

GOVERNANCE COMMITTEE

Monday, 8th February, 2016
at 5.00 pm

PLEASE NOTE TIME OF MEETING

Conference Room 3 - Civic Centre

This meeting is open to the public

Members of the Committee

Councillor Barnes-Andrews (Chair)
Councillor Daunt
Councillor Inglis
Councillor Jordan
Councillor Noon
Councillor O'Neill
Councillor Keogh

Contacts

Service Director, Legal and Governance
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Democratic Support Officer
Ed Grimshaw
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PUBLIC INFORMATION

Role of the Governance Committee

Information regarding the role of the Committee's is contained in Part 2 (Articles) of the Council's Constitution.

[02 Part 2 - Articles](#)

It includes at least one Councillor from each of the political groups represented on the Council, and at least one independent person, without voting rights, who is not a Councillor or an Officer of the Council.

Public Representations

At the discretion of the Chair, members of the public may address the meeting on any report included on the agenda in which they have a relevant interest. Any member of the public wishing to address the meeting should advise the Democratic Support Officer (DSO) whose contact details are on the front sheet of the agenda

Southampton City Council's Priorities:

- .Jobs for local people
- Prevention and early intervention
- Protecting vulnerable people
- Affordable housing
- Services for all
- City pride
- A sustainable Council

Smoking policy – The Council operates a no-smoking policy in all civic buildings.

Mobile Telephones:- Please switch your mobile telephones to silent whilst in the meeting

Use of Social Media:- The Council supports the video or audio recording of meetings open to the public, for either live or subsequent broadcast. However, if, in the Chair's opinion, a person filming or recording a meeting or taking photographs is interrupting proceedings or causing a disturbance, under the Council's Standing Orders the person can be ordered to stop their activity, or to leave the meeting.

Access – Access is available for disabled people. Please contact the Democratic Support Officer who will help to make any necessary arrangements.

Fire Procedure – in the event of a fire or other emergency a continuous alarm will sound and you will be advised by Council officers what action to take.

Dates of Meetings: Municipal Year 2015/16

2015	2016
15 June	8 February
14 September	25 April
9 November	
14 December	

CONDUCT OF MEETING

Terms of Reference

The terms of reference of the Governance Committee are contained in Part 3 of the Council's Constitution.

[03 - Part 3 - Responsibility for Functions](#)

Rules of Procedure

The meeting is governed by the Council Procedure Rules as set out in Part 4 of the Constitution.

Business to be discussed

Only those items listed on the attached agenda may be considered at this meeting.

Quorum

The minimum number of appointed Members required to be in attendance to hold the meeting is 3.

DISCLOSURE OF INTERESTS

Members are required to disclose, in accordance with the Members' Code of Conduct, **both** the existence **and** nature of any "Disclosable Pecuniary Interest" or "Other Interest" they may have in relation to matters for consideration on this Agenda.

DISCLOSABLE PECUNIARY INTERESTS

A Member must regard himself or herself as having a Disclosable Pecuniary Interest in any matter that they or their spouse, partner, a person they are living with as husband or wife, or a person with whom they are living as if they were a civil partner in relation to:

- (i) Any employment, office, trade, profession or vocation carried on for profit or gain.
- (ii) Sponsorship:

Any payment or provision of any other financial benefit (other than from Southampton City Council) made or provided within the relevant period in respect of any expense incurred by you in carrying out duties as a member, or towards your election expenses. This includes any payment or financial benefit from a trade union within the meaning of the Trade Union and Labour Relations (Consolidation) Act 1992.

(iii) Any contract which is made between you / your spouse etc (or a body in which the you / your spouse etc has a beneficial interest) and Southampton City Council under which goods or services are to be provided or works are to be executed, and which has not been fully discharged.

(iv) Any beneficial interest in land which is within the area of Southampton.

(v) Any license (held alone or jointly with others) to occupy land in the area of Southampton for a month or longer.

(vi) Any tenancy where (to your knowledge) the landlord is Southampton City Council and the tenant is a body in which you / your spouse etc has a beneficial interests.

(vii) Any beneficial interest in securities of a body where that body (to your knowledge) has a place of business or land in the area of Southampton, and either:

- a) the total nominal value of the securities exceeds £25,000 or one hundredth of the total issued share capital of that body, or
- b) if the share capital of that body is of more than one class, the total nominal value of the shares of any one class in which you / your spouse etc has a beneficial interest that exceeds one hundredth of the total issued share capital of that class.

Other Interests

A Member must regard himself or herself as having an, 'Other Interest' in any membership of, or occupation of a position of general control or management in:

Any body to which they have been appointed or nominated by Southampton City Council

Any public authority or body exercising functions of a public nature

Any body directed to charitable purposes

Any body whose principal purpose includes the influence of public opinion or policy

Principles of Decision Making

All decisions of the Council will be made in accordance with the following principles:-

- proportionality (i.e. the action must be proportionate to the desired outcome);
- due consultation and the taking of professional advice from officers;
- respect for human rights;
- a presumption in favour of openness, accountability and transparency;
- setting out what options have been considered;
- setting out reasons for the decision; and
- clarity of aims and desired outcomes.

In exercising discretion, the decision maker must:

- understand the law that regulates the decision making power and gives effect to it. The decision-maker must direct itself properly in law;
- take into account all relevant matters (those matters which the law requires the authority as a matter of legal obligation to take into account);
- leave out of account irrelevant considerations;
- act for a proper purpose, exercising its powers for the public good;
- not reach a decision which no authority acting reasonably could reach, (also known as the "rationality" or "taking leave of your senses" principle);
- comply with the rule that local government finance is to be conducted on an annual basis. Save to the extent authorised by Parliament, 'live now, pay later' and forward funding are unlawful; and
- act with procedural propriety in accordance with the rules of fairness.

AGENDA

Agendas and papers are now available via the Council's Website

1 APOLOGIES AND CHANGES IN PANEL MEMBERSHIP (IF ANY)

To note any changes in membership of the Panel made in accordance with Council Procedure Rule 4.3.

2 DISCLOSURE OF PERSONAL AND PECUNIARY INTERESTS

In accordance with the Localism Act 2011, and the Council's Code of Conduct, Members to disclose any personal or pecuniary interests in any matter included on the agenda for this meeting.

NOTE: Members are reminded that, where applicable, they must complete the appropriate form recording details of any such interests and hand it to the Democratic Support Officer.

3 STATEMENT FROM THE CHAIR

4 MINUTES OF PREVIOUS MEETING (INCLUDING MATTERS ARISING)

(Pages 1 - 2)

To approve and sign as a correct record the Minutes of the meeting held on 14th December 2015 and to deal with any matters arising, attached.

5 PRUDENTIAL LIMITS AND TREASURY MANAGEMENT STRATEGY 2016/17 TO 2018/19

(Pages 3 - 44)

Report of the Council's Chief Financial Officer detailing the context within which the Council's treasury management activity operates and setting out a proposed strategy for the coming year, attached.

6 ANNUAL GOVERNANCE STATEMENT

(Pages 45 - 54)

Report of the Chief Financial Officer seeking to approve the assurance gathering process to support the development of the 2015-16 Annual Governance Statement and to note the content of the 2014-15 Action Plan, attached

7 EXTERNAL AUDIT PROGRESS REPORT - JANUARY 2016

(Pages 55 - 78)

Report of the Chief internal Auditor providing an update against external audit activity against the agreed audit plan, attached.

8 CERTIFICATION OF CLAIMS AND RETURNS ANNUAL REPORT 2014-15

(Pages 79 - 88)

Report of the Chief Internal Auditor summarising the results of the external auditors work on Southampton City Council's 2014-15 grant claims, attached.

9 REVISIONS TO THE CONSTITUTION – TRANSFORMATION PROJECTS

(Pages 89 - 92)

Report of the Service Director: Legal and Governance regarding revisions to various elements of the Constitution as part of the Council's significant Transformation agenda in order to enable early decision making which will permit quicker project implementation and realisation of financial savings, attached.

Friday, 29 January 2016

Service Director, Legal and Governance

GOVERNANCE COMMITTEE

MINUTES OF THE MEETING HELD ON 14 DECEMBER 2015

Present: Councillors Barnes-Andrews (Chair), Daunt, Inglis, Jordan, Noon, O'Neill and Keogh

23. **MINUTES OF PREVIOUS MEETING (INCLUDING MATTERS ARISING)**

RESOLVED: that the minutes for the Committee meeting on 9 November 2015 be approved and signed as a correct record.

24. **EXTERNAL AUDIT ANNUAL AUDIT LETTER**

The Committee noted the report of the Chief Internal Auditor detailing the External Auditors' Annual Audit letter for 2014/15.

25. **EXTERNAL AUDIT - PROGRESS REPORT**

The Committee noted the report of the Chief Internal Auditor updating the Committee on the external audit progress.

26. **SOUTHERN INTERNAL AUDIT PARTNERSHIP - EXTERNAL QUALITY ASSESSMENT**

The Committee noted the report of the Chief Internal Auditor detailing the External Quality Assessment of the Southern Internal Audit Partnership.

27. **INTERNAL AUDIT - PROGRESS REPORT**

The Committee noted the report of the Chief Internal Auditor setting out the Internal Audit Progress Report to the period November 2015 as attached.

28. **REVISIONS TO THE CONSTITUTION - TRANSFORMATION PROJECTS**

The Committee considered the report of the Head of Legal and Democratic Services seeking approval to make changes to the Constitution

RESOLVED

That the Committee considered the revisions to the constitution as set out in the report and made the follow comments:

- (i) That the figure of £5,000,000 was high and requested that evidence relating to the number and type of projects that would be delayed if the threshold be reviewed to a lower sum;
- (ii) That efforts be made to ensure that there was a greater involvement from Councillors in consultation. Committee recommended that the Leader of the Council always be consulted notwithstanding that he was part of the Transformation Information Board and that a group leaders meeting been convened to share information as required.
- (iii) That the Transformation Implementation Director provide details of the list in (i) above to Council on 16th December 2015

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Agenda Item 5

DECISION-MAKER:	GOVERNANCE COMMITTEE COUNCIL		
SUBJECT:	PRUDENTIAL LIMITS AND TREASURY MANAGEMENT STRATEGY 2016/17 TO 2018/19		
DATE OF DECISION:	8 FEBRUARY 2016 10 FEBRUARY 2016		
REPORT OF:	CHIEF FINANCIAL OFFICER		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Mel Creighton	Tel: 023 80 4897
	E-mail:	mel.creighton@southampton.gov.uk	
Director	Name:	Andrew Lowe	Tel: 023 80 2049
	E-mail:	andrew.lowe@southampton.gov.uk	
STATEMENT OF CONFIDENTIALITY			
NOT APPLICABLE			
BRIEF SUMMARY			
<p>With overall annual expenditure in excess of £600M and an extensive capital programme, the Council is required to actively manage its cash-flows on a daily basis. The requirement to invest or to borrow monies to finance capital programmes, and to cover daily operational needs is an integral part of daily cash and investment portfolio management.</p>			
<p>This report explains the context within which the Council's treasury management activity operates and sets out a proposed strategy for the coming year in relation to the Council's cash flow, investment and borrowing, and the management of the numerous risks related to this activity.</p>			
<p>The core elements of the 2016/17 strategy are :</p> <ul style="list-style-type: none"> • To continue to make use of short term variable rate debt to take advantage of the current market conditions of low interest rates. • To constantly review longer term forecasts and to lock into longer term rates through a variety of instruments as appropriate during the year, in order to provide a balanced portfolio against interest rate risk. • To secure the best short term rates for borrowing and investments consistent with maintaining flexibility and liquidity within the portfolio. • To invest surplus funds prudently, the Council's priorities being: <ul style="list-style-type: none"> - Security of invested capital - Liquidity of invested capital - An optimum yield which is commensurate with security and liquidity. • To approve borrowing limits that provide for debt restructuring opportunities and to pursue debt restructuring where appropriate and within the Council's risk boundaries. 			

- To approve the 2016 Minimum Revenue Provision (MRP) Statement

RECOMMENDATIONS:

GOVERNANCE COMMITTEE

It is recommended that Governance Committee:

	(i)	Endorse the Treasury Management (TM) Strategy for 2016/17 as outlined in the report;
	(ii)	Endorse the 2016 Minimum Revenue Provision (MRP) Statement as detailed in paragraphs 77 to 835;
	(iii)	Note that the indicators as reported have been set on the assumption that the recommendations in the Capital update report will be approved by Council on 10 February 2016. Should the recommendations change, the Prudential Indicators may have to be recalculated; and
	(iv)	Note that due to the timing of this report, changes may still be required following the finalisation of capital and revenue budgets and therefore any significant changes to this report will be highlighted in the final version that is presented to Full Council.

COUNCIL

It is recommended that Council:

	(i)	Approve the Council's Treasury Management (TM) Strategy and Prudential Indicators for 2016/17, 2017/18 and 2018/19, as detailed within the report;
	(ii)	Approve the 2016 Minimum Revenue Provision (MRP) Statement as detailed in paragraphs 77 to 83 and to delegate authority to the Chief Financial Officer (CFO) to approve any changes necessary that aid good financial management whilst maintaining a prudent approach;
	(iii)	Approve the Annual Investment Strategy as detailed in paragraphs 38 to 57;
	(iv)	Note that at the time of writing this report the recommendations in the Capital update report, submitted to Council on the 10 February 2016, have not yet been approved. The indicators in the report are based on the assumption that they will be approved, but should the recommendations change, the Prudential Indicators may have to be recalculated; and
	(v)	Continue to delegate authority to the Chief Financial Officer (CFO) to approve any changes to the Prudential Indicators or borrowing limits that will aid good treasury management. For example, agreeing an increase in the percentage for variable rate borrowing to take advantage of the depressed market for short term rates. Any amendments will be reported as part of quarterly financial and performance monitoring and in revisions to the TM Strategy.

REASONS FOR REPORT RECOMMENDATIONS

1.	In order to comply with Part 1 of the Local Government Act 2003, and the established TM procedures that have been adopted by the Authority, each year the Council must set certain borrowing limits and approve TM Strategy which
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	<p>includes:</p> <ul style="list-style-type: none"> • Treasury Management Strategy for 2016/17: <ul style="list-style-type: none"> ○ Borrowing – Paragraphs 25 to 36, ○ Debt Rescheduling – Paragraph 37 ○ Investments – Paragraphs 38 to 57 • Treasury Management Indicators – Paragraphs 58-66 • MRP Statement – Paragraphs 77 to 83 <p>Other Prudential Indicators – Paragraphs 86 to 105</p>
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	Alternative options for borrowing would depend on decisions taken on the review of the capital update report being taken at Full Council on 10 February 2016.
DETAIL (Including consultation carried out)	
	CONSULTATION
3.	The proposed Capital Update report on which this report is based has been subject to separate consultation processes.
	BACKGROUND
4.	The Local Government Act 2003 introduced a system for borrowing based largely on self-regulation by local authorities themselves. The basic principle of the new system is that local authorities will be free to borrow as long as their capital spending plans are affordable, prudent and sustainable.
5.	As per the requirements of the Prudential code, the Authority adopted the CIPFA Treasury Management Code at its Council meeting on 19 February 2003 and all its subsequent updates. The latest one being <i>Treasury Management in the Public Services: Code of Practice 2011 Edition</i> in February 2012.
6.	In addition, the Department for Communities and Local Government (CLG) issued revised <i>Guidance on Local Authority Investments</i> in March 2010 that requires the Authority to approve an investment strategy before the start of each financial year.
7.	This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA code and the CLG guidance.
8.	Overall responsibility for treasury management remains with the Council. No TM activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives. The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk.
9.	<p>The purpose of this TMSS is to allow Council to approve:</p> <ul style="list-style-type: none"> • Treasury Management Strategy for 2016/17 • Annual Investment Strategy 2016/17 • Prudential Indicators for 2016/17, 2017/18 and 2018/19 • 2016 MRP Statement

10.	The strategy takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the Prudential Indicators and the current and projected Treasury position (Appendix 1). The outlook for interest rates (Appendix 2) has also been taken into account in developing this strategy		
11.	The Council acknowledges that effective TM will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in TM, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management. To aid the Council in carrying out its TM function, it has appointed TM Advisors (Arlingclose), who advise the Council on strategy and provide market information to aid decision making. However it should be noted that the decisions are taken independently by the CFO taking into account this advice and other internal and external factors.		
12.	Some alternative strategies, with their financial and risk management implications, are listed below.		
	Options	Impact on income and expenditure	Impact on risk management
	Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
	Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses will be smaller
	Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs will be more certain
	Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long term costs will be less certain
	Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs will be less certain
	<u>Economic Background</u>		
13.	Domestic demand has grown robustly, supported by sustained real income growth and a gradual decline in private sector savings. Low oil and commodity prices were a notable feature of 2015, and contributed to annual CPI inflation falling to 0.1% in October. Wages are growing at 3% a year, and the unemployment rate has dropped to 5.4%. Mortgage approvals have risen to over 70,000 a month and annual house price growth is around 3.5%. These factors have boosted consumer confidence, helping to underpin retail spending and hence GDP growth, which was an encouraging 2.3% a year in the third quarter of 2015. Although speeches by the Bank of England's Monetary Policy Committee (MPC) members sent signals that some were willing to countenance		

	higher interest rates, the MPC held policy rates at 0.5% for the 81st consecutive month at its meeting in November 2015. Quantitative easing (QE) has been maintained at £375bn since July 2012.
14.	China's growth has slowed and its economy is performing below expectations, reducing global demand for commodities and contributing to emerging market weakness. US domestic growth has accelerated but the globally sensitive sectors of the US economy have slowed. Strong US labour market data and other economic indicators however suggest recent global turbulence has not knocked the American recovery off course. The Federal Reserve did not raise policy rates at its meetings in October and November, but the statements accompanying the policy decisions point have made a rate hike in December 2015 a real possibility. In contrast, the European Central Bank finally embarked on QE in 2015 to counter the perils of deflation.
	<u>Credit Outlook</u>
15.	The varying fortunes of different parts of the global economy are reflected in market indicators of credit risk. UK Banks operating in the Far East and parts of mainland Europe have seen their perceived risk increase, while those with a more domestic focus continue to show improvement. The sale of most of the government's stake in Lloyds and the first sale of its shares in RBS have generally been seen as credit positive.
16.	Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the UK, USA and Germany. The rest of the European Union will follow suit in January 2016, while Australia, Canada and Switzerland are well advanced with their own plans. Meanwhile, changes to the UK Financial Services Compensation Scheme and similar European schemes in July 2015 mean that most private sector investors are now partially or fully exempt from contributing to a bail-in. The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Authority; returns from cash deposits however remain stubbornly low.
	<u>Interest Rate Forecast</u>
17.	The Authority's treasury advisor Arlingclose projects the first 0.25% increase in UK Bank Rate in the third quarter of 2016, rising by 0.5% a year thereafter, finally settling between 2% and 3% in several years' time. Persistently low inflation, subdued global growth and potential concerns over the UK's position in Europe mean that the risks to this forecast are weighted towards the downside.
18.	A shallow upward path for medium term gilt yields is forecast, as continuing concerns about the Eurozone, emerging markets and other geo-political events weigh on risk appetite, while inflation expectations remain subdued. Arlingclose projects the 10 year gilt yield to rise from its current 2.0% level by around 0.3% a year. The uncertainties surrounding the timing of UK and US interest rate rises are likely to prompt short-term volatility in gilt yields.
19.	A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix 2
20.	For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.5%, and that new long-term

	loans will be borrowed at an average rate of 4%.																																																												
	BALANCE SHEET SUMMARY AND FORECAST																																																												
21.	The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The CFR, together with balances and useable reserves, are the core drivers of TM Activity.																																																												
22.	At 31/12/2015 the Authority held £323M of debt (£244M borrowing plus £79M other long term liabilities) and £102M investments which is set out in further detail in Appendix 1.																																																												
23.	Forecast changes in these sums are shown in the balance sheet analysis in Table 1 below.																																																												
24.	CIPFA's <i>Prudential Code for Capital Finance in Local Authorities</i> recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation and shows the impact of the capital programme and maturing debt if no new borrowing is taken.																																																												
	<p>Table 1: Balance sheet Summary and Forecast</p> <table border="1"> <thead> <tr> <th></th> <th>31.3.15 Actual £M</th> <th>31.3.16 Estimate £M</th> <th>31.3.17 Forecast £M</th> <th>31.3.18 Forecast £M</th> <th>31.3.19 Forecast £M</th> </tr> </thead> <tbody> <tr> <td>General Fund CFR</td> <td>274.1</td> <td>284.1</td> <td>352.1</td> <td>345.4</td> <td>338.3</td> </tr> <tr> <td>HRA CFR</td> <td>153.5</td> <td>174.6</td> <td>193.9</td> <td>190.2</td> <td>190.6</td> </tr> <tr> <td>Total CFR</td> <td>427.6</td> <td>458.7</td> <td>546.0</td> <td>535.6</td> <td>528.8</td> </tr> <tr> <td>Less: Other debt liabilities *</td> <td>(82.4)</td> <td>(80.1)</td> <td>(77.2)</td> <td>(75.0)</td> <td>(72.5)</td> </tr> <tr> <td>Borrowing CFR</td> <td>345.2</td> <td>378.5</td> <td>468.8</td> <td>460.6</td> <td>456.3</td> </tr> <tr> <td>Less: External borrowing</td> <td>(252.3)</td> <td>(240.8)</td> <td>(229.6)</td> <td>(218.1)</td> <td>(206.6)</td> </tr> <tr> <td>Internal borrowing</td> <td>92.9</td> <td>137.7</td> <td>239.4</td> <td>242.5</td> <td>249.7</td> </tr> <tr> <td>Less: Usable reserves and working capital</td> <td>(175.6)</td> <td>(163.2)</td> <td>(161.2)</td> <td>(145.6)</td> <td>(139.5)</td> </tr> <tr> <td>(Investments) / New borrowing Requirement</td> <td>(83.1)</td> <td>(25.7)</td> <td>78.0</td> <td>96.9</td> <td>110.2</td> </tr> </tbody> </table> <p>* finance leases, PFI liabilities and transferred debt that form part of the Authority's total debt</p>		31.3.15 Actual £M	31.3.16 Estimate £M	31.3.17 Forecast £M	31.3.18 Forecast £M	31.3.19 Forecast £M	General Fund CFR	274.1	284.1	352.1	345.4	338.3	HRA CFR	153.5	174.6	193.9	190.2	190.6	Total CFR	427.6	458.7	546.0	535.6	528.8	Less: Other debt liabilities *	(82.4)	(80.1)	(77.2)	(75.0)	(72.5)	Borrowing CFR	345.2	378.5	468.8	460.6	456.3	Less: External borrowing	(252.3)	(240.8)	(229.6)	(218.1)	(206.6)	Internal borrowing	92.9	137.7	239.4	242.5	249.7	Less: Usable reserves and working capital	(175.6)	(163.2)	(161.2)	(145.6)	(139.5)	(Investments) / New borrowing Requirement	(83.1)	(25.7)	78.0	96.9	110.2
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25.	The Authority's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Authority's long-term plans change is a secondary objective.																																																												
	<u>Strategy</u>																																																												
26.	Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term																																																												

	rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.
27.	Affordability and the “cost of carry” remained important influences on the Authority’s borrowing strategy alongside the consideration that, for any borrowing undertaken ahead of need, the proceeds would have to be invested in the money markets at rates of interest significantly lower than the cost of borrowing. As short-term interest rates are likely to remain, at least over the forthcoming two years, lower than long-term rates, the Authority determined it was more cost effective in the short-term to use internal resources and will look to borrow short-term loans instead
28.	By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of [internal / short-term] borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Arlingclose will assist the Authority with this ‘cost of carry’ and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2016/17 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
29.	Alternatively, the Authority may arrange forward starting loans during 2016/17, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period. In addition, the Authority may borrow short-term loans (normally for up to one month) to cover unexpected cash flow shortages.
	<u>Sources</u>
30.	The approved sources of long-term and short-term borrowing are: <ul style="list-style-type: none"> • Public Works Loan Board (PWLB) and any successor body • any institution approved for investments (see below) • any other bank or building society authorised to operate in the UK • UK public and private sector pension funds (except HCC Pension Fund) • capital market bond investors • UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues
31.	In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities: <ul style="list-style-type: none"> • operating and finance leases • hire purchase • Private Finance Initiative • sale and leaseback
32.	The Authority has previously raised the majority of its long-term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans, bank loans and the Municipal Bond Agency (see paragraph 33 below) which may be available at more favourable rates.
33.	UK Municipal Bonds Agency plc (MBA) was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds

	<p>on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities may be required to provide bond investors with a joint and several guarantee over the very small risk that other local authority borrowers default on their loans; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. The arrangements are set out in a framework agreement which SCC can access by executing a simple accession deed and a guarantee and by certifying to MBA that SCC has the necessary power and authority to enter the arrangement. Any borrowing by SCC under the arrangements would carry with it three costs:</p> <ol style="list-style-type: none"> 1. The interest payable under the loan, the rate of which will be known when the loan is taken out. 2. The costs potentially arising under the contribution loan mechanism in the framework agreement. 3. The costs potentially arising under the guarantee that SCC is required to give as a condition of using the arrangement. <p>It is under 2 and 3 that the potentially significant risk arises, however neither of these two risks are present if SCC accedes to the arrangement but does not borrow any money. Advice was sought from Legal and from a legal perspective a decision to accede but not borrow raises no concerns, however if the Council does borrow it would assume the risk of incurring the costs under 2 and 3 above and should consider the potential scale of that risk with reference to the following issues on each occasion it wished to borrow. Any initial decision to borrow from the Agency will therefore be the subject of a separate report to both Governance Committee and Full Council. Further a report setting out in full the details, options and risks of the MBA will be considered by full Council on 10 February 2016.</p>
	<p><u>Lender's Option Borrower's Option Loans (LOBOs)</u></p>
34.	<p>The Authority holds £9M of LOBO loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. All of these LOBOS have options during 2016/17 and although the Authority understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Authority will take the option to repay LOBO loans at no cost if it has the opportunity to do so.</p>
	<p><u>Short Term and Variable Rates</u></p>
35.	<p>Included within the PWLB portfolio is £35M of variable rate Loans, which are currently averaging 0.70% and are helping to keep the overall cost of borrowing down. Whilst in current climate of low interest rates this remains a sound strategy, these loans leave the authority exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators (paragraph 60), the Council review these regularly and if appropriate will switch into fixed rate loans.</p>
36.	<p>A 'Treasury Risk Reserve' is maintained to offset the risk of any unexpected rise in interest rates or the possible loss of investment due to the changes in banking regulations which increased the risk to Local Authorities. This reserve currently stands at £2M and is reviewed in line with the associated risks as detailed in CFO</p>

	statement within the Budget Setting Report.
	<u>Debt Rescheduling</u>
37.	The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.
	INVESTMENT STRATEGY
38.	Both the CIPFA and DCLG's Investment Guidance requires the authority to invest prudently and have regard to the security and liquidity of investments before seeking the optimum yield.
39.	The Authority has held significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months the Authority's investment balances have ranged between £92M and £125M and are currently £102M. Projected balances indicate that on present levels of spend we should have similar balances to last year, but this will be dependent on any borrowing decisions taken.
	<u>Objectives</u>
40.	Both the CIPFA Code and the CLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk receiving unsuitably low investment income.
	<u>Strategy</u>
41.	Given the increasing risk and continued low returns from short-term unsecured bank investments, the Authority aims to continue to diversify into more secure and/or higher yielding asset classes during 2016/17. Table 2 below shows the makeup of the Authority's current investments.

Table 2 – Investments as at 31 December 2015					
			Current Investment	Average Yield/ Rate	Forecast Yield
			£M	%	£'000
<u>Specified Investments</u>					
Cash			46.4	0.49	200
Short Term Fixed Deals			-	0.43	2
Corporate Bonds (not subject to Bail in)			15.3	0.98	185
Other Bonds			12.0	0.82	82
			73.7		469
<u>Unspecified Investments</u>					
Long term Bonds (not subject to Bail in)			15.9	1.90	300
Other Bonds			5.1	0.69	29
CCLA Property Fund			7.0	4.75	360
			28.0		689
<u>Total Investment</u>			101.7	1.84	1,158
<u>Total Investment excluding CCLA</u>			94.7	1.30	798
<u>Approved Counterparties</u>					
42.	The Authority may invest its surplus funds with any of the following counterparty types, subject to the cash limits (per counterparty) and time limits detailed in Appendix 4.				
43.	Credit Rating: Investment decisions are informed by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.				
44.	Banks Unsecured: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.				
45.	Banks Secured: Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.				
46.	Government: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in				

	unlimited amounts for up to 50 years.
47.	Corporates: Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.
48.	Registered Providers: Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain a high likelihood of receiving government support if needed.
49.	Pooled Funds: Shares in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods. Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority’s investment objectives will be monitored regularly.
50.	The Chief Financial Officer (CFO), under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported quarterly to Cabinet.
51.	Any institution will be suspended or removed should any of the factors identified in paragraph 55 below give rise to concern. Specifically credit ratings are monitored by the Authority on a daily basis. Arlingclose advises the Authority on ratings changes and appropriate action to be taken.
	<u>Risk Assessment and Credit Ratings</u>
52.	Credit ratings are obtained and monitored by the Authority’s treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then: <ul style="list-style-type: none"> • no new investments will be made, • any existing investments that can be recalled or sold at no cost will be, and • full consideration will be given to the recall or sale of all other existing investments with the affected counterparty. Where a credit rating agency announces that a rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can

	be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.
	<u>Other Information on the Security of Investments</u>
53.	The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.
54.	When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority’s cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office for example, or invested in government treasury bills for example or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.
	<u>Specified Investments</u>
55.	<p>The CLG Guidance defines specified investments as those:</p> <ul style="list-style-type: none"> • denominated in pound sterling, • due to be repaid within 12 months of arrangement, • not defined as capital expenditure by legislation, and • invested with one of: <ul style="list-style-type: none"> ○ the UK Government, ○ a UK local authority, parish council or community council, or ○ a body or investment scheme of “high credit quality”. <p>The Authority defines “high credit quality” organisations as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of A- or higher.</p>
	<u>Non-Specified Investments</u>
56.	Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and

investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in Table 3 below.

Table 3 – Non Specified Investment Limits 2016/17

	Cash Limit
Total long-term investments	£55M
Total investments without credit ratings or rated below A-	£10M
Total investments in foreign countries rated below AA+	£5M
Total non-specified investments	£70M

57.

Investment Limits: The Authority's revenue reserves and balances available to cover investment losses (excluding Schools, capital and HRA) are forecast to be £75.3M on 31st March 2016. In order that there is no immediate pressure on available reserves in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £10M. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries. Appendix 3 shows the current working limits in more detail.

	Cash limit
Any single organisation, except the UK Central Government	£10M each*
UK Central Government	unlimited
Any group of organisations under the same ownership	£10M per group*
Any group of pooled funds under the same management	£10M per manager
Negotiable instruments held in a broker's nominee account	£70M per broker
Foreign countries	£10M per country
Registered Providers	£5M in total
Unsecured investments with Building Societies	£5M in total
Loans to unrated corporates	£0.5M in total
Money Market Funds	£10M* per fund and no more than 50% of investments in total

**This is the absolute limit and the working limit will be monitored against actual cash flows and movement on reserves together with advice from our financial advisors and will be adjusted each quarter as necessary in agreement with the CFO.*

	<u>Liquidity Management</u>																								
	The Authority undertakes high level cash flow forecasting to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium term financial plan and cash flow forecast.																								
	<u>TREASURY MANAGEMENT INDICATORS</u>																								
58.	The Authority measures and manages its exposure to treasury management risks using the following indicators.																								
	<u>Liquidity</u>																								
59.	The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments and has set a £25M minimum threshold on cash available in instant access accounts, if balances were to fall below this limit we would consider taking short term loans which are available at competitive rates.																								
	<u>Upper Limits for Fixed and Variable Interest Rate Exposure</u>																								
60.	The following Prudential Indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises, which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short term rates on investments.																								
	Table 4 – Upper Limits for Fixed and Variable Interest Rate Exposure																								
	<table border="1"> <thead> <tr> <th></th> <th>Existing Level 31 December 2014</th> <th>2014/15 Approved</th> <th>2015/16 Estimate</th> <th>2016/17 Estimate</th> <th>2017/18 Estimate</th> </tr> <tr> <th></th> <th>%</th> <th>%</th> <th>%</th> <th>%</th> <th>%</th> </tr> </thead> <tbody> <tr> <td>Upper Limit for Fixed Interest Rate Exposure</td> <td>100</td> <td>100</td> <td>100</td> <td>100</td> <td>100</td> </tr> <tr> <td>Upper Limit for Variable Interest Rate Exposure</td> <td>50</td> <td>50</td> <td>50</td> <td>50</td> <td>50</td> </tr> </tbody> </table>		Existing Level 31 December 2014	2014/15 Approved	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate		%	%	%	%	%	Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100	Upper Limit for Variable Interest Rate Exposure	50	50	50	50	50
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61.	Fixed rate investments and borrowing are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.																								
62.	The Council will also limit and monitor large concentrations of fixed rate debt needing to be replaced. The limits provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Council's TM strategy.																								

<u>Maturity Structure of Fixed Rate borrowing</u>																																																																																																										
63.	This indicator is set to control the authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing as set out in Table 5 below:																																																																																																									
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64.	Time periods start on the first day of each financial year and the maturity date of borrowing is the earliest date on which the lender can demand repayment. As all LOBO are now in their call options they have been included as under 12 months within this indicator.																																																																																																									
65.	<p>Table 6 below details the level of our current fixed rate debt and shows that all debt is within existing limits.</p> <table border="1"> <thead> <tr> <th></th> <th>Lower Limit %</th> <th>Upper Limit %</th> <th>Actual Fixed Debt as at 31/12/2015 £M</th> <th>Average Fixed Rate as at 31/12/2015 %</th> <th>% of Fixed Rate as at 31/12/2015</th> <th>Compliance with set Limits?</th> </tr> </thead> <tbody> <tr> <td>Under 12 months</td> <td>0</td> <td>45</td> <td>9.4</td> <td>3.10</td> <td>4.47</td> <td>Yes</td> </tr> <tr> <td>12 months and within 24 months</td> <td>0</td> <td>45</td> <td></td> <td></td> <td></td> <td>Yes</td> </tr> <tr> <td>24 months and within 5 years</td> <td>0</td> <td>50</td> <td>11.5</td> <td>2.83</td> <td>5.48</td> <td>Yes</td> </tr> <tr> <td>5 years and within 10 years</td> <td>0</td> <td>75</td> <td>49.5</td> <td>3.51</td> <td>23.67</td> <td>Yes</td> </tr> <tr> <td>10 years and within 15 years</td> <td>0</td> <td>75</td> <td></td> <td></td> <td></td> <td>Yes</td> </tr> <tr> <td>15 years and within 20 years</td> <td>0</td> <td>75</td> <td></td> <td></td> <td></td> <td>Yes</td> </tr> <tr> <td>20 years and within 25 years</td> <td>0</td> <td>75</td> <td>10.0</td> <td>4.68</td> <td>4.78</td> <td>Yes</td> </tr> <tr> <td>25 years and within 30 years</td> <td>0</td> <td>75</td> <td>5.0</td> <td>4.60</td> <td>2.39</td> <td>Yes</td> </tr> <tr> <td>30 years and within 35 years</td> <td>0</td> <td>75</td> <td>25.0</td> <td>4.62</td> <td>11.95</td> <td>Yes</td> </tr> <tr> <td>35 years and within 40 years</td> <td>0</td> <td>75</td> <td>36.7</td> <td>3.54</td> <td>17.55</td> <td>Yes</td> </tr> <tr> <td>40 years and within 45 years</td> <td>0</td> <td>75</td> <td>47.9</td> <td>3.59</td> <td>22.90</td> <td>Yes</td> </tr> <tr> <td>45 years and within 50 years</td> <td>0</td> <td>75</td> <td>14.2</td> <td>3.70</td> <td>6.81</td> <td>Yes</td> </tr> <tr> <td>50 years and above</td> <td>0</td> <td>100</td> <td></td> <td></td> <td></td> <td>Yes</td> </tr> <tr> <td colspan="3"></td> <td>209.2</td> <td>3.57</td> <td>100</td> <td></td> </tr> </tbody> </table>		Lower Limit %	Upper Limit %	Actual Fixed Debt as at 31/12/2015 £M	Average Fixed Rate as at 31/12/2015 %	% of Fixed Rate as at 31/12/2015	Compliance with set Limits?	Under 12 months	0	45	9.4	3.10	4.47	Yes	12 months and within 24 months	0	45				Yes	24 months and within 5 years	0	50	11.5	2.83	5.48	Yes	5 years and within 10 years	0	75	49.5	3.51	23.67	Yes	10 years and within 15 years	0	75				Yes	15 years and within 20 years	0	75				Yes	20 years and within 25 years	0	75	10.0	4.68	4.78	Yes	25 years and within 30 years	0	75	5.0	4.60	2.39	Yes	30 years and within 35 years	0	75	25.0	4.62	11.95	Yes	35 years and within 40 years	0	75	36.7	3.54	17.55	Yes	40 years and within 45 years	0	75	47.9	3.59	22.90	Yes	45 years and within 50 years	0	75	14.2	3.70	6.81	Yes	50 years and above	0	100				Yes				209.2	3.57	100	
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	<u>Principal Sums Invested for Periods Longer than 364 days</u>				
66.	The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end is shown in Table 7 .				
	Table 7 – Principal Sums Invested for Periods Longer than 364 days				
		Current £M	2016/17 £M	2017/18 £M	2018/19 £M
	Limit on principal invested beyond year end	55	55	55	55
	<u>OTHER ITEMS</u>				
67.	There are a number of additional items that the Authority is obliged by CIPFA or CLG to include in its Treasury Management Strategy.				
	<u>Policy on Use of Financial Derivates</u>				
68.	Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).				
69.	The Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.				
70.	Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.				
	<u>Housing Revenue Account Self-Financing</u>				
71.	On 1st April 2012, the Authority notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account.				
72.	Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance. This balance will be measured and interest transferred between the General Fund and HRA at an				

	<p>agreed rate. Housing Legislation does not allow impairment losses to be charged to the HRA and consequently any credit related losses on the authority's investments will be borne by the General Fund alone. It is therefore appropriate that the General Fund is compensated for bearing this risk, and all interest transferred to the HRA should be adjusted downwards. The rate will be based on investments with the Debt Management Office. The rate of return on comparable investments with the government is lower and often referred to as the risk-free rate.</p>
	<p><u>Training</u></p>
73.	<p>CIPFA's Code of Practice requires the CFO to ensure that all Members tasked with TM responsibilities, including scrutiny of the TM function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Member training was last undertaken on the 2 November 2015. The Council adopts a continuous performance and development programme to ensure staff are regularly appraised and any training needs addressed. Relevant staff also attend regular training sessions, seminars and workshops which ensure their knowledge is up to date. Details of training received are maintained as part of the performance and development process.</p>
	<p><u>Treasury Management Advisors</u></p>
74.	<p>The CLG's Guidance on local government investments recommend that the Investment Strategy should state:</p> <p>Whether and, if so, how the Authority uses external contractors offering information, advice or assistance relating to investment and</p> <p>How the quality of any such service is controlled.</p> <p>The Council has a contract in place with Arlingclose Limited as treasury advisory service and receives the following services:</p> <ul style="list-style-type: none"> • Credit advice • Investment advice • Technical advice • Economic & interest rate forecasts • Workshops and training events • HRA support • Ad hoc advice <p>The Authority maintains the quality of the service with its advisors by holding quarterly meetings and tendering periodically. It should also be noted that decisions are taken independently by the CFO taking into account this advice and other internal and external factors.</p>
	<p><u>Investment of Money Borrowed in Advance of Need</u></p>
75.	<p>The Authority may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Authority is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Authority's overall management of its treasury risks.</p>

	The total amount borrowed will not exceed the authorised borrowing limit for the period. The maximum period between borrowing and expenditure is expected to be two years, although the Authority is not required to link particular loans with particular items of expenditure.
	<u>FINANCIAL IMPLICATIONS</u>
76.	The budget for debt interest paid in 2016/17 is £14.5M based on an average debt portfolio of £401.5M and an average interest rate of 3.6%. Investment income for 2016/17 is budgeted at £0.8M based on an average portfolio of £55.2M at an average of 1.44%. If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondently different.
	<u>2016/17 MINIMUM REVENUE PROVISION (MRP) STATEMENT</u>
77.	Where the Authority finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Authority to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the CLG Guidance) most recently issued in 2012.
78.	The CLG Guidance requires the Authority to approve an Annual MRP Statement each year. We have undertaken a prudency review of borrowing prior to the prudential regime and are currently discussing the proposed changes with our auditors. We will apply either the Regulatory or CFR method depending on the outcome of this. The asset life method will be applied to prudential borrowing unless it is for Investment purposes in which case no MRP will be applied.
79.	We will continue to review MRP and it is proposed that delegated powers should be given to the CFO to change the proposed methods to aid good financial management whilst maintaining a prudent approach. Any changes to the original MRP Statement during the year will be reported as part of quarterly financial and performance monitoring and in revisions to the TM strategy as part of the year end and midyear reviews.
80.	Following the HRA self-financing settlement, HRA debt increased from £100M to £174M with a borrowing cap of £200M. There is no requirement for the HRA to make debt repayments but it has opted to make voluntary repayments relating to debt inherited at the split and provision has been made within its business plan to show that it can pay down the remaining debt over the life of the 30 year business plan.
81.	MRP in respect of leases and Private Finance Initiative schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.
82.	Capital expenditure incurred during 2016/17 and funded from borrowing will not be subject to a MRP charge until 2017/18.
83.	Based on the Authority's latest estimate of its Capital Financing Requirement on 31 March 2016 the budget for MRP has been set on the assumption that we will be using the regulatory method for borrowing prior to the prudential regime (but

reducing the percentage applied from 4% to 2%) and using the asset life method for prudential borrowing where it applies. These assumptions form the basis of the MRP savings included within the General Fund Budget Report 2016/17 to 2019/20 to be reported to Council 10 February 2016. The estimated levels of MRP and CFR are shown in **Table 8** below:

Table 8 – Estimated MRP and CFR for 2016/17

	31/03/2015 Actual CFR £M	2015/16 MRP £M	31/03/2016 Estimated CFR £M	2016/17 Estimated MRP £M
Capital expenditure before 01.04.2008	95.6	1.47	91.9	1.39
Unsupported capital expenditure after 31.03.2008	96.0	3.01	112.1	3.32
Transferred debt	15.7	0.36	15.3	0.36
Finance leases and Private Finance Initiative	66.8	2.06	64.8	2.53
Total General Fund	274.1	7.17	284.1	7.60
Assets in the Housing Revenue Account	100.9	Nil	127.1	Nil
HRA subsidy reform payment	52.6	5.14	47.5	5.17
Total Housing Revenue Account	153.5	5.14	174.6	5.17
Total	427.6	12.31	458.7	12.77

MONITORING AND REPORTING ON THE ANNUAL TREASURY OUTTURN AND OTHER PRUDENTIAL INDICATORS

84. The Chief Financial Officer will report to the Governance Committee on TM activity / performance as follows:
- (a) A mid-year review against the strategy approved for the year.
 - (b) An outturn report on its treasury activity, no later than 30 September after the financial year end.

85. In addition, a quarterly update will be presented to Cabinet as part of Quarterly Revenue Financial Monitoring.

PRUDENTIAL INDICATORS

Background

86. The Local Government Act 2003 requires the Authority to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code

	are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Authority has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.																																								
	<u>Gross Debt and the Capital Financing Requirement</u>																																								
87.	This is a key indicator of prudence. In order to ensure that over the medium term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This view takes into account current commitments, existing plans and the proposals in the approved budget.																																								
88.	There is a significant difference between the gross external borrowing requirement and the net external borrowing requirement represented by the Council's level of balances, reserves, provisions and working capital. The Council's current strategy is only to borrow to the level of its net borrowing requirement. The reasons for this are to reduce credit risk, take pressure off the Council's lending list and also to avoid the cost of carry existing in the current interest rate environment.																																								
89.	The estimated gross debt and capital financing requirement is shown in the tables below: Table 9 – Gross Debt																																								
	<table border="1"> <thead> <tr> <th></th> <th>31/03/2016 Revised £M</th> <th>31/03/2017 Estimate £M</th> <th>31/03/2018 Estimate £M</th> <th>31/03/2019 Estimate £M</th> </tr> </thead> <tbody> <tr> <td>Borrowing (Long Term)</td> <td>110.84</td> <td>186.5</td> <td>187.2</td> <td>187.8</td> </tr> <tr> <td>Borrowing (Temporary)</td> <td>30.0</td> <td>30.0</td> <td>30.0</td> <td>30.0</td> </tr> <tr> <td>Finance leases and Private Finance Initiative</td> <td>64.8</td> <td>62.3</td> <td>60.4</td> <td>58.3</td> </tr> <tr> <td>Transferred debt</td> <td>15.6</td> <td>15.3</td> <td>14.9</td> <td>14.6</td> </tr> <tr> <td>Total General Fund Debt</td> <td>221.24</td> <td>294.1</td> <td>292.5</td> <td>290.7</td> </tr> <tr> <td>HRA</td> <td>174.6</td> <td>193.9</td> <td>190.2</td> <td>190.6</td> </tr> <tr> <td>Total</td> <td>395.8</td> <td>488.0</td> <td>482.7</td> <td>481.3</td> </tr> </tbody> </table>		31/03/2016 Revised £M	31/03/2017 Estimate £M	31/03/2018 Estimate £M	31/03/2019 Estimate £M	Borrowing (Long Term)	110.84	186.5	187.2	187.8	Borrowing (Temporary)	30.0	30.0	30.0	30.0	Finance leases and Private Finance Initiative	64.8	62.3	60.4	58.3	Transferred debt	15.6	15.3	14.9	14.6	Total General Fund Debt	221.24	294.1	292.5	290.7	HRA	174.6	193.9	190.2	190.6	Total	395.8	488.0	482.7	481.3
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Total	395.8	488.0	482.7	481.3																																					

Table 10 – Movement in CFR				
	31/03/2016 Revised £M	31/03/2017 Estimate £M	31/03/2018 Estimate £M	31/03/2019 Estimate £M
Balance Brought Forward	274.1	284.1	352.1	345.4
New Borrowing	17.5	75.5	0.3	0.1
MRP	(4.5)	(4.7)	(4.8)	(4.8)
Appropriations	(0.6)			
Movement in Other Liabilities	(2.4)	(2.8)	(2.2)	(2.4)
Total General Fund Debt	284.1	352.1	345.4	338.3
HRA (see Table 15 for breakdown)	174.6	193.9	190.2	190.5
Total	458.7	546.0	535.6	528.8
<u>Estimates of Capital Expenditure</u>				
90.	The Authority's planned capital expenditure and financing is summarised below, further detail is provided in the General Fund and HRA Capital programme report submitted elsewhere on the agenda.			

Table 11 – Capital Expenditure

Capital Expenditure and Financing	2015/16 Estimate	2015/16 Revised	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
	£M	£M	£M	£M	£M
General Fund	46.78	49.25	111.08	6.28	0.27
HRA	65.55	54.96	58.89	35.37	38.67
Total Expenditure	112.33	104.21	169.97	41.65	38.94
Capital receipts	14.04	1.02	3.73	3.48	2.77
Capital Grants	28.02	25.05	31.15	4.95	0.00
Contributions	4.04	6.66	3.51	1.90	0.08
Major Repairs Allowance	18.97	18.98	19.89	20.33	20.71
Revenue	12.03	9.36	11.63	9.26	9.76
Total Financing	77.10	61.07	69.91	39.92	33.32
Temporary Financing	(1.00)	0.00	0.00	0.00	0.00
Unsupported borrowing	36.22	43.14	100.06	1.73	5.62
Total Funding	35.22	43.14	100.06	1.73	5.62
Total Financing & Funding	112.33	104.21	169.97	41.65	38.94

Ratio of Financing Costs to Net Revenue Stream

91. This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. The ratio is based on costs net of investment income. The upper limit for this ratio is currently set at 10% and will remain so for the General Fund to allow for known borrowing decision in the next two years and to allow for additional borrowing affecting major schemes. The table below shows the likely position based on the proposed capital programme.

92.	This indicator is not so relevant for the HRA, especially since the introduction of self-financing, as financing costs have been built into their 30 year business plan, including the voluntary payment of MRP. No problem is seen with the affordability but if problems were to arise then the HRA would have the option not to make principle repayments in the early years.						
Table 12 – Ratio of Financing Costs to Net Revenue Stream							
93.	Ratio of Financing Costs to Net Revenue Stream	2014/15 Actual %	2015/16 Approved %	2015/16 Forecast %	2016/17 Estimate %	2017/18 Estimate %	2018/19 Estimate %
	General Fund	5.76%	6.83%	4.7%	7.22%	8.38%	8.67%
	HRA	14.61%	14.93%	14.18%	15.48%	15.60%	16.11%
	Total	9.07%	10.17%	8.45%	10.74%	11.52%	11.98%
<u>Incremental Impact of Capital Investment Decisions</u>							
94.	This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement (i.e. Interest and MRP) of the current approved capital programme with an equivalent calculation arising from the proposed programme. The incremental impact of capital investments decisions are shown below. These figures exclude any borrowing taken for Invest to Save schemes, as borrowing costs will be offset by income generation.						
Table 13– Incremental Impact of Capital Investment Decisions							
95.	Incremental Impact of Capital Investment Decisions	2015/16 Approved	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate		
		£	£	£	£		
	Increase / (Decrease) per average number of equivalent band D properties for Council Tax purposes	5.36	7.44	12.03	12.15		
	Increase in Average Weekly Housing Rents	57.92	58.89	35.37	38.67		
96.	It should be noted that these indicators are for illustrative purposes only and show the amount per equivalent band D properties that this change would equate to since the last capital update published in September.						
97.	As per the General Fund these indicators are illustrative as HRA rent levels are currently set under the Government's rent restructuring formula, which is independent of the level of capital investment and borrowing. The calculation of the indicator ignores this factor.						
<u>Authorised Limit and Operational Boundary for External Debt</u>							

98.	The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.																																									
99.	<p>The Authorised Limit sets the maximum level of external borrowing on a gross basis (i.e. excluding investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.</p> <p>The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements, for example a complete debt restructure which requires monies to be borrowed in advance of repayment of existing debt. The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).</p>																																									
Table 14 – Authorised Limit for External Debt																																										
100.	<table border="1"> <thead> <tr> <th>Authorised Limit for External Debt</th> <th>Actual 31 December 2015</th> <th>2015/16 Approved</th> <th>2015/16 Estimate</th> <th>2016/17 Estimate</th> <th>2017/18 Estimate</th> <th>2018/19 Estimate</th> </tr> <tr> <td></td> <td>£M</td> <td>£M</td> <td>£M</td> <td>£M</td> <td>£M</td> <td>£M</td> </tr> </thead> <tbody> <tr> <td>Borrowing</td> <td>244.2</td> <td>640</td> <td>651</td> <td>779</td> <td>943</td> <td>929</td> </tr> <tr> <td>Other Long-term Liabilities</td> <td>78.8</td> <td>87</td> <td>87</td> <td>84</td> <td>81</td> <td>79</td> </tr> <tr> <td>Total</td> <td>323.0</td> <td>727</td> <td>738</td> <td>863</td> <td>1,024</td> <td>1,008</td> </tr> </tbody> </table>	Authorised Limit for External Debt	Actual 31 December 2015	2015/16 Approved	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate		£M	£M	£M	£M	£M	£M	Borrowing	244.2	640	651	779	943	929	Other Long-term Liabilities	78.8	87	87	84	81	79	Total	323.0	727	738	863	1,024	1,008						
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101.	The Operational Boundary is linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit																																									
Table 15–Operational Boundary for External Debt																																										
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	Other Long-term Liabilities	78.8	87	87	84	81	79
	Total	323.0	553	596	700	738	747

103. The CFO has delegated authority, within the above limits for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Council will be notified of any use of this delegated authority.

HRA Limit on Indebtedness

104. Local authorities are required to report the level of the HRA CFR compared to the level of debt which is imposed (or subsequently amended) by the DCLG at the time of implementation of self – financing. The HRA is still within the HRA Debt Cap set CLG of £199.6M.

Table 16 – HRA Limit on Indebtedness

105.	HRA Summary of Borrowing	2015/16 Approved	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
		£M	£M	£M	£M	£M
	Brought Forward	157.5	153.5	174.6	193.9	190.2
	Maturing Debt	(5.1)	(5.1)	(5.2)	(5.2)	(5.2)
	New borrowing	34.4	25.6	24.5	1.5	5.5
	Appropriations		0.6			
	Carried forward	186.8	174.6	193.9	190.2	190.5

RESOURCE IMPLICATIONS

Capital/Revenue

106. The revenue and capital implications are considered as part of ongoing monitoring which is reported to Cabinet each quarter and as part of the budget setting process.

Property/Other

107. None

LEGAL IMPLICATIONS

Statutory power to undertake proposals in the report:

108. Local Authority borrowing is regulated by Part 1, of the Local Government Act 2003, which introduced the new Prudential Capital Finance System. From 1 April 2004, investments are dealt with, not in secondary legislation, but through guidance. Similarly, there is guidance on prudent investment practice, issued by the Secretary of State under Section 15(1) (a) of the 2003 Act. A local authority has the power to invest for "any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs". The reference to the "prudent management of its financial affairs" is included to cover investments, which are not directly linked to identifiable statutory functions but are simply made in the course of treasury management. This also allows the temporary investment of funds borrowed for the purpose of expenditure in the

	reasonably near future; however, the speculative procedure of borrowing purely in order to invest and make a return remains unlawful.
Other Legal Implications:	
109.	None
POLICY FRAMEWORK IMPLICATIONS	
110.	This report has been prepared in accordance with the CIPFA Code of Practice on TM.

KEY DECISION?	No	
WARDS/COMMUNITIES AFFECTED:	None	
<u>SUPPORTING DOCUMENTATION</u>		
Appendices		
1.	Existing Investment & Debt Portfolio Position and Projections	
2.	Economic and Interest Outlook	
3.	Counterparty Cash and Time Limits	
4.	Treasury Management Policy Statement	
5.	Glossary of Treasury Terms	
Documents In Members' Rooms		
1.	None	
Equality Impact Assessment		
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.		No
Privacy Impact Assessment		
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.		No
Title of Background Paper(s)		Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	Treasury Management Strategy and Prudential Limits 2016/17 to 2017/18	Item 80
2.	Treasury Management Strategy and Prudential Limits Midyear Review 2015	Item 12

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Appendix 1

EXISTING INVESTMENT & DEBT PORTFOLIO POSITION AND PROJECTIONS

	31-Mar-15 Actual £M	31-Mar-16 Mid Year Review £M	Current Portfolio £M	31-Mar-16 Current Estimate £M	31-Mar-17 Current Estimate £M	31-Mar-18 Current Estimate £M	31-Mar-19 Current Estimate £M
External Borrowing:							
Fixed Rate – PWLB Maturity	139	191	139	183	290	298	311
Fixed Rate – PWLB EIP	69	58	64	58	47	35	23
Variable Rate – PWLB	35	35	35	35	35	35	35
Variable Rate – Market	9	9	9	9	9	9	9
Long Term Borrowing	252	293	247	285	381	377	378
Short Term Borrowing							
Fixed Rate – Market	0	30	0	30	30	30	30
Other Long Term Liabilities							
PFI / Finance leases	67	65	65	65	62	60	58
Deferred Debt Charges	16	15	15	16	15	15	15
Total Gross External Debt	335	403	327	396	488	482	481
Investments:							
Managed In-House							
Deposits and monies on call and Money Market Funds	(55)	(25)	(37)	(25)	(25)	(25)	(25)
Financial Instruments	(32)	(60)	(57)	(62)	(57)	(52)	(47)
Managed Externally							
Pooled Funds	(5)	(7)	(7)	(7)	(7)	(7)	(7)
Total Investments	(92)	(92)	(101)	(94)	(89)	(84)	(79)
Net Borrowing Position	243	311	226	302	399	398	402

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Agenda Item 5

Appendix 2

ECONOMIC AND INTEREST OUTLOOK

The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, for December 2015 is detailed below. The Council will reappraise its strategy from time to time and, if needs be, realign it with evolving market conditions and expectations for future interest rates.

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18
Official Bank Rate													
Upside risk		0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75
Downside risk				-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-1.00	-1.00	-1.25	-1.25
3-month LIBID rate													
Upside risk	0.20	0.30	0.30	0.30	0.35	0.35	0.35	0.35	0.40	0.40	0.40	0.40	0.40
Arlingclose Central Case	0.55	0.60	0.70	0.80	0.95	1.05	1.15	1.30	1.40	1.55	1.65	1.80	1.85
Downside risk		-0.20	-0.30	-0.45	-0.55	-0.65	-0.80	-0.90	-1.05	-1.10	-1.20	-1.20	-1.20
1-yr LIBID rate													
Upside risk	0.25	0.35	0.35	0.35	0.40	0.40	0.40	0.40	0.45	0.45	0.45	0.45	0.45
Arlingclose Central Case	1.10	1.20	1.35	1.45	1.55	1.70	1.80	1.95	2.00	2.10	2.15	2.15	2.15
Downside risk	-0.15	-0.25	-0.35	-0.50	-0.60	-0.70	-0.85	-0.95	-1.10	-1.15	-1.25	-1.25	-1.25
5-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	1.50	1.55	1.60	1.70	1.80	1.90	2.00	2.10	2.20	2.25	2.30	2.35	2.35
Downside risk	-0.35	-0.45	-0.55	-0.60	-0.70	-0.80	-0.90	-1.00	-1.10	-1.15	-1.20	-1.25	-1.25
10-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	2.00	2.05	2.10	2.20	2.30	2.40	2.50	2.60	2.65	2.70	2.75	2.80	2.80
Downside risk	-0.35	-0.45	-0.55	-0.60	-0.70	-0.80	-0.90	-1.00	-1.10	-1.15	-1.20	-1.25	-1.25
20-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	2.45	2.50	2.55	2.55	2.60	2.65	2.70	2.75	2.80	2.85	2.90	2.95	2.95
Downside risk	-0.30	-0.40	-0.50	-0.55	-0.65	-0.75	-0.85	-0.95	-1.05	-1.10	-1.15	-1.20	-1.20
50-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	2.45	2.50	2.55	2.60	2.65	2.70	2.75	2.80	2.85	2.90	2.95	3.00	3.00
Downside risk	-0.25	-0.35	-0.45	-0.50	-0.60	-0.70	-0.80	-0.90	-1.00	-1.05	-1.10	-1.15	-1.15

Underlying Assumptions:

- The UK economic growth softened in Q3 2015 but remained reasonably robust; the first estimate for the quarter was 0.5% and year-on-year growth fell slightly to 2.3%. Negative construction output growth offset fairly strong services output, however survey estimates suggest upwards revisions to construction may be in the pipeline.
- Household spending has been the main driver of GDP growth through 2014 and 2015 and remains key to growth. Consumption will continue to be supported by real wage and disposable income growth.
- Annual average earnings growth was 3.0% (including bonuses) in the three months to August. Given low inflation, real earnings and income growth continue to run at relatively strong levels and could feed directly into unit labour costs and households' disposable income. Improving productivity growth should support pay growth in the medium term. The development of wage growth is one of the factors being closely monitored by the MPC.
- Business investment indicators continue to signal strong growth. However the outlook for business investment may be tempered by the looming EU referendum,

increasing uncertainties surrounding global growth and recent financial market shocks.

- Inflation is currently very low and, with a further fall in commodity prices, will likely remain so over the next 12 months. The CPI rate is likely to rise towards the end of 2016.
- China's growth has slowed and its economy is performing below expectations, which in turn will dampen activity in countries with which it has close economic ties; its slowdown and emerging market weakness will reduce demand for commodities. Other possible currency interventions following China's recent devaluation will keep sterling strong against many global currencies and depress imported inflation.
- Strong US labour market data and other economic indicators suggest recent global turbulence has not knocked the American recovery off course. Although the timing of the first rise in official interest rates remains uncertain, a rate rise by the Federal Reserve seems significantly more likely in December given recent data and rhetoric by committee members.
- Longer term rates will be tempered by international uncertainties and weaker global inflation pressure.

Forecast:

- Our Advisors forecast the first rise in official interest rates in Q3 2016. Further weakness in inflation, and the MPC's expectations for its path, suggest policy tightening will be pushed back into the second half of the year. Risks remain weighted to the downside. Arlingclose projects a slow rise in Bank Rate, the appropriate level of which will be lower than the previous norm and will be between 2 and 3%.
- The projection is for a shallow upward path for medium term gilt yields, with continuing concerns about the Eurozone, emerging markets and other geo-political events, weighing on risk appetite, while inflation expectations remain subdued.
- The uncertainties surrounding the timing of UK and US monetary policy tightening, and global growth weakness, are likely to prompt short term volatility in gilt yields.

COUNTERPARTY CASH AND TIME LIMITS

These operational limits will be reviewed each quarter and adjusted as necessary for predicated cash flows and balances and any advice from our Financial Advisors.

Credit Rating	Banks Unsecured	Banks Secured	Government & Local Authorities	Corporates	Registered Providers
	£M	£M			
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£5M 5 years	£10M 20 years	£10M 50 years	£5M 20 years	£5M 20 years
AA+	£5M 5 years	£10M 10 years	£10M 25 years	£5M 10 years	£5M 10 years
	£5M 4 years	£10M 5 years	£10M 15 years	£5M 5 years	£5M 10 years
AA-	£5M 3 years	£10M 4 years	£10M 10 years	£5M 4 years	£5M 10 years
A+	£5M 2 years	£10M 3 years	£5M 5 years	£5M 3 years	£5M 5 years
A	£5M 13 months	£10M 2 years	£5M 5 years	£5M 2 years	£5M 5 years
A-	£5M 6 months	£10M 13 months	£5M 5 years	£5M 13 months	£5M 5 years
BBB+	£2.5M 100 days	£5M 6 months	£2.5M 2 years	£2.5M 6 months	£5M 2 years
BBB	£2.5M next day only	£5M 100 days	n/a	n/a	n/a
None	£1M 6 months	n/a	£10M 25 years	£0.5M 5 years	£5M 5 years
Pooled funds	£10M per fund				

Please read notes in paragraph 59 of main report in conjunction with this table.

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GLOSSARY OF TREASURY TERMS

Amortised Cost Accounting:

Values the asset at its purchase price, and then subtracts the premium/adds back the discount linearly over the life of the asset. The asset will be valued at par at its maturity.

Authorised Limit (Also known as the Affordable Limit):

A statutory limit that sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities).

Balances and Reserves:

Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.

Bail - in Risk:

Following the financial crisis of 2008 when governments in various jurisdictions injected billions of dollars into banks as part of bail-out packages, it was recognised that bondholders, who largely remained untouched through this period, should share the burden in future by making them forfeit part of their investment to "bail in" a bank before taxpayers are called upon.

A bail-in takes place before a bankruptcy and under current proposals, regulators would have the power to impose losses on bondholders while leaving untouched other creditors of similar stature, such as derivatives counterparties. A corollary to this is that bondholders will require more interest if they are to risk losing money to a bail-in.

Bank Rate:

The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.

Basis Point:

A unit of measure used in finance to describe the percentage change in the value or rate of a financial instrument. One basis point is equivalent to 0.01% (1/100th of a percent). In most cases, it refers to changes in **interest rates** and **bond yields**. For example, if interest rates rise by 25 basis points, it means that rates have risen by 0.25% percentage points. If rates were at 2.50%, and rose by 0.25%, or 25 basis points, the new interest rate would be 2.75%. In the bond market, a basis point is used to refer to the yield that a bond pays to the investor. For example, if a bond yield moves from 5.45% to 5.65%, it is said to have risen by 20 basis points. The usage of the basis point measure is primarily used in respect to yields and interest rates, but it may also be used to refer to the percentage change in the value of an asset such as a stock.

Bond:

A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The repayment date is also set at the onset but can be traded during its life, but this will affect the price of a bond which may vary during its life.

<p>Capital Expenditure:</p> <p>Expenditure on the acquisition, creation or enhancement of capital assets.</p>
<p>Capital Financing Requirement (CFR):</p> <p>The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need.</p>
<p>Certainty Rate:</p> <p>The government has reduced by 20 basis points (0.20%) the interest rates on loans via the Public Works Loan Board (PWLB) to principal local authorities who provide information as specified on their plans for long-term borrowing and associated capital spending.</p>
<p>CD's:</p> <p>Certificates of Deposits with banks and building societies</p>
<p>Capital Receipts:</p> <p>Money obtained on the sale of a capital asset.</p>
<p>Comprehensive Spending Review (CSR):</p> <p>Comprehensive Spending Review is a governmental process in the United Kingdom carried out by HM Treasury to set firm expenditure limits and, through public service agreements, define the key improvements that the public can expect from these resources. Spending Reviews typically focus upon one or several aspects of public spending while the CSR focuses upon each government department's spending requirements from a zero base (i.e. without reference to past plans or, initially, current expenditure).</p>
<p>Constant Net Asset Value (CNAV)</p> <p>These are Money Market Funds which maintain a stable price of £1 per share when investors redeem or purchase shares which mean that that any investment will not fluctuate in value.</p>
<p>Corporate Bonds:</p> <p>Corporate bonds are bonds issued by companies. The term is often used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.</p>
<p>Cost of Carry:</p> <p>The "cost of carry" is the difference between what is paid to borrow compared to the interest which could be earned. For example, if one takes out borrowing at 5% and invests the money at 1.5%, there is a cost of carry of 3.5%.</p>
<p>Counterparty List:</p> <p>List of approved financial institutions with which the Council can place investments with.</p>
<p>Covered Bond:</p> <p>Covered bonds are debt securities backed by cash flows from mortgages or public sector loans. They are similar in many ways to asset-backed securities created in securitisation, but covered bond assets remain on the issuer's consolidated balance sheet (usually with an appropriate capital charge). The covered bonds continue as obligations of the issuer (often</p>

a bank); in essence, the investor has recourse against the issuer and the collateral, sometimes known as "dual recourse."

CPI :

Consumer Price Index – the UK’s main measure of inflation.

Credit Rating:

Formal opinion by a registered rating agency of a counterparty’s future ability to meet its financial liabilities; these are opinions only and not guarantees.

Department for Communities and Local Government (DCLG) :

The DCLG is the UK Government department for Communities and Local Government in England. It was established in May 2006 and is the successor to the Office of the Deputy Prime Minister, established in 2001.

Debt Management Office (DMO):

The DMO is an Executive Agency of Her Majesty's Treasury and provides direct access for local authorities into a government deposit facility known as the **DMADF**. All deposits are guaranteed by HM Government and therefore have the equivalent of a sovereign triple-A credit rating.

Diversification /diversified exposure:

The spreading of investments among different types of assets or between markets in order to reduce risk.

European Investment Bank (EIB):

The European Investment Bank is the European Union's non-profit long-term lending institution established in 1958 under the Treaty of Rome. It is a "policy driven bank" whose shareholders are the member states of the EU. The EIB uses its financing operations to support projects that bring about European integration and social cohesion.

Federal Reserve:

The US central bank. (Often referred to as “the Fed”).

Floating rate notes (FRNs) :

Floating rate notes (FRNs) are debt securities with payments that are reset periodically against a benchmark rate, such as the three-month Treasury bill or the three-month London inter-bank offer rate (LIBOR). FRNs can be used to balance risks incurred through other interest rate instruments in an investment portfolio.

FTSE 100 Index:

The FTSE 100 Index is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalisation. It is one of the most widely used stock indices and is seen as a gauge of business prosperity for business regulated by UK company law. The index is maintained by the FTSE Group, a subsidiary of the London Stock Exchange Group.

General Fund:

This includes most of the day-to-day spending and income.

Gilts:

Gilts are bonds issued by the UK Government. They take their name from 'gilt-edged': being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.

Gross Domestic Product (GDP):

Gross Domestic Product measures the value of goods and services produced with in a country. GDP is the most comprehensive overall measure of economic output and provides key insight as to the driving forces of the economy.

The G7:

The G7, is a group consisting of the finance ministers of seven industrialised nations: namely the US, UK, France, Germany, Italy, Canada and Japan. They are seven of the eight (China excluded) wealthiest nations on Earth, not by GDP but by global net wealth. The G7 represents more than the 66% of net global wealth (\$223 trillion), according to Credit Suisse Global Wealth Report September 2012.

IFRS:

International Financial Reporting Standards.

International Labour Organisation (ILO):

The ILO Unemployment Rate refers to the percentage of economically active people who are unemployed by ILO standard and replaced the Claimant Unemployment Rate as the international standard for unemployment measurement in the UK.. Under the ILO approach, those who are considered as unemployed are either out of work but are actively looking for a job or out of work and are waiting to start a new job in the next two weeks. ILO Unemployment Rate is measured by a monthly survey, which is called the Labour Force Survey in United Kingdom. Approximately 40,000 individuals are interviewed each month, and the unemployment figure reported is the average data for the previous three months.

LIBID:

The London Interbank Bid Rate (LIBID) is the rate bid by banks on Eurocurrency deposits (i.e. the rate at which a bank is willing to borrow from other banks). It is "the opposite" of the LIBOR (an offered, hence "ask" rate, the rate at which a bank will lend). Whilst the British Bankers' Association set LIBOR rates, there is no correspondent official LIBID fixing.

LIBOR:

The London Interbank Offered Rate (LIBOR) is the rate of interest that banks charge to lend money to each other. The British Bankers' Association (BBA) work with a small group of large banks to set the LIBOR rate each day. The wholesale markets allow banks who need money to be more fluid in the marketplace to borrow from those with surplus amounts. The banks with surplus amounts of money are keen to lend so that they can generate interest which it would not otherwise receive.

LOBO:

Stands for Lender Option Borrower Option. The underlying loan facility is typically very long-term - for example 40 to 60 years - and the interest rate is fixed. However, in the LOBO facility the lender has the option to call on the facilities at pre-determined future dates. On these call dates, the lender can propose or impose a new fixed rate for the remaining term of the facility and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan facility. The upshot of this is that on the option exercise date, the lender could propose an extreme fixed rate, say 20 per cent, which would

effectively force the repayment of the underlying facility. The borrower's so called 'option' is only the inalienable right to accept or refuse a new deal such as a fixed rate of 20 per cent.

Maturity:

The date when an investment or borrowing is repaid.

Maturity Structure / Profile:

A table or graph showing the amount (or percentage) of debt or investments maturing over a time period. The amount or percent maturing could be shown on a year-by-year or quarter-by quarter or month-by-month basis.

Minimum Revenue Provision (MRP):

An annual provision that the Council is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets.

Money Market Funds (MMF):

An open-end mutual fund which invests only in money markets. These funds invest in short term debt obligations such as short-dated government debt, certificates of deposit and commercial paper. The main goal is the preservation of principal, accompanied by modest dividends. The fund's net asset value remains constant (eg £1 per unit) but the interest rate does fluctuate. These are liquid investments, and therefore, are often used by financial institutions to store money that is not currently invested. Risk is extremely low due to the high rating of the MMFs; many have achieved AAA credit status from the rating agencies:

- **Constant net asset value (CNAV)** refers to funds which use amortised cost accounting to value all of their assets. They aim to maintain a net asset value (NAV), or value of a share of the fund, at €1/£1/\$1 and calculate their price to two decimal places known as "penny rounding". Most CNAV funds distribute income to investors on a regular basis (distributing share classes), though some may choose to accumulate the income, or add it on to the NAV (accumulating share classes). The NAV of accumulating CNAV funds will vary by the income received.
- **Variable net asset value (VNAV)** refers to funds which use mark-to-market accounting to value some of their assets. The NAV of these funds will vary by a slight amount, due to the changing value of the assets and, in the case of an accumulating fund, by the amount of income received.

This means that a fund with an unchanging NAV is, by definition, CNAV, but a fund with a NAV that varies may be accumulating CNAV or distributing or accumulating VNAV.

Multilateral Development Banks:

See Supranational Bonds below.

Municipal Bonds Agency

An independent body owned by the local government sector that seeks to raise money on the capital markets at regular intervals to on-lend to participating local authorities.

Non Specified Investment:

Investments which fall outside the CLG Guidance for **Specified investments** (below).

Operational Boundary:

This linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised

Limit reflecting the most likely prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

Premiums and Discounts:

In the context of local authority borrowing,

- (a) the premium is the penalty arising when a loan is redeemed prior to its maturity date and
- (b) the discount is the gain arising when a loan is redeemed prior to its maturity date.

If on a £1 million loan, it is calculated that a £150,000 premium is payable on premature redemption, then the amount paid by the borrower to redeem the loan is £1,150,000 plus accrued interest. If on a £1 million loan, it is calculated* that a £50,000 discount receivable on premature redemption, then the amount paid by the borrower to redeem the loan is £950,000 plus accrued interest. PWLB premium/discount rates are calculated according to the length of time to maturity, current market rates (plus a margin), and the existing loan rate which then produces a premium/discount dependent on whether the discount rate is lower/higher than the coupon rate.

**The calculation of the total amount payable to redeem a loan borrowed from the Public Works Loans Board (PWLB) is the present value of the remaining payments of principal and interest due in respect of the loan being repaid prematurely, calculated on normal actuarial principles. More details are contained in the PWLB's lending arrangements circular.*

Property:

Investment property is property (land or a building or part of a building or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both.

Prudential Code:

Developed by CIPFA and introduced on 01/4/2004 as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.

Prudential Indicators:

Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators

Public Works Loans Board (PWLB):

This is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.

Quantitative Easing (QE):

In relation to the UK, it is the process used by the Bank of England to directly increase the quantity of money in the economy. It *“does not involve printing more banknotes. Instead, the Bank buys assets from private sector institutions – that could be insurance companies, pension funds, banks or non-financial firms – and credits the seller’s bank account. So the seller has more money in their bank account, while their bank holds a corresponding claim against the Bank of England (known as reserves). The end result is more money out in the wider economy”*. Source: Bank of England.

Repo Rate:

The interest rate at which the central bank in a country repurchases government securities (such as Treasury securities) from commercial banks. The central bank raises the repo rate when it wishes to reduce the money supply in the short term, while it lowers the rate when it wishes to increase the money supply and stimulate growth.

Revenue Expenditure:

Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.

RPI:

Retail Prices Index is a monthly index demonstrating the movement in the cost of living as it tracks the prices of goods and services including mortgage interest and rent. Pensions and index-linked gilts are updated using the RPI index.

(Short) Term Deposits:

Deposits of cash with terms attached relating to maturity and rate of return (Interest).

Specified Investments:

Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than one year. UK government, local authorities and bodies that have a high credit rating.

Supported Borrowing:

Borrowing for which the costs are supported by the government or third party.

Supranational Bonds:

Instruments issued by supranational organisations created by governments through international treaties (often called **multilateral development banks**). The bonds carry a AAA rating in their own right. Examples of supranational organisations are the European Investment Bank, the International Bank for Reconstruction and Development.

Treasury (T) -Bills:

Treasury Bills are short term Government debt instruments and, just like temporary loans used by local authorities, are a means to manage cash flow. Treasury Bills (T-Bills) are issued by the Debt Management Office and are an eligible sovereign instrument, meaning that they have a AAA-rating.

Temporary Borrowing:

Borrowing to cover peaks and troughs of cash flow, not to fund capital spending.

Treasury Management Code:

CIPFA's Code of Practice for Treasury Management in the Public Services, initially brought in 2003, subsequently updated in 2009 and 2011.

Treasury Management Practices (TMP):

Treasury Management Practices set out the manner in which the Council will seek to achieve its policies and objectives and prescribe how it will manage and control these

activities.

Unsupported Borrowing:

Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing.

Variable Net Asset Value (VNAV):

Redemptions and investments in Money Market Funds (MMF's) are on the basis of the fund's Net Asset Value (NAV) per share. The NAV of any money market fund is the market value of the fund's assets minus its liabilities and is stated on a per share basis. The net value of the assets held by an MMF can fluctuate, and the market value of a share may not always be exactly the amount that has been invested.

Yield:

The measure of the return on an investment instrument.

TREASURY MANAGEMENT POLICY STATEMENT

1. INTRODUCTION AND BACKGROUND

- 1.1. The Council adopts the key recommendations of CIPFA's Treasury Management in the Public Services: Code of Practice (the Code), as described in Section 5 of the Code.
- 1.2. Accordingly, the Council will create and maintain, as the cornerstones for effective treasury management:-
 - A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities
 - Suitable Treasury Management Practices (TMPs), setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.
- 1.3. The Council (i.e. full Council) will receive reports on its treasury management policies, practices and activities including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.
- 1.4. The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to Governance Committee and for the execution and administration of treasury management decisions to Chief Financial Officer, who will act in accordance with the organisation's policy statement and TMPs and CIPFA's Standard of Professional Practice on Treasury Management.
- 1.5. The Council nominates Governance committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

2. POLICIES AND OBJECTIVES OF TREASURY MANAGEMENT ACTIVITIES

- 2.1. The Council defines its treasury management activities as:

“The management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.”

- 2.2. This Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

- 2.3. This Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.”
- 2.4. The Council’s borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council transparency and control over its debt.
- 2.5. The Council’s primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority’s investments followed by the yield earned on investments remain important but are secondary considerations.

Agenda Item 6

DECISION-MAKER:	GOVERNANCE COMMITTEE		
SUBJECT:	ANNUAL GOVERNANCE STATEMENT		
DATE OF DECISION:	8 FEBRUARY 2016		
REPORT OF:	CHIEF FINANCIAL OFFICER		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Peter Rogers	Tel: 023 8083 2835
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Director	Name:	Andy Lowe	Tel: 023 8083 2049
	E-mail:	andrew.lowe@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY	
None	
BRIEF SUMMARY	
<p>In accordance with the Accounts and Audit Regulations the Council is required to develop and publish an Annual Governance Statement ('AGS'). The AGS reports on the extent to which the Council has complied with its Code of Corporate Governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.</p>	
RECOMMENDATIONS:	
	(i) To note and approve the assurance gathering process to support the development of the 2015-16 Annual Governance Statement (Appendix 1); and
	(ii) To note the content of the Annual Governance Statement 2014-15 Action Plan - Status Report (Appendix 2).
REASONS FOR REPORT RECOMMENDATIONS	
1.	The Governance Committee has responsibility to provide independent assurance on the adequacy of the risk management framework and the internal control and reporting environment, including (but not limited to) the reliability of the financial reporting process and the annual governance statement.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	No alternative options have been considered
DETAIL (Including consultation carried out)	
3.	Regulation 6 (1) of the Accounts and Audit (England) Regulations 2015 requires that the relevant body must conduct a review at least once a year of the effectiveness of its system of internal control and to prepare a statement on internal control in accordance with proper practices.

4.	The purpose of the AGS, which is published with the statement of accounts, is to provide an accurate representation of the corporate governance arrangements in place during the year and to identify or highlight those areas where there are significant gaps or where improvements are required.
5.	The AGS is produced following a review of the Council's governance arrangements. The review requires the systems and processes that comprise the Council's corporate governance arrangements to be brought together and reviewed.
6.	An 'assurance gathering process' based on CIPFA/SOLACE guidance is in place and comprises an overall 'Assurance Framework' document together with 'Annual Governance - Self Assessment Statement' completed by each Director. Both the documents cover the key processes and systems that comprise the Council's governance arrangements and are intended to identify any areas where improvement or further development is required.
7.	The process to support the development of the AGS is largely unchanged from the previous year on the basis that it is considered that it is aligned with good practice. It should also be noted that the council's external auditors, Ernst & Young, are required to "consider the completeness of disclosures in the Council's AGS, identify any inconsistencies with the other information which we know about from our work, and consider whether it complies with relevant guidance". In their 'Annual Audit Letter for the year ended 31 March 2015' they state that "We completed this work and did not identify any areas of concern".
8.	The AGS itself is developed by a 'Controls Assurance Management Group' (comprising the Section 151 Officer, Chair of the Governance Committee, Monitoring Officer and Chief Internal Auditor) who are responsible for evaluating the assurances and supporting evidence provided, prior to drafting the AGS.
9.	The draft AGS will be presented to the Governance Committee for review and approval prior to being forwarded to the Chief Executive and Leader of the Council for signing.
RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
10.	N/A
<u>Property/Other</u>	
11.	N/A
LEGAL IMPLICATIONS	
<u>Statutory power to undertake proposals in the report:</u>	
12.	The Accounts and Audit (England) Regulations 2015 which require that the Council must each financial year conduct a review of the effectiveness of the system of internal control and prepare an AGS for approval by a committee or members of the authority. The AGS must be approved in advance of the relevant authority approving the statement of accounts.
<u>Other Legal Implications:</u>	

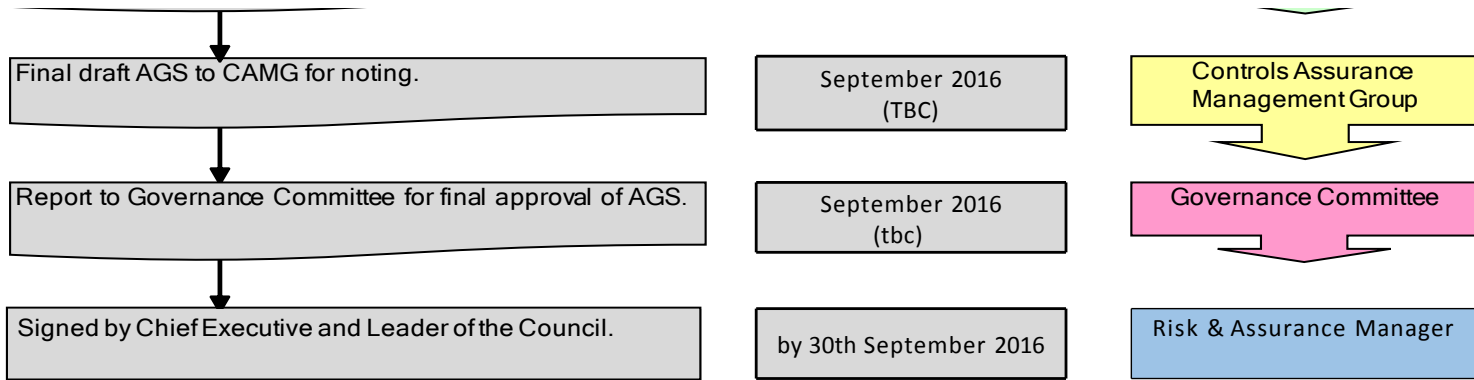
13.	None
POLICY FRAMEWORK IMPLICATIONS	
14.	None
KEY DECISION?	No
WARDS/COMMUNITIES AFFECTED:	N/A
<u>SUPPORTING DOCUMENTATION</u>	
Appendices	
1.	AGS 2015-16 : Process and timelines
2.	Annual Governance Statement 2014-15 Action Plan - Status Report
Documents In Members' Rooms	
1.	N/A
Equality Impact Assessment	
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
Privacy Impact Assessment	
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.	No
Other Background Documents	
Equality Impact Assessment and Other Background documents available for inspection at:	
Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	None.

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Annual Governance Statement 2015/16 - Process and timelines

Action	Meeting / Target Date	Responsibility
Report to Governance Committee to outline the assurance gathering process to support development of the 2015-16 AGS.	8th Feb 2016	Governance Committee
Review and update the 'AGS - Self Assessment Statement' document to ensure that it remains aligned with good	9th - 19th February 2016	Risk & Assurance Manager
Review of the Code of Corporate Governance against current CIPFA/SOLACE guidance.	1st - 18th March 2016	Risk & Assurance Manager
Issue 'AGS Self Assessment Statements' to Service Directors for completion	1st April 2016	Risk & Assurance Manager
Return of completed 'AGS Self Assessment Statements' and completion of Assurance Framework document.	25th April 2016	Council Management Team
Validation of self assessments by Internal Audit.	26th April - 13th May 2016	Chief Internal Auditor
Draft AGS developed in consultation with Controls Assurance Management Group . NOTE: further ad hoc meetings may be required and will be arranged as necessary.	16th May 2016	Controls Assurance Management Group
Report to CMT to review the draft 2015-16 AGS.	24th May 2016 (Provisional)	Council Management Team
Report to Governance Committee to review draft 15-16 AGS	June 2016 (tbc)	Governance Committee
Submission of final draft of AGS to Council Management Team.	August 2016 (TBC)	Council Management Team

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ANNUAL GOVERNANCE STATEMENT 2014-15: Status Report

The following is a summary of the status of the agreed actions that were identified to address the significant governance issues were identified and recorded on the Council's Annual Governance Statement 2014-15:

	Governance Issue	Agreed Action	Target Date	Responsible Officer	Status	Comments
1.	The published Corporate Procurement Strategy refers to the period 2009-12	The slippage is mainly due to the implementation of the 2015 Public Contract Regulations in February 2015 and the time it has taken to understand the new regulations, whilst also briefing the organisation what it needs to do to comply with the new regulations. As a result CPR's need to be completely revised to take account of both the new regulations and the fact that Capita Procurement now manage all of the councils' procurements. In addition, we are reviewing contract management and procurement as part of our operating model work with PwC.	Dec 15 (Review status March 16)	Chief Financial Officer	IN PROGRESS	Work has been ongoing with PwC as part of the overall Transformation programme to review procurement spend, and in addition dialogue has been taking place with Capita concerning the delivery of the overall procurement strategy and savings programme for 2015/16 onwards. As these two pieces of work are a critical forerunner to a revision of the overall procurement strategy, these have taken precedence. As this work is completed, the Procurement Strategy will be refreshed to take the outcomes into account.
2.	Business continuity plans need to be reviewed and updated to reflect the high level of organisational change that has taken place and is ongoing.	A new Business Continuity Policy and associated templates have been drafted and are to be presented to the Council's Management Team in June 15 for approval. The new Business Continuity Plan template will then rolled out across the service areas (Dec 15).	Dec 15	Director of Place	COMPLETED Dec 15	A new Corporate Business Continuity Plan and 12 Service Business Continuity Plans are now in place. Review of these plans will take place following implementation of the new operating model.

3.	<p>Information Governance arrangements need to be reviewed and aligned with new organisational structures and operational arrangements.</p>	<p>(i) Review and implement appropriate arrangements to provide adequate organisational resources in each Directorate to enable compliance and oversight of information governance, to include monitoring and reviewing compliance, report breaches, ensuring action plans are implemented.</p> <p>(ii) To compile and submit the annual Information Governance NHS Toolkit to ensure data sharing can continue.</p>	<p>Sept 15 (Revised date Mar 15)</p> <p>July 15</p>	<p>(i) Head of Legal & Democratic Services</p> <p>(ii) Director of People</p>	<p>IN PROGRESS</p> <p>COMPLETED July 15</p>	<p>The Senior Risk Information Officer role is now picked up within the Directorates at Business Support level however these individuals do not attend the Information Governance Board nor are they part of policy development in this area. The HLDS has reviewed the position, recognising the need for a more strategic and senior oversight to ensure there is a risk and compliance role/function that ensures the organisation is able to comply with the relevant statutory frameworks. Proposals have been submitted to CMT and are being considered.</p>
4.	<p>The level of employee understanding and awareness in respect of their responsibilities for the management of information is potentially inconsistent.</p> <p>Not all staff have completed the mandatory Information Governance e-learning (including Data Protection, Freedom Of Information Act and Protecting Information). There are concerns regarding the accuracy and robustness of the training database that captures training which is being urgently investigated.</p>	<p>Completion of the mandatory training needs to be rigorously enforced with a sanction in the event of continued non-compliance.</p> <p>A revised database package consolidating the components is being investigated as is a different and more appropriate style of roll out to those colleagues who do not ordinarily access IT.</p>	<p>Sept 15</p>	<p>Head of Legal & Democratic Services</p>	<p>IN PROGRESS</p>	<p>The mandatory e-learning modules have been reduced down from four to two. In addition, 'You Tube' access has been made available for those who have no easy access to IT. This has increased compliance rates. A dedicated Leadership Group took place in October to focus on IG, breaches, best practice etc. End of Q3 has seen an improvement in compliance figures to a 53.7% completion and pass rate across the Council.</p>

5.	The skill and competencies of employees will need to be aligned with, and reflect, the organisational needs going forward.	<p>Development and delivery of a standard Corporate Induction Programme for new employees.</p> <p>Development of a management template identifying the standard required competencies and skills required. To incorporate ongoing learning requirements in respect of awareness of key policies and processes.</p> <p>Assessment of chief officer graded employees and leadership development plans put in place</p>	Dec 15	Head of Strategic HR	<p>COMPLETED Oct 15</p> <p>COMPLETED Dec 15</p> <p>COMPLETED Dec 15</p>	<p>New Induction Checklist and associated manager's guide approved and published on intranet</p> <p>Performance will form a key part of the job description and person specifications for the new posts.</p> <p>The assessment, in respect of the Strategic and Operations components (top structure Phase 1) was completed in December 15 and implemented from 1st February 2016. Development plans and framework contracts are being put into place and will finalise the Phase 1 structure.</p>
6.	Some of the documents, policies and strategies referred to in the published Code of Corporate Governance have since been updated.	Review and update document to ensure that it refers to current documents, policies and strategies	May 15	Head of Legal & Democratic Services	COMPLETED	Review of the Code of Corporate Governance is an ongoing process.

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Agenda Item 7

DECISION-MAKER:	GOVERNANCE COMMITTEE		
SUBJECT:	EXTERNAL AUDIT – PROGRESS REPORT – JANUARY 2016		
DATE OF DECISION:	8 FEBRUARY 2016		
REPORT OF:	CHIEF FINANCIAL OFFICER		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Neil Pitman	Tel: 0162 845139
	E-mail:	Neil.pitman@southampton.gov.uk	
Director	Name:	Andrew Lowe	Tel: 023 8083 2049
	E-mail:	Andrew.lowe@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY	
NOT APPLICABLE	
BRIEF SUMMARY	
<p>The purpose of this report is to provide the Governance Committee with an overview of the final position against the Council's 2014/15 audit plan, and the external auditors initial plans for the 2015/16 audit.</p> <p>The Sector Briefing is designed to summarise some of the current issues facing the Local Government sector and is for information only.</p>	
RECOMMENDATIONS:	
	(i) To note the Progress Report – January 2016
REASONS FOR REPORT RECOMMENDATIONS	
1.	The Progress Report is a key mechanism in ensuring that the external audit is aligned with the Governance Committee's service expectations.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	No alternative options considered
DETAIL (Including consultation carried out)	
3.	The progress report has been discussed and agreed with senior officers within the Council.
RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
4.	None.
<u>Property/Other</u>	
5.	None.

LEGAL IMPLICATIONS	
Statutory power to undertake proposals in the report:	
6.	External audit is undertaken in accordance with the requirements of the Local Audit & Accountability Act 2014 the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments Ltd, auditing standards and other professional requirements.
Other Legal Implications:	
7.	None.
POLICY FRAMEWORK IMPLICATIONS	
8.	None.

KEY DECISION?	No
WARDS/COMMUNITIES AFFECTED:	N/A
<u>SUPPORTING DOCUMENTATION</u>	
Appendices	
1.	Progress Report – January 2016
2.	Local government audit committee briefing
Documents in Members' Rooms	
1.	None
Equality Impact Assessment	
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
Privacy Impact Assessment	
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.	No
Other Background Documents	
Equality Impact Assessment and Other Background documents available for inspection at:	
Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	None

Southampton City Council

Governance Committee Progress Report

February 2016



Governance Committee
Southampton City Council
Civic Road
Southampton
SO14 7LY

8 February 2016

Dear Committee Members

Audit Progress Report

We are pleased to attach our Audit Progress Report.

The purpose of this report is to provide the Committee with an overview of the final position against the Council's 2014/15 audit plan, and our initial plans for the 2015/16 audit. This report is a key mechanism in ensuring that our audit is aligned with the Committee's service expectations.

Our audit is undertaken in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements.

We welcome the opportunity to discuss this report with you as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Helen Thompson
Executive Director
For and behalf of Ernst & Young LLP

Contents

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2015/16 audit	3
Timetable	5

In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued ‘Statement of responsibilities of auditors and audited bodies 2015-16’. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk)

The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The ‘Terms of Appointment from 1 April 2015’ issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This progress update is prepared in the context of the Statement of responsibilities. It is addressed to the Governance Committee, and is prepared for the sole use of the audited body. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute..

2014/15 audit

We are presenting our annual report on the certification of claims and returns to the Committee today. This completes our work in relation to the 2014/15 financial year.

2015/16 audit

Financial Statements

We adopt a risk based approach to the audit and as part of our ongoing continuous planning we have held a number of meetings with key officers and other stakeholders:

- January 2016 – our monthly meeting with the Chief Finance Officer and the Deputy Chief Finance Officer to update our understanding of the challenges and risks you are facing. This forms a key part of our continuous audit planning;
- January 2016 – attendance at the Monthly Audit Operational Meeting to discuss audit timings and emerging audit issues; and
- We have continued to liaise with Internal Audit to ensure we can place reliance on their work where possible.

Our work to identify the material income and expenditure systems was completed in January 2016. The testing of the controls and critical path of each material system is planned for February and March 2016. We will communicate the results of this work to you in our Audit Plan which will be presented to the Governance Committee in April 2016.

We will continue to use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular payroll, cash payments and receipts and journal entries.

Value for money

Our initial risk assessment is ongoing and we will report the risks we have identified and associated work we will carry out to the April 2016 Governance Committee.

Accelerating your financial close arrangements

On 17 February 2015, the Accounts and Audit Regulations 2015 were laid before Parliament, having been made (signed by the Minister) under the Local Audit and Accountability Act 2014 on 12 February 2015.

A key area of the regulations is that from the 2017/18 financial year, the timetable for the preparation and approval of accounts will be brought forward to a draft accounts deadline of 31 May and an audit deadline of 31 July. These changes provide challenges for both the preparers and the auditors of the financial statements.

The good news is that with good planning, communication and joint working, those deadlines are highly attainable. The majority of Councils are on the right trajectory having met the current reporting deadlines consistently for the last few years, the challenge now is upping the speed of that trajectory to achieve the faster deadlines. Below we have included some suggestions which will help achieve this new statutory deadline. We will continue to engage with officers to ensure that the Council is well placed to meet these new statutory deadlines.

As with any project, the key to success is in the planning, together with timely engagement and collaboration between the preparers of the financial statements and the auditors of those statements. We appreciate that each client starts from a slightly different base position. Therefore, there is no one size fits all solution. However, there are areas where we can continue to work with your officers :

- revisit the current project timetable;
- an early in-year financial hard close;
- review the format of your accounts;
- review your approach to estimates;
- review your year-end journal process;

- review the operation of your ledger system; and
- consider how fit for purpose is your current financial reporting system?

We attend monthly Operational Delivery Group meetings with the finance team and use this as a mechanism to discuss options for early close and early substantive testing. We will continue to provide the Committee with regular updates on our progress in this area.

Other issues of interest

In addition to our formal reporting and deliverables we provide practical business insights and updates on regulatory matters through our Sector Briefings. We attach the latest briefing to this progress report.

Timetable

We set out below a timetable showing the key stages of the audit, including the value for money work, and the deliverables we will provide to you through the 2015/16 Governance Committee cycle.

Audit phase	EY Timetable	Deliverable	Reported	Status
High level planning	Ongoing	Audit Fee Letter	Issued 24 April 2015	Completed
Risk assessment and setting of scope of audit	Dec 2015 - January 2016	Audit Plan	April 2016	In progress
Testing of routine processes and controls	Feb-March 2016	Audit Plan/Progress Report	April 2016	In progress
Year-end audit	August- September 2016	<p>Audit results report to those charged with governance</p> <p>Audit report (including our opinion on the financial statements and a conclusion on your arrangements for securing economy, efficiency and effectiveness in your use of resources)</p> <p>Whole of Government Accounts Submission to NAO based on their group audit instructions</p> <p>Audit Completion certificate</p>	August 2016	Work is planned to start during June 2016.

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ey.com

Local government audit committee briefing

Contents at a glance

Government and economic news

Accounting, auditing and governance

Regulation news

Key questions for the audit committee

Find out more

This sector briefing is one of the ways that we hope to continue to support you and your organisation in an environment that is constantly changing and evolving.

It covers issues which may have an impact on your organisation, the Local government sector and the audits that we undertake.

The public sector audit specialists who transferred from the Audit Commission form part of EY's national Government and Public Sector (GPS) team. Their extensive public sector knowledge is now supported by the rich resource of wider expertise across EY's UK and international

business. This briefing reflects this, bringing together not only technical issues relevant to the local government sector but wider matters of potential interest to you and your organisation.

Links to where you can find out more on any of the articles featured can be found at the end of the briefing, as well as some examples of areas where EY can provide support to Local Authority bodies.

We hope that you find the briefing informative and should this raise any issues that you would like to discuss further please do contact your local audit team.



Government and economic news

EY Item Club Autumn Forecast

The latest EY Item Club forecast (Autumn 2015) predicts tougher times for the UK economy as what it describes as the 'consumer sugar rush' begins to fade.

GDP is forecast to grow by 2.5% this year (compared to 2.9% in 2014) and slow further to 2.4% in 2016 and 2.3% the year after. Consumer Price Inflation is expected to remain below target until 2018. Prospects for exports remain poor, and domestic consumption is likely to be affected by rising inflation and tighter fiscal policy from early 2016. Progress is seen to depend upon productivity gains rather than coming from the commodity price falls that are supporting demand this year. Businesses will need to work hard on overseas markets as opposed to relying on consumer-led domestic markets.

The forecast highlights that the last decade has seen a strong increase in the supply of labour which has depressed real wages and, arguably, productivity, but that we are now seeing a more normal recovery. This is characterised by an increase in the demand for labour, which boosts real wages and productivity. Wage inflation is highlighted as being strong. This is expected to be boosted further in April 2016 by the National Living Wage, the effects of which could be very significant for some sectors and regions.

Provided that increased productivity matches wage inflation, the expectation is that the Monetary Policy Committee will keep base rates on hold until next autumn.

For details of the EY Item Club's latest forecast, see <http://www.ey.com/UK/en/Issues/Business-environment/Financial-markets-and-economy/ITEM---Forecast-headlines-and-projections>

Housing Associations Right to Buy

The Chartered Institute of Public Financial Accountants (CIPFA) has produced a briefing following the Government's announcement in October that it intends to extend its Right to Buy scheme to Housing Associations. The briefing seeks to explore the potential impact of these plans on Local Authorities.

Local authority housing is intended to be self-financing, based on 30 year business plans established in 2012 with the HRA self-financing regime, with Council housing for each council financed from its own rental income. This principle was reflected in the 30 year business plans, but CIPFA suggests that these business plans do not reflect recent changes contained within the budget. These changes include amendments to the rent policies as well as the proposed sale of high value local authority housing stock in order to compensate housing associations for the shortfall in income caused by the new Right to Buy scheme.

According to CIPFA, research has shown properties sold under the existing Right to Buy scheme have in many instances returned to the rental market at a higher level of rent than council levels. They have cited the example of Barking and Dagenham where it is said that 41% of properties purchased under the Right to Buy scheme are now let privately.

CIPFA warns 'Any legislation that leads to a negative impact on the housing business plan models of local authorities could seriously undermine the very basis of self-financing which promised autonomy for local authorities in the delivery of housing in their areas.'



Government and economic news

However, Communities Secretary Greg Clark said:

“We’re determined to ensure that home ownership is seen as a reasonable aspiration for working people.

Right to Buy is a key part of this, offering a helping hand to millions of people who would have no hope of buying their own home without it.

Today’s historic agreement with housing associations and the National Housing Federation will extend that offer even more widely, whilst at the same time delivering thousands of new affordable homes across the country.”

The Government agreement with housing associations and the National Housing Federation will see housing association tenants able to buy their homes from 2016.

CIPFA’s briefing document can be downloaded from <http://www.cipfa.org/cipfa-thinks/briefings>, and further information from the government is available at <https://www.gov.uk/government/news/historic-agreement-will-extend-right-to-buy-to-13-million-more-tenants>

Consultation: improving efficiency on Council Tax Collection

Council tax collection rates have been relatively high in recent years: 97% across England in both 2014/15 and 2013/14. However, the Government is looking at ways to enable local authorities to further improve collection rates.

To this end, the Government has issued a consultation on its proposals to improve the collection and enforcement process for council tax. The government’s stated intention is to help local authorities to keep council tax rates low, and so the proposals are aimed at ensuring that everyone contributes fairly.

The consultation follows a trial by Manchester City Council, Salford City Council, HMRC and the Cabinet office under the ‘Better Business Compliance Cabinet programme’, and reflects consideration of the findings from this trial.

An example of this is the Government’s proposal to extend the data-sharing gateway which currently exists between HMRC and local authorities. This would enable HMRC to share employment information with councils where council tax debtors have not voluntarily shared the information within 14 days of receiving a liability order. Manchester estimates, based on its pilot with HMRC, that this would recover £2.5mn of debt in its area alone.

The consultation also asks for other suggestions to improve council tax collection.

Responses are requested by 18 November 2015.

For more information on the consultation and details on how to respond, please see https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/466386/150930_Improving_Efficiency_of_Council_Tax_collection_Consultation_Doc.pdf



Government and economic news

Local Plans for New Homes

In October, the Government announced that councils will be required to produce local plans for new homes by 2017. Where councils fail to do so, the Government will consult with local people to ensure that plans are produced for them.

In 2012, the National Planning Policy Framework was introduced to provide guidance for local planning authorities and decision-takers, both in drawing up plans and making decisions about planning applications. This framework reinforced the role of local plans. It required the plans to include an annual trajectory over a period of around 15 years of how many homes they plan to build in their area, and it required local authorities to review this plan approximately every 5 years. Councils were also encouraged to give local people more say on where new developments would be located and what they would look like.

The Government have said that the response to this has been mixed:

- ▶ 82% of councils have published local plans which state how many homes they intend to build over a given period
- ▶ 65% have fully adopted these plans
- ▶ Nearly 20% of councils do not have an up to date plan

If councils fail to produce and bring into force an up to date plan for new homes by 2017, the Government intends to work with local people to ensure one is created.

Read the government press release at <https://www.gov.uk/government/news/prime-minister-councils-must-deliver-local-plans-for-new-homes-by-2017>



Accounting, auditing and governance

Proposals for further emergency services collaboration announced

The Government has launched a consultation which is looking into how the three core emergency services of Police, Fire and Rescue and the Ambulance service could potentially work together in a more efficient and effective manner. Key features of the consultation include:

- ▶ Enabling Police and Crime Commissioners (PCCs) to take on the duties and responsibilities of Fire and Rescue Authorities where a local case was made for this to happen
- ▶ Where a case is made by a local PCC to take on such a role, there would also be the possibility for them to take on the role of a single employer and in doing so enable the sharing of back office support functions
- ▶ Improving joint working between PCCs and local NHS Ambulance Foundation Trusts by encouraging them to allow PCCs to sit on their Council of Governors

The Government also intends to introduce a new statutory duty for the three emergency services to collaborate with one another; and sees this as not being a burden, but is about seeking efficiencies.

However, a key legal distinction would remain under the new proposals, in that a member of a police force will not be permitted under law to become a firefighter, and firefighters will not be given the power of arrest. In order to maintain transparency for local taxpayers, funding from central government will remain separate for police and fire organisations, as will council tax precepts.

<https://www.gov.uk/government/news/proposals-for-further-emergency-services-collaboration-announced>

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/459986/Consultation_-_Enabling_closer_working_between_the_Emergency_Services__w__2_.pdf

Finance in the Cloud?

Cloud computing allows users to rent access to a variety of virtual computing options, conveniently, ranging from network-accessible data storage and software development environments to fully featured applications. As such, the data and applications are not required to be stored on local servers or 'on-premise'; rather, they are hosted and managed by third-party cloud service providers (CSPs).

Enterprises essentially outsource varying levels of IT functionality to CSPs, and users only need an internet connection to access the data and applications via virtual servers. By moving into the cloud, organisations have the potential to reduce greatly, or even eliminate, the total cost of ownership (TCO) of the IT function, thereby forever altering their business model.

The benefits of cloud adoption are highly touted. However, over a decade ago, on-premise enterprise resource planning (ERP) solutions made similar promises. Although the trigger for rushed ERP implementations in the 1990s was the much-fretted Year 2000 (or Y2K) calamity, Y2K concerns turned out to be largely unfounded, and many finance executives would now argue that they have yet to reap genuine, tangible benefits from investing in costly ERP systems.



Accounting, auditing and governance

Although a company's financial management system is critical to success, EY is finding that many organisations have systems averaging from 10 to 15 years old, with upgrade cycles ranging from 5 to 10 years. Despite aging legacy systems, many finance decision-makers are hazy on how cloud solutions are really any different from the ERP solutions hyped in the previous decade.

Organisations that truly understand cloud technology, as well as the associated challenges and risks, are better placed to manage the impact of cloud computing on the finance function. Moreover, they must engage an agile innovation strategy focused on deploying the right operating model in order to realize fully the benefits of cloud computing.

In EY's experience, organisations that fail to make a robust cloud risk assessment often need to make subsequent, costly changes to the cloud model, thereby negating any savings gained from cloud migration. EY recommends that organisations develop a clear, attainable cloud strategy, including an appropriate operating model accompanied with a cloud risk management approach to mitigate risks and avoid a premature move to the cloud.

EY has a proven framework for cloud models, along with risk assessments and broad-based diagnostics to evaluate and optimise a cloud strategy that enables minimal disruption whilst accelerating an organisation's evolution. For more information on this, please talk to a member of your engagement team or read the EY publication at http://performance.ey.com/wp-content/uploads/downloads/2015/10/EY-Performance-Finance-in-the-cloud_Final.pdf

Value for Money Conclusion guidance

The NAO have recently released a consultation document (<http://www.nao.org.uk/keep-in-touch/wp-content/uploads/sites/11/2015/08/Vfm-arrangements-auditor-guidance-consultation-document.pdf>) a consultation document for auditors on their review of arrangements to secure economy, efficiency and effectiveness in their use of resources. This is also referred to as the three E's or the Value for Money (VfM) conclusion. The guidance covers the VfM work for 2015/16.

Based on the responses received to a similar consultation in 2014 the new draft guidance seeks to:

- ▶ Take forward existing guidance and reflect changing circumstance for public sector organisations such as finding savings and maintain financial stability over the medium and long term
- ▶ Update the definition of 'proper arrangements'
- ▶ Strengthen guidance on the identification and work around significant risks whilst maintaining a risk based approach
- ▶ Update and clarify the range of reporting opinions available to auditors and expectations at key stages of the audit
- ▶ Maintain sector specific guidance that will sit outside of the statutory guidance but can provide up-to-date information on sector specific risks

The consultation closed on 30 September and the NAO will communicate a summary of the responses once they have reviewed them. Further information can be found at <https://www.nao.org.uk/keep-in-touch/our-surveys/consultation-auditors-work-on-value-for-money-arrangements/>.



Regulation news

Consultation on 2016/17 proposed fee scales

Public Sector Audit Appointments (PSAA) is currently consulting on both the work programme and scale of fees for 2016/17 audits. The consultation describes the work that auditors will undertake at principal audited bodies for 2016/17 and their associated scales of fees.

There are no planned changes to the overall work programme for 2016/17 and their proposal is to set scale audit fees at the same level as the scale fees for 2015/16 which already reflect a reduction of 25% in addition to the reduction of up to 40% made from 2012/13.

A change in accounting requirements in 2016/17 relating to highways infrastructure assets will require additional audit work at some authorities. As the amount will differ between authorities, the fee variation process will apply in 2016/17 for this additional work.

The consultation closes on Friday 15th January 2016, and the final work programme will be published following this in March 2016.

For details of the consultation, please refer to the PSAA website at <http://www.psaa.co.uk/audit-and-certification-fees/consultation-on-201617-proposed-fee-scales/>

NAO Case Study: Managing reductions in local authority government funding

The National Audit Office (NAO) has made available more than 30 case studies which give examples of how organisations have used their recommendations or analysis to support the achievement of financial savings.

One of these case studies follows the production of its 2014 report 'Financial Sustainability of Local Services'

The NAO case study states that following their report, the Department for Communities and Local Government (DCLG) has acknowledged that its processes for estimating local authority spending requirements and assessment the potential impacts of spending reductions need to be improved.

They also note use of their report in the sector, citing the following examples:

- ▶ Leeds City Council and Birmingham City Council have drawn on the work in their debates with central government over devolution
- ▶ Wolverhampton City Council and Oldham Council have used the work to inform discussion and decision-making in cabinet meetings and audit and scrutiny meetings
- ▶ The Local Government Association and treasurers' societies have used the analysis from the report to inform their thinking

Find out more about the impact made by NAO reports in their interactive pdf at <https://www.nao.org.uk/wp-content/uploads/2015/10/Impacts-case-studies-2014.pdf>



Key questions for the audit committee

What questions should the Audit Committee ask itself?

Have we considered the impact of the extension of Right to Buy and reflected our consideration in our Medium Term financial plans and/or Local Plan?

How successful are we in systematically improving our collection rates for Council Tax? Is there best practice that we could share via the Government's consultation?

What is our mid to long term IT strategy? Are we considering cloud-based IT and if so how robust are our risk assessments supporting the shift?

Have we formulated a response to the PSAA consultation on the work programme and scale of fees for 2016/17?



Find out more

EY Item Club Autumn Forecast

For details of the EY Item Club's latest forecast, see <http://www.ey.com/UK/en/Issues/Business-environment/Financial-markets-and-economy/ITEM---Forecast-headlines-and-projections>

Housing Associations Right to Buy

For further information, please see the government press release at <https://www.gov.uk/government/news/historic-agreement-will-extend-right-to-buy-to-13-million-more-tenants> and access the CIPFA report at <http://www.cipfa.org/cipfa-thinks/briefings>

Consultation: Improving Efficiency on Council Tax Collection

For more information on the consultation and details on how to respond, please see https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/466386/150930_Improving_Efficiency_of_Council_Tax_collection_Consultation_Doc.pdf

Local Plans for New Homes

Read the government press release at <https://www.gov.uk/government/news/prime-minister-councils-must-deliver-local-plans-for-new-homes-by-2017>

Proposals for further emergency services collaboration announced

For more information on the Government's proposals, please see <https://www.gov.uk/government/news/proposals-for-further-emergency-services-collaboration-announced>, and for a copy of the consultation document please see https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/459986/Consultation_-_Enabling_closer_working_between_the_Emergency_Services__w__2_.pdf

Finance in the Cloud?

To find out more about Cloud Computing and how EY can support you, please ask a member of your engagement team or read the EY publication at http://performance.ey.com/wp-content/uploads/downloads/2015/10/EY-Performance-Finance-in-the-cloud_Final.pdf

Value for Money Conclusion guidance

Further information can be found at <https://www.nao.org.uk/keep-in-touch/our-surveys/consultation-auditors-work-on-value-for-money-arrangements/>, and a copy of the NAO's consultation document is available at <http://www.nao.org.uk/keep-in-touch/wp-content/uploads/sites/11/2015/08/Vfm-arrangements-auditor-guidance-consultation-document.pdf>

Consultation on 2016/17 proposed fee scales

For further details on the consultation and how to respond to it, please visit:

<http://www.psaa.co.uk/audit-and-certification-fees/consultation-on-201617-proposed-fee-scales/>

NAO Case Study: Managing reductions in local authority government funding

Find out more about the impact made by NAO reports in their interactive pdf at <https://www.nao.org.uk/wp-content/uploads/2015/10/Impacts-case-studies-2014.pdf>

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ED None

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Agenda Item 8

DECISION-MAKER:	GOVERNANCE COMMITTEE		
SUBJECT:	CERTIFICATION of CLAIMS and RETURNS ANNUAL REPORT 2014-15		
DATE OF DECISION:	8 FEBRUARY 2016		
REPORT OF:	CHIEF INTERNAL AUDITOR		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Neil Pitman	Tel: 01962 845139
	E-mail:	Neil.pitman@southampton.gov.uk	
Director	Name:	Andrew Lowe	Tel: 023 803 2049
	E-mail:	Andrew.lowe@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY	
NOT APPLICABLE	
BRIEF SUMMARY	
<p>The purpose of this paper is to provide the Governance Committee with the outcomes of the external auditor's Certification of Claims and Returns – Annual Report 2014/15.</p> <p>Local authorities claim large sums of public money in grants and subsidies from central government and other grant-paying bodies and are required to complete returns providing financial information to government departments.</p> <p>Under section 28 of the Audit Commission Act 1998, as transitionally saved, the Audit Commission made arrangements for certifying claims and returns in respect of the 2014-15 financial year. These arrangements required only the certification of the housing benefits subsidy claim. In certifying this the external auditors followed a methodology determined by the Department for Work and Pensions and did not undertake an audit of the claim.</p>	
RECOMMENDATIONS:	
	(i) to note the External Auditor's annual report on the Certification of Claims and Returns 2014/15 as attached (Appendix 1).
REASONS FOR REPORT RECOMMENDATIONS	
1.	The Governance Committee's Terms of Reference require it to be satisfied and provide assurance that appropriate action is being taken on risk and internal control related issues identified by the external auditors. Specifically the Committee has responsibility for oversight of the reports of external audit.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
	None
DETAIL (Including consultation carried out)	
	The following external audit report is attached for consideration in Appendix 1: Certification of Claims and Returns – Annual Report 2014/15 The external auditor will be in attendance at the Committee meeting to answer any questions. The report, as attached at Appendix 1, has been discussed and agreed with appropriate officers.

RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
	None
<u>Property/Other</u>	
	None
LEGAL IMPLICATIONS	
<u>Statutory power to undertake proposals in the report:</u>	
	section 28 of the Audit Commission Act 1998
	Account & Audit Regulation (England) 2015
<u>Other Legal Implications:</u>	
	None
POLICY FRAMEWORK IMPLICATIONS	
	None

KEY DECISION?	No
WARDS/COMMUNITIES AFFECTED:	
<u>SUPPORTING DOCUMENTATION</u>	
Appendices	
1.	Certification of claims and returns annual report 2014-15
Documents In Members' Rooms	
1.	None
Equality Impact Assessment	
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
Privacy Impact Assessment	
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.	No
Other Background Documents	
Equality Impact Assessment and Other Background documents available for inspection at:	
Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	None

Certification of claims and returns annual report 2014-15

Southampton City Council

December 2015

Ernst & Young LLP



Building a better
working world

The Members of the Governance Committee
Southampton City Council
Civic Centre
Southampton
SO14 7LY

December 2015
Ref: SCC/Claims/2014-15

Direct line: 023 8038 2099
Email: HThompson2@uk.ey.com

Dear Members

Certification of claims and returns annual report 2014-15 Southampton City Council

We are pleased to report on our certification work. This report summarises the results of our work on Southampton City Council's 2014-15 claims.

Scope of work

Local authorities claim large sums of public money in grants and subsidies from central government and other grant-paying bodies and must complete returns providing financial information to government departments. In some cases these grant-paying bodies and government departments require appropriately qualified auditors to certify the claims and returns submitted to them.

Under section 28 of the Audit Commission Act 1998, as transitionally saved, the Audit Commission made arrangements for certifying claims and returns in respect of the 2014-15 financial year. These arrangements required only the certification of the housing benefits subsidy claim. In certifying this we followed a methodology determined by the Department for Work and Pensions and did not undertake an audit of the claim.

Statement of responsibilities

The Audit Commission's 'Statement of responsibilities of grant-paying bodies, authorities, the Audit Commission and appointed auditors in relation to claims and returns' (statement of responsibilities) applied to this work. It serves as the formal terms of engagement between ourselves as your appointed auditor and the Council as audited body.

This report is prepared in the context of the statement of responsibilities. It is addressed to those charged with governance and is prepared for the sole use of the Council. As appointed auditor we take no responsibility to any third party.

Summary

Section one of this report outlines the results of our 2014-15 certification work and highlights any significant issues.

We checked and certified the housing benefits subsidy claim with a total value of £116.7m. We met the submission deadline. We issued a qualification letter: details of the issues giving rise to the qualification are included in section one.



Fees for certification work are summarised in section three. The fees for 2014-15 were published by the Audit Commission on 27 March 2014 and are now available on the Public Sector Audit Appointments Ltd (PSAA's) website (www.psaa.co.uk).

We welcome the opportunity to discuss the contents of this report with you at the Governance Committee on 8 February 2016.

Yours faithfully

Helen Thompson
Director
For and on behalf of Ernst & Young LLP
Enc.

Contents

1. Housing benefits subsidy claim.....	1
2. 2014-15 certification fees.....	2
3. Looking forward.....	3

1. Housing benefits subsidy claim

Scope of work	Results
Value of claim presented for certification	£116,730,117
Amended/Not amended	Not amended
Qualification letter	Yes
Fee – 2014-15	£25,340
Fee – 2013-14	£26,032

Local government administers the Government's housing benefits scheme for tenants and can claim subsidies from the Department for Work and Pensions (DWP) towards the cost of benefits paid.

The certification guidance requires auditors to complete more extensive '40+' or extended testing if initial testing identifies errors in the calculation of benefit or compilation of the claim. 40+ testing may also be carried out as a result of errors that have been identified in the audit of the previous year's claim. We found an error in our initial testing and carried out extended testing in one area, the classification of overpayments.

We reported the extrapolated value of this error in a qualification letter. The DWP then decides whether to ask the Council to carry out further work to quantify the error or to claw back the benefit subsidy paid. The issue we reported was:

- From an initial sample of 20 rent allowance cases we identified one error (total value £36) whereby an overpayment had been misclassified as claimant error when it should have been classified as local authority or administrative delay error. Testing of a further 40 cases identified no further errors of this type. The extrapolated error of misclassified overpayments in our qualification letter was £3,361.

As well as testing the calculation of individual benefits awards, the certification instructions require us to perform further tests including reviewing the reconciliation of benefit awarded to benefit paid during the year. Our testing found there were only minor unreconciled amounts, totalling £48. As there is no concept of materiality for the certification work, we were required to report this to the DWP through the qualification letter, which is similar to previous years.

2. 2014-15 certification fees

The Audit Commission determined a scale fee each year for the audit of claims and returns. For 2014-15, these scale fees were published by the Audit Commission on 27 March 2014 and are now available on the PSAA's website (www.psa.co.uk).

Claim or return	2013-14	2014-15	2014-15
	Actual fee £	Indicative fee £	Actual fee £
Housing benefits subsidy claim	26,032	25,340	25,340
Pooling of Housing Capital receipts	1,600	0	0
Total	27,632	25,340	25,340

3. Looking forward

From 1 April 2015, the duty to make arrangements for the certification of relevant claims and returns and to prescribe scales of fees for this work was delegated to (PSAA) by the Secretary of State for Communities and Local Government.

The Council's indicative certification fee for 2015-16 is £19,524. This was prescribed by PSAA in April 2015, based on no changes to the work programme for 2015-16.

Details of individual indicative fees are available at the following web address:
<http://www.psaa.co.uk/audit-and-certification-fees/201516-work-programme-and-scales-of-fees/individual-indicative-certification-fees/>

We must seek the agreement of PSAA to any proposed variations to these indicative certification fees. If necessary, we would discuss this with the Chief Finance Officer before seeking any such variation.

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Agenda Item 9

DECISION-MAKER:	GOVERNANCE COMMITTEE AND COUNCIL		
SUBJECT:	REVISIONS TO THE CONSTITUTION – TRANSFORMATION PROJECTS		
DATE OF DECISION:	8 th FEBRUARY 2016 (GOVERNANCE COMMITTEE) 10 th FEBRUARY 2016 (COUNCIL)		
REPORT OF:	SERVICES DIRECTOR: LEGAL AND GOVERNANCE		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Richard Ivory	Tel: 023 8083 2794
	E-mail:	Richard.ivory@southampton.gov.uk	
Director	Name:	Dawn Baxendale	Tel: 023 8083 4428
	E-mail:	Dawn.baxendale@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY

None

BRIEF SUMMARY

The report details previously considered revisions to various elements of the Constitution as part of the Council's significant Transformation agenda in order to enable early decision making which will permit quicker project implementation and realisation of financial savings. The matter was considered last cycle and deferred. Revisions have now been made following informal discussions with members. All proposals over £500,000 will be treated as Key Decisions and considered by Cabinet. No matters will require consideration by Council once the overall budget proposal has initially been considered and agreed.

RECOMMENDATIONS:

GOVERNANCE COMMITTEE

	(i)	That Governance Committee considers the revisions to the Constitution as set out in this report and recommends to Council the following changes:
		<ul style="list-style-type: none"> Revise section 5 of the Officer Scheme of Delegation (Transformation Implementation Director) stating "<i>The Transformation Implementation Director, following consultation with the Transformation Improvement Board, Chief Finance Officer and Head of Legal and Democratic Services, shall be empowered to take all decisions or actions necessary to develop, implement and deliver transformation projects approved by the Transformation Board up to a value of £5,000,000 including but not limited to incurring expenditure, structural re-organisations, service reorganisations and entering into contracts and partnership arrangements to deliver services as required together with all ancillary matters necessary to give effect to or conducive to the delivery of such projects. All proposals which are estimated to exceed £500,000 shall be considered by Cabinet. The £5,000,000 ceiling requiring</i>

		reference to full Council is waived for such proposals.”
		<ul style="list-style-type: none"> Amend the Budget and Policy Framework Procedure Rules at page 6 (section 5(b) to add “(iii) The Transformation Implementation Director, following consultation with Transformation Improvement Board and Chief Finance Officer, shall be entitled to vire across budget heads where each individual virement does not exceeds £5,000,000 for the purpose of delivering any transformation project
		<ul style="list-style-type: none"> Amend Financial Procedure Rules with an additional row in the tables at A12, B37 and B42 (HRA matters) stating “any amount not exceeding £5,000,000 relating to a transformation project approved as above can be vired / approved by the Transformation Implementation Director following consultation with the Transformation Improvement Board (including virement of expenditure and income budgets and acceptance of external funding).
COUNCIL		
	(i)	That Council approves the revisions to the Constitution as set out above.
REASONS FOR REPORT RECOMMENDATIONS		
1.	As set out in the summary above, time is of the essence in delivering any corporate transformation projects to capture such significant financial savings as have been broadly or specifically identified in the budget proposal previously agreed. By increasing the scheme of delegation to officers after consultation with Transformation Improvement Board more timely implementation will be achieved. Proposals will, of course, still be treated as Key Decisions where appropriate and considered by Cabinet where over £500,000.	
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED		
2.	To leave the Constitution as it stands. This would add delay in implementing significant transformation projects in that matters may have to be referred to full Council for decision due to the value involved. That may well require special meetings on an ad hoc basis as projects and proposals develop. That builds in inherent delay and inconvenience to members.	
DETAIL (Including consultation carried out)		
3.	As Members will recall this matter was considered last cycle and deferred at Council for further consultation between the Transformation Implementation Director and members. That has taken place and therefore the item is re-tabled for further consideration. The Council’s Transformation agenda and projects gather pace agility is needed to ensure delivery in as quick a manner as appropriate. This does not circumvent publicity or transparency as any proposed decisions will be published and the role of Overview and Scrutiny Committee will remain intact. The proposed changes aid that by quicker delivery, nothing more.	
4.	To assist delivery, prior to and/or following each Transformation Improvement Board, a working group standing meeting of officers to include finance, legal, HR and policy / strategy will meet to review projects and	

	identify those where there may be political sensitivities and identify consultation requirements with staff, service users, wider public along with any EIA / PIA implications and requirements that must be addressed before formal decisions taken.
5.	Formal sign off of any projects approved by the Transformation Implementation Director under the proposed delegations will be recorded with reasons with a report to Transformation Improvement Board (TIB) as necessary. For more operational matters, as now, a report by email containing the same level of information to meet the legal requirement to evidence reasons for decision under the current law on officer decision making will be compiled. There will be no sign off, whatever value, without discussion with and the agreement of the Leader of the Council (who may not always be present at TIB).
RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
6.	None
<u>Property/Other</u>	
7.	None
LEGAL IMPLICATIONS	
<u>Statutory power to undertake proposals in the report:</u>	
8.	S.111 Local Government Act 1972, Local Government Act 2000
<u>Other Legal Implications:</u>	
9.	None
POLICY FRAMEWORK IMPLICATIONS	
10.	None. All decisions must be made with Council agreed policy and budget.

KEY DECISION?	No	
WARDS/COMMUNITIES AFFECTED:	None	
<u>SUPPORTING DOCUMENTATION</u>		
Appendices		
1.	None	
Documents In Members' Rooms		
1.	None	
Equality Impact Assessment		
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out?		No
Privacy Impact Assessment		
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out?		No
Other Background Documents		
Equality Impact Assessment and Other Background documents available for inspection at:		
Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)	
1.	None	