MID SUSSEX
DISTRICT COUNCIL

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15 February 2019

Dear Councillor,

A meeting of **AUDIT COMMITTEE** will be held in the **COUNCIL CHAMBER** at these offices on **MONDAY, 25TH FEBRUARY, 2019 at 7.00 pm** when your attendance is requested.

Yours sincerely,
KATHRYN HALL
Chief Executive

A G E N D A

		Pages
1.	To note Substitutes in Accordance with Council Procedure Rule 4 - Substitutes at Meetings of Committees etc.	
2.	To receive apologies for absence.	
3.	To receive Declarations of Interest from Members in respect of any matter on the Agenda.	
4.	To consider any items that the Chairman agrees to take as urgent business.	
5.	To confirm the Minutes of the meeting held on 20 November 2018.	**3 - 6**
6.	Internal Audit Monitoring Report 31 January 2019	**7 - 50**
7.	Three Year Internal Audit Plan	**51 - 56**
8.	Treasury Management Strategy Statement and Annual Investment Strategy 2019/20 to 2021/22	**57 - 94**
9.	Capital Strategy 2019/20	**95 - 102**
10.	External Audit Plan	**103 - 104**

To: **Members of Audit Committee:** Councillors J Belsey (Chairman), R de Mierre (Vice-Chair), A Boutrup, T Dorey, Andrew Lea, L Stockwell and N Walker

Minutes of a meeting of Audit Committee held on Tuesday, 20th November, 2018 from 7.00 pm - 7.25 pm

Present: J Belsey (Chairman)
R de Mierre (Vice-Chair)

T Dorey Andrew Lea N Walker

Absent: Councillors A Boutrup and L Stockwell

Also Present: Judy Llewellyn-Burke
(Cabinet Member for Finance and Economic Growth)
Tom Clark, Head of Regulatory Services
Gillian Edwards, Audit and Risk Manager Crawley Borough Council
Peter Stuart, Head of Corporate Resources and Section 151 Officer
Alison Hammond, Democratic Services Officer

1. TO NOTE SUBSTITUTES IN ACCORDANCE WITH COUNCIL PROCEDURE RULE 4 - SUBSTITUTES AT MEETINGS OF COMMITTEES ETC.

None.

2. TO RECEIVE APOLOGIES FOR ABSENCE.

Apologies were received from Councillors Boutrup and Stockwell.

3. TO RECEIVE DECLARATIONS OF INTEREST FROM MEMBERS IN RESPECT OF ANY MATTER ON THE AGENDA.

Councillor Andrew Lea declared a personal interest as a serving Member of West Sussex County Council.

4. TO CONFIRM THE MINUTES OF THE PREVIOUS MEETING.

The Minutes of the meeting of the Committee held on 5 September 2018 were agreed as correct record and signed by the Chairman after noting that the post implementation presentation on XCD and update report on cyber threats would now be provided in February. In response to a Members question it was noted that a sentence was incomplete in the Internal Audit monitoring report. It should have read "Whilst virus protection measures were in place, they were bypassed by a member of staff googling the website and going through the link".

5. TO CONSIDER ANY ITEMS THAT THE CHAIRMAN AGREES TO TAKE AS URGENT BUSINESS.

None.

6. REVIEW OF TREASURY MANAGEMENT ACTIVITY 1 APRIL - 30 SEPTEMBER 2018.

Peter Stuart, Head of Corporate Resources introduced the report which stated that all transactions were in order and the performance of the service had met the requirements of the Service Level Agreement (SLA) with our shared services provider. He explained the key points which were that the shared service had adhered to all borrowing limits and counterparty lending limits approved in the Treasury Management Strategy Statement; interest earned on investments was significantly higher than forecast, whilst interest on borrowing is in line with the budget. He highlighted the revised estimates for Capital Expenditure and noted that the capital receipts, Hurst Farm site, were now expected mid to late 2019/20 and not as previously reported.

In response to a Members question the Head of Corporate Resources confirmed that the revised figures had already been presented to Cabinet in the Budget Management Report. The Chairman noted that any changes would have been authorised and requested that a copy of the report be circulated to the Committee Members.

RESOLVED

The Committee received and noted the contents of the report:

(i) that no new borrowing has been necessary in the 6 months to 30th September 2018 and the outstanding borrowing has reduced from £12.698m at 31 March 2018 to £12.635m. An additional £5m will be repaid on 19th November 2018.

(ii) the increase in investments from £31.55m at 31 March 2018 to £44.27m at 30 September 2018 (both figures exclude the £6m investment in the CCLA Local Authorities' Property Fund); and

The Committee approved the amendment of the Treasury Management Strategy Statement and the Annual Investment Strategy to remove the minimum sovereign credit rating requirement from investments in UK institutions. In the unlikely event that the UK's sovereign rating is downgraded, the Council must still be able to invest in UK banks and building societies.

7. INTERNAL AUDIT - MONITORING REPORT 30 JUNE 2018.

Gillian Edwards, Audit and Risk Manager introduced the report which noted that the purpose of the report was twofold; to update the Committee on the progress of the 2018/2019 Internal Audit Plan and to report on the progress made in implementing previously agreed recommendations. She also informed the Committee that a Substantial Assurance had been provided following an audit on Taxi and Private Hire Drivers Licenses. Other work that had been undertaken in the period was listed in Appendix A. The Audit and Risk Manager noted that the Business Unit Leader for Revenues and Benefits had identified Data Tank through a procurement process for a wider Single Person Discount (SPD) review that also investigates data matches, such as the National Fraud Initiative (NFI) Data Matching, and the matches have been passed to this company for investigation. She commented that 4,000 letters had now been sent to review the SPD status and advised that an update report would follow in February 2019. The audit plan should be substantially completed by

31 March 2019 and additional resources were available if required to ensure the deadline is met. It was noted that acronyms should be listed in full in the report, for the first time it is used.

In response to a Members question regarding the potential impact of Brexit, the External Audit and Risk Manager noted that she currently had no proposals and would wait for recommendations from the Auditors.

She confirmed that under an exemption in the General Data Protection Regulations (GDPR) the Council could legitimately use personal data for the detection of crime and any data used is encrypted and securely uploaded.

RESOLVED

The Committee received and noted the report.

8. COMMITTEE WORK PROGRAMME

Members were asked to note the Work Programme. Several Members commented on the number of the reports that had been rescheduled for the February meeting. A discussion was held to determine whether the Chairman and Vice-Chairman could deal with non-urgent reports. However the Committee meetings should be held to ensure transparency to the Public.

RESOLVED

That the Committee Work Programme for 2018/19 be noted accordingly.

9. QUESTIONS PURSUANT TO COUNCIL PROCEDURE RULE 10.2 DUE NOTICE OF WHICH HAS BEEN GIVEN.

None.

The meeting finished at 7.25 pm

Chairman

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INTERNAL AUDIT – MONITORING REPORT 31st January 2019

REPORT OF: Audit and Risk Manager
Contact Officer: Gillian Edwards
Email: gillian.edwards@midsussex.gov.uk Tel: 01444 477241
Wards Affected: All MSDC Wards
Key Decision: No
Report to: Audit Committee
25th February 2019

Purpose of Report

1. The purpose of this report is twofold; to update the Committee on the progress of the 2018/2019 Internal Audit Plan and to report on the progress made in implementing previously agreed recommendations.

Recommendation

2. The Committee is asked to receive this report.

Background

3. Work Completed

Since the last meeting of this Committee in November, we have completed the following audits:

Payroll
High Priority findings – 2 – please see section 5 for details.
Medium Priority findings – 5

The medium priority findings that we identified related to the following:

- Job descriptions need to be updated to reflect the changes made by the introduction of the new Payroll system – *agreed implementation date - 28th February 2019*

- Training of additional staff on the Payroll system is needed to provide cover if the Payroll Manager is absent – *agreed implementation date - 31st March 2019*

- Checks are not being made on overtime to ensure that if paid, flexi leave is not also claimed – *agreed implementation date - 31st January 2019*
Status of agreed action –implemented.

- We identified on example where a person working at the Council had approved the overtime of a close relative – *agreed implementation date – 31st January 2019*
Status of agreed action – implemented.

- Payroll checklists are not signed by the Payroll Manager and the Payroll Officer to confirm the checks that they have made – *agreed implementation date – 31st January 2019*
Status of agreed action –implemented.

Income Collection
There are no findings to report.

Payments (Creditors)
Medium Priority findings – 1

This medium priority finding related to the absence of an independent check when an invoice is received that contains different bank details than those recorded on the Payments system. In such cases, the bank details are changed by Finance staff to that shown on the invoice. This is an area that is vulnerable to fraud.

It was confirmed that all relevant staff have been advised of the requirement to independently confirm with the business that the changes to bank details are genuine, and to make a record of this check.
Status of agreed action – implemented immediately.

Treasury Management
There are no findings to report.

Housing Benefits
High Priority findings – 1 – please see section 5 for details.
Medium priority findings – 3

The medium priority findings that we identified related to the following:

- Procedure notes for the Housing Benefits section have not been updated to reflect the new structure and processes that are not in place – *agreed implementation date – ongoing. Whilst a date for completion had not been set, this is an ongoing piece of work, and we will report progress towards this at the next meeting of this Committee.*
  Status of agreed action – work in progress.

- From a sample of 20 overpayments reviewed, we identified that two were not pursued in a timely manner. This was due to other priorities during the restructure – *agreed implementation date – 31st January 2019.*
  Status of agreed action –implemented.

- Whilst a review is currently being undertaken to confirm that access to the Housing Benefit system is appropriately restricted, this is not yet complete - – *agreed implementation date – 18th March 2019.*
  Status of agreed action – not yet due for implementation.

4. Work in Progress

The reviews in progress and other work that has been undertaken in the period are shown at Appendix A.

All work has been planned and allocated to Audit staff and we are confident that the audit plan will be substantially complete by 31st March 2019.

5. High priority findings in this period

Payroll Audit 2018/2019

High Priority Finding 1

During our previous audit for 2017/2018, an agreed action in the Management Action Plan for Payroll was that procedures would be completed was that the Payroll Manager should update her written or electronic files with the changes in the Payroll routines following the introduction of XCD in 2017. The Management Response stated that there was a plan to combine the procedures that the payroll consultant provided and information available through salesforce (XCD); and local requirements. This agreed action was originally due for implementation by 20th September 2018.

However, during our 2018/2019 Internal audit, we found that this agreed action has not been completed and therefore written Payroll procedures are not in place in place to include the new XCD system. This exposes the Council to the risk of disruption to the Payroll process if the Payroll Manager is absent for the Payroll processing to be completed. The Payroll Manager has advised that in the event of her absence the Council could engage staff from XCD to produce the Council's Payroll or use existing HR or Systems staff. However without any Council specific Payroll procedures in place this would be difficult.

Action has been agreed, to be implemented by 28th February 2019, that the Payroll Manager should update her written or electronic procedures with the changes in the Payroll routines following the introduction of XCD in 2017. This should be completed as a matter of urgency.

High Priority Finding 2

There is not a separate audit trail for when the Payroll Manager and the Payroll Officer makes a change to their salaries or benefits which under the XCD system are referred to as the Rewards. We were advised that there is an "unwritten rule" that neither of these employees can change their Rewards in the XCD system. However there is a risk that such changes could be made without any Management approval. The only compensating control is that Finance monitor the budget versus cost for each Business Unit at a post level but there is no guarantee that any unauthorised salary payments would be detected by this control.

As a final check, we tested the Payroll transactions for both the Payroll Manager and the Payroll Officer and that nothing untoward was found.

Action has been agreed, to be implemented by 28th February 2019, whereby the BUL HR, Training and Payroll should work with XCD to create a report that would run whenever there are any changes to the Rewards module for the two staff responsible for Payroll data input and checking.

It was also agreed that the BUL HR, Training and Payroll would work with XCD to create a report that would run whenever there are any changes to the Rewards module for the two staff responsible for Payroll data input and checking.

Progress towards implementation of these will be reported at the next meeting of this Committee.

Housing Benefits 2018/2019

High Priority Finding 1

We reviewed the Declaration of Interests forms completed by Revenues and Benefits staff to prevent them from processing any claims for a known associate or relative. Whilst we are advised that they were last completed in 2017, we cannot confirm this as the records were not available for review, and the most recent ones on file relate to October 2017. We understand that more recent declarations wee shredded in error.

New forms were issued to all Academy users on 12th December 2018 to be completed by 4th January 2019 and this has now been done.

6. Follow Up of Audits Previously Reported to the Audit Committee

None.

Background Papers

- Internal Audit reports relating to 2018/2019
- Working papers relating to 2018/2019

Appendix A

Internal Audit Plan 2018/2019

Progress Report as at 31st January 2019

Audit	Audit Plan Year	Audit Opinion- Assurance	Number of High Priority Findings	Comments
A. Work Completed in the Current Period				
Payroll	2018/19	Satisfactory	**2**	
Income Collection	2018/19	Substantial		
Payments (Creditors)	2018/19	Substantial		
Treasury Management	2018/19	Substantial		
Housing Benefits	2018/19	Satisfactory	**1**	
B. Work In Progress				
XCD Post Implementation Review	2018/19			
Sundry Debtors	2018/19			
Capital Accounting and Asset Management	2018/19			
Council Tax	2018/19			
NNDR	2018/19			
Follow Ups				
Payroll	2018/19			
Housing Benefits	2018/19			

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Mid Sussex District Council

Audit planning report

Year ended 31 March 2019

January 2019

Building a better working world

25 January 2019

Mid Sussex District Council
Oaklands Road
Haywards Heath
West Sussex
RH16 1SS

Dear Audit 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 Audit Committee with a basis to review our proposed audit approach and scope for the 2018/19 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 Audit 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 25 February 2019 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Kevin Suter

For and on behalf of Ernst & Young LLP

Contents

Public Sector Audit Appointments Ltd (PSAA) issued the "Statement of responsibilities of auditors and audited bodies". It is available from the PSAA website (https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/).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 and further guidance (updated April 2018)" 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 Audit Committee and management of Mid Sussex District Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, and management of Mid Sussex District 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 Audit Committee and management of Mid Sussex District 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.

01 Overview of our 2018/19 audit strategy

Overview of our 2018/19 audit strategy

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

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	As identified in ISA 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 would otherwise appear to be operating effectively.
Risk of incorrect capitalisation of revenue expenditure	Fraud risk	Existing risk with new focus	Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. We believe the risk of manipulation is most likely to manifest in the incorrect capitalisation of revenue expenditure, as there is an incentive to reduce expenditure which is funded from Council Tax.
Valuation of Land and Buildings/ Investment properties	Inherent risk	No change in risk or focus	The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represents significant balances in the Council's accounts and is subject to valuation changes and impairment reviews. Management is required to make material judgements about key assumptions and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.
Pension Liability Valuation	Inherent risk	No change in risk or focus	The Council's pension fund liability is a material estimated balance and the Code requires that this asset 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 Hymans Robertson. 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.

Overview of our 2018/19 audit strategy

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

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
IFRS 9 financial instruments	Inherent risk	New accounting standard	This new accounting standard is applicable for local authority accounts from the 2018/19 financial year and will change: • How financial assets are classified and measured; • How the impairment of financial assets are calculated; and • The disclosure requirements for financial assets. The Council will need to assess the impact of this accounting standard.
IFRS 15 Revenue from contracts with customers	Inherent risk	New accounting standard	This new accounting standard is applicable for local authority accounts from the 2018/19 financial year. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations. The Council will need to assess the impact of this accounting standard.

Materiality

Planning materiality
£1.47m

Materiality has been set at £1.47m, which represents 2% of the prior years gross expenditure on provision of services.

Performance materiality
£1.09m

Performance materiality has been set at £1.09m, which represents 75% of materiality.

Audit differences
£73k

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, and collection fund) greater than £73k. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2018/19 audit strategy

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 Mid Sussex District Council give a true and fair view of the financial position as at 31 March 2019 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 statements;
- Developments in financial reporting and auditing standards;
- The quality of systems and processes;
- 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.

Audit team changes

Partner in charge – Kevin Suter

Kevin takes over from Paul King as the Engagement Lead. Kevin has significant public sector audit experience over 20 years, with a portfolio of Local Authorities, Local Government Pension Funds and National Park Authority audits.

02 Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

	What is the risk?	What will we do?

Misstatements due to fraud or error *	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.
		We will undertake our standard procedures to address fraud risk, which include:
		➢ Inquiring 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.
		➢ Considering the effectiveness of management's controls designed to address the risk of fraud.
		➢ Performing mandatory procedures regardless of specifically identified fraud risks, including;
		  ➢ testing of journal entries and other adjustments in the preparation of the financial statements.
		  ➢ Review accounting estimates for evidence of management bias.
		  ➢ Evaluate the business rationale for significant unusual transactions.

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Risk of incorrect capitalisation of revenue expenditure*

Financial statement impact

Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income and expenditure accounts. We are focussing our testing on capital additions.

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

We believe the risk of manipulation is most likely to manifest in the incorrect capitalisation of revenue expenditure, as there is an incentive to reduce expenditure in the general fund which is funded from Council Tax.

This could then result in funding of that expenditure, that should properly be defined as revenue, through inappropriate sources such as capital receipts, capital grants, or borrowing

What will we do?

We will:

- Test PPE additions to ensure that the expenditure incurred and capitalised is clearly capital in nature.
- Test REFCUS, if material, to ensure that it is appropriate for the revenue expenditure incurred to be financed from ring fenced capital resources.
- Seek to identify and understand the basis for any significant journals transferring expenditure from revenue to capital codes within the general ledger.

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.

What is the risk/area of focus?	What will we do?
Valuation of Land and Buildings/Investment Properties The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and is subject to valuation changes and impairment reviews. Management is required to make material judgements about key assumptions and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.	We will: • Consider the work performed by the Council's valuers (Wilks, Head & Eve), including the adequacy of the scope of the work performed, their professional capabilities and the results of their work; • Challenge the assumptions used by the Council's valuer by reference to external evidence and our EY valuation specialists as necessary – for example, significant or unusual movements in valuation, difficult to value specialist assets, or investments in areas of the economy under stress such as retail; • Sample testing key asset information used by the valuers in performing their valuation (e.g. building areas to support valuations based on price per square metre); • 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 also consider 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 2018/19 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.

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.

What is the risk/area of focus?	What will we do?
Pension Liability Valuation 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 West Sussex 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. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We will: • Obtain assurances over the information supplied to the actuary in relation to the 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. • Where outturn information is available at the time we undertake our work after production of the Council's draft financial statements (for example the year-end actual valuation of pension fund assets), we will use this to inform our assessment of the accuracy of estimated information included in the financial statements and whether any adjustments are required.
IFRS 9 financial instruments This new accounting standard is applicable for local authority accounts from the 2018/19 financial year and will change: • How financial assets are classified and measured; • How the impairment of financial assets are calculated; and • The disclosure requirements for financial assets. There are transitional arrangements within the standard; and the 2018/19 CIPFA Code of practice on local authority accounting provides guidance on the application of IFRS 9.	We will: • Assess the Council's implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19; • Consider the classification and valuation of financial instrument assets; • Review the new expected credit loss model impairment calculations for assets; and • Check additional disclosure requirements.

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.

What is the risk/area of focus?	What will we do?
IFRS 15 Revenue from contracts with customers This new accounting standard is applicable for local authority accounts from the 2018/19 financial year. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations. The 2018/19 CIPFA Code of practice on local authority accounting provides guidance on the application of IFRS 15 and includes a useful flow diagram and commentary on the main sources of LG revenue and how they should be recognised. The impact on local authority accounting is likely to be limited as large revenue streams like council tax, non domestic rates and government grants will be outside the scope of IFRS 15. However where that standard is relevant, the recognition of revenue will change and new disclosure requirements introduced.	We will: • Assess the Council's implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19; • Consider application to the authority's revenue streams, and where the standard is relevant test to ensure revenue is recognised when (or as) it satisfies a performance obligation; and • Check additional disclosure requirements.

03 Value for Money Risks

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 2018/19 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 for 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.

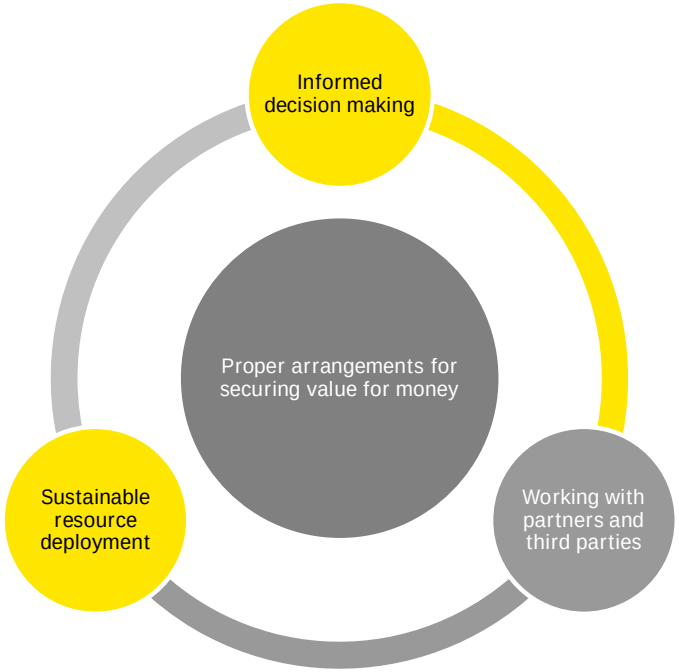
We are only required to determine whether there are any risks that we consider significant, which the Code of Audit Practice defines as:

"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. We consider business and operational risks insofar as they relate to proper arrangements at both sector and organisation-specific level.

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. We've also considered the Council's progress on savings in 2018/19 to date, the medium term financial plan and the Council's history of delivery against such plans.

This has resulted in the identification of a significant risk relating to the Councils commitment to the purchase of local property (investment properties) to support the revenue position in the medium and long-term.



Value for money risks (continued)

Purchase of Investment Property

What is the risk?

The Council is under continuing financial pressure and needs to ensure it is financially resilient over the medium and long-term.
The Council's strategy involves the purchase of local property for rental purposes. This rental income would then be used to support the Council's expenditure.

There is a risk that the desired returns may not be achieved, or that the purchase price of these assets is not resilient in the medium and long-term.

This reflects upon the Council's arrangements for:

- Sustainable resource deployment; and
- Informed decision making.

What will we do?

Our approach will focus on reviewing:

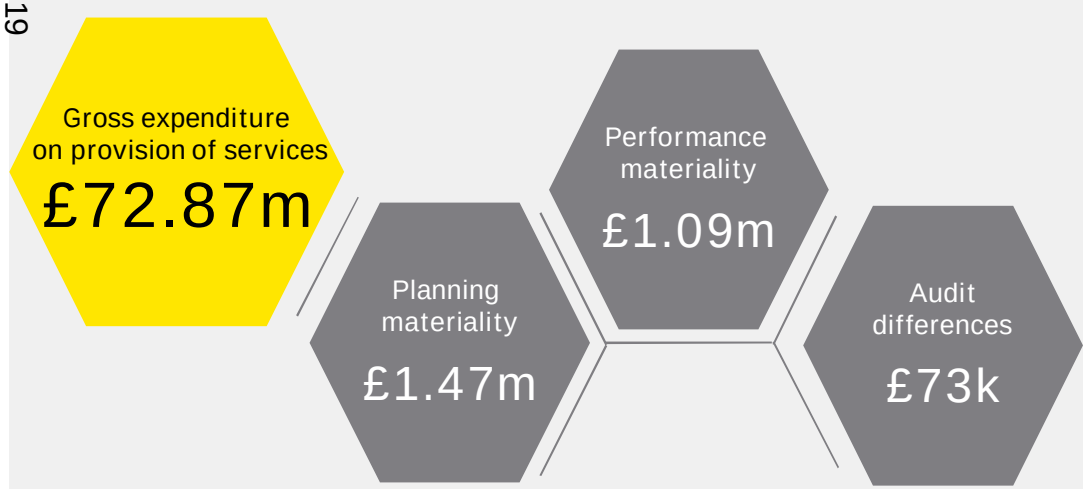
- any external advice obtained by the Council which has been relied upon to support this strategy. We shall also review the Council's response to this advice.
- any due diligence work that has been undertaken.
- that the proper decision making mechanisms have been followed prior to the purchase of these assets.
- the extent to which the Council has complied with key guidance such as the CIPFA Prudential code and statutory guidance on Local Authority Investments.

04 Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2018/19 has been set at £1.47m. This represents 2% of the Council's prior year gross expenditure on provision of services. It will be reassessed throughout the audit process. We have provided supplemental information about audit materiality in Appendix C.



We request that the Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

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 £1.09m which represents 75% of planning materiality. The rationale for using 75% is based on the anticipation of identifying few or no errors during the audit. This expectation has been built on our experience of the Council in the prior year.

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 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 audit committee, or are important from a qualitative perspective.

Specific materiality – We have set a materiality of £1,000 for sensitive disclosures such as the remuneration disclosures , related party transactions, members' allowances and exit packages. This reflects our understanding that an amount less than our materiality would influence the economic decisions of users of the financial statements in relation to this.

05 Scope of our audit

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).

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 Statement; 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 2018/19 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 Audit Committee.

Internal audit:
We will meet with the Head of Internal Audit, 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 plan, where they raise issues that could have an impact on the financial statements.

06 Audit team

Audit team

Audit team structure:

Kevin Suter
Associate Partner

Tom Wilkins
Manager

John Darlison
Team Lead

Working together with the Pension Fund

We are working together with officers to identify continuing improvements in communication and processes for the 2018-19 audit.

We will continue to keep our audit approach under review to streamline it where possible.

Audit team changes

Key changes to our team.

Kevin Suter, Associate Partner

- Kevin takes over from Paul King as the Associate Partner for the engagement. Kevin has extensive local government experience and has access to the wider EY network of local government auditors

John Darlison, Team Lead

- John takes over from Vivek Mistry as the Team Leader for the engagement. John was on our audit team in the prior year, supporting Vivek.

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	• Wilkes, Head and Eve – Management's RICS Registered Valuers • EY property valuers
Pensions disclosure	• EY Actuaries • PWC consulting actuary commissioned by NAO • Hymans Robertson- Management's Actuary

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering 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.

07 Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2018/19.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

Audit phase	Timetable	Audit committee timetable	Deliverables
Planning: Risk assessment and setting of scopes.	November		
	November		
Walkthrough of key systems and processes	December		
	January		
Interim audit testing	February	Audit Committee	Audit Planning Report
	March		
	April		
	May		
	June		
Year end audit Audit Completion procedures	July	Audit Committee	Audit Results Report Audit opinions and completion certificates
	August - October		Annual Audit Letter

08 Independence

Independence

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	**Final 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.	▸ 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 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 Kevin Suter, your audit engagement 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.

We believe that it is appropriate for us to undertake permissible non-audit services and we will comply with the policies that you have approved.

None of the services are prohibited under the FRC's ES or the National Audit Office's Auditor Guidance Note 01 and the services have been approved in accordance with your policy on pre-approval. The ratio of non audit fees to audits fees is not permitted to exceed 70%.

At the time of writing, we have proposed to under take the role of reporting accountant for the DWP's Housing Benefit Assurance Process (HBAP). We have determined appropriate safeguards.

A self 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 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.

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.

EY Transparency Report 2018

Ernst & 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.

Details 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 is required to publish by law. The most recent version of this Report is for the year ended 1 July 2018 and can be found here:

https://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018

09 Appendices

Appendix A

Fees

Public Sector Audit Appointments Ltd (PSAA) has published the fee scale for the audit of the 2018/19 accounts of opted-in principal local government and police 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 requirements of the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

	Planned fee 2018/19	Scale fee 2018/19	Final Fee 2017/18
	£	£	£
Total Fee – Code work (1)	38,917	38,917	50,542
Total audit	38,917	38,917	50,542
Other non-audit services not covered above (Housing Benefits) (2)	13,172	N/A	17,858
Total other non-audit services	13,172	N/A	17,858
Total fees	52,089	38,917	68,400

All fees exclude VAT

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.

Notes:

(1) Our 2018/19 Code work includes additional planned procedures highlighted in section two of this report to address the new accounting requirements of IFRS 9 Financial Instruments and IFRS 15 Revenue from contracts with customers. As at the date of our planning report the Council is yet to evidence their assessment of the impact of these standards, and so we cannot currently quantify the expected scale fee variation for these additional procedures. We will agree this with management, depending on the identified impact of the new standards.

(2) Certification of the Housing Benefit claim is no longer under the remit of PSAA. The fee quoted is the agreed and contracted fee for delivery of the certification audit assuming no errors identified. Errors which result in additional testing and reporting in the auditor report will be charged as an additional fee.

Required communications with the Audit Committee

We have detailed the communications that we must provide to the Audit Committee.

		Our Reporting to you
Required communications	What is reported?	When and where
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the 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 approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit planning report
Significant findings from the audit	• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures; • 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; and, • Other matters if any, significant to the oversight of the financial reporting process.	Audit results report

Required communications with the Audit Committee (continued)

		Our Reporting to you
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	• 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 Audit 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 Audit Committee (continued)

		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
External 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 Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	Audit results report
Internal controls	• Significant deficiencies in internal controls identified during the audit	Audit results report

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	What is reported?	When and where
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
Auditors 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

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 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, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and • Maintaining auditor independence.

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 circumstances 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.

THREE YEAR INTERNAL AUDIT PLAN

Report from:	Audit and Risk Manager
Contact Officer:	Gillian Edwards Email@ gillian.edwards@midsussex.gov.uk Tel: (01444) 477241
Wards Affected:	All
Key Decision:	No
Report to:	Audit Committee 25th February 2018

1. PURPOSE OF REPORT

To inform the Committee of the detailed work proposed for 2019/2020 and the overall Internal Audit Plan, for the three years 2019/2020, 2020/2021, and 2021/2022.

2. SUMMARY

2.1 The three year internal audit plan has been compiled to respond to the changes within the organisation, its structure and how its services are delivered, whilst also ensuring that key controls are effective.

2.2 The plan allows for examination of the main financial areas from a systems and ICT perspective, which is key to ensuring the Council's finances remain properly controlled, whilst also undertaking strategic and service based work each with a varying risk to the organisation.

2.3 The plan also includes some specific reviews from previous audit work, designed to ensure that agreed actions have been satisfactorily implemented and that the Council is being consistent in its approach year on year.

2.4 The plan continues to include coverage of specific key controls agreed with the External Auditor to support their year-end work as required.

2.5 It should be noted that the coverage in year 3 may be subject to amendment, based upon changing situations, risks identified, and priorities.

3. RECOMMENDATIONS

The Committee is asked to comment on the detailed Internal Audit Plan for 2019/2020 (Appendix A) and the 3 Year Internal Audit Plan (Appendix B).

4. INTRODUCTION AND BACKGROUND

4.1 The work of Internal Audit is managed through a risk-based planning process which this year comprises detailed one year and three year plans.

4.2 The purpose of this report is for the Committee to consider the proposed Internal Audit Plans.

5.0 INTERNAL AUDIT PLANS

Preparation

5.1 The preparation process for the detailed one year and three year plans included engagement with management, consideration of findings of previous audit work and the inclusion of fundamental systems, including the major financial systems.

5.2 The detailed plan for 2019/2020 is shown in Appendix A, with the three year plan in Appendix B.

Fundamental Systems

5.3 These are the main financial systems and as such, adequate control is key to the proper operation of the Council's financial affairs. The External Auditor no longer relies upon the work of Internal Audit in formulating their audit opinion, and test the systems themselves to gain assurance. These systems are still examined annually by internal audit and a total of 99 days is allocated for this work in 2019/2020, which represents 42% of the total available audit days.

Computer Audit

5.4 This category deals with examining the control of the Council's main computer systems and infrastructure. An ICT risk assessment is undertaken at the beginning of each financial year, to determine how the resources allocated to this area can be best utilised.

Risk Based and Corporate Audits

5.5 This area relates to work requested and/or having been identified by Internal or External audit as a key risk to the Council.

Follow Ups

5.6 It is important for the effectiveness of Internal Audit that there should be a process of following up previously agreed actions to ensure they are implemented satisfactorily and in a timely manner. A total of 10 days have been allocated for this work each year.

Contingency

5.7 After consultation with the Head of Corporate Resources, the number of audit days have been increased from 220 last year, to 236 days to allow coverage of areas identified as being necessary to include comprehensive coverage of areas where it is deemed the risk is sufficient to require this. There is no time allocated to contingency at present, however, if any additional resources were required, they would be agreed with the Head of Corporate Resources, and provided by Crawley Borough Council.

Management and Planning

5.8 In addition to undertaking the audits referred to above, Internal Audit also carry out a number of support and planning activities. These include liaison with the External Auditor to ensure the two functions complement each other and avoid duplication. In addition, we liaise with management to agree the audit programmes and scope, allocate appropriately skilled resources, provide guidance to management on internal issues and present to the Audit Committee.

Resources

5.9 The Internal Audit Service for the forthcoming financial year has a total of 236 allocated to it, with 220 days per annum in years two and three. This will be kept under constant review and any changes will be discussed and agree with the Head of Corporate Resources. This work will be managed by Gillian Edwards, Audit and Risk Manager at Crawley Borough Council, as part of the shared service arrangement. Specialists, including computer auditors, will be brought in as required.

6.0 Risk Assessment

6.1 This plan has been produced after engaging with stakeholders, consideration of the findings of Internal and External Audit and review of relevant documentation. There is scope for additional resources to be allocated to the plan, to cover unexpected eventualities and unforeseen risks, by agreement with the Head of Corporate Resources and the Audit and Risk Manager.

6.2 The three year plan is intended to focus on the strategic direction of the Council. Management Team are committed to Heads of Service taking responsibility for ensuring that controls are maintained within their areas of responsibility. If there are concerns over any issues, these can be discussed with Internal Audit for advice and there is sufficient flexibility in the plan to allow for this. Additionally, Heads of Service can ask Internal Audit to undertake examinations on a one off basis, subject to agreement by the Head of Corporate Resources.

7. Policy Context

This report explains how the Internal Audit function will contribute to the work of the Council Internal Audit is a statutory function required under the Accounts and Audit Regulations 2015.

8. Financial Implications

8.1 The detailed 2019/2020 Internal Audit Plan has been compiled to ensure it remains within the budget agreed with the Head of Corporate Resources.

Appendix A

Mid Sussex District Council Internal Audit Plan 2019/2020

	Systems	IT	Total	Comments
Fundamentals				
Housing Benefits	20		20	This work will ensure compliance
Council Tax	12		12	
				with Ernst &Young's requirements
NNDR	12		12	
Payroll	10		10	It will also include reviews to confirm
Income Collection (Cashiers)	8		8	
				that key controls are present in the
Treasury Management	5		5	
Payments (Creditors)	8		8	fundamental financial systems and
Sundry Debtors	8		8	
				and assess whether they are
Capital Accounting & Asset Management	7		7	
Budgetary Control	4		4	operating in a satisfactory manner.
FMS	5		5	
Sub Total	**99**	**0**	**99**	
Risk Based and Corporate				
Commercial Properties	8		8	
FMS Project Group Attend and Advise	5		5	
Housing Allocations	8		8	
Temporary Accommodation	8		8	
Refuse Collection – Contract Monitoring	8		8	
Anti-Fraud Work including NFI	30		30	
ICT Audits				
To be allocated		20	20	
Sub Total	**166**	**20**	**186**	
Follow Ups	10		10	
Contingency				
Sub Total	**176**	**20**	**196**	

	Systems	IT	Total	Comments
Management and Planning				
Committees	10		10	
Operational Management	15		15	
Head of Audit Time	15		15	To include preparation of Head of Audit Annual Report
Total Days	**216**	**20**	**236**	

Appendix B

Mid Sussex District Council – 3 Year Internal Audit Plan

	2018/2019 Year 1	2019/2020 Year 2	2020/2021 Year 3
Fundamentals			
Housing Benefits	20	20	20
Council Tax	12	12	12
NNDR	12	12	12
Payroll	10	10	10
Income Collection (Cashiers)	8	8	8
Treasury Management	5	5	5
Payments (Creditors)	8	8	8
Sundry Debtors	8	8	8
Capital Accounting & Asset Management	7	7	7
Budgetary Control	4	4	4
FMS	5	5	5
Risk Based and Corporate	**99**	**99**	**99**
Commercial Properties	8	0	0
FMS Project Group Attend and Advise	5	0	0
Housing Allocations	8		0
Temporary Accommodation	8		0
Refuse Collection – Contract Monitoring	8		
Anti-Fraud Work including NFI	30	30	30
ICT Audits	20	20	20
Follow Ups	10	10	10
Contingency		16	16
Management and Planning			
Committees	10	10	10
Operational Management	15	15	15
Head of Audit Time	15	15	15
Total Days	**236**	**220**	**220**

TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2019/20 TO 2021/22

REPORT OF: Head of Corporate Resources
Contact Officer: Peter Stuart
Email: peter.stuart@midsussex.gov.uk Tel: 01444 477315
Wards Affected: All
Key Decision: No
Report to: Audit Committee
25th February 2019

Purpose of Report

1. This report sets out the Council's investment and borrowing strategy for the forthcoming three years and reports the counterparty list with which investments may be made. It also sets out the Prudential Limits that provide the parameters for approved future lending and borrowing, including the incidental cost of so doing.

Summary

2. The purchase of the Orchard Shopping Centre head lease in November 2016 necessitated borrowing of £22m from other Local Authorities. £10m was repaid in 2017 and £5m was repaid in November 2018, using the cash flow generated by matured fixed term deposits.

3. Lending is restricted to the same counterparties and within the same limits as in the previous strategy approved in March 2018 except for the following amendments:

   (i) removal of the sovereign credit rating from UK investments, which was approved together with the half year treasury management report in November 2018;

   (ii) addition of the CCLA Public Sector Deposit Fund to the list of specified Money Market Funds, approved with the Annual Review in August 2018;

   (iii) addition of the JP Morgan GBP Liquidity LVNAV Fund to the list of specified Money Market Funds;

   (iv) amendment to the specified banks to include only the ring fenced entities, where appropriate, approved with the Annual Review in August 2018;

   (v) the list of Building Societies has been updated to add those which have increased their assets to over £1 billion (Leek United and Newbury).

Recommendations

4. The Committee is recommended to propose that Council agree:

   (i) the proposed Treasury Management Strategy Statement (TMSS) for 2019/20 and the following two years, including the additions to specified investments listed above;
   (ii) the Annual Investment Strategy (AIS) and the Minimum Revenue Provision Statement (MRP) as contained in Sections 4 and 2.3 respectively of the report;
   (iii) the Prudential Indicators contained within this report.

Background

5. The Council applies and upholds the Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code"). CIPFA has defined Treasury Management as:

"the management of the organisation's borrowing, 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."

6. The Code requires local authorities to produce an annual Treasury Management Strategy Statement (TMSS), which documents the Council's approach to capital financing and investments for the forthcoming financial year (2019/20) and the following two years. This report fulfils that requirement.

7. In producing the TMSS, The Local Government Act 2003 (the Act) and supporting regulations require the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years. The indicators are established to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

8. Additionally, the Act and its subsequent Investment Guidance require the Council to set out its treasury management strategy for borrowing, and to prepare an Annual Investment Strategy (AIS). The Council's borrowing position is reported in Section 3, with arrangements for making Minimum Revenue Provision (MRP) for repayment of debt explained in Section 2.3. The AIS is contained in Section 4 of this report, and describes the Council's policies for managing its investments, and for giving priority to the security and liquidity of those investments.

9. Statute requires that the AIS, MRP Statement, and Prudential Indicators are approved by full Council before the start of the new financial year.

Policy Context

10. Providing transparency and approval of the strategies contained in this report is an important part of the Council's statutory role. Treasury Management has become increasingly topical given the nature of the world's financial markets in recent years, and Members are expected to have a basic understanding of how the Council uses its reserves and cash flows which are in the stewardship of the Head of Corporate Resources.

Other Options Considered

11. None – this report is statutorily required.

Financial Implications

12. This report has no quantifiable financial implications. Interest payable and interest receivable arising from treasury management operations, and annual revenue provisions for repayment of debt, form part of the revenue budget but are not required to support the provision of services.

Risk Management Implications

13. This report has no specific implications for the risk profile of the Authority.

Equality and Customer Service Implications

14. None.

Background Papers

- Treasury Management Strategy Statement & Annual Investment Strategy 2018/19 to 2020/21 (March 2018)
- Annual Review of Treasury Management 2017-18 (July 2018)
- Review of Treasury Management Activity 1 April – 30 September 2018 (Nov. 2018)
- Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes (CIPFA)
- The Prudential Code for Capital Finance in Local Authorities (CIPFA, December 2017)
- MHCLG Investment Guidance (Revised for April 2018) and MRP Guidance
- Link Asset Services report template (January 2019)

Treasury Management Strategy Statement & Annual Investment 2019/20 to 2021/22

1. INTRODUCTION

Background

1. The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

2. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

3. The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

4. Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure),and are separate from the day to day treasury management activities.

5. Revised reporting is required for the 2019/20 reporting cycle due to revisions of the MHCLG Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The capital strategy is being reported separately.

Reporting requirements

<u>Capital Strategy</u>

6. The CIPFA revised 2017 Prudential and Treasury Management Codes require, for 2019-20, all local authorities to prepare an additional report, a capital strategy report, which will provide the following:

   - a high-level long term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
   - an overview of how the associated risk is managed
   - the implications for future financial sustainability

7. The aim of this capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

8. This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy will show:

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

9. Where a physical asset is being bought, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

10. Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the MHCLG Investment Guidance and CIPFA Prudential Code have not been adhered to. If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the capital strategy.

Treasury Management reporting

11. The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals:

a. **Prudential and treasury indicators and treasury strategy** (this report) - the first, and most important report covers:

- the capital plans (including prudential indicators);
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

12. The approval of the Treasury Management Strategy and Annual Investment Strategy is the function of the Council, however the Head of Corporate Resources shall also report to the Audit Committee on treasury management activity performance as follows:

b. **A mid year treasury management report** – This will update Members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision. The report will be submitted as soon after 30 September as practically possible.

c. **An annual treasury report** – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy. The report will be submitted no later than 30 September after the financial year end.

Scrutiny

13. The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Audit Committee, which may make recommendations regarding any aspects of treasury management policy and practices it considers appropriate in fulfilment of its scrutiny role. Such recommendations, as may be made shall be incorporated within the above named reports and submitted to meetings of the Council for consideration at the next available opportunity.

14. The Council's Scheme of Delegations is set out in Appendix E.

Treasury Management Strategy for 2019/20

15. The strategy for 2019/20 covers two main areas:

Capital issues

- the capital expenditure plans and the associated prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management issues

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

16. These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, MHCLG MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

Training

17. The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate training. This especially applies to Members responsible for scrutiny. During 2019/20 appropriate mandatory treasury management training will be provided to the Audit Committee by. The training needs of the treasury management officers at Adur District Council, who provide the shared treasury service to Mid Sussex District Council, are periodically reviewed. Officers attend courses provided by appropriate trainers such as CIPFA and Link Asset Services.

External Service Providers

18. The Council obtains treasury management services under a Shared Services Arrangement (SSA) from the in-house treasury management team formed out of the partnership working between Adur District and Worthing Borough Councils. The operation for all three Councils' treasury management is based at Worthing Town Hall, utilising similar banking arrangements.

19. The SSA is provided under a Service Level Agreement (SLA) that commenced in October 2016 and which defines the respective roles of the client and provider authorities for a period of three years. In making this arrangement the Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that reliance beyond the terms and arrangements specified in the SLA is not placed upon the shared service providers. The SSA uses Link Asset Services as its external treasury management advisors.

20. The Council will ensure that the terms of the appointment of the shared services providers, and the methods by which their value will be assessed, are properly agreed and documented and subjected to regular review.

2. THE CAPITAL PRUDENTIAL INDICATORS 2019/20 – 2021/22

21. The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the Prudential Indicators, which are designed to assist Members' overview and confirm capital expenditure plans.

Capital expenditure

22. This Prudential Indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Capital expenditure	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
General Fund	3.477	13.533	2.426	2.389	1.455

23. The above financing need excludes other long term liabilities, such as leasing arrangements which already include borrowing instruments.

24. The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital expenditure	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Total	3.477	13.533	2.426	2.389	1.455
Financed by:					
Capital receipts	0.000	1.269	0.000	0.000	0.000
Capital grants, Contributions & S106 receipts	1.500	3.017	1.084	1.983	0.900
General Reserves, Specific Reserves & Revenue Contributions	1.977	9.247	1.342	0.406	0.555
Net financing need for the year	0.000	0.000	0.000	0.000	0.000

The Council's borrowing need (the Capital Financing Requirement)

25. The second prudential indicator is the Council's 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 indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR. The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life

26. The CFR includes any other long term liabilities (e.g. finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council currently has one finance lease recognised in 2018 and ending in 2028.

27. The Council is asked to approve the CFR projections below:

Capital Financing Requirement	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Total CFR at 31/03	25.357	27.947	7.437	6.915	6.381
Movement in CFR	(0.379)	2.590	(20.510)	(0.522)	(0.534)
Movement in CFR represented by:					
Net financing need for the year (above)	0.000	3.088	(20.000)	0.000	0.000
Less MRP and other financing movements	(0.379)	(0.498)	(0.510)	(0.522)	(0.534)
Movement in CFR	(0.379)	2.590	(20.510)	(0.522)	(0.534)

Minimum revenue provision (MRP) policy statement

28. The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

29. MHCLG regulations have been issued which require the full Council to approve an MRP Statement in advance of each year. A variety of options is provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

30. The Council's policy for MRP relating to unfunded capital expenditure is to provide for MRP on an annuity basis over the life of the loans (except as detailed below for the Orchard Shopping Centre). As an annuity is a fixed annual sum comprising interest and principal, the MRP for repayment of debt will increase each year over the asset life as the proportion of interest calculated on the principal outstanding reduces as the debt is repaid.

31. The purchase of the Orchard Shopping Centre head lease in November 2016 increased the Capital Financing Requirement. However, as the Council is forecasting possible capital receipts of over £20m in 2019/20, MRP will only be provided on the balance of nearly £5m. This will be done on a level basis of £100,000 per year.

32. Repayments included in finance leases are applied as MRP.

3. BORROWING

33. The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

Current portfolio position

34. The overall treasury management portfolio as at 31 March 2018 and for the position as at 31 December 2018 are shown below for both borrowing and investments.

	Principal at 31.03.18 £m	Actual 31.03.2018 %	Principal at 31.12.18 £m	Actual 31.12.2018 %
External Borrowing				
PWLB	(0.698)	5%	(0.635)	6%
Other Borrowing	(12.000)	95%	(7.000)	67%
Finance lease	(0.000)		(2.886)	27%
TOTAL BORROWING	**(12.698)**	100%	**(10.521)**	100%
Treasury Investments:				
Local Authority Property Fund	5.851	16%	5.851	15%
In-house:				
Banks	6.000	16%	9.010	24%
Building societies - unrated	12.000	32%	10.000	26%
Building societies - rated	8.000	21%	6.000	16%
Local authorities	4.000	11%	2.000	5%
Money market funds	1.550	4%	5.130	14%
TOTAL INVESTMENTS	**37.401**	100%	**37.991**	100%
NET INVESTMENTS	**24.703**		**27.470**	

35. The Council's forward projections for borrowing are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

External Debt	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	**£m**	**£m**	**£m**	**£m**
Debt at 1 April	22.819	12.698	7.571	7.437	5.298
Expected change in Debt	(10.121)	(5.127)	(0.134)	(2.139)	(5.146)
Other long-term liabilities (OLTL)	0.158	0.000	2.817	2.541	2.258
Expected change in OLTL	(0.158)	2.817	(0.276)	(0.283)	(0.288)
Actual gross debt at 31 March	12.698	10.388	9.978	7.556	2.122
The Capital Financing Requirement	25.357	27.947	7.437	6.915	6.381
Under/(over) borrowing	12.659	17.559	(2.541)	(0.641)	4.259

36. The Council's debt comprises one loan from the Public Works Loan Board (PWLB), which matures on 1 March 2023 and 2 loans with other local authorities, totalling £7m, with remaining lives of between 1 and 3 years, to fund the purchase of the Orchard Shopping Centre head lease. The local authority loans are at rates lower than those that were available from the PWLB, ranging from 1.0% to 1.1% (average rate), and they will be repaid using capital receipts and maturing investments. The "other long term liability" is in respect of capital assets acquired by finance leases.

37. Within the range of Prudential Indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2019/20 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

38. The Head of Corporate Resources reports that the Council complied with this Prudential Indicator in the current year. The respective timings of capital receipts and repayment of debt results in a projected over borrowing position in the subsequent two years. However this is due to the Council's ability to fund its capital expenditure from grants and other resources and is not an indication of imprudent borrowing. In addition, both the CFR and the outstanding debt are small relative to the size of the Council's budget. This view takes into account current commitments, existing plans, and the proposals in this report.

Treasury Indicators: limits to borrowing activity

39. **The operational boundary** - This is the limit which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Operational Boundary	2018/19	2019/20	2020/21	2021/22
	£m	**£m**	**£m**	**£m**
Debt	£28.0m	£28.0m	£28.0m	£28.0m
Other long term liabilities	£4.0m	£4.0m	£4.0m	£4.0m
Total	**£32.0m**	**£32.0m**	**£32.0m**	**£32.0m**

40. **The authorised limit for external debt** – This is a key Prudential Indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

(i) The Council is asked to approve the authorised limit:

Authorised Limit	2018/19	2019/20	2020/21	2021/22
	£m	**£m**	**£m**	**£m**
Debt	£30.0m	£30.0m	£30.0m	£30.0m
Other long term liabilities	£4.0m	£4.0m	£4.0m	£4.0m
Total	**£34.0m**	**£34.0m**	**£34.0m**	**£34.0m**

(ii) This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

(iii) The limits for the "Other long term liabilities" have been increased to £4m to allow for the new finance lease.

41. The Head of Corporate Resources has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of the Council at the earliest opportunity.

Prospects for interest rates and the economy

42. This section contains a commentary for the economic outlook provided by the Council's shared service provider's treasury management consultants, Link Asset Services . This includes a central view of forecast interest rates as follows:

Link Asset Services Interest Rate View	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%	1.75%	2.00%
3 Month LIBID	0.90%	1.00%	1.10%	1.20%	1.30%	1.40%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%
6 Month LIBID	1.00%	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%
12 Month LIBID	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%	2.30%	2.40%
5yr PWLB Rate	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%
10yr PWLB Rate	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
25yr PWLB Rate	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB Rate	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%

43. The flow of generally positive economic statistics after the quarter ended 30 June meant that it came as no surprise that the MPC came to a decision on 2 August to make the first increase in Bank Rate above 0.5% since the financial crash, from 0.5% to 0.75%. Growth became increasingly strong during 2018 until slowing significantly during the last quarter. At their November quarterly Inflation Report meeting, the MPC left Bank Rate unchanged, but expressed some concern at the Chancellor's fiscal stimulus in his Budget, which could increase inflationary pressures. However, it is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. On a major assumption that Parliament and the EU agree a Brexit deal in the first quarter of 2019, then the next increase in Bank Rate is forecast to be in May 2019, followed by increases in February and November 2020, before ending up at 2.0% in February 2022.

44. The overall longer run future trend is for gilt yields, and consequently PWLB rates, to rise, albeit gently. However, over about the last 25 years, we have been through a period of falling bond yields as inflation subsided to, and then stabilised at, much lower levels than before, and supported by central banks implementing substantial quantitative easing purchases of government and other debt after the financial crash of 2008. Quantitative easing, conversely, also caused a rise in equity values as investors searched for higher returns and purchased riskier assets. In 2016, we saw the start of a reversal of this trend with a sharp rise in bond yields after the US Presidential election in November 2016, with yields then rising further as a result of the big increase in the US government deficit aimed at stimulating even stronger economic growth. That policy change also created concerns around a significant rise in inflationary pressures in an economy which was already running at remarkably low levels of unemployment. Unsurprisingly, the Fed has continued on its series of robust responses to combat its perception of rising inflationary pressures by repeatedly increasing the Fed rate to reach 2.25 – 2.50% in December 2018. It has also continued its policy of not fully reinvesting proceeds from bonds that it holds as a result of quantitative easing, when they mature. We therefore saw US 10 year bond Treasury yields rise above 3.2% during October 2018 and also investors causing a sharp fall in equity prices as they sold out of holding riskier assets. However, by early January 2019, US 10 year bond yields had fallen back considerably on fears that the Fed was being too aggressive in raising interest rates and was going to cause a recession. Equity prices have been very volatile on alternating good and bad news during this period.

45. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment. Such volatility could occur at any time during the forecast period.

46. Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

Investment and borrowing rates

47. Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years.

48. Borrowing interest rates have been volatile so far in 2018-19 and while they were on a rising trend during the first half of the year, they have backtracked since then until early January. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt;

49. There will remain a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

Borrowing strategy

50. The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

51. Against this background and the risks within the economic forecast, caution will be adopted with the 2019/20 treasury operations. The Head of Corporate Resources will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

52. Any decisions will be reported to the appropriate decision making body at the next available opportunity.

Policy on borrowing in advance of need

53. The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism

Debt rescheduling

54. The Council has one loan from the Public Works Loan Board, repaid by fixed annuities over the life of the loan. As it would not be possible to prematurely repay the existing loan without incurring a premium charge for early settlement, there is currently no intention to redeem the loan early. The loans for the purchase of the Orchard Shopping Centre head lease will be repaid within 3 years and are all at competitively low interest rates.

55. Any rescheduling will be reported to the Council at the earliest meeting following its action.

4. ANNUAL INVESTMENT STRATEGY

Investment policy – management of risk

56. The MHCLG and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy, (a separate report).

57. The Council's investment policy has regard to the following: -

- MHCLG's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018

58. The Council's investment priorities will be security first, portfolio liquidity second and then yield, (return).

59. The Head of Corporate Resources, under delegated powers, will undertake through the Shared Service Arrangement the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements, and Prudential Indicators. As conditions in the financial markets remain uncertain, the proposed maximum limits for Specified and Unspecified Investments for 2019/20 are the same as for 2018/19.

60. Investment instruments identified for use in the financial year are listed in Appendices C and D under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Council's treasury management practices.

61. The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

(i) Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

(ii) **Other information**: ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

(iii) **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

(iv) This authority has defined the list of **types of investment instruments** that the treasury management team is authorised to use. There are two lists in Appendices C and D under the categories of 'specified' and 'non-specified' investments.

- **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.

- **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

(v) Lending limits, (amounts and maturity), for each counterparty are set out in Appendices C and D.

(vi) This authority will set a limit for the amount of its investments which are invested for longer than 365 days, (see paragraph 4.8).

(vii) Investments will only be placed with counterparties from countries with a specified minimum sovereign rating, (see paragraph 4.5). The UK is excluded from this limit because it will be necessary to invest in UK banks and other institutions even if the sovereign rating is cut.

(viii) Through the shared service, this authority has access to external consultants, to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

(ix) All investments will be denominated in sterling.

(x) As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing from 1.4.18. Consequently any fluctuations in the value of the Council's investment in the Local Authorities' Property Fund will not be taken through the general fund for the period of the override).

However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 4.14). Regular monitoring of investment performance will be carried out during the year.

Changes in risk management policy from last year

62. The above criteria are unchanged from last year, with the exception of the removal of the sovereign rating requirement from the UK.

Creditworthiness policy

63. The primary principle governing the Council's investment criteria through the Shared Services Arrangement (SSA) is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the SSA will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections in Appendices C and D; and

- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's Prudential Indicators covering the maximum principal sums invested.

64. The SSA will maintain a counterparty list in compliance with the criteria in the Appendices and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

65. Credit rating information is supplied to the SSA by Link Asset Services, our treasury advisors, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating Watches (notification of a likely change), rating Outlooks (notification of the longer term bias outside the central rating view) are provided to the SSA almost immediately after they occur and this information is considered before dealing. For instance, a negative rating Watch applying to a counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

Use of additional information other than credit ratings

66. Additional requirements under the Code require the Council to supplement credit rating information. Whilst the above criteria rely primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties.

67. Link Asset Services use a sophisticated modelling approach with credit ratings from all three credit rating agencies – Fitch, Moody's and Standard and Poor's. However it does not rely solely on the current credit ratings of counterparties but also uses the following as overlays:

- credit watches and credit outlooks from credit rating agencies
- credit Default Swap (CDS) spreads to give early warning of likely changes in credit ratings
- sovereign ratings to select counterparties from only the most creditworthy countries

68. This additional market information will be applied to compare the relative security of differing investment counterparties.

69. The proposed criteria for specified and non-specified investments are shown in the Appendices for approval.

70. Using Link's ratings service, potential counterparty ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications. The effect of a change in ratings may prompt the following responses:

- If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

- In addition to the use of Credit Ratings the shared service will be advised by Link of movements in Credit Default Swaps and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending lists.

71. The officers of the shared service recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets, the government support for banks, and the credit ratings of that government support.

72. Accordingly, the shared service will exercise discretion to deviate from Link's suggested durational bands – for example the Council approves the use of Building Societies as set out in the Appendices.

The Council's Minimum Investment Creditworthiness Criteria

73. The minimum credit ratings criteria used by the Council generally will be a short term rating (Fitch or equivalents) of F1, and long term rating A-. There may be occasions when the counterparty ratings from one or more of the three Ratings Agencies are marginally lower than the minimum requirements of F1 Short term, A- Long term (or equivalent). Where this arises, the counterparties to which the ratings apply may still be used with discretion, but in these instances consideration will be given to the whole range of topical market information available, not just ratings.

74. The Council includes **Building Societies** with asset size in excess of £1 billion in the specified investments. It is recognised that they may carry a lower credit rating than the Council's other counterparties, or no rating, therefore the lending limits for the building societies shall be £4m each for the top 3 and £3m for the others.

UK banks – ring fencing

75. The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as "ring-fencing". Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

76. Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and "riskier" activities are required to be housed in a separate entity, a non-ring-fenced bank, (NRFB). This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

77. While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the new-formed entities in the same way that they do others and those with sufficiently high ratings, (and any other metrics considered), will be considered for investment purposes.

Country Limits and Proposed Monitoring Arrangements

78. Due care will be taken to consider the country, group and sector exposure of the Council's investments.

79. The SSA has determined that it will only use approved counterparties from countries (other than the UK) with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide one). The list of countries that qualify using these credit criteria as at the date of this report is reflected in the counterparty approved lending list shown at Appendix B. This list will be added to, or deducted from, by officers should ratings change, in accordance with this policy. No more than 25% of investments shall be placed in non-UK financial institutions for more than 7 days.

Investment strategy

80. **In-house funds** - Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed. For cash flow balances, the shared service will seek to use notice accounts, money market funds and short-dated deposits to benefit from the compounding of interest

- If it is thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.

- Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

81. The Head of Corporate Resources, through the shared service, 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 to the meetings of the Audit Committee and the Council in accordance with the reporting arrangements

82. **Investment returns expectations** - Bank Rate is forecast to increase steadily but slowly over the next few years, to reach 2.00% by quarter 1 2022. Bank Rate forecasts for financial year ends (March) are:

2018/19	:	0.75%
2019/20	:	1.25%
2020/21	:	1.50%
2021/22	:	2.00%

83. The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows:

2018/19	:	0.75%
2019/20	:	1.00%
2020/21	:	1.50%
2021/22	:	1.75%
2022/23	:	1.75%
2023/24	:	2.00%
Later years	:	2.50%

84. The overall balance of risks to economic growth in the UK is probably neutral. The balance of risks to increases in Bank Rate and shorter term PWLB rates are probably also even and are dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quicly the Brexit negotiations move forward positively.

Funds available for investment

85. The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances.

Investments	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m
Balance at 1 April	37.401	26.238	46.127	33.078
Capital Expenditure	(13.533)	(2.426)	(2.389)	(1.455)
Grants, capital receipts & other new funds	7.497	22.449	(8.521)	2.615
Loan repayments	(5.127)	(0.134)	(2.139)	(5.000)
Balance at 31 March	26.238	46.127	33.078	29.238

Investment treasury indicator and limit - total principal funds invested for greater than 365 days

86. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

87. The Council is asked to approve the treasury indicator limit: -

Maximum proportion of principal sums invested > 365 days	2019/20	2020/21	2021/22
Principal sums invested > 365 days	50%	50%	50%

88. In any sustained period of significant stress in the financial markets, the default position is for investments to be placed with The Debt Management Account Deposit Facility of the Debt Management Office (DMO) of the UK central government. The rates of interest are below equivalent money market rates, however, the returns are an acceptable trade-off for the guarantee that the Council's capital is secure.

89. The Council's proposed investment activity for placing cash deposits in 2019/20 will be to use:

- AAA-rated Money Market Funds with a Constant Net Asset Value (CNAV) or a Low Volatility Net Asset Value (LVNAV) under the new money market fund regulations
- other local authorities, parish councils etc.
- bank business reserve accounts and term deposits. These are primarily restricted to UK institutions that are rated at least A- long term.
- Building Societies with asset size in excess of £1 billion

Other Options for Longer Term Investments

90. To provide the Council with options to enhance returns above those available for short term durations, it is proposed to retain the option to use the following for longer term investments, as an alternative to cash deposits:

a) **Supranational bonds** greater than 1 year to maturity

b) **Gilt edged securities** with a maturity of greater than one year. These are Government bonds and so provide the highest security of interest and the repayment of principal on maturity. Similar to category (a) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.

c) **Building Societies** not meeting the basic security requirements under the specified investments, but on the list in Appendix C (b). The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings.

d) Any **bank** that has a minimum long term credit rating of A- for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).

e) Any **non-rated subsidiary** of a credit rated institution included in the specified investment category. These institutions will be included as an investment category subject to a guarantee from the parent company, and exposure up to the limit applicable to the parent.

g) **Property Investment Funds** for example the Local Authorities' Property Fund. The Councils will consult the Treasury Management Advisors and undertake appropriate due diligence before investment of this type is undertaken. Some of these funds are deemed capital expenditure – the Councils will seek guidance on the status of any fund considered for investment.

h) Other **local authorities**, parish councils etc.

i) Other investments listed in Appendices C and D - the Council will seek further advice on the appropriateness and associated risks with investments in these other categories as and when an opportunity presents itself.

91. The **accounting treatment** may differ from the underlying cash transactions arising from investment decisions made by the Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, the accounting implications of new transactions will be reviewed before they are undertaken.

92. The Council will not transact in any investment that may be deemed to constitute capital expenditure (e.g. Share Capital, or pooled investment funds other than Money Market Funds), without the resource implications being approved as part of the consideration of the Capital Programme or other appropriate Committee report.

93. **Investment risk benchmarking** – The shared service will subscribe to Link's Investment Benchmarking Club to review the investment performance and risk of the portfolios.

94. At the end of the financial year the Council will report on investment activity as part of the Annual Treasury Report.

External fund managers

95. The Council does not use external fund managers, but reserves the option to do so in future should this be deemed to be appropriate. Should consideration be given to exercising this option in the future, the relevant Committee will be advised of the reasons for doing so and the Council requested to consider whether it wishes to proceed with the selection and appointment of external fund managers.

THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2019/20 – 2021/22

1. The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the Prudential Indicators, which are designed to assist Members' overview and confirm capital expenditure plans.

Capital expenditure	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
General Fund	3.477	13.533	2.426	2.389	1.455

Affordability Prudential Indicators

2. The previous sections cover the overall capital and control of borrowing Prudential Indicators, but within this framework Prudential Indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

Ratio of financing costs to net revenue stream

3. This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	%	%	%	%	%
Ratio	-0.68%	0.62%	0.58%	-1.44%	-1.30%

4. The estimates of financing costs include current commitments and the proposals in this budget report.

Maturity structure of borrowing

5. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits. However as the Council currently has only two significant loans, the upper limits need to be set very high. The Council does not have any variable rate borrowing.

6. The Council is asked to approve the following treasury indicators and limits:

Maturity structure of fixed interest rate borrowing 2019/20		
	Lower	Upper
Under 12 months	0%	50%
12 months to 2 years	0%	70%
2 years to 5 years	0%	80%
5 years to 10 years	0%	60%
Over 10 years	0%	50%

TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT

1. The MHCLG issued Investment Guidance in 2018, and this forms the structure of the Council's policy below. These guidelines do not apply to either trust funds or pension funds which operate under a different regulatory regime.

2. The key intention of the Guidance is to maintain the current requirement for councils to invest prudently, and that priority is given to security and liquidity before yield. In order to facilitate this objective the guidance requires this Council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes, which will apply to all investment activity. In accordance with the Code, the Council will comply with the treasury management practices (TMPs). This part, TMP 1(1), covering investment counterparty policy requires approval each year.

3. **Annual investment strategy** - The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of the annual treasury strategy for the following year, covering the identification and approval of following:

   - The strategy guidelines for choosing and placing investments, particularly non-specified investments.
   - The principles to be used to determine the maximum periods for which funds can be committed.
   - Specified investments that the Council will use. These are high security (i.e. high credit rating, although this is defined by the Council, and no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than a year.
   - Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time.

4. **Strategy guidelines** – The main strategy guidelines are contained in the body of the treasury strategy statement.

SPECIFIED AND NON SPECIFIED INVESTMENTS

5. Specified Investments will be those that meet the criteria in the MHCLG Guidance, i.e. the investment

   - is sterling denominated
   - has a maximum maturity of 1 year or where the Council has the right to be repaid within 12 months
   - meets the "high" credit criteria as determined by the Council or is made with the UK government or is made with a local authority in England, Wales and Scotland.
   - the making of which is not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate).

"Specified" Investments identified for the Council's use are:

- Deposits in the DMO's Debt Management Account Deposit Facility
- Deposits with UK local authorities

- Deposits with banks and building societies
- *Certificates of deposit with banks and building societies
- *Gilts : (bonds issued by the UK government)
- *Bonds issued by multilateral development banks
- AAA-rated Money Market Funds with a Constant Net Asset Value (Constant NAV) or appropriate Low Volatility Net Asset Value (LVNAV) under the new regulations.
- Other Money Market Funds and Collective Investment Schemes– i.e. credit rated funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573.

  * Investments in these instruments will be on advice from the Shared Service's treasury advisor.

6. For credit rated counterparties, the minimum criteria, excepting for the Council's own banker and the specified building societies, (see below) will be the short-term / long-term ratings assigned by various agencies which may include Moody's Investors Services, Standard and Poor's, Fitch Ratings, being:

   Long-term investments (over 365 days): minimum: A- (Fitch) or equivalent
   Or
   Short-term investments (365 days or less): minimum: F1 (Fitch) or equivalent

7. For all investments the Shared Service will also take into account information on corporate developments of, and market sentiment towards, investment counterparties.

8. Where appropriate the Ring Fenced entities of banks will be used.

9. If the Council's own banker (currently Lloyds Bank) falls beneath the specified criteria, it will still be used for transactional purposes.

APPROVED INVESTMENT INSTITUTIONS

Specified Investments identified for use by the Council

New specified investments will be made within the following limits:

(a) Banks

Major U.K. and European Banks and their wholly-owned subsidiaries meeting the Council's approved investment criteria.

	Counterparty	Group	Maximum Sum	Maximum Period *
1	HSBC Bank plc	N/A	£4m	5 years
2	The Royal Bank of Scotland Group:	£5m		
	The Royal Bank of Scotland plc		£4m	5 years
	National Westminster Bank plc		£4m	5 years
			£1m	1 year
3	Lloyds Group::	£5m		
	Lloyds Bank plc		£4m	5 years
	Halifax plc		£4m	5 years
	Bank of Scotland plc		£4m	5 years
	HBOS Treasury Services plc		£4m	5 years
4	Barclays Bank plc	N/A	£4m	5 years
5	Santander UK	N/A	£4m	5 years
6	Clydesdale Bank	N/A	£4m	5 years
7	Handelsbanken plc	N/A	£4m	1 year
8	Goldman Sachs International Bank	N/A	£4m	5 years
9	Close Brothers Ltd	N/A	£4m	5 years

*Specified investments are for a maximum period of 1 year, the maximum limits shown in this column are for non-specified investments with these institutions.

(b) Building Societies

(i) Building Societies (Assets in excess of £1 billion):

Rank	Name of Counterparty	Individual	
		Sum	Period*
1	Nationwide	£4m	3 years
2	Coventry	£4m	3 years
3	Yorkshire	£4m	3 years
4	Skipton	£3m	3 years
5	Leeds	£3m	3 years
6	Principality	£3m	3 years
7	West Bromwich	£3m	3 years
8	Nottingham	£3m	3 years
9	Newcastle	£3m	3 years
10	Cumberland	£3m	3 years
11	National Counties	£3m	3 years
12	Progressive	£3m	3 years
13	Cambridge	£3m	3 years
14	Monmouthshire	£3m	3 years
15	Leek United	£3m	3 years
16	Saffron	£3m	3 years
17	Newbury	£3m	3 years

*Specified investments are for a maximum period of 1 year, the maximum limits shown in this column are for non-specified investments with these institutions.

(c) Money Market Funds

Counterparty	Sum	
Invesco Aim – Sterling	£3m	For Short Term Operational Cash Flow Purposes
Blackrock Institutional Sterling Liquidity Fund	£3m	
Goldman Sachs Sterling Liquidity Reserve Fund	£3m	
Fidelity Institutional Cash Fund plc – Sterling	£3m	
CCLA Public Sector Deposit Fund	£3m	
JP Morgan GBP Liquidity LVNAV Fund	£3m	
Federated Short-Term Sterling Prime Liquidity Fund	£3m	

The limit for investing in any one Money Market Fund is £3 million. Total investments in Money Market Funds shall not exceed the higher of £9m or 25% of the total investment portfolio, for more than one week at any one time.

(d) Local Authorities

(i) All the following local authorities mentioned in the Regulations

Schedule Part II Ref	Details	Individual	
		Sum	Period*
1	County Councils (England and Wales)	£3m	5 years
2	District Councils in England and Wales (including Borough, City, Metropolitan Borough Councils and Unitary Councils)	£3m	5 years
3	London Borough Councils	£3m	5 years
4	The Common Council of the City of London	£3m	5 years
5	The Council of the Isles of Scilly	£3m	5 years
7	Combined Police Authorities	£3m	5 years
16	Regional, Islands, or District Councils in Scotland	£3m	5 years
17	Joint boards under s.235 (1) of LG (Scotland) Act 1973	£3m	5 years
28	District Councils in Northern Ireland	£3m	5 years
29	Police Authorities (now Police and Crime Commissioners) under s.3 Police Act 1964 as substituted by s.2 Police & Magistrates Courts Act 1994	£3m	5 years

*Specified investments are for a maximum period of 1 year, the maximum limits shown in this column are for non-specified investments with these institutions.

NON-SPECIFIED INVESTMENTS DETERMINED FOR USE BY THE COUNCIL

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use.

	In-house use	Use by Fund Managers	Maximum Maturity	Maximum % of portfolio or £m	Capital Expenditure?
• Deposits with banks and building societies and Local Authorities • Certificates of deposit with banks and building societies	√ √	 √	5 years	The higher of £10m or 50% of funds	No
Gilts and Bonds: • Gilts • Bonds issued by multilateral development banks • Bonds issued by financial institutions guaranteed by the UK government • Sterling denominated bonds by non-UK sovereign governments	√ √ √ √ (on advice from treasury advisor)	√ √ √ √	5 years	The higher of £3m or 25% of funds	No
Money Market Funds and Collective Investment Schemes (pooled funds which meet the definition of a collective investment scheme as defined in SI 2004 No. 534 and SI 2007, No. 573), but which are not credit rated.	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date.	The higher of £9m or 25% of funds	No
Government guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	√ (on advice from treasury advisor)	√	5 years	The higher of £2m or 10% of funds	Subject to test
Property Funds approved by HM Treasury and operated by managers regulated by the Financial Conduct Authority – specifically the Local Authorities' Property Fund	√	√	These funds do not have a defined maturity date.	The higher of £4m or 25% of funds	No
Non-guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	√ (on advice from treasury advisor)	√	5 years	The higher of £2m or 10% of funds	Subject to test
Collective Investment Schemes (pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No. 534 or SI 2007, No. 573.	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date	The higher of £2m or 20% of funds	Subject to test

In determining the period to maturity of an investment, the investment is regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.

Accounting treatment of investments

The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

TREASURY MANAGEMENT SCHEME OF DELEGATION

(i) **Full Council**

- approval of annual treasury management strategy and Annual Investment Strategy
- approval of MRP Statement

(ii) **Executive Committee (e.g. Cabinet)**

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices
- budget consideration and approval
- approval of the division of responsibilities
- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers and agreeing terms of appointment.

(iii) **Audit Committee**

Receiving and reviewing the following, and making recommendations to the Cabinet

- regular monitoring reports on compliance with the Treasury Management Strategy, practices and procedures.

(iv) **The S151 (responsible) officer**

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

The Revised CIPFA Treasury Management and Prudential Codes have extended the functions of the S151 role in respect of non-financial investments. Guidance notes giving specific information will follow, but additional responsibilities are likely to include:

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management
- ensuring that the capital strategy is prudent, sustainable and affordable in the long term and provides value for money

- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authorities
- ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed

COUNTERPARTIES WHERE THE COUNCIL HAS OPTED UP TO PROFESSONAL INVESTOR STATUS

(i) **Money Market Funds**

Invesco
Federated Investors

(ii) **Building Societies**

Skipton Building Society
Coventry Building Society
Progressive Building Society (paperwork not yet approved)

(iii) **Brokers**

BGC (Sterling)
Tradition
ICAP

(iv) **Other**

ICD (Portal used for money market fund investments)
Link Asset Services

These arrangements will be regularly reviewed as appropriate.

ECONOMIC BACKGROUND

Global Outlook

1. **World growth** has been doing reasonably well, aided by strong growth in the US. However, US growth is likely to fall back in 2019 and, together with weakening economic activity in China and the eurozone, overall world growth is likely to weaken.

2. **Inflation** has been weak during 2018 but, at long last, unemployment falling to remarkably low levels in the US and UK has led to a marked acceleration of wage inflation. The US Fed has therefore increased rates nine times and the Bank of England twice. However, the ECB is unlikely to start raising rates until late in 2019 at the earliest.

KEY RISKS - central bank monetary policy measures

3. Looking back on nearly ten years since the financial crash of 2008 when liquidity suddenly dried up in financial markets, it can be assessed that central banks' monetary policy measures to counter the sharp world recession were successful. The key monetary policy measures they used were a combination of lowering central interest rates and flooding financial markets with liquidity, particularly through unconventional means such as quantitative easing (QE), where central banks bought large amounts of central government debt and smaller sums of other debt.

4. **The key issue now** is that that period of stimulating economic recovery and warding off the threat of deflation, is coming towards its close. A new period is well advanced in the US, and started more recently in the UK, of reversing those measures i.e. by raising central rates and, (for the US), reducing central banks' holdings of government and other debt. These measures are now required in order to stop the trend of a reduction in spare capacity in the economy and of unemployment falling to such low levels, that the re-emergence of inflation is viewed as a major risk. It is, therefore, crucial that central banks get their timing right and do not cause shocks to market expectations that could destabilise financial markets. In particular, a key risk is that because QE-driven purchases of bonds drove up the price of government debt, and therefore caused a sharp drop in income yields, this also encouraged investors into a search for yield and into investing in riskier assets such as equities. Consequently, prices in both bond and equity markets rose to historically high valuation levels simultaneously. This meant that both asset categories were exposed to the risk of a sharp downward correction and we have indeed, seen a sharp fall in equity values in the last quarter of 2018. It is important, therefore, that central banks only gradually unwind their holdings of bonds in order to prevent destabilising the financial markets. It is also likely that the timeframe for central banks unwinding their holdings of QE debt purchases will be over several years. They need to balance their timing to neither squash economic recovery, by taking too rapid and too strong action, or, conversely, let inflation run away by taking action that was too slow and/or too weak. **The potential for central banks to get this timing and strength of action wrong are now key risks.** At the time of writing, (early January 2019), financial markets are very concerned that the Fed is being too aggressive with its policy for raising interest rates and was likely to cause a recession in the US economy.

5. The world **economy** also needs to adjust to a sharp change in **liquidity creation** over the last five years where the US has moved from boosting liquidity by QE purchases, to reducing its holdings of debt, (currently about $50bn per month). In addition, the European Central Bank ended its QE purchases in December 2018.

6. **UK.** The flow of positive economic statistics since the end of the first quarter of 2018 has shown that pessimism was overdone about the poor growth in quarter 1 when adverse weather caused a temporary downward blip. Quarter 1 at 0.1% growth in GDP was followed by a return to 0.4% in quarter 2 and by a strong performance in quarter 3 of +0.6%. However, growth in quarter 4 is expected to weaken significantly.

7. At their November quarterly Inflation Report meeting, the MPC repeated their well-worn phrase that future Bank Rate increases would be gradual and would rise to a much lower equilibrium rate, (where monetary policy is neither expansionary of contractionary), than before the crash; indeed they gave a figure for this of around 2.5% in ten years time, but declined to give a medium term forecast. However, with so much uncertainty around Brexit, they warned that the next move could be up or down, even if there was a disorderly Brexit. While it would be expected that Bank Rate could be cut if there was a significant fall in GDP growth as a result of a disorderly Brexit, so as to provide a stimulus to growth, they warned they could also *raise* Bank Rate in the same scenario if there was a boost to inflation from a devaluation of sterling, increases in import prices and more expensive goods produced in the UK replacing cheaper goods previously imported, and so on. In addition, the Chancellor could potentially provide fiscal stimulus to support economic growth, though at the cost of increasing the budget deficit above currently projected levels.

8. It is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. Getting parliamentary approval for a Brexit agreement on both sides of the Channel will take well into spring 2019. However, in view of the hawkish stance of the MPC at their November meeting, the next increase in Bank Rate is now forecast to be in May 2019, (on the assumption that a Brexit deal is agreed by both the UK and the EU). The following increases are then forecast to be in February and November 2020 before ending up at 2.0% in February 2022.

9. **Inflation.** The Consumer Price Index (CPI) measure of inflation has been falling from a peak of 3.1% in November 2017 to 2.3% in November. In the November Bank of England quarterly Inflation Report, inflation was forecast to still be marginally above its 2% inflation target two years ahead, (at about 2.1%), given a scenario of minimal increases in Bank Rate. This inflation forecast is likely to be amended upwards due to the Bank's report being produced prior to the Chancellor's announcement of a significant fiscal stimulus in the Budget; this is likely to add 0.3% to GDP growth at a time when there is little spare capacity left in the economy, particularly of labour.

10. As for the **labour market** figures in October**,** unemployment at 4.1% was marginally above a 43 year low of 4% on the Independent Labour Organisation measure. A combination of job vacancies hitting an all-time high, together with negligible growth in total employment numbers, indicates that employers are now having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to 3.3%, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates less CPI inflation), earnings are currently growing by about 1.0%, the highest level since 2009. This increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC was right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

11. In the **political arena**, the Brexit deal put forward by the Conservative minority government was defeated on 15 January. It is unclear at the time of writing, how this situation will move forward. However, our central position is that Prime Minister May's government will endure, despite various setbacks, along the route to reaching an orderly Brexit though the risks are increasing that it may not be possible to get full agreement by the UK and EU before 29 March 2019, in which case this withdrawal date is likely to be pushed back to a new date. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary and fiscal policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

12. **USA.** President Trump's massive easing of fiscal policy is fuelling a, (temporary), boost in consumption which has generated an upturn in the rate of strong growth which rose from 2.2%, (annualised rate), in quarter 1 to 4.2% in quarter 2 and 3.5%, (3.0% y/y), in quarter 3, but also an upturn in inflationary pressures. The strong growth in employment numbers and the reduction in the unemployment rate to 3.9%, near to a recent 49 year low, has fed through to an upturn in wage inflation which hit 3.2% in November. However, CPI inflation overall fell to 2.2% in November and looks to be on a falling trend to drop below the Fed's target of 2% during 2019. The Fed has continued on its series of increases in interest rates with another 0.25% increase in December to between 2.25% and 2.50%, this being the fifth increase in 2018 and the ninth in this cycle. However, they did also reduce their forecast for further increases from three to two. This latest increase compounded investor fears that the Fed is over doing the rate and level of increases in rates and that it is going to cause a US recession as a result. There is also much evidence in previous monetary policy cycles, of the Fed's series of increases doing exactly that. Consequently, we have seen stock markets around the world plunging under the weight of fears around the Fed's actions, the trade war between the US and China, an expectation that world growth will slow, Brexit etc.

13. The tariff war between the US and China has been generating a lot of heat during 2018, but it is not expected that the current level of actual action would have much in the way of a significant effect on US or world growth. However, there is a risk of escalation if an agreement is not reached soon between the US and China.

14. **Eurozone.** Growth was 0.4% in quarters 1 and 2 but fell back to 0.2% in quarter 3, though this was probably just a temporary dip. In particular, data from Germany has been mixed and it could be negatively impacted by US tariffs on a significant part of manufacturing exports e.g. cars. For that reason, although growth is still expected to be in the region of nearly 2% for 2018, the horizon is less clear than it seemed just a short while ago. Having halved its quantitative easing purchases of debt in October 2018 to €15bn per month, the European Central Bank ended all further purchases in December 2018. The ECB is forecasting inflation to be a little below its 2% top limit through the next three years so it may find it difficult to warrant a start on raising rates by the end of 2019 if the growth rate of the EU economy is on a weakening trend.

15. **China.** Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems. Progress has been made in reducing the rate of credit creation, particularly from the shadow banking sector, which is feeding through into lower economic growth. There are concerns that official economic statistics are inflating the published rate of growth.

16. **Japan** - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It is likely that loose monetary policy will endure for some years yet to try to stimulate growth and modest inflation.

17. **Emerging countries.** Argentina and Turkey are currently experiencing major headwinds and are facing **challenges** in external financing requirements well in excess of their reserves of foreign exchange. However, these countries are small in terms of the overall world economy, (around 1% each), so the fallout from the expected recessions in these countries will be minimal.

INTEREST RATE FORECASTS

18. The interest rate forecasts provided by Link Asset Services in paragraph 3.2 are predicated on an assumption of an agreement being reached on Brexit between the UK and the EU. In the event of an orderly non-agreement exit, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall. If there was a disorderly Brexit, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

The balance of risks to the UK

19. The overall balance of risks to economic growth in the UK is probably neutral.

20. The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are broadly dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

21. One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed for ten years since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

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

22. **Brexit** – if it were to cause significant economic disruption and a major downturn in the rate of growth.

23. **Bank of England monetary policy** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.

24. A resurgence of the **eurozone sovereign debt crisis**, possibly in **Italy**, due to its high level of government debt, low rate of economic growth and vulnerable banking system, and due to the election in March of a government which has made a lot of anti-austerity noise. The EU rejected the initial proposed Italian budget and demanded cuts in government spending which the Italian government initially refused. However, a fudge was subsequently agreed, but only by delaying the planned increases in expenditure to a later year. This can has therefore only been kicked down the road to a later time. The rating agencies have started on downgrading Italian debt to one notch above junk level. If Italian debt were to fall below investment grade, many investors would be unable to hold it. Unsurprisingly, investors are becoming increasingly concerned by the words and actions of the Italian government and consequently, Italian bond yields have risen – at a time when the government faces having to refinance large amounts of debt maturing in 2019.

25. Weak capitalisation of some **European banks**. Italian banks are particularly vulnerable; one factor is that they hold a high level of Italian government debt - debt which is falling in value. This is therefore undermining their capital ratios and raises the question of whether they will need to raise fresh capital to plug the gap.

26. **German minority government**. In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. Then in October 2018, the results of the Bavarian and Hesse state elections radically undermined the SPD party and showed a sharp fall in support for the CDU. As a result, the SPD is reviewing whether it can continue to support a coalition that is so damaging to its electoral popularity. After the result of the Hesse state election, Angela Merkel announced that she would not stand for re-election as CDU party leader at her party's convention in December 2018, (a new party leader has now been elected). However, this makes little practical difference as she is still expected to aim to continue for now as the Chancellor. However, there are five more state elections coming up in 2019 and EU parliamentary elections in May/June; these could result in a further loss of electoral support for both the CDU and SPD which could also undermine her leadership.

27. **Other minority eurozone governments**. Spain, Portugal, Ireland, the Netherlands and Belgium all have vulnerable minority governments dependent on coalitions which could prove fragile. Sweden is also struggling to form a government due to the anti-immigration party holding the balance of power, and which no other party is willing to form a coalition with. The Belgian coalition collapsed in December 2018 but a minority caretaker government has been appointed until the May EU wide general elections.

28. **Austria, the Czech Republic and Hungary** now form a strongly anti-immigration bloc within the EU while Italy, in 2018, also elected a strongly anti-immigration government. Elections to the EU parliament are due in May/June 2019.

29. Further increases in interest rates in the US could spark a **sudden flight of investment funds** from more risky assets e.g. shares, into bonds yielding a much improved yield. Throughout the last quarter of 2018, we saw sharp falls in equity markets interspersed with occasional partial rallies. Emerging countries which have borrowed heavily in dollar denominated debt, could be particularly exposed to this risk of an investor flight to safe havens e.g. UK gilts.

30. There are concerns around the level of **US corporate debt** which has swollen massively during the period of low borrowing rates in order to finance mergers and acquisitions. This has resulted in the debt of many large corporations being downgraded to a BBB credit rating, close to junk status. Indeed, 48% of total investment grade corporate debt is now rated at BBB. If such corporations fail to generate profits and cash flow to reduce their debt levels as expected, this could tip their debt into junk ratings which will increase their cost of financing and further negatively impact profits and cash flow.

31. **Geopolitical risks**, especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates

32. **Brexit** – if both sides were to agree a compromise that removed all threats of economic and political disruption.

33. **The Fed causing a sudden shock in financial markets** through misjudging the pace and strength of increases in its Fed Funds Rate and in the pace and strength of reversal of QE, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world.

34. The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.

35. **UK inflation**, whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

CAPITAL STRATEGY 2019/20

REPORT OF: HEAD OF CORPORATE RESOURCES
Contact Officer: Peter Stuart
Email: peter.stuart@midsussex.gov.uk Tel: 01444 477315
Wards Affected: All
Key Decision: Yes
Report to: Audit Committee
Date of Meeting: 25 February 2019

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1. Purpose of Report

1.1 To present the Capital Strategy for 2019/20 for approval by the Committee.

2 Recommendations

2.1 The Committee is recommended to forward the draft Strategy for approval by Council at the next appropriate meeting

3. Background

3.1 Each year the Council is required to approve a corporate plan and budget that shows how it will deliver its services and spend its financial resources in the following financial year. This includes publishing a Capital Programme which sets out the level of investment in the Council's assets and the financing of that investment.

3.2 Our Corporate Plan has in the past included a Strategy designed to guide such investment but this good practice has now been formalised through a revision to the CIPFA Prudential Code. Authorities need therefore to present and have adopted a Capital Strategy by the end of financial year 2018/19.

3.3 Appendix 1 contains a draft Capital Strategy to fulfil the requirements of the Code. It sets out the principles by which we will make capital investment and aims to balance needs and expectations with available resources.

3.4 Members are invited to scrutinise the Strategy and satisfy themselves that it represents their collective view.

4. Policy Context

4.1 Adopting a Capital Strategy fulfils the Councils statutory duties:

5. Risk Management Implications

5.1 None. It is not considered that adopting this strategy brings forward any significant risk. All expenditure decisions are assessed individually.

6. Legal Implications

6.1 None.

7. Financial Implications

7.1 This report has no financial implications.

8. Equality and customer service implications

8.1 None.

9. Background Papers

9.1 None

Appendix 1

MID SUSSEX DISTRICT COUNCIL

CAPITAL STRATEGY 2019/20 to 2021/22

1. INTRODUCTION

1.1 Overview

This strategy forms the framework for capital investment decisions over the next three years and will inform the detailed annual capital budgets over this period. It is closely linked to the Treasury Management Strategy, the Investment Strategy and the Borrowing Strategy. The strategy aims to balance capital expenditure needs and expectations (e.g. replacement of business critical IT systems) with the scarcity of available resources.

1.2 Member approval and review

The Treasury Management Code allows authorities to delegate the detailed management of Treasury Management, including the Capital Strategy, to a sub-committee and this responsibility is delegated to the Audit Committee. This delegation will facilitate more active discussion of the Capital Strategy and its implementation, though overall responsibility will at all times remain with the full Council.

1.3 Strategic Direction of the Council

A key driver of the Capital Strategy is the Council's Statement of Main Purpose 'To be an effective Council delivering value for money services and helping to create a strong economy, environment and community' and the accompanying priorities:

- Efffective and responsive services
- Sustainable economic growth
- Strong and resilient communities
- Financial independence

This statement gives a strategic direction to the Council to enable it to meet the demands of the future.

1.4 Capital Expenditure

Capital expenditure, defined in accordance with the Council's approved accounting policies and procedures, can be funded in a variety of ways:

- Grants
- Section 106 contributions
- Capital receipts
- Direct Revenue contributions
- Borrowing

The method of funding for any particular scheme will depend on a number of factors and this is covered in more detail below. It should be noted that the Council has limited resources for the funding of capital expenditure,with

balances having reduced significantly over recent years due to the use of reserves for property investment, earmarking for certain specific projects and financing the overall capital programme.

1.5 Whole life costing for capital schemes

Whole life costing can be defined as "the systematic consideration of all relevant costs and revenues associated with the acquisition and ownership of an asset." In practical terms this means that any appraisal of a proposed capital project will need to consider not just the initial capital cost but all costs and income streams associated with the project that are likely to occur in future years, including possible replacement or disposal costs. This is vital to ensure that the Council is not committing itself to future liabilities that are unsustainable.

1.6 Scheme Evaluation and Risk

Any appraisal of proposed new capital schemes should include a full evaluation of risk, having regard to the whole life costing methodology set out above.

1.7 Monitoring of approved capital schemes

For approved capital schemes it is the responsibility of the relevant budget holder to manage costs and to provide explanations for any variations from the approved budget, in accordance with Financial Procedure Rules. Budget monitoring statements are presented to Corporate Management Team and Cabinet on a roughly quarterly basis.

2. GENERAL FUND PROGRAMME

2.1 Core annual programme

The Council has a core annual programme comprising asset management (all owned or leased assets), Information Technology and Disabled Facilities Grants (DFGs). DFGs pay for essential adaptations to help people with disabilities stay in their own homes. The DFG programme is entirely funded by Government Grant whereas the asset management and Information technology programmes are funded by revenue contributions.

2.2 Land and Property Revenue Reserve

A property investment fund has been established with the aim of acquiring properties to generate a return for the Council. Property acquisitions have been funded from earmarking a proportion of the Council's general reserve but in the future we will prioritise the use of receipts from land and property disposals. Acquisitions can only be made once a full business case has been completed and the risks fully understood and evaluated. Further details are set out in Corporate Plan 2017/18 which will be restated as a Property Investment Strategy and Process during the next year.

2.3 Other Schemes

In addition to the core annual programme other schemes will be considered subject to the criteria set out below. However, the key issue here is the modest funding, as reflected in the Council's medium term financial strategy which envisages only a modest programme. It is therefore particularly important that any new schemes have a clear benefit to ensure that limited resources are used in the most effective possible way.

2.4 Prioritising new schemes

In common with other local authorities Mid Sussex is facing a challenging financial climate and it is therefore essential that systems are in place to ensure that scarce resources are allocated in the most effective possible way. New schemes will be assessed against the following criteria:

- Link to the Council's strategic direction
- Availability of specific external funding
- Demonstration of a sound business case
- Whole life cost implications (see 1.5 above)
- Value for money

High priority will be given to the replacement of business critical IT systems for which we have created an ICT reserve to reduce the possibility of funding being unavailable.

New schemes will have a Justification Statement that sets out the key factors considered prior to approval by Members.

2.5 Affordability and available resources

In addition to considering the merits of individual schemes the Council will need to assess the overall affordability of any new programme, having regard to the availability of resources, existing financial commitments and the projected level of balances forecast in the medium term financial strategy. As outlined in 1.4 above, possible sources of funding for capital schemes are:

- Grants
- Section 106 contributions
- Capital receipts
- Direct Revenue contributions
- Borrowing

2.6 Specific resource issues

Grants and Section 106 contributions are generally used to fund specific capital schemes linked to the conditions imposed by the relevant grant or section 106 contribution. There is little, if any, latitude in the way this funding can be applied. Capital receipts are derived from the sale of the Council's assets. It is the Council's policy to use these receipts to support the General Fund capital programme. A proportion of these receipts may be earmarked for the purchase of land and property Reserve (see 2.2 above). Revenue contributions are a flexible source of funding but they put an immediate strain on the General Fund balance and can therefore only be used to a limited extent. Borrowing spreads the cost over a number of years but loan servicing costs and the overall level of debt exposure both need to be considered and clearly flagged in a business case.

2.7 Major schemes already approved and committed

The existing capital programme includes a number of schemes which the Council is fully committed to delivering, although these are not individually significant.. It is however likely that until capital receipts become available, the scale of approval for new schemes will be limited.

3. LINKS TO OTHER COUNCIL STRATEGIES

3.1 Treasury Management Strategy

The capital strategy is closely linked to the Treasury Management Strategy and it is essential that any investment decisions are informed by both strategies. In particular the assessment of affordability outlined in 3.5 above will need to have regard to the relevant elements of the Treasury Management Strategy including:

- The incremental impact of capital investment on council tax levels
- The borrowing strategy
- The authorised limit for external debt

3.2 Property Investment Strategy

This Strategy will set out the policies relating to the Land and Property Reserve (see above). While this is being worked up we are working to the general principles outlined in the 2016/17 Corporate Plan and the approval process contained therein; *'Individual transactions would need concurrent agreement by a variety of key Members, i.e. appropriate Cabinet Portfolio Holders and the Chairs of the Scrutiny Committee for Leader and Service Delivery and the Audit Committee.'*

3.3 Asset Management Strategy

As outlined in 2.1 above, there is a core annual programme to cover capitalised repairs and improvements for all the Council's assets. The asset management strategy establishes the priorities for this programme having regard to the condition of the various assets and their respective priorities in terms of delivering Council services or generating rental income.

Proposed New Projects - Capital Programme 2019/20 - 2022/23						
	Project Justification	Total 2019/20	Total 2020/21	Total 2021/22	Total 2022/23	Revenue Implications
Project		**£'000s**	**£'000s**	**£'000s**	**£'000s**	**£'000s**
ICT Projects/ CenSus ICT						
Workstation Replacement	Yes	50	50	50	50	
Relocation of IDOX Uniform and Northgate software to Oaklands	Yes	37				5
Firewall replacement	Yes	25				
Supporting Infrastructure Refresh	Yes	30				
Telephony System Replacement	Yes	120				
Total ICT Projects:		**262**	**50**	**50**	**50**	**0**
Others:						
Oaklands Window Replacement	Yes	183	177	234		
Total Others:		**183**	**177**	**234**	**0**	**0**
Major Capital Renewals						
Oaklands:						
Refurbish West Wing Grd Floor Gents W011	n/a	20				
Refurbish East Wing Kitchen E104	n/a	15				
Refurbish East Wing Gents	n/a	20				
Refurbish IT Suite	n/a	20				
Intruder Alarm Upgrade	n/a	30				
Pavilions:						
Cuckfield Rec Pavilion Refurbishment - Capital	n/a	57				
Car Parks:						
Tolgate Car Park Upgrade - Lindfield	n/a	22				
Trinity Road Car Park Upgrade- Hurstpierpoint	n/a	45				
Unallocated funding for future years	n/a		179	271	444	
Total Major Capital Renewals	n/a	**229**	**179**	**271**	**444**	**0**
Housing						
Affordable Housing	n/a		1,083			
Total Housing		**0**	**1,083**	**0**	**0**	**0**
Environmental Health						
Disabled Facility Grants	n/a	900	900	900		
Total Environmental Health		**900**	**900**	**900**	**0**	**0**
S106 Partly Funded Schemes:						
Pavilions:						
Cuckfield Rec Pavilion Refurbishment -community funding	n/a	27				
Total S106 Partly Funded Schemes:		**27**	**0**	**0**	**0**	**0**
Total New Capital Projects		**1,601**	**2,389**	**1,455**	**494**	**0**
Financed By:						
Grant Contributions WSCC		900	900	900	0	
S106 Agreements -time limited		27	0	0	0	
S106 Agreements -non time limited		0	0	0	0	
S106 Housing - non time limited		0	1,083	0	0	
Met from Revenue Contributions (for MCR)		229	179	271	444	
General Reserve		183	177	234	0	
Specific Reserve		262	50	50	50	
Total Financed:		**1,601**	**2,389**	**1,455**	**494**	**0**

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EXTERNAL AUDIT PLAN

REPORT OF:	Head of Corporate Resources
Contact Officer:	Peter Stuart, Head of Corporate Resources Email: Peter.Stuart@midsussex.gov.uk Tel: 01444 477315
Wards Affected:	All
Key Decision:	No
Date of Meeting:	25 February 2019

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1. Purpose of Report

To inform the Committee of the External Auditor's Audit Plan.

2. Recommendations

The Audit Committee is recommended to note the 2018/19 Audit Plan;

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3 **Background**

3.1 Attached at Appendix 1 is the Audit Plan which outlines the work and the emphasis to be given to our audit for this financial year.

3.2 Members will note that while there are no issues of particular concern this year, as part of the Value for Money assessment, the Auditors will consider the arrangements by which investment property is acquired. It should be stressed that this is not in response to any particular concern that has been raised specifically in relation to Mid Sussex. All authorities investing in commercial property are being subject to this diligence as a response to the sector's increasing exposure to this market.

3.3 The Audit Director will be able to elucidate on any points raised.

4 Financial implications

4.1 There are no financial implications arising from this report. .

5 Equalities implications

5.1 The report raises no implications of this nature.

6 Risk analysis

6.1 No material risks arise from this report

Background Papers
None

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EXTERNAL AUDIT: CERTIFICATION REPORT

REPORT OF:	Head of Corporate Resources
Contact Officer:	Peter Stuart, Head of Corporate Resources Email: Peter.Stuart@midsussex.gov.uk Tel: 01444 477315
Wards Affected:	All
Key Decision	No
Date of Meeting:	25 February 2019

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1. Purpose of Report

To inform the Committee of the External Auditor's Annual Report for the Certification of Claims and Returns 2017/18.

2. Recommendations

The Audit Committee is recommended to note the Certification of Claims and Returns Annual Report 2017/18.

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4 Background

4.1 Appendix 1 contains the report that sets out the findings from work to certify the Housing Benefit Subsidy claim. In essence, while the audit identified some minor quality issues with the underlying claims, this is a vastly improved position on previous years.

4.2 This year Members will be pleased to note that the level of error in the caseload is again much lower than in previous years and this is reflected in the level of overpayment and therefore repayment to DWP. This turnaround is a great achievement by the team and evidence that the training programme instigated over the past few years, with its emphasis on accuracy over speed has finally borne fruit.

4.3 The team aim to achieve an 'unqualified' opinion at the earliest opportunity.

5 Financial implications

5.1 There are no financial implications arising from this report. .

6 Equalities implications

6.1 The report raises no implications of this nature.

7 Risk analysis

7.1 No material risks arise from this report

Background Papers
None

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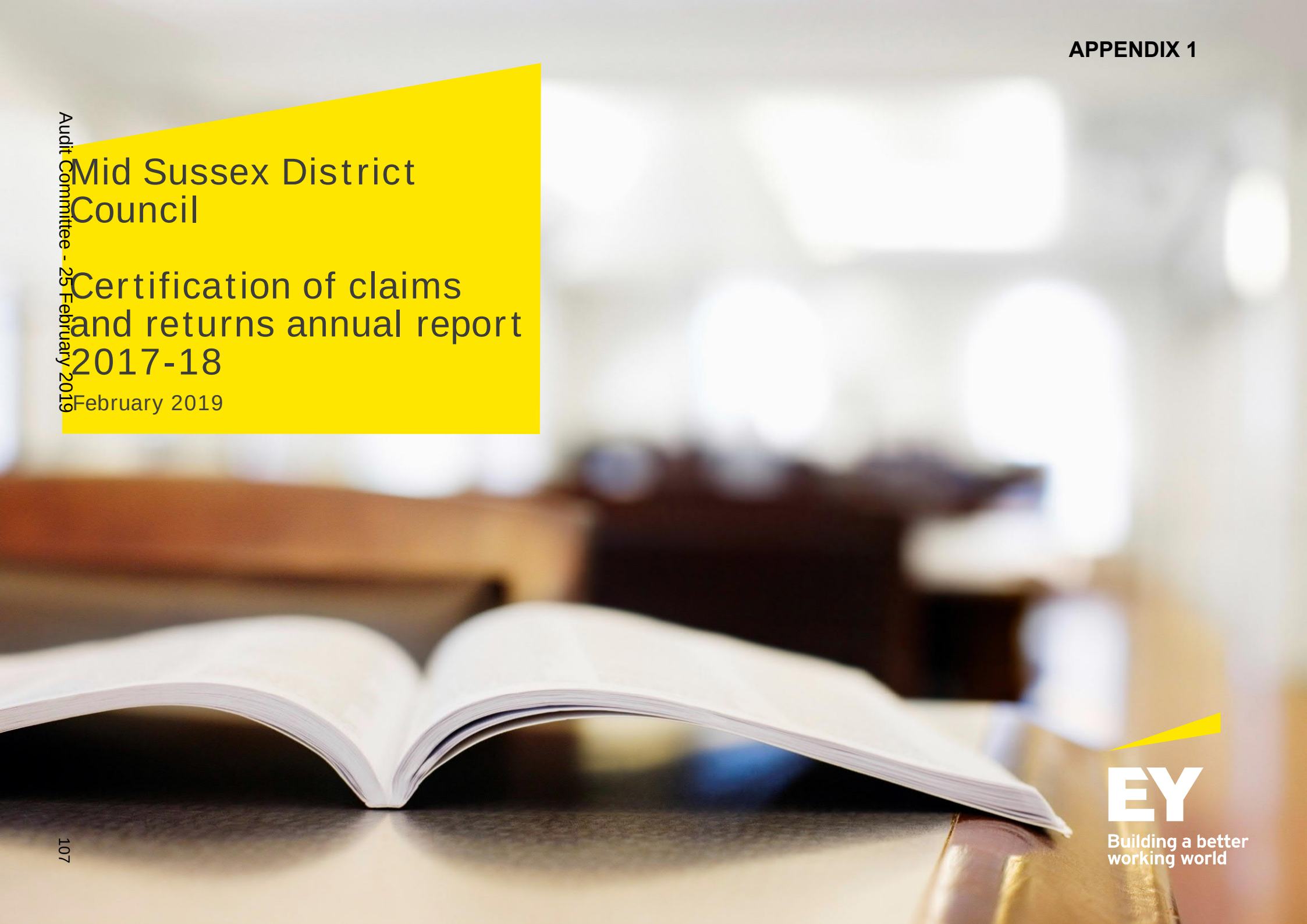
APPENDIX 1

Audit Committee - 25 February 2019

Mid Sussex District Council

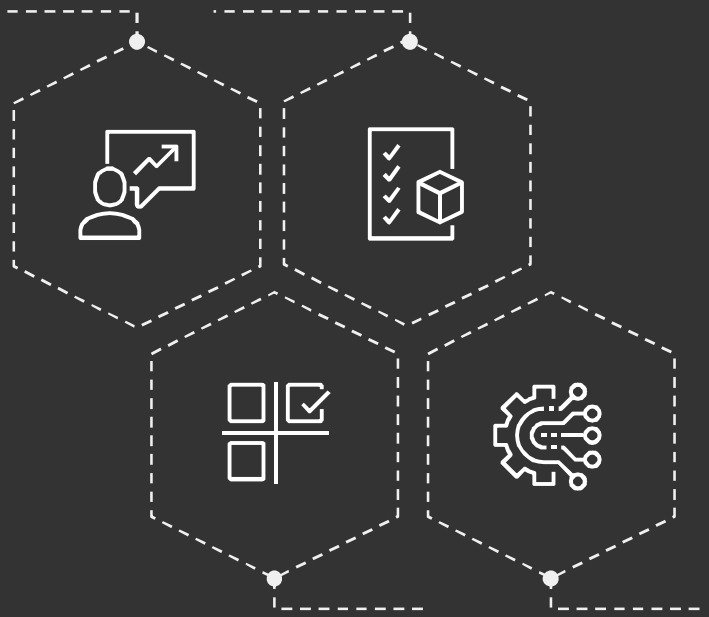
Certification of claims and returns annual report 2017-18

February 2019



Building a better working world

Contents



01 Housing benefits subsidy claim

Housing benefits subsidy claim

Scope of work	Results
Value of claim presented for certification	£32,312,436
Amended/Not amended	Amended but no impact on subsidy claimed.
Qualification letter	Yes
Fee – 2017-18	£17,858
Fee – 2016-17	£12,533

Recommendations from 2016-17	Findings in 2017-18
Undertake work or review the 2016-17 subsidy claims in high risk areas, such as claims with self-employed earnings and earned income, to ensure that these claims have been correctly processed and to reduce the likelihood of future qualifications of the subsidy claim.	Our certification work suggests progress has been made in reducing the quantity of error in each of the relevant areas, as shown by our extrapolated figures. The Council should continue to focus on ensuring those areas where we identified errors, to reduce the likelihood of future qualification further.

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 to claimants. We certify that claim.

The certification guidance requires reporting accountants to complete testing of an initial sample of 20 cases from each of the Non-HRA Rent Rebate and Rent Allowances case types, plus more extensive '40+' or extended testing if:

- initial testing identifies errors in the calculation of benefit or compilation of the claim; or,
- our cumulative knowledge and experience from prior year certifications gives us reason to expect errors in specific areas.

A number of errors were identified and extended testing was completed in relation to the following:

- Rent Allowance tenants:
    - Incorrect calculation of earned income: Testing of the initial sample identified two cases where benefit was overpaid and two cases where benefit was underpaid as a result of incorrectly calculating the claimants earnings. Testing of an additional random sample of 40 cases within cell 94 containing earned income identified four cases where benefit had been overpaid as a result of incorrectly calculating the claimants income and one case where the incorrect calculation of earned income had no impact on subsidy claimed. Overpayments totalled £1,124, which was extrapolated across the total population of Rent Allowance cases in cell 94 containing earned income. This extrapolated error totalled £64,749.

Housing benefits subsidy claim

- Incorrect recording of Working Tax Credit: Testing of the initial sample identified one case where a claimants Working Tax Credit was incorrectly recorded, resulting in an underpayment of benefit. As errors entering the Working Tax Credit could result in overpayments, an additional sample was tested. Over and underpayments were identified in one further case. The total value of overpayments was £3.24. This was extrapolated across all Rent Allowance cases which contained Working Tax Credit. This extrapolated error totalled £98.

Extended 40+ testing was undertaken in the following areas due our cumulative knowledge and experience from prior year certifications gives us reason to expect errors in specific areas.

Rent Allowances:

- Eligible Rent: Testing of the 2016/2017 claim identified errors in the rent used in the assessment calculations for benefit. Whilst no errors were identified in our initial sample of Rent Allowance claims in 2017/2018, using our knowledge of the subsidy claim, we selected an additional sample of 40 claims for testing from the headline cell. Testing of the sample identified one case where benefit had been overpaid as a result of the claimants rent liability being incorrectly recorded and used in the calculation of benefit. This error totalled £2.46 and was extrapolated across all cases within cell 94, Rent Allowances. This extrapolated error totalled £180.
- Classification of Overpayments: Testing of the 2016/2017 claim identified errors in the classification of overpayments, where evidence did not support their classification as eligible overpayments. Whilst no errors were identified in our initial sample of Rent Allowance claims in 2017/2018, using our knowledge of the subsidy claim, we selected an additional sample of 40 claims for testing from cell 114 Rent Allowances – Eligible Overpayments. Testing of the sample of 40 cases identified one case where benefit had been overpaid as a result of the claimants rent liability being incorrectly recorded. This error totalled £46 and was extrapolated across all overpayments classified as eligible (cell 114). This extrapolated error totalled £1,149.

We identified one further issue relating to the Council's Risk Based Verification policy that was reported to the DWP in our Qualification Letter:

Our testing identified that while the Authority has an RBV policy in place for the 2017/2018 year:

a) a report was not made from the Section 151 Officer to Members before the RBV policy was approved for the 2017/2018 financial year; and,

b) the RBV policy has not been formally approved by Members for the 2017/2018 financial year.

We note HB/CTB circular S11/2011 states that any failure by the local authority to apply its RBV policy causes expenditure to be treated as local authority error (error type 6 - failure to apply RBV policy). However, while the policy had not been properly approved, the policy had been appropriately applied to RBV cases. We have therefore not noted these items as failures in our testing. We have been informed that the Authority will ensure that the RBV Policy for 2018/19 is approved by members and that in view of the reduction of new claims due to the roll out of Universal Credit the Authority will be with member support withdrawing the RBV Policy from the 1 April 2019 and introducing a new Verification Policy to protect against Fraud.

03 2017-18 certification fees

2017-18 certification fees

Public Sector Audit Appointments Ltd (PSAA) determine an indicative fee each year for the certification of the housing benefits subsidy claim. For 2017-18, these fees were published by PSAA and are available on their website (www.psaa.co.uk).

Claim or return	2017-18	2017-18	2016-17
	Actual fee £	Indicative fee £	Actual fee £
Housing benefits subsidy claim	17,858	17,858	12,533

Actual fee represents the fee payable as set by the PSAA.

04 Looking forward

Looking forward

2018/19 and beyond

From 2018/19, the Council is responsible for appointing their own reporting accountant to undertake the work on their claims in accordance with the instructions determined by the relevant grant paying body.

As your appointed auditor for the financial statements audit, we are pleased that for 2018-19 the Council has appointed us to act as reporting accountants in relation to the certification of the Housing Benefit Subsidy Claim.

We welcome this opportunity to continue undertaking this work for the Council providing a seamless quality service, drawing on vast array of experienced and knowledgeable public sector professionals in these areas, whilst realising the synergies and efficiencies that are achieved by undertaking both the audit and grant work.

05 Summary of recommendations

Summary of recommendations

This section highlights the recommendations from our work and the actions agreed.

Recommendation	Priority	Agreed action and comment	Deadline	Responsible officer
Housing benefits subsidy claim	Medium	Quality assurance processes need to continue to be focused around those areas where errors were identified, particularly calculation of claimant income.	31/3/19	Kevin Stewart

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