



## **Audit and Standards Committee**

**Thursday 9<sup>th</sup> February, 2017, 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 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 8<sup>th</sup> December, 2016 as a correct record.
5. Grant Thornton Letter: Grant Certification Work 2015/16. (Pages 1-6)
6. Treasury Management. (Pages 7-23)
7. Invitation to become an Opted-in Authority – Public Sector Audit Appointments. (Pages 24-30)
8. To consider any questions from Members to the Chair where two clear days notice has been given to the Monitoring Officer (Council Procedure Rule 11.8).

Under the provisions of Part I of Schedule 12A to the Local Government Act 1972, the Monitoring Officer 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 relating to any individuals under Part I of Schedule 12A to the Local Government Act 1972, as amended.”

**Agenda - Private Session**  
**(Meeting not open to the public and press)**

10. Audit Services Interim Performance Report. (Pages 31-34)
11. Risk Management Strategy. (Pages 35-49)
12. Future Meeting Date – Wednesday 29<sup>th</sup> March 2017



**Chief Executive**

**Dated: 1<sup>st</sup> February, 2017**

**Distribution:**

Councillor P Brothwood (Chair)

Councillors A. Aston; J Baines, S Craigie, J Hill, M Mottram, A Taylor, S Waltho (Vice-Chair), and T Westwood

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- The Democratic Services contact officer for this meeting is Lisa Jury, Telephone 01384 8185240 or E-mail [lisa.jury@dudley.gov.uk](mailto:lisa.jury@dudley.gov.uk)

**Minutes of Audit and Standards Committee**

**Thursday 8<sup>th</sup> December 2016 at 6.00 p.m.**  
**in Committee Room 3, The Council House, Dudley**

**Present:-**

Councillor P Brothwood (Chair)  
Councillor S Waltho (Vice-Chair)  
Councillors, J Baines, C Bayton, S Craigie, J Hill, M Mottram, A Taylor and T Westwood.

**Officers:**

I Newman (Chief Officer Finance and Legal Services) ; S Butcher (Chief Officer People for agenda item no. 11 only); R Cooper (Head of Financial Services); S Denyer (Senior Auditor), A Evans (Auditor), M Granger (Corporate Fraud Manager); S Griffiths (Democratic Services Manager for agenda item no. 6 only), G Harrison (Audit Manager – Central Services); A McCormack (Chief Officer – Transformation and Performance for agenda item no. 10 only), S Norman (Chief Executive for agenda item no. 7 only); T Oakman (Strategic Director People for agenda item no. 11 only); M Spittle (Head of Access and Prevention, for agenda item no. 11 only) and L Jury (Democratic Services Officer).

**Also in Attendance:-**

S Joberns and T Tobin (Grant Thornton)

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24     **Declarations of Interest**

No member made a declaration of interest in accordance with the Members' Code of Conduct.

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25     **Minutes**

**Resolved**

That the minutes of the meeting held on 20<sup>th</sup> September, 2016, be approved as a correct record and signed.

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26     **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. 9, 11, 10, 7, 6, 5, 8, and 12.

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### 27 **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) and that in all the circumstances, the public interest in disclosing the information is outweighed by the public interest in maintaining the exception from disclosure.

<u>Description of Item</u>	<u>Relevant Paragraphs of Part 1 of Schedule 12A of the Local Government Act 1972</u>
Annual Audit Report in relation to the Place Directorate.	2 and 7
Suspension under the Provisions of the Employee Improvement and Disciplinary Procedure	2 and 7

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### 28 **Annual Audit Report in relation to the People Directorate**

A report of the Chief Officer Finance and Legal Services was submitted on the audit work undertaken in the People Directorate for the financial year 2015/16 and incorporating more important findings in Appendices 3 and 4 of the report submitted.

During the presentation the Audit Manager made reference to 2015/16 being the first year of the operation of the new Directorate, bringing together Children, Adult and other services of the Council under a new Strategic Director, who had been appointed the previous year. It was noted early on by the new Director, the need for some major improvements in Children's Services, which had later been reinforced by OFSTED. Recently a Children's Commissioner had been appointed and a follow-up visit had been undertaken by OFSTED in October which had given a more positive message about progress to improve. However, it must be acknowledged that at the time the 2015/16 audits were carried out, Children's Services particularly, were under immense pressure.

The Audit Manager, outlined the number of reviews undertaken and the number of recommendations noting that 43 were classified as high priority and 20 recommendations had been unimplemented from the previous review. It was also reported that 28 school audits had been undertaken and of the 396 recommendations made, 18 were high priority, with 77 recommendations unimplemented from the previous year. It was noted that Audit follow up all high priority recommendations approximately 6 months after the issue of the final report and although this review identified a number of recommendations still unimplemented, it was evident that action was being taken.

The percentage of final reports issued within 6 weeks of the date of issue of the draft report was 25% which was significantly below the 76% achieved last year and way below the Committee's target of 80%.

The Audit Manager made specific reference to paragraph 9 of the report in relation to the assurance rating given to Adult Social Care Funding and Looked After Children and the reasons for the rating. It was noted that Audit were currently undertaking a review of these two areas and initial indications suggested that progress was being made, however, a lot of work was still required to fully implement the recommendations.

Referring to the high number of unimplemented recommendations detailed in the Emergency Planning audit, it was noted that new management are now responsible for Emergency Planning who acknowledged the issues raised and a recent follow-up review had found that good progress had been made on implementing the recommendations.

Concluding, the Audit Manager outlined the information included in the Appendices to the report submitted, making specific reference to Appendix 3, clarifying that the Management Response, as indicated in the appendix, was given at the time of the audit and the Management Action was the current progress made on implementing the recommendations.

In response to the report, the Strategic Director People confirmed that the Directorate was not in an acceptable position and he welcomed the audit and its recommendations. Continuing a detailed account of the findings of the audit were presented, indicating that significant improvements were required but acknowledging that this would take time to implement to ensure that the service was maximising every opportunity within budget restrictions to put things right. The robustness of the audit process within the whole of the People Directorate needed embedding and in conjunction with Audit, this would be monitored on a regular basis, to assess where progress was underway and to address where issues were falling behind.

In conclusion, the Strategic Director commented that his officer team were committed to making audit work and making sure that recommendations from the audit findings would be applied to the Directorate's practices and operating proceedings.

Arising from consideration of the report, members asked questions to which officers gave detailed responses including the number of unimplemented recommendations that had not been actioned; factors relating to the low percentage of reports that had been issued within 6 weeks of the date of issue of the draft reports and a question relating to the Adoption and Fostering Service. In response, it was noted that a new IT system was being considered which would significantly improve communications between all services with the aim of achieving a holistic one-service approach. The Committee were also reassured that a financial assessment review would be undertaken on an annual basis as recommended.

Reference was also made to the remodelling of the Dementia Gateway and the redesign of the transport which had enabled the second Dementia Gateway to remain open and ensuring that transport was of the highest standard.

Concerns were expressed at the timescales given to complete follow-up reviews for recommendations and a detailed explanation of the follow-up process was reported.

It was reported that improvements to all systems within the Directorate were required to achieve better compliance and the Strategic Director assured the Committee that the Directorate would do its utmost to improve and achieve the expected standards.

### **Resolved**

That, the information contained in the report and Appendices to the report submitted in respect of the 2015/16 audit work undertaken in the Directorate of People, be accepted.

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### **Suspensions under the provisions of the Employee Improvement and Disciplinary Procedure**

A report of the Chief Officer Transformation and Performance was submitted informing the Committee of the number of employees who were suspended pending investigations into allegations of gross misconduct during the period 1<sup>st</sup> October 2015 to 30<sup>th</sup> September 2016.

During the presentation, the Chief Officer Transformation and Performance made specific reference to paragraph 9 of the report which set out the statistics for disciplinary suspensions for the period 1<sup>st</sup> October 2015 to 30<sup>th</sup> September 2016 noting that 11 suspensions had been invoked, 10 of which had been resolved with 1 still on-going.

It was reported that the average length of a suspension had been 80 days, although 1 case had been on-going significantly longer and the details of the case were presented to the Committee.

Concluding, the Chief Officer Transformation and Performance reported on the number of employees who were suspended who subsequently presented as sick.

Arising from consideration of the report, a discussion took place in relation to employees presenting as sick whilst on suspension and in response, the Chief Officer Transformation and Performance agreed to report back to the Committee the sickness taken in relation to the suspensions and format the tabulation to reflect these figures in future reports.

Referring to disciplinary cases where possible criminal charges may be given, and why hearings could not be scheduled whilst criminal proceedings were still outstanding, the Chief Officer Transformation and Performance agreed to seek clarification on this issue from Legal Services and report back to the Committee.

In response to a question raised regarding six cases referred to in the report submitted, that had been carried over from last year and how long they had taken to conclude or whether they were still on-going, the Chief Officer Transformation and Performance agreed to report the information to the Committee and ensure that information relating to cases carried over from one year to the next, were included in future reports.

Referring to the number of disciplinary cases involving safeguarding allegations and the number in Dudley in comparison to other Authorities, the Chief Officer Transformation and Performance agreed to undertake a benchmarking exercise with neighbouring authorities and report back to Committee.

## **Resolved**

- (1) That, the information contained in the report submitted in respect of suspensions under the provisions of the Employees Improvement and Disciplinary Procedure or relevant Schools Disciplinary Procedure, be noted.
- (2) That, the Chief Officer Transformation and Performance agreed to undertaken the following:
  - report back to the Committee the number of employees on sick leave whilst on suspension and format the tabulation to reflect these figures in future reports to provide more accurate data;
  - seek clarification from Legal Services on why disciplinary cases could not be heard until criminal proceedings had been concluded;
  - report back to Committee the conclusion of cases carried forward from last year and include this information in future reports;

- undertake a benchmarking exercise with neighbouring authorities in relation to the number of disciplinary/suspensions relating to safeguarding allegations.

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## 30 **Risk Management Report**

A report of the Chief Officer Finance and Legal was submitted updating members on current corporate risks and other matters relating to risk management. Appendix 1 to the report, showed details of Corporate Risks which were generally acknowledged as being the most significant facing the Council; impacting upon at least one or several of the Council's key objectives. In addition to risks shown in Appendix 1, the Committee were requested to identify any particular risk for closer scrutiny the next time a risk report was scheduled.

In presenting the report, the Chief Officer Finance and Legal reported that the Committee requested it should receive details of Corporate Risks three times per annum and at its previous meeting, the Committee agreed to scrutinise risk R.82 which related to Corporate Reorganisation.

The Chief Executive was then invited to present the risk to the Committee.

The Chief Executive reported on the risks associated with the corporate reorganisation that had taken place in the authority since her appointment in 2015 and Dudley's bold decision to implement a much leaner senior management structure. It was acknowledged that restructuring of this nature would always be associated with risks as it created instability and uncertainty in staff. However, it was important to realise that it had also created opportunities for the Council to look at implementing new ideas, review roles and save funds. Two particular areas of mitigation referred to in the risk register around staff engagement and culture change were highlighted and it was noted that a further review of the new senior management structure had already been undertaken on the departure of the Strategic Director Resources and Transformation.

Referring to staff engagement and culture change, the Chief Executive then highlighted activities that had been undertaken, which included; the launch of the Working for Dudley Plan 2016-19; the launch of the values and behaviors framework; the bi-monthly leadership forums, and the bi-monthly express briefings which were accessible to all staff. A mini-policy review on attendance management had also been undertaken to ensure that a robust and consistent approach was being given to managing attendance and reducing sickness absence where appropriate to do so and as a result, a reduction in short-term absence had been noted. Performance reviews of all staff were being undertaken annually and recorded and a review of the PRD process had been carried out to make it more effective and a further review of the process would be undertaken. Reference was also made to a new information system, referred to as the PIMS Project, that would ensure that a strong information management system was in place across the Council which joined up Finance and HR to provide accurate information relating to staff and enabling the development of a more automated system that would reduce requirements on staff time.

Concluding, the Chief Executive reported that Corporate Board had discussed the restructuring at its meeting in November and felt that the new senior management structure was now embedded in the organisation and therefore, the risk around restructuring had now receded, and that this specific risk would be removed from the Corporate Risk register in the new year, however members could be assured that the management structure within the authority would be continually reviewed to ensure that the right structure was in place .

Arising from consideration given to the presentation, the Chief Executive responded to questions raised by the Committee including a question raised by the Chair in relation to the capacity of time spent by the Chief Executive and Senior Directors on work for the Combined Authority. In response, it was acknowledged that the combined authority did require some capacity, however, it was noted that the additional work being undertaken included issues that Dudley should be focusing on including, the metro, enterprise zones, the mental health commission, regeneration and land reclamation. The Chief Executive assured members that the situation was regularly reviewed to ensure that focus was being given to key strategic issues whilst ensuring that day-to-day operational issues were being dealt with, which including Councillor contact.

In response to a question raised relating to attendance management, the Chief Executive agreed to provide the Committee with information relating to the improvement in attendance figures.

Following a brief discussion, members of the Committee suggested that R14 relating to Equal Pay Settlements be the particular risk identified for closer scrutiny the next time a risk report was presented to this Committee.

### **Resolved**

- (1) That, the information contained in the report and Appendix 1 to the report submitted on corporate risks appearing at the highest level on the Council's risk register, be noted.
- (2) That, the information contained in the presentation on R82 associated with Corporate Reorganisation, be noted.
- (3) That, the risk R14 in relation to Equal Pay Settlements, be the particular risk identified for closer scrutiny the next time a risk report was referred for consideration by the Committee.
- (4) That the Chief Executive report back to the Committee on information relating to the improvement in short-term sickness levels, which had been included in the most recent quarterly performance report that had been submitted to Overview and Scrutiny Management Board.

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**Annual Report of the Committee on Standards in Public Life**

A report of the Monitoring Officer was submitted on the annual report of the Committee on Standards in Public Life for 215/16.

Presenting the report, the Democratic Services Manager stated that the report submitted summarized the issues the Committee had reviewed nationally, with a focus on the functions of this Committee.

Reference was made to Dudley's Code of Conduct where the seven Principles of Public Life, referred to in the annual report, were reflected. An overview of the activities of the Committee that had been reviewed this year and those proposed for review next year were highlighted and specific reference was made to the Local Government Ethical Standards, as referred to in paragraph 6 of the report.

Consideration had been given to the adoption of a mandatory code nationally and that the role of the Independent Persons appointed in line with the Localism Act, be reviewed. Evidence however from the Committee, suggested that the Independent Persons had reduced the number of vexatious claims made on the code of conduct, noting that this also reflected Dudley's position. Reference was also made to the effectiveness of sanctions and promoting the 7 principles as a guide.

Concluding, the Democratic Services Manager reported that should any issues arise that would require the authority to review its own local standard arrangements; such issues would be brought to this Committee for consideration.

**Resolved**

That the Annual Report of the Committee on Standards in Public Life 2015/16, be noted.

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**Grant Thornton Annual Letter 2015/16**

A joint report of the Chief Executive and the Chief Officer Finance and Legal was submitted in respect of the Council's External Auditor's (Grant Thornton UK LLP) Annual Audit letter for 2015/16 together with the External Auditor's briefing to the Council on the authority's and auditor's responsibilities in respect of the authority's financial position.

At this juncture, before inviting Ms Jobens to present the External Auditor's briefing to the Committee, the Chief Officer Finance and Legal informed the Committee that Ms Jobens would be leaving Grant Thornton and that this would be her last Committee. Thanks were expressed to Ms Jobens on her work for the authority and Mr T Tobin was introduced to the Committee as the new Audit Manager.

In presenting the report, Ms Jobens reported that the Letter attached as Appendix 1, highlighted the conclusions set out in the Audit Findings Report that were presented to the Committee on 20<sup>th</sup> September, 2016, and which had resulted in the auditor issuing an unqualified opinion on the Council's financial statements. A qualified 'except for' value for money conclusion had also be given based around OFSTED's inspection of Children's Services and the gaps in the medium term financial strategy.

It was noted that work had been completed on the Whole of the Government Accounts (WGA) and the accounts had been closed by a financial certificate being issued. Outstanding work on Housing Benefits had now been completed and this would be reported to Committee at its meeting in February 2017.

Mention was made of the potential Section 24 recommendation around the medium term financial strategy that was discussed at the Committee meeting held in September this year. It was noted that the External Auditors had been pleased with the response they had received from this Committee and Officers in relation to the action being taken to try and close the financial gap, particularly with the draft medium term financial strategy, and felt that it would be inappropriate at this point to issue the written recommendation due to the action the Council were already undertaking.

Concluding, Ms Jobens expressed thanks to the Committee, Finance and Internal Audit for the support she had received over many years as the Council's External Auditor.

Arising from consideration of the presentation, the Chair reminded the Committee that although the External Auditors had not issued the Section 24 at this point, the Authority needed to be mindful that there were still many tough decisions to be made to ensure that an appropriate and sustainable budget was set.

### **Resolved**

That the information contained in the report, and Appendix 1 to the report, submitted on the Annual Audit Letter 2015/16, be noted.

The meeting ended at 7.15pm.

CHAIR

**Audit and Standards Committee – 9th February 2017**

**Report of the Chief Officer Finance and Legal Services**

**Grant Thornton Letter: Grant Certification Work 2015/16**

**Purpose of Report**

1. The External Auditor's Letter on Certification of Claims and Returns for 2015/16 is attached and representatives from Grant Thornton will be available at the meeting to deal with any issues.

**Background**

2. For 2015/16, the External Auditors undertook work to certify council grant claims and returns totalling £96.5m. Their grant claims certification letter on that work is attached as an Appendix A. The letter outlines issues arising from their work.
3. 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**

4. Fees charged by Grant Thornton in relation to the Housing Benefits and other grants are detailed within Appendix B and C of this report. They total £27,500 and are funded from within the Chief Executives budget.

**Law**

5. Legislation appertaining to Local Authority Audit and Accounts is contained in the Local Audit and Accountability Act 2014 and regulations made therein.

## **Equality Impact**

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

## **Recommendation**

7. That Members note and comment on the External Auditor's Letter on the Certification of Claims and Returns for 2015/16 which is attached to this report.



**Iain Newman**  
**Chief Officer Finance and Legal Services**

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## **List of Background Papers**

Certification of claims and returns letter for 2015/16



# Grant Thornton

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11th January 2017

Dear Iain

## **Certification work for Dudley Metropolitan Borough Council for year ended 31 March 2016**

We are required to certify the Housing Benefit subsidy claim 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.

The Local Audit and Accountability Act 2014 gave the Secretary of State power to transfer Audit Commission responsibilities to other bodies. Public Sector Audit Appointments (PSAA) have taken on the transitional responsibilities for HB COUNT issued by the Audit Commission in February 2015

We have certified the Housing Benefit subsidy claim for the financial year 2015/16 relating to expenditure of £96.5 million. 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. The type and number of errors identified are in line with what we would expect to see at a local authority processing a large number of complex transactions. We are satisfied that the Council has appropriate arrangements to compile complete, accurate and timely claims for audit certification.

The indicative fee for 2015/16 for the Council is based on the final 2013/14 certification fees, reflecting the amount of work required by the auditor to certify the Housing Benefit subsidy claim that year. The indicative scale fee set by the Audit Commission for the Council for 2015/16 is £11,540. However more audit work was required in 2015/16 than in the base year. As a consequence of this we have proposed a revised fee of £15,000. This fee should not be considered final until confirmation from the PSAA. This is set out in more detail in Appendix B.

Yours sincerely

For Grant Thornton UK LLP

**Appendix A - Details of claims and returns certified for 2015/16**

<b>Claim or return</b>	<b>Value</b>	<b>Amended?</b>	<b>Amendment (£)</b>	<b>Qualified?</b>	<b>Comments</b>
Housing benefits subsidy claim	96,531,428	Yes	246	Y	The claim was amended and qualified because of a range of errors 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.

**Appendix B: Fees for 2015/16 certification work**

<b>Claim or return</b>	<b>2013/14 fee (£)</b>	<b>2014/15 fee (£)</b>	<b>2015/16 indicative fee (£)</b>	<b>2015/16 actual fee (£)</b>	<b>Variance (£)</b>	<b>Explanation for variances</b>
Housing benefits subsidy claim (BEN01)	15,387	15,350	11,540	15,000	-350	The indicative fee for 2015/16 was based on the level of work in 2013/14 with a 25% reduction. Additional work, over and above that undertaken in 2013/14, was required for 2015/16.
<b>Total</b>	15,387	15,350	11,540	15,000		

## Appendix C-Summary of other claims audited by Grant Thornton in 2015/16

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Claim or return	2013/14 fee (£)	2014/15 fee (£)	2015/16 actual fee (£)	Variance (£)	Explanation for variances
Pooling of Capital Receipts	1,031*	3,500	3,500	0	From 14/5 this claim was subject to updated certification instructions which increased the level of testing required.
Teachers' Pensions	6,000	6,000	4,500	(1,500)	Reduction due to improvement in the compilation of the claim and supporting working
Homes & Community Agency (HCA) – The Walk	N/A	N/A	4,500	4,500	New claim requiring independent certification.
<b>Total</b>	<b>7,031</b>	<b>9,500</b>	<b>12,500</b>	<b>3,000</b>	

**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 – 9th February 2017**

**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 2016/17 up to the end of December;
  - to seek approval of the Treasury Strategy Statement 2017/18

**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 £763m on our own account and another £152m 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 Base Rate dropped to 0.25% in August and is likely to remain at this rate in the medium term.

## Treasury Activity 2016/17 - Dudley fund

5. Treasury activities in the current year have been undertaken in the context of the Treasury Strategy Statement 2016/17 approved by Audit Committee and Full Council in February 2016. 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 £28.7M (with significant day to day variation as a result of cash flow). The average return on these investments was 0.44% (excluding the long term investment with Salford City Council, the average return was 0.25%). All investments were placed with institutions that satisfied the criteria for credit-worthiness set out in the Treasury Strategy Statement 2016/17. The performance of our investments is largely dependent on movements in short-term (up to one year) rates which reduced in line with the drop in the bank base rate. The average 7-day LIBID<sup>1</sup> for the year to the end of December has been 0.36%. Our investment activity for 2016/17 (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 2016 was £599.0 million. The average rate of interest on these borrowings was 3.69% 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 2016-17 from 2.07% to 3.28% and was standing at 2.77% in early January. The Council is eligible to apply for "certainty rates" at 0.2% below these rates which is available to local authorities who provide central government with the required information on their plans for long-term borrowing and associated capital spending.
10. The Treasury has published a consultation paper on the new Public Works Loan Board Local Infrastructure Rate (PWLB LIR) first announced during the 2016 Autumn Statement. The government's intention is to support further local authority investment in local infrastructure by permitting £1bn of discounted lending to local authorities at gilts plus 0.60% to support "local infrastructure projects that are high value for money". The rate would be available for a period of three years and would replace the Project Rate that was previously made available via Local Enterprise Partnerships
11. In the current year we have taken out 2 maturity loans with duration of 2 years (The total value of these long term loans is £20m and the average interest is

0.95%). We are monitoring interest rates and cash flow closely and continue to anticipate that further action may be required before the financial year end.

12. It has not been necessary to undertake any short-term borrowing for Dudley in the current year to date.

#### Treasury activity 2016/17 - WMDAF

13. The Council has used short term borrowing on 4 occasions in the year to date to manage daily cash flow for the WMDAF. The average value of the borrowing has been £3.4m at an average rate of 0.37% for an average duration of 73 days. The latest estimate of interest payable by members of the WMDAF in 2017/18 is 6.2%. One investment has been made to date on the WMDAF for £3.0m at a rate of 0.28% for 54 days.

#### Treasury Strategy Statement 2017/18

13. 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 2017/18 is attached as **Appendix 2**.
14. 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 0.25% throughout 2017/18
  - **Long-term rates.** 20-year Government gilt rate is expected to be 1.40% in March and remain around 1.40% throughout 2017/18
  - **Very long- term rates.** 50-year Government gilt rates is expected to be 1.30% in March and remain around 1.30% throughout 2017/18
15. 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.
16. 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**

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

## **Law**

18. 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**

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

## **Recommendation**

20. That the Committee:
- notes the treasury activities in 2016/17 outlined in this report;
  - approves the Treasury Strategy 2017/18 attached as Appendix 2;
  - authorises the Chief Officer (Finance & 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 22nd February



.....  
Iain Newman  
Chief Officer (Finance & Legal Services)

Contact Officer: Amarjit Uppal  
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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)

## Investment Activity 2016/17 to 3 January 2017

Counterparty name	Number of investments	Average value £ million	Average rate %	Average duration (days)
Debt Management Office	68	11.85	0.18	13
Leeds City Council	1	1.98	0.22	122
Highland Council	1	1.73	0.26	124
Bank of Scotland Call Account	NA	4.93	0.26	Call
Santander Call Account	NA	4.55	0.29	Call
HSBC Call Account	NA	3.20	0.24	Call
Salford City Council *	1	0.50	11.25	Matures in 2020

\* 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 2017/18**

### **1.0 Introduction**

1.1 This Treasury Strategy Statement details the expected activities of the treasury function in the financial year 2017/18. 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 2017 is as follows:

	<b>£m</b>
Long-term debt:	
- PWLB fixed rate	539.9
- PWLB variable rate	13.0
- Market fixed rate	26.8
- Market LOBO <sup>2</sup>	10.0
Short-term debt	10.00
<b>Total debt</b>	<b>580.3</b>

2.2 The average rate of interest on the above debt is expected to be 3.69%.

<sup>2</sup> 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 2016/17 to early January 2017 was £28.7m. 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 2017 is as follows:

	<b>£m</b>
Long-term debt:	
- PWLB fixed rate	141.1
- Market fixed rate	6.8
- Market LOBO3	10.0
Short-term debt	0.0
<b>Total debt</b>	<b>157.9</b>

- 2.5 The average rate of interest charged to the West Midlands fund is expected to be 6.2%.

### **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 Treasury Indicators in the Prudential Code**

- 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.
- 3.4 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.

	2015/16	2016/17	2017/18	2018/19	2019/20
		Revised	Revised	Revised	
	£m	£m	£m	£m	£m
Authorised limit for external debt:					
Borrowing	n/a	976	983	937	908
Other long term liabilities	n/a	34	33	29	25
<b>Total</b>	n/a	1,010	1,016	966	933
Operational boundary:					
Borrowing	n/a	802	918	919	849
other long term liabilities	n/a	34	33	29	25
<b>Total</b>	n/a	836	951	948	874
Actual External Debt:					
Borrowing	771	n/a	n/a	n/a	n/a
Other long term liabilities	26	n/a	n/a	n/a	n/a
<b>Total</b>	<b>797</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>

### 3.5 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 2016/17, and expects to do so in future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

### 3.6 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.

### 3.7 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.

	2016/17	2017/18	2018/19	2019/20
Upper limit for fixed interest rate exposure	100	100	100	100
Upper limit for variable rate exposure	10	10	10	10

### 3.8 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

### 3.9 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 The major external influence on the Authority's treasury management strategy for 2017/18 will be the Government's negotiations to leave the EU and the associated uncertainty over future economic prospects.
- 4.2 The fall in sterling and increase in the oil price have driven inflation expectations upwards. The Bank of England is forecasting that Consumer Price Inflation (CPI) will breach its 2% target in 2017, the first time since 2013, but the bank is expected to look through near term inflation overshoots when setting interest rates to avoid derailing the economy, but further monetary loosening is less likely.
- 4.3 Initial post referendum economic data showed that the feared collapse in business and consumer confidence has not immediately led to lower growth but

the prospect of leaving the single market has dented business confidence resulting in delays in business investment which could weaken growth in 2017-18.

- 4.4 The global environment is uncertain, with repercussions for financial market volatility and long term interest rates, however financial markets appear to be expecting stronger global growth, although the potential rise in protectionism could dampen future growth prospects.
- 4.5 The depreciation in sterling will, however, assist the economy to rebalance away from spending and export volumes will increase marginally.

## 5.0 Credit outlook

- 5.1 Markets have expressed concern over the financial viability of a number of European banks recently. Sluggish economies and continuing fines for pre-crisis behaviour have weighed on bank profits, and any future slowdown will exacerbate these concerns.
- 5.2 Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the European Union and the USA, and progressing in Canada and the USA. The credit risk associated with making unsecured bank deposits has therefore increased but returns from cash deposits continue to fall.

## 6.0 Prospects for Interest Rates:

- 6.1 The Authority's treasury adviser Arlingclose's expect the UK Bank Rate to remain at 0.25% during 2017/18. Given the current upward pressure on inflation, further falls in the rate look less likely. There is a low probability of the rate going negative if the UK enters a recession as a result of concerns over leaving the EU.
- 6.2 Gilt yields have risen sharply, but remain at low levels. Arlingclose expect yields to decline when the government triggers article 50. Long term economic fundamentals remain weak and further Quantitative Easing in support of the UK economy in 2017/18 is possible, to keep long term interest rates low
- 6.3 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 0.25% throughout 2017/18
  - **Long-term rates.** 20-year Government gilt rate is expected to be 1.40% in March and remain around 1.40% throughout 2017/18
  - **Very long- term rates.** 50-year Government gilt rates is expected to be 1.30% in March and remain around 1.30% throughout 2017/18
- 6.4 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 minimum of £0.5m in May to a high of £44m early in the year.
- 7.3 Both the CIPFA Code and the Department for Communities and Local Government (DCLG) require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return or yield. The Council’s 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 The Council will be prepared to lend to the West Midlands Combined Authority. Such lending will be as part of arrangements agreed with the Combined Authority and other constituent authorities
- 7.4.3 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).

7.4.4 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).

7.4.5 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.

7.4.6 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

7.4.7 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.

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

7.4.9 If conditions in the financial markets worsen during 2017-18 or other factors indicate that increased security of Council funds is required, the Chief Officer (Finance and Legal) may impose tighter restrictions on the type of investments and institutions used by the Council, than those detailed in this strategy.

7.4.10 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 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's strategy is to maintain borrowing and investments at a minimum (well below their underlying levels) thereby maximising the use of internal borrowing. This keeps borrowing costs lower than they would otherwise be and keeping cash balances low reduces credit risk.

9.3 The balance sheet forecast indicates a requirement to increase the level of external borrowing in the medium and long term. Our interest rate expectations (outlined in 6.2) provide a variety of options on the type of borrowing we will undertake :

- 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 2017/18, 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.

9.4 Against this background caution will be adopted with the 2017/18 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

9.5 With respect to the West Midlands Debt, variances due to timing differences between the maturity profile of the debt and repayments from authorities can be managed by short term borrowing in 2017-18. As a result, we do not anticipate that further long-term borrowing will be needed during 2017-18.

9.6 The approved sources of long-term and short-term borrowing are :

- Public Works Loans Board
- Any institution approved for investments (above)
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except the West Midlands Pension Fund)

In addition capital finance may be raised by finance leases and similar arrangements which may be classed as debt liabilities.

## **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) 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 and other members of the Council.
- 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 & 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

**Audit and Standards Committee – 9<sup>th</sup> February, 2017**

**Report of the Chief Executive and the Chief Officer Finance and Legal Services**

**Invitation to become an Opted-in Authority - Public Sector Audit Appointments**

**Purpose of Report**

1. To seek endorsement of proposals to opt in to the national scheme for auditor appointments.

**Background**

2. The Council's current external auditors, Grant Thornton, have been in place since financial year 2012/13 under national arrangements that were set up following the Government's decision to abolish the Audit Commission. These arrangements cover the financial years up to 2017/18. From 2018/19, the Council has the option to either appoint its own external auditors or to opt in to new national arrangements managed by Public Sector Audit Appointments Ltd (PSAA).
3. If the Council opts to appoint its own external auditors, then it will need to:
  - establish an audit panel with independent members;
  - manage the auditor procurement and cover its costs;
  - monitor the independence of the appointed auditor for the duration of the appointment;
  - deal with the replacement of any auditor if required; and
  - manage the contract with the auditor.
4. PSAA is a not for profit company established by the Local Government Association (LGA). It already has a track record in that it administers audit contracts under the current (mandatory) national arrangements. It has now been specified by the Secretary of State for Communities and Local Government as the appointing person for principal local government bodies. This means that it will be able to make auditor appointments for 2018/19 onwards to principal local government bodies that choose to opt in to the new national arrangements. Further details of the scheme are set out in the invitation to opt in (attached as Appendix 1).
5. It is anticipated that opting into the PSAA arrangements will enable the Council to secure high quality, independent, cost-effective external audit services while avoiding the costs associated with directly managing the contract. It will also give an opportunity to support collaborative working by appointing the same auditor to the Constituent Councils of the Combined Authority and to the Combined Authority itself.

6. The deadline for opting in is 9<sup>th</sup> March 2017. This matter will be considered by Cabinet on 8<sup>th</sup> February 2017 and Cabinet will be asked to make a recommendation to Full Council (27<sup>th</sup> February 2017) to opt in to the national scheme for auditor appointments.

### **Finance**

7. The current cost of external audit, including audit of grants, is approximately £175,000 per year.

### **Law**

8. The Authority is required to comply with Part 3 of the Local Audit and Accountability Act 2014 in relation to the appointment of local auditors. Section 7 of the Act requires the Authority to appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding financial year.

Public Sector Audit Appointments Limited (PSAA) has been specified as an appointing person under the 2014 Act and the Local Audit (Appointing Person) Regulations 2015, and has the power to make auditor appointments for audits of the accounts from 2018/19 on behalf of the Authority.)

### **Equality Impact**

9. There are no equality issues arising from this report.

### **Recommendation**

10. It is recommended that Committee note the contents of this report and endorse the recommendation to Full Council to opt in to the national scheme for auditor appointments.



**Iain Newman**  
**Chief Officer Finance & Legal Services**

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**Sarah Norman**  
**Chief Executive**

### **List of Background Papers**

Appendix 1 – Invitation to opt in to the national scheme for auditor appointments

27 October 2016

**Email:** [appointingperson@psaa.co.uk](mailto:appointingperson@psaa.co.uk)

Sarah Norman  
Dudley Metropolitan Borough Council  
3-5 St James Road  
Dudley West Midlands DY1

Copied to: Iain Newman, Chief Officer - finance and legal services, Dudley Metropolitan  
Borough Council  
Mohammed Farooq, Assistant Director - Law & Governance, Dudley  
Metropolitan Borough Council

Dear Ms Norman

### **Invitation to opt into the national scheme for auditor appointments**

As you know the external auditor for the audit of the accounts for 2018/19 has to be appointed before the end of 2017. That may seem a long way away, but as there is now a choice about how to make that appointment, a decision on your authority's approach will be needed soon.

We are pleased that the Secretary of State has expressed his confidence in us by giving us the role of appointing local auditors under a national scheme. This is one choice open to your authority. We issued a prospectus about the scheme in July 2016, available to download on the [appointing person](#) page of our website, with other information you may find helpful.

The timetable we have outlined for appointing auditors under the scheme means we now need to issue a formal invitation to opt into these arrangements. The covering email provides the formal invitation, along with a form of acceptance of our invitation for you to use if your authority decides to join the national scheme. We believe the case for doing so is compelling. To help with your decision we have prepared the additional information attached to this letter.

I need to highlight two things:

- we need to receive your formal acceptance of this invitation by 9 March 2017; and
- the relevant regulations require that, except for a body that is a corporation sole (a police and crime commissioner), the decision to accept the invitation and to opt in needs to be made by the members of the authority meeting as a whole. We appreciate this will need to be built into your decision making timetable.

If you have any other questions not covered by our information, do not hesitate to contact us by email at [appointingperson@psaa.co.uk](mailto:appointingperson@psaa.co.uk).

Yours sincerely



Jon Hayes, Chief Officer

## Appointing an external auditor

### Information on the national scheme

#### Public Sector Audit Appointments Limited (PSAA)

We are a not-for-profit company established by the Local Government Association (LGA). We administer the current audit contracts, let by the Audit Commission before it closed.

We have the support of the LGA, which has worked to secure the option for principal local government and police bodies to appoint auditors through a dedicated sector-led national procurement body. We have established an advisory panel, drawn from representative groups of local government and police bodies, to give access to your views on the design and operation of the scheme.

#### The national scheme for appointing local auditors

We have been specified by the Secretary of State for Communities and Local Government as the appointing person for principal local government bodies. This means that we will make auditor appointments to principal local government bodies that choose to opt into the national appointment arrangements we will operate for audits of the accounts from 2018/19. These arrangements are sometimes described as the 'sector-led body' option, and our thinking for this scheme was set out in a prospectus circulated to you in July. The prospectus is available on the [appointing person](#) page of our website.

We will appoint an auditor for all opted-in authorities for each of the five financial years beginning from 1 April 2018, unless the Secretary of State chooses to terminate our role as the appointing person beforehand. He or she may only do so after first consulting opted-in authorities and the LGA.

#### What the appointing person scheme will offer

We are committed to making sure the national scheme will be an excellent option for auditor appointments for you.

We intend to run the scheme in a way that will save time and resources for local government bodies. We think that a collective procurement, which we will carry out on behalf of all opted-in authorities, will enable us to secure the best prices, keeping the cost of audit as low as possible for the bodies who choose to opt in, without compromising on audit quality.

Our current role means we have a unique experience and understanding of auditor procurement and the local public audit market.

Using the scheme will avoid the need for you to:

- establish an audit panel with independent members;
- manage your own auditor procurement and cover its costs;
- monitor the independence of your appointed auditor for the duration of the appointment;
- deal with the replacement of any auditor if required; and
- manage the contract with your auditor.

Our scheme will endeavour to appoint the same auditors to other opted-in bodies that are involved in formal collaboration or joint working initiatives, if you consider that a common auditor will enhance efficiency and value for money.

We will also try to be flexible about changing your auditor during the five-year appointing period if there is good reason, for example where new joint working arrangements are put in place.

Securing a high level of acceptances to the opt-in invitation will provide the best opportunity for us to achieve the most competitive prices from audit firms. The LGA has previously sought expressions of interest in the appointing person arrangements, and received positive responses from over 270 relevant authorities. We ultimately hope to achieve participation from the vast majority of eligible authorities.

### **High quality audits**

The Local Audit and Accountability Act 2014 provides that firms must be registered as local public auditors with one of the chartered accountancy institutes acting in the capacity of a Recognised Supervisory Body (RSB). The quality of registered firms' work will be subject to scrutiny by both the RSB and the Financial Reporting Council (FRC), under arrangements set out in the Act.

We will:

- only contract with audit firms that have a proven track record in undertaking public audit work;
- include obligations in relation to maintaining and continuously improving quality in our contract terms and in the quality criteria in our tender evaluation;
- ensure that firms maintain the appropriate registration and will liaise closely with RSBs and the FRC to ensure that any quality concerns are detected at an early stage; and
- take a close interest in your feedback and in the rigour and effectiveness of firms' own quality assurance arrangements.

We will also liaise with the National Audit Office to help ensure that guidance to auditors is updated as necessary.

### **Procurement strategy**

In developing our procurement strategy for the contracts with audit firms, we will have input from the advisory panel we have established. The panel will assist PSAA in developing arrangements for the national scheme, provide feedback to us on proposals as they develop, and helping us maintain effective channels of communication. We think it is particularly important to understand your preferences and priorities, to ensure we develop a strategy that reflects your needs within the constraints set out in legislation and in professional requirements.

In order to secure the best prices we are minded to let audit contracts:

- for 5 years;
- in 2 large contract areas nationally, with 3 or 4 contract lots per area, depending on the number of bodies that opt in; and
- to a number of firms in each contract area to help us manage independence issues.

The value of each contract will depend on the prices bid, with the firms offering the best value being awarded larger amounts of work. By having contracts with a number of firms, we will be able to manage issues of independence and avoid dominance of the market by one or two firms. Limiting the national volume of work available to any one firm will encourage competition and ensure the plurality of provision.

## **Auditor appointments and independence**

Auditors must be independent of the bodies they audit, to enable them to carry out their work with objectivity and credibility, and in a way that commands public confidence.

We plan to take great care to ensure that every auditor appointment passes this test. We will also monitor significant proposals for auditors to carry out consultancy or other non-audit work, to protect the independence of auditor appointments.

We will consult you on the appointment of your auditor, most likely from September 2017. To make the most effective allocation of appointments, it will help us to know about:

- any potential constraints on the appointment of your auditor because of a lack of independence, for example as a result of consultancy work awarded to a particular firm;
- any joint working or collaboration arrangements that you think should influence the appointment; and
- other local factors you think are relevant to making the appointment.

We will ask you for this information after you have opted in.

Auditor appointments for the audit of the accounts of the 2018/19 financial year must be made by 31 December 2017.

## **Fee scales**

We will ensure that fee levels are carefully managed by securing competitive prices from firms and by minimising our own costs. Any surplus funds will be returned to scheme members under our articles of association and our memorandum of understanding with the Department for Communities and Local Government and the LGA.

Our costs for setting up and managing the scheme will need to be covered by audit fees. We expect our annual operating costs will be lower than our current costs because we expect to employ a smaller team to manage the scheme. We are intending to fund an element of the costs of establishing the scheme, including the costs of procuring audit contracts, from local government's share of our current deferred income. We think this is appropriate because the new scheme will be available to all relevant principal local government bodies.

PSAA will pool scheme costs and charge fees to audited bodies in accordance with a fair scale of fees which has regard to size, complexity and audit risk, most likely as evidenced by audit fees for 2016/17. Pooling means that everyone in the scheme will benefit from the most competitive prices. Fees will reflect the number of scheme participants – the greater the level of participation, the better the value represented by our scale fees.

Scale fees will be determined by the prices achieved in the auditor procurement that PSAA will need to undertake during the early part of 2017. Contracts are likely to be awarded at the end of June 2017, and at this point the overall cost and therefore the level of fees required will be clear. We expect to consult on the proposed scale of fees in autumn 2017 and to publish the fees applicable for 2018/19 in March 2018.

## Opting in

The closing date for opting in is 9 March 2017. We have allowed more than the minimum eight week notice period required, because the formal approval process for most eligible bodies, except police and crime commissioners, is a decision made by the members of an authority meeting as a whole.

We will confirm receipt of all opt-in notices. A full list of authorities who opt in will be published on our website. Once we have received an opt-in notice, we will write to you to request information on any joint working arrangements relevant to your auditor appointment, and any potential independence matters that would prevent us appointing a particular firm.

If you decide not to accept the invitation to opt in by the closing date, you may subsequently make a request to opt in, but only after 1 April 2018. The earliest an auditor appointment can be made for authorities that opt in after the closing date is therefore for the audit of the accounts for 2019/20. We are required to consider such requests, and agree to them unless there are reasonable grounds for their refusal.

## Timetable

In summary, we expect the timetable for the new arrangements to be:

- Invitation to opt in issued 27 October 2016
- Closing date for receipt of notices to opt in 9 March 2017
- Contract notice published 20 February 2017
- Award audit contracts By end of June 2017
- Consult on and make auditor appointments By end of December 2017
- Consult on and publish scale fees By end of March 2018

## Enquiries

We publish frequently asked questions on our [website](#). We are keen to receive feedback from local bodies on our plans. Please email your feedback or questions to: [appointingperson@psaa.co.uk](mailto:appointingperson@psaa.co.uk).

If you would like to discuss a particular issue with us, please send an email to the above address, and we will make arrangements either to telephone or meet you.