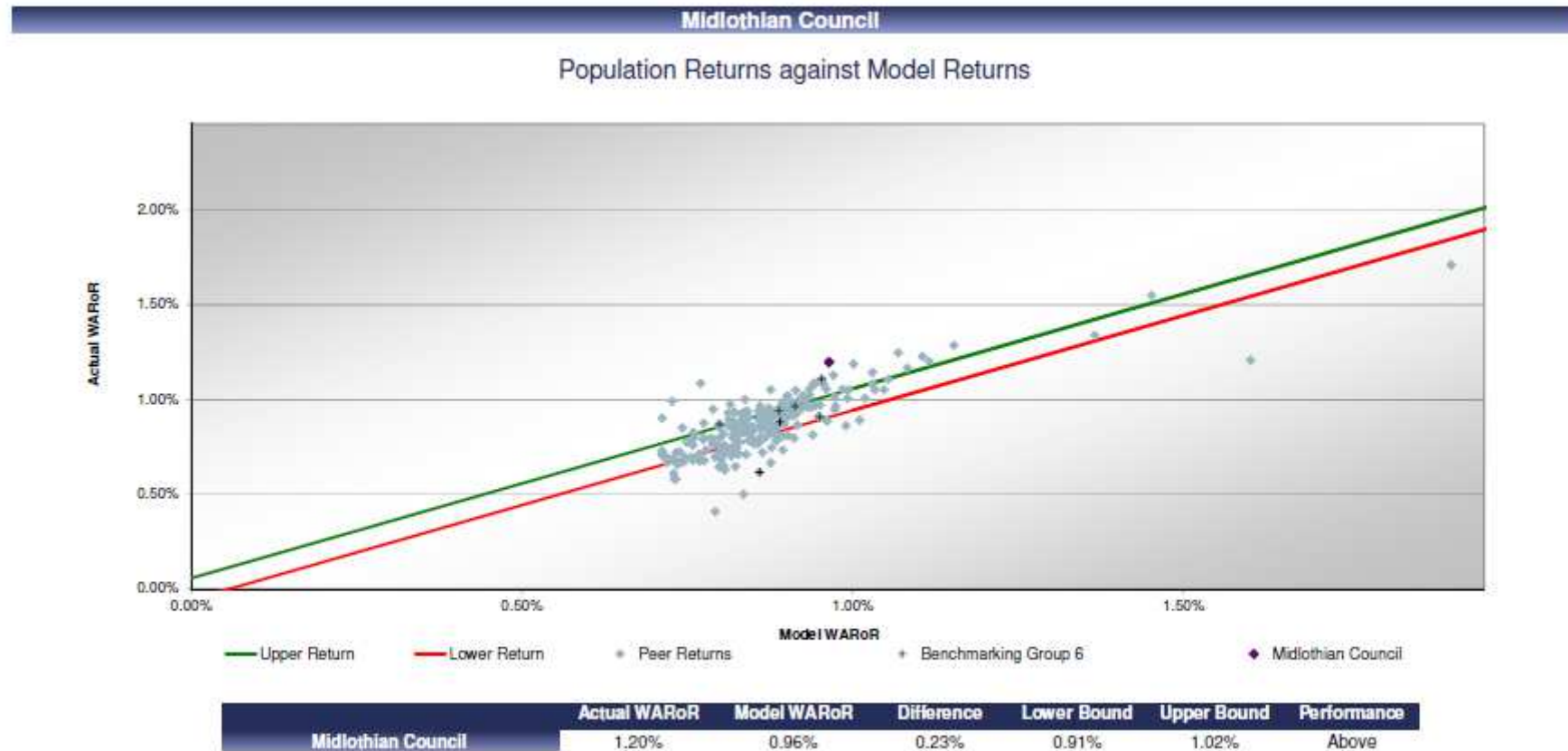
### Midlothian Council Investment Portfolio return as at 30 June 2019



## Midlothian Council Investment Portfolio return as at 30 September 2019



## Midlothian Council Investment Portfolio return as at 31 December 2019





## **Financial Statement 2019/20**

### **Report by Gary Fairley, Chief Officer Corporate Solutions**

#### **Report for Decision**

#### **1 Recommendations**

It is recommended that Audit Committee:

- a) Note that at the time of writing this report work continues to finalise the unaudited financial statements and that financial statements are expected to be submitted to the auditor by 30<sup>th</sup> June;
- b) Agree to remit to the Executive Director Place, in discussion with the Chair of the Audit Committee, arrangements for a special meeting/reconvened meeting of the Audit Committee prior to 31 August 2020 to consider the unaudited financial statements.

#### **2 Executive Summary**

The purpose of this report is to secure arrangements for Audit Committee to consider the unaudited financial statements for 2019/20 as submitted to the Auditor.

**Date: 15<sup>th</sup> June 2020**

**Report Contact: Gary Fairley. Chief Officer Corporate Solutions**

Email: gary.fairley@midlothian.gov.uk

### 3 The Local Authority Accounts (Scotland) Regulations 2014

Section 8 of the Local Authority Accounts (Scotland) regulations 2014 sets out the requirements in respect of unaudited accounts;

*(7) The Annual Accounts must be submitted to the auditor no later than 30th June immediately following the financial year to which the Annual Accounts relate.*

*(8) The local authority must publish a copy of the Annual Accounts submitted to the auditor, clearly identified as an unaudited version, on a website of the authority from the date they are submitted until the date on which the audited Annual Accounts are published in accordance with regulation 11.*

*(9) A local authority or a committee of that authority whose remit includes audit or governance functions must meet to consider the unaudited Annual Accounts as submitted to the auditor.*

*(10) The meeting referred to in paragraph (9) must be held no later than 31st August immediately following the financial year to which the Annual Accounts relate.*

In recognition of the impact of COVID 19 on Council resources and ways of working The Coronavirus (Scotland) Act 2020 included provisions which allows Councils to extend the dates relating to preparation and publication of financial statements if required. However it is not expected that these provisions will be required and that the unaudited financial statements will be submitted to the Auditor before the 30<sup>th</sup> June.

The Council's Finance Team has been able to make excellent progress in preparing the financial statements whilst working remotely and supporting the Council's response to the pandemic. However it was considered appropriate to provide additional time before I, as Section 95 Officer, certify the accounts. The additional time allows for there to be fuller consideration of the content of the financial statements particularly in respect of material estimations, for example Property Plant and Equipment valuations as well as the additional disclosures necessary as a consequence of COVID 19.

Accordingly to provide Audit Committee with adequate time to consider the unaudited accounts (which will be circulated to members of the committee at the same time as submitted to the Auditor) it is recommended that the Executive Director Place, in discussion with the Chair of the Audit Committee, make arrangements for a special meeting/reconvened meeting of the Audit Committee prior to 31 August 2020 to consider the unaudited accounts.

Considered separately on today's agenda is an addendum to the audit plan which considers the COVID-19 impact on the Audit though members should note that the intention is still to complete the Audit by 30 September 2020.



#### **4 Report Implications (Resource, Digital and Risk)**

##### **4.1 Resource**

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

##### **4.2 Digital**

None

##### **4.3 Risk**

The proposals mitigate the risk of audit committee not having adequate time to consider the financial statements in advance of today's meeting.

##### **4.4 Ensuring Equalities**

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

## APPENDIX A – Report Implications

### A.1 Key Priorities within the Single Midlothian Plan

Financial Stewardship supports the delivery of the key priorities and ensuring Audit Committee has adequate time to consider the financial statements supports the audit committee in promoting effective financial stewardship.

### A.2 Key Drivers for Change

Key drivers addressed in this report:

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

### A.3 Key Delivery Streams

Key delivery streams addressed in this report:

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

### A.4 Delivering Best Value

The report does not directly impact on Delivering Best Value.

### A.5 Involving Communities and Other Stakeholders

There has been engagement with EY our external Auditors during the completion of the financial statements.

### A.6 Impact on Performance and Outcomes

There is no impact on performance or outcomes.

### A.7 Adopting a Preventative Approach

There is no direct impact on the Councils approach to prevention.

### A.8 Supporting Sustainable Development

There are no direct sustainability issues arising from this report.

**Audit Committee Annual Report 2019/20**  
**Report by Chair of Audit Committee****1. Purpose of the Report**

The purpose of this report is to provide Members with the Audit Committee Annual Report 2019/20 and the annual self-assessments of the Committee against best practice.

**2. Background**

It is important that the Council's Audit Committee fully complies with best practice guidance on Audit Committees to ensure it can demonstrate its effectiveness as a scrutiny body as a foundation for sound corporate governance for the Council.

The Chartered Institute of Public Finance and Accountancy (CIPFA) issued an updated guidance note Audit Committees Practical Guidance for Local Authorities and Police 2018 Edition (hereinafter referred to as CIPFA Audit Committees Guidance). It incorporates CIPFA's Position Statement: Audit Committees in Local Authorities and Police which sets out CIPFA's view of the role and functions of an Audit Committee. The CIPFA Audit Committees Guidance includes the production of an annual report on the performance of the Audit Committee against its remit for submission to the Council.

**3. Audit Committee Annual Report 2019/20 and Self-Assessments**

The Audit Committee Annual Report 2019/20, which is appended to this report as Appendix 1 for consideration, is intended both to provide assurance to full Council and to identify areas of improvement which are designed to enhance the Audit Committee's effectiveness as a scrutiny body. Midlothian Council continues to adopt this best practice.

The Audit Committee carried out self-assessments of Compliance with the Good Practice Principles Checklist and Evaluation of Effectiveness Toolkit from the CIPFA Audit Committees Guidance during an Informal Session on 10 March 2020 facilitated by the Chief Internal Auditor. The self-assessments are appended to this report as Appendix 2 (Good Practice Principles) and Appendix 3 (Effectiveness) for consideration.

The outcome of the self-assessments was a medium degree of performance against the good practice principles and a medium degree of effectiveness. Improvements were identified focussing on skills and knowledge competency to fulfil role.

## **4. Report Implications**

### **4.1 Resource**

The Council has provided support and resources to the Audit Committee throughout the year including a Democratic Services Officer as the Minute secretary.

In terms of accountability and independence to ensure conformance with the Public Sector Internal Audit Standards (PSIAS), the Chief Internal Auditor reports functionally to the Audit Committee as outlined within the Internal Audit Charter.

### **4.2 Risk**

The role of the Audit Committee includes the high level oversight of the effectiveness of the Council's systems of internal financial control, internal control and governance, including risk management.

There is a risk that the Audit Committee does not fully comply with best practice guidance thus limiting its effectiveness as a scrutiny body as a foundation for sound corporate governance. The completion of the annual self-assessment and identification of improvement actions as evidenced through this Annual Report will mitigate this risk.

### **4.3 Single Midlothian Plan**

Themes addressed in this report:

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

### **4.4 Key Priorities within the Single Midlothian Plan**

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

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

### **4.5 Impact on Performance and Outcomes**

The members of the Audit Committee have reflected on the performance and outcomes against the remit of the Committee through the completion of annual self-assessments. The identification of improvement actions as evidenced through the Annual Report are designed to enhance its effectiveness as a scrutiny body as a foundation for sound corporate governance for the Council.

#### **4.6 Adopting a Preventative Approach**

Assurances received by the Audit Committee from Management, Internal Audit and External Audit set out the assessment of prevention and detection internal controls and governance arrangements.

#### **4.7 Involving Communities and Other Stakeholders**

The Audit Committee in fulfilling its governance role acts as a bridge between the Council and other stakeholders.

#### **4.8 Ensuring Equalities**

There are no equalities issues with regard to this report.

#### **4.9 Supporting Sustainable Development**

There are no sustainability issues with regard to this report.

#### **4.10 IT Issues**

There are no IT issues with regard to this report.

### **5. Recommendations**

The Audit Committee is therefore asked to approve the Audit Committee Annual Report 2019/20 (Appendix 1) and its self-assessments using the CIPFA Audit Committees Guidance (Appendices 2 and 3), and agrees that the Audit Committee Annual Report 2019/20 should be presented to the Council.

**Date:** 13 May 2020  
**Report Authors:** Jill Stacey, Chief Internal Auditor  
**E-Mail:** [Jill.Stacey@midlothian.gov.uk](mailto:Jill.Stacey@midlothian.gov.uk)



**MIDLOTHIAN COUNCIL  
AUDIT COMMITTEE  
ANNUAL REPORT FROM THE CHAIRMAN – 2019/20**

This annual report has been prepared to inform the Midlothian Council of the work carried out by the Council's Audit Committee during the financial year. The content and presentation of this report meets the requirements of the CIPFA Audit Committees Practical Guidance for Local Authorities and Police 2018 Edition (hereinafter referred to as CIPFA Audit Committees Guidance) to report to full Council on a regular basis on the Committee's performance in relation to the terms of reference and the effectiveness of the Committee in meeting its purpose.

### **Meetings**

The Audit Committee has met 6 times during the financial year which included meetings on 28 May, 24 June, 24 September, 3 December 2019, 28 January and 10 March 2020 to consider reports pertinent to the audit cycle and its terms of reference.

The Audit Committee is a key component of Midlothian Council's corporate governance. It provides an independent and high-level focus on the audit, assurance and reporting arrangements that underpin good governance and financial standards. The purpose of the audit committee is to provide independent assurance to elected members of the adequacy of the risk management framework and the internal control environment. It provides independent review of Midlothian Council's governance, risk management and control frameworks, and oversees the financial reporting and annual governance processes. It oversees internal and external audit, helping to ensure efficient and effective assurance arrangements are in place.

The Audit Committee scrutinised the Annual Report and Accounts of the Council at appropriate times in accordance with its terms of reference, which also includes the promotion of good governance, and financial and ethical standards. The Audit Committee also reviewed the Annual Governance Statement in order to assess whether it properly reflects the risk environment and whether the content is consistent with its evaluation of the internal controls and governance arrangements based on evidence received during the year.

The Audit Committee approved the terms of reference for Internal Audit (Internal Audit Charter) and the Internal Audit Strategy and Annual Plan. It considered Internal Audit's reports which set out executive summaries of findings, audit opinions, good practice and recommendations associated with each assurance review, as well as other work. It monitored the implementation of agreed actions through receipt of two reports during the year from Internal Audit to ensure that audit recommendations had been fully implemented to its satisfaction. It monitored Internal Audit's performance including progress against annual plan, conformance with Public Sector Internal Audit Standards (PSIAS), and quality assurance and improvement plan (QAIP) within Internal Audit mid-term performance and annual assurance reports, and considered the statutory annual audit opinion within the Internal Audit Annual Assurance Report.

The Audit Committee has reviewed the External Audit Strategy and Plan Overview for Midlothian Council, considered External Audit reports including the annual report to Members and the Controller of Audit on the annual audit of the Council, reviewed the main issues arising from the External Audit of the Council's statutory accounts, and monitored the implementation of agreed actions arising.

The Audit Committee considered the effectiveness of the risk management process throughout the Council through the receipt of periodic reports from the Risk Manager during the year on corporate risks and mitigations and the appropriate challenge of Senior Management to ensure that the most significant risks are being identified, evaluated and managed.

The Audit Committee considered the adequacy and effectiveness of the Council's counter fraud arrangements by way of an annual report which set out the counter fraud activity and outcomes, and received assurances from Auditors on fraud risks and counter fraud controls.

The Audit Committee is the body responsible for scrutiny of the treasury management strategy, mid-term and annual performance reports prior to their presentation to Council for approval. The sequencing of reports presentation was applied during the year with the exception of the mid-term performance report which was considered by Audit Committee after its presentation to Council. The schedule of meetings for 2020 needs to be considered to ensure the sequencing of all three treasury management reports presentation to enable the Audit Committee to effectively fulfil its role on scrutiny of treasury management, in response to a previous Internal Audit recommendation.

The minutes of Audit Committee meetings were presented for approval by the Council, and any exceptional items or recommendations were referred to the Council in accordance with the remit.

## Membership

The Membership of the Audit Committee is part of the approved Midlothian Council's Standing Orders (amended June 2017) namely being six Members of the Council and two non-voting members appointed from an external source. Two of the six Elected Members on the Audit Committee are in the Cabinet (Committee with executive decision-making powers). However, this is considered as difficult to avoid in a small Council and the Audit Committee operates with an independent Chair and independent member to ensure adequate independence and challenge. The two non-voting external members were appointed from the community following a recruitment and selection process carried out during 2017. This enhances the robustness and independence of the Audit Committee's role in the scrutiny process of internal controls and governance.

The Committee membership during the year included Mr M Ramsay (Chair), Councillors K Baird (to 12 March 2020), A Hardie, D Milligan, J Muirhead, K Parry and P Smaill, and Mr P De Vink.

The attendance by each member at the Committee meetings throughout the year was as follows:

Member	28 May 2019	24 June 2019	24 September 2019	3 December 2019	28 January 2020	10 March 2020
<b>Mr M Ramsay (Chair)</b>	√	√	√	√		√
<b>CLlr K Baird</b>						
<b>CLlr A Hardie</b>	√	√	√	√	√	√
<b>CLlr D Milligan</b>	√	√	√	√	√	√
<b>CLlr J Muirhead</b>	√	√	√	√	√	√
<b>CLlr K Parry</b>		√				
<b>CLlr P Smaill</b>		√	√	√	√	√
<b>Mr P De Vink</b>	√	√	√		√	
<b>CLlr D Alexander (substitute)</b>	√		√	√	√	√
<b>CLlr C Cassidy (substitute)</b>	√	√	√	√	√	√

Every meeting of the Audit Committee in 2019/20 was quorate (i.e. at least three elected members present). At the one meeting when Mr M Ramsay was unavailable, CLlr P Smaill was Chair of the meeting following approval by the Committee. Substitutes attended as indicated.

All other individuals who attended the meetings are recognised as being "In Attendance" only. The Chief Executive, Directors, Chief Officer Corporate Solutions (Section 95 Officer), External Audit (EY), and Internal Audit attend all Audit Committee meetings, and other senior officers also routinely attend Audit Committee meetings. The Council has provided support and resources to the Audit Committee throughout the year including a Democratic Services Officer as the Minute secretary.



## **Skills and Knowledge**

Given the wider corporate governance remit of Audit Committees within local government and the topics now covered by the external and internal audit functions, it is noteworthy that there is a range of skills, knowledge and experience that Audit Committee members bring to the committee, not limited to financial and business management. This enhances the quality of scrutiny and discussion of reports at the meetings. No one committee member would be expected to be expert in all areas.

## **Self-Assessment of the Committee**

The annual self-assessment was carried out by members of the Audit Committee on 10 March 2020 during an Informal Session facilitated by the Chief Internal Auditor using the Good Practice Principles Checklist and Evaluation of Effectiveness Toolkit from the CIPFA Audit Committees Guidance. This was useful for Members to ensure the Committee can demonstrate its effectiveness as a scrutiny body as a foundation for sound corporate governance for the Council.

The outcome of the self-assessments was a medium degree of performance against the good practice principles and a medium degree of effectiveness. Improvements were identified focussing on skills and knowledge competency to fulfil role. In summary these are: Check schedule of meetings for 2020/21 to ensure the sequencing of all three Treasury Management reports presentation prior to Council to enable the Audit Committee to effectively fulfil its role; Utilise the CIPFA Skills and Knowledge toolkit; Obtain feedback on its performance from a range of Directors and others who interact with the Committee; Review and scrutinise the Risk Management Policy and Strategy on a regular basis; and Understand the effectiveness of Committees fulfilling their remits on which the Audit Committee places reliance, for example Council monitoring progress of Best Value Action Plan.

## **Assurance Statement to the Council**

The Audit Committee provides the following assurance to the Council:

- The Council has received the Minutes of the Audit Committee throughout the year.
- The Audit Committee has operated in accordance with its agreed terms of reference, covering the themes of Governance, Risk and Control, Internal Audit, External Audit, Financial Reporting, and Accountability Arrangements, and accordingly conforms to the Audit Committee principles within the CIPFA Position Statement for Audit Committees. The application in practice of the Audit Committee's treasury management scrutiny role needs further refinement i.e. to ensure the sequencing of all three treasury management reports presentation to enable the Audit Committee to effectively fulfil its role on scrutiny of treasury management, in response to a previous Internal Audit recommendation.
- It focused entirely on matters of risk management, internal control and governance, giving specialist advice to the Council on the value of the audit process, on the integrity of financial reporting and on governance arrangements, and acted as a bridge between the Council and other stakeholders. It did this through material it received from Internal Audit, External Audit, other Audit bodies, and assurances from Management relevant to audit cycle of reporting.
- The Audit Committee will review the unaudited Annual Accounts 2019/20 of the Council at its virtual meeting on 22 June 2020. Specifically, to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements. It will review the draft Annual Governance Statement prior to approval and consider whether it properly reflects the risk environment and supporting assurances. It will review the final audited accounts at its meeting in September 2020 alongside the External Audit report on their annual audit 2019/20, to consider whether there are concerns arising from the audit that need to be brought to the attention of the Council, in order to decide whether to recommend to the Council that they be adopted.

- The Audit Committee has reflected on its performance during the year, and has agreed areas of improvements to enable it to fulfil its scrutiny and challenge role and to enhance its effectiveness.

#### **Recommendation of the Terms of Reference for the Audit Committee for the coming year**

The Council in August 2019 approved amendments to the Terms of Reference for the Audit Committee in response to recommendations made in the previous year's annual report from the Committee, to ensure they continue to be relevant to the local government operating environment and best practice and to explicitly address all the core areas identified in CIPFA's Position Statement. It is noted that these approved amendments are not yet formally reflected in the Council's Scheme of Administration, which is under review and update for approval, nor on the committee management system CMIS.

Mike Ramsay  
Chairman of Audit Committee  
14 May 2020

## CIPFA 'audit committees' Practical Guidance for Local Authorities and Police 2018 Edition

### Midlothian Council Audit Committee – self-assessment of Good Practice at 10 March 2020

Audit committee purpose and governance	Yes/Partly /No	Comments
Does the authority have a dedicated audit committee?	<input type="text" value="Yes"/>	Standing Orders approved by the Council includes the remit of the Audit Committee.
Does the audit committee report directly to full council?	<input type="text" value="Yes"/>	All Minutes of Audit Committee are circulated to full Council for noting and approval of any of their recommendations. An annual report is submitted by the Chair of the Audit Committee to full Council.
Do the terms of reference clearly set out the purpose of the committee in accordance with CIPFA's Position Statement?	<input type="text" value="Yes"/>	Terms of Reference in place and periodically reviewed against CIPFA's best practice by the Chief Internal Auditor.
Is the role and purpose of the audit committee understood and accepted across the authority?	<input type="text" value="Yes"/>	Role of Audit Committee is set out in the Council's Standing Orders. Senior Management and Elected Members have access to Standing Orders on the Council's Intranet. The Chief Executive, Directors and Section 95 Officer, External Audit (EY) and Internal Audit attend all Audit Committee meetings.
Does the audit committee provide support to the authority in meeting the requirements of good governance?	<input type="text" value="Yes"/>	Audit Committee carries out the role set out in the Terms of Reference contributing to the Council's governance framework.
Are the arrangements to hold the committee to account for its performance operating satisfactorily?	<input type="text" value="Yes"/>	All Minutes of Audit Committee are circulated to full Council for noting and approval of any recommendations. An annual report is submitted by the Chair of the Audit Committee to full Council. It sets out the activities to enable stakeholders to understand how the Audit Committee has discharged its duties and identifies areas of improvement to fulfil its remit. MLC continues to be a lead authority in adopting this best practice.

## CIPFA 'audit committees' Practical Guidance for Local Authorities and Police 2018 Edition

### Midlothian Council Audit Committee – self-assessment of Good Practice at 10 March 2020

#### Functions of the committee

Yes/Partly  
/No

#### Comments

Do the committee's terms of reference explicitly address all the core areas identified in CIPFA's Position Statement?

- |  |                                  |   |
|--|----------------------------------|---|
| • good governance  | <input type="text" value="Yes"/> | Functions in Terms of Reference Nos. 1, 3 & 4   |
| • assurance framework, including partnerships and collaboration arrangements | <input type="text" value="Yes"/> | Assurance Framework Function in Terms of Reference No. 6 and explicit references to these service delivery models in Nos. 3, 6 & 7 within the revised TOR approved by Council in August 2019. |
| • internal audit   | <input type="text" value="Yes"/> | Functions in Terms of Reference Nos. 13-24  |
| • external audit   | <input type="text" value="Yes"/> | Functions in Terms of Reference Nos. 25-29  |
| • financial reporting  | <input type="text" value="Yes"/> | Functions in Terms of Reference Nos. 30-31  |
| • risk management  | <input type="text" value="Yes"/> | Functions in Terms of Reference Nos. 6-8  |
| • Value for money or best value  | <input type="text" value="Yes"/> | Function in Terms of Reference No. 5  |
| • Counter-fraud or corruption  | <input type="text" value="Yes"/> | Functions in Terms of Reference Nos. 9-11   |
| • Supporting the ethical framework   | <input type="text" value="Yes"/> | Function in Terms of Reference No. 12 Treasury Management and explicit references to ethics in Functions 3 & 19 within the revised TOR Approved by Council in August 2019.                    |

## CIPFA 'audit committees' Practical Guidance for Local Authorities and Police 2018 Edition

### Midlothian Council Audit Committee – self-assessment of Good Practice at 10 March 2020

Functions of the committee (cont'd)	Yes/Partly /No	Comments
Is an annual evaluation undertaken to assess whether the committee is fulfilling its terms of reference and that adequate consideration has been given to all core areas?	Yes	Annual self-assessment undertaken on 10 March 2020 against CIPFA good practice checklist and effectiveness toolkit with the outcome / output referenced as part of the annual report submitted by the Chair of the Audit Committee to full Council.
Has the audit committee considered the wider areas identified in CIPFA's Position Statement and whether it would be appropriate for the committee to undertake them?	Yes	The Audit Committee is responsible for scrutiny of the treasury management strategy, mid-term and annual performance reports prior to their presentation to Council for approval (Audit function no. 12). Improvement required in practice: Check schedule of meetings for 2020/21 to ensure the sequencing of all three reports presentation to enable the Audit Committee to effectively fulfil its role.
Where coverage of core areas has been found to be limited, are plans in place to address this?	Yes	Terms of Reference covers core areas.
Has the committee maintained its non-advisory role by not taking on any decision-making powers that are not in line with its core purpose?	Yes	Terms of Reference is limited to governance, risk and control; it is non-decision-making though does have an advisory function to recommend improvements to Council within its remit.

## CIPFA 'audit committees' Practical Guidance for Local Authorities and Police 2018 Edition

### Midlothian Council Audit Committee – self-assessment of Good Practice at 10 March 2020

Membership and support	Yes/Partly /No	Comments
<p>Has an effective audit committee structure and composition of the committee been selected?</p> <p>This should include:</p> <ul style="list-style-type: none"> <li>• separation from the executive</li> <li>• an appropriate mix of knowledge and skills among the membership</li> <li>• a size of committee that is not unwieldy</li> <li>• consideration has been given to the inclusion of at least one independent member</li> </ul>	Yes*	<p>No (1<sup>st</sup> bullet) - Two of the six Elected Members on the Audit Committee are in the Cabinet (Committee with executive decision-making powers). However this is considered as difficult to avoid in a small Council and the Audit Committee operates with an independent Chair and independent member and there is therefore effective independent scrutiny and challenge.</p> <p>Yes (2<sup>nd</sup> 3<sup>rd</sup> and 4<sup>th</sup> bullet points) – Committee comprises of six Elected Members and two independent members (one of which is the Chair) who have a mix of skills, knowledge and experience.</p>
Have independent members appointed to the committee been recruited in an open and transparent way and approved by the full council?	Yes	An external recruitment, selection and appointment process was undertaken in 2017 for independent members on the Audit Committee.
Does the chair of the committee have appropriate knowledge and skills?	Yes	The independent Chair of the Audit Committee has previous experience of chairing meetings and a previous career within the financial sector.
Are arrangements in place to support the committee with briefings and training?	Yes	The previous year's improvement action to undertake briefings / seminars on Statutory Accounts (June and September 2019) and Treasury Management (November 2019) to enhance skills and knowledge was progressed during the year. Informal Sessions are used for development purposes.
Has the membership of the committee been assessed against the core knowledge and skills framework and found to be satisfactory?	No	Improvement required: Utilise the CIPFA Skills and Knowledge toolkit.
Does the committee have good working relations with key people and organisations, including external audit, internal audit and the chief financial officer?	Yes	The Chair meets with Chief Internal Auditor (CIA) in advance of each Audit Committee meeting and has the option to meet with External Auditors, EY, in private. Prior to each Audit Committee meeting the Chair has pre-meeting with Chief Executive, CIA, Executive Director Place, and Section 95 Officer. Informal Sessions are scheduled prior to each meeting.
Is adequate secretariat and administrative support to the committee provided?	Yes	A Democratic Services Officer is assigned to the Audit Committee.

## CIPFA 'audit committees' Practical Guidance for Local Authorities and Police 2018 Edition

### Midlothian Council Audit Committee – self-assessment of Good Practice at 10 March 2020

Effectiveness of the committee	Yes/Partly/No	Comments
Has the committee obtained feedback on its performance from those interacting with the committee or relying on its work?	Partly	External Audit comment on Audit Committee as part of Governance within the Annual Audit Report. Audit Committee Annual Report presented to Council in August 2019 as an opportunity. Improvement required: The Audit Committee will obtain feedback on its performance from CMT.
Are meetings effective with a good level of discussion and engagement from all members?	Yes	As reflected in the Minutes of the Committee.
Does the committee engage with a wide range of leaders and managers, including discussion of audit findings, risks and action plans with the responsible officers?	Yes	The Chief Executive, Directors, and Section 95 Officer attend all Audit Committee meetings and respond to members' questions as appropriate for the business being considered by the Committee to ensure action findings and action plans are acted upon. The Risk Manager presents a quarterly update on the Corporate Risk Register to the Committee setting out the corporate risks, evaluation and mitigations.
Does the committee make recommendations for the improvement of governance, risk and control and are these acted on?	Yes	Recommendations are made by the Committee to Council in accordance with the business considered by the Committee. An Action Tracker for Audit Committee is in place to monitor completion of their recommended actions.
Has the committee evaluated whether and how it is adding value to the organisation?	Yes	The Audit Committee carries out an annual self assessment of performance against the CIPFA good practice checklist and the effectiveness toolkit from the CIPFA guidance 2018 'audit committees', the latter enabling evaluation of how effectively it fulfils its Audit functions. The 2019/20 self-assessment was carried out on 10 March 2020 during an Informal Session.
Does the committee have an action plan to improve any areas of weakness?	Yes	As part of its annual self-assessment 2019/20 the Committee has recognised where it could improve in respect of its scrutiny and challenge role to fulfil its remit and to further add value. Improvements are set out within the Audit Committee Annual Report 2019/20.
Does the committee publish an annual report to account for its performance and explain its work?	Yes	The Audit Committee Annual Report is presented to the Council each year. It sets out the activities to enable stakeholders to understand how the Committee has discharged its duties. MLC continues to be a lead authority in adopting this best practice.







Areas where the Audit Committee can add value by supporting improvement	Examples of how the audit committee can add value and provide evidence of effectiveness	Self-evaluation, examples, areas of strength and weakness	Overall assessment 5-1 See key below
1. Promoting the principles of good governance and their application to decision making	Supporting the development of a local code of governance. Providing robust review of the Annual Governance Statement (AGS) and the assurances underpinning it. Working with key members/governors to improve their understanding of the AGS and their contribution to it. Supporting reviews/audits of governance arrangements. Participating in self-assessments of governance arrangements. Working with partner audit committees to review governance arrangements in partnerships.	Committee scrutinised Local Code of Corporate Governance, and recommended it for Council approval, and scrutinised AGS within Annual Report and Accounts. Chair met with Chief Executive, Director Resources and S95 officer on a regular basis. Committee supports the role of audit in improving internal control and governance. Committee considered Audit Scotland toolkits for Councillors. Informal liaison with other Audit Committees to share practice e.g. MIJB, Borders	4 (2018/19 4)
2. Contributing to the development of an effective control environment.	Actively monitoring the implementation of recommendations from auditors. Encouraging ownership of the internal control framework by appropriate managers. Raising significant concerns over controls with appropriate senior managers.	Committee received periodic progress reports from Auditors e.g. follow-up activity. Directors attended Committee meetings to discuss progress with Audit actions. Audit Committee Action Tracker introduced in-year to hold Management to account.	4 (2018/19 4)
3. Supporting the establishment of arrangements for the governance of risk and for effective arrangements to manage risks.	Reviewing risk management arrangements and their effectiveness, e.g. risk management benchmarking. Monitoring improvements. Holding risk owners to account for major/strategic risks.	Members were not aware when the Risk Management Policy and Strategy was most recently reviewed and scrutinised by the Committee. Committee received quarterly reports from Risk Manager on corporate risks and mitigations. Directors attended meetings to respond to questions on risks and mitigations.	3 (2018/19 3)

Areas where the Audit Committee can add value by supporting improvement	Examples of how the audit committee can add value and provide evidence of effectiveness	Self-evaluation, examples, areas of strength and weakness	Overall assessment 5-1 See key below
4. Advising on the adequacy of the assurance framework and considering whether assurance is deployed efficiently and effectively.	Specifying its assurance needs, identifying gaps or overlaps in assurance. Seeking to streamline assurance gathering and reporting. Reviewing the effectiveness of assurance providers, e.g. internal audit, risk management, external audit.	Annual Strategies and Plans and periodic progress Reports received from Auditors. Induction programme outlined Governance and Assurance Framework and Audit Cycle. Reliance on other Committees fulfilling their remits; need to understand effectiveness.	4 (2018/19 4)
5. Supporting the quality of the internal audit activity, particularly by underpinning its organisational independence.	Reviewing the audit charter and functional reporting arrangements. Assessing the effectiveness of internal audit arrangements, providing constructive challenge and supporting improvements. Actively supporting the quality assurance and improvement programme (QAIP) of internal audit.	Committee considered and approved the Internal Audit Charter. Committee considered and approved the Internal Audit Strategy and Plan, and considered regular Reports raising queries and endorsing Internal Audit recommendations. Committee received Internal Audit QAIP and PSIAS conformance within mid-term performance and annual assurance reports.	4 (2018/19 4)
6. Aiding the achievement of the authority's goals and objectives through helping to ensure appropriate governance, risk, control and assurance arrangements	Reviewing how the governance arrangements support the achievement of sustainable outcomes. Reviewing major projects and programmes to ensure that governance and assurance arrangements are in place. Reviewing the effectiveness of performance management arrangements.	Committee received National Reports from Audit Scotland on governance arrangements for transformation, sustainability, and performance management, including lessons learned and sharing best practice. Reliance on other Committees fulfilling their remits; need to understand effectiveness.	4 (2018/19 4)
7. Supporting the development of robust arrangements for ensuring value for money.	Ensuring that assurance on value for money arrangements is included in the assurances received by the audit committee. Considering how performance in value for money is evaluated as part of the AGS.	Auditors provided assurance on value for money arrangements e.g. transformation, sustainability, and performance management. AGS sets out the Governance Framework including arrangements for best value. Best Value Action Plan presented to Council.	4 (2018/19 4)

Areas where the Audit Committee can add value by supporting improvement	Examples of how the audit committee can add value and provide evidence of effectiveness	Self-evaluation, examples, areas of strength and weakness	Overall assessment 5-1 See key below
8. Helping the authority to implement the values of good governance, including effective arrangements for countering fraud and corruption risks.	<p>Reviewing arrangements against the standards set out in the Code of Practice on Managing the Risk of Fraud and Corruption (CIPFA, 2014).</p> <p>Reviewing fraud risks and the effectiveness of the organisation's strategy to address those risks.</p> <p>Assessing the effectiveness of ethical governance arrangements for both staff and governors.</p>	<p>Committee received Counter Fraud Annual Report and update on National Fraud Initiative, and note Anti-Fraud Policy and Strategy is regularly reviewed.</p> <p>Auditors provided assurance reports on fraud risks and counter fraud controls, and recommended improvements which were endorsed by the Committee.</p>	4 (2018/19 4)
9. Promoting effective public reporting to the authority's stakeholders and local community and measures to improve transparency and accountability.	<p>Improving how the authority discharges its responsibilities for public reporting; for example, better targeting at the audience, plain English.</p> <p>Reviewing whether decision making through partnership organisations remains transparent and publicly accessible and encourages greater transparency.</p> <p>Publishing an annual report from the committee.</p>	<p>Committee scrutinised Annual Report and Accounts 2018/19 prior to publication and audit, and scrutinised Treasury Management Strategy and Annual Performance Report prior to Council approval (though not mid-term performance report in sequence).</p> <p>Audit Committee Annual Report presented to Council in public.</p>	4 (2018/19 3)

Assessment key	
5	Clear evidence is available from a number of sources that the committee is actively supporting improvements across all aspects of this area. The improvements made are clearly identifiable.
4	Clear evidence from some sources that the committee is actively and effectively supporting improvement across some aspects of this area.
3	The committee has had mixed experience in supporting improvement in this area. There is some evidence that demonstrates their impact but there are also significant gaps.
2	There is some evidence that the committee has supported improvements, but the impact of this support is limited.
1	No evidence can be found that the audit committee has supported improvements in this area.

