Public Document Pack

Governance Committee

Monday, 12th February, 2018 at 5.00 pm

PLEASE NOTE TIME OF MEETING

Committee Room 1 - Civic Centre

This meeting is open to the public

Members of the Committee

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

Contacts

Service Director, Legal and Governance Richard Ivory Tel. 023 8083 2394 Email: richard.ivory@southampton.gov.uk

Senior Democratic Support Officer Claire Heather Tel. 023 8083 2412 Email: claire.heather@southampton.gov.uk

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.

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

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

The Southampton City Council Strategy (2016-2020) is a key document and sets out the four key outcomes that make up our vision.

- Southampton has strong and sustainable economic growth
- Children and young people get a good start in life
- People in Southampton live safe, healthy, independent lives
- Southampton is an attractive modern City, where people are proud to live and work

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. By entering the meeting room you are consenting to being recorded and to the use of those images and recordings for broadcasting and or/training purposes. The meeting may be recorded by the press or members of the public.

Any person or organisation filming, recording or broadcasting any meeting of the Council is responsible for any claims or other liability resulting from them doing so.

Details of the Council's Guidance on the recording of meetings is available on the Council's website.

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 2017/18

2017	2018
12th June	12th February
24th July	23rd April
13th November	
11th 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

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.

Rules of Procedure

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

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

1 APOLOGIES

To receive any apologies.

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 <u>MINUTES OF PREVIOUS MEETING (INCLUDING MATTERS ARISING)</u> (Pages 1 - 4)

To approve and sign as a correct record the Minutes of the meeting held on 13th November 2017 and to deal with any matters arising, attached.

5 QUARTERLY HR STATISTICS (Pages 5 - 12)

Report of Service Director Human Resources and Organisational Development detailing Quarter 3 Human Resources Casework.

6 TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS 2018/19 TO 2021/22 (Pages 13 - 58)

Report of Service Director Finance and Commercialisation providing 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.

7 <u>CERTIFICATION OF CLAIMS AND RETURNS ANNUAL REPORT 2016/17</u> (Pages 59 - 70)

Report of External Auditor detailing the Certification of Claims and Returns Annual Report 2016/17.

8 LOCAL APPOINTMENT OF EXTERNAL AUDITORS (Pages 71 - 74)

Report of the Service Director Finance and Commercialisation providing an update regarding the arrangements for appointing External Auditors at conclusion of the 2017/18 audits

9 EXTERNAL AUDIT PLAN YEAR ENDING 31ST MARCH 2018 (Pages 75 - 112)

Report of External Auditor detailing the External Audit Plan for year ending 31st March 2018.

10 ANNUAL GOVERNANCE STATEMENT 2017-18 (Pages 113 - 118)

Report of the Chief Financial Officer seeking approval of the assurance gathering process to support development of the 2017-18 Annual Governance Statement, attached.

11 PROCUREMENT - SUB £100K SPEND (Pages 119 - 126)

Report of Service Director, Digital and Business Operations updating the Governance Committee on the actions set out in the report entitled "Procurement – Sub 100k spend" which was presented to Governance Committee on 24th July 2017.

12 EXCLUSION OF THE PRESS AND THE PUBLIC

Chair to move that in accordance with the Council's Constitution, specifically the Access to Information Procedure Rules contained within the Constitution, the press and public be excluded from the meeting in respect of the appendix to the following item based on Category 5 of paragraph 10.4 of the Access to Information Procedure Rules. Having applied the public interest test it is not appropriate to disclose this information.

13 INTERNAL AUDIT PROGRESS REPORT 2017-18 (Pages 127 - 156)

Report of the Chief Internal Auditor providing an update on the progress made against the Audit Plan and highlighting any areas of concern.

Friday, 2 February 2018

Service Director, Legal and Governance

Agenda Item 4

GOVERNANCE COMMITTEE MINUTES OF THE MEETING HELD ON 13 NOVEMBER 2017

<u>Present:</u> Councillors Barnes-Andrews (Chair), Keogh (Vice-Chair), Inglis, Jordan,

Noon and O'Neill

<u>Apologies:</u> Councillors Parnell

23. MINUTES OF PREVIOUS MEETINGS (INCLUDING MATTERS ARISING)

RESOLVED: that the minutes of the following meetings be approved and signed as a correct record:-

(i) Governance Committee – 24th July 2017;

- (ii) Employment and Appeal Panel 21st June and 12th July 2017; and
- (iii) Joint Employment Panel for the Appointment of a Joint Director of Public Health with Portsmouth City Council 31st October 2016

24. SOUTHAMPTON CITY COUNCIL COMPLAINTS ANNUAL REVIEW 2016/17

The Committee received and noted the report of the Service Director; Legal and Governance detailing the Southampton City Council Complaints Review 2016/2017. The report summarised the type and number of complaints received from 1st April 2016 and 31st March 2017 together with the Local Government Ombudsman Annual Review for the same period. The Committee noted that overall complaints registered with the Council had decreased by 12%, Corporate complaints had decreased by 12%, Adult Services complaints had decreased by 23% and Children and Families complaints had decreased by 40%.

25. QUARTERLY HUMAN RESOURCES STATISTICS

The Committee received and noted the report of the Service Director; Human Resources and Organisational Development providing the quarterly summary of Council wide information on key employment data covering disciplinaries, dismissals, referrals to the police and suspensions and grievances.

The Committee acknowledged that whilst the Annual Internal Audit Report would provide information relating to police referrals/theft investigations it would not provide details behind any of the other criteria therefore the Committee requested going forward that the quarterly reports contained an anonymised confidential appendix providing detail behind all of the identified criteria where there had been activity.

26. EXTERNAL AUDIT - ANNUAL AUDIT LETTER 2016/17

The Committee received and noted the report of the External Auditor detailing the Annual Audit Letter as detailed in appendix 1 to the report which summarised key findings from across the range of the auditor's work and responsibilities under statute and the National Audit Office's Code of Audit Practice.

27. STRATEGIC RISK REGISTER 2017-18

The Committee received and noted the report of the Service Director; Finance and Commercialisation detailing the Council's Strategic Risk Register 2017-18 as detailed in Appendix 1 of the report and the key strategic risks identified together with an assessment of the adequacy of controls in place to manage the risks and any further required actions. The Committee also particularly noted paragraphs 4-8 of the report which summarised the process in place in respect of the identification, management and review of the Council's strategic risk.

28. ANNUAL GOVERNANCE STATEMENT 2016-17 ACTIONS: STATUS REPORT

The Committee received and noted the report of the Service Director; Finance and Commercialisation detailing the Annual Governance Statement 2016-17 Actions: Status Report as detailed in appendix 1 of the report.

29. TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS MID YEAR REVIEW 2017/18

The Committee considered the report of the Service Director Finance and Commercialisation providing an overview of the Treasury Management activities and performance for 2017/18 against the approved Prudential Indicators for External Debt and Treasury Management and to approve any changes as a result of activity to date and updates to the capital programme.

The Committee specifically referenced paragraphs 10-17 of the report and noted that the DCLG were currently undertaking a consultation which potentially could have far reaching consequences, therefore it was recommended that a report be submitted to the February meeting assessing the impact of the consultation outcome.

RESOLVED:

- (i) That the current and forecast position with regards to these indicators be noted and any changes endorsed;
- (ii) That the continued proactive approach to Treasury Management had led to reductions in borrowing costs and safeguarded investment income during the year be noted;
- (iii) That the cost implication of the Capital Programme on the Authority as detailed in table 5 of the report be noted;
- (iv) That the proposed changes to the Prudential and Treasury Management Codes, in particular the inclusion of non-treasury investments such as commercial investments in properties in the definition of "investments" as well as loans made or shares brought for service purposes, as detailed in paragraphs 13-17 of the report be noted; and
- (v) That a report be submitted to the February meeting detailing any impact arising from the outcome of the DCLG consultation.

30. **PENSION FUND POSITION STATEMENT**

The Committee received and noted the report of the Service Director; Finance and Commercialisation following a request from the previous meeting regarding further information relating to the Pension Fund and the outstanding reported liability. The report provided clarification on the pension fund liability as at the 31st March 2017 and the supporting information. The Committee requested that officers look at the level of contributions/deficits being made by HCC and Southampton outside of the meeting.

31. INTERNAL AUDIT PROGRESS REPORT 2017-18

The Committee received and noted the report of the Chief Internal Auditor providing an internal audit progress report for the period 11th July 2017 to 25th October 2017 as detailed in appendix 1 of the report.

32. **EXCLUSION OF THE PRESS AND PUBLIC**

<u>RESOLVED</u>: that the Chair moved in accordance with the Council's Constitution, specifically the Access to Information Procedure Rules contained within the Constitution, the press and public be excluded from the meeting in respect of appendix 1 to the following item.

Confidentiality was based on Categories 3, 4 and 7a of paragraph 10.4 of the Access to Information Procedure Rules. The information contained therein was potentially exempt as it related to information relating to an individual, information likely to disclose the identity of an individual and information relating to the financial or business affairs of any person including the Authority. Having applied the public interest test it is not appropriate to disclose this information having regard to the nature of a confidential investigation.

33. **SOUTHAMPTON GUILDHALL CONTRACT**

The Committee received and noted the report of the Service Director; Digital and Business Operations providing an overview of the Southampton Guildhall Contract and the benefits to the City. The Committee considered appendix 1 of the report in confidential session.



DECISION-MAKE	R:	GOVERNANCE COMMITTEE									
SUBJECT:		QUARTERLY HR STATISTICS									
DATE OF DECISI	ON:	February 12 th 2018									
REPORT OF:		Service Director HR and OD									
		CONTACT DETAILS									
AUTHOR:	Name:	Janet King	Tel:	023 8083 2378							
	E-mail:	Janet.king@southampton.gov.	uk								
Chief Executive:	Name:	Dawn Baxendale	Tel:	023 8083 4428							
	E-mail:	dawn.baxendale@southamptor	າ.gov.u	ık							
STATEMENT OF	CONFID	ENTIALITY									
None.											

RECOMMENDATIONS:

i. To note the Quarter 3 2017/8 HR statistics as requested.

REASONS FOR REPORT RECOMMENDATIONS

1. The Governance Committee requested quarterly, Council wide information on key employment data covering disciplinaries, dismissals, and referrals to the police, suspensions and grievances. A format for the information was agreed with the Committee for reports from November 2017 onwards.

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

2. None.

DETAIL (Including consultation carried out)

- 3. **Quarter 3**: In the period October December 2017 the Council had:
 - 0 Final Written Warnings;

A total of 31 dismissals:

- 3 on disciplinary grounds
- 17 as a result of Phase 3 service restructures (6 in Adult Social Care,
 6 in Growth and 5 in Children and Families)
- 1 on capability
- 6 for ill health reasons
- 1 due to unsuccessful completion of probationary period
- 3 "other" (2 agreed settlement exits and 1 by mutual consent of termination of contract)
- no referrals to the police
- 2 suspensions with investigations underway
- 0 grievance cases

- Our HR policies are regularly reviewed for legislative compliance and business effectiveness. The revised policies for 2017 were approved at HR and OD Board and CMT and formally published in November 2017. The inclusion of mediation as a suitable step to resolve appropriate matters at matters at a service level with a trained mediator is now in place and two cases have been managed through this route avoiding formal grievance process.
- 5. Case work is supported by the HR Advisor to the service area to ensure application of correct policies and procedures and consistency of practice. The monitoring is tracked by the HR Management team to help identify any specific areas or issues of concern which require additional investigation or support.

The data highlights no key areas of concern in respect of any specific service at this time.

RESOURCE IMPLICATIONS

Capital/Revenue

6. None

Property/Other

7. Not applicable.

LEGAL IMPLICATIONS

Statutory power to undertake proposals in the report:

8. S.101 Local Government Act 1972 and associate employment legislation

Other Legal Implications:

None

POLICY FRAMEWORK IMPLICATIONS

10. None

KEY DECISION? No.

SUPPORTING DOCUMENTATION

Appendices

1.	Q1-Q3 table of data
2.	Q3 Disciplinary Dismissals Detail

Documents In Members' Rooms

	None
- 1	

Equality Impact Assessment

Do the implications/subject of the report require an Equality and Safety	No
Impact Assessment (ESIA) to be carried out?	

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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Agenda Item 5 Appendix 1

Southampton City Counci	I - Quarterly Governance Stats

							Quar	ter 1 (April '1	/ - June 1/) Dismissals					
Service Area		Disciplin	naries				Resolutions	Sus	pensions					
Jei vice Area	Final WW	Dismissed	Referral to Police	Total Dismissals	Capability	Disciplinary	Health	Probation	Restructures	Other	Commentary	Step 3 Resolutions	Total Suspensions	Length of Suspensions
Adults, Housing & Communities	0	2	0	0	0	2	0	0	0	0		1	0	
Children & Families	0	0	0	0	0	0	0	0	0	0		0	0	
Digital & Business Operations	0	0	0	0	0	0	0	0	0	0		0	0	
Finance & Commercialisation	0	0	0	0	0	0	0	0	0	0		0	0	
Growth	0	0	0	0	0	0	0	0	0	0		3	0	
Human Resources & Org Development	0	0	0	0	0	0	0	0	0	0		Ö	0	
Intelligence Insight & Communications	0	0	0	0	0	0	0	0	0	0		0	0	
Legal & Governance	0	0	0	0	0	0	0	0	0	0		0	0	
Public Health	0	0	0	0	0	0	0	0	0	0		0	0	
Quality & Integration	0	0	0	0	0	0	0	0	0	0		Ö	0	
Transactions & Universal Services	1	0	0	0	0	0	0	0	2	0		0	0	
Southampton City Council (Total)	1	2	0	0	0	2	0	0	2	0		4	0	

							Quar	ter 2 (July '17	' - Sept. '17)					
Service Area		Disciplin	naries				Resolutions	Sus	pensions					
Service Area	Final WW	Dismissed	Referral to Police	Total Dismissals	Capability	Disciplinary	Health	Probation	Restructures	Other	Commentary	Step 3 Resolutions	Total Suspensions	Length of Suspensions
Adults, Housing & Communities	0	1	0	0	0	1	0	0	0	0		0	0	
Children & Families	0	0	0	0	0	0	0	0	1	0		0	0	
Digital & Business Operations	0	0	0	0	0	0	0	0	0	0		0	0	
														Suspension from 28th
Finance & Commercialisation	0	0	0	0	0	0	0	0	0	0		0	1	Sept. to date
Growth	0	1	0	0	0	1	0	0	0	0		0	0	
Human Resources & Org Development	0	0	0	0	0	0	0	0	0	0		0	0	
Intelligence Insight & Communications	0	0	0	0	0	0	0	0	0	0		0	0	
Legal & Governance	0	0	0	0	0	0	0	0	0	0		0	0	
Public Health	0	0	0	0	0	0	0	0	0	0		0	0	
Quality & Integration	0	0	0	0	0	0	0	0	0	0		0	0	
Transactions & Universal Services	0	0	0	0	0	0	0	1	1	0		1	0	
Southampton City Council (Total)	0	2	0	0	0	2	0	1	2	0		1	1	

							Quar	ter 3 (Oct. '1	7 - Dec. '17)					
Service Area		Disciplin	aries				Resolutions	Suspensions						
Service Area	Final WW	Dismissed	Referral to Police	Total Dismissals	Capability	Disciplinary	Health	Probation	Restructures	Other	Commentary	Step 3 Resolutions	Total Suspensions	Length of Suspensions
Adults, Housing & Communities	0	0	0	8	0	0	2	0	6	0		0	0	
				9										* One suspension from 15/11/17 to current * One suspension from
Children & Families	0	2	0	1	0	2	1	0	5	1		0	2	18.10.17 - 05.12.17
Digital & Business Operations	0	0	0	2	1	0	0	0	0	1		0	0	
Finance & Commercialisation	0	0	0	1	0	0	0	0	0	1		0	0	
Growth	0	0	0	6	0	0	0	0	6	0		0	0	
Human Resources & Org Development	0	0	0	1	0	0	0	1	0	0		0	0	
Intelligence Insight & Communications	0	1	0	2	0	1	1	0	0	0		0	0	
Legal & Governance	0	0	0	0	0	0	0	0	0	0		0	0	
Public Health	0	0	0	0	0	0	0	0	0	0		0	0	
Quality & Integration	0	0	0	0	0	0	0	0	0	0		0	0	
Transactions & Universal Services	0	0	0	2	0	0	2	0	0	0		0	0	
Southampton City Council (Total)	0	3	0	31	1	3	6	1	17	3		0	2	

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Agenda Item 5

Appendix 2

The previously published Appendix 2 has been removed as it contained factual inaccuracies.

A corrected version will be reported to the next available meeting of the Governance Committee via the approval of the minutes.



AOTHOR.	Name: E-mail:			023 8083 4153			
AUTHOR:	Mana	Sue Cuerden Tel: 023 8083 4153					
		CONTACT DETAIL	<u>_S</u>				
REPORT OF:		SERVICE DIRECTOR FINANCE AND COMMERCIALISATION (S151)					
DATE OF DEC	CISION:	12 FEBRUARY 2018 21 FEBRUARY 2018					
SUBJECT:		TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS 2018/19 TO 2021/22					
DECISION-MA	KER:	GOVERNANCE COMMITTEE COUNCIL					

STATEMENT OF CONFIDENTIALITY

NOT APPLICABLE

BRIEF SUMMARY

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.

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.

The core elements of the 2018/19 strategy are:

- 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:
 - 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.

• T	n annro	ve the 2018 Minimum Revenue Provision (MRP) Statement
		ATIONS:
		E COMMITTEE
		nded that Governance Committee:
	(i)	Endorse the Treasury Management (TM) Strategy for 2018/19 as outlined in the report.
	(ii)	Endorse the 2018 Minimum Revenue Provision (MRP) Statement as detailed in paragraphs 85 to 94.
	(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 21 February 2018. Should the recommendations change, the Prudential Indicators may have to be recalculated.
	(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.
COUN It is re		nded that Council:
	(i)	Approve the Council's Treasury Management (TM) Strategy and Prudential Indicators for 2018/19, 2019/20, 2020/21 and 2021/22, as detailed within the report.
	(ii)	Approve the 2018 Minimum Revenue Provision (MRP) Statement as detailed in paragraphs 85 to 94 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 43 to 66.
	(iv)	Note that at the time of writing this report the recommendations in the Capital update report, submitted to Council on the 21 February 2018, 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.
	(v)	Continue to delegate authority to the Chief Financial Officer (CFO) to approve any changes to the Prudential Indicators, Minimum Revenue Provision or borrowing limits that will aid good treasury management. Fo 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 to cabinet as part of quarterly financial and performance monitoring and in revisions to the TM Strategy
REAS	ONS FO	R REPORT RECOMMENDATIONS
1.		er to comply with Part 1 of the Local Government Act 2003, and the ished TM procedures that have been adopted by the Council, each year the

Council must set certain borrowing limits and approve TM Strategy which includes:

- Treasury Management Strategy for 2018/19:
 - Borrowing Paragraphs 30 to 41,
 - Debt Rescheduling Paragraph 42
 - o Investments Paragraphs 43 to 66
- Treasury Management Indicators Paragraphs 67 to 83
- MRP Statement Paragraphs 85 to 94
- Other Prudential Indicators Paragraphs 95 to 117

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

2. Alternative options for borrowing would depend on decisions taken on the review of the General Fund & Housing Revenue Account Capital Strategy and Programme update report being taken at Full Council on 21 February 2018.

DETAIL (Including consultation carried out)

CONSULTATION

3. The proposed General Fund & Housing Revenue Account Capital Strategy and Programme 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 Council adopted the CIPFA Treasury Management Code at its Council meeting on 19 February 2003 and all its subsequent updates. The latest one being *Treasury Management in the Public Services: Code of Practice 2011 Edition* in February 2012.
- 6. CIPFA published revised editions of the Treasury Management and Prudential Codes in December 2017.

The Council is currently considering the changes from the 2011 Code for incorporation into future Treasury Management Strategies and monitoring reports. However, Minimum Revenue Provision (MRP) changes have been incorporated into the Medium Term Financial Strategy & Budget report which will be reported to Council February 2018, as the changes result in a pressure in 2018/19 and future years.

- 7. In addition, the Ministry of Housing, Communities and Local Government (MHCLG) issued revised *Guidance on Local Authority Investments* in March 2010 that requires the Council to approve an investment strategy before the start of each financial year.
- 8. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA code and the MHCLG guidance.
- 9. 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 council 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. Our current policy is shown in appendix 1. This report covers treasury activity and the associated monitoring and control of risk. 10. The purpose of this Treasury Management Strategy (TMS) is to allow Council to approve: Treasury Management Strategy for 2018/19 Annual Investment Strategy 2018/19 Prudential Indicators for 2018/19 to 2021/22 2018 MRP Statement 11. 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 2). The outlook for interest rates (Appendix 3) has also been taken into account in developing this strategy 12. 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. In accordance with the MHCLG Guidance, the Council will be asked to approve 13. a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change in interest rates; material change to the Council's capital programme or in the level of its investment It should be noted that once the arrangements regarding the Local Authority Trading Company (LATCo) have been finalised it is expected that the strategy will need to be updated. 14. The MHCLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Council believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below. **Options** Impact on income and Impact on risk management expenditure Invest in a narrower range Interest income will be Lower chance of losses from of counterparties and/or lower credit related defaults, but any such for shorter times losses may be greater Invest in a wider range of Interest income will be Increased risk of losses from credit counterparties and/or for higher related defaults, but any such losses longer times 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	In the medium term, increases in debt interest costs will be broadly offset by rising investment income in 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			
	Economic Background					
15.		progress in negotiating	easury management strategy for it's exit from the European			
16.						
17.	Consumer price inflation reached 3.0% in September 2017 as the post-referendum devaluation of sterling continued to feed through to imports. Unemployment continued to fall and the Bank of England's Monetary Policy Committee judged that the extent of spare capacity in the economy seemed limited and the pace at which the economy can grow without generating inflationary pressure had fallen over recent years. With its inflation-control mandate in mind, the Bank of England's Monetary Policy Committee raised official interest rates to 0.5% in November 2017.					
18.	raising interest rates in reg	gular steps to remove provided for the past do but has started to tape	ecade. The European Central er its quantitative easing			
	Credit Outlook					
19.	High profile bank failures in Italy and Portugal have reinforced concerns over the health of the European banking sector. Sluggish economies and fines for precrisis behaviour continue to weigh on bank profits, and any future economic slowdown will exacerbate concerns in this regard.					
20.	will rescue failing banks in implemented in the Europ Canada are progressing will ring-fence their retail to	nstead of taxpayers in ean Union, Switzerlan with their own plans. In panking functions into e uncertainty over how	stors including local authorities the future, has now been fully d and USA, while Australia and addition, the largest UK banks separate legal entities during v these changes will impact upon			

The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Council; returns from cash deposits however remain very low. Interest Rate Forecast The Council's treasury management advisor's, Arlingclose, central case is for UK Bank Rate to remain at 0.50% during 2018/19, following the rise from the historic low of 0.25%. The Monetary Policy Committee re-emphasised that any prospective increases in Bank Rate would be expected to be at a gradual pace and to a limited extent. Future expectations for higher short term interest rates are subdued and on-
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Future expectations for higher short term interest rates are subdued and on-
going decisions remain data dependant and negotiations on exiting the EU cast a shadow over monetary policy decisions. The risks to Arlingclose's forecast are broadly balanced on both sides. The Arlingclose central case is for gilt yields to remain broadly stable across the medium term.
A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix 3
For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.39% for short term and 4.50% for long term (average of 2.8%), and that new long-term loans taken over the period of the strategy will be borrowed at an average rate of 2.92%.
BALANCE SHEET SUMMARY AND FORECAST
The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.
At 31/12/2017 the Council held £321M of debt (£244M borrowing plus £77M other long term liabilities) and £69M investments which is set out in further detail in Appendix 2.
Forecast changes in these sums are shown in the balance sheet analysis in Table 1 below.
 Table 1 shows that the Council will: Comply with this recommendation; That the Council has an increasing CFR due to the impact of the capital programme; Decreasing investments; and Will need to borrow over the forecast period.

Table 1:	Balance sheet	Summary	and	Forecast
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	31/03/2018	31/03/2019	31/03/2020	31/03/2021	31/03/2022
	Forecast	Forecast	Forecast	Forecast	Forecast
	£M	£M	£M	£M	£M
General Fund CFR	334.87	357.07	352.06	360.69	380.54
Housing CFR	171.84	182.69	181.40	182.25	180.93
Total Opening CFR (see Table 11)	506.71	539.76	533.46	542.94	561.47
Less Other Long Term Liabilities*	(74.97)	(72.51)	(69.13)	(65.60)	(61.66)
Borrowing CFR	431.74	467.25	464.33	477.34	499.81
Less External Borrowing					
Long Term	(217.81)	(206.34)	(169.88)	(150.60)	(147.87)
Short Term	(48.54)				
Internal Borrowing	165.39	260.91	294.45	326.74	351.94
Less Usable Reserves	(122.52)	(117.51)	(112.51)	(107.51)	(102.51)
Less Working Capital	(42.87)	(42.87)	(42.87)	(42.87)	(42.87)
Underlying need to borrow	0.00	100.53	139.07	176.36	206.56

^{*} finance leases, PFI liabilities and transferred debt which form part of the Council's total debt

BORROWING STRATEGY

30. The Council currently holds £244M of loans a decrease of £16M since the 31st March 2017 and reflects the current strategy of only borrowing when cash flows dictate, thus lowering both borrowing costs and investment risk. The estimated forecast as shown in Appendix 4, table 4 is that based on the current capital programme and expected cash flows, the Council expects to borrow £266M by 31st March 2018, this is an additional £22M (see appendix 2) and a further £41M in 2018/19 bringing estimated borrowing to £307M.

If it was cost effective the Council could also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing.

Objectives

31. The Council'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 Council's long-term plans change is a secondary objective.

Strategy

- 32. Given the significant cuts to public expenditure and in particular to local government funding, the Council'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.
- 33. Affordability and the "cost of carry" remain important influences on the Council'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 period of 2017/18 and 2018/19, lower than long-term rates, the Council determines it will be more cost effective in the short-term to use internal resources and will look to

borrow short-term loans instead From 2019/20 the Medium Term Financial Strategy assumes that the majority of new borrowing will be on a long term basis. By doing so, the Council is able to reduce net borrowing costs (despite foregone 34. investment income) and reduce overall treasury risk. The benefits of internal and short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when longterm borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2018/19 with a view to keeping future interest costs low, even if this causes additional cost in the short-term. Alternatively, the Council may arrange forward starting loans during 2018/19, 35. 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 Council may borrow further short-term loans to cover unexpected cash flow shortages. Sources 36. The approved sources of long-term and short-term borrowing are: 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 Council bond issues 37. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities: operating and finance leases hire purchase Private Finance Initiative sale and leaseback 38. The Council 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 Council loans and bank loans which may be available at more favourable rates. UK Municipal Bonds Agency plc (MBA) was established in 2014 by the Local 39. Government Association as an alternative to the PWLB. It plans to issue bonds 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 Council 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.

A report setting out in full the details, options and risks of the MBA was considered by full Council on 10 February 2016 and any initial proposal to borrow from the Agency will therefore need to be the subject of a separate report to both Governance Committee and Full Council.

Lender's Option Borrower's Option Loans (LOBOs)

40. The Council 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 Council 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 2018/19 and although the Council understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so.

Short Term and Variable Rates

41. Included within the PWLB portfolio is £35M of variable rate Loans, which are currently averaging 0.45% and are helping to keep the overall cost of borrowing down. Whilst in the current climate of low interest rates this remains a sound strategy, these loans leave the Council 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 70), the Council review these regularly and if appropriate will switch into fixed rate loans.

Debt Rescheduling

42. 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 Council 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

- 43. The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During the financial year the Council's investment balances have ranged between £58M and £101M and are currently £69M as at 31st December 2017. Projected balances indicate that on present levels of spend balances will be lower than last year, but this will be dependent on any borrowing decisions taken. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested, however it should be noted that a lower rate is an acceptable offset for higher credit and less risk, for example a covered bond.
- 44. As a result of the second Markets in Financial Instruments Directive (MiFID II), from 3rd January 2018 local authorities will be treated as retail clients but can "opt up" to professional client status, providing that they meet certain criteria which includes having an investment balance of at least £10 million and the person(s) authorised to make investment decisions on behalf of the Council have at least a year's relevant professional experience. In addition, the regulated financial services firms to whom this directive applies must assess that

that person(s) have the expertise, experience and knowledge to make investment decisions and understand the risks involved. The Council has met the conditions to opt up to professional status and has done so in order to maintain its MiFID II status prior to January 2018. As a result, the Council will continue to have access to products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice.

Objectives

45. Both the CIPFA Code and the MHCLG Guidance require the Council 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 Council'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 of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested, however it should be noted that a lower rate is an acceptable offset for higher credit and less risk, for example a covered bond.

Negative Interest Rates

46. If the UK enters into a recession in 2018/19, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

Strategy

47. Given the increasing risk and very low returns from short-term unsecured bank investments, the Council aims to continue to diversify into more secure and/or higher yielding asset classes during 2018/19. This is especially the case for the estimated £40M that is available for longer-term investment. Appendix 2 shows the makeup of the Council's current investments.

Approved Counterparties

48. The Council may invest its surplus funds with any of the following counterparty types, subject to the cash limits (per counterparty) and time limits detailed below. 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.

Table 2: Approved Investment counterparties and Limits

Credit Rating	Banks Unsecured	Banks Secured	Government & Local Authorities	Corporates	Registered Providers
	£M	£M	£M	£M	£M
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£5M	£10M	£10M	£5M	£5M
	5 years	20 years	50 years	20 years	20 years
AA+	£5M	£10M	£10M	£5M	£5M
	5 years	10 years	25 years	10 years	10 years
AA	£5M	£10M	£10M	£5M	£5M
	4 years	5 years	15 years	5 years	10 years
AA-	£5M	£10M	£10M	£5M	£5M
	3 years	4 years	10 years	4 years	10 years
A+	£5M	£10M	£5M	£5M	£5M
	2 years	3 years	5 years	3 years	5 years
А	£5M	£10M	£5M	£5M	£5M
	13 months	2 years	5 years	2 years	5 years
A-	£5M	£10M	£5M	£5M	£5M
	6 months	13 months	5 years	13 months	5 years
None	£1M	n/a	£10M	£0.5M	£5M
THORIC	6 months	11/ α	25 years	5 years	5 years
Pooled funds	£10M per fu advice	nd for MMFs.	, other funds (e.g	. CCLA) subject	to specific

This table must be read in conjunction with the notes below.

- 49. **Credit Rating:** Investment limits are set 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. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
- 50. **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. See paragraph 56 for arrangements relating to operational bank accounts.
- 51. **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.

- 52. **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.
- 53. **Corporates:** Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bailin, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made either following an external credit assessment or to a maximum of £1M per company as part of a diversified pool in order to spread the risk widely.
- 54. **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 the likelihood of receiving government support if needed.
- 55. **Pooled Funds:** Shares in diversified investment vehicles consisting of 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 Council 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 Council's investment objectives will be monitored regularly.

The Council has invested £27M in property funds. These offer the potential for enhanced returns over the longer term, but may be more volatile in the shorter term and are managed by professional fund managers which allows the Authority to diversify into asset classes.

Operational bank accounts: The Council may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept to a

- minimum. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.
- 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.

Risk Assessment and Credit Ratings

- 58. Credit ratings are obtained and monitored by the Council'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:
 - 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.

Other Information on the Security of Investments

- 59. The Council 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.
- 60. 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 Council 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 Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office 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.

Specified Investments

- 61. The MHCLG Guidance defines specified investments as those:
 - 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:
 - the UK Government,
 - o a UK local Council, parish council or community council, or
 - a body or investment scheme of "high credit quality".

The Council 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.

Non-Specified Treasury Investments

Any investment not meeting the definition of a specified investment is classed as non-specified. The Council 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 Treasury 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

	Cash Limit
Total long-term investments	£20M
Total investments without credit ratings or rated below A-	£30M
Total investments in foreign countries rated below AA+	£5M
Total non-specified investments	£55M

63. Investment Limits: The Council's revenue reserves and balances available to cover investment losses (excluding Schools, capital and HRA) are forecast to be £69.7M at 31st March 2018. 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 and property funds) 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 in table 4 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.

Table	. 1 _	Invoc	tmor	۱ t٠	imits
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	1
	Cash limit
Any single organisation, except the UK Central Government and property funds (subject to specific advice)	£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	25% per manager unless under specific advice
Negotiable instruments held in a broker's nominee account	£30M per broker
Foreign countries	£10M per country
Registered Providers	£5M in total
Unsecured investments with Building Societies	£5M in total
Loans to unrated corporates	£1M in total
Money Market Funds**	£10M* per fund and no more than 0.50% of any investments fund in total for non- government funds

^{*}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.

Liquidity Management

64. The Council 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 Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

Non Treasury Investments

65.

Although not classed as treasury management activities and therefore not covered by the existing CIPFA Code or the MHCLG Guidance, the Council may

^{**}We would not normally invest more than 50% of our overall investment portfolio in MMF on the advice of our advisors, however as part of our revised strategy to reduce short term investments and move into longer term investments, there will be occasions as bonds mature when this limit is exceeded. This advice is with regards to cash flow risk, however we feel this is mitigated by spreading over a number of funds and not just the highest yielding ones and having funds in other instant access accounts. In addition money can be borrowed short term from the market on the day.

	also purchase property for investment purposes and may also make loans and investments for service purposes. As part of the new code which is being considered by the Council there will be a need to include indicators for these investments in future reports.						
66.	Such loans and investments will be subject to the Council's normal approval processes for revenue and capital expenditure and at the time of writing need not comply with this treasury management strategy.						
	TREASURY MANAGEMEN	IT INDICAT	<u>rors</u>				
67.	The Council measures and using the following indicator	-	ts exposure	e to treasur	ry manag	ement	risk
	<u>Security</u>						
68.	The Council has adopted a monitoring the value-weighth This is calculated by applying and taking the arithmetic and taking	ted averag ng a score average, w	e credit ra to each inv eighted by	ting of its vestment (/ the size	investme AAA=1, A of each	ent porti AA+=2, investn	foli eta
				Tar	rget		
	Portfolio average credit rati	ing			A		
60	Liquidity The Council has adopted as				t- li	ماند، سنمار	
69.	Liquidity The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below which are available without	ish availabl old on cast this limit we	e to meet un available would cor	inexpected in instant a nsider takir	d paymen access ac ng short to	ts and l counts erm loa	ha , if
69.	The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below	ish availabl old on cast this limit we	e to meet un available would cor	inexpected in instant a nsider takir	d paymen access ac ng short to	ts and l counts erm loa	ha , if
70.	The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below which are available without	ish available old on cash this limit we given prior the Couvariable is are those from the si	e to meet un available e would con notice and uncil's exponate interest where the tart of the f	inexpected in instant ansider takin at competions of the competion	d payment access acting short to itive rates terest rate posures. Interest is ear or the	e risk. Fixed	ha , if ns T ra or
	The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below which are available without interest Rate Exposure This indicator is set to contrupper limits on fixed and investments and borrowing least 12 months, measured	ish available old on cash this limit we given prior the Couvariable research the sare those from the sare the s	e to meet un available e would con notice and uncil's exporate interest where the tart of the following as a second control of the following as a second contro	inexpected in instant ansider takin at competions at competions at competions at rate experience of instancial yeariable rate	d payment access acong short to itive rates terest rate posures. Interest is ear or the te.	e risk. Fixed	ha , if ns T ra or
	The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below which are available without interest Rate Exposure This indicator is set to contrupper limits on fixed and investments and borrowing least 12 months, measured date if later. All other instructions	ish available old on cash this limit we given prior the Couvariable research the sare those from the sare the s	e to meet un available e would con notice and uncil's exporate interest where the tart of the following as a second control of the following as a second contro	inexpected in instant ansider takin at competions at competions at competions at rate experience of instancial yeariable rate	d payment access acong short to itive rates terest rate posures. Interest is ear or the te.	e risk. Fixed fixed fransa	ha , if ns TI ra or
	The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below which are available without interest Rate Exposure This indicator is set to contrupper limits on fixed and investments and borrowing least 12 months, measured date if later. All other instructions	sh available old on cash this limit we given prior the Couvariable is are those from the siments are contacted and Vailable and Vailable stimate	e to meet un available e would connotice and uncil's exportate interest where the classed as riable Interest 2019/20 Estimate	inexpected in instant ansider takin at competion of the c	d payment access acting short to itive rates terest rate posures. Interest is ear or the te. posure 2021/22 Estimate	e risk. Fixed fixed fransa	ha , if ns TI ra or
	The Council has adopted a monitoring the amount of caset a £10M minimum thresh balances were to fall below which are available without interest Rate Exposure This indicator is set to contrupper limits on fixed and investments and borrowing least 12 months, measured date if later. All other instructions	ash available old on cash this limit we given prior the Couvariable is are those from the siments are concept and Vailable 2018/19	e to meet un available would connotice and uncil's exponsate interest where the tart of the folassed as riable Interest 2019/20	inexpected in instant ansider takin at competions at competions at rate experience at rate of infinancial yeariable rate at Rate Experience at Rat	d payment access acting short to itive rates terest rate posures. The terest is ear or the te. posure 2021/22	e risk. Fixed fixed fransac	ha , if ns TI ra or

71. This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing as set out in **Table** 6.

Table 6 – Maturity Structure

	Lower Limit %	Upper Limit %
Under 12 Months	0	45
12 months and within 24 months	0	45
24 months and within 5 years	0	50
5 years and within 10 years	0	55
10 years and within 20 years	0	60
20 years and within 30 years	0	65
30 years and above	0	75

- 72. 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. Although all LOBOs are now in their call options they are not expected to be called in the near future so are shown at their maturity date in table below.
- 73. **Table 7** details the level of our current debt and shows that all debt is within existing limits.

Table 7 - Current Debt

	Lower Limit	Upper Limit	Actual Debt as at 31/12/2017	Average Rate as at 31/12/2017	% of Overall Debt as at 31/12/2017	Compliance with set Limits?
	%	%	£M	%		
Under 12 months	0	45	29.11	1.45	11.92	Yes
12 months and within 24 months	0	45	11.50	3.23	4.71	Yes
24 months and within 5 years	0	50	55.69	2.61	22.81	Yes
10 years and within 20 years	0	55	6.00	4.94	2.46	Yes
20 years and within 30 years	0	65	18.00	4.67	7.37	Yes
30 years and within 40 years	0	75	84.10	3.81	34.45	Yes
40 years and within 50 years	0	75	39.75	3.55	16.28	Yes
			244.15	3.30	100.00	

Principal Sums Invested for Periods Longer than 364 days

74. The purpose of this indicator is to control the Council'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 8**.

	Table 8 – Principal Sums Invested for Periods Longer than 364 days										
		Current £M	2018/19 £M	2019/20 £M	2020/21 £M	2021/22 £M					
	Limit on principal invested beyond year end	40.60	37.60	33.00	30.00	30.00					
	OTHER ITEMS										
75.	There are a number of additional items that the Council is obliged by CIPFA or MHCLG to include in its Treasury Management Strategy.										
	Policy on Use of Financial Derivatives										
76.	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).										
77.	The Council 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 Council 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.										
78.	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.										
	Housing Revenue Account Self-Financing										
79.	On 1st April 2012, the Council 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.										
80.	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 agreed rate. Housing Legislation does not allow impairment losses to be charged to the HRA and consequently any credit related losses on the Council'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.

Training

81. 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.

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.

Treasury Management Advisors

82. The MHCLG's Guidance on local government investments recommends that the Investment Strategy should state:

Whether and, if so, how the Council uses external contractors offering information, advice or assistance relating to investment and

How the quality of any such service is controlled.

The Council has a contract in place with Arlingclose Limited as treasury advisory service and receives the following services:

- Credit advice
- Investment advice
- Technical advice
- Economic & interest rate forecasts
- Workshops and training events
- HRA support
- Ad hoc advice

The Council 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.

Investment of Money Borrowed in Advance of Need

83. The Council 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 Council 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 Council's overall management of its treasury risks. 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 Council is not required to link particular loans with

particular items of expenditure.

	FINANCIAL IMPLICATIONS
84.	The budget for borrowing costs in 2018/19 is £14.6M. This is made up of borrowing of £8.2M based on an average debt portfolio of £310.5M at an average interest rate of 2.63% plus MRP and other costs of £6.4M. Investment income for 2018/19 is budgeted at £1.4M based on an average portfolio of £50M at an average of 2.80%.
	If actual levels of investments and borrowing, and/or interest rates differ from those forecast, performance against budget will be correspondently different.
	2018/19 MINIMUM REVENUE PROVISION (MRP) STATEMENT
85.	Where the Council 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 Council to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the MHCLG Guidance) most recently issued in 2012.
86.	The broad aim of the MHCLG guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant. This guidance is currently subject to consultation and any subsequent amendments required will be built into future reports.
87.	The MHCLG Guidance requires the Council to approve an Annual MRP Statement each year. For borrowing prior to the prudential regime we use the regulatory method (over a 50 year life) and for prudential borrowing the asset life method.
88.	The exception to this is investment properties acquired as part of the Property Investment Fund which have been purchased with a view to generating long term rental income streams to support the delivery of Council services in the future and reduce dependence on Central Government funding, in this case we have adopted the depreciation method. As investment properties these assets are valued each year and any downward movement in the value for the year (i.e. depreciation) will be spread over the
	remaining life of the asset as a charge to revenue in lieu of MRP. Following the update of the Treasury Management Code of Practice, which comes into effect from 2018/19, it will no longer be possible to charge a 'nil' MRP for these properties. The assets will revert back to the regularity method detailed in paragraph 87 above. The Financial impact of this has been built into the update of the Medium Term Financial Strategy and Budget Update report being reported to Council in February 2018.
89.	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.
- 90. 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.
- 91. 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.
- 92. Capital expenditure incurred during 2018/19 and funded from borrowing will not be subject to a MRP charge until 2019/20.
- 93. Based on the Council's latest estimate of its Capital Financing Requirement on 31 March 2018 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 (over the remainder of a 50 year life) and using the asset life method for prudential borrowing where it applies. As previously reported the Council has been taking a holiday from MRP payments due to over provision in the past, the balance of which will be used during 2018/19.
- 94. The current and estimated levels of MRP and CFR are shown in **Table 9** below:

Table 9 –Current and Estimated MRP and CFR for 2018/19						
	31/03/2017 Actual CFR	2017/18 MRP Liability				
	£M	£M				
Capital expenditure before 01.04.2008	97.78	1.70				
Unsupported capital expenditure after 31.03.2008	152.60	3.65				
Transferred debt	14.92	0.36				
Finance leases and Private Finance Initiative	62.26	1.84				
Total General Fund CFR and MRP Liability	327.56	7.55				
MRP Holiday	(5.00)	(5.35)				
Net General Fund CFR and MRP Liability (Table 11)	322.56	2.20				
Assets in the Housing Revenue Account	126.86	Nil				
HRA subsidy reform payment	36.40	5.51				
Total Housing Revenue Account (Table 17)	163.26	5.51				

Total

31/03/2018 Estimated CRF	2018/19 Estimated MRP
£M	£M
97.78	1.70
162.79	4.01
14.55	0.36
60.42	2.10
335.54	8.17
(0.67)	(0.67)
334.87	7.50
140.95	Nil
30.89	5.50
171.84	5.50
506.71	13.00

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

485.82

7.71

- 95. 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.
- 96. In addition, a quarterly update will be presented to Cabinet as part of Quarterly Revenue Financial Monitoring.

	PRUDENTIAL INDICATORS					
	Background					
97.	The Local Government Act 2003 requires the Council 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 Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.					
	Gross Debt and the Capital Financing Requirement					
98.	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 Council 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.					
99.	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.					
100.	The estimated gross debt and capital financing requirement is shown in the tables below: Table 10 – Current and Estimated Movement in Gross Debt					

Gross Debt	31/03/2017	31/03/2018	31/03/2019	31/03/2020	31/03/2021	31/03/2022
	Actual	Forecast	Forecast	Forecast	Forecast	Forecast
	£M	£M	£M	£M	£M	£M
Borrowing B/Fwd	96.40	96.40	94.51	124.18	127.55	144.72
Maturing Debt		(21.15)	(25.21)	(73.87)	(20.02)	(11.43)
New Borrowing Requirement (Appendix 4	Table 1)	19.26	54.88	77.24	37.19	40.22
Total General Fund Borrowing	96.40	94.51	124.18	127.55	144.72	173.51
HRA Borrowing B/Fwd	163.25	163.25	171.84	182.69	181.40	182.25
Maturing Debt		(20.35)	(34.43)	(62.78)	(9.25)	(1.32)
New Borrowing Requirement (Appendix 4	Table 2)	28.94	45.28	61.49	10.10	0.00
Total HRA Borrowing	163.25	171.84	182.69	181.40	182.25	180.93
Total Borrowing	259.65	266.35	306.87	308.95	326.97	354.44
Finance leases and Private Finance	62.26	60.42	58.32	55.30	52.13	48.56
Initiatives						
Transferred Debt	14.92	14.55	14.19	13.82	13.46	13.07
Total Debt	336.83	341.32	379.38	378.07	392.56	416.07

Table 11 – Current and Estimated Movement in Capital Financing Requirement

	31/03/2017	31/03/2018	31/03/2019	31/03/2020	31/03/2021	31/03/2022
	Actual	Forecast	Forecast	Forecast	Forecast	Forecast
	£M	£M	£M	£M	£M	£M
Balance Brought forward	280.75	322.56	334.87	357.07	352.06	360.69
Capital Spend Financed from	43.72	14.51	29.71	4.37	17.79	29.48
Borrowing (Table 12)						
MRP	(5.00)	(5.35)	(5.71)	(6.00)	(5.62)	(5.69)
Appropriations (to) from HRA	0.98	0.00	0.00	0.00	0.00	0.00
Movement in Other Liabilities	(2.89)	(2.20)	(2.47)	(3.38)	(3.54)	(3.94)
MRP Holiday	5.00	5.35	0.67	0.00	0.00	0.00
Total General Fund Debt	322.56	334.87	357.07	352.06	360.69	380.54
HRA (see table 17 below for breakdown)	163.25	171.84	182.69	181.40	182.25	180.93
Total CFR	485.81	506.71	539.76	533.46	542.94	561.47

Estimates of Capital Expenditure

101. The Council'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.

102	Table	12 –	Capital	Expenditure
102.	IUNIO	. —	Oupitui	Exponditure

	Forecast	Forecast	Forecast	Forecast	Forecast
	2017/18	2018/19	2019/20	2020/21	2021/22
	£M	£M	£M	£M	£M
General Fund	48.44	68.78	23.98	23.75	29.48
HRA	44.92	53.12	41.15	43.69	34.01
Total Expenditure	93.36	121.90	65.13	67.44	63.49
Capital receipts	7.55	17.56	0.00	0.96	1.66
Capital Grants	18.70	24.20	19.31	5.65	0.00
Contributions	5.26	5.95	0.00	0.00	0.00
Major Repairs Allowance	19.95	13.84	23.48	22.47	21.10
Other Council Resources	13.29	14.29	1.76	10.48	11.25
Total Financing	64.75	75.84	44.55	39.56	34.01
Council Resources - Borrowing GF	14.51	29.71	4.37	17.79	29.48
Council Resources - Borrowing HRA	14.10	16.35	16.21	10.09	0.00
Total Funding	28.61	46.06	20.58	27.88	29.48
Total Financing & Funding	93.36	121.90	65.13	67.44	63.49

Ratio of Financing Costs to Net Revenue Stream

- 103. 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 the forecast of net revenue expenditure in the medium term financial model. The upper limit for this ratio is currently set at 10% and will remain so for the General Fund to allow for known borrowing decisions 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.
- 104. 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, which is the main contributor for the increase in 2019/20 and 2020/21. 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 13 – Ratio of Financing Costs to Net Revenue Stream

105.

Ratio of Financing Costs to Net Revenue Stream	2016/17* Actual	2017/18* Forecast	2018/19* Forecast	2019/20 Forecast	2020/21 Forecast	2021/22 Forecast
	%	%	%	%	%	%
General Fund	8.56	7.79	8.06	9.74	9.90	10.26
HRA	14.12	15.02	15.86	33.04	20.96	9.66
Total	11.17	10.59	11.06	17.47	14.28	11.45

^{*}Includes MRP due for the year to reflect true impact of borrowing, they have not been adjusted to reflect the MRP holiday taken.

Incremental Impact of Capital Investment Decisions

106. 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

I	generation.									
	Table 14– Incremental Impact of Capital Investment Decisions									
107.	Incremental Impact Investment Decision		2017/18 Forecas				2020/21 Estimate			
			£	£	£	£	£			
	Increase / (Decreas number of equivale properties for Coun	nt band D	,	(9.95	5) (4.25	3.51	16.15			
	Increase / (Decreas Weekly Housing Re		(34.4	8) (25.57	') (11.32	(40.65)	(22.30			
	It should be noted show the amount equate to since the As per the Gener	per equiva ne last capit	lent band D tal update re	properties ported in l	that this o	change woo 2017.	uld			
	currently set unde independent of the the indicator igno	er the Gove e level of c	rnment's re apital invest	nt restructi	uring form	ula, which i	S			
	Authorised Limi	t and Oper	ational Bou	undary for	<u>External</u>	<u>Debt</u>				
110.	The Council has treasury position borrowing will the of the Council and CFR.	in accordar refore arise	nce with its a e as a conse	approved sequence of	trategy ar	nd practice. ancial trans	Overall actions			
111.	The <i>Authorised Limit</i> 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. 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									
	Authorised Limit i Government Act	s the statut	ory limit det	ermined u	nder Secti	on 3(1) of t	bt. The he Local			
		s the statut 2003 (refer	ory limit det red to in the	ermined ui legislation	nder Secti	on 3(1) of t	bt. The he Local			
112.	Government Act	s the statut 2003 (refer	ory limit det red to in the	ermined ui legislation	nder Secti	on 3(1) of t	bt. The he Local			
112.	Government Act : Table 15 – Author Authorised Limit for	s the statut 2003 (refer ised Limit f Actual 31 December	ory limit det red to in the or External	ermined ui legislation Debt 2018/19	nder Secti as the Af	on 3(1) of t fordable Lii 2020/21	bt. The he Local mit).			

	Other Long- term Liabilities	77		81	75	73	70	
	Total	321		898	860	730	720	8
113.	The Operationa CFR and estimate based on the sate prudent but not included within the favourable opposition.	ites of other me estimat worst case the Authoris	day to one day to one day to one day the day the day to one day the day to one day to one day to one day to one day the day to one day the day to one day	day cas e Autho b but wi	sh flow rorised Li	equireme mit reflec e addition	nts. This ir ting the mo al headroo	ndicatoi st likely m
	Table 16-Operat	ional Bound	dary for	Externa	al Debt			
114.	Operational Boundary for External Debt	Actual 31 December 2017	2017/ Approv	· _	2018/19 stimate	2019/20 Estimate	2020/21 Estimate	2021/2 Estima
		£M	£M		£M	£M	£M	£M
	Borrowing	263		566	705	599	602	6
	Other Long- term Liabilities	78		81	75	73	70	
	Total	341		647	780	672	672	7
115.	The CFO has delegated authority, within the above limits for any individual yea 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							
	other long term option appraisal use of this deleg	ient betwee liabilities. I s and best gated Autho	n the se Decisions value co prity.	parately s will be	y agreed e based	d limits fo on the ou	r borrowing itcome of fi	and nancial
116.	other long term option appraisal use of this delegent that the level of debt the time of implementation of the level of debt the time of implementation.	nent betwee liabilities. It is and best gated Author indebtedner are require which is im- ementation MHCLG of	n the se Decisions value co ority. ss ed to rep aposed (of self – f £199.61	parately s will be onsiderate oort the or subs financi M.	y agreed e based ations. (level of sequentling. The	the HRA y amende HRA is s	r borrowing atcome of fill be notified CFR comped) by the Notified within the street of the Notified CFR comped) by the Notified within the street of the Notified CFR comped) by the Notified CFR comped)	and nancial of an ared to MHCLG
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116.	other long term option appraisal use of this delegent that the level of debt the time of implementation of the level of debt the time of implementation.	nent betwee liabilities. It is and best gated Author indebtedner are require which is im- ementation MHCLG of	n the se Decisions value co ority. ss ed to rep aposed (of self – f £199.61	parately s will be onsiderate oort the or subs financi M.	level of sequently ing. The	the HRA y amende HRA is s	cr borrowing atcome of fill be notified by the	and nancial ed of an ared to MHCLG e HRA
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RESOURCE IMPLICATIONS

CLG) Headroom

36.35

27.76

16.91

18.20

17.35

18.67

Capital/Revenue 118. 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 119. None LEGAL IMPLICATIONS Statutory power to undertake proposals in the report: 120. Local Authority borrowing is regulated by Part 1, of the Local Government Act 2003, which introduced the new Prudential Capital Finance System.

121. 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: 122. None POLICY FRAMEWORK IMPLICATIONS 123. This report has been prepared having regard with the CIPFA Code of Practice on Treasury Management.

KEY D	KEY DECISION? No					
WARE	S/COMMUNITIES AFFE	CTED:	None			
SUPPORTING DOCUMENTATION						
Apper	ndices					
1.	Policy Statement					
2.	Existing Investment &	Debt Portfo	lio Position and Projections			
3.	Economic and Interest	Outlook				
4.	Forecast of Long Term	Borrowing	Requirement and Actual Deb	ot		
5.	Glossary of Treasury	Terms				
Docur	nents In Members' Roo	ms				
1.	None					
Equal	ty Impact Assessment					
	Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.					
Privac	y Impact Assessment					
	Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.					
Other	Background Document	S				
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.	Prudential Limits and Treasury Management Strategy 2017/18 to 2020/21	Item 76
2.	Prudential Limits and Treasury Management Mid Year Review 2017/18	Item 10



Appendix 1

TREASURY MANAGEMENT POLICY STATEMENT

1. INTRODUCTION AND BACKGROUND

- 1.1. In accordance with CIPFA's Code of Practice for Treasury Management in the Public Services the Council has regard to the key recommendations when determining the current strategy.
- 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 the 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.

Appendix 2

EXISTING INVESTMENT & DEBT PORTFOLIO POSITION AND PROJECTIONS

	31-Mar-17	31-Mar-17	31-Dec-17	31-Dec-17	31-Mar-18
	Balance	Average	Balance	Average	Estimated
		Rate		Yield/	Balance
				Rate	
	£M	%	£M	%	£M
External Borrowing:					
Public Works Loan	220.30	3.27	211.80	3.32	208.81
LOBO Loans from Banks	9.00	4.86	9.00	4.86	9.00
Long Term Borrowing	229.30	3.33	220.80	3.43	217.81
Short Term Borrowing					
Fixed Rate – Market	30.35	0.40	23.35	0.56	48.54
Total External Borrowing	259.65	3.14	244.15	3.30	266.35
Other Long Term Liabilities					
PFI Schemes	62.26	9.51	62.26	8.47	60.42
Deferred Debt Charges (HCC)	14.92	3.08	14.55	2.74	14.55
Total Gross External Debt	336.83	4.36	320.96	3.96	341.32
Investments:					
Managed In-House					
Cash (Instant access)	(17.90)	0.83	(24.40)	0.37	(10.00)
Cash (Notice Account)	(5.00)	1.00	(4.00)	0.55	(3.00)
Short Term Bonds	(4.66)	2.03	(6.08)	1.30	(3.00)
Long Term Bonds	(14.72)	0.50	(7.62)	2.54	(7.62)
Managed Externally					
Pooled Funds (CCLA)	(17.00)	4.77	(27.00)	4.64	(27.00)
Total Treasury Investments	(59.28)	2.14	(69.10)	3.69	(50.62)
Net Debt	277.55		251.86		290.70



ECONOMIC AND INTEREST OUTLOOK

Appendix 3

The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, for January 2018 is detailed in table 1 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.

Table 1 - Economic Interest Rate Outlook

	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Average
Official Bank Rate														
Upstde rtsk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.21
Arlingolose Central Case	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downstde rtsk	0.00	0.00	0.00	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.17
3-month LIBID rate														$\vdash \vdash \vdash$
Upstde risk	0.10	0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.23
Arlingolose Central Case	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk	-0.10	-0.15	-0.15	-0.15	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.22
1-yr LIBID rate														==
Upside risk	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.28
Arlingolose Central Case	0.70	0.70	0.70	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.80	0.78
Downside risk	-0.20	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.15	-0.15	-0.15	-0.26
DOWNSIDE FISK	-0.20	-0.30	-0.30	-0.30	-0.30	-0.50	-0.30	-0.50	-0.30	-0.30	-0.13	-0.13	-0.13	-0.20
5-yr gilt yield														
Upstde rtsk	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.33
Arlingolose Central Case	0.75	0.80	0.80	0.80	0.85	0.90	0.90	0.95	0.95	1.00	1.05	1.10	1.15	0.92
Downstde rtsk	-0.20	-0.25	-0.25	-0.25	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.35
10-yr gilt yield														$\vdash \vdash \vdash$
Upstde risk	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.33
Arlingolose Central Case	1.25	1.25	1.25	1.25	1.30	1.30	1.35	1.40	1.45	1.50	1.55	1.55	1.60	1.38
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.34
00 4 11														
20-yr gilt yield														
Upstde rtsk	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.33
Arlingolose Central Case	1.85	1.85	1.85	1.85	1.90	1.90	1.95	1.95	2.00	2.05	2.05	2.05	2.10	1.95
Downside risk	-0.30	-0.25	-0.25	-0.30	-0.35	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.41
50-yr gilt yield														
Upstde rtsk	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.33
Arlingolose Central Case	1.70	1.70	1.70	1.70	1.75	1.80	1.85	1.90	1.95	1.95	1.95	1.95	2.00	1.84
Downside risk	-0.30	-0.25	-0.25	-0.30	-0.35	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.41

Underlying Assumptions:

- In a 7-2 vote, the MPC increased Bank Rate in November 2017 in line with market expectations to 0.5%. Market rate expectations are broadly unchanged since the rise and policymakers continue to emphasise that any prospective increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.
- Further potential movement in Bank Rate is reliant on economic data and the likely outcome of the EU negotiations. Policymakers have downwardly assessed the supply capacity of the UK economy, suggesting inflationary growth is more likely. However, the MPC will be wary of raising rates much further amid low business and household confidence.
- The UK economy faces a challenging outlook as the government continues to negotiate the country's exit from the European Union. While recent economic data has improved, it has done so from a low base: UK Q3 2017 GDP growth was 0.4%, after a 0.3% expansion in Q2. Forecasts for future GDP growth have generally been revised downwards.

- Household consumption growth, the driver of recent UK GDP growth, has softened following a contraction in real wages, despite both saving rates and consumer credit volumes indicating that some households continue to spend in the absence of wage growth. Policymakers have expressed concern about the continued expansion of consumer credit; any action taken will further dampen household spending.
- More recent labour market data suggested that employment has plateaued, although house prices (outside London) appear to be relatively resilient. However, both of these factors can also be seen in a negative light, displaying the structural lack of investment in the UK economy post financial crisis.
- The depreciation in sterling may assist the economy to rebalance away from spending. Export volumes will increase, helped by a stronger Eurozone economic expansion.
- Near-term global growth prospects have continued to improve and broaden, and expectations of inflation are subdued. Central banks are moving to reduce the level of monetary stimulus.

Forecast:

- The MPC has increased Bank Rate but future expectations for higher short term interest rates are subdued. On-going decisions remain data dependant and negotiations on exiting the EU cast a shadow over monetary policy decisions.
- The Arlingclose central case for Bank Rate is 0.5% over the medium term. The risks to the forecast are broadly balanced on both sides.
- The Arlingclose central case is for gilt yields to remain broadly stable across the medium term. Upward movement will be limited, although the UK government's seemingly deteriorating fiscal stance is an upside risk.

Forecast of Long Term Borrowing Requirement and Actual Debidix 4

Table 1

Movement on Estimated Long Term Borrowing Requirement - General Fund	2017/18 Forecast £M	2018/19 Forecast £M	2019/20 Forecast £M	2020/21 Forecast £M	2020/21 Forecast £M
Capital Programme	14.51				
Maturing Debt	21.15	25.21	73.87	20.02	11.43
Movement in Internal Borrowing	(16.40)	5.00	5.00	5.00	5.00
Less Repayment of Debt Principal	(5.35)	(5.71)	(6.01)	(5.62)	(5.69)
Plus MRP Holiday	5.35	0.67	0.00	0.00	0.00
New Borrowing Required	19.26	54.88	77.24	37.19	40.22

Table 2

Movement on Estimated Long Term Borrowing Requirement - HRA	2017/18 Forecast £M	2018/19 Forecast £M	2019/20 Forecast £M	2020/21 Forecast £M	2020/21 Forecast £M
Capital Programme	14.10	16.35	16.21	10.10	0.00
Maturing Debt	20.35	34.43	62.78	9.25	1.32
Movement in Internal Borrowing	0.00	0.00	0.00	0.00	0.00
Less Repayment of Debt Principal	(5.51)	(5.50)	(17.50)	(9.25)	(1.32)
New Borrowing Required	28.94	45.28	61.49	10.10	0.00

Table 3

Table 3					
Total Borrowing Requirement	2017/18	2018/19	2019/20	2020/21	2020/21
	Forecast	Forecast	Forecast	Forecast	Forecast
	£M	£M	£M	£M	£M
General Fund	19.26	54.88	77.24	37.19	40.22
Housing Revenue Account	28.94	45.28	61.49	10.10	0.00
Total Borrowing Need	48.20	100.16	138.73	47.29	40.22

Table 4

Borrowing	31/03/2018	31/03/2019	31/03/2020	31/03/2021	31/03/2022	
	Forecast	Forecast	Forecast	Forecast	Forecast	
	£M	£M	£M	£M	£M	
Long Term						
Balance brought forward	229.30	217.81	206.34	298.58	316.60	
Maturing in Year	(11.49)	(11.47)	(36.46)	(19.28)	(2.73)	
New Loans Raised in year			128.70	37.30	30.20	
Estimated Long Term Debt	217.81	206.34	298.58	316.60	344.07	
Short Term						
Balance brought forward	30.35	48.54	100.53	10.37	10.37	
Maturing in Year	(30.35)	(48.54)	(100.53)	(10.37)	(10.37)	
New Loans Raised in year	48.54	100.53	10.37	10.37	10.37	
Estimated Short Term Debt	48.54	100.53	10.37	10.37	10.37	
Estimated Total Debt	266.35	306.87	308.95	326.97	354.44	
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Appendix 5

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.

Asset Life Method - MRP:

As detailed under MRP, this is a charge to revenue to repay capital expenditure financed by borrowing. There are a number of options for a prudent provision for new borrowing under the Prudential system (for which no Government support is being given and is therefore self-financed) including the option to make provision over the estimated life of the asset for which the borrowing is undertaken.

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.

Capital Expenditure:

Expenditure on the acquisition, creation or enhancement of capital assets.

Capital Financing Requirement (CFR):

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.

Certainty Rate:

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.

CD's:

Certificates of Deposits with banks and building societies

Capital Receipts:

Money obtained on the sale of a capital asset.

Comprehensive Spending Review (CSR):

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).

Constant Net Asset Value (CNAV)

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.

Corporate Bonds:

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.

Cost of Carry:

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%.

Counterparty List:

List of approved financial institutions with which the Council can place investments with.

Covered Bond:

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 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.

CPIH:

Additional measure of consumer price inflation including a measure of owner occupiers' housing costs

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

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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.

Regularity Method - MRP:

As detailed under MRP, this is a charge to revenue to repay capital expenditure financed by borrowing. There are a number of options for a prudent provision and this is for debt prior to 2008 which is supported by the Government through the RSG system. Although regulation 28 is revoked by regulation 4(1) of the 2008 Regulations, authorities are able to calculate MRP as if it were still in force.

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 reporate 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 uprated 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.

DECISION-MAKER:			GOVERNANCE COMMITTEE					
SUBJECT:			CERTIFICATION OF CLAIMS AND RETURNS ANNUAL REPORT 2016/17					
DATE (OF DECIS	ION:	12 FEBRUARY 2018					
REPOR	RT OF:		EXTERNAL AUDITOR					
			CONTACT DETAILS					
AUTHO	R:	Name:	MARTIN YOUNG	Tel:	02380 382220			
		E-mail:	myoung1@uk.ey.com					
Directo	r	Name:	Helen Thompson	Tel:	02380 382099			
		E-mail:	HThompson2@uk.ey.com					
STATE	MENT OF	CONFID	ENTIALITY					
N/A								
BRIEF	SUMMAR	Υ						
The external auditor's report sets out their findings from the certification of the 2016/17 Housing Benefit subsidy claim								
RECON	MENDAT	TIONS:						
	(i)		he External Auditor's annual re s and Returns 2016/17 as attach					
REASC	NS FOR	REPORT	RECOMMENDATIONS					
1.	and prov	ride assur control rela	Committee's Terms of Reference rance that appropriate action is being ated issues identified by the external responsibility for oversight of the	ng take lal audi	n on risk and tors. Specifically			
ALTER	NATIVE C	PTIONS	CONSIDERED AND REJECTED					
2.	None.							
DETAIL	_ (Includir	ng consul	tation carried out)					
The Certification of Claims and Returns 2016/17 has been provided to relevant senior managers for comment.								
RESOURCE IMPLICATIONS								
<u>Capital/Revenue</u>								
4. N/A.								
Property/Other								
5. N/A.								
Pago 50								

LEGAL IMPLICATIONS						
<u>Statuto</u>	Statutory power to undertake proposals in the report:					
6.	N/A.					
Other L	egal Implications:					
7.	N/A.					
RISK M	ANAGEMENT IMPL	ICATIONS				
8.	N/A.					
POLICY	FRAMEWORK IMP	PLICATIONS				
9.	N/A.					
KEY DE	ECISION?	No				
WARDS	S/COMMUNITIES AF	FFECTED:	N/A			
	SL	JPPORTING D	<u>OCUMENTA</u>	<u>ATION</u>		
Append	dices					
1.	The Certification of	Claims and Re	eturns 2016/ <i>*</i>	17		
Docum	ents In Members' R	looms				
1.	None					
Equalit	y Impact Assessme	ent				
	implications/subjec	-	-	Equality and	No	
	Impact Assessmen	, ,	carried out.			
	Impact Assessme				T	
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.						
Other Background Documents						
Other Background documents available for inspection at: N/A						
Title of Background Paper(s)		Informat Schedul	Relevant Paragraph of the Access Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)			
	N/A					

Appendix 1

Certification of claims and returns annual report 2016-17

Southampton City Council

07 December 2017

Ernst & Young LLP







Ernst & Young LLP 1 More London Place London SE1 2AF Tel: + 44 20 7951 2000 Fax: + 44 20 7951 1345 ev.com

The Members Southampton City Council Civic Centre Southampton SO14 7LY 7 December 2017 Ref: HBReport1617

Direct line: 07974 007332 Email: HThompson2@uk.ey.com

Dear Members

Certification of claims and returns annual report 2016-17 Southampton City Council

We are pleased to report on our certification and other assurance work. This report summarises the results of our work on Southampton City Council's 2016-17 Housing Benefit subsidy claim.

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.

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 the Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government.

For 2016-17, 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.

Summary

We checked and certified the housing benefits subsidy claim with a total value of £108,428,329. We met the submission deadline. We issued a qualification letter, details of the matters identified are included in section 1. Our certification work also found minor errors which the Council corrected in their final claim form. The amendments had a marginal effect on the grant due.

Fees for certification and other returns work are summarised in section 2. The housing benefits subsidy claim fees for 2016-17 were published by the PSAA in March 2016 and are now available on the 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 12 February 2018.

Yours faithfully

Helen Thompson Associate Partner Ernst & Young LLP Enc

Contents

1.	Housing benefits subsidy claim	1
2.	2016-17 certification fees	3
3.	Looking forward	4

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1. Housing benefits subsidy claim

Scope of work	Results
Value of claim presented for certification	£108,428,482
Amended	Amended – subsidy reduced by £153.
Qualification letter	Yes
Fee – 2016-17	£15,208*
Fee – 2015-16	£19,524 *the 2016-17 fee has been reduced by 20% from £19,005 as a result of the Council agreeing to perform some of the initial testing themselves. We have done sufficient checking to satisfy ourselves that this testing was appropriately performed. This approach was reported to the Governance Committee in April 2017 as part of our progress report.

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. We found errors and carried out extended testing in three areas.

One area of extended testing identified an error which the Council amended. It had a small net impact on the claim. We have reported underpayments and the extrapolated value of other errors 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. These are the main issues we reported:

- Testing of the initial sample of Non HRA Rent Rebates identified one case (total value £3) where benefit had been underpaid as a result of the Authority miscalculating the claimant's average weekly income. Because errors miscalculating the claimant's average weekly income could result in overpayments, extended testing was required. This identified two further cases (total value £160) where benefit had been underpaid and one further case (total value £30) where benefit had been overpaid as a result of a similar error. The extrapolated error of benefit overpaid in our qualification letter was £3,185.
- Testing of the initial sample of Rent Allowances identified one case (total value £99) where benefit had been underpaid as a result of an earnings disregard not been awarded. In this case, no extended testing is required by our certificate instructions as the nature of the error detected could not give rise to an overpayment.
- Testing of the initial sample of Rent Allowances identified one case (total value £92) where benefit had been underpaid as a result of a dependant not been taken into account when awarding allowances. In this case, no extended testing is required by our certificate instructions as the nature of the error detected could not give rise to an overpayment.
- Testing of the initial sample of Rent Allowances identified one case (total value £40) where benefit had been underpaid as a result of the Authority miscalculating the claimant's average weekly income. Extended testing was required. This identified two further cases (total value £207) where benefit had been had been overpaid as a

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result of a similar error. The extrapolated error of benefit overpaid in our qualification letter was £28,845.

The Council has agreed to take the following actions to address the issues identified above:

- · all impacted cases will be corrected; and
- assessors will be reminded of the need to ensure correct entry of all payslip information when calculating earnings.

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2. 2016-17 certification fees

The PSAA determine a scale fee each year for the audit of claims and returns. For 2016-17, these scale fees were published by the PSAA in March 2016 and are now available on the PSAA's website (www.psaa.co.uk).

Claim or return	2016-17	2016-17	2015-16
	Actual fee £	Indicative fee £	Actual fee £
Housing benefits subsidy claim	15,208*	19,005	19,524

*the 2016-17 fee has been reduced by 20% from £19,005 as a result of the Council agreeing to perform some of the initial testing themselves. We have done sufficient checking to satisfy ourselves that this testing was appropriately performed. This approach was reported to the Governance Committee in April 2017 as part of our progress report. Under the terms of our contract, this reduction in fee must be approved by the PSAA. We are in the process of seeking this approval.

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3. Looking forward

2017-18

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 2017-18 is £19,524. This was set by PSAA and is based on final 2015-16 certification fees.

Details of individual indicative fees are available at the following web address: https://www.psaa.co.uk/audit-fees/201718-work-programme-and-scales-of-fees/individual-indicative-certification-fees/

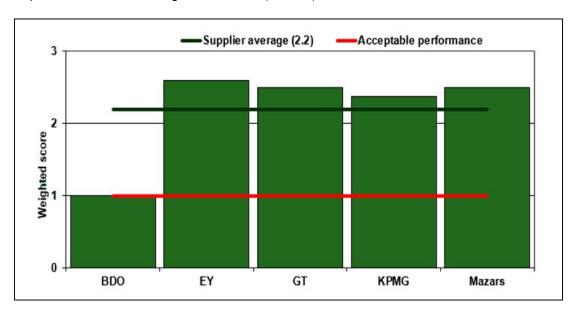
We must seek the agreement of PSAA to any proposed variations to these indicative certification fees. We will inform the Service Director – Finance and Commercialisation before seeking any such variation.

2018-19

From 2018-19, the Council will be responsible for appointing their own reporting accountant to undertake the certification of the housing benefit subsidy claim in accordance with the Housing Benefit Assurance Process (HBAP) requirements that are being established by the DWP. DWP's HBAP guidance is under consultation and is expected to be published around January 2018.

We would be pleased to undertake this work for you, and can provide a competitive quotation for this work. We have already engaged in discussions with Council Officers on this matter.

We currently provide HB subsidy certification to 106 clients, through our specialist Government & Public Sector team. We provide a quality service, and are proud that in the PSAA's latest Annual Regulatory and Compliance Report (July 2017) we score the highest of all providers, with an average score of 2.6 (out of 3).



As we also expect to be appointed by PSAA in December 2017 as your statutory auditor we can provide a comprehensive assurance service, delivering efficiencies for you and building on the knowledge and relationship we have established with your Housing Benefits service.

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EY | Assurance | Tax | Transactions | Advisory

Ernst & Young LLP

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Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

ey.com



DECISION-MAKE	R:	Governance Committee		
SUBJECT:		Local Appointment of External Auditors		
DATE OF DECIS	ION:	12 th February 2018		
REPORT OF:		Service Director Finance & Commercialisation		
	CONTACT DETAILS			
AUTHOR:	Name:	Peter Rogers Tel : 023 8083 2835		
	E-mail:	peter.rogers@southampton.gov.uk		
Director	Name:	Mel Creighton Tel: 023 8083 489		023 8083 4897
	E-mail:	mel.creighton@southampton.gov.uk		

STATEMENT OF CONFIDENTIALITY

N/A

BRIEF SUMMARY

This report provides an update regarding the appointment of an external auditor from 1st April 2018 and summaries that outcome of the procurement exercise undertaken by Public Sector Audit Appointments ('PSAA') in their capacity as an 'appointing person' (or 'sector led body'). This follows decision taken by Full Council in November 2016 that the Council should opt in to the national scheme rather than make its own auditor appointment.

RECOMMENDATIONS:

(i) To note to outcome of the procurement exercise undertaken by PSAA which has resulted in Ernst & Young LLP being appointed to audit the accounts of Southampton City Council for five years, from 2018/19 to 2022/23 and that scale fees are expected to reduce by approximately 23% compared to the 2017/18 fees.

REASONS FOR REPORT RECOMMENDATIONS

1. The appointment of Ernst & Young LLP via PSAA reflects the need for the Council to have external auditors in place from 1st April 2018. The appointment process has been undertaken by PSAA in accordance with the Local Audit and Accountability Act 2014 ('the Act') which allowed authorities to opt in for their external auditor to be appointed by an 'appointing person'.

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

2. Not applicable as the decision to opt in to the national sector led body was approved at Full Council on 16th November 2016.

DETAIL (Including consultation carried out)

- The Act brought to a close the Audit Commission and established transitional arrangements for the appointment of external auditors and the setting of audit fees for all local government and NHS bodies in England. Following closure of the Audit Commission, contracts let by them were novated to PSAA who were established to operate the transitional arrangements under powers delegated by the Secretary of State. PSAA is an independent, not-for-profit company limited by guarantee and established by the LGA.
- These transitional arrangements come to an end on 31 March 2018 at which Page 71

12.	PSAA have stated that they may be able to sustain the 23 per cent reduction for the full five years of the appointing period, but that it is not possible to be certain at this early stage. The key factors that could have an impact on future scale fees:
11.	The proposed scale fee for 2018/19 is £109,891 compared with the 2017/18 fee which was £142,715. PSAA have stated that they may be able to sustain the 23 per cent reduction for the full five years of the appointing period, but that it is not possible to be certain at this early stage.
Capital	/Revenue
RESOL	JRCE IMPLICATIONS
10.	Discussions will be held between the Council and Ernst & Young LLP in terms of the arrangements for the audit going forward.
9.	opted-in bodies was to ensure independence, and then to balance the remaining principles. PSAA have confirmed that the bid prices secured through this process are expected to result in a reduction of scale fees for all participating bodies of approximately 23% compared to the fees applicable for 2017/18. The PSAA Board will approve the final 2018/19 scale of fees for publication in March 2018.
	 Ensuring auditor independence; Meeting our contractual commitments; Accommodating joint/shared working arrangements where possible; Ensuring a blend of authority types for each audit firm; Taking account of a firm's principal locations; and Providing continuity of audit firm, if possible. The primary consideration in allocating proposed appointments to individual
8.	In respect of the appointment process the PSAA Board had regard to the following six principles:
7.	During the period August to December 2017 PSAA has consulted on and confirmed auditor appointments for opted-in bodies in. This followed a procurement exercise undertaken by PSAA which resulted in six firms being awarded an audit contract with them in June 2017.
6.	PSAA subsequently advised that 98% of the 494 eligible bodies decided to opt in to the national scheme rather than make their own auditor appointment.
5.	The Regulations required that a decision to opt in must be made by a meeting of the Council (meeting as a whole). A report was therefore taken to the Governance Committee on 14 th November 2016 and then to Full Council on 16 th November 2016 where it was agreed that the Council should accept PSAA's invitation to 'opt in' to the sector led option.
	The Local Audit (Appointing Person) Regulations 2015 ('the Regulations') made under the Act also included the provision for authorities to 'opt in' for their auditor to be appointed by an 'appointing person' with PSAA being specified by the Secretary of State as an 'appointing person' (or 'sector led body').

	period);
	 Any changes to the scope of auditors' work arising from changes to the Code of Audit Practice. A new code is required to be published every five years with the next code applicable from 2020/21; and
	Changes in financial reporting requirements: current scale fees reflect the audit work needed based on current financial reporting requirements. Changes to these requirements may have an impact on scale fees.
13.	It should be noted that PSAA is a not-for-profit company it does not therefore aim to generate surpluses. If, however, in the course of its activities any surplus funds are accumulated then they will be returned to opted-in bodies on a fair and proportionate basis.
Prope	rty/Other
14.	None
LEGA	L IMPLICATIONS
<u>Statut</u>	ory power to undertake proposals in the report:
15.	Section 7 of the Local Audit and Accountability Act 2014 ('the Act') requires a relevant authority to appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding year. Section 8 governs the procedure for appointment which is reserved to full Council.
16.	Section 12 of the Act makes provision for the failure to appoint a local auditor: the authority must immediately inform the Secretary of State, who may direct the authority to appoint the auditor named in the direction or appoint a local auditor on behalf of the authority.
17.	Section 17 gives the Secretary of State the power to make regulations in relation to an 'appointing person' specified by the Secretary of State. This power has been exercised in the Regulations (SI 192) and this gives the Secretary of State the ability to enable a Sector Led Body to become the appointing person. In July 2016 the Secretary of State specified PSAA as the appointing person.
<u>Other</u>	Legal Implications:
18.	None
RISK I	MANAGEMENT IMPLICATIONS
19.	The decision to opt in the sector led arrangement has ensured that the appointment of an audit firm has been made via a compliant procurement process, within required timescales and has delivered a cost saving.
POLIC	Y FRAMEWORK IMPLICATIONS
20.	None

KEY DECISION?	No	
WARDS/COMMUNITIES AF	FECTED:	Not applicable

SUPPORTING DOCUMENTATION Appendices 1. n/a

Documents In Members' Rooms

1.	None		
Equal	ity Impact Assessment		
	e implications/subject of the rep / Impact Assessment (ESIA) to b	• • •	No
Priva	cy Impact Assessment		·
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.			No
	Background Documents Background documents availab	ble for inspection at:	
Title of Background Paper(s) Relevant Paragraph of the Access Information Procedure Rules / Schedule 12A allowing document be Exempt/Confidential (if applic		Rules / document to	
1.	None		

DECISION-MAKER:		GOVERNANCE COMMITT	GOVERNANCE COMMITTEE			
SUBJECT:		EXTERNAL AUDIT PLAN YEAR ENDING 31 MARCI 2018		IG 31 MARCH		
DATE OF D	ECISION:	12 FEBRUARY 2018				
REPORT C	F:	EXTERNAL AUDITOR				
		CONTACT DETAILS				
AUTHOR:	Name:	MARTIN YOUNG	Tel:	02380 382220		
	E-mail	myoung1@uk.ey.com				
Director	Name:	Helen Thompson	Tel:	02380 382099		
	E-mail	HThompson2@uk.ey.com	<u>n</u>			
STATEMEN	NT OF CONFII	DENTIALITY				
NONE						
BRIEF SUM	MARY					
purpose is tauditors pro The plan su the develop	o provide the opposed scope a mmarises the	n sets out the how they will ca Governance Committee with a and audit approach for 2017/1 external auditor's initial asses ective audit for the Council, and	a basis to revi 18. ssment of the	ew the external key risks driving		
RECOMME	NDATIONS:					
(i)	(i) The Governance Committee is invited to comment on and note External Audit Plan Year Ending 31 March 2018 as attached.					
REASONS	FOR REPOR	RECOMMENDATIONS				
Na Re	itional Audit O esponsibilities i	ance with the Local Audit and fice's Code of Audit Practice, ssued by Public Sector Audit is and other professional requ	the Statemer Appointments	nt of		
1						

2. None.

DETAIL (Including consultation carried out)

The External Audit Plan Year Ending 31 March 2018 has been provided to relevant senior managers for comment.

RESOURCE IMPLICATIONS

Capital/Revenue

4. N/A.

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Prope	rty/Other				
5.	N/A.				
LEGA	LIMPLICATIONS				
Statut	ory power to under	take proposals	in the repor	<u>t</u> :	
6.	Local Audit and Adaptit Practice, the Appointments (PS requirements	Statement of F	Responsibilitie	s issued by Publi	c Sector Audi
<u>Other</u>	Legal Implications:				
7.	N/A.				
RISK	MANAGEMENT IMP	LICATIONS			
8.	N/A.				
POLIC	Y FRAMEWORK IM	IPLICATIONS			
9.	N/A.				
KEY D	ECISION?	No			
	<u>S</u>	UPPORTING D	OCUMENTA	TION	
Apper	ndices				
1.	The External Audi	t Plan Year End	ing 31 March	2018	
Docur	nents In Members'	Rooms			
1.	None				
Equal	ty Impact Assessm	ent			
	implications/subje Impact Assessmer	•	-	Equality and	No
Privac	y Impact Assessme	ent			
	implications/subje sment (PIA) to be c	-	t require a P	rivacy Impact	No
	Background Docun Background docun		for inspecti	on at: N/A	
Title o	f Background Pape	r(s)	Informat Schedul	t Paragraph of the ion Procedure Re e 12A allowing co pt/Confidential	tules / locument to
	N/A				





Private and Confidential Governance Committee Members Southampton City Council Civic Centre Southampton, Hampshire, SO14 7LY

Dear Governance Committee Members

Audit planning report

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Governance Committee with a basis to review our proposed audit approach and scope for the 2017/18 audit 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. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for the Council, and outlines our planned audit strategy in response to those risks.

This report is intended solely for the information and use of the Governance Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

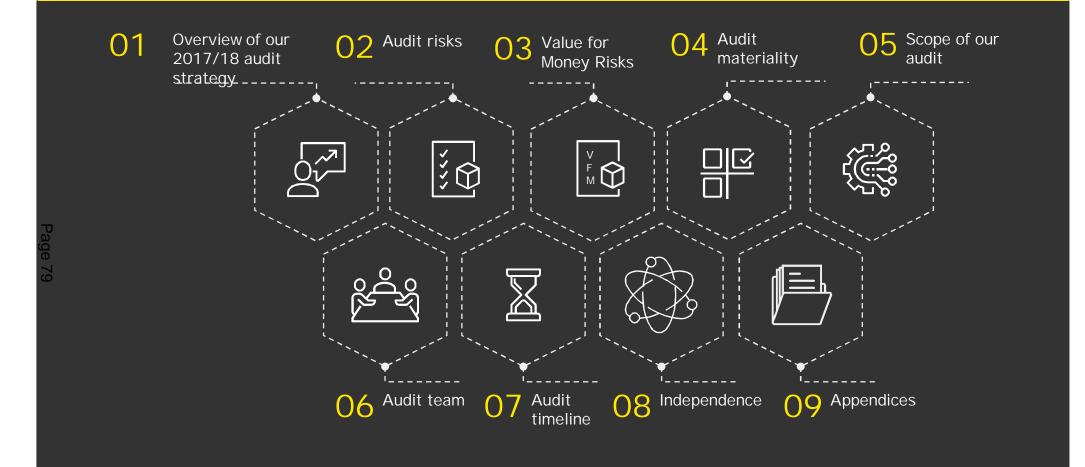
We welcome the opportunity to discuss this report with you on 12 February 2017 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

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

February 2018

Contents



In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued "Statement of responsibilities of auditors and audited bodies". It is available from the 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 (updated February 2017)" issued by the 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 in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Governance Committee and management of Southampton City Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Governance Committee and management of Southampton City Council those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Governance Committee and management of Southampton City Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.





Overview of our 2017/18 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Governance Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

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Audit risks a	nd areas	nt thelis
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Risk / area of focus	Risk identified	Change from PY	Details
Management override of controls	Significant and Fraud risk	No change in risk or focus from prior year	As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.
Valuation of Land and Buildings	Inherent risk	No change in risk or focus from prior year	The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.
🖶 ension Liability Valuation യ ര ര മ ച	Inherent risk	No change in risk or focus from prior year	Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. We are required to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.
Early close	Other area of audit focus	Increased focus	The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. The timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the accounts by 31 July.

Planning

Materiality has been set at £15.3m, which represents 2% of the prior years gross expenditure.

£15.3m Performance materiality

Performance materiality has been set at £11.5m, which represents 75% of planning materiality.

£11.5m

differences

£763k

We will report all uncorrected misstatements relating to the primary statements (comprehensive income and expenditure statement, balance sheet, movement in reserves statement, cash flow statement, housing revenue account and collection fund) greater than £763k. Other misstatements identified will be communicated to the extent that they merit the attention of the Governance Committee.

Audit scope

This Audit Plan covers the work that we plan to perform to provide you with:

- § our audit opinion on whether the financial statements of Southampton City Council give a true and fair view of the financial position as at 31 March 2018 and of the income and expenditure for the year then ended; and
- § our conclusion on the Council's arrangements to secure economy, efficiency and effectiveness.

We will also review and report to the National Audit Office (NAO), to the extent and in the form required by them, on the Council's Whole of Government Accounts return.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

strategic, operational and financial risks relevant to the financial developments in financial reporting and auditing standards; the quality of systems and processes;

- strategic, operational and financial risks relevant to the financial statements;

- changes in the business and regulatory environment; and,
- management's views on all of the above.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Council.



Our response to significant risks

Management override of controls

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What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

What will we do?

- · Identify fraud risks during the planning stages.
- Enquire of management about risks of fraud and the controls put in place to address those risks.
- Understanding the oversight given by those charged with governance of management's processes over fraud.
- Consider the effectiveness of management's controls designed to address the risk of fraud.
- Perform procedures sensitive to risk of management override including:
 - testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements:
 - reviewing accounting estimates for evidence of management bias (focusing on: the valuation of land and buildings, pension liability valuation, the Non Domestic Rates appeals provision and private finance Initiative models);
 - evaluating the business rationale for significant unusual transactions;
 - testing the appropriateness of minimum Revenue Provision charges;
 - testing capital additions;
 - testing the classification of expenditure treated as REFCUS (Revenue Expenditure Funded from Capital Under Statute;
 - testing transfers between the General Fund and the Housing Revenue Account;
 - testing adjustments made in the Movement in Reserves Statements; and
 - · reviewing any changes in accounting policy.

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

What is the risk/area of focus?

Valuation of Land and Buildings

The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the yearend balances recorded in the balance sheet.

Pension Liability Valuation

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The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Hampshire County Council.

The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet.

The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the County Council.

Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.

What will we do?

We will:

- consider the work performed by the Council's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work:
- sample testing key asset information used by the valuer in performing their valuation;
- consider the annual cycle of valuations to ensure that assets have been valued within
 a 5 year rolling programme as required by the Code for PPE and annually for IP. We
 have also considered if there are any specific changes to assets that have occurred
 and that these have been communicated to the valuer:
- review assets not subject to valuation in 2017/18 to confirm that the remaining asset base is not materially misstated;
- consider changes to useful economic lives as a result of the most recent valuation;
 and
- test accounting entries have been correctly processed in the financial statements,

We will:

- liaise with the auditors of Hampshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to Southampton City Council;
- assess the work of the Pension Fund actuary including the assumptions they have used by relying on the work of PWC Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team; and
- review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19.

Audit risks

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

What is the risk/area of focus?

Earlier deadline for production of the financial statements.

The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. The timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the accounts by 31 July.

These changes provide challenges for both the preparers and the auditors of the financial statements,

While these deadlines were met last year (in advance of need), it is important for both parties to continue to work together to ensure this success it repeated. As your auditor, we now have a more significant peak in our gudit work and a shorter period to complete the audit. Risks for auditors relate to delivery of all audits within same compressed timetable. Slippage at one client could potentially put delivery of others at risk.

We have identified the following additional specific risks to delivery at this Council:

- slippage in delivering data for analytics work; and
- the complex method the Council adopts to produce its financial statements from its ledger.

To mitigate this risk we request:

- that the Council streamlines it's methodology for producing its financial statement from its ledger;
- good quality draft financial statements and supporting working papers (including analytics data) by the agreed deadlines;
- appropriate Council staff to be available throughout the agreed audit period; and
- complete and prompt responses to audit questions.

If you are unable to meet key dates within our agreed timetable, we will notify you of the impact on the timing of your audit, which may be that we postpone your audit until later in the summer and redeploy the team to other work to meet deadlines elsewhere.

Where additional work is required to complete your audit, due to additional risks being identified, additional work being required as a result of scope changes, or poor audit evidence, we will notify you of the impact on the fee and the timing of the audit. Such circumstances may result in a delay to your audit while we complete other work elsewhere.

What will we do?

We:

- will work with the Council to facilitate early substantive testing (this
 is planned for March 2018);
- have provided the Council our working paper and data analytics requests for the early substantive testing in December 2017;
- have offered to run a local workshop for Southampton CC and Capita staff preparing the working papers to explain our requirements faceto-face and give them the opportunity to ask questions;
- have facilitated faster close workshops to provide an interactive forum for Local Authority accountants and auditors to share good practice and ideas to enable us all to achieve a successful faster closure of accounts for the 2017/18 financial year;
- have agreed the team and timing of each element of our work with management; and
- will agree with management the supporting working papers that we require to complete our audit during our planned visit in May / June 2018.



Value for Money

Background

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

For 2017/18 this is based on the overall evaluation criterion:

"In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people"

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- take informed decisions:
- deploy resources in a sustainable manner; and

work with partners and other third parties.

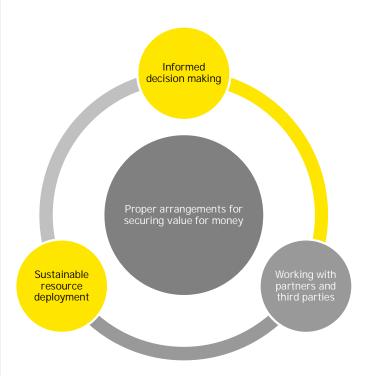
In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework Gor local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

We are only required to determine whether there are any risks that we consider significant, which the Code of Audit Practice defines as:

"A matter is significant if, in the auditor's professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public"

Our risk assessment supports the planning of sufficient work to enable us to deliver a safe conclusion on arrangements to secure value for money and enables us to determine the nature and extent of further work that may be required. If we do not identify any significant risks there is no requirement to carry out further work.

Our risk assessment has therefore considered both the potential financial impact of the issues we have identified, and also the likelihood that the issue will be of interest to local taxpayers, the Government and other stakeholders. This has resulted in the identification of the significant risks noted on the following page which we view as relevant to our value for money conclusion.





Value for Money Risks

What is the significant value for money risk?	What arrangements does the risk affect?	What will we do?
The Council's ability to deliver the savings required to support the sustainable delivery of services.	Deploy resources in a sustainable manner	 Our approach will focus on: reviewing achievement of the 2017/18 budget. A strong history of managing service delivery to budget, provides comfort over the Council's ability to set realistic and achievable budgets in the future; reviewing achievement of planned savings in 2017/18. A strong history of meeting planned efficiency and income generation targets provides comfort over the Council's ability to set realistic targets and achieve efficiency plans in the future; and reviewing the arrangement in place to deliver the savings plans in 2018/19 onwards.
Compliance with both Grocurement and Contracting policies as part of a sound system of internal control.	Take informed decisions	Our approach will focus on seeking assurance that current governance arrangements are robust and effective controls are in place to prevent, detect and correct any non compliance.



Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2017/18 has been set at £15.3m. This represents 2% of the Council's prior year gross expenditure. It will be reassessed throughout the audit process. We have provided supplemental information about audit materiality in Appendix C.



Key definitions

Planning materiality – the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Performance materiality – the amount we use to determine the extent of our audit procedures. We have set performance materiality at £11.5m, which represents 75% of planning materiality.

Audit difference threshold – we propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the comprehensive income and expenditure statement, balance sheet, housing revenue account and collection fund that have an effect on income or that relate to other comprehensive income.

Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement and movement in reserves statement or disclosures, and corrected misstatements will be communicated to the extent that they merit the attention of the Governance Committee, or are important from a qualitative perspective.



Our Audit Process and Strategy

Objective and Scope of our Audit scoping

Under the Code of Audit Practice our principal objectives are to review and report on the Council's financial statements and arrangements for securing economy, efficiency and effectiveness in its use of resources to the extent required by the relevant legislation and the requirements of the Code.

We issue an audit report that covers:

1. Financial statement audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK and Ireland).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we —will undertake during the course of our audit.

Procedures required by standards

Addressing the risk of fraud and error;

- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

Procedures required by the Code

- Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance; and
- Reviewing and reporting on the Whole of Government Accounts return, in line with the instructions issued by the NAO.
- 2. Arrangements for securing economy, efficiency and effectiveness (value for money)

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

- identifying and understanding the key processes and internal controls; and
- substantive tests of detail of transactions and amounts.

For 2017/18 we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Analytics

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

help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Governance Committee.

Internal audit

We regularly meet with the Chief Internal Auditor, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit work, where they raise issues that could have an impact on the financial statements, the annual governance statement of the narrative statement.





Audit team

Helen Thompson Associate Partner HThompson2@uk.ey.com Page 96 Martin Young Manager myoung1@uk.ey.com Sara Rowntree



∠ Audit team Use of specialists

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where either EY or third party specialists provide input for the current year audit are:

Area	Specialists	
Valuation of Land and Buildings	Southampton CC in house property valuers (management specialist) EY Valuations Team (auditor specialist)	
Aon Hewitt (management specialist) Pensions disclosure Pensions disclosure PwC (consulting actuary) and EY Actuaries (auditor specialists)		
L	EY Internal PFI Specialist (auditor specialist)	

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, consider their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Council's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

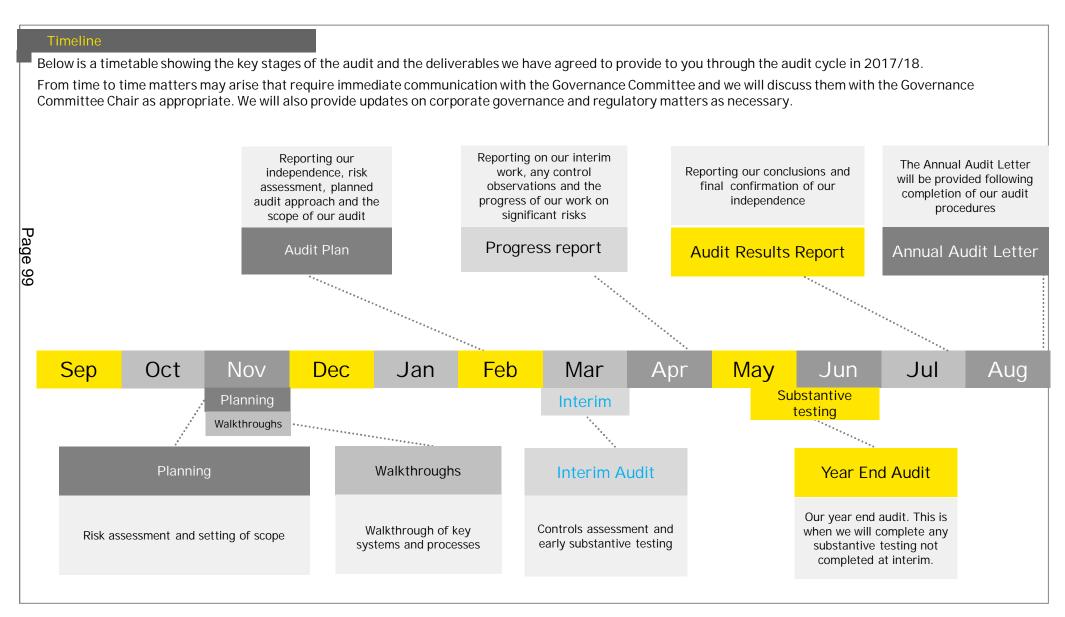
- analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- assess the reasonableness of the assumptions and methods used;
- consider the appropriateness of the timing of when the specialist carried out the work; and
- assess whether the substance of the specialist's findings are properly reflected in the financial statements.



Audit timeline

[OPTION 1]

Timetable of communication and deliverables







Introduction

The FRC Ethical Standard and ISA (UK) 260 "Communication of audit matters with those charged with governance", requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in June 2016, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications

Planning stage

- The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between the you, your affiliates and directors and us;
- The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review;
 - The overall assessment of threats and safeguards; Information about the general policies and process within EY to maintain objectivity and independence.
- Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard [note: additional wording should be included in the communication reflecting the client specific situation]

Final stage

- ▶ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed;
- Details of non-audit services provided and the fees charged in relation thereto;
- ▶ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us;
- ▶ Written confirmation that all covered persons are independent;
- Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy;
- Details of any contingent fee arrangements for non-audit services provided by us or our network firms;
 and
- ► An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

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

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



Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below (if any) to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non –audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Helen Thompson, your audit engagement associate partner, and the audit engagement team have not been compromised.

Self interest threats

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

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

At the time of writing, we have provided no non-audit services.

Result interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with FRC (Financial Reporting Council) Ethical Standard part 4.

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

Self review threats

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

At the time of writing, we have provided no non-audit services.

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

Management threats

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

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



Relationships, services and related threats and safeguards

Other threats

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

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

Other communications

EY Transparency Report 2017

Frnst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

etails of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm required to publish by law. The most recent version of this Report is for the year ended 1 July 2017 and can be found here:

http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2017





Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government.

PSAA has published a scale fee for all relevant bodies. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the NAO Code.

	Planned fee 2017/18	Scale fee 2017/18	Final Fee 2016/17
	£	£	£
Total Fee - Code work	142,715	142,715	147,101a
Tetal audit	142,715	142,715	147,101
Aher non-audit services not covered above (Housing Benefits)	19,524	19,524	15,204 ^b
Total other non-audit services	19,524	19,524	15,204
Total fees	162,239	162,239	162,305

The agreed fee presented is based on the following assumptions:

- ▶ officers meeting the agreed timetable of deliverables;
- ▶ our accounts opinion and value for money conclusion being unqualified;
- ▶ appropriate quality of documentation is provided by the Council; and
- ▶ the Council has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Council in advance.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

All fees exclude VAT

^aWe reported to you in our July 2017 Audit Results Report that for 2016/17 that a fee variation of £4,386 was agreed for additional work in: agreeing your financial statements to the general ledger (due to the complexity of the methodology) and assessing the impact of uncorrected errors.

^bWe reported to you in our July 2017 Audit Results Report that for 2016/17, the Council performed some of the initial Housing Benefit certification testing itself in return for a 20% or £3,801 reduction in our fee. This is subject to PSAA approval which has been sought. In 2017/18 we have agreed to perform this testing.



Required communications with the Governance Committee

We have detailed the communications that we must provide to the Governance Committee. Our Reporting to you Required communications What is reported? When and where Terms of engagement Confirmation by the Governance Committee of acceptance of terms of engagement as The statement of responsibilities serves as the written in the engagement letter signed by both parties. formal terms of engagement between the PSAA's appointed auditors and audited bodies. Our responsibilities Reminder of our responsibilities as set out in the engagement letter The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies. Planning and audit Communication of the planned scope and timing of the audit, any limitations and the Audit planning report proach significant risks identified. When communicating key audit matters this includes the most significant risks of material 106 misstatement (whether or not due to fraud) including those that have the greatest effect on the overall audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team Significant findings from Our view about the significant qualitative aspects of accounting practices including Audit results report accounting policies, accounting estimates and financial statement disclosures the audit Significant difficulties, if any, encountered during the audit Significant matters, if any, arising from the audit that were discussed with management Written representations that we are seeking Expected modifications to the audit report Other matters if any, significant to the oversight of the financial reporting process



Required communications with the Governance Committee (continued)

Required communications	What is reported?	When and where
Going concern	 Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: Whether the events or conditions constitute a material uncertainty Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements The adequacy of related disclosures in the financial statements 	Audit results report
Misstatements Ge 107	 Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation The effect of uncorrected misstatements related to prior periods A request that any uncorrected misstatement be corrected Corrected misstatements that are significant Material misstatements corrected by management 	Audit results report
Fraud	 Enquiries of the Governance Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity Any fraud that we have identified or information we have obtained that indicates that a fraud may exist A discussion of any other matters related to fraud 	Audit results report
Related parties	 Significant matters arising during the audit in connection with the entity's related parties including, when applicable: Non-disclosure by management Inappropriate authorisation and approval of transactions Disagreement over disclosures Non-compliance with laws and regulations Difficulty in identifying the party that ultimately controls the entity 	Audit results report



Required communications with the Governance Committee (continued)

		E Our Reporting to you
Required communications	What is reported?	When and where
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: The principal threats Safeguards adopted and their effectiveness An overall assessment of threats and safeguards Information about the general policies and process within the firm to maintain objectivity and independence	Audit Planning Report and Audit Results Report
ternal confirmations	 Management's refusal for us to request confirmations Inability to obtain relevant and reliable audit evidence from other procedures 	Audit results report
Consideration of laws and regulations	 Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off Enquiry of the Governance Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Governance Committee may be aware of 	Audit results report
Internal controls	Significant deficiencies in internal controls identified during the audit	Management letter / Audit results report
Representations	Written representations we are requesting from management and/or those charged with governance	Audit results report
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report



Appendix B

Required communications with the Governance Committee (continued) Our Reporting to you

Required communications	What is reported?	When and where
Auditors report	 Key audit matters that we will include in our auditor's report Any circumstances identified that affect the form and content of our auditor's report 	Audit results report
Fee Reporting	 Breakdown of fee information when the audit plan is agreed Breakdown of fee information at the completion of the audit Any non-audit work 	Audit planning report Audit results report
Certification work	Summary of certification work undertaken	Certification report
Page 109		

Additional audit information

Other required procedures during the course of the audit

In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.

Our responsibilities required by auditing standards

- Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the and Council's internal control.
- Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Concluding on the appropriateness of management's use of the going concern basis of accounting.
- Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Council to express an opinion on the consolidated financial statements. Reading other information contained in the financial statements, including the board's statement that the annual report is fair, balanced and understandable, the Governance Committee reporting appropriately addresses matters communicated by us to the Governance Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and
- Maintaining auditor independence.

²age 110



Additional audit information (continued)

Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines:

- The locations at which we conduct audit procedures to support the opinion given on the financial statements; and
- The level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the arcumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

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Agenda Item 10

DECISION-MAKER:		R:	Governance Committee		
SUBJECT: Annual Governance Statement 2017-18		8			
DATE	ATE OF DECISION: 12 th February 2018				
REPO	EPORT OF: Chief Financial Officer				
			CONTACT DETAILS		
AUTH	OR:	Name:	Peter Rogers	Tel:	023 8083 2835
		E-mail:	peter.rogers@southampton.gov	uk.	
Direct	tor	Name:	Mel Creighton	Tel:	023 8083 4897
		E-mail:	mel.creighton@southampton.go	v.uk	1
STATI	EMENT OF	CONFID	ENTIALITY		
None					
BRIEF	SUMMAR	Y			
the exincludi	tent to which ing how it has gements in the	h the Cou as monito he year, a	nual Governance Statement ('AGS') Incil has complied with its Code of Cored and evaluated the effectiveness and on any planned changes in the	Corpora of its	ate Governance, governance
RECO	MMENDAT	IONS:			
	(i)	(i) To note and approve the assurance gathering process to support the development of the 2017-18 Annual Governance Statement (Appendix 1).			
REAS	ONS FOR I	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.				
ALTE	RNATIVE C	PTIONS	CONSIDERED AND REJECTED		
2.		•	and publication of an AGS is a requit Regulations.	iireme	nt under the
DETA	IL (Includin	g consul	tation 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 purp is to prov arrangen	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	The AGS is produced following a review of the Council's governance arrangements. The review requires the systems and processes that			

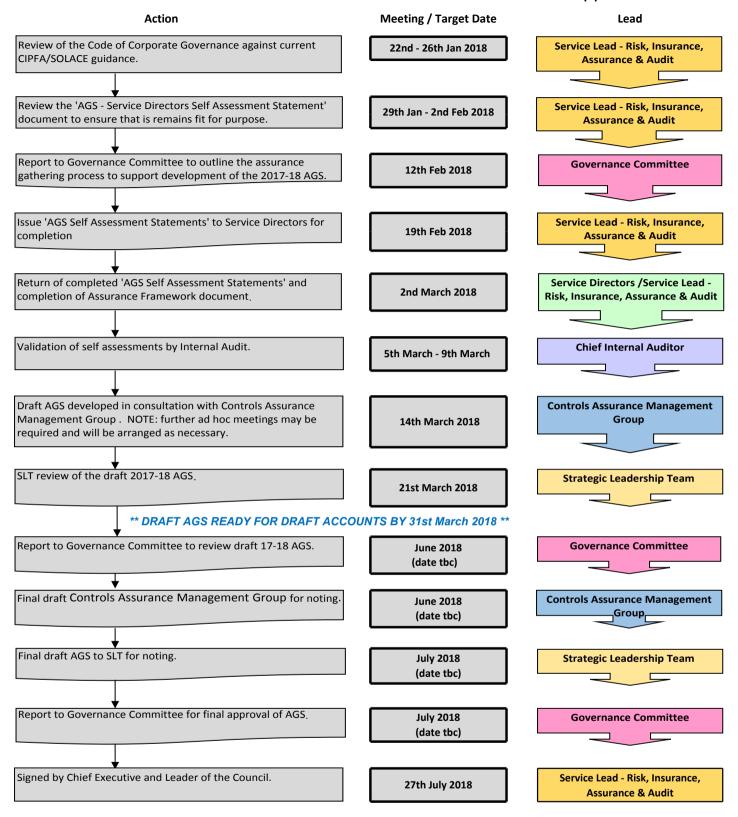
Page 113

	comprise the Council's corporate governance arrangements to be brought
	together and reviewed.
6.	The format and content of the 'assurance gathering process' remains largely unchanged from the previous year on the basis that it is considered to be aligned with good practice and noting that the council's external auditors, Ernst & Young, state in their 'Annual Audit Letter for the year ended 31 March 2017' that "The Governance Statement was consistent with our understanding of the Council". The only material change to the process is the timescales which have been amended in order that they are aligned with process in respect of production of the draft accounts.
7.	The key elements of the assurance gathering process comprise completion of the updated 'Assurance Framework' document together with 'Annual Governance - Self Assessment Statement' that is required to completed by each Service 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.
8.	The Council has in place a 'Controls Assurance Management Group' (comprising the Section 151 Officer, Chair of the Governance Committee, Monitoring Officer, Chief Strategy Officer and Chief Internal Auditor) which is responsible for evaluating the assurances and supporting evidence provided, and for drafting the AGS. This reflects CIPFA/Solace guidance which confirms that authorities should nominate an individual or group of individuals within the authority who have appropriate knowledge and expertise and levels of seniority to:
	 Consider the extent to which the authority complies with the principles of good governance; Identify systems, processes and documentation that provide evidence of compliance; Identify the individuals and committees responsible for monitoring and reviewing the systems, processes and documentation identified; Identify issues that have not been addressed in the authority and consider how they should be addressed; and Identify the individuals who would be responsible for undertaking the actions that are required.
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.
RESOU	RCE IMPLICATIONS
Capital	<u>Revenue</u>
10.	None
<u>Propert</u>	y/Other
11.	None
LEGAL	IMPLICATIONS
<u>Statuto</u>	ry power to undertake proposals in the report:
12.	The Accounts and Audit (England) Regulations 2015 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. Other Legal Implications:			
13. None			
RISK MANAGEMENT IMPLICATIONS			
The assurance gathering process as detailed in the body of the report together with process and timelines document (Appendix 1) manage in respect of compliance with the Accounts and Audit Regulations.			
POLICY FRAMEWORK IMPLICATIONS			
15. None			
KEY DECISION? No			
WARDS/COMMUNITIES AFFECTED: n/a			
Appendices			
Amandiac			
1. AGS 2017-18: Process and timelines			
Documents In Members' Rooms			
1. N/A			
Equality Impact Assessment			
Do the implications/subject of the report require an Equality and			
Safety Impact Assessment (ESIA) to be carried out.			
Privacy Impact Assessment Do the implications (subject of the report require a Brivacy Impact No.			
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.			
Other Background Documents			
Other Background documents available for inspection at:			
Title of Background Paper(s) Relevant Paragraph of the Ac Information Procedure Rules Schedule 12A allowing documents be Exempt/Confidential (if application).	/ nent to		



Agenda Item 10 Annual Governance Statement 2017/18 - Process and timelines, Applehaix 1





Agenda Item 11

DECI	ECISION-MAKER: GOVERNANCE COMMITTEE				
SUBJ	SUBJECT: Procurement - Sub £100k spend				
DATE	ATE OF DECISION: 12 February 2018				
REPC	ORT OF:		Service Director, Digital and Bus	siness	Operations
			CONTACT DETAILS		
AUTH	IOR:	Name:	Paul Paskins	Tel:	023 8083 4353
		E-mail:	paul.paskins@southampton.gov	/.uk	
Direc	tor	Name:	James Strachan	Tel:	023 8083 3436
		E-mail:	james.strachan@southampton.g	gov.uk	[
STAT	EMENT OF	CONFIDI	ENTIALITY		
N/A					
BRIE	F SUMMAR	Y			
entitle		ment - S	overnance Committee on the actic Sub 100k spend" which was pre 7.		•
RECC	OMMENDAT	IONS:			
	(i) The Governance Committee notes the progress in improving compliance and the further remedial actions which are being implemented.				
REAS	SONS FOR F	REPORT	RECOMMENDATIONS		
1.	The issues outlined in this paper are long-standing and challenging to resolve, but are being addressed through a series of robust remedial actions. The evidence demonstrates that these actions are having a marked positive effect, but there is still, however, significant non-compliance. Further remedial measures are being introduced over the coming months in order to make further improvements in compliance.				
ALTE	RNATIVE O	PTIONS	CONSIDERED AND REJECTED		
2.	N/A				
DETA	AL (Includin	g consul	tation carried out)		
	Backgrou	nd and S	cope		
3.	This report updates the Governance Committee on adherence with what is known as the 'Sub £100k' procurement process (i.e. procurement activities and projects with spend of less than £100k which is managed by the Sub £100k Team, which is part of the Procurement Service). Such spend is referred to as "In-Scope Spend" for the purpose of this report.				
4.	The Governance Committee are asked to note that if officers fail to adhere to the prescribed processes, the council may in some cases be missing opportunities to reduce some costs relating to the engagement of third party suppliers. Page 119				

5.	The Governance Committee are further asked to note that, in many cases, non-adherence to the process would have no effect on costs to the council and would not have meant that there has been any breach of legal obligations.
6.	There is no known evidence of any officer undertaking fraudulent activity in regard to the Sub £100k procurement process. If any fraudulent activity is identified as a result of the actions described in this report, then this would of course be dealt with in accordance with the council's Disciplinary Policy.
7.	The Supplier Management function was established in late 2016. Part of the remit of this function is to oversee the council's third party spend and the issues detailed in this report regarding adherence to the Sub £100k process were quickly identified. The supporting data was supplied to the associated audit by the Southern Internal Audit Partnership in respect of Procurement (Sub 100k) 2016/17 ("the audit report").
	The audit report found that "limited assurance could be placed on the effectiveness of the framework of risk management, control and governance designed to support the achievement of management objectives" and a number of management actions were put in place to address this.
8.	This report focusses on procurement requests of less than £100k in total value which should adhere to the Sub £100k process as set out in the Contract Procedure Rules (CPR's), which form part of the council's constitution.
	The arrangements for "feeder systems" (and other spend which does not pass through the Procurement Service on a case by case basis) are being reviewed and the related spend is not include within this report.
9.	This report also excludes activities which relate to spend below £100k which has been made against existing contractual obligations and exemptions which have been granted in accordance with the CPRs. In accordance with the scope of the audit report, it also excludes Integrated Commissioning Unit (ICU) spend, for which activity has not fully been undertaken by the Sub £100k function. The spend referred to in this paragraph 7 is referred to as 'Out of Scope' for the purpose of this report.
10.	CPRs mandate that all procurement activity above £1,000 in value is managed by the Sub 100k team to ensure that for these relatively low value, high volume requests; council officers are clear that they should not procure such requirements themselves.
	Issues
11.	The key issue identified by the Supplier Management team and highlighted in the audit report related to spend for which there is no current contract and where purchasing officers undertake the procurement themselves, in some cases without following the CPR process. For example, making a commitment to pay Page 120

before a purchase order has been authorised and/or directly engaging a supplier for an above £1,000 requirement without involving the Sub £100k team.

12. This report provides:

- an update against the actions recommended by the audit report and
- "non-adherence to process" data for the period between 1st July 2017 and 31st December 2017 compared to the previous 15 month period (1st April 2016 to 30th June 2017) which was presented in the Procurement Sub 100k spend" report in July 2017.

Data associated with the Sub 100k Procurement Process

13. The table below sets out the levels of adherence to the Sub £100k procurement process in the context of the total In-Scope and Out of Scope third party spend processed by the Procurement Service for each period.

	In-Scope spend	£ of In-Scope Spend not adhering to process	% of In- Scope Spend not adhering to process	Total In-Scope and Out of Scope spend
1st April 2016 to 31st March 2017 (12 months)	£27 million	£25.2 million	93%	£142 million
1 st April 2017 to 30 th June 2017 (3 months)	£2.5 million	£2.2 million	88%	£52 million
1 st July 2017 – 31 st July 2018 (3 months)	£2.03 million	£1.25 million	61%	£20.25 million
1 st August 2017 – 31 st December 2017 (3 months)	£1.48 million	£800k	54%	£14 million

Chart 1 - Summary of data 1st April 2016 – 31st December 2017

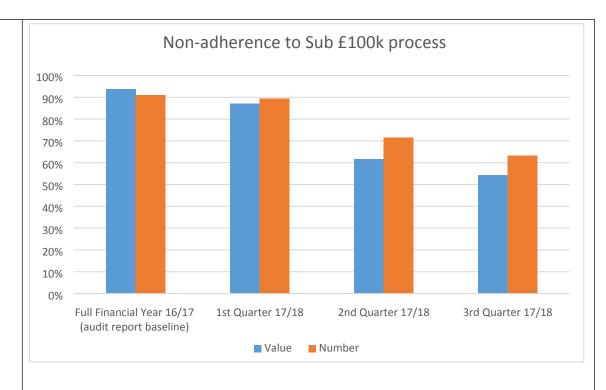


Chart 1 demonstrates that there has been a consistent increase in adherence to the Sub £100k process since data was last presented to the Governance Committee in July 2017.

This should be noted in the context of the overall below £100k spend across the council (incorporating both In-Scope Spend and spend referred to in paragraph 6 of this report) which is not represented in this data.

Remedial Action

- 14. An update against the actions recommended by the audit report and the previous "Procurement Sub 100k spend report" is set out in Appendix 1 to this report.
- In addition to the actions above, the following activity has been undertaken since July 2017 with the purpose of improving adherence rates with the Sub £100k process:
- A revised Procurement Strategy has been developed and was approved at the Cabinet meeting on 16th January 2018. This sets out the council's requirement for a centrally managed procurement service to achieve best value and compliancy for all council procurement activity.
- Development and implementation of the Procurement Service Development Plan which includes:
 - a. Developing (and rolling out during February March 2018) a mandatory e-learning training package for all relevant officers which focus on when and how council money can be spent.
 - b. Reviewing procurement processes and documentation including making more prominent the Sub £100k procurement process on Staff Stuff (the intranet);
 - c. Developing focused and clear process maps reflecting key "user

	journeys" and roles and responsibilities; d. Developing easy web links with service information via Staff Stuff including contact information, improved forms and guidance; e. Working with service areas to establish what their repeat needs are and procuring contractual arrangements to allow these needs to be met quickly and easily; f. Reviewing cross council spend to ensure that repeat requirements are effectively identified and procured compliantly and g. From April 2018, introducing a Requisitioning module in the upgraded Agresso system to help automate processes, make authorised purchasing quicker and strengthen system-led controls.				
18.	Working with the ICU service area to develop Sub £100k processes.				
19.	Development of the process to monitor adherence to the Sub £100k process.				
	Conclusions				
20.	The adherence data for the period July to December 2017 demonstrates a significant improvement in adherence to the Sub £100k process. The levels of non-compliance, however, remain significant.				
21.	It is anticipated that the completion of actions required by the audit report, coupled with the implementation of the e-learning module in early 2018 and improving guidance around the Sub £100k process will result in further improvements in compliance with the process over the next 12 months.				
22.	The Procurement and Contract Management Board (PCMB) will continue to monitor adherence to the Sub £100k process. Where appropriate, officers who do not adhere to the Sub £100k process may be subject to disciplinary proceedings in accordance with section 2.1 of the CPRs.				
RESO	URCE IMPLICATIONS				
Capita	al/Revenue				
23.	N/A				
Prope	rty/Other				
24.	N/A				
LEGA	L IMPLICATIONS				
	ory power to undertake proposals in the report:				
25.	N/A				
Other	Legal Implications:				
26.	N/A				
	MANAGEMENT IMPLICATIONS				
27.	See main body of this report.				

POLIC	POLICY FRAMEWORK IMPLICATIONS				
28.	28. N/A				
KEY [KEY DECISION? No				
WARE	WARDS/COMMUNITIES AFFECTED: All wards				
	·				
	SUPPORTING DOCUMENTATION				
Appendices					
1.	Progress against actions contained in audit report 2016-17				

Documents In Members' Rooms

1.	N/A				
Equality	Equality Impact Assessment				
	Do the implications/subject of the report require an Equality and Safety Impact Assessment (ESIA) to be carried out.				
Privacy	Impact Assessment				
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.				No	
	Other Background Documents Other Background documents available for inspection at: N/A				
Title of Background Paper(s) Relevant Paragraph of the Information Procedure Research Schedule 12A allowing do be Exempt/Confidential (in			Rules / locument to		
1.	N/A				

Agenda Item 11

Appendix 1

Appendix 1 – Progress against actions contained in audit report 2016-17

Action	Target date	Status
1.1 and 3.1 Develop a revised conformance dashboard with appropriate Quality Assurance process associated with it and a clear scope to ensure the compliance position is accurately reported.	End June 2017	Completed
1.2 and 3.2 Arrange for the new constituted Procurement and Contract Management Board (chaired by the COO) to review conformance on a monthly basis and allocate and review actions to address non-conformance.	End June 2017	Completed
1.3 Review processes to ensure that Procurement only have sight of categories of orders which are within scope for them to address.	End July 2017	Completed
2.1 Ensure that the conformance dashboard and aggregation data capture is effective.	End July 2017	Completed
2.2 Review how the Hays contract is being used and its fitness for purpose.	End July 2017	Complete (follow on actions are being developed)
4.1 Undertake a full review of the process associated with setting up new suppliers in Agresso, how this could effectively be restricted and how the process ensures compliance with Contract Procedure Rules.	End Sept 2017	Action superseded (being undertaken as part of the P2P element of the ERP)
4.2 Create and implement an action plan based on the outcome of the review described Management action 4.1.	End Oct 2017	Action superseded (being undertaken as part of the P2P element of the ERP)
5.1 Revise Contract Procedure Rules to incorporate the items observed in action plan 6.	End April 2017	Completed
5.2 Arrange for the approval of revised CPRs by Council.	End May 2017	Completed



DECISION-MAKER:		GOVERNANCE COMMITTEE			
SUBJECT:		INTERNAL AUDIT PROGRESS R	INTERNAL AUDIT PROGRESS REPORT 2017-18		
DATE OF DECIS	ION:	12 th February 2018			
REPORT OF:		CHIEF INTERNAL AUDITOR			
		CONTACT DETAILS			
AUTHOR:	Name:	Elizabeth Goodwin	Tel:	023 8083 4616	
E-mail:		Elizabeth.Goodwin@southampt	on.go	v.uk	
Director Name:		Mel Creighton Tel: 023 8083 4897			
E-mail:		Mel.Creighton@southampton.gov.uk			

STATEMENT OF CONFIDENTIALITY

There is a confidential appendix attached to this report, the confidentiality of which is based on Category 5 of paragraph 10.4 of the Council's Access to Information Procedure Rules. It is not in the public interest to disclose this information.

BRIEF SUMMARY

The Public Sector Internal Audit Standards 2017 (PSIAS), requires the Chief Internal Auditor (CIA) to provide periodical updates to the Governance Committee on:

- Progress made against the agreed annual audit plan.
- Results of audit activities and
- Management's response to risk that in the CIA's judgement maybe unacceptable to the Authority

All other PSIAS requirements are communicated in either the charter, strategy or annual audit opinion, which are reported separately to this committee at various times throughout the year.

throughout the year. Internal Audit Progress for the period 26th October 2017 to 26th January 2018 is covered in the attached Appendix 1. **RECOMMENDATIONS:** That the Governance Committee notes the Internal Audit Progress (i) report for the period 26th October 2017 to 26th January 2018. REASONS FOR REPORT RECOMMENDATIONS 1. In accordance with the Public Sector Internal Audit Standards the Chief Internal Auditor is required to provide an update on progress against the annual audit plan to the Governance Committee for information. ALTERNATIVE OPTIONS CONSIDERED AND REJECTED 2. None **DETAIL** (Including consultation carried out) 3. None RESOURCE IMPLICATIONS Page 127

Capita	Capital/Revenue				
4.	None				
Proper	ty/Other				
5.	None				
LEGAL	IMPLICATIONS				
Statuto	ory power to undertake proposals in the report:				
6.	The Accounts and Audit (England) Regulations 2015 state 'a relemble undertake an effective internal audit to evaluate the effective risk management, control and governance processes, taking into Public Sector Internal Auditing Standards.	veness of its			
Other I	Legal Implications:				
7.	None				
RISK N	MANAGEMENT IMPLICATIONS				
8.	The report is for note only, there is no decision to be made.				
POLIC	Y FRAMEWORK IMPLICATIONS				
9.	9. None				
KEY D	KEY DECISION? No				
WARD	WARDS/COMMUNITIES AFFECTED: None				
	SUPPORTING DOCUMENTATION				
Appendices					
1.	1. Internal Audit Progress Report for the period 26 th October 2017 to 26 th January 2018.				
2.	Confidential Audit Report.				
Docum	Documents In Members' Rooms				
1. None					
Equality Impact Assessment					
Do the implications/subject of the report require an Equality and Safety Impact Assessment (ESIA) to be carried out.					
Privac	Privacy Impact Assessment				
	Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.				
	Other Background Documents Other Background documents available for inspection at:				

applicable)

Relevant Paragraph of the Access to Information

Procedure Rules / Schedule 12A allowing

document to be Exempt/Confidential (if

Title of Background Paper(s):

None



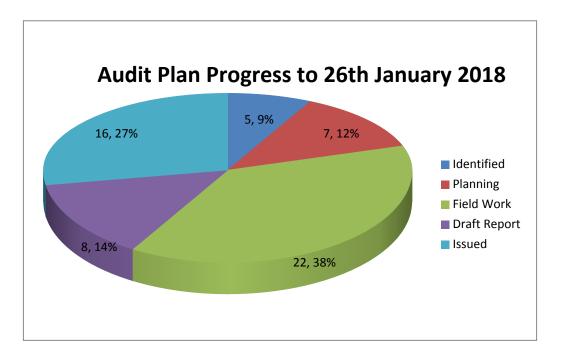
Internal Audit Progress Report 12th February 2018 Governance Committee

Elizabeth Goodwin - Chief Internal Auditor

Introduction: The internal audit function is a statutory function for all Local Authorities. Southampton City Council currently has a shared Chief Internal Auditor and an in house team of three members of staff, supported under a partnership agreement with Portsmouth City Council.

Purpose of report: The purpose of this report is to update the committee on the progress of the 2017/18 Audit Plan for the period 26th October 2017 to 26th January 2018 and highlight any areas of concern that may have arisen during the completed audits. In addition, changes to the audit plan and other unplanned pieces of work are also brought to the attention of the committee.

Audit Plan Progress:



27% of the Audit Plan has been completed as at 26th January 2018. 14% of the Audit Plan is in draft report stage. 53% of the Audit Plan is in progress. The remaining 9% has yet to commence. This is based on 58 audits.

Completed Audits between 26th October 2017 and 26th January 2018:

Project Name	Hub	Opinion	Direction	No. Critical Risk	No. High Risk	No. Medium Risk	No. Low Risk	Summary
F&C - Disabled Facilities Grant	Strategy	Reasonable Assurance	No previous audit	-	-	2	-	2 Medium risk exceptions arose. One relates to a lack of evidence regarding the 2016/17 grant determination sign off. The second relates to gaps in the information held relating to the grant expenditure.
F&C - Bus Subsidy	Strategy	Assurance	No previous audit	-	-	-	-	No exceptions arose
F&C - VAT	Strategy	Reasonable Assurance	2014/15 Substantial Assurance	-	-	1	-	1 Medium risk exception arose as a number of VAT numbers held against suppliers were not valid.
HR - Expenses Travel Subsistence	Strategy	Limited Assurance	No previous audit	-	2	1	-	2 high risk and 1 medium risk exceptions arose. The high risks relate to a lack of monitoring for employees with critical car usage and a lack of claim information/supporting evidence in enable VAT to be reclaimed. The medium risk relates to a lack of clarity for employees as to what they are entitled to claim for.
DBO - Email and Internet Controls	Operations	Limited Assurance	No previous audit	-	2	2	1	2 high, 2 medium and 1 low risk exception arose. The high risks relate to a low use of email encryption for sensitive emails. And accounts of former employees not being deleted. The medium risks relate to employee understanding of polices and a lack of correct authorisation on website access requests. The low risk relates to outdated IT policies.

HAC - Supported Housing Schemes	Operations	Limited Assurance	No previous audit	-	3	3	3	3 high, 3 medium and 3 low risk exceptions arose. The high risks relate to safe access, resident money being held in the safe and a weakness in security regarding personal data. The medium risks relate to Disclosure and Baring Service checks, TV licence payments and staff training. The low risks relate to lone working practice, banking process and family relationships within the staffing teams.
DBO - Tower Blocks	Operations	Limited Assurance	No previous audit	-	3	-	-	3 high risk exceptions arose. These relate to a lack of Fire Risk Assessments (FRA's) for all Tower Blocks, incomplete action plans from conducted FRA's and a lack of compliance with Statutory Inspections on a number of properties.
HAC - Appointeeships	Operations	No Assurance	No previous audit	-	8	2	-	Please see exempt item

Audits in Draft Report Stage:

Project Name	Hub	Project Status	Projected Reporting Date
L&G - Social Media	Strategy	Draft Report	April 2018
GRTH - Studio 144	Operations	Draft Report	April 2018
HAC - DOLs Deprivation of Liberty	Operations	Draft Report	April 2018
C&F - Home to School Transport	Operations	Draft Report	April 2018
F&C - Bank Account	Strategy	Draft Report	April 2018
F&C - Housing Rents and Debt Management	Strategy	Draft Report	April 2018
F&C - Purchase Cards	Strategy	Draft Report	April 2018

C&F - Fostering Arrangements	Operations	Draft Report	April 2018
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Audits in progress:

Project Name	Hub	Project Status	Projected Reporting Date
DBO - Disaster Recovery Business Continuity	Operations	Field Work	April 2018
DBO - CCTV	Operations	Field Work	April 2018
DBO - Procurement	Strategy	Field Work	April 2018
DBO - IT Telecommunications	Strategy	Field Work	April 2018
C&F - Adoption	Operations	Field Work	April 2018
HAC - Adults Safeguarding	Operations	Field Work	April 2018
ICU - Quality Assurance	Strategy	Field Work	April 2018
P&H - Public Health	Strategy	Field Work	April 2018
T&U - TranMan	Operations	Field Work	April 2018
F&C - Accounts Payable	Strategy	Field Work	April 2018
HAC - Direct Payments	Operations	Field Work	April 2018
C&F - Family Matters Grant	Operations	Field Work	April 2018
TRAN - Local Authority Trading Company	Transformation	Field Work	April 2018
F&C - Income and Collection Sites	Strategy	Field Work	April 2018
T&U - Water Quality	Operations	Field Work	April 2018
T&U - Asbestos	Operations	Field Work	April 2018
DBO - Contract Strategic Framework	Operations	Field Work	April 2018
HR - Recruitment	Strategy	Field Work	April 2018
DBO - British Gas	Operations	Field Work	April 2018
HAC - Residential Care Homes SCC run	Operations	Field Work	April 2018
DBO - Mobile Devices	Operations	Field Work	April 2018

HAC - Continuing Health Care	Operations	Field Work	April 2018	
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Additional Audit Plan Information:

In relation to the **Family Matters Grant** audit noted above. This audit requires a review and sign off of 4 claims submitted throughout the financial year. At the current time, 3 of the 4 claims have been reviewed and signed off. The remaining claim will be actioned in quarter 4. Until all 4 claims have been signed off, the audit will remain in 'Fieldwork' on these update reports.

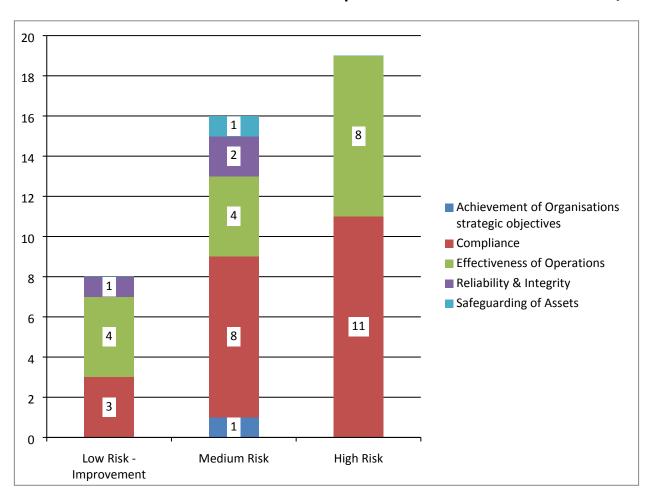
Unplanned Work:

Since 26th October 2017 to 26th January 2018, Internal Audit has provided advice in the following area. (For reference, Advice is only recorded when the time taken to provide the advice exceeds 1 hour.

- Direct Payments The Audit Manager is attending regular workshops regarding the changes proposed in the Direct Payments process.

 The purpose is to provide advice on risks and controls on changes to the current process.
- Pest Control A review of the processes for this service has taken place and Internal Audit has acted in a consultative capacity to assist.
- Housing Operations Advice was sought in relation to the control surrounding obsolete stock.

Exceptions Raised in Issued Audits 2017/18



Category	Example
Achievement of Organisational Objectives (AO)	Policy is out of date and not in line with current process
Compliance with Laws, Regulation and Policy (CMP)	Authority process /action is breaching legislation
Safeguarding of Assets (SOA)	Inventory of assets is not being maintained
Effectiveness of Operations (EOO)	Duplicate authorisation within a process
Reliability and Integrity of Data (R&I)	Reports used for decision making are inaccurate

The above table shows the number of exceptions raised based on the risk level and the category in which they were tested. At the current time, no significant trends are present in the data.

Audit Plan Status/Changes:

There have been no changes to the Audit Plan since the last update.

Areas of Concern:

1. Exempt Item

KEY:

KEY:	
Overall Assurance Levels:	Description / Examples
Assurance	No issues or minor improvements noted within the audit but based on the testing conducted, assurance can be placed that the activity is of low risk to the Authority
Reasonable Assurance	Control weaknesses or risks were identified but overall the activities do not pose significant risks to the Authority
Limited Assurance	Control weaknesses or risks were identified which pose a more significant risk to the Authority
No Assurance	Major individual issues identified or collectively a number of issues raised which could significantly impact the overall objectives of the activity that was subject to the Audit

Exception Priority Level	Description
Low Risk - Improvement	Very low risk exceptions or recommendations that are classed as improvements that are intended to help the service fine tune its control framework or improve service effectiveness and efficiency. An example of an improvement recommendation would be making changes to a filing system to improve the quality of the management trail.
Medium Risk	These are control weaknesses that may expose the system function or process to a key risk but the likelihood of the risk occurring is low.
High Risk	Action needs to be taken to address significant control weaknesses but over a reasonable timeframe rather than immediately. These issues are not "show stopping" but are still important to ensure that controls can be relied upon for the effective performance of the service or function. If not addressed, they can, over time, become critical. An example of an important exception would be the introduction of controls to detect and prevent fraud.
Critical Risk	Control weakness that could have a significant impact upon not only the system function or process objectives but also the achievement of the organisation's objectives in relation to: The efficient and effective use of resources, The safeguarding of assets, The preparation of reliable financial and operational information, Compliance with laws and regulations and corrective action needs to be taken immediately.

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Agenda Item 13 by virtue of paragraph number 5 of the Council's Access to information Procedure Rules

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