Audit and Standards Committee

Tuesday, 10th February, 2015 at 6.00pm
in Committee Room 3 at the Council House, Priory Road, Dudley

Agenda - Public Session
(Meeting open to the public and press)

1. Apologies for absence.

2. To report the appointment of any substitute Members for this meeting of the Sub-Committee.

3. To receive any declarations of interest under the Members' Code of Conduct.

4. To confirm and sign the minutes of the meeting held on 9th December, 2014 as a correct record.

5. Grant Thornton Audit Committee Update (Pages 1 – 15)

6. Grant Thornton Letter: Grant Certification Work 2013/14 (Pages 16 – 20)

7. Treasury Management (Pages 21 – 37)

8. To consider any questions from Members to the Chair where two clear days notice has been given to the Strategic Director (Resources and Transformation) (Council Procedure Rule 11.8).

   Under the provisions of Part I of Schedule 12A to the Local Government Act 1972, the Director of Corporate Resources has decided that there will be no advance disclosure of the following reports because the public interest in disclosing the information is outweighed by the public interest in maintaining the exemption from disclosure

   The submission of these reports complies with the Local Authorities (Executive Arrangements)(Meetings and Access to Information)(England) Regulations 2012

9. Resolution to exclude the public and press

Chair to move:

"That the public and press be excluded from the meeting for the following item of business on the grounds that it involves the likely disclosure of exempt information under Part I of Schedule 12A to the Local Government Act 1972, as amended, for the reasons stated on the agenda."

Agenda - Private Session

(Meeting not open to the public and press)

10. Audit Services Interim Performance Report (Pages 38 – 56)

11. Annual Audit Report in relation to the Directorate of Children's Services (Pages 57 – 102)

12. Employees not taking lunch breaks or compensatory breaks (Pages 103 – 109)

Strategic Director (Resources and Transformation)
Dated: 29th January, 2015

Distribution:

Councillor J Cowell (Chair)
Councillor M Roberts (Vice-Chair)
Councillors A. Aston; C Billingham; P Brothwood; M. Evans; D. Russell, A. Taylor and D Tyler

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- If you (or anyone you know) is attending the meeting and requires assistance to access the venue and/or its facilities, please contact the contact officer below in advance and we will do our best to help you.

- Information about the Council and our meetings can be viewed on the website **www.dudley.gov.uk**

- Elected Members can submit apologies by contacting the officer named below. The appointment of any Substitute Member(s) should be notified to Democratic Services at least one hour before the meeting starts.

- The Democratic Services contact officer for this meeting is Karen Taylor, Telephone 01384 818116 or E-mail **karen.taylor@dudley.gov.uk**

Minutes of Audit and Standards Committee

Tuesday 9th December, 2014 at 6.00 p.m.
in Committee Room 3, The Council House, Dudley

Present:-

Councillor J Cowell (Chair)
Councillor M Roberts (Vice-Chair)
Councillors P Brothwood, M Evans, J Martin, C Perks, D Russell and A Taylor

Officers:-

I Newman (Treasurer); L Bourne (Principal Information Security Officer); L Bradshaw (Head of Audit Services); L Cleeton (Review and Improvement Consultant); M Farooq (Assistant Director – Law and Governance); G Harrison (Audit Manager - Central Services); T Reilly (Assistant Director – HR and Organisational Development); R Sims (Assistant Director – Housing Strategy and Private Sector); A Taylor (Principal Auditor), and K Taylor (Democratic Services Officer).

Also in Attendance:-

S. Joberns (Grant Thornton)

28. **Apologies for Absence**

Apologies for absence from the meeting were submitted on behalf of Councillors A Aston, C Billingham and D Tyler.

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29. **Appointment of Substitute Members**

It was reported that Councillors J Martin and C Perks had been appointed as substitute members for Councillors A Aston and D Tyler, respectively, for this meeting of the Committee only.

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30. **Declarations of Interest**

No Member made a declaration of interest in accordance with Members' Code of Conduct in respect of any matter to be considered at this meeting.

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31. **Minutes**

Arising from consideration of the minutes, Councillor Roberts referred to the pre-amble to Minute 20 and reported that she had still not received a response from the Director of the Urban Environment in relation to the Castle Hill Development Project.

Resolved

That the minutes of the meeting held on 18th September, 2014, be approved as a correct record and signed.

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32. **Change in Order of Business**

Pursuant to Council Procedure Rule 13(c) it was:-

Resolved

That the remaining items of business be considered in the following order :-

Agenda Item Nos. 10, 12, 5, 6, 7 and 11

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33. **Exclusion of the Public**

That the public and press be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information relating to any individual(s) as defined under Part I of Schedule 12A to the Local Government Act 1972.

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34. **Suspensions under the provisions of the Employee Improvement and Disciplinary Procedure**

A report of the Director of Corporate resources was submitted on the numbers of employees suspended pending an investigation into allegations of gross misconduct during October, 2013 to September, 2014.

Arising from consideration of the report submitted, reference was made to the number of suspensions during October, 2013 and September, 2014, the majority of which related to Schools that were under the control of the Local Education Authority. It was also noted that the average length of suspensions, specifically those relating to schools, were high in view of the school holidays and the complexity of some cases.

The Assistant Director of HR and Organisational Development reported that the average cost spent on suspensions varied significantly dependent upon the salary level, contract and complexity of the case

It was also noted that due to the potentially high monetary value of unfair dismissal compensatory awards it was important that investigations and suspensions were undertaken correctly.

It was also noted that due to the corporate restructure and the reduction of Senior Management, it could affect future investigations in terms of the number of senior officers available for chairing disciplinary panels.,

Members asked a number of questions and made comments which were responded to, in particular, in respect of employees returning to their jobs following an investigation that resulted in them receiving action short of dismissal, and the procedure when an employee who had been suspended pending investigation went on sick leave.

At this juncture, Members requested specific information in relation to suspensions highlighted in the report submitted, in particular, the process undertaken and a chronology of events, in order to identify that investigations were undertaken effectively and whether there were sufficient members of staff in HR to support.

Following further discussion it was,

RESOLVED

> That the information contained in the report submitted be noted, but that full commentary on the report be deferred and that a further report detailing specific information in relation to a selection of four suspensions to be submitted to a future meeting of the Committee.

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35. **Annual Audit Report in relation to the Directorate of Adult, Community and Housing Services**

A report of the Treasurer was submitted on the audit work, undertaken in the Directorate of Adult, Community and Housing Services for the financial year 2013/14 and incorporating details of the more important findings as indicated in Appendix 2 and 3 to the report submitted.

Arising from consideration of the report, and Appendix to the report, submitted reference was made to the improvement of the number of post audit questionnaires completed and returned and the percentage of final reports issued within six weeks of the draft report.

It was noted that there were a high number of findings for the two Adult Care and Support Teams and the Access Team, however these were new audits following a reorganisation within Adult Social Care.

Members asked a number of questions and made comments which were responded to, in particular, in respect of the increase of unimplemented recommendations, and the management responses highlighted in the report.

Following comments made, the Assistant Director of Housing Strategy and Private Sector assured the Committee that work was being undertaken to address the recommendations highlighted in the report submitted.

In responding to a question raised by Members in relation to comparative costs from different companies that provided translations and interpretations not being reviewed on an annual basis, the Assistant Director of Housing Strategy and Private Sector undertook to provide Councillor Brothwood with data in relation to the costs involved from using the current and a different supplier.

Concerns were raised by Members in relation to employees not taking their lunch breaks or compensatory breaks, in accordance with the Working Time Directive. It was noted that staff were now having their breaks, however it had had a major impact on service delivery and it had been difficult to allocate a break, therefore some employees had written to HR requesting to opt out of the directive. In responding, the Assistant Director of Housing Strategy and Private Sector stated that the Assistant Director of Quality and Commissioning would be agreeable to attend a future meeting of the Committee to provide an update and discuss the matter further.

In responding to a question, the Review and Improvement Consultant undertook to provide the Chair with further information in relation to the amount of time during which there was not a protocol in place for the sharing of partnership information, and an update on the implementation of a GCSX account to transfer confidential information to third parties.

In responding to a question, the Review and Improvement Consultant undertook to update Councillor Taylor on the project plan for Shared Lives, which was currently on hold.

Resolved

(1) That the findings of the 2013/14 audit work be accepted.

(2) That the Assistant Director of Housing Strategy and Private Sector be requested to provide Councillor Brothwood with data in relation to the costs involved using the current and a different supplier for translations and interpretations.

(3) That the Review and Improvement Consultant be requested to provide the following:

a) Councillor Cowell with further information in relation to the amount of time during which there was not a protocol in place for the sharing of partnership information, and an update on the implementation of a GCSX account to transfer confidential information to third parties.

b) Councillor Taylor with an update in relation to the project plan for Shared Lives.

(4) That the Assistant Director of Quality and Commissioning be requested to attend a future meeting of the Committee to provide an update and further information in relation to the issues with regard to staff not taking a break in accordance with the Working Time Directive.

At this juncture, Councillor D Russell withdrew from the remainder of the meeting.

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36. **<u>Grant Thornton Annual Audit Letter 2013/14</u>**

A joint report of the Chief Executive and the Treasurer was submitted on the Council's external auditors annual Audit Letter for 2013/14. A copy of the letter was appended to the report submitted.

Ms S Joberns presented the report and Appendices to the report submitted, and issued an unqualified opinion.

Resolved

That the information contained in the report, and Appendices to the report, submitted on the Annual Audit Letter 2013/14, be noted.

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37. **<u>Annual Report of the Committee on Standards in Public Life</u>**

A report of the Monitoring Officer was submitted on the annual report of the Committee on Standards in Public Life 2013/14. A copy of the report was appended to the report submitted.

Arising from the presentation of the report and Appendix to the report, submitted, the Assistant Director of Law and Governance made particular reference to the comments on Local Government Standards arising from the introduction of the new standards regime under the Localism Act 2011.

Resolved

That the Annual Report of the Committee on Standards in Public Life, attached as Appendix 1 to the report submitted, be noted.

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38. **Risk Management**

A report of the Treasurer was submitted on current corporate risks and other matters relating to risk management, and to provide closer scrutiny of the Council's corporate risk – Risk ORG0013 – Information Governance – that was identified for consideration by the Committee at a previous meeting.

The Principal Information Security Officer gave a power point presentation in relation to Information Governance, and in doing so stated that the area covered a broad spectrum and there was continued pressure from the Government to recognise Information as a key asset.

The Principal Information Security Officer reported to the Committee that Local Authorities were required to comply with statutory obligations, and that there would be some changes to the Data Protection Act in 2016/17.

Reference was made to the legal requirement to maintain personal data for a number of years, including staff records, and that the information was held in a number of systems identified within the Information Asset Register.

The Principal Information Security Officer reported that 1,700 requests for information under the Data Protection Act, Freedom of Information and Environmental Information Regulations Act 2004 had been received during 2014, 82% of which were processed within time. It was noted that the estimated cost of handling requests in 2014 was £272,000, and that there were over 50 Agreements implemented with third parties to enable sharing and use of information.

It was noted that there was a robust programme of compliance throughout the Council, and 56 non-ICT breaches had been investigated during 2014, the majority of which were due to paper which continued to be the biggest risk. The number of requests received increased on a yearly basis, and it was evident that the quality of requests had improved.

Reference was then made to the mitigating controls that had been implemented including an Information Governance Board to oversee development of and compliance with information governance policies and a mandatory online training programme for Data Protection, Freedom of Information and Information Security for all staff. It was also noted that a Statement of Undertaking had been issued from the Information Commissioner following a breach, which resulted in an Action Plan being developed, and that the Information Commissioner was satisfied with the progress undertaken.

Arising from the presentation, Members asked a number of questions and the Principal Information Security Officer responded as follows:-

- In relation to the cost implications of Freedom of Information requests, it was reported that there was a limit of 18 hours or less than £450 of work that was free of charge to the requester, and that three requests had been received since 2004, where payment of a fee had been requested, and requests that appeared similar during a sixty day period, would be aggregated. It was noted however that the aim was to decrease the number of requests by allowing data that was not confidential to be readily available and on the Dudley MBC domain.
- Following a request by a Member, the Principal Information Security Officer undertook to circulate the presentation to Members of the Committee.
- That initial requests for Data Protection Subject Access information were not charged, however this may be looked at in the future.
- That there was a requirement legally to demonstrate and publish compliance with Freedom of Information requests on the website on a yearly basis, and following a request the Principal Information Security Officer undertook to look at publishing the information in a user-friendly format.

During his presentation of the content of the report, and Appendix 1 to the report submitted, the Treasurer referred, in particular, to the Committee giving consideration to identifying and scrutinising a specific risk from those shown in the Appendix for consideration when the Committee next considered the issue of corporate risks at its meeting in February, 2015. It was noted that due to the number of items to be considered at the next meeting of the Committee, the Committee may be minded to defer consideration of the risk until April, 2015.

Resolved

(1) That the information contained in the report, and Appendix 1 to the report, submitted on current corporate risks and other matters relating to risk management, be noted.

(2) That the risk ORG0013 – Information Governance, be noted.

(3) That the risk ORG0019 – Fraud - be the particular risk identified for closer scrutiny the next time a risk report was referred for consideration by the Committee, in April, 2015.

(4) That the Principal Information Security Manager be requested to circulate the presentation given to all Members of the Committee, and to look at ensuring the information submitted on the website, was easy to understand.

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39. **Exclusion of the Public**

That the public and press be excluded from the meeting for the following items of business on the grounds that it involves the likely disclosure of exempt information relating to any individual(s) as defined under Part I of Schedule 12A to the Local Government Act 1972.

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40. **Fraud Presentation**

The Head of Audit Services gave a power point presentation in relation to Fraud Awareness and outlined the roles and responsibilities in the prevention, detection and investigation of fraud. The presentation was given following a request made at the previous Committee meeting arising from a discussion on the skills and knowledge questionnaire undertaken by Members of the Committee and the need for further training.

During his presentation, the Head of Audit Services made particular references to the Fraud Act that was implemented in January, 2007, the outcome of fraud, and the Bribery Act 2010, which was also referenced in the Members' Code of Conduct, specifically in respect of declaring pecuniary and non-pecuniary interests. It was also reported that specific fraud areas such as Procurement, Housing and Council Tax were being looked at in line with the National Fraud Authority strategy.

Reference was made to the profile of staff that committed fraud and various ways in how to detect fraud, however ultimately it was the responsibility of managers to identify and detect fraud. It was noted that the introduction of the Fraud Hotline had resulted in an average of 150 calls, and had proven to be successful.

The Head of Audit Services referred to a fraud formula, namely, MOM (Motive + Opportunity + Means), and stated that Audit Services were concentrating on identifying the opportunity and means, specifically, weak control, poor management, and access to assets and cash.

It was noted that CIPFA had recently issued guidance and that Dudley MBC complied with the CIPFA Code of Practice "Managing the Risk of Fraud and Corruption", including implementing a Anti Fraud and Corruption Strategy, an Audit and Standards Committee and a Confidential Reporting Policy.

Arising from the presentation given, the Head of Audit Services responded to questions asked by the Committee in relation to the controlling measures in place in relation to attempted fraud via computers, and confirmed that the Fraud Hotline telephone number (01384 814242) had also been displayed on the side of vans used by employees in Housing.

Resolved

> That the presentation given in relation to Fraud Awareness be noted.

The meeting ended at 8.35 p.m.

CHAIR

Agenda Item No. 5

Audit and Standards Committee 10th February 2015

Report of the Chief Officer Finance and Legal Services

Grant Thornton Audit Committee Update

Purpose of Report

1. Grant Thornton have produced a report to update Audit and Standards Committee members on progress in delivering their responsibilities as Dudley's external auditors, and the Audit Manager will be available at the meeting to deal with any issues.

Background

2. The report is attached as Appendix 1. The report provides Audit and Standards Committee with an update on progress in delivering Grant Thornton's responsibilities as external auditors. The report also includes a summary of emerging national issues and developments that are relevant to the Council.

Finance

3. There are no resource implications as a consequence of the report.

Law

4. Legislation appertaining to Local Authority Audit and Accounts is contained in the Local Government Act 1999, the Audit Commission Act, 1998, and regulations made therein.

Equality Impact

5. The proposals take into account the Council's Policy on Equality and Diversity.

Recommendation

6. That Members note the Audit Committee Update report

………………………………………….
Iain Newman
Chief Officer Finance and Legal Services

Contact Officer: Jan Szczechowski
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Email: jan.szczechowski@dudley.gov.uk

List of Background Papers

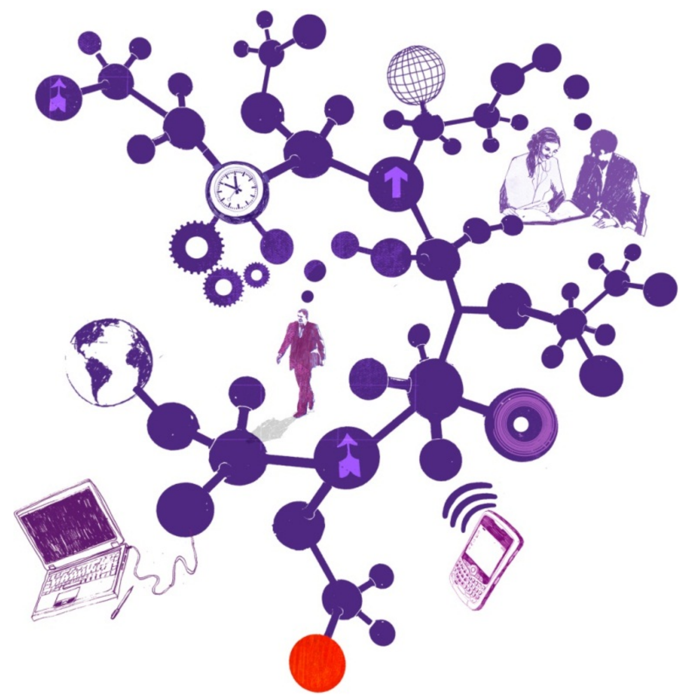
Appendix 1 Grant Thornton Audit Committee Update for Dudley Metropolitan Borough Council

Grant Thornton

Audit and Standards Committee Update

Year ended 31 March 2015

January 2015



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Contents

The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect your business or any weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

Introduction

This paper provides the Audit and Standards Committee with a report on progress in delivering our responsibilities as your external auditors. The paper also includes a summary of emerging national issues and developments that may be relevant to you; and

Members of the Audit and Standards Committee can find further useful material on our website www.grant-thornton.co.uk, where we have a section dedicated to our work in the public sector (http://www.grant-thornton.co.uk/en/Services/Public-Sector/). Here you can download copies of our publications including:

- Rising to the challenge: the evolution of local government, summary findings from our fourth year of financial health checks of English local authorities
- 2020 Vision, exploring finance and policy future for English local government
- Where growth happens, on the nature of growth and dynamism across England

Progress at January 2015

Work	Planned date	Complete?	Comments
2014-15 Accounts Audit Plan We are required to issue a detailed accounts audit plan to the Council setting out our proposed approach in order to give an opinion on the Council's 2014-15 financial statements.	April 2015	No	The audit plan with be issued to officer in February 2015 and presented to the April Committee Meeting.
Interim accounts audit Our interim fieldwork visit includes: • updating our review of the Council's control environment • updating our understanding of financial systems • review of Internal Audit reports on core financial systems • early work on emerging accounting issues • early substantive testing • proposed Value for Money conclusion.	January – March 2015	No	We have commenced our first interim visit and have arranged a further visit in March 2015.
2014-15 final accounts audit Including: • audit of the 2014-15 financial statements • proposed opinion on the Council 's accounts • proposed Value for Money conclusion.	June 2015	No	

Rising to the challenge

Grant Thornton

Our national report, Rising to the Challenge, the Evolution of Local Government, was published in December and is available at:
http://www.grant-thornton.co.uk/en/Publications/2014/Rising-to-the-challenge---The-evolution-of-local-government/

This is the fourth in our series of annual reports on the financial health of local government. Like previous reports, it covers key indicators of financial performance, strategic financial planning, financial governance and financial control. It also includes case studies of best practice and a comparison to the NHS. This year it has been extended to use benchmarking information on savings plans and budget performance.

The overall message is a positive one. What stands out is how well local authorities have navigated the first period of austerity in the face of ever increasing funding, demographic and other challenges. Many authorities are forecasting financial resilience confidently in their medium term financial strategy. This reflects an evolution in financial management that would have been difficult to envisage in 2010. However, there remains much to be achieved if the sector is to become sustainable in the long term, and authorities should consider if their:

- medium- to long-term strategy redefines the role of the authority creatively
- operational environment will adapt, working in partnership with other authorities and local organisations
- strategy looks beyond the traditional two- to three-year resource planning horizon
- organisational culture is aligned to where the authority needs to be in the medium to long term
- senior leadership teams – both officers and members – have the necessary skills and capacity to ensure delivery against the medium-term challenges
- corporate governance arrangements ensure effective oversight and scrutiny of the organisation as it adapts to the challenges it faces.

The importance of these actions will be magnified if local government devolves further, particularly in relation to fiscal devolution. The new-found confidence of local government in responding to the medium-term challenges will be tested significantly by the second phase of austerity.

Hard copies of our report are available from your Engagement Lead or Audit Manager.

2020 Vision

Grant Thornton
Our national report '2020 Vision' is available at: http://www.grant-thornton.co.uk/en/Publications/2014/2020-Vision-Exploring-finance-and-policy-futures-for-English-local-government-as-a-starting-point-for-discussion/ In a time of unprecedented challenge for English local government, how can the sector develop towards 2020 if it is to have a sustainable future? Our latest report provides a thorough analysis of the current political and economic context, explores a range of potential policies and outcomes, and suggests several scenarios to facilitate an open debate on the future for the sector. Produced in collaboration with the University of Birmingham's Institute for Local Government Studies (INLOGOV), our report suggests that fundamental changes to local government are both operationally necessary and constitutionally inevitable, for the sector to remain relevant by 2020. The report offers a thorough analysis of the current political and economic context and explores a range of potential future policies and outcomes that English local government will need to adopt and strive towards as they seek to adapt and overcome these challenges. Placed in the context of enhanced devolution, following the Scottish independence referendum, 2020 Vision maintains a wary eye fixed on the 2015/16 Spending Round and looks ahead to the life time of the next government. It highlights that the economic and financial situation remains increasingly untenable, with an expanding North/South divide arising from the pattern of funding reductions and economic growth. It highlights that English local authorities continue to face unprecedented challenges, relating to the pressures of austerity and central government funding reductions, and demographic and technological change. Our report highlights the vital role of a successful local government sector and encourages it to think hard about how it will cope in the future. Informed by the views of a broad range of local authority leaders, chief executives and other sector stakeholders, the report offers a set of six forward-looking scenarios* in which councils could be operating within by 2020. Though not mutually exclusive, we suggest that key stakeholders need to take urgent action to avoid a potential slow and painful demise for some councils by 2020. Hard copies of our report are available from your Engagement Lead or Audit Manager.

Pulling together the Better Care Fund

Grant Thornton
Our national report 'Pulling together the Better Care Fund' is available at: http://www.grant-thornton.co.uk/en/Publications/2014/Pulling-together-the-Better-Care-Fund/. The reports asks 'Do local authorities and clinical commissioning groups (CCGs) have effective arrangements to develop joint Better Care Plans for agreement by the health and wellbeing boards (HWBs) and how ready are they for the pooled fund in April 2015?' Our report draws on our review of the introduction of draft Better Care Fund (BCF) plans for both the February and April submissions. It is based on a sample of our findings from 40 HWB localities. It considers the partnership arrangements across a HWB planning area and is supported by discussions with the sector, across the country. The result is a snap shot of progress as at 30 June 2014, prior to the issue of revised planning guidance by NHS England and the Local Government Association on 25 July 2014. It provides you with: • an understanding of how your approach to introducing BCF compares to others across the country • assistance in identifying the key issues to delivering Better Care Fund plans effectively • insight into current best practice • practical areas for consideration for improving arrangements in the future. Hard copies of our report are available from your Engagement Lead or Audit Manager.

Accounting for schools

Accounting and audit issues

Accounting for schools

The debate about the recognition of school land and buildings on local authority balance sheets (which most commentators had thought settled) has been reignited. Grant Thornton is taking a leading role in trying to resolve this unexpected development.

In March, CIPFA/LASAAC Code concluded that under IFRS 10, maintained schools (but not free schools or academies) meet the definition of entities that need to be consolidated in group accounts. However, rather than requiring local authorities to prepare group accounts, the CIPFA/LASAAC Code requires local authorities to account for maintained schools within their single entity accounts. This includes school income and expenditure as well as assets and liabilities. The general expectation in the sector was that:

- the vast majority of voluntary aided, voluntary controlled and foundation schools would be recognised on local authority balance sheets
- a small number of school buildings that are provided at no charge by a religious body and where there was a realistic possibility that they could be taken back by their owners would be treated as assets of the religious body and so not recognised on the local authority balance sheet.

However, at the CIPFA conference in November, CIPFA clarified that it considers that most voluntary aided and voluntary controlled school buildings would **not** be recognised on the balance sheet. This is because the religious bodies have a legal right to take back these assets. Nor does CIPFA consider the position for foundation school building to be clear cut and local judgement would need to be applied. We have not seen evidence that would support the view taken by CIPFA and have concerns about:

- whether the treatment proposed by CIPFA complies with the Code
- the significant practical implications for the sector
- the potential for inconsistent accounting treatments depending on local judgement.

We are working with the Audit Commission, CIPFA and the other audit firms suppliers to try to seek a practical way forward as soon as possible.

Group accounting standards

Accounting and audit issues

The CIPFA Code has adopted a new suite of standards for accounting for subsidiaries, associates and joint arrangements. These changes affect how local authorities account for services delivered through other entities and joint working with partners.

The key changes for 2014/15 are to:

- the definition of control over 'other entities'. The revised definition is set out in IFRS 10 and determines which entities are treated as subsidiaries
- the accounting for joint arrangements. This now follows IFRS 11 and includes changes to the definition of joint ventures and how joint ventures are consolidated in group accounts
- disclosures in relation to subsidiaries, joint arrangements, associates and unconsolidated entities as set out in IFRS 12.

Changes to the definition of control over 'other entities'
Control was previously defined in terms of power to govern the financial and operating policies of an entity. IFRS 10 sets out three elements for an investor to be considered as controlling an investee (all of which must be met):

- the investor has the rights to direct the relevant activities of the investee (relevant activities being the ones that determine the return for the investors – the return could be in the form of a service rather than money)
- the investor has exposure, or rights, to variable returns from its involvement with the investee
- the investor has the ability to use its power over the investee to affect the amount of the investor's returns.

In the commercial sector, this is generally thought to have resulted in more entities being treated as subsidiaries. However, the change is in both directions: some subsidiaries have been redefined as associates. Local authorities with investments in 'other entities' will need to consider whether:

- they control any entities using the new definition. Local authorities will need to pay particular attention to special purpose vehicles and any other entities where there was a close judgement call under the old IAS 27
- there is a need for a prior period adjustment.

Group accounting standards (continued)

Accounting and audit issues

Changes to accounting for joint arrangements

Joint arrangements are contractual arrangements between two or more parties where there is joint control. IFRS 11 makes three key changes from IAS 31:

- there are now only two types of joint arrangements: joint operations and joint ventures
- under IAS 31 joint ventures were legal entities. IFRS 11 bases its definition of joint ventures on the substance of the arrangement rather than legal status. In a joint operation the investing parties have rights and obligations in relation to the arrangement's assets and liabilities, whereas in a joint venture the parties have rights to the arrangement's net assets
- local authorities are still required to consolidate joint ventures in their group accounts but must now do so using the equity (single line) method. The option for proportionate (line-by-line) consolidation has been removed.

The key challenge for most local authorities will be determining whether their joint arrangements are joint ventures or joint operations. The difference should be clear from the contract but in some cases judgement may be required. Local authorities that have previously used the proportionate consolidation method will need to account for the move to equity accounting as a prior period adjustment.

Disclosure of interests in other entities

IFRS 12 makes consistent the requirements for disclosures in relation to subsidiaries, joint arrangements, associates and unconsolidated entities. It includes the need for transparency about the risks to which the reporting entity is exposed as a consequence of its investment in such arrangements.

Earlier closure and audit of accounts

Accounting and audit issues
DCLG is consulting on proposals to bring forward the audit deadline for 2017/18 to the end of July 2018. Although July 2018 is almost 4 years away, both local authorities and their auditors will have to make real changes in how they work to ensure they are 'match-fit' to achieve this deadline. This will require leadership from members and senior management. Local government accountants and their auditors should start working on this now. Top tips for local authorities: • make preparation of the draft accounts and your audit a priority, investing appropriate resources to make it happen • make the year end as close to 'normal' as possible by carrying out key steps each and every month • discuss potential issues openly with auditors as they arise throughout the year • agree key milestones, deadlines and response times with your auditor • agree exactly what working papers are required.

Kerslake report on Birmingham City Council

Local government guidance

Sir Bob Kerslake published his report, The way forward: an independent review of the governance and organisational capabilities of Birmingham City Council, on 9th December.

Commissioned by the Secretary of State this comes off the back of well publicised failures in Children's Services and the Trojan Horse issue in Birmingham Schools. It includes some tough messages for Birmingham City, but there are issues that resonate with all large local authorities.

The report's recommendations include the following.

- The Council needs an external Improvement Board to show that it is making the changes it needs to effectively serve its population.
- Internal governance needs fundamental change, including the relationship between members and officers, how it plans for the future, a stronger corporate core and a programme of culture change.
- The Council needs more political clarity, moving away from annual thirds elections and reducing the number of members. This includes redesigning the model for representative governance.
- Medium term financial planning needs greater clarity, and the Council cannot assume that it will get any additional Government support.
- In moving from a 20,000 people organisation in 2010 to a 7,000 people one by 2018 the Council needs fit for purpose workforce planning.
- Devolution within the Council and across the City needs simplifying and a greater outcome focus.
- Partnership working needs redefining, with the Council moving away from a 'Big Brother' approach.
- The Council needs to work with the other West Midland MBCs to make the combined authority a reality that delivers jobs and prosperity to the region.

Grant Thornton

grant-thornton.co.uk

Agenda Item No. 6

Audit and Standards Committee – 10th February 2015

Report of the Chief Officer Finance and Legal Services

Grant Thornton Letter: Grant Certification Work 2013/14

Purpose of Report

1. The External Auditor's Letter on Certification of Claims and Returns for 2013/14 is attached and representatives from Grant Thornton will be available at the meeting to deal with any issues.

Background

2. As from 1 November 2012, the Council's external auditor is Grant Thornton. The external auditor undertakes a range of audits.

4. For 2013/14, the External Auditors undertook work to certify council grant claims and returns totalling £110m. Their grant claims certification letter on that work is attached as an Appendix. The letter outlines issues arising from their work and makes a couple of recommendations for the Council's grant claiming processes.

5. Auditors are required to conduct their work in accordance with instructions agreed with the grant awarding department or body and, subject to any permitted discretion, to issue qualifications where the strict grant conditions are not met. The vast majority of qualifications do not result in any withdrawal of grant by the awarding department or body.

Finance

6. Grant charged fees for grant certification work for 2013/14 of £16,418 which is less than the indicative fee as detailed in Appendix C in the Letter. Fees for schemes no longer requiring certification (such as the national non-domestic rates return) have been removed. The fees for certification of housing benefit subsidy claims have been reduced by 12 per cent, to reflect the removal of council tax benefit from the scheme. The certification of the Teachers Pension return for 2013-14 is now outside the scope of the Audit Commission regime. It is now subject to a separate engagement letter and fee of £6,500.

Law

7. Legislation appertaining to Local Authority Audit and Accounts is contained in the Local Government Act 1999, the Audit Commission Act, 1998, and regulations made therein.

<u>Equality Impact</u>

8. A number of the grants that the Council receives are for activities benefiting children and young and disadvantaged sections of the community.

<u>Recommendation</u>

9. That Members note and comment on the External Auditor's Letter on the Certification of Claims and Returns for 2013/14 which is attached to this report.

……………………………. …

Iain Newman
Chief Officer Finance and Legal Services

Contact Officer:	Jan Szczechowski Telephone: 01384 814805 Email: jan.szczechowski@dudley.gov.uk

List of Background Papers
Certification of claims and returns letter for 2013/14

Attachment

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5th January 2015

Dear Iain

Certification work for Dudley Metropolitan Borough Council for year ended 31 March 2014

We are required to certify certain claims and returns submitted by Dudley Metropolitan Borough Council ('the Council'). This certification typically takes place six to nine months after the claim period and represents a final but important part of the process to confirm the Council's entitlement to funding.

Arrangements for certification are prescribed by the Audit Commission, which agrees the scope of the work with each relevant government department or agency, and issues auditors with a Certification Instruction (CI) for each specific claim or return.

We have certified two claim for the financial year 2013/14(4 in 2012/13) relating to expenditure of £110.1million. Further details of the claims certified are set out in Appendix A.

There are no issues arising from our certification work which we wish to highlight for your attention. We are satisfied that the Council has appropriate arrangements to compile complete, accurate and timely claims/returns for audit certification.

The indicative fee for 2013/14 for the Council is based on the final 2011/12 certification fees, reflecting the amount of work required by the auditor to certify the claims and returns in that year. Fees for schemes no longer requiring certification (such as the national non-domestic rates return) have been removed. The fees for certification of housing benefit subsidy claims have been reduced by 12 per cent, to reflect the removal of council tax benefit from the scheme. The indicative scale fee set by the Audit Commission for the Council for 2013/14 is £16,418. This is set out in more detail in Appendix B.

Yours sincerely

Grant Thornton UK LLP

Appendix A - Details of claims and returns certified for 2013/14

Claim or return	Value	Amended?	Amendment	Qualified?	Comments
Housing benefits subsidy claim	£100,911,929	No	n/a	Yes	The claim was qualified because of a range of error found in the calculation and classification of benefit payments on the form. The Council has estimated that these should not have a signification impact on the total amount of subsidy but this will not be confirmed until the Department of Work and Pensions considers the qualifications. There were similar findings in respect of previous claim. Work completed was reported by 28 November 2014 as required by the certification instruction.
Pooling of housing capital receipts	£9,255,290	No	n/a	No	None

Appendix B: Fees for 2013/14 certification work

Claim or return	2012/13 fee (£)	2013/14 indicative fee (£)	2013/14 actual fee (£)	Variance (£)	Explanation for variances
Housing benefits subsidy claim.	19,928	15,387	15,387	0	The scale fee is based on the work required to certify the 2011-12 claim. The level of work required in 2013-14, based on the error rate in the claim, was the same as in 2011-12. Therefore no variation is proposed to the scale fee.
National non-domestic rates return	6,440	0	0	0	No requirement to certify this return in 2013/14
Pooling of capital receipts	1,180	3,956	1,031	(2,925)	We are only required to undertake detailed (Part B) testing every 3 years unless we identify the claim as high risk. We did not find any significant issues in 2011/12, when we undertook this testing. We therefore considered the claim to be low risk.
Teachers Pensions	6,600	0	0	0	The Teachers Pensions Agency have required certification of this return for 2013-14 but it is outside the scope of the Audit Commission regime. It is subject to a separate engagement letter and fee.
Local Transport plan (Brierly Hill Sustainable Access and Burnt Tree)	0	1,884	0	(1,884)	Certification of these claims was not required in 2013/14 as the amounts claimed were below the minimum value for certification.
Total	34,148	21,227	16,418	(4,809)	

Dudley Metropolitan Borough Council

Agenda Item No. 7

Note:

It is important to note that the Treasury Strategy Statement is adopted by the Council, based upon advice from its external Treasury advisors, and accordingly the Strategy is tailored to meet the specific and unique needs of the Council. All financial information contained within this Report and Statement should not be used by any individual or organisation as a basis for making investment or borrowing decisions. The Council and its Treasury advisors will not accept any liability on behalf of any individual or organisation that seeks to act on the financial information contained within this Report and Statement.

Audit and Standards Committee – 10th February 2015

Report of the Chief Officer Finance and Legal Services

Treasury Management

Purpose of Report

1. The purpose of this report is:

   - to outline treasury activity in the year 2014/15 up to the end of December;
   - to seek approval of the Treasury Strategy Statement 2015/16

Background

2. Treasury Management entails the management of the Council's cash flows, its borrowings and investments, the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks

3. The Council undertakes treasury management activity on its own behalf and as administering authority for the West Midlands Debt Administration Fund (WMDAF). We are responsible for administering capital funding of £755m on our own account and another £170m on behalf of other West Midlands councils in respect of the WMDAF. The treasury function is governed by the Council's Treasury Policy Statement and Treasury Management Practices.

4. Our borrowing and investment activities in the current year have been undertaken in the context of historically low interest rates. The Bank Rate has remained at 0.5% since March 2009 and is likely to remain at this rate into 2015-16 and rise gradually in the second half of 2015-16.

Treasury Activity 2014/15 - Dudley fund

5. Treasury activities in the current year have been undertaken in the context of the Treasury Strategy Statement 2014/15 approved by Audit Committee and Full Council in February 2014. In that document we anticipated that long term borrowing would be required in the next 12 months due to cashflow need.

6. Our investments up to early January have averaged £14.64 million (with significant day to day variation as a result of cash flow). The average return on these investments was 0.73% (excluding the long term investment with Salford City Council, the average return was 0.38%). All investments were placed with institutions that satisfied the criteria for credit-worthiness set out in the Treasury Strategy Statement 2014/15. The performance of our investments is largely dependent on movements in short-term (up to one year) rates. The average 7-day LIBID1 for the year to the end of December has been 0.43%. Our investment activity for 2014/15 (to date) is set out in more detail in **Appendix 1**.

7. The returns outlined above have been achieved without compromising on the security of the Council's investments. We have maintained and continue to maintain an approved investment list that sets the highest rating standards. We have an account with the Government's Debt Management Office which provides maximum security but low returns. We are only using this account where we cannot place funds with a bank that meets our strict criteria. The majority of short-term investments are in variable rate call accounts with approved counterparties, which offer a relatively good rate of return compared to fixed term deposit accounts as well as greater liquidity.

8. The average value of long-term borrowings up to the end of December 2014 was £535.2 million. The average rate of interest on these borrowings was 4.09% and they were due to mature on dates ranging from the current year to 2061.

9. The rate for a 50-year loan from the Public Works Loan Board (PWLB) has fluctuated during 2014-15 from 3.46% to 4.48% and was standing at 3.46% in early January. The Council is eligible to apply for certainty rates at 0.2% below these rates, introduced in 2012, for local authorities who provided the required information on their plans for long-term borrowing and associated capital spending. In addition the "Project Rate" which is set at 0.4% below standard rate, is available for approved single projects identified by Local Enterprise Partnerships (LEPs).

10. It has not as yet been necessary to undertake any new long-term borrowing due to favourable cash flow, but we are monitoring interest rates and cash flow closely. Medium term cash flow forecasts indicate an underlying requirement to borrow in 2015-16.

11. The Council has used short term borrowing on 22 occasions in the year to date to manage daily cash flow. The average value of the borrowing has been for £3.8m at an average rate of 0.40% for an average duration of 11 days. Daily cash balances have been mainly managed through the use of call accounts.

[1] 7-day LIBID is a measure of the average return from a 7-day investment on the London money market.

Treasury activity 2014/15 - WMDAF

12. Having consulted with our advisors at Arlingclose, we did not identify any opportunities to improve our position by restructuring of debt. The Council has used short term borrowing on 4 occasions in the year to date to manage daily cash flow for the WMADF. The average value of the borrowing has been £2.5m at an average rate of 0.44% for an average duration of 73 days. The latest estimate of interest payable by members of the WMDAF in 2014/15 is 6.4%.

Review of Investment Strategy

13. The Treasury Management Report to Audit & Standards Committee in September 2014 detailed amendments to the 2014-15 Investment Strategy which were made as a result of the Financial Services (Banking Reform) Act 2013. The legislation restricts the level of financial assistance that the UK Government can provide to a bank which gets into financial trouble, and in a serious failure there is a risk that a local authority could lose some or all of its investments with a failing institution (but this is very unlikely for a bank of very high credit quality). In order to mitigate this slightly increased risk, the amendments to the 2014-15 investment strategy essentially tightened up the Council's criteria for making investments. These amendments have been incorporated into the Treasury Strategy Statement 2015/16.

Treasury Strategy Statement 2015/16

14. The Treasury Strategy Statement covers our latest capital funding requirements, our view of interest rate movements and our strategy for borrowing and investment in the light of that view. As such, it needs to be reviewed annually. The proposed Treasury Strategy Statement for 2015/16 is attached as **Appendix 2.**

15. Our expectations for interest rates over the next twelve months, which will be subject to continuous review with our treasury advisors, are as follows (standard PWLB rates are generally about 1% above Government gilts while certainty rates are about 0.8% above gilts):

- **Short-term rates**. The Bank Rate will remain at 0.5% through 2014/15 and probably until the third quarter of 2015/16, rising very gradually thereafter
- **Long-term rates**. 20-year Government gilt rates will rise in 2015/16 from 2.95% to 3.20%
- **Very long- term rates**. 50-year Government gilt rates will rise in 2014/15 from 3.05% to 3.25%

16. The Local Government Act 2003 introduced a system of "prudential borrowing" allowing councils to set their own borrowing limits subject to criteria of prudence and affordability. These criteria are set out in more detail in the Chartered Institute of Public Finance & Accountancy (CIPFA) Prudential Code which specifically requires us to set a number of prudential indicators. The proposed indicators that relate to treasury management are set out in the Treasury Strategy Statement.

Local Government Association Bond Agency

17. The Local Capital Finance Company was established in 2014 by the Local Government Association (LGA) as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. The complexities associated with this source of borrowing, make it currently unsuitable for the Council anticipated borrowing needs for 2015-16 (paragraph 9.5 of Appendix 2)

Public Works Loans Board

18. The Department of Communities and Local Government has now confirmed that HM Treasury (HMT) are taking the steps to abolish the Public Works Loan Board (PWLB) in the coming months. HMT have stressed that this is purely to address the governance of the PWLB and that it will have no impact on existing loans or the government's policy on local authority borrowing. HMT has confirmed that its lending function will continue unaffected albeit under a different body so that local authorities will continue to access borrowing at rates which offer 'good value for money'.

Whilst it is not yet clear what the new governance arrangements will be, a consultation on the restructure is due out shortly.

19. In order to protect the Council's position if an individual or organisation were to act upon the views expressed in this report, we have deemed it necessary to produce a disclaimer which is shown as a note at the head of the report and **Appendix 2**.

Finance

20. Forecasts of performance against budget for treasury management activities are highly sensitive to movements in cash flow and interest rates.

Law

21. The Council has adopted CIPFA's Treasury Management in the Public Services : Code of Practice 2011 which requires the Council to approve a treasury management strategy before the start of the financial year and provide a mid-year update on treasury management activity. In addition, the Department for Communities and Local Government (DCLG) issued revised Guidance on Local Authority Investments in 2010 that required the Council to approve an investment strategy before the start of each financial year. This report fulfils the legal obligation under the Local Government 2003 to have regard to both the CIPFA code and the DCLG guidance.

Equality Impact

22. The treasury management activities considered in this report have no direct impact on issues of equality.

Recommendation

23. That the Committee:

- notes the treasury activities in 2014/15 outlined in this report;
- approves the Treasury Strategy 2015/16 attached as Appendix 2;
- authorises the Chief Officer Finance and Legal Services to effect such borrowings, repayments and investments as are appropriate and consistent with the approved Treasury Strategy and relevant guidance;
- refers all of the above for approval by full Council at its meeting on 23rd February

…………………………………………..

Iain Newman
Chief Officer Finance and Legal Services

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List of Background Papers

- Treasury Policy Statement, Treasury Management Practices and Schedules to the Treasury Management Practices.
- The Local Government Act 2003
- The Prudential Code for Capital Finance in Local Authorities (CIPFA)
- Guidance on Local Government Investments Issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003
- Code of Practice for Treasury Management in the Public Services (CIPFA)

Appendix 1

Investment Activity 2014/15 to 5th January 2015

Counterparty name	**Number of investments**	**Average value £ million**	**Average rate %**	**Average duration (days)**
Barclays Treasury Direct	5	1.13	0.33	16
Barclays	1	0.39	0.28	22
Debt Management Office	16	1.52	0.25	8
Nationwide Building Society	1	0.51	0.42	31
Bank of Scotland Call Account	NA	4.08	0.40	Call
Santander Call Account	NA	4.19	0.40	Call
HSBC Call Account	NA	2.31	0.32	Call
Salford City Council *	1	0.5	11.25	Matures in 2020

The table above includes investments that commenced during 2013/14 and were due to mature in the current financial year.

* This is a fixed term deposit that was made in 1985 and is due to mature in 2020.

Note:
It is important to note that the Treasury Strategy Statement is adopted by the Council, based on advice from its external Treasury advisors, and accordingly the Strategy is tailored to meet the specific and unique needs of the Council. All financial information contained within this Report and Statement should not be used by any individual or organisation as a basis for making investment or borrowing decisions. The Council and its Treasury advisors will not accept any liability on behalf of any individual or organisation that seeks to act on the financial information contained within this Report and Statement.

DUDLEY METROPOLITAN BOROUGH COUNCIL
TREASURY STRATEGY STATEMENT 2015/16

1.0 Introduction

1.1 This Treasury Strategy Statement details the expected activities of the treasury function in the financial year 2015/16. The suggested strategy is based upon officers' views of interest rates as advised by external advisors, supplemented with leading market forecasts. It should be noted that the use of expert external advisors does not remove the responsibility of Members and officers for treasury management functions and that those functions cannot be delegated to any outside organisation. The strategy covers:

- the current portfolio position
- prudential and treasury indicators
- prospects for interest rates
- temporary investment strategy
- requirements and strategy for long-term borrowing
- debt rescheduling and premature repayment opportunities
- treasury implications of HRA Self Financing

2.0 Current Portfolio Position

2.1 The Council's estimated debt position as at 1st April 2015 is as follows:

	£m
Long-term debt:	
- PWLB fixed rate	534.0
- PWLB variable rate	13.0
- Market fixed rate	6.8
- Market LOBO2	10.0
Short-term debt	11.0
Total debt	**574.8**

2.2 The average rate of interest on the above debt is expected to be 3.97%.

2 Lenders Option Borrowers Option (LOBO). This loan was at a fixed rate of 4.6% until February 2009 after which the rate may be varied at the lender's option. If the lender exercises this option to vary the rate then we, as the borrower, have the option to repay the loan.

2.3 The average level of investments held by the Council during 2014/15 to early January 2015 was £14.64m. Cash flow monitoring indicates that long term borrowing may be required in the next 12 months.

2.4 The Council also administers the debt of the former West Midlands County Council on behalf of the West Midlands districts. The estimated debt position at 1st April 2015 is as follows:

	£m
Long-term debt:	
- PWLB fixed rate	162.6
- Market fixed rate	6.8
- Market LOBO3	10.0
Short-term debt	0.0
Total debt	**179.3**

2.5 The average rate of interest charged to the West Midlands fund is expected to be 6.4%.

3.0 Prudential & Treasury Indicators

3.1 Under the Local Government Act 2003 and the Prudential Code for Capital Finance in Local Authorities, local authority capital spending and its borrowing to fund that spending is limited by what is affordable, prudent and sustainable. The Prudential Code sets out a number of indicators that enable the authority to assess affordability and prudence. The following indicators are relevant for the purposes of setting an integrated treasury management strategy.

3.2 <u>Treasury Indicators in the Prudential Code</u>

3.3 The Prudential Code requires that the total external debt does not exceed the Authorised Limit for external debt and only exceeds the Operational Boundary for external debt temporarily on occasions due to variation in cash flow.

These external debt indicators are intended to ensure that levels of external borrowing are affordable, prudent and sustainable. The authorised limit for external debt is a statutory limit (section 3 of the Local Government Act 2003) that should not be breached under any circumstances. It has been calculated to take account of the Council's capital expenditure and financing plans and allowing for the possibility of unusual cash movements. The operational boundary for external debt has also been calculated with regard to the Council's capital expenditure and financing plans allowing for the most likely, prudent, but not worst case scenario for cash flow. Temporary breaches of the operational boundary, due to variations in cash flow, will not be regarded as significant. Actual external debt represents the closing balance for borrowing and other long-term liabilities.

	2013/14	2014/15 Revised	2015/16 Revised	2016/17 Revised	2017/18
	£m	**£m**	**£m**	**£m**	**£m**
Authorised limit for external debt:					
Borrowing	n/a	904	893	882	860
Other long term liabilities	n/a	37	43	36	30
Total	n/a	**941**	**936**	**918**	**890**
Operational boundary:					
Borrowing	n/a	775	796	800	801
other long term liabilities	n/a	37	43	36	30
Total	n/a	**812**	**839**	**836**	**831**
Actual External Debt:					
Borrowing	735.9	n/a	n/a	n/a	n/a
Other long term liabilities	32.1	n/a	n/a	n/a	n/a
Total	**768.0**	**n/a**	**n/a**	**n/a**	**n/a**

Gross Debt and the Capital Financing Requirement:

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 capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

The Council has met this requirement in 2014/15, and expects to do so in future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3.4 Treasury Indicators in the Treasury Management Code

CIPFA Code of Practice for Treasury Management in the Public Services

The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Services.

Interest rate exposures

These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limit for fixed interest reflects the fact that it is possible to construct a prudent treasury strategy on the basis of using only fixed rate debt and investments, so long as the maturity dates of these debts and investments are reasonably spread. The same does not apply to variable rates where a 100% exposure could lead to significant year on year fluctuations in the cost of debt. The upper limit for variable rate exposure allows for the use of variable rate debt to offset our exposure to changes in short-term rates on our portfolio of investments. This limit reduces over time as our strategy is to gradually reduce our level of investments.

	2014/15	**2015/16**	**2016/17**	**2017/18**
Upper limit for fixed interest rate exposure	100	100	100	100
Upper limit for variable rate exposure	10	10	10	10

Maturity structure of borrowing and investments

The maturity structure of fixed rate borrowing is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

	Upper Limit %	**Lower Limit %**
Under 12 months	10	0
12 months and within 24 months	10	0
24 months and within 5 years	15	0
5 years and within 10 years	25	0
10 years and above	100	40

Upper Limit for total principal sums invested over 364 days

The purpose of the limits for principal sums invested for periods longer than 364 days is to contain the Council's exposure to the possibility of loss that might arise as a result of having to seek early repayment of principal sums invested. On the basis of prudent treasury management the proposed upper limit on principal maturing in any one year for sums invested for over 364 days is £10m.

4.0 Economic Background

4.1 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 the growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansions of Gross Domestic Product (GDP). However, inflationary pressure is benign and is likely to remain low in the short-term, partly due to recent large falls in the oil price. 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.

4.2 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 a 0.25% increase in rates at each of the meetings between August and December 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.

5.0 Credit outlook

5.1 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.

5.2 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.

6.0 Prospects for Interest Rates:

6.1 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%. Arlingclose believes 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. Arlingclose projects gilt yields on an upward path in the medium term (see below).

6.2 Our expectations of interest rates over the next twelve months, which will be subject to continuous review with our treasury advisors, are as follows (standard PWLB rates are generally about 1% above government gilts, whilst certainty rates are about 0.8% above gilts) :

- **Short-term rates**. The Bank Rate will remain at 0.5% through 2014/15 and probably until the third quarter of 2015/16, rising very gradually thereafter
- **Long-term rates**. 20-year Government gilt rates will rise in 2015/16 from 2.95% to 3.20%
- **Very long- term rates**. 50-year Government gilt rates will rise in 2014/15 from 3.05% to 3.25%

6.3 Our overall strategy will be based on the projections above. However, we will maintain flexibility to take account of unexpected variations from our forecast.

7.0 Annual Investment Strategy

7.1 Our investment activities are subject to government guidance issued under Section 15(1) (a) of the Local Government Act 2003. This section of the Treasury Strategy Statement constitutes an “Annual Investment Strategy” produced in accordance with the guidance.

7.2 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. We have a policy of keeping cash balances at minimum levels by maximising the use of internal borrowing to finance capital expenditure. In the current financial year, the Authority’s cash balance has ranged between a high of £35m in May to a deficit of £26m in December. This is substantially lower than last year when the balance ranged from a high of £84m to a low of zero in the same period. This is partly as a result of electing to pay employer’s superannuation contributions in single annual instalment in exchange for a reduction in those contributions. Based on seasonal trends, the level of investments (and therefore the risk) is likely to be significantly lower for the rest of this financial year and into next year.

7.3 In accordance with Investment Guidance issued by the Department of Communities and Local Government (DCLG) and best practice the Council’s primary objective in relation to the investment of public funds remains the security of capital. The liquidity or accessibility of the Council’s investments followed by the yields earned on investments is important but are secondary considerations.

7.4 *Strategy for “specified investments*”

7.4.1 The Council will make use of specified investments (as defined within the terms of the government guidance). These are investments that satisfy the following conditions:

a) The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling.
b) The Council may require that the investment be repaid or redeemed within 12 months of the date on which the investment was made.
c) The making of the investment is not defined as capital expenditure by legislation
d) The investment satisfies either of the following conditions:

I. The investment is made with the UK government, a local authority, a parish council or a community council. or
II. The investment is made with a body or in an investment scheme of high credit quality

7.4.2 For the purpose of this strategy a body or investment scheme is deemed to be of high credit quality if it has minimum short-term ratings of F1 (Fitch), P1 (Moody's), and A1 (Standard and Poors).

7.4.3 In order to reduce risk of loss from a bank default, the Council has also applied the following criteria for investments :

- Investments of a maximum duration of 3 months are permitted with UK institutions which have the highest short term credit rating from all three main credit rating agencies i.e. F1+ (Fitch), A1+ (Standard & Poors), P1 (Moody's)

- Investments of a maximum duration of 1 month are permitted with UK institutions with a minimum short term credit rating of F1 (Fitch), A1 (Standard & Poors), and P1 (Moody's).

7.4.4 Since the financial crisis of 2008, the Council has not allowed investments in non-UK institutions. The existing strategy is based on the implicit assumption that the UK Government would support a failing UK bank. This factor is less relevant in light of the Financial Services (Banking Reform) Act 2013 and proposed regulations. That said, current cash flow predictions do not suggest that there is any compelling need to widen the investment strategy to non-UK institutions and so there is no proposal to change.

7.4.5 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria

7.4.6 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 with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

7.4.7 The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

7.4.8 If conditions in the financial markets worsen during 2015-16 or other factors indicate that increased security of Council funds is required, the Chief Officer Finance and Legal Services may impose tighter restrictions on the type of investments and institutions used by the Council, than those detailed in this strategy.

7.4.9 The Council banks with HSBC. At the current time, it does meet the minimum credit criteria and has the highest credit rating for a UK bank. Even if the credit rating falls below the Council's minimum criteria HSBC will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

7.5 *Strategy for "non-specified investments"*

7.5.1 Non-specified investments are those that do not meet the criteria for a specified investment detailed in 7.4.1 above. The Council does not intend to make any investments denominated in foreign currencies, or any that are defined as capital expenditure by legislation such as company shares. Neither is there an intention to make new long term investments, especially in the light of maximising the length of any investment to 3 months irrespective of its credit quality. Therefore the Council will not place its funds with non-specified investments.

7.6 Liquidity of investments

7.6.1 In determining the maximum period for which investments may be held, we will have regard to our most recent cash-flow forecast. We will not enter into an investment where our cash-flow forecast indicates that, as a result of that investment, we would be forced to borrow money at a later date that we would not otherwise have had to borrow.

7.6.2 The criteria for investments detailed in 7.4.3 will ensure that investments are not made for periods exceeding 3 months thereby ensuring that the Council's cash is readily available for day to day operations, as well as reducing the risk of capital loss.

7.7 Limit on investments with a single institution

7.7.1 In order to limit the Council's exposure to a single default, investments with a single institution or group of banks **should not exceed £5million** at any time. This limit also applies to other local authorities but not to the Debt Management Office which has no upper limit as investments with the UK Government are deemed to be at the lowest level of risk.

8.0 Policy on the Use of Financial Derivatives

8.1 A financial derivative is a contract whose value is based on, or "derived" from, an underlying financial instrument such as a loan. Local authorities have previously been able to make use of financial derivatives embedded into loans and investments, both to reduce interest rate risk (e.g. forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans).

8.2 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). The CIPFA Code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy.

8.3 The Council does not intend to use standalone financial derivatives (such as swaps, forwards, futures and options). Should this position change, the Council may seek to develop a detailed and robust risk management framework governing the use of derivatives, but no change in strategy will be made without full Council approval.

9.0 Requirements and Strategy for Long-Term Borrowing

9.1 The primary factor in determining whether we undertake new long-term borrowing will be cash flow need. We will seek to minimise the time between borrowing and anticipated cash flow need, subject to the need to maintain day to day liquidity.

9.2 Our interest rate expectations (outlined in 6.2) provide a variety of options:

- that short-term variable rates will be good value compared to long-term rates, and are likely to remain so for potentially at least the next couple of years. Best value will therefore be achieved by borrowing short term at variable rates in order to minimise borrowing costs in the short term.

- that the risks intrinsic in the shorter term variable rates are such, when compared to historically relatively low long term fixed funding, which may be achievable in 2015/16, that the Council will maintain a stable, longer term portfolio by drawing longer term fixed rate funding at a marginally higher rate than short term rates.

9.3 Against this background caution will be adopted with the 2015/16 treasury operations. The Chief Officer Finance and Legal Services will monitor the interest rate market and adopt a pragmatic approach to changing circumstances.

Sensitivity of the forecast - The main sensitivities of the forecast are likely to be the two scenarios below. In conjunction with the treasury advisers, we will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- If it were felt that there was a significant risk of a sharp rise in long and short term rates, perhaps arising from a greater than expected increase in world economic activity, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still relatively cheap

- If it were felt that there was a significant risk of a sharp fall in long and short term rates, due to growth rates remaining low or weakening, then long term borrowings will be postponed

9.4 With respect to the West Midlands Debt, variances due to timing differences b etween the maturity profile of the debt and repayments from authorities can be managed by short term borrowing in 2015-16. As a result, we do not anticipate that further long-term borrowing will be needed during 2015/16. We shall take out long term borrowing on West Midlands debt when it is economically advantageous to do so.

Local Government Association Bond Agency

9.5 The Local Capital Finance Company was established in 2014 by the Local Government Association (LGA) 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.

9.6 Due to the nature of the Council's anticipated borrowing requirements, it does not intend to borrow from the LGA Bond Agency in 2015/16.

10.0 Debt Rescheduling and Premature Repayment Opportunities

10.1 We may consider rescheduling or premature repayment with the following aims:

- the generation of cash savings at minimum risk;
- in order to help fulfil the strategy outlined in 8 above;
- in order to enhance the balance of the long-term portfolio (by amending the maturity profile and/or the balance of volatility).

10.2 Any rescheduling or premature repayment will be reported to an appropriate committee at the meeting following its implementation.

11.0 HRA Self Financing

11.1 On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account.

11.2 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 which may be positive or negative. An average of this notional balance will be calculated annually and interest transferred between the General Fund and HRA at an internally determined rate of interest, adjusted for risk.

12.0 Training

12.1 CIPFA's Code of Practice requires the Chief Officer Finance and Legal Services to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Relevant training is provided by Arlingclose to the members of the Audit Committee.

12.2 The Council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Chief Officer Finance and Legal Services will recommend and implement the necessary arrangements.

13.0 Treasury Management Advisors

13.1 The Council uses Arlingclose Ltd as its external treasury management advisers. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

13.2 It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council maintains the quality of the service with its advisors by holding regular meetings and tendering periodically for the provision of treasury management advice

13.3 The Council receives the following services from Arlingclose :

a. Credit advice
b. Investment advice
c. Technical advice
d. Economic & interest rate forecasts
e. Workshops and training events for officers and members