

Governance Committee

Monday, 9th February, 2015
at 5.00 pm

PLEASE NOTE TIME OF MEETING

Conference Room 3 - Civic Centre

This meeting is open to the public

Members of the Committee

Councillor Burke (Chair)
Councillor Chamberlain
Councillor Daunt
Councillor Inglis
Councillor Keogh (Vice-Chair)
Councillor Noon
Councillor O'Neill

Independent Members

Mr David Blake
Mr Geoff Wilkinson

Contacts

Head of Legal and Democratic Services
Richard Ivory
Tel. 023 8083 2394
Email: richard.ivory@southampton.gov.uk

Democratic Support Officer
Pat Wood
Tel. 023 8083 2302
Email: pat.wood@southampton.gov.uk

PUBLIC INFORMATION

Role of the Governance Committee

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

[02 Part 2 - Articles](#)

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

Public Representations

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

Southampton City Council's Priorities:

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

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

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

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

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

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

Dates of Meetings: Municipal Year 2014/15

2014	2015
14 July	9 February
15 September	27 April
15 December	

CONDUCT OF MEETING

Terms of Reference

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

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

Rules of Procedure

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

Business to be discussed

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

Quorum

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

DISCLOSURE OF INTERESTS

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

DISCLOSABLE PECUNIARY INTERESTS

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

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

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

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

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

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

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

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

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

Other Interests

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

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

Any public authority or body exercising functions of a public nature

Any body directed to charitable purposes

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

Principles of Decision Making

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

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

In exercising discretion, the decision maker must:

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

AGENDA

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

1 APOLOGIES

To receive any apologies.

2 DISCLOSURE OF PERSONAL AND PECUNIARY INTERESTS

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

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

3 STATEMENT FROM THE CHAIR

4 MINUTES OF PREVIOUS MEETING (INCLUDING MATTERS ARISING)

(Pages 1 - 2)

To approve and sign as a correct record the Minutes of the meeting held on 15 December 2014 and to deal with any matters arising, attached.

5 ANNUAL GOVERNANCE STATEMENT (Pages 3 - 10)

Report of the Chief Financial Officer seeking to approve the assurance gathering process to support the development of the 2014-15 Annual Governance Statement and to note the content of the 2013-14 Action Plan, attached.

6 TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS 2015/16 TO 2017/18 (Pages 11 - 50)

Report of the Chief Financial Officer regarding the Council's proposed treasury management strategy for the coming year in relation to the Council's cash flow, investment and borrowing, and the management of the numerous risks related to this activity, attached.

7 INTERNAL AUDIT PROGRESS REPORT - DECEMBER 2014 (Pages 51 - 74)

Report of the Chief Internal Auditor providing a progress report on the Internal Audit Progress for the period to December 2014, attached.

8 EXTERNAL AUDIT - CERTIFICATION OF CLAIMS AND RETURNS ANNUAL REPORT 2013/14 (Pages 75 - 86)

To consider the report of the Chief Internal Auditor regarding the External Auditor's annual report on the Certification of Claims and Returns 2013/14, attached.

9 LOCALISM ACT 2011 - APPOINTMENT OF DESIGNATED INDEPENDENT PERSON (S) AND GOVERNANCE COMMITTEE INDEPENDENT MEMBERS
(Pages 87 - 90)

Report of Head of Legal and Democratic Services regarding the need for independent members and the appointment of Designated Independent Persons, attached.

Friday, 30 January 2015

Head of Legal and Democratic Services

GOVERNANCE COMMITTEE

MINUTES OF THE MEETING HELD ON MONDAY, 15 DECEMBER 2014

Present:

Members of the Council

Burke (Chair), Daunt, Inglis, Keogh (Vice-Chair), Noon and O'Neill

Independent Members

Mr David Blake and Mr Geoff Wilkinson

Apologies

Councillor Chamberlain

23. **STATEMENT FROM THE CHAIR**

The Chair, on behalf of the Committee, expressed appreciation and thanks to Kate Handy who was leaving Ernst & Young, the Council's Auditors.

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

RESOLVED: that the minutes for the Committee meeting held on 17th November 2014 be approved and signed as a correct record.

25. **RISK MANAGEMENT FRAMEWORK AND REPORTING**

The Committee considered the report of the Chief Financial Officer detailing the risk management framework and reporting procedures.

RESOLVED

- (i) To note the 'Strategic Risks' for 2014-15 (Appendix 1); and
- (ii) To note the 'Summary of Directorate Risk Registers' (Appendix 2).

26. **EXTERNAL AUDITORS - ANNUAL AUDIT LETTER**

The Committee considered the report of the Chief Internal Auditor detailing the External Auditors' Annual Audit letter for 2013/14.

RESOLVED to note the External Auditors' Annual Audit letter.

This page is intentionally left blank

Agenda Item 5

DECISION-MAKER:	GOVERNANCE COMMITTEE		
SUBJECT:	ANNUAL GOVERNANCE STATEMENT		
DATE OF DECISION:	9 FEBRUARY 2015		
REPORT OF:	CHIEF FINANCIAL OFFICER		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Peter Rogers	Tel: 023 8083 2835
	E-mail:	peter.rogers@southampton.gov.uk	
Director	Name:	Andy Lowe	Tel: 023 8083 2049
	E-mail:	andrew.lowe@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY	
None	
BRIEF SUMMARY	
In accordance with the Accounts and Audit Regulations the Council is required to develop and publish an Annual Governance Statement ('AGS'). The AGS reports on the extent to which the Council has complied with its Code of Corporate Governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.	
RECOMMENDATIONS:	
(i)	To note and approve the assurance gathering process to support the development of the 2014-15 Annual Governance Statement (Appendix 1); and
(ii)	To note the content of the Annual Governance Statement 2013-14 Action Plan - Status Report (Appendix 2).
REASONS FOR REPORT RECOMMENDATIONS	
1.	The Governance Committee has responsibility to provide independent assurance on the adequacy of the risk management framework and the internal control and reporting environment, including (but not limited to) the reliability of the financial reporting process and the annual governance statement.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	No alternative options have been considered
DETAIL (Including consultation carried out)	
3.	Regulation 4(3) of the Accounts and Audit (England) Regulations 2011 requires that the relevant body must conduct a review at least once a year of the effectiveness of its system of internal control and to prepare a statement on internal control in accordance with proper practices.
4.	The purpose of the AGS, which is published with the statement of accounts, is to provide an accurate representation of the corporate governance arrangements in place during the year and to identify or highlight those areas

	where there are significant gaps or where improvements are required.
5.	The AGS is produced following a review of the Council's governance arrangements. The review requires the systems and processes that comprise the Council's corporate governance arrangements to be brought together and reviewed.
6.	An 'assurance gathering process' based on CIPFA/SOLACE guidance is in place and comprises an overall 'Assurance Framework' document together with 'Annual Governance - Self Assessment Statement' completed by each Director. Both the documents cover the key processes and systems that comprise the Council's governance arrangements and are intended to identify any areas where improvement or further development is required.
7.	The process to support the development of the AGS is largely unchanged from the previous year on the basis that it is considered that it is aligned with good practice. In addition, External Audit, who are 'required to consider the completeness of the disclosures in the Authority's AGS, identify any inconsistencies with the other information of which they are aware of from their work, and to consider whether it complies with CIPFA/SOLACE guidance' stated in their Annual Audit letter (October 2014) that they had "no issues to report".
8.	The AGS itself is developed by a 'Controls Assurance Management Group' (comprising the Section 151 Officer, Chair of the Governance Committee, Monitoring Officer and Chief Internal Auditor) who are responsible for evaluating the assurances and supporting evidence provided, prior to drafting the AGS.
9.	The draft AGS will be presented to the Governance Committee for review and approval prior to being forwarded to the Chief Executive and Leader of the Council for signing.
RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
10.	None
<u>Property/Other</u>	
11.	None
LEGAL IMPLICATIONS	
<u>Statutory power to undertake proposals in the report:</u>	
12.	The Accounts and Audit (England) Regulations 2011 require the Council to adopt Good Governance arrangements in respect of the discharge of its functions. The above arrangements are intended to meet those responsibilities.
<u>Other Legal Implications:</u>	
13.	None
POLICY FRAMEWORK IMPLICATIONS	
14.	None

KEY DECISION?	No	
WARDS/COMMUNITIES AFFECTED:	n/a	
<u>SUPPORTING DOCUMENTATION</u>		
Appendices		
1.	AGS 2014-15 : Process and timelines	
2.	AGS 2013-14 Action Plan - Status Report	
Documents In Members' Rooms		
1.	None	
Equality Impact Assessment		
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.		No
Other Background Documents		
Equality Impact Assessment and Other Background documents available for inspection at:		
Title of Background Paper(s)		Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	None	

This page is intentionally left blank

Annual Governance Statement 2014/15 - Process and timelines

Action	Meeting / Target Date	Responsibility
Report to Governance Committee to outline the assurance gathering process to support development of the 2013-14 AGS.	9th Feb 2015	Governance Committee
Review and update the 'AGS - Self Assessment Statement' document to ensure that it remains aligned with good practice.	9th - 27th February 2015	Risk & Assurance Manager
Review of the Code of Corporate Governance against current CIPFA/SOLACE guidance.	2nd -23rd March 2015	Risk & Assurance Manager
Issue 'AGS Self Assessment Statements' to Directors for completion	1st April 2015	Risk & Assurance Manager
Return of completed 'AGS Self Assessment Statements' and completion of Assurance Framework document.	24th April 2015	Council Management Team
Validation of self assessments by Internal Audit.	27th April - 8th May 2015	Chief Internal Auditor
Draft AGS developed in consultation with Controls Assurance Management Group . NOTE: further ad hoc meetings may be required and will be arranged as necessary.	15th May 2015	Controls Assurance Management Group
Report to CMT to review the draft 2013-14 AGS.	19th May 2015	Council Management Team
Report to Governance Committee to review draft 14-15 AGS.	May/July 2015? (tbc)	Governance Committee
Submission of final draft of AGS to Council Management Team.	August 2015 (TBC)	Council Management Team
Final draft AGS to CAMG for noting.	September 2015 (TBC)	Controls Assurance Management Group
Report to Governance Committee for final approval of AGS.	September 2015 (tbc)	Governance Committee
Signed by Chief Executive and Leader of the Council.	30th September 2015	Risk & Assurance Manager

This page is intentionally left blank

ANNUAL GOVERNANCE STATEMENT 2013-14: Status Report

The following is a summary of the status of the agreed actions that were identified to address the significant governance issues were identified and recorded on the Council's Annual Governance Statement 2013-14:

	Governance Issue	Agreed Action	Target Date	Responsible Officer	Status	Comments
1.	The Council's Anti Money Laundering Policy has not been updated since Feb 2009.	Policy to be reviewed and updated to reflect current good practice together with a commitment for future periodic reviews. Appropriate arrangements to be made to communicate the updated policy.	July 2014	Director of Corporate Services	COMPLETED (July 2014)	Updated document published on the intranet in July 2014 (next review date 2017).
2.	The Corporate Procurement Strategy refers to the period 2009-12	Contract Procedure Rules to be reviewed and updated by end of 2014 with the revised and updated Strategy by early 2015.	March 2015 (revised to June 2015)	Director of Corporate Services	Open	The updated Corporate Procurement Strategy and the associated Contract Procedure Rules are expected to be published in June 2015. The slippage reflects that the lead officer has been seconded to lead on the Infrastructure Transformation workstream.
3.	Transparency information published on the internet includes a Members' 'Gifts & Hospitality Register' however the last entry on the document is dated April 2012.	The requirement to make such declarations was dropped when the new code, under the Localism Act, came into being in July 2012. It is however considered appropriate, in terms of transparency, to review the current approach to the publication of Members' 'Gifts and Hospitality'. A report to be taken to Governance Committee in Sept 14 with both an updated draft Code and proposed addition in relation to members gifts and hospitality with a de minimus level of £50 for registration.	Sept 2014	Director of Corporate Services	COMPLETED (Nov 2014)	Proposal approved and adopted as per the minutes of the Governance Committee meeting of 15 th September 2014 and the minutes of the Full Council meeting on 19 th November 2014.

4.	The 'Children's Services & Learning Complaints and Representation Procedure' published on the internet is dated September 2006.	Review and update the 'Children's Services & Learning Complaints and Representation Procedure' to ensure that it remains aligned with statutory procedures with a commitment for future periodic reviews.	July 2014	Director of Corporate Services	Open	Updated document published on the internet in July 2014.
5.	Understanding of and compliance with Information Governance policies and procedures.	Information Governance e-learning (including Data Protection, Freedom Of Information Act and Protecting Information) to be mandatory for all staff and new starters.	Ongoing	Director of Corporate Services	Ongoing	There is now a set of online training modules covering Information Governance through the Learning and Development Portal. These are mandatory for all staff to complete (and pass). Quarterly reports are considered by CMT
6.	Business continuity plans need to reflect the high level of organisational change that has taken place and is ongoing.	Business continuity plans to be reviewed, tested and evaluated to ensure that they reflect the new organisational structure.	May 2015	Director, Place	Open	On track for May target date. New Business Continuity policy and templates have been drafted.
7.	Understanding of and compliance with the council's 'Corporate Standards'	Learning and communication exercise to be rolled out to relevant officers in respect of the legal decision making process.	Commence Autumn 14	Director of Corporate Services	See comment	This has not been actioned due to competing priorities and reduction in resources. At the moment the H of LDS is unable to give any definitive date when it will be able to commence this project.

Agenda Item 6

DECISION-MAKER:	GOVERNANCE COMMITTEE COUNCIL		
SUBJECT:	TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS 2015/16 TO 2017/18		
DATE OF DECISION:	9 FEBRUARY 2015 11 FEBRUARY 2015		
REPORT OF:	CHIEF FINANCIAL OFFICER		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Mel Creighton	Tel: 023 8083 4897
	E-mail:	Mel.Creighton@southampton.gov.uk	
CFO	Name:	Andrew Lowe	Tel: 023 8083 2049
	E-mail:	Andrew.Lowe@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY

NOT APPLICABLE

BRIEF SUMMARY

This report explains the context within which the Council's treasury management activity operates and sets out a proposed strategy for the coming year in relation to the Council's cash flow, investment and borrowing, and the management of the numerous risks related to this activity.

The core elements of the 2015/16 strategy are :

- To continue to make use of short term variable rate debt to take advantage of the current market conditions of low interest rates.
- To constantly review longer term forecasts and to lock in to longer term rates through a variety of instruments, as appropriate during the year, in order to provide a balanced portfolio against interest rate risk.
- To secure the best short term rates for borrowing and investments consistent with maintaining flexibility and liquidity within the portfolio.
- To invest surplus funds prudently, the Council's priorities being:
 - Security of invested capital
 - Liquidity of invested capital
 - An optimum yield which is commensurate with security and liquidity.
- To approve borrowing limits that provide for debt restructuring opportunities and to pursue debt restructuring where appropriate and within the Council's risk boundaries

With overall annual expenditure in excess of £600M and an extensive capital programme, the Council is required to actively manage its cash-flows on a daily basis. The requirement to invest or to borrow monies to finance capital programmes, and to cover daily operational needs, is an integral part of daily cash and investment portfolio management.

As at 31 March 2015 the Council's gross external debt is expected to be £360M and the total value of investments is forecast at £70M. The Balance Sheet position as at 31

March 2014 showed the value of debt as £352M and the value of investments as £69M. The Council's Capital Financing Requirement (CFR), which measures the Council's underlying need to borrow for capital purposes and represents the cumulative capital expenditure which has not yet been paid for from either revenue or capital resources, is a key driver of the borrowing strategy. The projected CFR for 31 March 2015 is £423M, of which £266M is attributed to the General Fund and the remaining £157M to the Housing Revenue Account (HRA).

The Council's current strategy is to minimise borrowing to below its CFR, the difference representing balances, reserves, provisions and working capital. This approach lowers interest costs, reduces credit risk and relieves pressure on the Council's counterparty list. Borrowing is restricted to a few highly secure sources which include the Public Works Loan Board (PWLB), commercial banks, the European Investment Bank, structured finance, and products associated with other local authorities. Additionally, borrowing is restricted by two limits, the Authorised Limit, (a statutory limit that sets the maximum level of external borrowing on a gross basis), and the Operational Boundary, (which is determined by both the estimated CFR and day to day cash flow movements). For 2015/16 the proposed Authorised Limit is £727M and proposed Operational Boundary is £553M. These are substantially higher than our anticipated actual level of debt but they allow for debt restructure to be undertaken if an appropriate opportunity arises, which may require taking new borrowing in advance of paying off existing loans.

Throughout the year, capital expenditure levels, market conditions and interest rate levels are monitored to minimise borrowing costs over the medium to longer term and to maintain stability. The differential between debt costs and investment earnings continues to be acute, resulting in the use of internal resources in lieu of borrowing often being the most cost effective means of financing capital expenditure. An additional strand of the strategy is to actively monitor opportunities arising for debt rescheduling in order to deliver savings in interest costs but with minimal risk, and to balance the ratio of fixed rate to variable rate debt within the portfolio.

In order to service the Council's day to day cash needs, the Council maintains a portfolio of short term investments. The Council's investment priorities are: the security of invested capital, the liquidity of invested capital, and the optimum yield that is commensurate with security and liquidity, in that order. The report details the Council's investment strategy, explains the institutions (counterparties) with whom the Council is permitted to invest, the limits related to the size of individual investments and the overall holding with institutions.

As a result of continued pressure and uncertainty within the financial markets, the security of any investment is the key consideration in decision making and a cautious approach will always be adopted. Whilst this report identifies all permitted options in investment decision making, tighter controls govern daily activity limiting the number of counterparties with whom investments will be placed and the value of the total holding with any single institution. Regular monitoring of all institutions on the counterparty list is part of daily treasury management. Although not relevant in the present climate, in any period of significant stress in the markets, the default position will be to invest with the government's Debt Management Office (DMO).

The impact of interest rates is crucial to all treasury management activity and forecasts of interest rate movements are taken into account in developing treasury management strategy. Consequently, this strategy is kept under review and, taking market information into account, will be realigned, if required, in line with evolving market conditions and expectations for future interest rates.

RECOMMENDATIONS:

GOVERNANCE COMMITTEE

- i) to endorse the Treasury Management (TM) Strategy for 2015/16 as outlined in the report;
- ii) to note that the indicators as reported have been set on the assumption that the recommendations in the Capital Update report will be approved by Council on 11 February 2015. Should the recommendations change, the Prudential Indicators may have to be recalculated; and
- iii) to note that due to the early timing of this report, changes may still be required following the finalisation of capital and revenue budgets and therefore any significant changes to this report will be highlighted in the final version that is presented to Full Council.

COUNCIL

- i) to approve the Council's Treasury Management (TM) Strategy and Prudential Indicators for 2015/16, 2016/17 and 2017/18, as detailed within the report;
- ii) to approve the 2015 Minimum Revenue Provision (MRP) Statement as detailed in paragraphs 68 to 77;
- iii) to approve the Annual Investment Strategy as detailed in paragraphs 37 to 48;
- iv) to note that at the time of writing this report the recommendations in the Capital Programme Update report, submitted to Council on the 11 February 2015, have not yet been approved. The indicators in the report are based on the assumption that they will be approved, but should the recommendations change, the Prudential Indicators may have to be recalculated; and
- v) to continue to delegate authority to the Chief Financial Officer (CFO), following consultation with the Cabinet Member for Resources to approve any changes to the Prudential Indicators or borrowing limits that will aid good treasury management. For example, agreeing an increase in the percentage for variable rate borrowing to take advantage of the depressed market for short term rates. Any amendments will be reported as part of quarterly financial and performance monitoring and in revisions to the TM Strategy.

REASONS FOR REPORT RECOMMENDATIONS

In order to comply with Part 1 of the Local Government Act 2003, and the established TM procedures that have been adopted by the Authority, each year the Council must set certain borrowing limits and approve TM Strategy which includes:

- Treasury Management Strategy for 2015/16:
 - Borrowing – Paragraphs 22 to 34,
 - Debt Rescheduling – Paragraphs 35 to 36
 - Investments – Paragraphs 37 to 48
- Treasury Management Indicators – Paragraphs 49-66
- MRP Statement – Paragraphs 68 to 77
- Other Prudential Indicators – Paragraphs 80 to 94

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

1. Alternative options for borrowing would depend on decisions taken on the review of the capital programme, which are being taken at Full Council on 11 February 2015.

DETAIL (Including consultation carried out)

CONSULTATION

2. The proposed Capital Programme Update report on which this report is based has been subject to separate consultation processes.

BACKGROUND

3. The Local Government Act 2003 introduced a system for borrowing based largely on self-regulation by local authorities themselves. The basic principle of the new system is that local authorities will be free to borrow as long as their capital spending plans are affordable, prudent and sustainable.
4. The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services, (the "CIPFA TM Code"), and the Prudential Code require local authorities to determine a Treasury Management Strategy Statement (TMSS) and Prudential Indicators (PIs) on an annual basis. The TMSS also incorporates the Annual Investment Strategy (AIS), which is a requirement of the Department for Communities and Local Government's (CLG) Investment Guidance.
5. As per the requirements of the Prudential code, the Authority has adopted the CIPFA Treasury Management Code at its Council meeting on 19 February 2003 and all subsequent updates.
6. The Authority has borrowed and invested substantial sums of money and therefore has potential large exposures to financial risks including the loss of invested funds and the effect of changing interest rates. The successful identification, monitoring and control of risk is the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council. The main risks to the Council's treasury activities are:
 - Liquidity Risk (Inadequate cash resources)
 - Market or Interest Rate Risk (Fluctuations in interest rate levels and thereby in the value of investments).
 - Inflation Risks (Exposure to inflation)
 - Credit and Counterparty Risk (Security of Investments)
 - Refinancing Risks (Impact of debt maturing in future years)
 - Legal & Regulatory Risk (i.e. non-compliance with statutory and regulatory requirements, risk of fraud)
7. The purpose of this TMSS is to allow Council to approve:
 - Treasury Management Strategy for 2015/16
 - Annual Investment Strategy 2015/16
 - Prudential Indicators for 2015/16, 2016/17 and 2016/17

- 2015 MRP Statement

8. The strategy takes into account the impact of the Council’s Revenue Budget and Capital Programme on the Balance Sheet position, the Prudential Indicators and the current and projected Treasury position (Appendix 1). The outlook for interest rates (Appendix 2) has also been taken into account in developing this strategy

9. The Council acknowledges that effective TM will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in TM, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management. To aid the Council in carrying out its TM function, it has appointed TM Advisors (Arlingclose), who advise the Council on strategy and provide market information to aid decision making. However it should be noted that the decisions are taken independently by the CFO taking into account this advice and other internal and external factors.

10. Some alternative strategies, with their financial and risk management implications, are listed below.

Options	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses will be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs will be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long term costs will be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs will be less certain

11. All treasury activity will comply with relevant statute, guidance and accounting standards.

Economic Background

12. There is momentum in the UK economy, with a continued period of growth through domestically-driven activity and strong household consumption. There are signs that growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansion of GDP. However, inflationary pressure is currently extremely benign and is likely to remain low in the short-term. There have been large falls in unemployment but levels of part-time working, self-employment and underemployment are

significant and nominal earnings growth remains weak and below inflation.

13. The Monetary Policy Committee's (MPC) focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee. Despite two MPC members having voted for an 0.25% increase in rates at each of the meetings August 2014 the minutes of the January 2015 meeting showed unanimity in maintaining the Bank Rate at 0.5% as there was sufficient risk that low inflation could become entrenched and the MPC became more concerned about the economic outlook.

Credit outlook

14. The transposition of two European Union directives into UK legislation in the coming months will place the burden of rescuing failing EU banks disproportionately onto unsecured local authority investors. The *Bank Recovery and Resolution Directive* promotes the interests of individual and small businesses covered by the Financial Services Compensation Scheme and similar European schemes, while the recast *Deposit Guarantee Schemes Directive* includes large companies into these schemes. The combined effect of these two changes is to leave public authorities and financial organisations (including pension funds) as the only senior creditors likely to incur losses in a failing bank after July 2015.
15. The continued global economic recovery has led to a general improvement in credit conditions since last year. This is evidenced by a fall in the credit default swap spreads of banks and companies around the world. However, due to the above legislative changes, the credit risk associated with making unsecured bank deposits will increase relative to the risk of other investment options available to the Authority.

Outlook for Interest Rates

16. The Authority's treasury management advisor Arlingclose forecasts the first rise in official interest rates in August 2015 and a gradual pace of increases thereafter, with the average for 2015/16 being around 0.75%, they also believe the normalised level of the Bank Rate post-crisis to range between 2.5% and 3.5%. The risk to the upside (i.e. interest rates being higher) is weighted more towards the end of the forecast horizon. On the downside, Eurozone weakness and the threat of deflation have increased the risks to the durability of UK growth. If the negative indicators from the Eurozone become more entrenched, the Bank of England will likely defer rate rises to later in the year. Our Advisors projects gilt yields on an upward path in the medium term, taking the forecast average 10 year PWLB loan rate for 2015/16 to 2.7%. A more detailed economic and interest rate forecast provided by the Authority's treasury management advisor is attached at Appendix 2.

Balance Sheet and Treasury Position

17. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The CFR, together with balances and useable reserves, are the core drivers of TM Activity.
18. As at the 31 December 2014 the Authority had £334M of debt (£256M borrowing plus £78M other long term liabilities) and £76M investments which is set out in further detail in Appendix 1.
19. The Authority is able to borrow funds in excess of the current level of its CFR up to the projected level in 2017/18. The Authority is likely to only borrow in

advance of need if it felt the benefits of borrowing at interest rates now compared to where they are expected to be in the future, outweighs the current cost and risks associated with investing the proceeds until the borrowing was actually required.

20. The forecast movement in the CFR in coming years is one of the Prudential Indicators (PIs). The movement in actual external debt and usable reserves combine to identify the Authority's borrowing requirement and potential investment strategy in the current and future years is shown below.

	31/03/2014 Actual £M	31/03/2015 Approved £M	31/03/2015 Estimate £M	31/03/2016 Estimate £M	31/03/2017 Estimate £M	31/03/2018 Estimate £M
General Fund CFR	266	261	266	258	246	237
Housing CFR	159	185	157	187	196	193
Total CFR	425	446	423	445	442	430
Less Other Long Term Liabilities	(78)	(78)	(83)	(80)	(76)	(74)
Borrowing CFR	347	368	340	365	366	356
Less External borrowing	(274)	(283)	(253)	(241)	(230)	(218)
Internal (over) borrowing	73	85	88	124	136	138
Less Usable Reserves and Net Creditors	(136)	(66)	(92)	(71)	(68)	(57)
Net Borrowing Requirement / (internal Borrowing Capacity)	(63)	19	(4)	53	68	81

21. In order to demonstrate the Authority's need to borrow the table above reflects the increased capital borrowing and projected CFR as a result of the proposed capital programme and forecast fall in balances, but only shows loans to which the Authority is already committed, it excludes optional refinancing as a result of loans maturing or new capital borrowing .

BORROWING STRATEGY

22. The Authority currently holds £256M of loans, a decrease of £18M on the previous year (£274M), as part of its strategy for funding previous years' capital programmes. The balance sheet forecast identifies a need to borrow and the Authority expects to borrow up to £4M in 2014/15 and up to £77M between 2015/16 and 2017/18 to fund the capital programme (£54M) and to cover the expected fall in balances and cash flow requirements. The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing (see paragraph 90).
23. The Authority's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the Authority's long-term plans change is a secondary objective.
24. Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

25. By doing so, the Authority is able to reduce net borrowing costs (despite reducing investment income) and reduce overall treasury risk. Whilst such a strategy is most likely to be beneficial over the next 2-3 years as official interest rates remain low, it is unlikely to be sustained in the medium-term. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Our Advisors will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2015/16 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
26. In addition, the Authority may borrow short-term loans (normally for up to one month) to cover unexpected cash flow shortages.
27. The approved sources of long-term and short-term borrowing are:
- Public Works Loan Board (PWLB) and its successor body (see below)
 - Local authorities
 - Any institution approved for investments
 - Any other bank or building society authorised to operate in the UK
 - UK public and private sector pension funds (except Hampshire County Council)
 - Capital markets bond investors (stock issues, commercial paper and bills)
 - Local Capital Finance Company and other special purpose companies created to enable joint local authority bond issues (see paragraph 30 below for further details).
28. In addition, capital financing may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- Operating and finance leases
 - Hire purchase
 - Private Finance Initiative
 - Sale and leaseback
29. The Authority has previously raised the majority of its long-term borrowing from the PWLB, but it continues to investigate other sources of finance, such as local authority loans and bank loans, that may be available at more favourable rates. The Department of Communities & Local Government (CLG) has recently announced HM Treasury (HMT) are taking the necessary legislative steps to abolish the PWLB in the coming months. Whilst this announcement sounds dramatic both the CLG and HMT have stressed that this development is purely being taken to address the governance of the PWLB. The CLG have stated that it will have no impact on existing loans held by local authorities or the government's policy on local authority borrowing.
30. **LGA Bond Agency:** A Local Capital Finance Company (LCFC) was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for three reasons: borrowing authorities may be required to provide bond investors with a joint and several guarantee over the very small risk that other local authority borrowers default on their loans; there

will be a lead time of several months between committing to borrow and knowing the interest rate payable; and up to 5% of the loan proceeds will be withheld from the Authority and used to bolster the Agency's capital strength instead. The Authority is considering investing up to £0.02M in the LCFC to enable us to borrow from the Agency, subject to approval of a recommendation within the Council Tax and Budget Setting report.

31. The HRA has a material borrowing need in the short term whilst the General Fund has an estimated £35M reserves in the medium term which are invested. An alternative is to use some of the General Fund investment monies to act as lender to the HRA for some of their borrowing needs. Whilst it is not intended at this time to utilise this facility in 2015/16, it does remain a viable option. Further work with Arlingclose is being undertaken to determine the most appropriate mechanism for achieving this, in the event that this is progressed.
32. The Authority has £9M exposure to LOBO loans all of which can be "called" within 2015/16. A LOBO is called when the Lender exercises their right to amend the interest rate on the loan at which point the Borrower can accept the revised terms or reject them and repay the loan. Although unlikely in the low interest rate environment LOBO loans present a potential refinancing risk to the Authority since the decision to call a LOBO is entirely at the lender's discretion. Any LOBOs called will be discussed with the treasury advisers prior to acceptance of any revised terms. The default position will be the repayment of the LOBO without penalty i.e. the revised terms will not be accepted.
33. Included within the PWLB portfolio is £35M of variable rate Loans, which are currently averaging 0.69% and are helping to keep the overall cost of borrowing down. Whilst in current climate of low interest rates this remains a sound strategy, these loans leave the authority exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators (paragraph 52), the Council review these regularly and if appropriate will switch into fixed rate loans.
34. In order to mitigate these risks further, the Council approved the creation of an Interest Equalisation Reserve in 2009 to help manage volatility in the future and ensure that there was minimal impact on annual budget decisions or council tax in any single year. At that point a major debt restructuring exercise had taken place in order to take advantage of market conditions and produce net revenue savings. As reported in the 2013/14 outturn report in preparation of the banking regulation reform, this reserve was renamed 'Treasury Risk Reserve' to recognise the wider risk. The level of this reserve was reviewed as part of the budget setting process and it is recommended that £925,000 is released for general purposes.

DEBT RESCHEDULING

35. The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Some bank lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk.
36. Borrowing and rescheduling activity will be reported to the Governance Committee in the Annual Treasury Management Report and the mid-year update. Regular treasury management reports will also be presented as part

of quarterly monitoring to Cabinet.

INVESTMENT POLICY AND STRATEGY

37. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has ranged between £66M and £125M, and are expected to be maintained between £70M and £100M in the forthcoming year, which is lower than previous years due to falling balances. The Council's current level of investments is presented at Appendix 1.
38. Both the CIPFA Code and the CLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk receiving unsuitably low investment income.
39. Given the increasing risk and continued low returns from short-term unsecured bank investments, the Authority aims to further diversify into more secure and/or higher yielding asset classes during 2015/16. This is especially the case for the estimated £35M that is available for longer-term investment. The majority of the Authorities surplus cash is currently invested in short-term unsecured bank deposits, and money market funds. This diversification will therefore represent a substantial change in strategy over the coming year.
40. The Authority may invest its surplus funds with any of the following counterparty types, subject to the cash limits (per counterparty) and time limits detailed in Appendix 3.

Credit Rating: Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

Banks Unsecured: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the Authority's current account bank

Banks Secured: Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

Government: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government

may be made in unlimited amounts for up to 50 years.

Corporates: Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

Registered Providers: Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain a high likelihood of receiving government support if needed.

Pooled Funds: Shares in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

41. The Chief Financial Officer (CFO), under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported quarterly to Cabinet.
42. Any institution will be suspended or removed should any of the factors identified in paragraph 43 below give rise to concern. Specifically credit ratings are monitored by the Authority on a daily basis. Arlingclose advises the Authority on ratings changes and appropriate action to be taken.

Risk Assessment and Credit Ratings

43. The Authority uses long-term credit ratings from the three main rating agencies Fitch Ratings, Moody's Investors Service and Standard & Poor's Financial Services to assess the risk of investment default. The lowest available counterparty credit rating will be used to determine credit quality, unless an investment-specific rating is available. Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:
 - no new investments will be made,
 - any existing investments that can be recalled or sold at no cost will be, and
 - full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other Information on the Security of Investments

44. The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.
45. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority’s cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office for example, or invested in government treasury bills for example or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

Specified Investments

46. The CLG Guidance defines specified investments as those:
- denominated in pound sterling,
 - due to be repaid within 12 months of arrangement,
 - not defined as capital expenditure by legislation, and
 - invested with one of:
 - the UK Government,
 - a UK local authority, parish council or community council, or
 - a body or investment scheme of “high credit quality”.

The Authority defines “high credit quality” organisations as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of A- or higher.

Non-Specified Investments

47. Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in table below.

	Cash Limit
Total long-term investments	£35M
Total investments without credit ratings or rated below A-	£10M
Total investments in foreign countries rated below AA+	£5M
Total non-specified investments	£50M

48. **Investment Limits:** The Authority's revenue reserves available to cover investment losses (excluding Schools, capital and HRA) are forecast to be £40M on 31st March 2015. In order that there is no immediate pressure on available reserves in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £10M. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below:

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

TREASURY MANAGEMENT INDICATORS

49. The Authority measures and manages its exposure to treasury management risks using the following indicators.

Adoption of the CIPFA Treasury Management Code

50. The Authority adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* in February 2012.

Liquidity Management

51. The Authority undertakes high level cash flow forecasting to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium term financial plan and cash flow forecast.

Upper Limits for Fixed and Variable Interest Rate Exposure

52. The following Prudential Indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises, which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short term rates on investments.

	Existing Level 31 December 2014	2014/15 Approved	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate
	%	%	%	%	%
Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100
Upper Limit for Variable Interest Rate Exposure	50	50	50	50	50

53. The Council will also limit and monitor large concentrations of fixed rate debt needing to be replaced. The limits provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Council's TM strategy.

Maturity Structure of Fixed Rate borrowing

54. This indicator is set to control the authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Lower Limit %	Upper Limit %
Under 12 Months	0	45
12 months and within 24 months	0	45
24 months and within 5 years	0	50
5 years and within 10 years	0	75
10 years and above	0	75

55. Time periods start on the first day of each financial year and the maturity date of borrowing is the earliest date on which the lender can demand repayment. As all LOBO are now in their call options they have been included as under 12 months within this indicator.
56. This table below details the level of our current fixed rate debt and shows that all debt is within existing limits.

	Lower Limit	Upper Limit	Actual Fixed Debt as at 31/12/2014	Average Fixed Rate as at 31/12/2014	% of Fixed Rate as at 31/12/2014	Compliance with set Limits?
	%	%	£M	%		
Under 12 months	0	45	9.4	2.44	4	Yes
12 months and within 24 months	0	45	0.0	0.00	0	Yes
24 months and within 5 years	0	50	0.0	0.00	0	Yes
5 years and within 10 years	0	75	72.5	3.23	33	Yes
10 years and within 15 years	0	75	0.0	0.00	0	Yes
15 years and within 20 years	0	75	0.0	0.00	0	Yes
20 years and within 25 years	0	75	10.0	4.68	5	Yes
25 years and within 30 years	0	75	5.0	4.60	2	Yes
30 years and within 35 years	0	75	0.0	0.00	0	Yes
35 years and within 40 years	0	75	42.0	3.99	19	Yes
40 years and within 45 years	0	75	50.6	3.62	23	Yes
45 years and within 50 years	0	75	31.2	3.56	14	Yes
50 years and above	0	100	0.0	0.00	0	Yes
			220.7	3.43	100	

Principal sums invested for periods longer than 364 days

57. The purpose of this limit is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end will be:

	2014/15 Approved	2014/15 Revised	2015/16 Limit	2016/17 Limit	2017/18 Limit
	£M	£M	£M	£M	£M
Upper Limit for total principal sums invested over 364 days	30	35	35	35	35

OTHER ITEMS

58. There are a number of additional items that the Authority is obliged by CIPFA or CLG to include in its Treasury Management Strategy.

Policy on Use of Financial Derivates

59. Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).
60. The Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.
61. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

Housing Revenue Account Self-Financing

62. On 1st April 2012, the Authority notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account.
63. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance. This balance will be measured and interest transferred between the General Fund and HRA at an agreed rate. Housing Legislation does not allow impairment losses to be charged to the HRA and consequently any credit related losses on the authority's investments will be borne by the General Fund alone. It is therefore appropriate that the General Fund is compensated for bearing this risk, and all interest transferred to the HRA should be adjusted downwards. The rate will be based on investments with the Debt Management Office. The rate of return on comparable investments with the government is lower and often referred to as the risk-free rate.

Training

64. CIPFA's Code of Practice requires the CFO to ensure that all Members tasked with TM responsibilities, including scrutiny of the TM function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Member training was undertaken on the 20 January 2015. The Council adopts a continuous performance and development programme to ensure staff are regularly appraised and any training needs addressed. Relevant staff also attend regular training sessions, seminars and workshops which ensure their knowledge is up to date. Details of training received are

maintained as part of the performance and development process.

Treasury Management Advisors

65. The CLG's Guidance on local government investments recommend that the Investment Strategy should state:

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

How the quality of any such service is controlled.

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

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

The Authority maintains the quality of the service with its advisors by holding quarterly meetings and tendering periodically. It should also be noted that decisions are taken independently by the CFO taking into account this advice and other internal and external factors.

Investment of Money Borrowed in Advance of Need

66. The Authority may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Authority is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Authority's overall management of its treasury risks.

The total amount borrowed will not exceed the authorised borrowing limit for the period. The maximum period between borrowing and expenditure is expected to be two years, although the Authority is not required to link particular loans with particular items of expenditure.

BALANCED BUDGET REQUIREMENT

67. The Council complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

2015/16 MINIMUM REVENUE PROVISION (MRP) STATEMENT

68. Where the Authority finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Authority to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the CLG Guidance) most recently issued in 2012.

69. The broad aim of the CLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.
70. The CLG Guidance requires the Authority to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP.
71. The four MRP options available are:
- Option 1: Regulatory Method
 - Option 2: CFR Method
 - Option 3: Asset Life Method
 - Option 4: Depreciation Method

***NB** This does not preclude other prudent methods to provide for the repayment of debt principal.*

MRP in 2015/16: Option 1 and 2 will be used for the majority of General Fund historic debt particularly that deemed to be supported through the Revenue Support Grant. For major projects where capital expenditure is funded from prudential borrowing Option 3 will be used to provide MRP over the life of the asset to which the borrowing was applied.

72. Following the HRA self-financing settlement, HRA debt increased from £100M to £174M with a borrowing cap of £200M. There is no requirement for the HRA to make debt repayments but it has opted to make voluntary repayments relating to debt inherited at the split and provision has been made within its business plan to show that it can pay down the remaining debt over the life of the 30 year business plan.
73. MRP in respect of leases and Private Finance Initiative schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.
74. Guidance relating to the regulatory method (option 1), which is used to calculate borrowing prior to the prudential regime, allows for debt transferred from Hampshire County Council (HCC) when we became a Unitary Authority in 1997 to be excluded from the MRP calculation as we are already repaying the principal element to HCC.
75. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement should be put forward for approval by the Authority at that time.
76. Capital expenditure incurred during 2015/16 and funded from borrowing will not be subject to a MRP charge until 2016/17.

77. Based on the Authority's estimate of its Capital Financing Requirement on 31st March 2015, the budget for MRP has been set as follows:

	31/03/2015 Estimated CFR £M	2015/16 Estimate MRP £M
Capital expenditure before 01.04.2008	95.6	2.95
Unsupported capital expenditure after 31.03.2008	87.8	3.36
Finance leases and Private Finance Initiative	66.8	2.05
Transferred debt	15.6	0.63
Total General Fund	265.8	8.99
Assets in the Housing Revenue Account	104.9	Nil
HRA subsidy reform payment	52.6	4.9
Total Housing Revenue Account	157.5	4.9
Total	423.3	13.89

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

78. The Chief Financial Officer will report to the Governance Committee on TM activity / performance as follows:

- (a) A mid-year review against the strategy approved for the year.
- (b) An outturn report on its treasury activity, no later than 30 September after the financial year end.

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

PRUDENTIAL INDICATORS

Background

80. The Local Government Act 2003 requires the Authority to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Authority has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

Gross Debt and the Capital Financing Requirement

81. This is a key indicator of prudence. In order to ensure that over the medium term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This view takes into account current commitments, existing plans and the proposals in the

approved budget.

82. There is a significant difference between the gross external borrowing requirement and the net external borrowing requirement represented by the Council's level of balances, reserves, provisions and working capital. The Council's current strategy is only to borrow to the level of its net borrowing requirement. The reasons for this are to reduce credit risk, take pressure off the Council's lending list and also to avoid the cost of carry existing in the current interest rate environment:

	31/03/2015 Revised £M	31/03/2016 Estimate £M	31/03/2017 Estimate £M	31/03/2018 Estimate £M
Borrowing	183.4	178.0	169.3	162.9
Finance leases and Private Finance Initiative	66.8	64.8	62.3	60.4
Transferred debt	15.6	15.0	14.4	13.8
Total General Fund Debt	265.8	257.8	246.0	237.1
HRA	157.5	186.8	195.8	193.1
Total	423.3	444.6	441.8	430.2

Estimates of Capital Expenditure

83. The Authority's planned capital expenditure and financing is summarised below, further detail is provided in the General Fund and HRA Capital programme report submitted elsewhere on the agenda.

Capital Expenditure and Financing	2014/15 Estimate £000	2014/15 Revised £000	2015/16 Estimate £000	2016/17 Estimate £000	2017/18 Estimate £000
General Fund	56,141	48,967	46,781	5,551	533
HRA	53,399	34,929	65,546	46,641	42,030
Total Expenditure	109,540	83,896	112,327	52,192	42,563
Capital receipts	12,277	11,774	14,042	6,152	3,183
Government Grants	33,388	32,269	28,024	4,288	0
Contributions	13,574	4,227	4,043	245	1,375
Major Repairs Allowance	17,931	17,939	18,970	19,364	19,721
Revenue	12,339	12,284	12,029	10,858	16,134
Total Financing	89,509	78,493	77,108	40,907	40,413
Temporary Financing	(3,400)	0	(1,000)	(2,650)	0
Unsupported borrowing	23,431	5,403	36,219	13,935	2,150
Total Funding	20,031	5,403	35,219	11,285	2,150
Total Financing & Funding	109,540	83,896	112,327	52,192	42,563

Ratio of Financing Costs to Net Revenue Stream

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

capital programme.

85. This indicator is not so relevant for the HRA, especially since the introduction of self-financing, as financing costs have been built into their 30 year business plan, including the voluntary payment of MRP. No problem is seen with the affordability but if problems were to arise then the HRA would have the option not to make principle repayments in the early years.

Ratio of Financing Costs to Net Revenue Stream	2013/14 Actual %	2014/15 Approved %	2014/15 Forecast %	2015/16 Forecast %	2016/17 Forecast %	2017/18 Forecast %
General Fund	6.95%	6.96%	5.83%	6.83%	7.57%	8.40%
HRA	16.24%	16.33%	14.87%	14.93%	15.55%	15.33%
Total	10.28%	10.39%	9.20%	10.17%	11.27%	11.62%

86. Please note that the incremental increase in this ratio for the General Fund is more to do with the reduced revenue stream which has reduced from £193.3M in 2013/14 to £145.9M in 2017/18 rather than an increased in debt charges.

Incremental Impact of Capital Investment Decisions

87. This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement (i.e. Interest and MRP) of the current approved capital programme with an equivalent calculation arising from the proposed programme. The incremental impact of capital investments decisions are estimated to be:

Incremental Impact of Capital Investment Decisions	2014/15 Approved £	2015/16 Estimate £	2016/17 Estimate £	2017/18 Estimate £
Increase / (Decrease) per average number of equivalent band D properties for Council Tax purposes	(1.27)	5.36	(0.59)	(2.82)
Increase in Average Weekly Housing	27.81	57.92	127.58	35.01

88. It should be noted that these indicators are for illustrative purposes only and show the amount per equivalent band D properties that this change would equate to. The decision to restrict the capital programme and to use capital receipts to repay temporary financing results in an incremental decrease in the band D Council Tax.

89. As per the General Fund these indicators are illustrative as HRA rent levels are currently set under the Government's rent restructuring formula, which is independent of the level of capital investment and borrowing. The calculation of the indicator ignores this factor.

Authorised Limit and Operational Boundary for External Debt

90. The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.

91. The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. excluding investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.

The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements, for example a complete debt restructure which requires monies to be borrowed in advance of repayment of existing debt. The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

Authorised Limit for External Debt	Existing Level 31 December 2014	2014/15 Approved	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate
	£M	£M	£M	£M	£M	£M
Borrowing	256	674	622	640	678	749
Other Long-term Liabilities	78	86	82	87	84	81
Total	334	760	704	727	762	830

92. The **Operational Boundary** is linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit

Operational Boundary for External Debt	Existing Level 31 December 2014	2014/15 Approved	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate
	£M	£M	£M	£M	£M	£M
Borrowing	256	672	441	466	476	548
Other Long-term Liabilities	78	78	82	87	84	81
Total	334	750	523	553	560	629

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

HRA Limit on Indebtedness

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

HRA Summary of Borrowing	2014/15 Approved £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M	2017/18 Estimate £M
Brought Forward	167.1	158.6	157.5	186.8	195.8
Maturing Debt	(5.1)	(5.1)	(5.1)	(5.1)	(5.1)
New borrowing	23.1	4.0	34.4	14.1	2.4
Carried forward	185.1	157.5	186.8	195.8	193.1

RESOURCE IMPLICATIONS

Capital

95. The Capital implications are considered as part of the General Fund Capital Programme report and HRA Capital Programme report elsewhere on the Council agenda.

Revenue

96. The General Fund budget for investment income in 2015/16 is £0.61M, based on committed deals to date plus investments on cash at an average balance of £25M and an average interest rate of 0.4%. The budget for debt interest paid in 2015/16 is £11M based on an average debt portfolio of £299.4M at an average interest rate of 3.37%. If actual levels of investments and borrowing and / or actual interest rates differ from those forecast, performance against budget will be correspondingly different
97. The CLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, having consulted the Cabinet Member for Resources, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness, the Revenue implications of which have been considered as part of the General Fund Revenue Budget report and HRA Revenue Budget report elsewhere on the Council agenda.

Property/Other

98. None

LEGAL IMPLICATIONS

Statutory power to undertake proposals in the report:

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

Other Legal Implications:

100. None

POLICY FRAMEWORK IMPLICATIONS

101. This report has been prepared in accordance with CIPFA's Code of Practice on TM.

KEY DECISION? Yes/No

WARDS/COMMUNITIES AFFECTED:	N/A
-----------------------------	-----

SUPPORTING DOCUMENTATION

Appendices

1.	Existing Investment & Debt Portfolio Position and Projections
2.	Economic and Interest Outlook
3.	Counterparty Cash and Time Limits
4.	Treasury Management Policy Statement
5.	Glossary of Treasury Terms

Documents In Members' Rooms

1.	None
----	------

Equality Impact Assessment

Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
--	----

Other Background Documents

Equality Impact Assessment and Other Background documents available for inspection at:

Title of Background Paper(s)

Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)

1.	TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS 2014/15 to 2016/17 – Council 12 February 2014 http://www.southampton.gov.uk/modernGov/ieListDocuments.aspx?CId=122&MIId=2469&Ver=4
----	--

Agenda Item 6

Appendix 1

EXISTING INVESTMENT & DEBT PORTFOLIO POSITION AND PROJECTIONS

	31-Mar-14 Actual £M	31-Mar-15 Approved £M	Current Portfolio £M	31-Mar-15 Current Estimate £M	31-Mar-16 Current Estimate £M	31-Mar-17 Current Estimate £M	31-Mar-18 Current Estimate £M
External Borrowing:							
Fixed Rate – PWLB Maturity	139	148	139	143	192	207	220
Fixed Rate – PWLB EIP	81	81	73	70	58	46	35
Variable Rate – PWLB	35	35	35	35	35	35	35
Variable Rate – Market	9	9	9	9	9	9	9
Long Term Borrowing	264	273	256	257	294	297	299
Short Term Borrowing							
Fixed Rate – Market	10	10	0	20	30	30	30
Other Long Term Liabilities							
PFI / Finance leases	62	61	62	67	65	62	60
Deferred Debt Charges	16	17	16	16	15	14	14
Total Gross External Debt	352	361	334	360	404	403	403
Investments:							
Managed In-House							
Deposits and monies on call and Money Market Funds	(66)	(40)	(53)	(35)	(25)	(25)	(25)
Financial Instruments	(3)	(3)	(18)	(30)	(30)	(30)	(30)
Managed Externally							
Pooled Funds			(5)	(5)	(5)	(5)	(5)
Total Investments	(69)	(43)	(76)	(70)	(60)	(60)	(60)
Net Borrowing Position	283	318	258	290	344	343	343

This page is intentionally left blank

ECONOMIC AND INTEREST OUTLOOK

The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, for December 2014 is detailed below. The Council will reappraise its strategy from time to time and, if needs be, realign it with evolving market conditions and expectations for future interest rates.

	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
Official Bank Rate													
Upside risk				0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Case	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75	1.75
Downside risk			0.25	0.25	0.50	0.50	0.75	0.75	1.00	1.00	1.00	1.00	1.00
3-month LIBID rate													
Upside risk	0.10	0.20	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30
Arlingclose Central Case	0.55	0.60	0.80	0.90	1.05	1.15	1.30	1.40	1.55	1.65	1.80	1.95	2.00
Downside risk	0.15	0.20	0.30	0.40	0.55	0.65	0.75	0.85	0.95	0.95	0.95	0.95	1.00
1-yr LIBID rate													
Upside risk	0.10	0.20	0.20	0.30	0.30	0.30	0.30	0.30	0.40	0.40	0.40	0.40	0.40
Arlingclose Central Case	0.95	1.00	1.20	1.30	1.45	1.55	1.70	1.80	1.95	2.05	2.20	2.35	2.40
Downside risk	0.15	0.20	0.30	0.50	0.55	0.60	0.65	0.70	0.75	0.80	0.80	0.80	0.80
5-yr gilt yield													
Upside risk	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.45	0.45	0.45	0.45	0.50	0.50
Arlingclose Central Case	1.10	1.20	1.30	1.40	1.50	1.65	1.80	1.95	2.10	2.20	2.35	2.40	2.50
Downside risk	0.35	0.35	0.40	0.45	0.50	0.50	0.55	0.60	0.65	0.70	0.70	0.70	0.75
10-yr gilt yield													
Upside risk	0.35	0.40	0.40	0.40	0.40	0.45	0.45	0.45	0.45	0.50	0.50	0.55	0.55
Arlingclose Central Case	1.60	1.70	1.80	1.90	2.00	2.15	2.30	2.45	2.60	2.70	2.85	2.90	3.00
Downside risk	0.35	0.35	0.40	0.45	0.50	0.50	0.55	0.60	0.65	0.70	0.70	0.75	0.80
20-yr gilt yield													
Upside risk	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55	0.55
Arlingclose Central Case	2.10	2.20	2.30	2.35	2.45	2.50	2.65	2.75	2.90	3.00	3.15	3.20	3.30
Downside risk	0.35	0.40	0.50	0.60	0.70	0.75	0.75	0.75	0.80	0.85	0.85	0.90	0.90
50-yr gilt yield													
Upside risk	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55	0.55
Arlingclose Central Case	2.15	2.25	2.35	2.40	2.50	2.55	2.70	2.80	2.95	3.05	3.20	3.25	3.35
Downside risk	0.35	0.40	0.50	0.60	0.70	0.75	0.75	0.75	0.80	0.85	0.85	0.90	0.90

Underlying Assumptions:

- The UK economic recovery slowed towards the end of 2014, with economic and political uncertainty weighing on business investment. However, the Q3 growth rate of 0.7% remains slightly above the long run average, suggesting the recovery remains robust.
- Household consumption is key to the recovery in 2015. While we expect consumption growth to slow, given softening housing market activity and slower employment growth, the fall in inflation and resulting rise in both real (and nominal) wage growth and disposable income should support spending.
- Inflationary pressure is currently low (annual CPI is currently 0.5%) and is likely to remain so in the short-term. The fall in oil prices has yet to feed fully into the prices of motor fuel and retail energy and CPI is expected to fall further. Supermarket price wars are also expected to bear down on food price inflation.
- The MPC's focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee.

- Nominal earnings growth is strengthening, but remains relatively weak in historical terms, despite large falls in unemployment. Our view is that spare capacity remains extensive. The levels of part-time, self-employment and underemployment are significant and indicate capacity within the employed workforce, in addition to the still large unemployed pool. Productivity growth can therefore remain weak in the short term without creating undue inflationary pressure.
- However, we also expect employment growth to slow as economic growth decelerates. This is likely to boost productivity, which will bear down on unit labour costs and inflationary pressure.
- In addition to the lack of wage and inflationary pressures, policymakers are evidently concerned about the bleak prospects for the Eurozone. These factors will maintain the dovish stance of the MPC in the medium term. The MPC clearly believes the appropriate level for Bank Rate for the post-crisis UK economy is significantly lower than the previous norm. We would suggest this is between 2.5 and 3.5%.
- The ECB has introduced outright QE as expected. While this may alleviate some of the anxiety about the economic potential of the Eurozone, political risk remains significant (e.g. Greek election). Therefore fears for the Eurozone are likely to maintain a safe haven bid for UK government debt.

Forecast:

- Our Advisors forecast the first rise in official interest rates in Q3 2015, but the risks to this forecast are very much weighted to the downside. The February Inflation Report will be key to our review of the possible path for Bank Rate.
- We project a slow rise in Bank Rate. The pace of interest rate rises will be gradual and the extent of rises limited; we believe the normalised level of Bank Rate post-crisis to range between 2.5% and 3.5%.
- Market sentiment (derived from forward curves) has shifted significantly lower in the past three months; market expectations are now for a later increase in interest rates and a more muted increase in gilt yields.

COUNTERPARTY CASH AND TIME LIMITS

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

Please read notes in paragraph 40 of main report in conjunction with this table.

This page is intentionally left blank

TREASURY MANAGEMENT POLICY STATEMENT

1. INTRODUCTION AND BACKGROUND

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

2. POLICIES AND OBJECTIVES OF TREASURY MANAGEMENT ACTIVITIES

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

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

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

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

GLOSSARY OF TREASURY TERMS

<p>Amortised Cost Accounting:</p> <p>Values the asset at its purchase price, and then subtracts the premium/adds back the discount linearly over the life of the asset. The asset will be valued at par at its maturity.</p>
<p>Authorised Limit (Also known as the Affordable Limit):</p> <p>A statutory limit that sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities).</p>
<p>Balances and Reserves:</p> <p>Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.</p>
<p>Bail - in Risk:</p> <p>The Following the financial crisis of 2008 when governments in various jurisdictions injected billions of dollars into banks as part of bail-out packages, it was recognised that bondholders, who largely remained untouched through this period, should share the burden in future by making them forfeit part of their investment to "bail in" a bank before taxpayers are called upon.</p> <p>A bail-in takes place before a bankruptcy and under current proposals, regulators would have the power to impose losses on bondholders while leaving untouched other creditors of similar stature, such as derivatives counterparties. A corollary to this is that bondholders will require more interest if they are to risk losing money to a bail-in.</p>
<p>Bank Rate:</p> <p>The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.</p>
<p>Basis Point:</p> <p>A unit of measure used in finance to describe the percentage change in the value or rate of a financial instrument. One basis point is equivalent to 0.01% (1/100th of a percent). In most cases, it refers to changes in interest rates and bond yields. For example, if interest rates rise by 25 basis points, it means that rates have risen by 0.25% percentage points. If rates were at 2.50%, and rose by 0.25%, or 25 basis points, the new interest rate would be 2.75%. In the bond market, a basis point is used to refer to the yield that a bond pays to the investor. For example, if a bond yield moves from 5.45% to 5.65%, it is said to have risen by 20 basis points. The usage of the basis point measure is primarily used in respect to yields and interest rates, but it may also be used to refer to the percentage change in the value of an asset such as a stock.</p>
<p>Bond:</p> <p>A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The repayment date is also set at the onset but can be traded during its life, but this will affect the price of a bond which may vary during its life.</p>

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

bank); in essence, the investor has recourse against the issuer and the collateral, sometimes known as "dual recourse."
<p>CPI : Consumer Price Index – the UK’s main measure of inflation.</p>
<p>Credit Rating: Formal opinion by a registered rating agency of a counterparty’s future ability to meet its financial liabilities; these are opinions only and not guarantees.</p>
<p>Department for Communities and Local Government (DCLG) : The DCLG is the UK Government department for Communities and Local Government in England. It was established in May 2006 and is the successor to the Office of the Deputy Prime Minister, established in 2001.</p>
<p>Debt Management Office (DMO): The DMO is an Executive Agency of Her Majesty's Treasury and provides direct access for local authorities into a government deposit facility known as the DMADF. All deposits are guaranteed by HM Government and therefore have the equivalent of a sovereign triple-A credit rating.</p>
<p>Diversification /diversified exposure: The spreading of investments among different types of assets or between markets in order to reduce risk.</p>
<p>European Investment Bank (EIB): The European Investment Bank is the European Union's non-profit long-term lending institution established in 1958 under the Treaty of Rome. It is a "policy driven bank" whose shareholders are the member states of the EU. The EIB uses its financing operations to support projects that bring about European integration and social cohesion.</p>
<p>Federal Reserve: The US central bank. (Often referred to as “the Fed”).</p>
<p>Floating rate notes (FRNs) : Floating rate notes (FRNs) are debt securities with payments that are reset periodically against a benchmark rate, such as the three-month Treasury bill or the three-month London inter-bank offer rate (LIBOR). FRNs can be used to balance risks incurred through other interest rate instruments in an investment portfolio.</p>
<p>FTSE 100 Index: The FTSE 100 Index is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalisation. It is one of the most widely used stock indices and is seen as a gauge of business prosperity for business regulated by UK company law. The index is maintained by the FTSE Group, a subsidiary of the London Stock Exchange Group.</p>
<p>General Fund: This includes most of the day-to-day spending and income.</p>
<p>Gilts:</p>

<p>Gilts are bonds issued by the UK Government. They take their name from 'gilt-edged': being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.</p>
<p>Gross Domestic Product (GDP):</p> <p>Gross Domestic Product measures the value of goods and services produced with in a country. GDP is the most comprehensive overall measure of economic output and provides key insight as to the driving forces of the economy.</p>
<p>The G7:</p> <p>The G7, is a group consisting of the finance ministers of seven industrialised nations: namely the US, UK, France, Germany, Italy, Canada and Japan. They are seven of the eight (China excluded) wealthiest nations on Earth, not by GDP but by global net wealth. The G7 represents more than the 66% of net global wealth (\$223 trillion), according to Credit Suisse Global Wealth Report September 2012.</p>
<p>IFRS:</p> <p>International Financial Reporting Standards.</p>
<p>International Labour Organisation (ILO):</p> <p>The ILO Unemployment Rate refers to the percentage of economically active people who are unemployed by ILO standard and replaced the Claimant Unemployment Rate as the international standard for unemployment measurement in the UK.. Under the ILO approach, those who are considered as unemployed are either out of work but are actively looking for a job or out of work and are waiting to start a new job in the next two weeks. ILO Unemployment Rate is measured by a monthly survey, which is called the Labour Force Survey in United Kingdom. Approximately 40,000 individuals are interviewed each month, and the unemployment figure reported is the average data for the previous three months.</p>
<p>LIBID:</p> <p>The London Interbank Bid Rate (LIBID) is the rate bid by banks on Eurocurrency deposits (i.e. the rate at which a bank is willing to borrow from other banks). It is "the opposite" of the LIBOR (an offered, hence "ask" rate, the rate at which a bank will lend). Whilst the British Bankers' Association set LIBOR rates, there is no correspondent official LIBID fixing.</p>
<p>LIBOR:</p> <p>The London Interbank Offered Rate (LIBOR) is the rate of interest that banks charge to lend money to each other. The British Bankers' Association (BBA) work with a small group of large banks to set the LIBOR rate each day. The wholesale markets allow banks who need money to be more fluid in the marketplace to borrow from those with surplus amounts. The banks with surplus amounts of money are keen to lend so that they can generate interest which it would not otherwise receive.</p>
<p>LOBO:</p> <p>Stands for Lender Option Borrower Option. The underlying loan facility is typically very long-term - for example 40 to 60 years - and the interest rate is fixed. However, in the LOBO facility the lender has the option to call on the facilities at pre-determined future dates. On these call dates, the lender can propose or impose a new fixed rate for the remaining term of the facility and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan facility. The upshot of this is that on the option exercise date, the lender could propose an extreme fixed rate, say 20 per cent, which would effectively force the repayment of the underlying facility. The borrower's so called 'option' is only the inalienable right to</p>

accept or refuse a new deal such as a fixed rate of 20 per cent.
<p>Maturity:</p> <p>The date when an investment or borrowing is repaid.</p>
<p>Maturity Structure / Profile:</p> <p>A table or graph showing the amount (or percentage) of debt or investments maturing over a time period. The amount or percent maturing could be shown on a year-by-year or quarter-by quarter or month-by-month basis.</p>
<p>Minimum Revenue Provision (MRP):</p> <p>An annual provision that the Council is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets.</p>
<p>Money Market Funds (MMF):</p> <p>An open-end mutual fund which invests only in money markets. These funds invest in short term debt obligations such as short-dated government debt, certificates of deposit and commercial paper. The main goal is the preservation of principal, accompanied by modest dividends. The fund's net asset value remains constant (eg £1 per unit) but the interest rate does fluctuate. These are liquid investments, and therefore, are often used by financial institutions to store money that is not currently invested. Risk is extremely low due to the high rating of the MMFs; many have achieved AAA credit status from the rating agencies:</p> <ul style="list-style-type: none"> • Constant net asset value (CNAV) refers to funds which use amortised cost accounting to value all of their assets. They aim to maintain a net asset value (NAV), or value of a share of the fund, at €1/£1/\$1 and calculate their price to two decimal places known as "penny rounding". Most CNAV funds distribute income to investors on a regular basis (distributing share classes), though some may choose to accumulate the income, or add it on to the NAV (accumulating share classes). The NAV of accumulating CNAV funds will vary by the income received. • Variable net asset value (VNAV) refers to funds which use mark-to-market accounting to value some of their assets. The NAV of these funds will vary by a slight amount, due to the changing value of the assets and, in the case of an accumulating fund, by the amount of income received. <p>This means that a fund with an unchanging NAV is, by definition, CNAV, but a fund with a NAV that varies may be accumulating CNAV or distributing or accumulating VNAV.</p>
<p>Multilateral Development Banks:</p> <p>See Supranational Bonds below.</p>
<p>Municipal Bonds Agency</p> <p>An independent body owned by the local government sector that seeks to raise money on the capital markets at regular intervals to on-lend to participating local authorities.</p>
<p>Non Specified Investment:</p> <p>Investments which fall outside the CLG Guidance for Specified investments (below).</p>
<p>Operational Boundary:</p> <p>This linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely prudent but not worst case scenario but without the additional</p>

headroom included within the Authorised Limit.
<p>Premiums and Discounts:</p> <p>In the context of local authority borrowing,</p> <ul style="list-style-type: none"> (a) the premium is the penalty arising when a loan is redeemed prior to its maturity date and (b) the discount is the gain arising when a loan is redeemed prior to its maturity date. <p>If on a £1 million loan, it is calculated that a £150,000 premium is payable on premature redemption, then the amount paid by the borrower to redeem the loan is £1,150,000 plus accrued interest. If on a £1 million loan, it is calculated* that a £50,000 discount receivable on premature redemption, then the amount paid by the borrower to redeem the loan is £950,000 plus accrued interest. PWLB premium/discount rates are calculated according to the length of time to maturity, current market rates (plus a margin), and the existing loan rate which then produces a premium/discount dependent on whether the discount rate is lower/higher than the coupon rate.</p> <p><i>*The calculation of the total amount payable to redeem a loan borrowed from the Public Works Loans Board (PWLB) is the present value of the remaining payments of principal and interest due in respect of the loan being repaid prematurely, calculated on normal actuarial principles. More details are contained in the PWLB's lending arrangements circular.</i></p>
<p>Property:</p> <p>Investment property is property (land or a building or part of a building or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both.</p>
<p>Prudential Code:</p> <p>Developed by CIPFA and introduced on 01/4/2004 as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.</p>
<p>Prudential Indicators:</p> <p>Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators</p>
<p>Public Works Loans Board (PWLB):</p> <p>This is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.</p>
<p>Quantitative Easing (QE):</p> <p>In relation to the UK, it is the process used by the Bank of England to directly increase the quantity of money in the economy. It <i>“does not involve printing more banknotes. Instead, the Bank buys assets from private sector institutions – that could be insurance companies, pension funds, banks or non-financial firms – and credits the seller’s bank account. So the seller has more money in their bank account, while their bank holds a corresponding claim against the Bank of England (known as reserves). The end result is more money out in the wider economy”</i>. Source: Bank of England.</p>
<p>Repo Rate:</p>

<p>The interest rate at which the central bank in a country repurchases government securities (such as Treasury securities) from commercial banks. The central bank raises the repo rate when it wishes to reduce the money supply in the short term, while it lowers the rate when it wishes to increase the money supply and stimulate growth.</p>
<p>Revenue Expenditure:</p> <p>Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.</p>
<p>RPI:</p> <p>Retail Prices Index is a monthly index demonstrating the movement in the cost of living as it tracks the prices of goods and services including mortgage interest and rent. Pensions and index-linked gilts are uprated using the RPI index.</p>
<p>(Short) Term Deposits:</p> <p>Deposits of cash with terms attached relating to maturity and rate of return (Interest).</p>
<p>Specified Investments:</p> <p>Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than one year. UK government, local authorities and bodies that have a high credit rating.</p>
<p>Supported Borrowing:</p> <p>Borrowing for which the costs are supported by the government or third party.</p>
<p>Supranational Bonds:</p> <p>Instruments issued by supranational organisations created by governments through international treaties (often called multilateral development banks). The bonds carry a AAA rating in their own right. Examples of supranational organisations are the European Investment Bank, the International Bank for Reconstruction and Development.</p>
<p>Treasury (T) -Bills:</p> <p>Treasury Bills are short term Government debt instruments and, just like temporary loans used by local authorities, are a means to manage cash flow. Treasury Bills (T-Bills) are issued by the Debt Management Office and are an eligible sovereign instrument, meaning that they have a AAA-rating.</p>
<p>Temporary Borrowing:</p> <p>Borrowing to cover peaks and troughs of cash flow, not to fund capital spending.</p>
<p>Treasury Management Code:</p> <p>CIPFA's Code of Practice for Treasury Management in the Public Services, initially brought in 2003, subsequently updated in 2009 and 2011.</p>
<p>Treasury Management Practices (TMP):</p> <p>Treasury Management Practices set out the manner in which the Council will seek to achieve its policies and objectives and prescribe how it will manage and control these activities.</p>

Unsupported Borrowing:

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

Variable Net Asset Value (VNAV):

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

Yield:

The measure of the return on an investment instrument.

Agenda Item 7

DECISION-MAKER:	GOVERNANCE COMMITTEE		
SUBJECT:	INTERNAL AUDIT PROGRESS REPORT – DECEMBER 2014		
DATE OF DECISION:	9 FEBRUARY 2015		
REPORT OF:	CHIEF INTERNAL AUDITOR		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Neil Pitman	Tel: 023 8083 4616
	E-mail:	Neil.pitman@southampton.gov.uk	
Director	Name:	Mark Heath	Tel: 023 8083 2371
	E-mail:	Mark.heath@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY

N/A

BRIEF SUMMARY

Under the Accounts & Audit (England) Regulations 2011, the Council is responsible for:

- Ensuring that its financial management is adequate and effective and that it has a sound system of internal control which facilitates the effective exercise of functions and includes arrangements for the management of risk; and
- Undertaking an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with proper practices in relation to internal control.

In accordance with proper internal audit practices (Public Sector Internal Audit Standards), the Chief Internal Auditor is required to provide a written status report to the Governance Committee, summarising:

- Progress in implementing the audit plan;
- Internal audit reviews in progress
- Audit opinion on all internal audit reviews completed since the last report and executive summaries of published reports where critical weaknesses or unacceptable levels of risk were identified; and
- The status of 'live' reports, i.e. those where internal audit work is complete and actions are planned to improve the framework of governance, risk management and management control.

Appendix 1 summarises the activities of internal audit for the period to December 2014.

RECOMMENDATIONS:	
	(i) to note the Internal Audit Progress report for the period to December 2014.
REASONS FOR REPORT RECOMMENDATIONS	
1.	In accordance with proper internal audit practices (Public Sector Internal Audit Standards), the Governance Committee is required to receive the Chief Internal Auditor's progress report.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	None
DETAIL (Including consultation carried out)	
3.	The progress report to the period December 2014 is attached for consideration in Appendix 1.
RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
4.	None
<u>Property/Other</u>	
5.	None
LEGAL IMPLICATIONS	
<u>Statutory power to undertake proposals in the report:</u>	
6.	The Accounts & Audit (England) Regulations 2011 state 'a relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control'.
<u>Other Legal Implications:</u>	
7.	None
POLICY FRAMEWORK IMPLICATIONS	
8.	None

KEY DECISION?	No
WARDS/COMMUNITIES AFFECTED:	N/A

<u>SUPPORTING DOCUMENTATION</u>	
Appendices	
1.	Internal Audit Progress Report – December 2014
Documents In Members’ Rooms	
1.	None
Equality Impact Assessment	
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
Other Background Documents	
Equality Impact Assessment and Other Background documents available for inspection at:	
Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	None

This page is intentionally left blank

Internal Audit Progress Report

December 2014

Southampton City Council



Page 55

**Southern Internal
Audit Partnership**

Assurance through excellence
and innovation

Contents:

1.	Role of Internal Audit	3
2.	Purpose of report	4
3.	Performance dashboard	5
4.	Status of 'live' reports	6 – 7
5.	Executive summaries 'Limited' and 'No' assurance opinions	8 – 11
6.	Fraud and Irregularities	12 - 13
7.	Planning and resourcing	13
8.	Rolling work programme	14 - 19

1. Role of Internal Audit

The requirement for an internal audit function in local government is detailed within the Accounts and Audit (England) Regulations 2011, which states that a relevant body must:

‘Undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control’.

The standards for ‘proper practices’ in relation to internal audit are laid down in the Public Sector Internal Audit Standards 2013 [the Standards].

The role of internal audit is best summarised through its definition within the Standards, as an:

‘Independent, objective assurance and consulting activity designed to add value and improve an organisations operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes’.

The Council is responsible for establishing and maintaining appropriate risk management processes, control systems, accounting records and governance arrangements. Internal audit plays a vital role in advising the Council that these arrangements are in place and operating effectively.

The Council’s response to internal audit activity should lead to the strengthening of the control environment and, therefore, contribute to the achievement of the organisations objectives.

2. Purpose of report

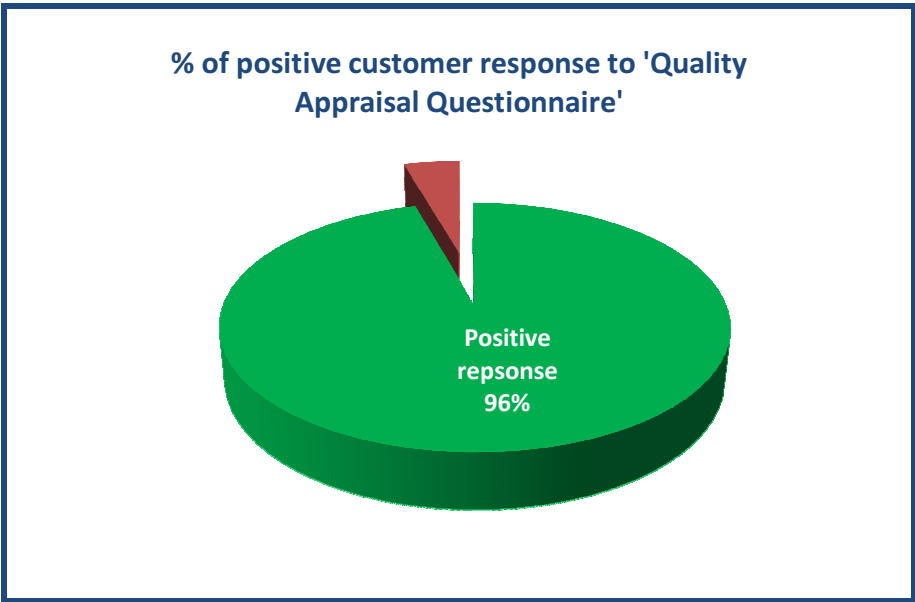
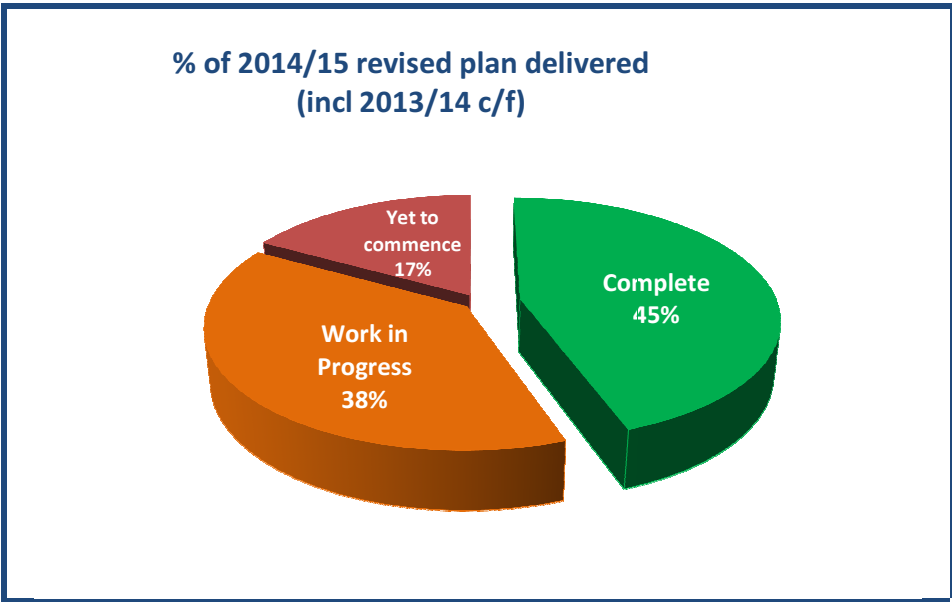
In accordance with proper internal audit practices (Public Sector Internal Audit Standards), and the Internal Audit Charter the Chief Internal Auditor is required to provide a written status report to ‘Senior Management’ and ‘the Board’, summarising:

- The status of ‘live’ internal audit reports;
- an update on progress against the annual audit plan;
- a summary of internal audit performance, planning and resourcing issues; and
- a summary a significant issues that impact on the Chief Internal Auditor’s annual opinion


Internal audit reviews culminate in an opinion on the assurance that can be placed on the effectiveness of the framework of risk management, control and governance designed to support the achievement of management objectives of the service area under review. Assurance opinions are categorised as follows:

Substantial	A sound framework of internal control is in place and operating effectively. No risks to the achievement of system objectives have been identified
Adequate	Basically a sound framework of internal control with opportunities to improve controls and / or compliance with the control framework. No significant risks to the achievement of system objectives have been identified
Limited	Significant weakness identified in the framework of internal control and / or compliance with the control framework which could place the achievement of system objectives at risk
No	Fundamental weaknesses identified in the framework of internal control or the framework is ineffective or absent with significant risk to the achievement of system objectives

3. Performance dashboard



Page 59


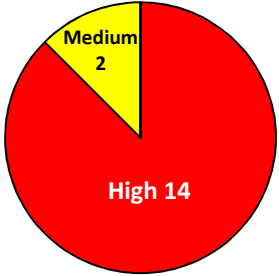
Compliance with Public Sector Internal Audit Standards / Local Government Application Note	
	<p>During 2013 – 14 The Head of the Southern Internal Audit Partnership undertook a self-assessment concluding overall compliance against the Standards and the LGAN. To provide independence to the process the self –assessment was reviewed by Hampshire County Council’s Monitoring Officer to ensure it presented a true and fair view.</p> <p>Independent analysis confirmed that the self-assessment provided <i>‘a fair assessment of the internal audit activity’</i></p>

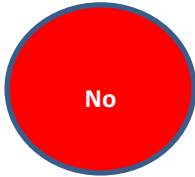
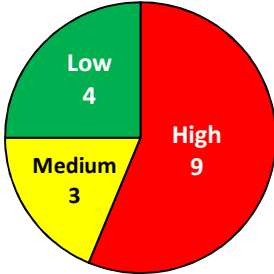
4. Status of 'Live' Reports

Audit title	Report date	Directorate Sponsor	Audit Assurance		Management Actions (of which are 'high' priority)			
			Original	Current	Reported	Pending	Cleared	Overdue
Cash Collection & Banking	21/01/13	Corporate Services	Limited	Adequate	12 (5)	0 (0)	9 (5)	3 (0)
Development Management	26/04/13	Place	Limited	Adequate	7 (4)	0 (0)	5 (4)	2 (0)
Quality Assurance	18/07/13	People	Adequate	Adequate	15 (9)	0 (0)	12 (6)	3 (3)
Neighbourhood wardens	22/10/13	People	Adequate	Adequate	7 (2)	0 (0)	6 (2)	1 (0)
Sholing Technology College	13/03/14	People	Adequate	Adequate	17 (4)	0 (0)	3 (1)	14 (3)
Highways	04/03/14	Place	Adequate	Adequate	4 (0)	0 (0)	1 (0)	3 (0)
Payroll	04/04/14	Corporate Services	Adequate	Adequate	11 (4)	0 (0)	5 (2)	6 (2)
Bevois Town Primary School	02/05/14	People	Limited	Adequate	20 (17)	0 (0)	18 (17)	2 (0)
St Monica Junior School	08/05/14	People	Limited	Adequate	28 (23)	0 (0)	20 (15)	8 (8)
Income Collection and Transactions	09/05/14	Corporate Services	Adequate	Adequate	6 (0)	0 (0)	4 (0)	2 (0)
Business Continuity & Emergency Planning	09/07/14	Place	Limited	Limited	11 (5)	3 (0)	3 (3)	5 (2)
Data Centre Security	16/07/14	Corporate Services	Limited	Limited	2 (0)	0 (0)	0 (0)	2 (0)
Information Governance	17/07/14	Corporate Services	Limited	Limited	21 (15)	6 (4)	13 (10)	2 (1)
Integrated Assessment–Data Performance	30/07/14	People	Adequate	Adequate	3 (3)	1 (1)	2 (2)	0 (0)
Itchen Bridge	31/07/14	Place	Adequate	Adequate	10 (5)	0 (0)	4 (3)	6 (2)

Audit title	Report date	Directorate Sponsor	Audit Assurance		Management Actions (of which are 'high' priority)			
			Original	Current	Reported	Pending	Cleared	Overdue
Partnership arrangements	01/08/14	Corporate Services	Adequate	Adequate	6 (0)	1 (0)	1 (0)	4 (0)
Learning and Development	05/09/14	People	Adequate	Adequate	5 (0)	0 (0)	3 (0)	2 (0)
Health and Safety	22/09/14	Corporate Services	Limited	Limited	16 (14)	4 (3)	2 (2)	10 (9)
Building Control	07/10/14	Place	Adequate	Adequate	3 (1)	0 (0)	1 (0)	2 (1)
Housing Office Security/Cash Handling	23/10/14	People	No	No	16 (9)	1 (0)	13 (8)	2 (1)
Across Schools Thematic Review (Payroll)	12/11/14	People	Limited	Limited	9 (0)	0 (0)	8 (0)	1 (0)
Maytree Infant and Nursery School	12/11/14	People	Limited	Adequate	23 (23)	1 (1)	18 (18)	4 (4)
Schools Thematic - Procurement Cards	12/11/14	People	Adequate	Adequate	6 (0)	1 (0)	0 (0)	5 (0)
Local Safeguarding Children's Board	13/11/14	People	Adequate	Adequate	2 (0)	0 (0)	0 (0)	2 (0)
Public Health Contracts	20/11/14	People	Adequate	Adequate	2 (0)	0 (0)	0 (0)	2 (0)
Fostering	09/01/15	People	Adequate	Adequate	10 (0)	3 (0)	7 (0)	0 (0)

5. Executive Summaries of new reports published concluding a ‘Limited’ or ‘No’ assurance opinion

Health and Safety 2014/15		
<p>Directorate Sponsor: Corporate Services</p> <p>Key Contacts: Mark Heath, Director of Corporate Services; John Spiers, Head of Property, Procurement and Health & Safety; Graham Armstrong, Health & Safety Manager</p> <p>Final Report Issued: 18 September 14</p>	<p>Assurance opinion:</p> <div style="text-align: center;">  <p>Limited</p> </div>	<p>Management Actions:</p> <div style="text-align: center;">  <p>High 14 Medium 2</p> </div>
<p>Summary of key observations:</p> <p>Health and safety guidance, procedures, reporting and self assessment tools are all available on the intranet. The majority of staff contacted (98.6%) were aware of where information could be found, however, testing identified navigation of the intranet and links embedded within documentation / guidance relating to health and safety require review and update to ensure a clear pathway to required information</p> <p>There are elements of health and safety training that are required to be carried out on a cyclical basis, however testing highlighted that this was not always achieved. Whilst reports on attendance are produced, no work is undertaken to identify and challenge staff that have not completed courses in the required timeframe. Further, concerns were raised by staff interviewed that training did not accommodate key aspects of their work (manual handling was raised on more than on occasion). It should be noted that there remains an onus on the employee to raise concerns with their manager should they feel there is an absence of health and safety training.</p> <p>Health & safety risk assessments were found to be inconsistent in their format and regularity of review. Sample testing also highlighted instances in which assessments were incomplete. There are further requirements for all sections of the Council to undertake an annual, management-led self-audit of health and safety. There was found to be no consistent approach to the completion of self audits and subsequently action plans to correct any omissions across the council.</p> <p>The Council maintain a database of asbestos conditions surveys & staff appeared to be aware of the requirements for the management of asbestos however, despite this awareness, an investigation is on-going into the remodelling of Council premises that includes non-compliance with HSE regulations.</p>		

<p>Fraud Thematic Review - Housing office security and cash handling 2014/15</p>		
<p>Directorate Sponsor: People</p> <p>Key Contacts: Nick Cross, Head of Housing Services; Mike Carey, Income Services Manager; David Little, Income manager</p> <p>Final Report Issued: 23 October 14</p>	<p>Assurance opinion:</p> <div style="text-align: center;">  </div>	<p>Management Actions:</p> <div style="text-align: center;">  </div>
<p>Summary of key observations:</p> <p>There were a number of weaknesses observed in respect of buildings security within the housing offices visited. Additionally incomplete inventories of keys holders increased the risk of loss and reduced accountability as a result of ineffective record keeping.</p> <p>Insurance limits for the cash held in safes were regularly exceeded and half of the offices kept safe keys on site overnight which could invalidate any insurance claim in the event of loss.</p> <p>The four offices which do not undertake their banking directly take income to the remaining two housing offices for banking however the amounts transferred are not signed over as agreed or kept in tamper proof bags, weakening the management trail and increasing the vulnerability of those staff involved in cash transfers .</p>		

School Thematic Review – Payroll 2013/14

Directorate Sponsor: People

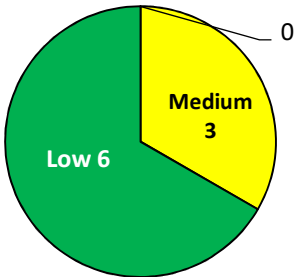
Key Contacts: Edward Harris, Principal Officer – Education and Early Years; Dave Cuerden, Finance Manager; Gary Wooldridge, Senior Accounting Technician

Final Report Issued: 12 November 2014

Assurance opinion:



Management Actions:



Summary of key observations:

Financial guidance is available to schools, however, review of central policies and procedures on the Council’s intranet site identified that some of the information requires review and update to ensure current practices and requirements are appropriately communicated (financial guidance, governors induction etc.).

Testing of payroll amendments concentrated on overtime payments and found issues at half of the school visited including incomplete / unauthorised claim forms and anomalies in overtime rates being claimed.

In the absence of relevant documentation we were unable to confirm the review of monthly payroll reports and in a majority of the schools visited there was no evidence of independent review by the Headteacher.

Maytree Infant and Nursery School 2014/15

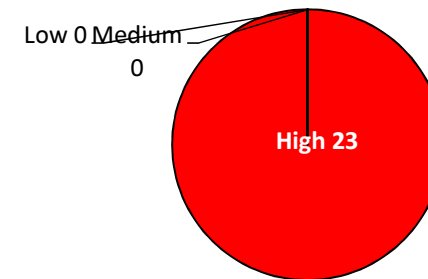
Directorate Sponsor: People

Key Contacts: Jan Goatley, Head teacher; Meenu Grewal, School Business Manager, Edward Harris, Principal Officer – Education and Early Years; Dave Cuerden, Finance Manager;
Final Report Issued: 12 November 14

Assurance opinion:



Management Actions:



Summary of key observations:

Imprest purchases were not routinely authorised or supported by receipts placing the finance officer in a vulnerable position as it is they that administer the account and are often the recipient of reimbursement. One transaction sampled (£150) was in relation to an advance / loan to a member of staff.

The school retains two purchasing cards, from sample testing there were occasions where VAT had not been accounted for correctly, receipts were not provided and expenditure had not been correctly coded.

Whilst the school maintains a contract register (albeit at the time of the audit visit was not up to date), review of a sample of purchases exceeding £10,000 found that Contract Procedure Rules were not routinely complied with.

The breakfast club budget was not being monitored, expenditure was not being authorised and receipts were not retained. The club receives grant funding, however, the grant conditions were not being met.

6. Fraud and Irregularities

In accordance with the Local Government Transparency Code 2014 there is a requirement on local authorities to publish the following information with regard counter fraud work:

Local Government Transparency Code 2014	01.04.14 – 31.12.14
Part 2 Requirements - Fraud	
Number of occasions powers under the Prevention of Social Housing Fraud (Power to Require Information) (England) Regulations 2014, or similar powers have been used	Nil
Total number (absolute and full time equivalent) of employees undertaking investigations and prosecutions of fraud	2 fte*
Total number (absolute and full time equivalent) of professionally accredited counter fraud specialists	3 fte*
Total amount of time spent by the authority on the investigation and prosecution of fraud	112 days*
Total number of fraud cases investigated	5**

*relates to internal audit staff across the wider SIAP only (does not include other areas of the Council that may affect reported figures i.e. legal, HR, Trading Standards, departmental investigating officers, housing benefits etc.)

**the definition of fraud is as set out by the Audit Commission in *Protecting the Public Purse - 'the intentional false representation, including failure to declare information or abuse of position that is carried out to make gain, cause loss or expose another to the risk of loss.'*

Fraud Grant Funding

The DCLG have made available £16m to assist Councils in developing innovative and holistic initiatives to tackle the fight against fraud.

During the summer local authorities were invited to submit proposals for funding that would result in real financial savings through effective counter fraud activities. A successful bid from the Southern Internal Audit Partnership (one of only 59 approved from 164 applications) has resulted in funding of £72,000 being awarded to support initiatives in respect of fraud detection and prevention.

Funding acquired will contribute to the development of a generic fraud risk assessment framework to inform and educate of key fraud risks. This assessment will inform a programme of proactive fraud initiatives moving forward, targeting demonstrably high risk areas.

This will be supported by the use of data analytics to more strategically analyse higher risk areas in the identification and investigation of data giving rise to irregular activity or conflicts with other sources of information.

The legacy from funding will strengthen measures for both fraud detection and prevention through provision of a clear understanding and assessment of fraud threats and the establishment of data analytics as preventative measures to combat fraud through the real time sharing and matching of data and fraud intelligence.

7. Planning & Resourcing

The internal audit plan for 2014/15 was approved by the Council's Management Team and the Governance Committee in April 2014.

The audit plan remains fluid to provide a responsive service that reacts to the changing needs of the Council. Progress against the plan is detailed within section 8

8. Rolling Work Programme

Audit title	Audit Progress					Final report issued
	TOR issued	Fieldwork commenced	Fieldwork complete	Draft report issued		
2013-14 Carry Forward Reviews						
Partnership arrangements	✓	✓	✓	✓		01/08/14
Information Governance	✓	✓	✓	✓		17/07/14
Business Continuity & Emergency Planning	✓	✓	✓	✓		09/07/14
Change control	✓	✓	✓	✓		27/05/14
Across Schools Thematic Review 1 (payroll)	✓	✓	✓	✓		12/11/14
Data and performance management – Support Services	✓	✓	✓	✓		30/07/14
Itchen Bridge	✓	✓	✓	✓		31/07/14
Delivery of statutory functions - Family Centres and children centres	✓	✓	✓	✓		27/06/14
Client Monies Services	✓	✓	✓	✓		
Reablement	✓	✓	✓	✓		30/07/14
Learning and Development	✓	✓	✓	✓		05/09/14

Audit title	Audit Progress					Final report issued
	TOR issued	Fieldwork commenced	Fieldwork complete	Draft report issued		
Fostering	✓	✓	✓	✓		09/01/15
Public Health Contracts	✓	✓	✓	✓		20/11/14
Public Health	✓	✓	✓	✓		06/06/14
2014-15 Reviews						
Corporate Cross Cutting						
Transformation	✓	✓	✓			
Health and Safety	✓	✓	✓	✓		22/09/14
Human Resources						
Procurement	✓	✓	✓			
Corporate Governance						
Annual Governance Statement	✓	✓	✓	✓		N/A
Fraud Thematic Review – Housing Office Security/Cash Handling	✓	✓	✓	✓		23/10/14
Precautions against fraud	N/A	✓				
Reactive Fraud	N/A	✓	N/A	N/A	N/A	N/A

Audit title	Audit Progress					Final report issued
	TOR issued	Fieldwork commenced	Fieldwork complete	Draft report issued		
National Fraud Initiative	N/A	✓	N/A	N/A		N/A
Effectiveness of the Role of Internal Audit	✓	✓	✓	✓		14/07/14
Financial Management						
Teachers Pensions - annual claim (TR17)	✓	✓	✓			
Council Tax (including council tax support)	✓	✓	✓			
Income Collection and Transactions	✓	✓				
Accounts Receivable	✓					
Financial Management (budget monitoring)						
Treasury Management						
Value Added Tax	✓	✓	✓			
Bank account change/control						
ICT						
Capacity Planning and Management	✓	✓	✓	✓		
Capita development days / Capita Contract Management						

Audit title	Audit Progress					Final report issued
	TOR issued	Fieldwork commenced	Fieldwork complete	Draft report issued		
Data Centre Security	✓	✓	✓	✓		16/07/14
Corporate Priorities						
Building control	✓	✓	✓	✓		07/10/14
General school reviews – Maytree Infant and Nursery School	✓	✓	✓	✓		12/11/14
General school reviews – Redbridge Community School	✓	✓	✓			
Across Schools Thematic Review - Procurement Cards 14/15	✓	✓	✓	✓		12/11/14
Across Schools Thematic Review – Governance 14/15						
Transport	✓	✓	✓	✓		
Integrated Commissioning Unit						
Contact scheme	✓	✓	✓			
MASH - Multi Agency Safeguarding Hub	✓	✓				
MARP - Multi Agency Resource Panel	✓	✓	✓			
SFVS - School Financial Value Standards	✓	✓	✓		N/A	N/A
School Capital programme	✓	✓	✓			

Audit title	Audit Progress					Final report issued
	TOR issued	Fieldwork commenced	Fieldwork complete	Draft report issued		
Street Lighting PFI	✓	✓	✓	✓		27/10/14
Housing - stock control	✓					
Housing allocation policy	✓					
City Deal						
Adoption						
Better Care Fund						
Delivery of statutory functions - LADO – Local Authority Duty Officer	✓	✓				
Families Matters Governance	✓	✓				
Families Matters grant claims	N/A	✓	✓	N/A		N/A
Financial Assessment Process	✓	✓	✓	✓		
Contribution and charging policies	✓	✓	✓	✓		
Direct payments	✓	✓	✓	✓		
PARIS (Advice role)	✓	✓	✓	N/A		N/A
Local Safeguarding Children's Board	✓	✓	✓	✓		13/11/14

Audit title	Audit Progress				
	TOR issued	Fieldwork commenced	Fieldwork complete	Draft report issued	Final report issued
Delivery of statutory functions - EDT – Emergency Duty team	✓	✓			
Public Health					
Miscellaneous Reviews					
BEEMS	✓	✓	✓	N/A	N/A
PUSH	✓	✓	✓	✓	11/07/14

This page is intentionally left blank

Agenda Item 8

DECISION-MAKER:	GOVERNANCE COMMITTEE		
SUBJECT:	EXTERNAL AUDIT – CERTIFICATION OF CLAIMS AND RETURNS – ANNUAL REPORT 2013/14		
DATE OF DECISION:	9 FEBRUARY 2015		
REPORT OF:	CHIEF INTERNAL AUDITOR		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Neil Pitman	Tel: 023 8083 4616
	E-mail:	neil.pitman@southampton.gov.uk	
Director	Name:	Mark Heath	Tel: 023 8083 2371
	E-mail:	Mark.heath@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY	
N/A	
BRIEF SUMMARY	
<p>The purpose of this paper is to provide the Governance Committee with the outcomes of the external auditor's Certification of Claims and Returns – Annual Report 2013/14.</p> <p>Local authorities claim large sums of public money in grants and subsidies from central government and other grant-paying bodies and are required to complete returns providing financial information to government departments.</p> <p>The 'Certification of Claims and Returns – Annual Report' summarises the findings from the external auditor's certification of 2012/13 claims. It includes the messages arising from their assessment of the Council's arrangements for preparing the claims and returns and information on claims that were amended or qualified.</p> <p>Of the work carried out on the two claims and returns, the external auditor issued a qualification letter with their certificate on the 2013/14 Housing Benefit Subsidy claim.</p>	
RECOMMENDATIONS:	
	(i) to note the External Auditor's annual report on the Certification of Claims and Returns 2013/14 as attached (Appendix 1).
REASONS FOR REPORT RECOMMENDATIONS	
1.	The Governance Committee's Terms of Reference require it to be satisfied and provide assurance that appropriate action is being taken on risk and internal control related issues identified by the external auditors. Specifically the Committee has responsibility for oversight of the reports of external audit.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	None

DETAIL (Including consultation carried out)	
3.	The following external audit report is attached for consideration in Appendix 1: Certification of Claims and Returns – Annual Report 2013/14 The external auditor will be in attendance at the Committee meeting to answer any questions. The report, as attached at Appendix 1, has been discussed and agreed with appropriate officers.
RESOURCE IMPLICATIONS	
<u>Capital/Revenue</u>	
4.	None
<u>Property/Other</u>	
5.	None
LEGAL IMPLICATIONS	
<u>Statutory power to undertake proposals in the report:</u>	
6.	The Accounts and Audit (England) Regulations 2011
<u>Other Legal Implications:</u>	
7.	None
POLICY FRAMEWORK IMPLICATIONS	
8.	None

KEY DECISION?	No
WARDS/COMMUNITIES AFFECTED:	
<u>SUPPORTING DOCUMENTATION</u>	
Appendices	
1.	Certification of Claims and Returns – Annual Report 2013/14
Documents In Members' Rooms	
1.	None
Equality Impact Assessment	
Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
Other Background Documents	
Equality Impact Assessment and Other Background documents available for inspection at:	
Title of Background Paper(s)	Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)
1.	None

Certification of claims and returns annual report 2013/14

Southampton City Council

January 2015

Ernst & Young LLP



Building a better
working world

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

28 January 2015

Ref: SCC/Claims/2013-14

Direct line: 02380 832043

Email: KHandy@uk.ey.com

Dear Members

Certification of claims and returns annual report 2013/14 Southampton City Council

We are pleased to report on our certification work. This report summarises the results of our work on Southampton City Council's 2013/14 claims and returns.

Scope of work

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

Under section 28 of the Audit Commission Act 1998, the Audit Commission may, at the request of authorities, make arrangements for certifying claims and returns because scheme terms and conditions include a certification requirement. When such arrangements are made, certification instructions issued by the Audit Commission to appointed auditors of the audited body set out the work they must undertake before issuing certificates and set out the submission deadlines.

Certification work is not an audit. Certification work involves executing prescribed tests which are designed to give reasonable assurance that claims and returns are fairly stated and in accordance with specified terms and conditions.

In 2013/14, the Audit Commission did not ask auditors to certify individual claims and returns below £125,000. The threshold below which auditors undertook only limited tests remained at £500,000. Above this threshold, certification work took account of the audited body's overall control environment for preparing the claim or return. The exception was the housing and council tax benefits subsidy claim where the grant paying department set the level of testing.

Where auditors agree it is necessary audited bodies can amend a claim or return. An auditor's certificate may also refer to a qualification letter where there is disagreement or uncertainty, or the audited body does not comply with scheme terms and conditions.

Statement of responsibilities

In March 2013 the Audit Commission issued a revised version of the 'Statement of responsibilities of grant-paying bodies, authorities, the Audit Commission and appointed auditors in relation to claims and

returns' (statement of responsibilities). It is available from the Chief Executive of each audited body and via the Audit Commission website.

The statement of responsibilities serves as the formal terms of engagement between the Audit Commission's 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.

This annual certification report is prepared in the context of the statement of responsibilities. It is addressed to those charged with governance and is prepared for the sole use of the audited body. We, as appointed auditor, take no responsibility to any third party.

Summary

Section 1 of this report outlines the results of our 2013/14 certification work and highlights the significant issues.

We checked and certified two claims and returns with a total value of £120,821,944. We met all submission deadlines. We issued one qualification letter for the Housing and Council Tax Benefits claim. Details of the qualification matters are included in section 1. Our certification work found a more minor error which the Council corrected in respect of the Pooling of Housing Capital receipts return. We have not made any recommendations for improvement.

Fees for certification work are summarised in section 2.

We welcome the opportunity to discuss the contents of this report with you at the 9 February 2015 Governance Committee.

Yours faithfully

Kate Handy
Audit Director
For and on behalf of Ernst & Young LLP
Southampton

Enc.

Contents

1. Summary of 2013/14 certification work.....	1
2. 2013/14 certification fees.....	3
3. Looking forward	4

1. Summary of 2013/14 certification work

We certified 2 claims and returns in 2013/14. The main findings from our certification work are provided below.

Housing benefits subsidy claim

Scope of work	Results
Value of claim presented for certification	£114,996,900
Limited or full review	Full
Amended	Not amended
Qualification letter	Yes
Fee – 2013/14	£26,032
Fee – 2012/13	£28,790
Recommendations from prior year:	
None	

Councils run the Government's housing benefits scheme, and claim subsidies from the Department for Work and Pensions (DWP) towards the cost of benefits paid.

Our testing identified no errors in the calculation and classification of benefits awarded to claimants during the year, as presented in the subsidy claim.

As well as testing the calculation of individual benefits awards, the certification instructions require further tests including reviewing the reconciliation of benefit awarded to benefit paid during the year. Our testing found there were minor unreconciled amounts, totalling £59.86. As there is no concept of materiality for the certification work, we were required to report this to the DWP through a qualification letter, which is similar to previous years.

Pooling of housing capital receipts

Scope of work	Results
Value of return presented for certification	£5,825,044
Limited or full review	Full
Amended	Yes
Qualification letter	No
Fee – 2013/14	£1,600
Fee - 2012/13	£1,130
Recommendations from prior year:	
None	

Councils pay part of a housing capital receipt into a pool run by the Department of Communities and Local Government (DCLG). Regional housing boards redistribute the receipts to those councils with the greatest housing needs. Pooling applies to all local

authorities that have a housing function, including those that are debt-free and those with closed Housing Revenue Accounts, who typically have housing receipts in the form of mortgage principal and right to buy discount repayments.

The testing carried out identified one error in classification of disposals between two claims cells in the return for Quarter 2. This was corrected, and made no difference to the total amount certified.

2. 2013/14 certification fees

The Audit Commission sets composite indicative fee for certification work for each body. The indicative fee for 2013/14 was initially based on actual certification fees for 2011/12, reduced by 40%. This was then further adjusted to reflect the fact that a number of schemes would no longer require auditor certification, and a 12% reduction was also applied to the Housing Benefit Subsidy claim due to the replacement of Council Tax Benefit with Council Tax Support which is not part of that claim.

The indicative composite fee for Southampton City Council for 2013/14 was £29,036.

We have completed the work required within this indicative fee total.

Claim or return	2013/14	2013/14	2012/13
	Indicative fee	Actual fee	Actual
	£	£	£
Housing and council tax benefits subsidy	27,436	26,032	28,790
Pooling of housing capital receipts return	1,600	1,600	1,130
Teachers' superannuation return	n/a	n/a	1,850
National non-domestic rates return	n/a	n/a	1,180
Total	29,036	27,632	32,950

Note: Fees for annual reporting and for planning, supervision and review have been allocated directly to the claims and returns.

Fees fell overall due to the reduction in claims requiring certification.

Housing Benefits Subsidy

The indicative fee was set based on work completed in 2011/12, when due to identified errors additional 40+ testing was undertaken on the claims, and a qualification letter issued.

As we found no errors this year, there was no such requirement for extended testing. Therefore, we were able to complete the work in comparatively less time.

Pooling of housing capital receipts

Due to errors identified in the prior year, we undertook comparatively more extensive testing.

3. Looking forward

The Council's indicative certification fee for 2014/15 is £25,340. This is based on the outturn from 2012/13 certification work, again adjusted for claims no longer requiring review. The actual certification fee for 2014/15 may be higher or lower than the indicative fee, if we need to undertake more or less work than in 2012/13 on individual claims or returns. Details of individual indicative fees are available at the following link:

<http://www.audit-commission.gov.uk/audit-regime/audit-fees/201415-work-programme-and-scales-of-fees/individual-indicative-certification-fees/>

We must seek the agreement of the Audit Commission, or its successor body, to any proposed variations to indicative certification fees. The Audit Commission expects variations from the indicative fee to occur only where issues arise that are significantly different from those identified and reflected in the 2012/13 fee.

The Audit Commission has changed its instructions to allow appointed auditors to act as reporting accountants where the Commission has not made or does not intend to make certification arrangements. This removes the previous restriction saying that the appointed auditor cannot act if the Commission has declined to make arrangements.

EY | Assurance | Tax | Transactions | Advisory

Ernst & Young LLP

© Ernst & Young LLP. Published in the UK.
All Rights Reserved.

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

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

ey.com

This page is intentionally left blank

Agenda Item 9

DECISION-MAKER:	COUNCIL GOVERNANCE COMMITTEE		
SUBJECT:	LOCALISM ACT 2011 – APPOINTMENT OF DESIGNATED INDEPENDENT PERSON(S) AND GOVERNANCE COMMITTEE INDEPENDENT MEMBERS		
DATE OF DECISION:	18 MARCH 2015 (COUNCIL) AND 9 FEBRUARY 2015 (GOVERNANCE COMMITTEE)		
REPORT OF:	HEAD OF LEGAL AND DEMOCRATIC SERVICES		
<u>CONTACT DETAILS</u>			
AUTHOR:	Name:	Richard Ivory	Tel: 023 8083 2794
	E-mail:	Richard.ivory@southampton.gov.uk	
Director	Name:	Mark Heath	Tel: 023 8083 2028
	E-mail:	Mark.heath@southampton.gov.uk	

STATEMENT OF CONFIDENTIALITY		
None		
BRIEF SUMMARY		
<p>This report has two parts, however both are related as they refer to the revised arrangements for appointment of independent persons/members in relation to the Council's decision making and democracy. The first relates to the need under the Localism Act 2011 to appoint a Designated Independent Person (DIP) in relation to Members Code of Conduct complaints. The second relates to the appointment of independent members to the Governance Committee which is a locally agreed convention since July 2012. Both sets of appointments are due for review as the terms of office are to expire shortly.</p>		
RECOMMENDATIONS:		
COUNCIL resolves that:		
	(i)	<p>(a) one Designated Independent Person as required under S.28(7) Localism Act 2011 be appointed from 1st July 2015 for a term of 3 years;</p> <p>(b) the two independent member appointments to the Governance Committee cease on 20th May 2015 and it be noted that the appointment of independent members will end ;</p> <p>(c) the current independent members, David Blake and Geoff Wilkinson be thanked for their work during the past three years;</p> <p>(d) the Head of Legal and Democratic Services be authorised to carry out all actions to give effect to this resolution.</p>
GOVERNANCE COMMITTEE resolves		
	(i)	that having considered this report it recommends to Council (i) as above or such other decision as it decides.

REASONS FOR REPORT RECOMMENDATIONS	
1.	As described in the Brief Summary above.
ALTERNATIVE OPTIONS CONSIDERED AND REJECTED	
2.	None, both sets of appointments are to expire shortly and decisions on the future of the positions are required.
DETAIL (Including consultation carried out)	
Designated Independent Person	
3.	On 16th May 2012 the Council resolved as part of the new standards arrangements under the Localism Act 2011 to appoint two Designated Independent Persons. The Act specifies that "Arrangements" adopted by Councils must include provision for the appointment by the Council of at least one DIP. The DIP must be appointed through a process of public advertisement, application and appointment. This process was delegated to the Head of Legal and Democratic Services.
4.	The statutory criteria for a DIP is as follows:-
	<p>A person is considered not to be "Independent" if –</p> <ul style="list-style-type: none"> • He/she is, or has been within the last 5 years, an elected or co-opted member or an officer of the Council. • He/she is, or has been within the last 5 years, an elected or co-opted member of any Committee or Sub Committee of the Council (which would preclude any of the co-opted independent members of Standards Committee from being appointed as an Independent Person); or • He/she is a relative or close friend of a current elected or co-opted member or officer of the Council.
5.	Statutory functions of the Designated Independent Person
	<p>The functions of the DIP(s) are:–</p> <ul style="list-style-type: none"> • They must be consulted by the Authority before it makes a finding as to whether a Member has failed to comply with the Code of Conduct or decides on action to be taken in respect of that Member. • They may be consulted by the Authority in respect of a standards complaint at any other stage; and • They may be consulted by a Member or co-opted member of the Council against whom a complaint has been made.
6.	Since the adoption of the new Code of Conduct for Members there have been very few complaints. All those that have been made have been minor and have been investigated by the Monitoring Officer (Director of Corporate Services) or his Deputy (Head of Legal and Democratic Services) under delegated powers. None of the complaints have been made out. On occasions there has been a need to involve the DIPs as a "sounding board" but there have never been any formal complaints that have required the involvement of the Governance Committee or crucially both DIPs at once because of any conflict.
How many DIPS are still required	
7.	The Act gives discretion to appoint one or more DIP. At the outset, some three years ago, it was considered that on occasions there could be a conflict

	of interests and accordingly it was prudent to appoint at least two, at least initially whilst the new arrangements settled in. This need has not been borne out over this period. Very few authorities nationally have two DIPs or have found difficulties in only having one appointed. Accordingly, it is not considered there is any need to continue with two DIPs.
--	--

Independent Members

8.	As part of the revised arrangements for the Governance Committee the Council also resolved to appoint two independent members. It is a locally agreed convention that is rare in other authorities nationally. The reasoning behind the appointments was that it was considered the new standards regime, as it was entirely local and internally managed, could become political if solely judged by peers. Accordingly they added both transparency and obviously an element of independence to any “sanction” process should a breach of the code require investigation by the Governance Committee.
9.	As referred to above the Committee has never had to investigate or pass judgement on any breaches as the complaints have been very minimal and minor in nature.
10.	The members are invited to attend each Governance Committee as non voting members irrespective of the business on the agenda, which in the main is financial or audit related. Accordingly, after discussion with the Chair of the Governance Committee, as the appointments are about to expire it is considered reasonable to bring the appointments to an end.

RESOURCE IMPLICATIONS

Capital/Revenue

11.	Each DIP and independent member receives an allowance under the Members Allowance scheme of £645, therefore an annual amount of £2580 is budgeted. The reduction of the roles from 4 to 1 would result in a small annual budget saving of £1935.
-----	--

Property/Other

12.	None
-----	------

LEGAL IMPLICATIONS

Statutory power to undertake proposals in the report:

13.	Section 28(7) Localism Act 2011 requires the appointment of at least 1 DIP. The Local Government Act 1972 and 2000 permits external and non voting independent members.
-----	---

Other Legal Implications:

14.	None
-----	------

POLICY FRAMEWORK IMPLICATIONS

15.	None
-----	------

KEY DECISION?	No
WARDS/COMMUNITIES AFFECTED:	None

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