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Horsham District Council

Audit Committee

Wednesday, 16th December, 2020 at 5.30 pm
via Remote Video Link

Councillors: Stuart Ritchie (Chairman)
John Blackall (Vice-Chairman)
Tony Bevis
Paul Clarke
Ruth Fletcher
Richard Landeryou
Jack Saheid

You are summoned to the meeting to transact the following business

Glen Chipp
Chief Executive

Agenda

Audit Committee
20 OCTOBER 2020

Present: Councillors: Stuart Ritchie (Chairman), John Blackall (Vice-Chairman), Tony Bevis, Paul Clarke, Ruth Fletcher, Richard Landeryou and Jack Saheid

AAG/16 **MINUTES**

The minutes of the meeting held on 15 July were approved as an accurate record and it was agreed that they would be signed by the Chairman once the COVID-19 situation had abated.

AAG/17 **DECLARATIONS OF MEMBERS' INTERESTS**

There were no declarations of interest.

AAG/18 **ANNOUNCEMENTS**

The Chairman informed the Committee that the Annual Statement of Accounts had been audited and brought back to note and approve the changes.

AAG/19 **RISK MANAGEMENT - QUARTERLY UPDATE**

The Director of Corporate Resources presented the Risk Management Quarterly Update to the Committee. The report included an update on the Corporate Risk Register for consideration and provided an update on progress with the quarterly departmental risk register reviews.

There were five High Risks on the corporate risk register with CRR19 being a new risk:

CRR01b - Funding from Government is less generous than assumed in the Medium-Term Financial Strategy (MTFS) from 2021

CRR19 - Ongoing reduction in planning fees; reduced car parking income; increased homelessness; and increased housing benefit claims; leisure centres; property income; investment income.

CRR35 - COVID-19 (i) The Council is unable to deliver statutory front line services to the community due to, for example, staff shortages or unavailability of key officers. (ii) Substantial financial loss to the Council.

CRR01c - Decrease in Rateable Value due to appeals and businesses going under. This may cause the Council to fall below the business rates baseline, resulting in loss of funding.

CRR18 (i) - A malicious attacker exploits a known or unknown security weakness to penetrate the Council's ICT systems. (ii) IT not working due to environmental problems: fire, flood, power cut.

Departmental risk registers had been reviewed and updated.

AAG/20 **INTERNAL AUDIT - QUARTERLY UPDATE REPORT**

The Chief Internal Auditor provided Members with an update on all internal audit and counter-fraud activity completed during the quarter, with a summary of all key findings. There were also updates on the progress of delivery of the annual audit plan and the performance of the internal audit service.

Of the two formal audits finalised during the quarter, one received an opinion of 'reasonable assurance', and the other was a non-opinion review.

Formal follow-up reviews would continue to be carried out for all audits that had received 'minimal assurance' and high risk areas that had received 'partial assurance' opinions.

Internal Audit had continued to liaise with departments to identify any new or emerging risks.

It was reported that the internal audit plan for the year remained under regular review to ensure that the service continues to focus its resources in the highest priority areas based on an assessment of risk. Through discussions with management, the following reviews had been added to the audit plan during the year:

• Review of the Community Hubs – Covid-19 Red Response;
• Purchase Cards, including areas of spend.

Through the same process, audits had been deferred from the audit plan and would be considered for inclusion in the 2021/22 plan as part of the overall risk assessment completed during the annual audit planning process:

• Capitol Bar and Catering Facility;
• Volunteers.

AAG/21 **EXTERNAL AUDIT - AUDIT RESULTS REPORT**

The External Auditors provided a summary of their Audit Results Report for the year ending 31st March 2020 following their Audit Progress report from July 2020.

The External Auditors had substantially completed their audit of Horsham District Council's financial statements and performed the procedures outlined in the Audit planning report.

Subject to satisfactory completion of the following outstanding items the External Auditors expected to issue an unqualified opinion on the Authority's financial statements:

• Completion of subsequent events review;
• Receipt of the response from Those Charged with Governance; and
• Receipt of the signed management representation letter

The Chairman requested that the External Auditors report their property valuation methods in future reports.

AAG/22 **STATEMENT OF ACCOUNTS AND LETTER OF REPRESENTATION**

The Head of Finance summarised the changes made to the Statement of Accounts for the Committee.

RESOLVED

i) That the Audit Committee delegate approval of the 2019/20 Audited Statement of Accounts to the Chairman of the Audit Committee, in consultation with the Director of Corporate Resources, to be completed before 30 November 2020.

ii) That the letter of Representation be agreed by the Audit Committee and signed by the Director of Corporate Resources and the Chairman of the Audit Committee.

AAG/23 **URGENT BUSINESS**

There was no urgent business.

The meeting closed at 6.25 pm having commenced at 5.30 pm

CHAIRMAN

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Report to Audit Committee

16th December 2020

By the Director of Corporate Resources

INFORMATION REPORT

Partially Exempt under Paragraph 5 of Part 1 of Schedule 12A to the Local Government Act 1972

Risk Management ~ Quarterly Report

Executive Summary

This report includes an update on the Corporate Risk Register for consideration and provides an update on progress with the quarterly departmental risk register reviews.

Recommendations

That the Committee is recommended to:

i) Note the contents of this report.

Reasons for Recommendations

As part of good governance, it is important that Members understand the key risks facing the Council.

Background Papers

Corporate Risk Register

Wards affected: All

Contact: Jane Eaton, Director of Corporate Resources, 01403 215300.

Background Information

1 Introduction and Background

1.1 The Audit Committee is charged with responsibility for monitoring the effectiveness of the Council's risk management arrangements.

1.2 The report provides details of key changes to the Council's Corporate Risk Register, and an update on progress regarding the departmental risk registers (see 3.1 and 3.2 below).

2 Relevant Council Policy

2.1 The Council's Risk Management Policy is detailed in the Council's Risk Management Toolkit. The Council's Risk Management Strategy is a component part of the Policy, and this document sets out to achieve the following objectives:

- Fully integrate risk management into the culture of the Council and its strategic and service planning processes;
- Ensure that the risk management framework is understood and that ownership and accountability for managing risks is clearly assigned;
- Ensure the benefits of risk management are realised through maximising opportunities and minimising threats;
- Ensure consistency throughout the Council in the management of risk.

3 Details

3.1 Corporate Risk Register

The Senior Leadership Team has reviewed the Corporate Risk Register and comments have been updated to reflect the current position for each risk (see Appendix 1 and exempt appendix 2).

The Corporate risk profile is shown in the following heat map which shows the total number of risks in each segment. The red / amber / green zones are in accordance with the Council's risk appetite.

	CRR02 CRR03 CRR06 CRR32 CRR33 CRR34 CRR35a	CRR18	CRR01c	CRR35 CRR19
		CRR17 CRR36	CRR01b CRR05	

There are six risks which are currently considered to be high and nine medium.

The high risk area relates to the following:

CRR35	COVID-19 (i) The Council is unable to deliver statutory front line services to the community due to, for example, staff shortages or unavailability of key officers. (ii) Substantial financial loss to the Council.
CRR19	Ongoing reduction in planning fees; reduced car parking income; increased homelessness; and increased housing benefit claims; leisure centres; property income; investment income.
CRR01c	Decrease in Rateable Value due to appeals and businesses going under. This may cause the Council to fall below the business rates baseline, resulting in loss of funding.
CRR18	(i) A malicious attacker exploits a known or unknown security weakness to penetrate the Council's ICT systems. The level of threat has been raised by the Cabinet Office to amber. (ii) IT not working due to environmental problems: fire, flood, power cut.
CRR01b	Funding from Government is less generous than assumed in the Medium Term Financial Strategy (MTFS) from 2021
CRR05	Officers are either unaware of expected controls or do not comply with control procedures.

Please see the risk register in Appendix 1 which provides full details of all risks on the "live" register together with details of the control actions and responsible officers. Two Risks, CRR33 and CRR36 are shown in the exempt appendix 2.

3.2 Departmental Risk Registers

Departmental risk registers have been reviewed and updated.

4 Outcome of Consultations

4.1 Officers who are responsible for control actions and the Senior Leadership Team have been consulted in updating the Corporate Risk Register.

5 Other Courses of Action Considered but Rejected

5.1 Not applicable.

6 Financial Consequences

6.1 There are no financial consequences as this report is for noting.

7 Legal Consequences

7.1 There are no legal consequences as this report is for noting.

8 Staffing Consequences

8.1 There are no staffing consequences as this report is for noting.

9 Risk Assessment

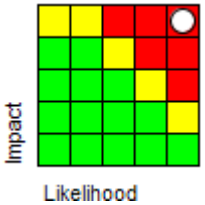
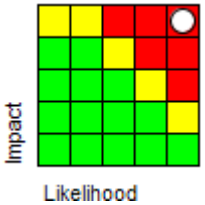
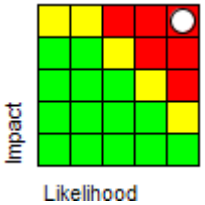
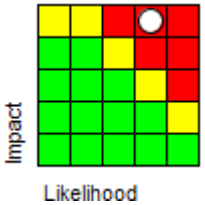
9.1 The report provides an update on the Council's corporate risks and how these are being managed by the Senior Leadership Team. See Appendix 1 for the latest version of the Council's Corporate Risk Register.

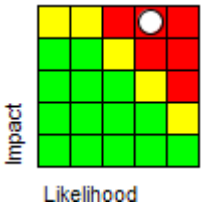
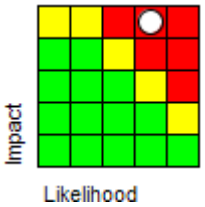
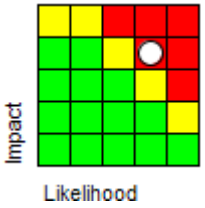
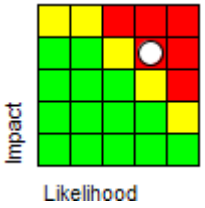
10 Other Considerations

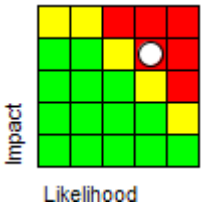
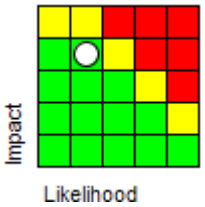
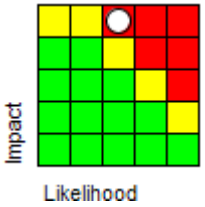
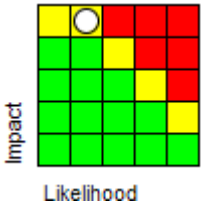
10.1 Risk management encompasses all risks within the organisation, including strategic, operational, and project/change risks. This includes consideration of Crime & Disorder; Human Rights; Equality & Diversity; and Green issues.

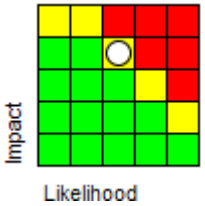
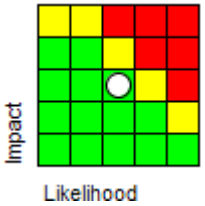
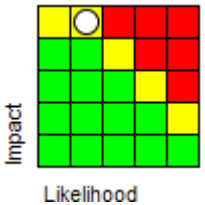
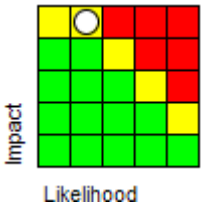
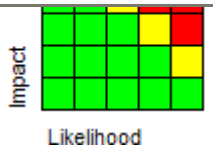
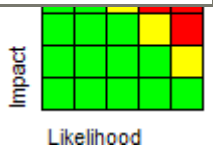
Appendix 1 Corporate Risk Report December 2020
Risks ordered by RAG not numerically

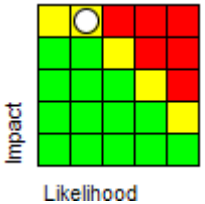
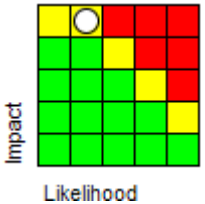
Generated on: 01 December 2020

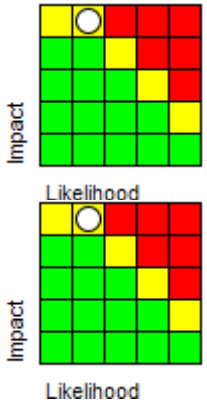
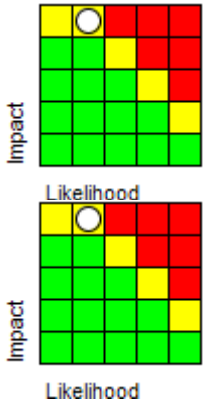
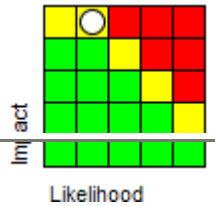
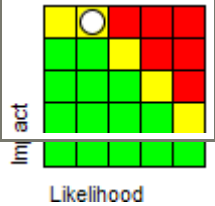
Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
CRR19 Cause: Uncertainty in the UK and World economy. The Government has spoken about an additional 5% reduction in local government funding, and further cuts in years to come. The impact on the financial markets and the pound following Covid-19 has brought forward a deeper depression and caused a slowdown in the property and financial markets. Risk: Ongoing reduction in planning fees; reduced car parking income; increased homelessness; and increased housing benefit claims, leisure centres, property income; investment income.	Financial Service Delivery Compliance with Regulations	Jane Eaton		CRR.19.2 Monitor the external environment CRR.19.3 Monitor internal indicators, particularly income generation and respond appropriately to adverse trends	Dominic Bradley Dominic Bradley		November 2020 update Covid-19 has triggered a sudden and deep recession. The impact on the economy and the Council's income in particular is severe, and income alone is estimated at £6m shortfall compared to budget. Swift action was undertaken to review income and revenue and capital expenditure, revisiting the MTFS. A budget update was presented to Members in July and September setting out the extent of the situation. A budget shortfall of £3m a year over the medium term is forecast. A restructure consultation commenced in October 2020 to help deliver some savings in 2021/22. The budget challenge process is undertaken during November, which will feed into the January / February budget setting process aimed at setting a balanced budget for 2021/22 and manageable budget deficits over the MTFS.
CRR35 Cause: COVID-19 is a new illness that can affect your lungs and airways and is caused by a virus called coronavirus. The illness is highly contagious, and people with underlying health conditions are at a higher risk of becoming very ill. This includes older adults, and/or people with chronic medical conditions such as heart disease; diabetes; and lung disease.	Failure of business objectives Health and safety Financial Service Delivery Compliance with regulations Reputation Staffing and culture	Glen Chipp		CRR.35.1 Essential services have been highlighted with the intention of redeployment of staff from other service areas. Staffing shortages on refuse collection may benefit from availability in the labour market. CRR.35.2 Funding from Government	Jane Eaton Jane Eaton		November 2020 Update (i) A second wave of COVID-19 is now with us and case numbers are rising in Horsham District. As at 27 October 2020 staff workloads are not excessively affected by this. (ii) Revenues and Benefits caseload remains high and Business Rate payment is low. The Council has 2 Court dates in December so some improved payment may be expected in the next few months.

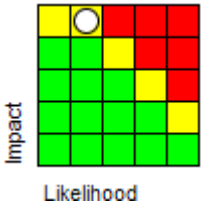
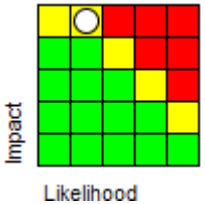
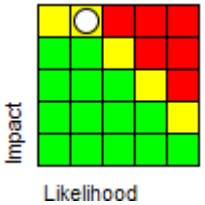
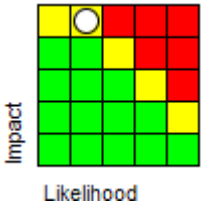
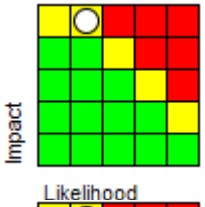
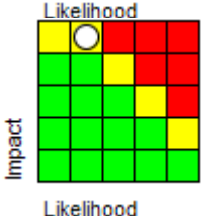
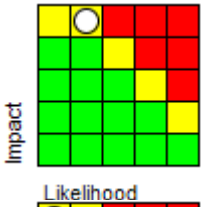
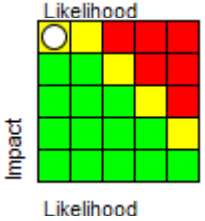
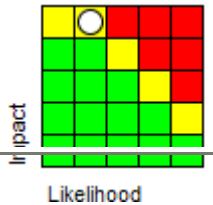
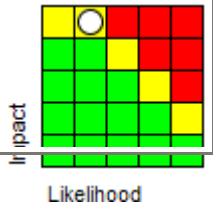
Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
Risk: (i) The Council is unable to deliver statutory front line services to the community due to, for example, staff shortages or unavailability of key officers. (ii) Substantial financial loss to the Council.							(iii) Funding from Government is still expected to leave an overspend on the year and the impact if the second wave takes the area into further lock-down is unknown.
CRR01c Financial Cause: The Council is reliant on Central Controlled Government funding (e.g. Business Rates). Risk: Decrease in Rateable Value due to appeals and businesses going under. This may cause the Council to fall below the business rates baseline, resulting in loss of funding.	Reductions in funding Financial	Jane Eaton		CRR.01c.1 Continue to keep a watching brief	Dominic Bradley		November 2020 update With business rates reform postponed and the COVID-19 recession, further reductions in business rates seem inevitable. The impact in 2021/22 may depend on whether Government gives business rate relief to retail and leisure businesses on the same scale again in 2021/22.
CRR01b Financial Cause: The Council is reliant on Central Controlled Government funding (e.g. Business Rates). Risk: (ii) Funding from Government is less generous than assumed in the MTFS from 2021	Reductions in funding Adverse effect on morale Financial Failure to achieve agreed objectives	Jane Eaton		CRR.01b.1 Continue to keep a watching brief CRR.01b.2 Revisit the MTFS and if necessary 2020/21 budget in year, with Cabinet in September.	Dominic Bradley Dominic Bradley		November 2020 update The Government has withdrawn the changes to business rates and revenue funding through the Fair Funding Review for the time being. This has removed this part of the risk temporarily, although Government has indicated that local government will get only a one-year settlement in 2021/22, giving little insight into the medium term. One-off Government funding for expenditure and income for the impact of COVID-19 is expected to cover some but not all of the Council's 2020/21 losses. The estimated net loss after grant income for 2020/21 may end up at around 20% of net expenditure (between £1.5m and £2m overspend). With income severely reduced, £3m budget deficits are expected across later years of the MTFS unless significant action is taken. Further one-off Government funding is not expected.

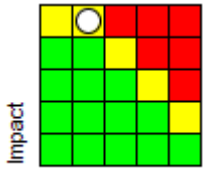
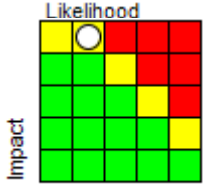
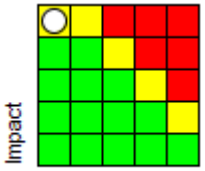
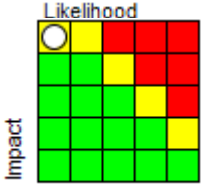
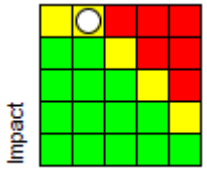
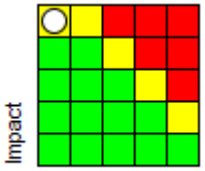
Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
CRR05 Governance <u>Cause</u>: Managers are responsible for ensuring that controls to mitigate risks are consistently applied. <u>Risk</u>: Officers are either unaware of expected controls or do not comply with control procedures.	Failure of business objectives Health & Safety Financial Service Delivery Compliance with Regulations Personal Privacy Infringement Reputation damage	Jane Eaton		CRR.05.1 Officer training CRR.05.3 All Service Managers required to sign an Assurance Statement. (By 30th June Annually) (Cyclical) CRR.05.4 "Cultural compliance" Internal Audits identify service-based issues and help managers to resolve these.	Jane Eaton Jane Eaton Jane Eaton		November 2020 Update Internal audit reports during summer 2020 report an increase in non-compliance as do the number minor incidents noted by the s151 officer and the Monitoring Officer this autumn. Increasing silo working arising from lockdown seems to be contributing to this. New training for officers is being prepared over the winter.
CRR18 Technological <u>Cause</u>: Council services are increasingly reliant on IT systems at a time when there are greater opportunities for malicious attackers to exploit security weaknesses. <u>Risk 1:</u> A malicious attacker exploits a known or unknown security weakness to penetrate the Council's ICT systems. <u>Risk 2:</u> IT not working due to environmental problems: fire, flood, power cut	Loss of key systems-disruption to Council services. Cost of investigation and recovery of systems. Fraud/theft. Loss of the integrity of Council Records. Penalties from the ICO. Adverse media coverage.	Jane Eaton		CRR.18.1 Staff and Member Training CRR.18.2 Awareness of current threats CRR.18.3 An effective ICT Service delivery team CRR.18.4 Effective patching and updates to mitigate known vulnerabilities CRR.18.5 Compliance with expected security standards. (PSN, PCI-DSS) CRR.18.6 Effective policies in place which outline security requirements for users of ICT CRR.18.7 Effective back-up and recovery processes in place for Council ICT systems. CRR.18.8 Transferring the risks to the cloud provider	Claire Ward / Robert Laban Andrea Curson Andrea Curson Andrea Curson Andrea Curson Andrea Curson Andrea Curson Andrea Curson		November 2020 update: Level of attack, particularly Ransomware attacks has been raised by the Cabinet Office. Remediation ongoing. CRR.18.1 IT Security Training has been rolled out to all staff and the IT Security Officer has reviewed the training and some items have been sent out to staff. More staff training to follow. CRR.18.2 This work is ongoing. CRR.18.3 All work is ongoing. CRR.18.4 Patching of devices ongoing. CRR.18.5 PSN Accreditation CRR.18.6 This work is ongoing. New policies have been updated and are reviewed regularly.

Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
				CRR.18.9 LGA Cyber Security review plan developed, approved internally and being carried out.	Andrea Curson		CRR.18.7 This work is ongoing. CRR 18.8 This work is ongoing CRR 18.9 We have undertaken a second stock take with an improved score and have adjusted the action plan accordingly. Work is progressing
CRR17 Cause: The External Auditors audit the HDC Benefits Grant Subsidy return to the Department for Work and Pensions (DWP) on an annual basis to identify errors. Risk: The Benefit Subsidy claim may be qualified and/or financial losses. HDC has a case load with a particularly high number of working people with many changes of circumstances.	Financial Service Delivery Compliance with regulations Reputation	Jane Eaton		CRR.17.1 Continuously monitor the level of quality control checking.	Beccy Salmon		November 2020 update The service continues to maintain a robust QC process to mitigate financial loss via a qualified subsidy loss. Despite the QC process that is in place the Amber status correctly reflects the potential for historic error in the caseload to be uncovered during a subsidy audit. Workload increases arising from COVID-19 recession may mean accuracy falls during 2020/21 but this will not be known until November 2021.
CRR02 Managerial / Professional Cause: The Council has a legal obligation to protect personal data. The Information Commissioners powers are much more far reaching when they change in May 2018. Risk 1: Major data breach or leak of sensitive information to a third party. Risk 2: Risk of significant ICO fine for non-compliance with new General Data Protection Regulations (GDPR).	People and businesses come to harm and suffer loss that might not otherwise have occurred Complaints / claims / litigation Resources consumed in defending claims Financial losses Fines from regulators Adverse publicity Reputation damage	Jane Eaton		CRR.02.1 Develop appropriate processes & procedures which underpin the IT Security Policy	Andrea Curson / Sharon Evans		November 2020 update: CRR.02.1 This work is ongoing CRR02.3 The Information Security Officer has compiled Information Security Training to be delivered to staff and members. The Head of Technology Services has obtained funding from the LGA to obtain Certified Information Security Accreditation by January 2021. CRR02.4 PSN Accreditation work underway to obtain 2020 Accreditation. CRR02.5 This is continuing and is ongoing.
CRR02 Managerial / Professional	People and	Jane Eaton		CRR.02.3 Provide a programme of Induction and	Robert Laban		November 2020 update:

Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
Cause: The Council has a legal obligation to protect personal data. The Information Commissioners powers are much more far reaching when they change in May 2018. Risk 1: Major data breach or leak of sensitive information to a third party. Risk 2: Risk of significant ICO fine for non-compliance with new General Data Protection Regulations (GDPR). CRR03 Legal Cause: The Civil Contingencies Act places a legal obligation upon the Council, with partners, to assess the risk of, plan, and exercise for emergencies, as well as undertaking emergency and business continuity management. The Council is also responsible for warning and informing the public in relation to emergencies, and for advising local businesses. Risk: The Council is found to have failed to fulfil its obligations under the Act in the event of a civil emergency.	businesses come to harm and suffer loss that might not otherwise have occurred Complaints / claims / litigation Resources consumed in defending claims Financial losses Fines from regulators Adverse publicity Reputation damage People and businesses come to harm and suffer loss that might not otherwise have occurred Complaints / claims / litigation Resources consumed in defending claims Financial losses Censure by regulators Reputation damaged	Adam Chalmers		at least annual training on Information Security to all staff.			CRR.02.1 This work is ongoing CRR02.3 The Information Security Officer has compiled Information Security Training to be delivered to staff and members. The Head of Technology Services has obtained funding from the LGA to obtain Certified Information Security Accreditation by January 2021. CRR02.4 PSN Accreditation work underway to obtain 2020 Accreditation. CRR02.5 This is continuing and is ongoing. November 2020 Update CRR.03.1 Lessons identified through departmental de-briefs are being incorporated into corporate BC plan. 2nd wave plan has been written and agreed and implemented by the BC working group. BC working group meeting every two weeks and any new developments or relevant information will be added to the BC plan. CRR.03.2 All departments asked to complete debrief proforma to capture valuable lessons learned from the last 5 months. Full reviews of department BC plans were due to take place in Oct/Nov but as the second wave is due to hit in Nov this will be pushed back to the new year (Feb/Mar). CRR.03.5 All bite size sessions postponed. Debrief and review sessions will be introduced and run once COVID-19 guidelines allow. (Estimated Mar/Apr 2021 but might
				CRR.02.4 Annual PSN Accreditation	Andrea Curson		
				CRR.02.5 Representatives from each department meet every other month to maintain compliance, updates and training	Sharon Evans		
				CRR.03.1 Update corporate business continuity plan and regular review.	Rob Jarvis		

Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
							extend depending upon the pandemic).
CRR03 Legal Cause: The Civil Contingencies Act places a legal obligation upon the Council, with partners, to assess the risk of, plan, and exercise for emergencies, as well as undertaking emergency and business continuity management. The Council is also responsible for warning and informing the public in relation to emergencies, and for advising local businesses. Risk: The Council is found to have failed to fulfil its obligations under the Act in the event of a civil emergency. CRR06 Physical Cause: The Council is responsible for the health & safety of its clients, staff and other stakeholders, owns and maintains significant assets, and also has responsibility for H&S in some partner organisations where it does not have operational control. Risk: A health & safety failure occurs.	People and businesses come to harm and suffer loss that might not otherwise have occurred Complaints / claims / litigation Resources consumed in defending claims Financial losses Censure by regulators Reputation damaged People come to harm Complaints/claims/ litigation Financial losses Censure by audit / inspection Reputation damage Adverse effect on morale Stress and absenteeism	Adam Chalmers Glen Chipp		CRR.03.2 Update departmental business continuity plans and regular review. CRR.03.5 Bitesize workshops to address new procedures and processes. CRR.03.6 Fortnightly BC meetings during Covid-19 CRR.06.2 H&S Management Forum reviews corporate inspection strategy quarterly.	Rob Jarvis Rob Jarvis Rob Jarvis Robert Laban / Health & Safety Officer		November 2020 Update CRR.03.1 Lessons identified through departmental de-briefs are being incorporated into corporate BC plan. 2nd wave plan has been written and agreed and implemented by the BC working group. BC working group meeting every two weeks and any new developments or relevant information will be added to the BC plan. CRR.03.2 All departments asked to complete debrief proforma to capture valuable lessons learned from the last 5 months. Full reviews of department BC plans were due to take place in Oct/Nov but as the second wave is due to hit in Nov this will be pushed back to the new year (Feb/Mar). CRR.03.5 All bite size sessions postponed. Debrief and review sessions will be introduced and run once COVID-19 guidelines allow. (Estimated Mar/Apr 2021 but might extend depending upon the pandemic). November 2020 update Corporate inspection strategy and training programme fully implemented. Now an ongoing requirement.
CRR06 Physical Cause: The Council is responsible for the health & safety of its clients, staff and other stakeholders, owns and	People come to harm Complaints/claims/ litigation	Glen Chipp Jane Eaton		CRR.06.3 Training programme includes annual refreshers on a rolling programme. All mandatory training must be completed as part of probation	Robert Laban		November 2020 update Corporate inspection strategy and training programme fully implemented. Now an ongoing

Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
maintains significant assets, and also has responsibility for H&S in some partner organisations where it does not have operational control. Risk: A health & safety failure occurs. CRR32 Cause: Nationally, NHS Foundation Trusts (and some NHS Trusts) have applied for mandatory charitable relief on their business rates, on the basis that they should be treated as charities. Risk: Decrease in Rateable Value, and potentially backdated refunds to 2010.	Financial losses Censure by audit / inspection Reputation damage Adverse effect on morale Stress and absenteeism Reductions in funding Financial			CRR.32.1 Continue to keep a watching brief	Dominic Bradley		requirement. November 2020 update A High Court judicial review dismissed the hearing in November 2019. The claimants have appealed to the Court of Appeal. The date of the appeal hearing has not yet been set. Permission for consideration of the appeal was granted on 28 July 2020. One NHS Foundation Trust appeal in the district has been received and was included in the business rates appeals provision at 31 March 2019. No separate provision has been created for appeals that have not yet been received.
CRR34 Cause: Uncertainty in the UK and World economy. Instability and recent high-profile failures. Risk: Key contractor failure	Financial	Jane Eaton		CRR.34.1 Regularly check accounts of key suppliers	Heads of Service		November 2020 Update: The COVID-19 recession continues to make losses of contractors more likely. The business continuity group continues to monitor progress as we move through the second wave.
CRR34 Cause: Uncertainty in the UK and World economy. Instability and recent high-profile failures. Risk: Key contractor failure CRR35a Cause: Covid-19 infection Risk: Serious risk to the health and safety of workers	Financial Failure of Health and safety, Service Delivery, Compliance with regulations, Reputational loss.	Jane Eaton Jane Eaton	 	CRR.34.2 Check public liability insurance of key suppliers	Heads of Service	 	November 2020 Update: The COVID-19 recession continues to make losses of contractors more likely. The business continuity group continues to monitor progress as we move through the second wave. November 2020 Update The work is ongoing and is monitored every fortnight by the Business Continuity Group.
CRR34 Cause: Uncertainty in the UK and World economy. Instability and recent high-profile failures.	Financial Failure of Health and safety, Service Delivery,	Jane Eaton Jane Eaton Jane		CRR.34.3 Ask for key suppliers' business continuity plans CRR.34.4 Consider whether the failure of a key supplier	Heads of Service Heads of Service		November 2020 Update: The COVID-19 recession continues to make losses of contractors more likely. The business continuity group

Risk Code & Description	Effect	Risk Owner	Current Risk Matrix	Control Action	Control Action Owner	Target Risk Matrix	Quarterly Update
Risk: Key contractor failure CRR35a Cause: Covid-19 infection Risk: Serious risk to the health and safety of workers CRR35a Cause: Covid-19 infection Risk: Serious risk to the health and safety of workers	Compliance with regulations, Reputational loss. Failure of Health and safety, Service Delivery, Compliance with regulations, Reputational loss.	Eaton	 	needs to go in service business continuity plan CRR.35a.1 The director led Business Continuity Group to oversee H&S measures (staff H&S representative observes) CRR.35a.3 Regular updates on government advice on keeping safe	 Jane Eaton Robert Laban	 	continues to monitor progress as we move through the second wave. November 2020 Update The work is ongoing and is monitored every fortnight by the Business Continuity Group. November 2020 Update The work is ongoing and is monitored every fortnight by the Business Continuity Group.
CRR35a Cause: Covid-19 infection Risk: Serious risk to the health and safety of workers	Failure of Health and safety, Service Delivery, Compliance with regulations, Reputational loss.	Jane Eaton		CRR.35a.4 A balanced approach to home/office working in line with government advice CRR.35a.5 Re-modelling of workspaces to ensure social distancing CRR.35a.6 Provision of sanitary products and PPE CRR.35a.7 Risk assessments for offices and specific staff CRR.35a.8 Managed opening /closure of the Capitol, Museum, Leisure, Sports services and Reception in line with safety concerns	Andrea Curson/Robert Laban Brian Elliott Brian Elliott Robert Laban Vicky Wise		November 2020 Update The work is ongoing and is monitored every fortnight by the Business Continuity Group.

By virtue of paragraph(s) 5 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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Report to Audit Committee

16th December 2020
By the Horsham Chief Internal Auditor

INFORMATION REPORT

Not Exempt

Internal Audit Progress Report – Quarter 2 (01/07/20 - 30/09/20)

Executive Summary

To provide Members with an update on all internal audit and counter-fraud activity completed during the quarter, including a summary of all key findings. The report also includes details of progress on delivery of the annual audit plan along with an update on the performance of the internal audit service during the period.

Recommendations

The Committee is recommended to:

- Note the report and consider any further action required in response to the issues raised; and
- Identify any new or emerging risks for consideration for inclusion in the internal audit plan.

Reasons for Recommendations

i) To comply with the requirements set out in the Public Sector Internal Audit Standards 2013 (amended April 2017).

ii) The Audit Committee is responsible for reviewing the effectiveness of the Council's systems of internal control.

Background Papers

Internal Audit Strategy and Annual Plan 2020-21

Wards affected: All.

Report Author: Paul Miller, Horsham Chief Internal Auditor
Contact Details: Russell Banks, Orbis Chief Internal Auditor Tel No. 01273 481447
Paul Miller, Horsham Chief Internal Auditor Tel No. 01403 215319

Background Information

1 Introduction and Background

Background

1.1 This progress report covers work completed between 1 July 2020 and 30 September 2020.

Supporting Information

1.2 The current annual plan for internal audit is contained within the Internal Audit Strategy and Annual Plan 2020-21 which was approved by the Audit Committee on 01 April 2020.

2 Relevant Policy / Professional Standards

2.1 Internal Audit follows the mandatory standards set out in the Public Sector Internal Audit Standards (PSIAS) published by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors.

2.2 The Council's Constitution supports the statutory requirements outlined above. Financial Procedure Rule 4e 27 states that: "the Chief Finance Officer ensures that the Council has appropriate arrangements in place to maintain an adequate and effective internal audit". The terms of reference for internal audit are detailed in the Council's Internal Audit Charter which is approved and reviewed by the Audit Committee.

3 Conclusion and Reasons for Recommendation

3.1 Key audit findings from final reports are summarised in Appendix A.

3.2 Overall, of the four formal audits finalised during the quarter, one received an opinion of 'reasonable assurance', two received an opinion of "partial assurance", and one received an opinion of "minimal assurance".

3.3 Formal follow up reviews continue to be carried out for all audits where 'minimal assurance' opinions have been given and for higher risk areas receiving 'partial assurance'. Progress on action tracking is provided in Section 3 of Appendix A, and details of outstanding high and medium actions are provided in Section 3.4.

3.4 Members will recall that flexibility was built into the audit plan to allow resources to be directed to any new and emerging risks. We continue to liaise with departments to identify these but would also welcome input from Members. Details of those reviews added and removed from the plan so far this year are set out in section 4 of Appendix A.

3.5 Progress against our performance targets (focussing on a range of areas relating to our service) can be found in section 5 of Appendix A.

4 Next Steps

4.1 The Committee will be kept informed about progress in terms of the delivery of the audit plan for 2020/21.

5 Outcome of Consultations

5.1 Heads of Service / Service Managers are consulted during each audit. At the end of each review, audit findings are discussed with the relevant Head(s) of Service at a final meeting, and actions are agreed. An action plan is incorporated into the final report including details of responsible officers and agreed implementation dates. There are occasions when a director may also be consulted, particularly for audits which span a number of departments.

6 Other Courses of Action Considered but Rejected

6.1 Not applicable.

7 Resource Consequences

7.1 This report summarises information about the work undertaken by Internal Audit, and therefore there are no direct financial or HR consequences.

8 Legal Consequences

8.1 There are no legal consequences. Where compliance issues are identified during audit fieldwork, the Head of Legal & Democratic Services (or relevant legal specialist) will be consulted.

9 Risk Assessment

9.1 All Internal Audit work is undertaken using a risk based approach.

10 Other Considerations

10.1 Internal Audit is a reporting function and there are no consequences in respect of Crime & Disorder; Human Rights; Equality & Diversity; or Sustainability. However these areas are considered where appropriate during audit fieldwork.

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Appendix A

Internal Audit and Counter Fraud

Quarter 2 Progress Report 2020/21

CONTENTS

1. Summary of Completed Audits

Travel Expenses (2020/21)

1.1 Employees authorised by their manager to travel on Council business are entitled to claim reimbursement of the costs associated with their business journeys. The Council provides a range of options to pay for travel expenses, including reimbursement of work mileage outside of normal commuting mileage and associated costs; booking of public transport; booking of accommodation when required; and an essential user allowance.

1.2 The purpose of this audit was to provide assurance that controls are in place to meet the following objectives:

- There are clear and comprehensive policies and procedures in place, associated with all aspects of staff travel and travel expenses;
- There are robust controls in place regarding the authorisation of staff travel and expenses;
- Staff travel and expenses are claimed and paid in accordance with the Council's policies and procedures;
- There are appropriate monitoring and reporting arrangements in place.

1.3 Overall, we found a range of weaknesses for administering staff travel claims and expenses. This included inconsistencies in relation to compliance with policies and procedures, and within the process itself, particularly in relation to staff mileage claims, where we identified overpayments and other errors. Therefore, we were only able to provide an opinion of **minimal assurance** over the controls in place.

1.4 In response to this, a number of improvements have been agreed with the Senior Leadership Team which are summarised as follows:

- The Council's Vehicle Allowance Policy and Procedure document will be reviewed and enhanced, incorporating guidance on other forms of transport and accommodation bookings, and additional policy requirements identified during the audit.
- Guidance will be provided to managers outlining the checks that should be completed prior to mileage claims being signed off.
- Controls will be introduced to help prevent the incidence of inaccurate claims, including duplicate submissions and excess mileage. More robust management checks will be introduced, and there is a new requirement for mileage claims to be submitted monthly.
- Claimants will be expected to provide more information when describing their journeys, providing postcodes where possible. However, the Senior Leadership Team (SLT) will allow some departments flexibility in circumstances where officers travel to multiple sites on a daily basis. Such an arrangement, whilst improving efficiency, does carry a degree of risk. However, SLT has considered this, and on balance, this is something they are prepared to accept in the interests of efficiency.
- The Chief Executive will send a reminder to all staff that journey details recorded on mileage claim forms must be complete, accurate, and in accordance with the Council's policy.
- Managers have been reminded of the mandatory requirement to provide VAT receipts to evidence purchase card spend.

- Staff will be reminded that annual checks of driver and vehicle documentation are a mandatory requirement, and following management verification checks, documents will be stored in the Technology One system as evidence of approval.

1.5 As the overall opinion was "minimal assurance", a follow up review will be undertaken in 2021/22 to ensure that the agreed actions have been implemented.

Cultural Compliance (Building Control) (2020/21)

1.6 The Building Control service at Horsham District Council aims to ensure that building work complies with the building regulations, by following a set of standards intended to protect people's safety, health and welfare in and around built environments. The Building Control team check all aspects of construction including, but not limited to: foundations, damp-proofing, structure, insulation, ventilation, heating, sanitation, accessibility, fire protection, and means of escape in case of fire.

1.7 The purpose of this audit was to provide assurance that controls are in place to meet the following objectives:

- Management has put in place appropriate arrangements for monitoring delivery of the service and assessing it's performance and effectiveness;
- All key activities undertaken by the team are conducted in accordance with the Council's policies and procedures and comply with basic internal controls;
- Robust management arrangements are in place and all members of staff are subject to appropriate management and supervision;
- Expenditure is only incurred for legitimate Council business and is in line with the relevant procurement process.

1.8 Overall, we were only able to provide an opinion of **partial assurance** over the controls operating in the area under review. This is because a number of areas of poor compliance with corporate policies and procedures were identified.

1.9 A management action plan has therefore been agreed with the Head of Building Control, this included measures to:

- Appoint a new risk champion who is responsible for ensuring the Building Control risk register is regularly updated to reflect the current risk profile and submitted to the Performance Team for quarterly reporting purposes.
- Improve data protection controls through the development of an Information Asset Register and Data Flow spreadsheet and ensuring all records that are currently kept by an external records management company, offsite, are returned, reviewed and stored at Parkside or destroyed in line with the Council's records management policy.
- Return the periodic budget monitoring reports with comprehensive forecasts.
- Complete all mandatory e-learning training for all staff in the Building Control team. In addition, all probationary review forms and induction checklists will be completed for future new starters and retrospectively for those staff who started at the beginning of 2020.

- Strengthen purchase card (P-Card) controls by ensuring all P-Card transactions are supported by evidence, the assigned P-Card owner is the only officer to use the P-Card and the card details are not shared with, or retained by, other members of staff in the team.
- Engage agency staff from the approved framework arrangement, in the first instance, in order to secure value for money.
- Improve the mileage claim process to ensure sufficient journey descriptions are completed and 'home to work' mileage has not been claimed, to aid verification and approval by an independent person.

1.10 As we have given an opinion of partial assurance, we will carry-out a follow up review to ascertain progress made in implementing the agreed actions.

Cultural Compliance (The Capitol) Follow-up (2020/21)

1.11 The Capitol is an arts and cultural venue located in Horsham, owned and operated by the Council. The venue consists of a theatre, two cinema screens, studio theatre, meeting room and gallery space, as well as a café and bar.

1.12 This follow up review has focussed specifically on the implementation of actions agreed in the audit report of May 2019. It should be noted that, where areas tested in the previous audit were well controlled and were mitigating the potential risks, these have not been re-tested during this review, as it is assumed these controls are continuing to operate.

1.13 The purpose of the audit was to provide assurance that:

- Management has put in place appropriate arrangements for monitoring delivery of the service and assessing its performance and effectiveness;
- There is an adequate budget setting and monitoring process in place and that appropriate measures are taken in a timely manner to address budget pressures;
- Expenditure is only incurred for legitimate Council business and is in line with the relevant procurement process;
- Where chargeable services are delivered, appropriate prices are set and regularly reviewed and all income attributable to the work undertaken by the service is invoiced correctly;
- There is effective staff supervision and performance management, including administration of staff development and well-being in accordance with the Council's procedures;
- Assets purchased for the Council are held securely and are appropriately managed.

1.14 As a result of this work, we were only able to provide **partial assurance** over the controls operating within the area under review.

1.15 There were 14 findings in our previous 2019 audit, and we found that 3 of these had only been partly implemented. The audit opinion was also informed by additional testing that was undertaken following a review and enquiry into an employee's declaration of interest that was not available previously, where a potential conflict of interest may exist. Additional testing particularly focussed on: additional hours worked by permanent staff; casual worker claims; and compliance with the working time directive.

1.16 A number of improvements have been agreed with the Head of Leisure and Culture and the Capitol Operations Manager which are summarised below:

- All staff at The Capitol have now submitted a completed declaration of interest for approval. In the event of a potential conflict of interests, management checks will be undertaken to ensure that private work is being undertaken outside of normal working hours, and the working time directive is not being breached.
- The use of casual workers will be reduced, and proper supervisory checks of casual worker timesheets will be undertaken to ensure that claims are accurate; not duplicated; and there is no breach of the working time directive.
- All overtime claimed will be recorded accurately for hours worked on specific days and it will not be approved unless the claim is appropriate. Any training attended by a part-time member of staff will be undertaken as part of their contracted working hours and not claimed as overtime hours.
- Internal records maintained to support TMA (Theatre Management Association) payments will include the name of the individual; the date; their start and end hours; and total hours, in order for this information to be reconciled with other claim forms submitted.

1.17 A robust action plan to strengthen controls was agreed with management and an additional follow up review will be completed in 2021/22 to assess the implementation of the agreed actions.

Cultural Compliance (Property & Facilities) Follow-up (2020/21)

1.18 The Property & Facilities team deliver a property and facilities management service across the Council; lead on property development and investment activity; and manage assets and property within the Council's investment and operational portfolios.

1.19 This follow up review has focussed specifically on the implementation of actions agreed in the audit report of August 2019. It should be noted that, where areas tested in the previous audit were well controlled and were mitigating the potential risks, these have not been re-tested during this review, as it is assumed these controls are continuing to operate.

1.20 The purpose of this review was to provide assurance that controls are in place to meet the following objectives:

- Management has put in place appropriate arrangements for monitoring delivery of the service and assessing its performance and effectiveness;
- There is an adequate budget setting and monitoring process in place and that appropriate measures are taken in a timely manner to address budget pressures;
- Expenditure is only incurred for legitimate Council business and is in line with the relevant procurement process;
- Where chargeable services are delivered, appropriate prices are set and regularly reviewed and that all income attributable to the work undertaken by the service is invoices correctly;
- There is effective staff supervision and performance management including administration of staff development and well-being in accordance with the Council's procedures;

- Assets purchased for the Council are held securely and are appropriately managed.

1.21 We found that the majority of actions had been implemented and were, therefore, able to give an improved opinion of **reasonable assurance**.

1.22 Two actions from the previous review had only been partly implemented, relating to the timeliness of budget monitoring returns and addressing contractual arrangements with a specific supplier, neither of which are considered of a high risk nature.

2. Counter Fraud and Investigation Activities

Proactive Counter Fraud Work

2.1 The Orbis Internal Audit structure came into effect from 1st April 2018. The integrated structure was designed to deliver resilience, flexibility and quality, along with specific specialisms. A key strand of the structure was the formation of a counter fraud team that would deliver both reactive and proactive fraud services across the partnership.

National Fraud Initiative (NFI)

2.2 The organisation is currently in the process of uploading the required data sets, and this exercise is due to be completed by 1st December 2020. Data matches will then be made available by the Cabinet Office on 28th January 2021, and will be subsequently investigated.

Fraud Risk Assessments

2.3 A Fraud risk assessment has been undertaken to ensure that the current fraud threat for the Council has been considered and appropriate mitigating actions identified. The outcomes from the assessment help to inform the annual internal audit plan

Counter-Fraud Strategy and Framework

2.4 The Orbis Counter Fraud team has developed a Counter-Fraud Strategy and Framework for Horsham. This has been approved by the Council's Senior Leadership Team and is published on the Council's Intranet.

3. Action Tracking

3.1 All high and medium priority actions agreed with management as part of individual audit reviews are subject to action tracking. As at the end of quarter 2, 98% of high and medium priority actions due had been implemented within agreed timescales.

3.2 The implementation of high and medium priority agreed audit actions (based on a 12 month rolling period) is summarised in the following table:

Period to:	High & Medium Priority Agreed Actions Due	Not implemented	Implemented	% Implemented
30/09/20	61	1	60	98%

3.3 Internal Audit will continue to work with senior management to ensure that sufficient attention is given to actions that remain overdue and an update on progress will continue to be reported to this committee.

3.4 Details of outstanding priority agreed action:

Audit / Agreed Action	Directorate	Due Date	Revised Date	Progress to date
Medium Priority Purchase Orders (P.Os): To review the take up of purchase orders and encourage usage, with the expectation that the use of P.Os (as measured by P.Os raised as a percentage of invoices received) will increase.	Corporate Resources	31/12/17	31/03/21	November 2020 Management Update: The impact of Covid-19 has set back plans to roll out purchase order training. Other day to day activities have been prioritised such as payments of business grants, and remote year end closedown. Plans for the roll out of training have also now been put on hold due to social distancing and remote working. It is felt that remote training in a technical area will not be efficient. This will be revisited as necessary. A few officers have been provided with some adhoc training in the Parkside office.

4. Amendments to the Audit Plan

4.1 In accordance with proper professional practice, the internal audit plan for the year remains under regular review to ensure that the service continues to focus its resources in the highest priority areas based on an assessment of risk. Through discussions with management, the following reviews have been added to the audit plan during the year:

- Review of the Community Hubs – Covid-19 Red Response; and
- Purchase Cards, including areas of spend.

4.2 Through the same process, audits have been removed or deferred from the audit plan and, where appropriate, will be considered for inclusion in the 2021/22 plan as part of the overall risk assessment completed during the annual audit planning process:

- Capitol Bar and Catering Facility;
- Volunteers;
- Hop Oast (Cultural Compliance) follow-up; and
- Capital Grant Funding / External Funding

5. Internal Audit Performance

5.1 In addition to the annual assessment of internal audit effectiveness against Public Sector Internal Audit Standards (PSIAS), the performance of the service is monitored on an ongoing basis against a set up agreed key performance indicators as set out in the following table:

Aspect of Service	Orbis IA KPI	Target	RAG score	Actual Performance
Quality	Annual Audit Plan agreed by Audit Committee	By end April	G	Approved by the Audit Committee on 1st April 2020.
	Annual Audit Report and Opinion	By end July	G	2019/20 report presented to the Audit Committee on 15th July 2020.
	Customer Satisfaction levels	90% satisfied	G	100%
Productivity and process efficiency	Audit Plan – completion to draft report stage	90%	A	44% completed to draft report stage at the end of Quarter 2, against a target of 45%.
Compliance with professional standards	Public Sector Internal Audit Standards complied with	Conforms	G	January 2018 - External assessment by the South West Audit Partnership gave an opinion of 'Generally Conforms' – the highest of three possible rankings. June 2020 - Internal Self-Assessment completed. There were no major areas of non-compliance with PSIAS identified. June 2020 - Internal Quality Review completed, no major areas of non-compliance with our own processes identified.

	Relevant legislation such as the Police And Criminal Evidence Act, Criminal Procedures and Investigations Act	Conforms	**G**	No evidence of non-compliance identified.
Outcome and degree of influence	Implementation of management actions agreed in response to audit findings	95% for high & Medium priority agreed actions	**G**	98%
Our staff	Professionally qualified / accredited	80%	**G**	90%[1]

[1] Includes part-qualified staff

Appendix B

Audit Opinions and Definitions

Opinion	Definition
Substantial Assurance	Controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.
Reasonable Assurance	Most controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.
Partial Assurance	There are weaknesses in the system of control and/or the level of non-compliance is such as to put the achievement of the system or service objectives at risk.
Minimal Assurance	Controls are generally weak or non-existent, leaving the system open to the risk of significant error or fraud. There is a high risk to the ability of the system/service to meet its objectives.

Horsham District Council

Annual Audit Letter for the year ended 31 March 2020

November 2020

EY
Building a better working world

Contents

Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk). [**OR** As part the Auditor Engagement process, we have agreed with you the respective responsibilities of auditors and audited bodies. Copies of the Engagement Letter and Terms and Conditions of our appointment are available from the Chief Executive or via the bodies minutes on their website].

This Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The 'Terms of Appointment (updated April 2018)' issued by PSAA [**OR** The Terms and Conditions of our appointment contained within the Engagement Letter] sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Results Report is prepared in the context of the Statement of responsibilities / Terms and Conditions of Engagement. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Hywel Ball, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Section 1

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Horsham District Council (the Council) following completion of our audit procedures for the year ended 31 March 2020.Covid-19 had an impact on a number of aspects of our 2019/20 audit. We set out these key impacts below.

Area of impact	Commentary
Impact on the delivery of the audit	
▸ Changes to reporting timescales	As a result of Covid-19, new regulations, the Accounts and Audit (Coronavirus) (Amendment) Regulations 2020 No. 404, have been published and came into force on 30 April 2020. This announced a change to publication date for final, audited accounts from 31 July to 30 November 2020 for all relevant authorities. We worked with the Council/ Pension Fund to deliver our audit in line with the revised reporting timescale.
Impact on our risk assessment	
▸ Valuation of Property Plant and Equipment	The Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in the year-end valuation reports produced by the Council's external valuer. We consider that the material uncertainties disclosed by the valuer gave rise to an additional risk relating to disclosures on the valuation of property, plant and equipment.
▸ Disclosures on Going Concern	Financial plans for 2020/21 and medium term financial plans will need revision for Covid-19. We considered the unpredictability of the current environment gave rise to a risk that the council would not appropriately disclose the key factors relating to going concern, underpinned by managements assessment with particular reference to Covid-19 and the Council's actual year end financial position and performance.
▸ Events after the balance sheet date	We identified an increased risk that further events after the balance sheet date concerning the current Covid-19 pandemic will need to be disclosed. The amount of detail required in the disclosure needed to reflect the specific circumstances of the Council.
Impact on the scope of our audit	
▸ Information Produced by the Entity (IPE)	We identified an increased risk around the completeness, accuracy, and appropriateness of information produced by the entity due to the inability of the audit team to verify original documents or re-run reports on-site from the Council's systems. We undertook the following to address this risk: ▸ Used the screen sharing function of Microsoft Teams to evidence re-running of reports used to generate the IPE we audited; and ▸ Agree IPE to scanned documents or other system screenshots.
▸ Consultation requirements	Additional EY consultation requirements concerning the impact on auditor reports. The changes to audit risks and audit approach changed the level of work we needed to perform.

Executive Summary (cont'd)

The tables below set out the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Council's :	
► Financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the Council as at 31 March 2020 and of its expenditure and income for the year then ended
► Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Accounts
► Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	We concluded that you have put in place proper arrangements to secure value for money in your use of resources

Area of Work	Conclusion
Reports by exception:	
► Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Council
► Public interest report	We had no matters to report in the public interest
► Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report.
► Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Executive Summary (cont'd)

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	We had no matters to report. The Council is below the specified audit threshold of £500mn. Therefore, we did not perform any audit procedures on the consolidation pack.

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 22 October 2020

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Andrew Brittain
Associate Partner
For and on behalf of Ernst & Young LLP

Section 2

Purpose and Responsibilities

Ref: EY-000092651-01

Purpose

The Purpose of this Letter
The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council. We have already reported the detailed findings from our audit work in our 2019/20 Audit Results Report to the 20 October 2020 Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

Responsibilities

Responsibilities of the Appointed Auditor

Our 2019/20 audit work has been undertaken in accordance with the Audit Plan that we issued on 18 December 2020 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- Expressing an opinion:
  - On the 2019/20 financial statements; and
  - On the consistency of other information published with the financial statements.
- Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- Reporting by exception:
  - If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - Any significant matters that are in the public interest;
  - Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. The Council is below the specified audit threshold of £500mn. Therefore, we did not perform any audit procedures on the return.

Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement (AGS). In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Section 3

Financial Statement Audit

Financial Statement Audit

Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office and issued an unqualified audit report on 20 October 2020.

Our detailed findings were reported to the October 2020 Audit Committee.

The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
Misstatements due to fraud or error The financial statements as a whole are not free of material misstatements whether caused by fraud or error. As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.	[We obtained a full list of journals posted to the general ledger during the year, and analysed these journals using criteria we set to identify any unusual journal types or amounts. We then tested a sample of journals that met our criteria and tested these to supporting documentation. We considered the following accounting estimates most susceptible to bias; pension net asset, NDR appeal provision, and valuation on Property. For each estimate we reviewed and challenged the underlying support and assumptions. We evaluated the business rationale for any significant unusual transactions We have not identified any material weaknesses in controls or evidence of material management override. We have not identified any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Risk of fraud in revenue recognition - inappropriate capitalisation of revenue expenditure Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. Linked to the risk of 'misstatements due to fraud and error', inappropriate revenue or expenditure recognition would most likely be affected through the override of controls. This risk manifests itself in areas where management makes judgements that impact the general fund balance through determining whether items of expenditure are financed from capital or revenue resources. As such we associate this risk with capital additions. To gain assurance in this area we: • Examined invoices for significant additions, capital expenditure authorisations, leases and other data that support the additions. We reviewed the sample selected against the definition of capital expenditure in IAS 16. To gain the required level of assurance in relation to the risk we extended our testing of items by lowering our testing threshold. We also reviewed a larger random sample of capital additions below our testing threshold.	We did not identify any instances of inappropriate capitalisation of revenue expenditure

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Valuation of Property, including investment property The Council holds a significant investment in retail property. The valuation of property is complex and subject to several assumptions and judgements. A small movement in these assumptions can have a material impact on the financial statements. Difficulties in the retails sector have led to many retailers, including well-known names, closing stores, going into administration, or otherwise looking to reduce their rental costs by renegotiating existing leases. These difficulties have had a direct impact on the value of the retail units (high street shops, out of town retail parks and shopping centres) leased to retailers. To gain assurance in this area we: • Considered the work performed by the Council's valuer, this included a review of the adequacy of the scope of the work performed, their professional capabilities and the results of their work. • Sample tested key asset information used by the valuer in performing the valuation (e.g. floor plans to support valuations based on price per square metre). This included instructing our Real Estates experts to review in detail a sample of retail properties and specialised assets carried valued at depreciated replacement cost, which we considered to be higher risk. • Considered the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code for land and buildings within Plant, Property and Equipment and annually for Investment Properties. We also considered if any specific changes to assets had been made and, if so, whether these had been properly communicated to the valuer. • Reviewed assets not subject to valuation in 2018/19 to confirm that the remaining asset base is not materially misstated. • Considered changes to useful economic lives as a result of the most recent valuation. • Tested accounting entries had been correctly processed in the financial statements.	In our judgement the value of Council's retail property is overstated by £433k. We instructed our property valuation team to review a sample of the valuation performed by the Council. The review focuses on whether the valuation is based on reasonable and supportable assumptions. From this review we identified for one asset the assumptions used by the Councils Valuation team were not within a supportable range. Our valuations team reperformed the calculation using supportable assumptions which identified a judgemental difference of £433k. As the difference is not above our materiality level, we conclude that the balance is materially fairly stated and do not modify our audit opinion in respect of this matter. The Council's external valuer did disclose a 'material uncertainty' in its year end valuation report in line with RICS guidance. We requested the Council repeat the 'material uncertainty' in the statement of accounts. Based on the work we have undertaken we are satisfied that the carrying value of PPE disclosed in the financial statements is materially accurate. We intend to include an emphasis of matter paragraph in our audit report highlighting the Council's disclosure in this area to the reader of the accounts. For clarity, an emphasis of matter paragraph is not a modification of our opinion. It is a paragraph in our report which highlights a disclosure in the financial statements that, in our judgment, is of importance to the users' understanding of the financial statements.

Financial Statement Audit (cont'd)

Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	We determined planning materiality to be £1.5m (2019: £1.6m), which is 2% of gross revenue expenditure reported in the accounts of £74.5 million. We consider gross revenue expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council
Reporting threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £74k (2019: £80k)

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- Remuneration disclosures including any severance payments, exit packages and termination benefits
- Related party transactions

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

Section 4

Value for Money

Value for Money

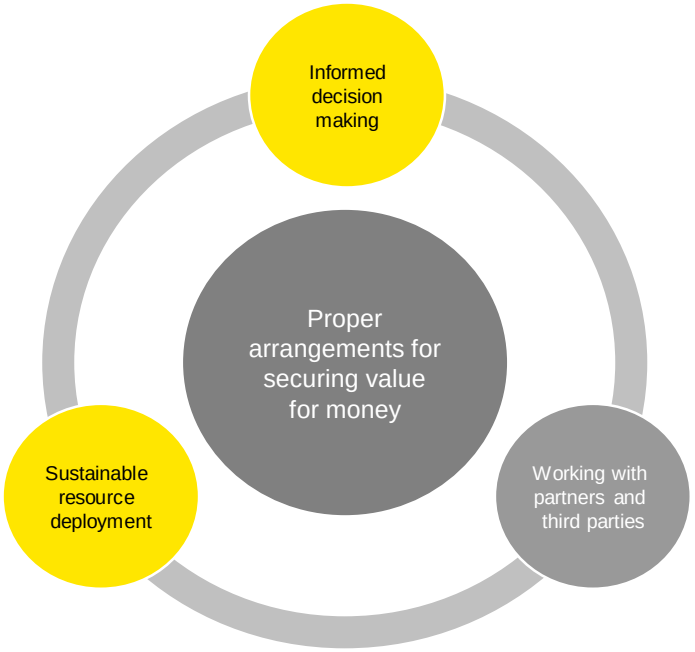
We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness in its use of resources. This is known as our value for money conclusion.

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

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

On 16 April 2020 the National Audit Office published an update to auditor guidance in relation to the 2019/20 Value for Money assessment in the light of Covid-19. This clarified that in undertaking the 2019/20 Value for Money assessment auditors should consider NHS bodies' response to Covid-19 only as far as it relates to the 2019-20 financial year; only where clear evidence comes to the auditor's attention of a significant failure in arrangements as a result of Covid-19 during the financial year, would it be appropriate to recognise a significant risk in relation to the 2019-20 VFM arrangements conclusion.

We did not identify any significant risks in relation to these criteria



Section 5

Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

We are required to perform the procedures specified by the National Audit Office on the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes.

The Council is below the specified audit threshold of £500mn. Therefore, we were not required to perform any audit procedures on the consolidation pack

Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any areas of concern

Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.

Other Reporting Issues (cont'd)

Objections Received

We did not receive any objections to the 2019/20 financial statements from members of the public.

Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the Audit Committee on 20 October 2020. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

Our audit did not identify any controls issues to bring to the attention of the [Audit] Committee.

Section 6

Focused on your future

Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the Council is summarised in the table below.

Standard	Issue	Impact
IFRS 16 Leases	It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2021/22 financial year. Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet. There are transitional arrangements within the standard and although the 2020/21 Accounting Code of Practice for Local Authorities has yet to be updated, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.	Until the revised 2020/21 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area. However, what is clear is that the Council will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.

Section 8

Audit Fees

Audit Fees – revised proposed scale fee

We outlined in our audit plan the basis on which the scale fees are set by PSAA. We also outlined a combination of factors which mean that we do not believe the existing scale fees provide a clear link with both a public sector organisation's risk and complexity and therefore it endangers the sustainability of Local Audit in the future. Based on these factors, and in light of requests from PSAA to provide further detailed analysis we have estimated the impact on the Council as shown below.

We have shared the analysis below with officers and the Audit Committee, but as noted below these amounts are subject to the approval of PSAA.

Note the revised proposed scale fee does not include the impact of any specific requirements in relation to additional work in response to COVID-19, or other one off costs.

	Rationale for fee variation	Fee
Scale fee		38,572
Changes in risk profile	As a result of macro changes in the sector and the impact on the council in terms of the risks being faced, the decisions being made and the financial reporting of those, this in turn increases audit risk, as outlined in our audit plans, and we need to extend our procedures to address these.	8,102
Changes in regulatory environment	There has been a significant increase in the focus on areas of the financial statements especially where judgemental estimates are made. This is to address regulatory expectations from FRC reviews on the extent of audit procedures performed in areas such as the valuation of land and buildings and pension assets and liabilities. Our required procedures now entail higher samples sizes, increased requirements for corroborative evidence to support the assumptions and the increased use of specialists. We have also seen wider changes in the regulatory environment which all firms have needed to respond to. These include the various reviews, completed or ongoing, which all have a focus on audit quality and what is expected of external auditors. This has increased compliance and quality assurance costs which are now required for us to continue to provide services to the sector.	12,250
Revised Proposed Scale Fee		**58,924**

Audit Fees – additional 2019/20 cost

The below table analyses our proposed fee variations in relation to work done to address risks specific to 2019/20 brought about by either the advent of C-19 or changes in scope. The below fees are yet to be agreed with Officers or PSAA.

	Rationale for fee variation	Fee
Revised Proposed Scale Fee		58,924
Covid-19 – Increased Property valuation risk	Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty were included in the year-end valuation reports produced by the Authority's valuer. We considered that the material uncertainties disclosed by the valuer gave rise to an additional risk relating to the valuation of property and as a consequence increased the involvement of our specialist valuation team in this years audit.	4,510
Covid 19 – review of managements Going Concern assessment	Financial plans for 2020/21 and medium term financial plans needed revision for Covid-19. We considered the unpredictability of the current environment gave rise to a risk that the council would not appropriately disclose the key factors relating to going concern, underpinned by managements assessment with particular reference to Covid-19 and the Council's actual year end financial position and performance. We performed additional work which included; review of key documents, performed our own sensitivity analysis of management's forecast under both a base case and worst case scenario, reviewed the impact of managements forecasts position and the stressed tested scenarios on the Council's cash flow, consideration of proposed wording, associated documentation on audit file and review	2,718
Covid 19 – Cost of consultations – Professional Practice Directorate (PPD)	As a result of the uncertainties presented by C-19 on matters such as going concern and valuation of property assets, EY introduced an internal consultation process for all audit reports to ensure that the audit report being issued provided the right assurance to the reader of the accounts. This consultation is part of EY delivering a NAO Code compliant audit.	629
Additional work to audit the restatement of prior year figures	Additional work to audit the restatement of prior year figures in relation to the changes to the internal reporting structure which affected the Comprehensive Income and Expenditure Statement, the Expenditure and Funding Analysis and the related notes to the account.	1,197
Revised scale fee		67,978

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ED None

EY-000070901-01 (UK) 07/18. CSG London.

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Report to Audit Committee

16th December 2020

By the Director of Corporate Resources

INFORMATION REPORT

Not exempt

Annual Governance Statement – Review of Action Plan 2020/21

Executive Summary

The annual review of the Council's governance, risk management and internal control arrangements was completed in the spring leading to the production of the Annual Governance Statement for 2019/20. This review included information and assurance gathering processes to ensure that the published Annual Governance Statement was correct as well as a review of the Council's Governance Framework against the best practice framework devised by CIPFA/SOLACE. The Annual Governance Statement was approved at the Audit Committee on 15th July 2020.

This report reviews progress against the Action Plan at midway through the year. Appendix A shows the progress to date.

Recommendations

That the Committee is recommended:

i) To note the progress against the Annual Governance Statement Action Plan 2020/21.

Reasons for Recommendations

i) As part of good governance, it is important the improvement actions are reviewed, progressed and completed.

Background Papers: None

Wards affected: All

Contact: Dominic Bradley, Head of Finance and Performance.

Attachments:

Appendix A: AGS Action Plan 2020/21

Background Information

1 Introduction and Background

1.1 The Accounts and Audit (England) Regulations 2015 require the Council to review, at least annually, the effectiveness of its governance arrangements and publish an Annual Governance Statement.

1.2 Senior officers are consulted and supporting documentation provided to prepare the document. This report reviews progress against the 2019/20 Annual Governance Statement Action Plan.

2 Relevant Council Policy

2.1 The Audit Committee is responsible for approving the Annual Governance Statement in accordance with the Committee's terms of reference.

3 Details

3.1 The Annual Governance Statement - Action Plan 2020/21 is attached in Appendix A. This has been updated for progress to 25 November 2020.

4 Next Steps

4.1 The Committee is asked to note the progress against the Annual Governance Statement Action Plan 2020/21.

5 Outcome of Consultations

5.1 Key officers have been consulted when reviewing and updating the Annual Governance Statement Action Plan including the Senior Leadership Team and the Monitoring Officer.

6 Other Courses of Action Considered but Rejected

6.1 None.

7 Resource Consequences

7.1 There are resource consequences arising from this report.

8 Legal Consequences

8.1 Regulation 6 of The Accounts and Audit (England) Regulations 2015 requires that:-

6.—(1) A relevant authority must, each financial year—

(a) conduct a review of the effectiveness of the system of internal control required by regulation 3; and
(b) prepare an annual governance statement;

(2) If the relevant authority referred to in paragraph (1) is a Category 1 authority, following the review, it must—

(a) consider the findings of the review required by paragraph (1)(a)—

(i) by a committee; or
(ii) by members of the authority meeting as a whole; and

(b) approve the annual governance statement prepared in accordance with paragraph (1)(b) by resolution of—

(i) a committee; or
(ii) members of the authority meeting as a whole.

8.2 In 2016 CIPFA/SOLACE published a revised framework for Corporate Governance: "Delivering Good Governance in Local Government Framework". This framework provides a useful and practical update and follows seven core principles of good governance. The Framework urges local authorities to review and report on the effectiveness of the governance arrangements.

9 Risk Assessment

9.1 There are no risks associated with this report.

10 Other Considerations

10.1 This report has no effect on Crime & Disorder; Human Rights; Equality & Diversity or Sustainability.

4

APPENDIX A:

ANNUAL GOVERNANCE STATEMENT ~ ACTION PLAN 2020/21

No.	Area for Improvement	Actions	Responsible Officer	Target Date	Progress at 24 November 2020
1	Potential overlaps and conflicts between the Policy Development Advisory Groups and the Overview & Scrutiny Committee	Governance Committee to review the functions and make recommendations to Council for changes (if any)	Head of Legal & Democratic Services	31/3/21	The Review was commissioned by the Governance Committee at its October 2020 meeting and the research phase of the project is underway.
2	Mandatory governance training courses	Identify the courses needed, annual refresh and implement a refresh programme, reminders to be issued 31/03/20	Head of HR & OD	31/05/20	Complete
3	S151 and Monitoring Officer sign off for Cabinet decision reports on Modern.gov	Roll out of tracking and sign off through Modern.gov	Democratic Services Manager	31/3/20	Delayed by the Council's management restructure but training has been booked for the roll-out of this work during winter 2020/21.

Report to Audit Committee
16 December 2020
By the Director of Corporate Resources
INFORMATION REPORT

Not exempt

Treasury Management and Prudential Indicators mid-year report 2020/21

Executive Summary

This report covers treasury activity and prudential indicators for the first half of 2020/21. During the period the Council complied with its legislative and regulatory requirements and the statutory borrowing limit, the Authorised Limit, was not breached.

At 30 September 2020, the Council had no external debt and its investments totalled £53.6m (£42.9m at 30 September 2019).

During the first half of 2020/21, the Council's cash balances were invested in accordance with the Council's treasury management strategy apart from one breach of the limit for a single local authority. Interest of £0.43m was earned on investments at an average return of 1.7% (2.3% full year 2019/20).

Treasury investment income for the full year is likely to be significantly below the budget as the pandemic keeps interest rates and dividend yields low. Commercial property income is also likely to underperform as some tenants suffer from the fallout from the pandemic.

Recommendations

The Committee is recommended to:

i) Note the treasury management stewardship report at the mid-year 2020/21
ii) Note the mid-year prudential indicators for 2020/21

Reasons for Recommendations

i) This mid-year report is a requirement of the Council's reporting procedures
ii) This report meets the requirements of the relevant CIPFA Codes of Practice for Treasury Management and Prudential Indicators in Capital Finance.

Background Papers
"Capital Strategy 2020/21 incorporating Investment and Treasury Management Strategy" – Audit Committee 18 December 2019
"Budget 2020/21 and Medium Term Financial Strategy to 2023/24" – Cabinet 23 January 2020

Consultation: Arlingclose Limited. Council's Treasury management advisors
Wards affected: All
Contact: Julian Olszowka, Group Accountant, Technical 01403 215310

Background Information

1 Introduction

The purpose of this report

1.1 This report covers treasury management activity and prudential indicators for the first half of 2020/21. It meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. The Council is required to comply with both Codes through Regulations issued under the Local Government Act 2003. The Code recommends that Members are informed of Treasury Management activities at least twice a year.

Background

1.2 In line with the CIPFA Prudential Code for Capital Finance in Local Authorities the Council adopts prudential indicators for each financial year and reports on performance relative to those indicators. This requirement is designed to show that capital spending is prudent, affordable and sustainable and that treasury practices adequately manage risk. The original indicators for 2020/21 together with Capital Strategy were approved by Council on 14 October 2020. The Capital Strategy including the Treasury Management Strategy 2020/21 had been recommended for approval by this Committee on 18 December 2019. The late approval of the strategy was an unfortunate procedural error.

1.3 The economic background to treasury management remains challenging with the pandemic adding to existing concerns over Brexit, indebtedness, productivity and growth weighing on the economy and financial system which has still not fully recovered from the 2008 financial crisis. Arlingclose Limited, the Council's treasury management advisors, have provided a commentary on the half-year so far in Appendix A.

Local Context

1.4 At the end of 2019/20 the Council's underlying need to borrow for capital purposes as measured by the Capital Financing Requirement (CFR) was £33.9m, while usable reserves and working capital which are the underlying resources available for investment were £73m. The Council had no borrowing and £39m of investments reflecting its use of internal resources rather than borrowing in order to reduce risk and keep interest costs low.

1.5 On 30 September 2020, the Council had no borrowing and investments of £53.6m. Investment totals had fluctuated much more than usual as Covid-19 related grants flowed in and out of the Council. Short term rates collapsed to near zero in the period. With the large amounts of cash being held at times, the Council had to use the Government to invest its cash more than it would usually plan to. In a few instances the rate became negative although only by some hundredths of 1%.

1.6 Rates on offer for short term cash look like remaining effectively at zero for an extended period challenging any hope of significant short-term investment returns. A £2m investment in a multi-asset fund was undertaken in September 2020. The first dividend received was an income return of just under 3%.

2 Treasury management

Borrowing Activity

2.1 There was no borrowing in the period. No borrowing is envisaged in the second half of the year although the Council's balances will fall towards the end of the year as tax receipts are significantly front loaded.

Investment Activity

2.2 The treasury management position at 30 September 2020 is shown below. This is the month end position but the daily position can vary as a large portion of income comes in at the beginning of month to be distributed to precepting authorities a few days later.

	31.3.20 Balance £m	Movement £m	30.9.20 Balance £m	30.9.20 Rate %
Call accounts	0.5	3.5	4.0	0.1
Money Market Funds – call	5.5	9.0	14.5	0.2
Money Market Funds – cash plus or short bonds	9.3	0.1	9.4	0.9
Short-term deposits	4.0	-1.0	3.0	1.1
Pooled Funds - Property	4.8	-0.2	4.6	4.2
Pooled Funds – Multi-Asset	4.5	2.2	6.7	4.6
Pooled Funds – Equity	2.9	0.6	3.5	3.3
Pooled Funds – Bonds	5.5	0.4	5.9	2.6
REIT	2.0	0.0	2.0	1.3
Total Investments	39.0	14.6	53.6	1.7

2.3 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

2.4 Investment income on an accrued basis in the period was £0.43m which just below the budget of £0.44m. The average return was 1.7% below the budgeted figure of 2.1%. Average cash balances were more than those in the budget but the excess cash doesn't increase returns with rates effectively at zero. Although the Council's revenue income was depressed by pandemic effects the receipt of Covid-19 grant monies and a slowdown in capital spend more than compensated.

2.5 The returns in the second half of the year are expected to be severely reduced by cash rates close to zero and dividends squeezed by the pandemic's effect on the economy. The outturn position on income is expected to be £150,000 below budget. That said the recent news on vaccines may bring a favourable movement in dividend income as companies become less defensive but it is still too early to rely on that happening.

2.6 Given the risk and low returns from short-term unsecured bank investments, the Council has reduced its exposure to them except through well diversified money market funds or call accounts. Otherwise the Council has used local authorities and central government alongside strategic pooled funds. These strategic pooled funds, comprising equity, bonds and property, are a key part of the strategy. As can be seen from the table above they are a significant contributor to overall income.

2.7 Pooled funds asset values though can be volatile in the short term. The market crash in March 2020 caused by the Covid-19 pandemic left values down £1.9m at the end of 2019/20 relative to the purchase price. At the end of the first half of the year the value of these investments was recovering but was still £0.7m below the initial investment. The positive news about vaccines has buoyed up asset prices and the capital value loss is now below £0.2m. However, it should be remembered that these investments are longer term so any snapshot of capital gain or loss should not be overemphasised.

Compliance

2.8 The Director of Corporate Resources reports that all treasury management activities undertaken during the first half of 2020/21 complied with the CIPFA Code of Practice and the Treasury Management Strategy recommended by this Committee with the exception of one breach of the local authority limit.

2.9 As mentioned in the 2019/20 end of year treasury management report to this committee on 15 July 2020, there was a breach on the first day of 2020/21 when an investment of £5m was made with a local authority while the relevant limit was £4m. It was due to a misreading of limits during the early days of remote working when the Council was having to deal with abnormal amounts of cash being routed through the Council for emergency grants. The investment was returned without any issue in May 2020.

2.10 The background to the investment was that the Council was receiving a payment of £29m on 1 April 2020 on top of its normal Council Tax and NNDR inflows. This meant investing just under £40m on the day. With many of the traditional counterparties seen as too risky, the use of local authorities became more prominent. The Council had invested in local authorities before but in £1m to £2m amounts. With the amount of money having to be invested, larger deals were necessary. In the pressured situation of finding counterparties, a deal was done at £5m when the limit was £4m due to a mix up as to which limits referred to which type of investment, not helped by the fact that staff had just started working from home using conferencing software for the first time.

2.11 The investment was repaid on 5 May 2020. Although in breach of the limit, the risk of the default of the counterparty was judged to be minimal. Local authorities are seen as very secure investments with extremely small risk attached. Added to that, the timescale of the investment was one where central government was providing a large cash injection to the sector and the failure of any council at that time would have been unthinkable from the perspective of central government.

2.12 Security of capital has remained the Council's main investment objective. Key to this is the counterparty policy as set out in its treasury management strategy. Counterparty credit quality was assessed and monitored with reference to credit

ratings, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

Treasury Management Indicators

2.13 The Council measures and manages its exposures to treasury management risks using the following indicators.

2.14 **Security benchmark** – The Council set a security benchmark rating of A, which is the average credit rating for the investment portfolio. The average rating was at above the benchmark at either A+ or AA- during the first half of the year.

2.15 **Liquidity benchmark** – The Council sets a benchmark to maintain a minimum of liquidity. The benchmark set was that £3m is available within a rolling three-month period without additional borrowing. The Director of Corporate Resources can report that liquidity arrangements were well within benchmark during the year to date with overnight cash alone not falling below £9m.

Compliance with Prudential Indicators

2.16 The Council can confirm compliance with its Prudential Indicators for 2020/21, which were set out in the Council's Treasury Management Strategy.

Treasury Management Indicators

2.17 **Interest rate exposures** - This indicator is set to control the Council's exposure to interest rate risk. The exposures to variable rate interest rates is quantified by the one-year revenue impact of a 1% rise or fall in interest rates. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates. This indicator is close to its limits as cash balances in money markets funds are much larger than normally planned as a result of the cash held significantly exceeding the projected cash balances and opportunities to invest for a meaningful return being very limited. It is worth noting that the possibility of a 1% change in interest rates in the short term is very low.

Interest rate risk indicator - Upper limit	Limit	Actual	Complied
One-year revenue impact of a 1% rise	£0.2m	£0.19m	✓
One-year revenue impact of a 1% fall	£0.2m	£0.19m	✓

2.18 **Principal sums invested for periods longer than 364 days** – The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its long-term investments. There was no investments for more than 364 days so the Council was well within the indicator set:

	Original Indicator	Maximum Position
Maximum principal sums invested > 364 days	£12m	£0m

3 **Prudential Indicators 2020/21**

3.1 The Local Government Act 2003 requires the Council to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much it can afford to borrow. The objectives of the Prudential Code are to ensure that capital investment plans are affordable, prudent and

sustainable. To demonstrate that the Council meets these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

3.2 **The Council's Capital Expenditure and Financing 2020/21 -** This is one of the required prudential indicators and shows total capital expenditure for the year and how this is financed. The estimated indicator is shown below.

2020/21	Original estimate £m	Current projection £m
Total capital expenditure	18.4	6.5
Resourced by:		
External Resources	5.5	2.5
Internal Resources	7.7	2.2
Debt	5.2	1.8
Total financing	18.4	6.5

3.3 The estimated capital spend in 2020/21 is well under the original budget with financing similarly lower than expected. The original indicator had £3.5m included for leases under accounting rule changes that were postponed. The capital programme was then pared down by £7.2m in a report to cabinet on 23 July 2020 dealing with the pandemic's effect.

3.4 **The Council's overall borrowing need -** The Council's underlying need to borrow is termed the Capital Financing Requirement (CFR). It represents the accumulated net capital expenditure which has not been financed by revenue or other resources. Part of the Council's treasury activities is to address this borrowing need, either through borrowing from external bodies, or utilising temporary cash resources within the Council.

3.5 The Council is required to make an annual revenue charge, the Minimum Revenue Provision (MRP), to reduce the CFR – effectively a repayment of the borrowing need. The Council's 2020/21 MRP Policy was approved on 12 February 2020 within the 2020/21 Budget report.

3.6 The Council's CFR for the year is shown below, and represents a key prudential indicator. The current projection is much less than the original estimate because the projected unfinanced capital spend is much lower than the original. No increase in long-term borrowing is projected in this financial year.

Capital Financing Requirement and External Debt Year end 2020/21	Original estimate £m	Current projection £m
CFR	39.5	34.8
External debt	0	0

3.7 External borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2020/21 and next two financial years. No difficulties are envisaged for the current or future years in complying with this Prudential Indicator as no long-term borrowing is currently planned.

3.8 **Borrowing limits** - The Council approved these Prudential Indicators as part of the 2020/21 Budget report.

3.9 **Operational boundary for external debt:** The operational boundary is the Council's estimate of most likely, but not worst case scenario for external debt.

3.10 **Authorised limit for external debt:** The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Council can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

	Limit	Actual	Met?
Operational boundary – borrowing	£0m	£0m	✓
Operational boundary – other long-term liability	£4m	£0m	✓
Operational boundary – **TOTAL**	**£4m**	**£0m**	✓
Authorised limit – borrowing	£15m	£0m	✓
Authorised limit – other long-term liability	£6m	£0m	✓
Authorised limit – **TOTAL**	**£21m**	**£0m**	✓

3.11 **The ratio of financing costs to net revenue stream -** This indicator identifies the trend in the cost of capital (financing costs net of interest and investment income) against the net revenue stream. The indicator for the year was 2%. Based on current estimates the ratio is expected to be 1% for the year.

4 Non-Treasury Investments

4.1 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

4.2 The Council has a significant directly owned property portfolio valued at £55m at the end of 2019/20. The original investment strategy set £3.8m as the income net of direct costs figure from the property portfolio and the present forecast is £3.6m. The final income figure is uncertain because of the effects of the pandemic. The Head of Property and Facilities is engaging with tenants who may be affected and the final income figure will depend on the outcome of discussions.

4.3 There are a number of other indicators that were set for the year that cannot be definitively calculated until the end of the year when the accounts are closed and all relevant income and expenditure is accrued and central expenses are apportioned across all the Council's services. Some indicators can estimated as a snap shot from property records and the table below shows the original estimated indicators and the latest projections.

Indicator	Estimate	Latest
Average Vacancy levels	1%	3%
Tenant over 5%	5	5
Weighted Average Unexpired Lease Term	9yr	9yr
Bad debts written off	£10,000	£200,000

4.4 A number of indicators for the investment properties require the end of year value of properties. A valuation of all properties is carried out at year end as a part of the final accounts. Valuations have been affected by the uncertainty caused by the pandemic and this may still affect the values at 31 March 2021 which is the year end date.

4.5 The Council has one small loan (£0.3m) to a community run leisure centre. The centre has been given a year's payment holiday in its repayments as it has been heavily affected by the pandemic. It is expected to recommence payment in 2021/22 and no increase in the expectation of any credit loss is envisaged. The interest income of £7,000 will not be paid this year but the unpaid interest will be wrapped up into future interest payments.

4.6 No other loan has been made against the overall limit of £1.5m. It was expected there would be loans to the Council's housing company this year. None were made in the first half of the year and none is expected to be made in the rest of the year. The initial planning and preparation of sites have taken longer than expected. This is a new venture for the Council and the pandemic has also slowed progress.

4.7 The Council has a limit on share investment of £0.5m. Equity investment of £60,000 has been made in the half year and the forecast is for £60,000 more equity investment to be made before the end of the financial year.

5 Staffing consequences

5.1 There are no direct staff resourcing consequences. However, the risks in the investment environment highlights the continuing need for staff training and staff will take advantage of courses run by its advisors Arlingclose Limited.

6 Financial consequences

6.1 Interest earned in 2020/21 is projected to be £0.78m, which is £0.15m under budget of £0.93m. MRP is projected at £0.88m which is £0.05m under budget of £0.93m.

7 Other considerations

7.1 There are no consequences of any action proposed in respect of Risk; Crime & Disorder; Human Rights; Equality & Diversity and Sustainability.

Appendix A

Economic background to the midpoint of 2020/21

Economic background: The spread of the coronavirus pandemic dominated the period as countries around the world tried to balance containing the virus and getting their populations and economies working again. After a relatively quiet few months of Brexit news it was back in the headlines towards the end of the period as agreement between the UK and EU on a trade deal was looking difficult and the government came under fire, both at home and abroad, as it tried to pass the Internal Market Bill which could override the agreed Brexit deal, potentially breaking international law.

The Bank of England (BoE) maintained Bank Rate at 0.1% and its Quantitative Easing programme at £745 billion. The potential use of negative interest rates was not ruled in or out by BoE policymakers, but then a comment in the September Monetary Policy Committee meeting minutes that the central bank was having a harder look at its potential impact than was previously suggested took financial markets by surprise.

Government initiatives continued to support the economy, with the furlough (Coronavirus Job Retention) scheme keeping almost 10 million workers in jobs, grants and loans to businesses and 100 million discounted meals being claimed during the 'Eat Out to Help Out' (EOHO) offer.

GDP growth contracted by a massive 19.8% (revised from first estimate -20.4%) in Q2 2020 (Apr-Jun) according to the Office for National Statistics, pushing the annual growth rate down to -21.5% (first estimate -21.7%). Construction output fell by 35% over the quarter, services output by almost 20% and production by 16%. Recent monthly estimates of GDP have shown growth recovering, with the latest rise of almost 7% in July, but even with the two previous monthly gains this still only makes up half of the lost output.

The headline rate of UK Consumer Price Inflation (CPI) fell to 0.2% year/year in August, further below the Bank of England's 2% target, with the largest downward contribution coming from restaurants and hotels influenced by the EOHO scheme. The Office for National Statistics' preferred measure of CPIH which includes owner-occupied housing was 0.5% y/y.

In the three months to July, labour market data showed the unemployment rate increased from 3.9% to 4.1% while wages fell 1% for total pay in nominal terms (0.2% regular pay) and was down 1.8% in real terms (-0.7% regular pay). Despite only a modest rise in unemployment over the period, the rate is expected to pick up sharply in the coming months as the furlough scheme ends in October. On the back of this, the BoE has forecast unemployment could hit a peak of between 8% and 9%.

The US economy contracted at an annualised rate of 31.7% in Q2 2020 (Apr-Jun). The Federal Reserve maintained the Fed Funds rate at between 0% and 0.25% but announced a change to its inflation targeting regime. The move is to a more flexible form of average targeting which will allow the central bank to maintain interest rates at low levels for an extended period to support the economy even when inflation is 'moderately' above the 2% average target, particularly given it has been below target for most of the last decade.

The European Central Bank maintained its base rate at 0% and deposit rate at -0.5%.

Financial markets: Equity markets recovered from March lows. The FTSE 100 and 250 have made up around half of their losses at the height of the pandemic in March. Central bank and government stimulus packages continue to support asset prices, but volatility remains.

Ultra-low interest rates and the flight to quality continued, keeping gilts yields low but volatile over the period with the yield on some short-dated UK government bonds remaining negative. The 5-year UK benchmark gilt yield started and ended the June–September period at -0.06% (with much volatility in between). The 10-year gilt yield also bounced around, starting at 0.21% and ending at 0.23% over the same period, while the 20-year rose from 0.56% to 0.74%. 1-month, 3-month and 12-month bid rates averaged 0.02%, 0.06% and 0.23% respectively over the period.

Credit background: Credit default swap spreads eased over most of the period but then started to tick up again through September. In the UK, the spreads between ring-fenced and non-ring-fenced entities remains, except for retail bank Santander UK whose CDS spread remained elevated and the highest of those we monitor at 85bps while Standard Chartered was the lowest at 41bps. The ring-fenced banks are currently trading between 45 and 50bps.

After a busy second quarter of the calendar year, the subsequent period has been relatively quiet for credit changes for the names on our counterparty list. Fitch assigned a AA- deposit rating to Netherlands lender Rabobank with a negative outlook and prior to that, while not related to our counterparty list but quite significant, revised the outlook on the US economy to Negative from Stable while also affirming its AAA rating.

There continues to remain much uncertainty around the extent of the losses banks and building societies will suffer due to the impact from the coronavirus pandemic and for the UK institutions on our list there is the added complication of the end of the Brexit transition period on 31st December and what a trade deal may or may not look like. The institutions on Arlingclose’s counterparty list and recommended duration remain under constant review, but at the end of the period no changes had been made to the names on the list or the recommended maximum duration of 35 days.

Report to Audit Committee

16 December 2020

By the Director of Corporate Resources

DECISION REQUIRED

Not exempt

Horsham District Council

Capital Strategy 2021/22 incorporating Investment and Treasury Management Strategy

Executive Summary

This report combines an overview of how capital expenditure, capital financing, treasury and other investment activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. The strategies set limits and indicators that embody the risk management approach that the Council believes to be prudent. The strategies are set against the mid-term financial strategy, the context of the UK economy and projected interest rates.

The report sets treasury investment criteria and limits which are largely unchanged with the exception of changes to the limits for money market funds and local authorities detailed in Appendix B.

- Limits on money market funds rises from £30m to £50m
- Limit on individual local authority goes from £4m to £5m

These changes follow advice from the Council's advisor and review of the risks inherent in the type of investment.

The investment strategy in section 5 and appendix C pulls together information on service loans and commercial property to demonstrate the Council's risk management approach in that area. The strategy is largely unchanged apart from recommended increases in the service loans and overall commercial property portfolio limits.

- The limit on service loans increases from £1.5m to £3m
- The limit on overall commercial property rises from £60m to £70m

The increase in loan value is to enable lending to the Council's own Housing Company and the overall portfolio limit increase to cover developments of existing assets and to provide headroom for possible upward revaluations of property values.

Recommendations

The Committee is asked to:

i) approve this Capital Strategy as an appropriate overarching strategy for the Council while leaving the full Council to approve the updated capital strategy that will accompany the 2021/22 budget to Council.

ii) recommend that the full Council approve the Treasury Management Strategy for 2021/22 and the associated limits and specific indicators included in section 4 and appendix B of this report.

iii) recommend that the full Council approve the Investment Strategy for 2021/22 and the associated limits and specific indicators included in section 5 and appendix C of this report.

Reasons for Recommendations

i) The Council is required to have regard to the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) and Prudential Code which requires the Council to approve a Capital strategy, Investment strategy and Treasury Management Strategy before the start of each financial year.

ii) The Ministry for Housing Communities and Local Government (MHCLG) issued revised guidance on local authority investments in 2017 that the Council is required to have regard to.

Background Paper
"Update on the Council's financial position" – Cabinet 26 November 2020

Consultation: Arlingclose Limited

Wards affected: All

Contact: Julian Olszowka, Group Accountant, Technical, 01403 215310

Background Information

1 Introduction

The purpose of this report

1.1 This report covers the requirements of Codes and guidance that the Council must, by statue, have regard to. Section 3 gives a high-level overview of:

- how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services
- how associated risk is managed and;
- the implications for future financial sustainability.

1.2 The Treasury Management Strategy in section 4 covers the aspects of investments that this Committee has historically considered. It covers management of the Council's cash flows, borrowing and investments, and the associated risks.

1.3 The Investment Strategy in section 5 is a requirement introduced for 2019/20 and covers investments held for service purposes or for commercial yield. The changes to guidance were designed to bring together areas which CIPFA and MHCLG consider should be regarded in the round. They were also a response to the increasing commercialisation of local government and especially the increasing investment in commercial property.

1.4 The guidance requires the Capital and Investment Strategies to be approved by the full Council while the Treasury Management Strategy can now be approved by a subcommittee of the Council. However, here we follow the Council's existing Constitution that this Committee recommends the Treasury Management Strategy be approved by the full Council.

2 Background

Economic background

2.1 The Council's strategies must take account of expectations for the economy and specifically the finance sector. The Council receives advice on this from its advisors Arlingclose Ltd. Appendix A is a commentary by them on the current economic background, the outlook for creditworthiness and interest rates.

2.2 The forecast for the Bank Rate is that it remains at current levels in the medium term. For the purpose of the interest budget, any new investments are estimated to be on or about the Bank Rate.

2.3 The treasury management environment remains difficult with yields and quality counterparties which were first reduced in the fallout from the 2008 financial crisis being further depressed by worries around Brexit and the Covid-19 pandemic. Governments and regulators have put in place measures prompted by the financial crisis that restrict any government bail-out of individual financial institutions. This means an institution in difficulty may have to use its own resources and its deposits to continue to operate, exposing any depositor's

capital. At the moment the Council's advisers have recommended avoiding almost all financial institutions for any period apart from the short term.

Statutory background

2.4 This report is part of the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the Ministry for Housing, Communities and Local Government (MHCLG) Guidance.

2.5 The regulatory background has been complicated by the revision by both CIPFA and MHCLG codes and guidance. Both CIPFA and the MHCLG state they do not seek to prescribe precisely how councils invest but they clearly have concerns that some councils are taking increasing commercial risks using borrowed money. This approach means that Members are asked to look at a more extensive strategy so that more of the risks that the Codes and guidance highlight are apparent to Members.

Relevant Council policy

2.6 The Council's constitution requires that the Council approve Prudential Code indicators and Treasury Management Strategy. The Investment Strategy covering commercial property has been split from the traditional Treasury Management Strategy here for ease of understanding as it deals with a different type of investment but it can be considered to be encompassed in the definition of the Treasury Management Strategy as used by the Constitution.

2.7 The existing strategies and Prudential indicators were approved by the Council on 14 October 2020 the former having been recommended for adoption by this Committee on 18 December 2019. The late approval of the strategy was an unfortunate procedural error.

3 Capital Expenditure and Financing

3.1 Capital expenditure is where the Council spends money on assets, such as property or vehicles that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing or leasing).

3.2 Service managers bid annually in October to include projects in the Council's capital programme. Bids are collated by Finance who calculate the financing cost (which can be nil if the project is fully externally financed). The Senior Leadership Team appraises all bids based on a comparison of service priorities against financing costs and makes recommendations to the informal cabinet. The final capital programme is then presented to Cabinet in January and to Council in February each year.

3.3 The current projected capital programme and financing is shown below. It includes current estimates for capital bids for 2021/22 and beyond. The use of reserves is in line with the Update on the Council's Financial Position report to

the Cabinet of 26 November 2020. It will be revised if necessary as the 2021/22 budget process develops and the final figures that appear alongside the Budget in February 2021 will constitute one of the prudential indicators required by the CIPFA Prudential Code.

£millions	2019/20 Actual £000	2020/21 Estimate £000	2021/22 Estimate £000	2022/23 Estimate £000	2023/24 Estimate £000
Projected Capital Expenditure	9.9	6.5	6.6	9.9	8.7
Financed by:					
External resources	3.1	2.5	3.4	4.2	6.0
Internal Resources *	5.3	2.2	2.5	3.7	2.7
Debt	1.5	1.8	0.7	2.0	0.0
Total Financing	9.9	6.5	6.6	9.9	8.7

* Includes use of New Homes Bonus

3.4 The term 'Debt' used above does not automatically lead to external borrowing as the Council may be able to use cash it holds in reserves and as working capital which is usually termed 'internal borrowing'. Over time all debt whether it be internal or external borrowing must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). The Council is required to make an annual MRP statement and this will be included in the Budget report in January 2021 and the methodology will be on the same basis as 2020/21. The current planned MRP payments are as follows:

£millions	2019/20 actual	2020/21 forecast	2021/22 budget	2022/23 budget	2023/24 budget
MRP	0.84	0.9	0.9	0.9	1.0

3.5 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and any capital receipts used to replace debt. The CFR is expected to reduce marginally during 2021/22. The Council's estimated CFR is projected as follows:

£millions	31.3.2020 actual	31.3.2021 forecast	31.3.2022 budget	31.3.2023 budget	31.3.2024 budget
CFR	33.9	34.8	34.5	35.5	34.5

3.6 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets. Repayments of capital grants, loans and investments also generate capital receipts. Loans repaid below are estimates of those from the Council's Housing Company. The Council projects capital receipts as follows:

£millions	2019/20 actual	2020/21 forecast	2021/22 estimate	2022/23 estimate	2023/24 estimate
Asset sales	1.7	1.1	1.8	2.4	0.8
Loans repaid	0.0	0.0	0.0	0.9	1.4
TOTAL	**1.7**	**1.1**	**1.8**	**3.3**	**2.2**

4 Treasury Management

4.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

4.2 **Borrowing strategy**: The Council has no plans to borrow but could find itself in a position which calls for borrowing. In that circumstance the main objectives when borrowing would be to achieve a low but certain cost of finance while retaining flexibility. These objectives are often conflicting, and the Council therefore would seek to strike a balance between cheap short-term loans (currently available effectively at zero) and long-term fixed rate loans where the future cost is known but higher (currently about 2%).

4.3 Projected levels of the Council's total outstanding debt are shown below, compared with the Capital Financing Requirement. Statutory guidance is that debt should remain below the Capital Financing Requirement, except in the short-term. As can be seen from the table the Council expects to comply with this in the medium term.

£millions	31.3.2020 actual	31.3.2021 forecast	31.3.2022 budget	31.3.2023 budget	31.3.2024 budget
Debt	0	0	0	0	0
CFR	33.9	34.8	34.5	35.5	34.5

4.4 The table above demonstrates that the Council is relying on internal borrowing i.e. using reserves and other cash resources that it holds rather than borrowing from external sources. From projections of the capital programme and use of reserves this strategy is seen as sustainable in the medium term although the Director of Corporate Resources will monitor the actual position against the projections in order to be ready to respond should external borrowing become advisable.

4.5 **Affordable borrowing limit**: Irrespective of plans to borrow or not the Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the

limit. Although no borrowing is planned, limits are set in case a need develops. Further details on borrowing are in appendix B.

£millions	2020/21 limit	2021/22 limit	2022/23 limit	2023/24 limit
Authorised limit – borrowing	15	15	15	15
Authorised limit – leases	6	6	6	6
Authorised limit – total external debt	21	21	21	21
Operational boundary – borrowing	0	0	0	0
Operational boundary – leases	4	0	0	0
Operational boundary – total external debt	4	0	0	0

4.6 **Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management and will be dealt with in the Investment Strategy in section 5 and Appendix C.

4.7 The Council's policy on treasury investments is to prioritise security and liquidity over yield that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice. The future longer term investments in the table below are strategic pooled funds that the council intends to hold for the longer term although they can be sold if required.

	31.3.2020 actual	31.3.2021 forecast	31.3.2022 estimate	31.3.2023 estimate	31.3.2024 estimate
Near-term investments	19	8	10	11	10
Longer-term investments	20	22	22	22	22
TOTAL	**39**	**30**	**32**	**33**	**32**

4.8 The projections show cash balances at year-end, which is a cash low point, in the region of £30m in the medium term. The Capital programme no longer features major projects while developers' contributions and New Homes Bonus flow in faster than they are spent. The New Homes Bonus projection used follows that in the 2020/21 Budget Report. Further detail on treasury investments are in Appendix B including limits and indicators which the Committee is asked to consider. The significant changes compared to last year's limits are an increase in limits on money market funds from £30m to £50m and on local authorities from £4m to £5m. More detail on the justification is in Appendix B.

4.9 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Corporate Resources and staff, who must act in line with the Treasury Management Strategy as

approved by the Council following this committee's scrutiny and recommendation. The Audit Committee receives a mid-year and full year report and is responsible for scrutinising treasury management decisions.

5 Investment Strategy (loans, shares and property)

5.1 This section is the disclosure required in 2019/20 by CIPFA and MHCLG guidance. Both bodies have concerns over the increasing risks that they see in the sector as councils have become more commercial and made large commercial property purchases.

Investments for Service Purposes

5.2 The Council has the ability to make investments to assist local public services, including making loans to local service providers and buying shares and making loans to any Council subsidiaries that provide services. In light of the public service objective, the Council is willing to take more risk than with treasury investments. However it still plans for such investments to generate a profit after all costs to offset risk. Further details on service investments are in appendix C. the overall limits are £3m on the total exposure to loans for service purposes and £0.5m exposure permitted for shares being held. The former is an increase from this year's £1.5m reflecting the expected activity of the Council's housing company.

5.3 **Governance:** Decisions on service investments are made by the full Council after the relevant Head of Service has submitted a comprehensive analysis in consultation with the Director of Corporate Resources and must meet the criteria and limits. Most loans and shares are capital expenditure and will therefore also be approved as part of the capital programme in the Budget report or by full Council.

Commercial Activities

5.4 With central government financial support for local public services declining, the Council invests in commercial property purely or mainly for financial gain. Total commercial investments were valued at £55m on 31 March 2020. These provide a net return after direct costs of just under 7% based on the last set of final accounts which value the assets at market value rather than historical value.

5.5 As financial return is the main objective, the Council recognises the higher risk on commercial investment compared with treasury investments. The principal risk exposures include individual vacancies, falls in market value, changes in the overall and local economy. Individual property risks are constantly monitored and managed by the Head of Property and Facilities. Should income not meet expectations the Council holds at least £6m of general reserves available to balance the revenue budget in the short term while the Head of Property and Facilities reviews the performance of the portfolio.

5.6 In order that commercial investments remain proportionate to the financial capacity of the Council, these are subject to an overall maximum investment limit which is to be set at £70m which is an increase on this year's £60m. The increase is required to give the Council some headroom as the current value of

£55m will be added to by small developments to existing properties and the revaluation at year-end could increase asset values generally.

5.7 **Governance:** Decisions on new commercial investments are made by the Cabinet after consideration by the Policy Development Advisory Group for Finance & Assets in line with the criteria and limits approved by the Council in this strategy. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme. Further details on commercial investments and limits on their use are in appendix C.

Other Liabilities

5.8 The Council has set aside £1.1m to cover risks of Business Rates Appeals. The Council is also at risk of having to pay for historic insurance claims but has not put aside any money because there is no reasonable assessment of the amount required.

5.9 **Governance:** Decisions on incurring new discretionary liabilities are taken by the relevant director in consultation with the Director of Corporate Resources. If significant these would be discussed at the quarterly corporate risk management meeting and final decisions as to recognition taken by the Director of Corporate Resources. New liabilities exceeding £1m are reported to full Council for approval or notification as appropriate. Further details on liabilities are in note 18 of the 2019/20 statement of accounts.

Revenue Budget Implications

5.10 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants. Because the Council has no debt and significant investment income the financing costs are very low.

	2019/20 actual	**2020/21 forecast**	**2020/21 budget**	**2021/22 budget**	**2023/24 budget**
Financing costs (£m)	0.0	0.1	0.4	0.3	0.1
Proportion of net revenue stream	0%	1%	4%	3%	1%

5.11 **Sustainability:** Due to the long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 40 years into the future. The Director of Corporate Resources is satisfied that the proposed capital programme is prudent, affordable and sustainable because the net budget demand on the Council and the risks in the programme have been reviewed and fall within the Council's tolerances.

Knowledge and Skills

5.12 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Director of Corporate Resources and S151 Officer is a qualified accountant with over 30 years' experience and the Head of Property is a fellow of RICS with over 35 years' of experience in commercial property. The Council will support junior staff to study towards relevant professional qualifications.

5.13 Where Council staff do not have the knowledge and skills required, use is made of external advisers that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers and for any significant property investment would use property consultants with specialist knowledge of the appropriate property sector. This approach ensues access to right knowledge and skills and can be more cost effective than employing such staff directly. The overarching requirement is that the Council has access to knowledge and skills commensurate with its risk appetite.

6 Other courses of action considered but rejected

6.1 The MHCLG Investment Guidance and the CIPFA Codes of Practice do not prescribe any particular strategies for local authorities to adopt. The above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below:

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses will be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses will be smaller
Borrow additional sums at long-term fixed interest rates using less internal funds	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Invest more in service loans	Interest income will be higher and service benefits will accrue	Increased risk of losses from credit related defaults or service body being unable to pay loan and provide service
Reduce investment in property	Income will be lower	Lower chance of losses from non-paying tenants or falling property values.
Invest additional sums in property	income will be higher	Increased chance of losses from vacancies or falling property values. Reputational and regulatory risk if Council incurs large loss

7 Staffing consequences

7.1 There are no staffing consequences apart from the need for appropriate training.

8 Financial consequences

8 .1 The budgeted treasury investment income in 2021/22 is £0.79m (2020/21 £0.93m), which is equivalent to an average investment portfolio of £49m at an interest rate of 1.6%. The decline is a consequence of almost zero cash returns and depressed pooled fund dividends. The budget for debt interest paid in 2021/22 is £5,000 which is a contingency for possible short term borrowing. The budget for commercial property net income is £3.6m which is a yield of 6.3% from an investment portfolio of £56m. Income in 2021/22 is expected to be squeezed by the effects of the pandemic.

9 Other considerations

9.1 Risks such as security of funds, liquidity, and interest rate risk are considered in the report. There are no consequences of any action proposed in respect of Crime & Disorder; Human Rights; Equality & Diversity and Sustainability.

Appendix A Economic background and interest rate forecast

Economic background

The impact on the UK from coronavirus, together with its exit from the European Union and future trading arrangements with the bloc, will remain a major influence on the Authority's treasury management strategy for 2021/22.

The Bank of England (BoE) maintained Bank Rate at 0.10% in November 2020 and also extended its Quantitative Easing programme by £150 billion to £895 billion. The Monetary Policy Committee voted unanimously for both, but no mention was made of the potential future use of negative interest rates. Within the latest forecasts, the Bank expects the UK economy to shrink -2% in Q4 2020 before growing by 7.25% in 2021, lower than the previous forecast of 9%. The BoE also forecasts the economy will now take until Q1 2022 to reach its pre-pandemic level rather than the end of 2021 as previously forecast.

UK Consumer Price Inflation (CPI) for October 2020 registered 0.6% year on year, up from 0.2% in the previous month. Core inflation, which excludes the more volatile components, rose to 1.3% from 0.9%. The most recent labour market data for the three months to August 2020 showed the unemployment rate rose to 4.5% while the employment rate fell to 75.6%. Both measures are expected to deteriorate further due to the ongoing impact of coronavirus on the jobs market, particularly when the various government job retention schemes start to be unwound in 2021, with the BoE forecasting unemployment will peak at 7.75% in Q2 2021. In August, the headline 3-month average annual growth rate for wages were 0% for total pay and 0.8% for regular pay. In real terms, after adjusting for inflation, total pay growth fell by -0.8% while regular pay was up 0.1%.

GDP growth fell by -19.8% in the second quarter of 2020, a much sharper contraction from -2.0% in the previous three months, with the annual rate falling -21.5% from -1.6%. All sectors fell quarter-on-quarter, with dramatic declines in construction (-35.7%), services (-19.2%) and production (-16.3%), and a more modest fall in agriculture (-5.9%). Monthly GDP estimates have shown the economy is recovering but remains well below its pre-pandemic peak. Looking ahead, the BoE's November Monetary Policy Report forecasts economic growth will rise in 2021 with GDP reaching 11% in Q4 2021, 3.1% in Q4 2022 and 1.6% in Q4 2023.

Credit outlook

After spiking in late March as coronavirus became a global pandemic, credit default swap (CDS) prices for the larger UK banks have steadily fallen back to almost pre-pandemic levels. Although uncertainly around COVID-19 related loan defaults lead to banks provisioning billions for potential losses in the first half of 2020, drastically reducing profits, reported impairments for Q3 were much reduced in some institutions. However, general bank profitability in 2020 is likely to be significantly lower than in previous years.

The credit ratings for many UK institutions were downgraded on the back of downgrades to the sovereign rating. Credit conditions more generally though in banks and building societies have tended to be relatively benign, despite the impact of the pandemic.

Looking forward, the potential for bank losses to be greater than expected when government and central bank support starts to be removed remains a risk, as does the

UK not achieving a Brexit deal, suggesting a cautious approach to bank deposits in 2021/22 remains advisable.

Interest rate forecast:

The Authority's treasury management adviser Arlingclose is forecasting that BoE Bank Rate will remain at 0.1% until at least the end of 2023. The risks to this forecast are judged to be to the downside as the BoE and UK government continue to react to the coronavirus pandemic and the Brexit transition period ends. The BoE extended its asset purchase programme to £895 billion in November while keeping Bank Rate on hold. However, further interest rate cuts to zero, or possibly negative, cannot yet be ruled out but this is not part of the Arlingclose central forecast.

Gilt yields are expected to remain very low in the medium-term while short-term yields are likely remain below or at zero until such time as the BoE expressly rules out the chance of negative interest rates or growth/inflation prospects improve. The central case is for 10-year and 20-year to rise to around 0.5% and 0.75% respectively over the time horizon. The risks around the gilt yield forecasts are judged to be broadly balanced between upside and downside risks, but there will almost certainly be short-term volatility due to economic and political uncertainty and events.

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
Official Bank Rate													
Upside risk	0.00	0.00	0.00	0.15	0.15	0.15	0.15	0.30	0.30	0.30	0.30	0.30	0.30
Arlingclose Central Case	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Downside risk	-0.10	-0.20	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
3-month money market rate													
Upside risk	0.05	0.05	0.05	0.10	0.10	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30
Arlingclose Central Case	0.10	0.10	0.15	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
Downside risk	-0.40	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
5yr gilt yield													
Upside risk	0.40	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70
Arlingclose Central Case	0.00	0.00	0.05	0.10	0.15	0.15	0.20	0.20	0.25	0.25	0.25	0.25	0.25
Downside risk	-0.30	-0.40	-0.50	-0.55	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60
10yr gilt yield													
Upside risk	0.40	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70
Arlingclose Central Case	0.30	0.30	0.35	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.55	0.55	0.55
Downside risk	-0.30	-0.40	-0.50	-0.55	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
20yr gilt yield													
Upside risk	0.40	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70
Arlingclose Central Case	0.70	0.70	0.70	0.75	0.75	0.75	0.80	0.80	0.85	0.85	0.85	0.85	0.85
Downside risk	-0.20	-0.20	-0.25	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30
50yr gilt yield													
Upside risk	0.40	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70
Arlingclose Central Case	0.60	0.60	0.60	0.65	0.65	0.65	0.70	0.70	0.75	0.75	0.75	0.75	0.75
Downside risk	-0.20	-0.20	-0.25	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%

Appendix B Treasury Management Strategy

Mid year position and forecast

1 On 30 September 2020 the Council held no borrowing and £53.6m of investments at market value; broken down as follows:

	Principal £m	Interest Rate %
Call accounts	4.0	0.1
Money Market Funds – call	14.5	0.2
Money Market Funds – cash plus or short bonds	9.4	0.9
Short-term deposits	3.0	1.1
Pooled Funds - Property	4.6	4.2
Pooled Funds – Multi-Asset	6.7	4.6
Pooled Funds – Equity	3.5	3.3
Pooled Funds – Bonds	5.9	2.6
REIT	2.0	1.3
Net Investments	**53.6**	**1.7**

2 Taking the forecasts within the capital strategy, the balance sheet of the Council can be projected to estimate the amounts available for investments. Below is the current projected analysis of the balance sheet to illustrate the trajectory of the Council's funds.

All figures at year-end £m	**Actual 19/20**	**Estimate 20/21**	**Estimate 21/22**	**Estimate 22/23**	**Estimate 23/24**
CFR	33.9	34.8	34.5	35.5	34.5
Less external borrowing	0	0	0	0	0
Internal borrowing	33.9	34.8	34.5	35.5	34.5
Useable reserves, receipts, contributions held	63.3	55.6	57.5	59.6	57.0
Working capital/other balances	9.5	9.6	9.6	9.7	9.7
Estimated Investments	38.9	30.4	32.6	33.8	32.2

3 The Council's strategy has been to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing. In spite of the continuation of this, the Council is projected to hold significant investment balances even at the end of the financial year which is the low point for cash.

Borrowing Strategy

4 As shown above the Council is not expecting to borrow long term funds although it may need short term borrowing if short term cash flow issues require it.

5 **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board
- Any institution approved for investments (see below)
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except West Sussex County Council Pension Fund)
- Capital market bond investors
- UK Municipal Bond Agency and other special purpose companies created to enable joint local authority bond issues.

6 In addition, capital finance may be raised by the use of leases and hire purchase that are not borrowing, but may be classed as other debt liabilities.

7 The Council has previously raised its long-term borrowing from the PWLB. The government increased PWLB rates by 1% in October 2019 making it a relatively expensive option. On 25 November HM Treasury revised PWLB rates to 0.8% over relevant gilt rate. However, at the same time restrictions were introduced as to the access to PWLB if a council was planning what the Treasury term 'debt for yield'. This could restrict the Council's access to PWLB. In the event longer term borrowing is required the Council would consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code.

8 **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds and lend the proceeds to local authorities. This will be a more complicated than the PWLB due to the need for the Council to provide some degree of guarantee to bond investors and the long lead times. Any decision to use the Agency will therefore be the subject of a separate report to full Council.

9 Short-term and variable rate loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

Investment Strategy

10 The Council holds significant funds, representing income received in advance of expenditure plus balances and reserves held. In the past year, the Council's total investments have ranged between £34m and £82m and although the level of reserves is expected to reduce in the longer term, there will still be significant short to medium-term cash flow surpluses leading to larger sums being held than the

core reserves of the Council would indicate. The current projections show year-end balances in the region of £30m for the next three years.

11 Both the CIPFA Code and the MHCLG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

12 **Negative interest rates:** It is possible that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

13 Given the increased risk and very low returns from unsecured bank investments, the Council will continue to move away from them into more secure and/or higher yielding asset classes during 2021/22 continuing the present strategy that has moved investment into pooled funds and other local authorities.

14 **Business models:** Under the IFRS9 standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows rather than buying and selling investments and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

15 **Approved counterparties**: The Council may invest with any of the counterparty types in the table below; subject to the cash limits (per counterparty) and the time limits shown (changes from 20/21 limits are in bold):

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities	10 years	**£5m**	Unlimited
Governments and government entities rated A- and above	5 years	£4m	Unlimited
Secured investments rated AA and above	5 years	£4m	Unlimited
Secured investments rated A- to A+	13 months	4m	Unlimited

Banks (unsecured) rated A and above	13 months	£2.5m	Unlimited
Banks (unsecured) rated A-	6 months	£2.5m	Unlimited
Building societies (unsecured)	13 months	£1m	£8m
Registered providers (unsecured) Rated A-and above	5 years	£4m	£8m
Registered providers unrated(unsecured)	3 years	£3m	
Money market funds	n/a	£5m	**£50m**
Strategic pooled funds – Property Investments	n/a	£5m	£7m
Strategic pooled funds – Equity, Bond and Diversified assets	n/a	£5m	£18m
Real estate investment trusts	n/a	£5m	£5m
Other Corporates rated A- and above*	1 year	£2.5m	£5m
Unrated corporates	5 years	£50,000	£2m

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

16 **Credit Rating**: Investment limits are set with reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

17 **Government**: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

18 **UK Local Authority:** The Council will consider investments with a UK local government body up to £5m for up to 10 years. The Council is confident that as a sector local authorities are secure investments in the context of support from Central Government and the legal surcharging framework that guarantees debts will be paid. However, for any investment over six months the financial resilience of the relevant council will be assessed in consultation with the Council's advisor. This is an increase from £4m which has been the limit for a number of years. In view of the decreasing numbers of other counterparties the Council is likely to use the Local Authority market more frequently and dealing sizes of £5m are now quite common and give the Council access to a wider range of investment opportunities.

19 **Secured Investments**: Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.

20 **Banks Unsecured**: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

21 **Building Societies:** Although the regulation of building societies is no longer any different to that of banks the Council takes additional comfort from building societies' business model. The Council will therefore consider investing with unrated building societies where independent credit analysis shows them to be suitably creditworthy. A minimum asset size of £250m applies and limits of £1m per Society and £8m in total apply for unrated societies.

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

23 **Money market funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee.

24 Previously the Council's advisor had recommended a sector limit for money market funds which the Council had set at £30m. However, the advisor has reconsidered their advice and recommends that there is no need to have a sector limit as long as the Council takes care to diversify its liquid investments over a variety of providers to ensure access to cash at all times. The Council will relax the limit to £50m in response to the advice. The Council only uses funds from its advisor's recommended list and the list is regularly reviewed for appropriateness. The limits of £5m per fund remains.

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

26 **Real estate investment trusts (REIT):** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties. The Council will carry out a detail appraisal and take expert advice before any investment.

27 **Corporates**: Loans, bonds and commercial paper issued by companies other than banks and registered providers. Non-bank companies cannot be bailed-in but can become insolvent placing the Authority's investment at risk. Loans to unrated companies will only be made either following an external credit assessment or to a maximum of £50,000 per company as part of a diversified pool in order to spread the risk widely.

28 **Operational bank accounts:** The Council may incur exposure though its current accounts to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but still subject to the risk of a bank bail-in and balances will therefore be kept below £2.5m. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity. The Council currently banks with NatWest rated A.

29 **Risk Assessment and Credit Ratings:** Credit ratings are monitored by the Council's treasury advisors, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be ended at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty

30 Where a credit rating agency announces that a rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then no investments other than call investments will be made with that organisation until the outcome of the

review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

31 **Other Information on the Security of Investments**: 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 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 Council's credit rating criteria.

32 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected in credit ratings, but can be seen in other market measures. In those circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government or with other local authorities. This will reduce investment income earned, but will protect the principal sum invested.

33 **Investment limits**: The Council's revenue reserves available to cover investment losses were in the region of £16m on 31 March 2020 well above the stated minimum long term target of £6m. In order that no more than 2/3 of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government or Local Authority) will be £4m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, and foreign countries as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Category	Cash limit
Any group of organisations under the same ownership	£4m per group
Any group of pooled funds under the same management	£10m per manager
Negotiable instruments held in a broker's nominee account	£20m per broker
Foreign countries	£10m per country

Cash flow management

34 The Council's officers maintain a detailed cash flow forecast for each coming year revising it as more information is available. This informs the short term investments such as those to cover precept payments. The forecast is compiled on a prudent

basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Long term investment strategy is based on the Council's medium term financial strategy.

Treasury Management Indicators

35 **Security benchmark: average credit rating** The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk. The benchmark for 2021/22 will be an average credit rating of A unchanged from 2020/21.

36 **Liquidity benchmark:** The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing. For 2021/22 the benchmark amount available will be £3m unchanged from 2020/21.

Interest rate exposures

37 This indicator is set to control the Council's exposure to interest rate risk. New CIPFA guidance has led to a change in this indicator which is now an upper limits on the one year revenue impact of a 1% rise or fall in interest rates. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates. The figures are the same as last year.

	Limit
Upper limit on one-year revenue impact of a 1% rise in interest rates	£200,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	£200,000

Maturity structure of borrowing

38 This indicator is set to control the Council's exposure to refinancing risk and is really most useful for councils with a portfolio of loans. The upper and lower limits on the maturity structure of fixed rate borrowing are shown below. The Council is not planning to borrow but will set limits to allow flexibility of term and maturity date for any new borrowing.

	Upper	Lower
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within five years	100%	0%
Five years and within 10 years	100%	0%
10 years and above	100%	0%

Principal sums invested for periods longer than a year

39 The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total long-term principal sum invested to final maturities beyond the period end will be:

	2021/22	2022/23	2023/24
Limit on principal invested beyond year end	£12m	£10m	£8m

Other Treasury Management issues

40 **Financial Derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

41 The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

42 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

43 In line with the CIPFA Code, the Authority will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

44 **Markets in Financial Instruments Directive**: The Council has opted up to professional client status with its providers of financial services allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. The Director of Corporate Resources believes this to be the most appropriate status.

45 **Ethical Investment:** The investment fund management sector is increasing taking into account Environmental, Social and Governance (ESG) criteria to screen out

investments or to guide their engagement with corporate bodies. Each of the Council's fund managers are reacting differently to this trend and the influence the Council can bring to bear is probably not great. However; the Council will work with its advisers to review the Council's opportunity to promote ESG factors without compromising security, liquidity and yield.

Appendix C Investment Strategy

1. This Investment Strategy was a new report starting in 2019/20, meeting the requirements of statutory guidance widening the coverage beyond strict treasury investments. It focuses on the financial support of local public services by lending to or buying shares in other organisations or its own subsidiaries (service investments) and commercial property investment income.

Service Investments: Loans

2. The Council can lend money to local bodies or its subsidiaries to support local public services and stimulate local economic growth. Historically the Council has only done this in very limited circumstances where a significant service outcome is expected. At present only one £300,000 loan is outstanding with a community run leisure centre for it to develop a specific local service.

3. There is no intention to increase the use of loans to local bodies and they are expected to be infrequent. The Council will, however, be lending to a subsidiary in the guise of its housing company. The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk, and ensure that total exposure to service loans remains proportionate to the size of the Council, upper limits on the outstanding exposure has been set at £3m. This is an increase on last year's £1.5m to reflect the increase in potential loans to its housing subsidiary. The Council controls the company and so is in a position to determine the level of risk its subsidiary takes on.

4. Accounting standards require the Council to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Council's statement of accounts will be shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

5. **Risk assessment**: The Council assesses the risk of loss before entering into service loans by assessing the counterparty's resilience, the service users' needs that the loan is designed to help meet and how these will evolve over time. During the life of the loan any change in original assumptions will be monitored. The Council will use external advisors if felt appropriate by the Director of Corporate Resources. All loans will be subject to contract agreed by Head of Legal. All new classes of loans must be approved by full Council and will be monitored by Director of Corporate Resources.

Service Investments: Shares

6. The Council does not currently intend to invest in any shares except for in its local housing company. The overall limit for 2021/22 is £0.5m.

7. **Security:** One of the risks of investing in shares is that they potentially fall in value meaning that the initial outlay may not be recovered. In order to limit this risk upper limits on the sum invested in subsidiaries will be set at the lowest practical level if and when exposure is allowed.

8. **Risk assessment:** The Council would assess the risk of loss before entering into and whilst holding shares by going through an extensive process of risk analysis. The risk analysis will include an assessment of the market that the subsidiary will be active in including the nature and level of competition, how the market will evolve over time, the barriers to entry and exit and any ongoing investment requirements. The Council will use external advisors as thought appropriate by Director of Corporate Resources.

9. **Liquidity:** Although this type of investment is fundamentally illiquid, in order to limit this the Council, when it sets a limit in this area, will initially set out the maximum periods for which funds may prudently be committed and how the Council will ensure it stays within its stated investment limits. The life of the housing companies has not been explicitly set but the invested equity will be reviewed at a five-year interval.

10. **Non-specified Investments:** Shares are the only investment type that the Council has identified that meets the definition of a non-specified investment in the government guidance. The limits above on share investments are therefore also the Council's required upper limits on non-specified investments. The Council has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

Commercial Investments: Property

11. The Council invests in local commercial property in order to make a return that will be spent on local public services. These include retail units, business centres, and commercial leisure facilities. They contributed £3.7m of income net of direct costs in 2019/20 providing a significant support to the Council's finances.

12. The table below lists the property by major category and by whether they are 'legacy' properties, which is taken as having been on the Council's books on 31 March 2007, and the acquisitions and developments since then. The reason for the choice of 31 March 2007 is twofold: firstly, this was the date of the implementation of asset accounting under International financial reporting

standard that required the Council to keep detail records of historic asset values and secondly it separates out the last decade where the recent purchases are reported. It is these more recent purchases which were made to provide commercial income to support the Council's budget as Central Government support reduced that is the main concern of the guidance. For the recent purchases the cost records are available whereas the Council does not have comprehensive records of actual purchase costs so the 31 March 2007 values are used.

Property by type £millions	**Actual**	**31.3.2020 actual**		**31.3.2021 expected**	
	Purchase cost or 31 March 2007 value	**Gains or losses**	**Value in accounts**	**Gains or losses**	**Value in accounts**
Retail – legacy	2.7	2.2	4.9	1.9	4.6
Retail – Swan Walk	9.7	-7.0	2.7	-7.1	2.6
Light industrial - legacy	9.3	6.3	15.6	6.3	15.6
Healthcare – legacy	6.5	1.3	7.8	1.3	7.8
Office - legacy	1.2	0.9	2.1	0.9	2.1
Retail - recent	14.6	-1.5	13.1	-2.2	12.4
Light industrial – recent	4.7	0.1	4.8	0.1	4.8
Healthcare – recent	0.6	0.3	0.9	0.3	0.9
Education -recent	1.8	-0.1	1.7	-0.1	1.7
Leisure – recent*	1.5	-0.6	0.9	-0.6	0.9
Total	**52.6**	**1.9**	**54.5**	**0.8**	**53.4**

13. In the table above the Swan Walk Centre has been taken out of the legacy retail category as it has a significant effect and has its own distinct history. The major loss in value is due to the movement of the valuation of the Council's equity share in Swan Walk from £8.4m in 2007 to a current value of £2.7m. A true separable purchase price for the Swan Walk equity share is not available as the Swan Walk development was a complex set of multiparty arrangements rather than a simple purchase.

14. The values at year end are uncertain due to the possible effect of the pandemic on the future rental income. The estimates for the end of 2020/21 above assume values broadly hold their value apart from retail where investor sentiment is currently poor and a discount allowance of 5% has been applied.

15. **Security:** In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.

16. The fair value assessment of the Council's investment property portfolio is slightly above the 'purchase' cost which means that the whole portfolio does provide 'security' in terms of the government guidance.

17. The Head of Property and Facilities has considered the prospects for the overall value of the portfolio and bearing in mind it is normal for assets within the portfolio to perform differently depending on market conditions concludes that the best course of action is to hold the assets for the long term as they are sound assets with dependable income streams.

18. The commercial properties are revalued each year-end by an external valuer so should the audited values at the end of 2020/21 fall below their purchase price the Head of Property and Facilities will consider whether their current course of action of holding the assets is appropriate and bring any alternative actions to Council in an update to the Investment Strategy. This is in line with the current government guidance.

19. **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding property investments by :
    - assessing the relevant market including the level of competition, the barriers to entry and exit and future market prospects;
    - using advisors if thought appropriate by the Director of Corporate Resources;
    - consulting Policy Development Advisory Group for Finance & Assets
    - taking final comprehensive report on all new investments to Cabinet
    - continually monitoring risk in the whole portfolio and any specific assets

20. **Liquidity:** Clearly property is relatively difficult to sell and convert to cash at short notice, and can take a considerable period to sell in certain market conditions. To ensure that the invested funds can be accessed when they are needed the Head of Property and Facilities ensures that at least £5m of commercial property could be sold as a going concern within a six month period.

Loan Commitments and Financial Guarantees

20 Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Council and are included here for completeness. The Council plans to provide loan commitments up to £6m to its Housing Company subsidiary. It does not plan to provide any guarantees in the foreseeable future.

Proportionality

21 The Council is dependent on profit generating investment activity to achieve a balanced revenue budget. The table below shows the extent to which the expenditure planned to meet the service delivery objectives is dependent on achieving the expected net profit from investments over the lifecycle of the

Medium Term Financial Strategy. The figures are best estimates bearing in mind the uncertainty due to the pandemic. They assume depressed levels of rents for this year and the next before a recovery for 2022/23. There is a risk that this is overoptimistic and that a longer lasting recession depresses income for the whole period.

Proportionality of Investments £m	**2019/20 Actual**	**2020/21 Forecast**	**2021/22 Budget**	**2022/23 Budget**	**2023/24 Budget**
Gross service expenditure	35	36	34	35	36
Investment income	3.7	3.4	3.6	3.9	4.0
Proportion	10%	10%	10%	11%	11%

22 **Capacity, Skills and Culture**

Elected Members and statutory officers: The Council recognises that those elected Members and statutory officers involved in the investments decision making process must have appropriate capacity, skills and information to enable them to:

- take informed decisions as to whether to enter into a specific investment;
- assess individual assessments in the context of the strategic objectives and risk profile of the Council; and
- understand how new decisions have changed the overall risk exposure of the Council.

The Council will ensure that the relevant officers and the Members of Audit Committee and Policy Development Advisory Group for Finance & Assets have appropriate skills, providing training and advisor support where there is a skills gap.

23 **Commercial deals:** The Council will ensure that the Audit Committee, Policy Development Advisory Group for Finance & Assets, Cabinet, and officers negotiating commercial deals are aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate.

24 **Corporate governance:** Any investment decisions will be scrutinised by Senior Leadership Team, Policy Development Advisory Group for Finance & Assets, and Cabinet before final approval. The Overview and Scrutiny committee review all decisions made by the Cabinet. Although after the event the Committee can make any recommendations to the Council if it sees fit.

Investment Indicators

25 The Council has set the following quantitative indicators to allow elected Members and the public to assess its total risk exposure as a result of its investment decisions.

26 **Total risk exposure:** The first indicator shows the total exposure to potential investment losses.

Total investment exposure £m	31.03.2020 Actual	31.03.2021 Forecast	31.03.2022 Forecast
Treasury management investments	39	30	32
Service investments: Loans	0.2	0.2	2.7
Service investments: Shares	0	0.1	0.1
Commercial investments: Property	54	53	56
TOTAL INVESTMENTS	93.2	83.3	90.8
Commitments to lend	0	0	6
Guarantees issued on loans	0	0	0
TOTAL EXPOSURE	93.2	83.3	96.8

27 **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Council does not have any borrowing the Council's investments are funded by usable reserves and income received in advance of expenditure.

28 **Rate of return received**: This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Investments net rate of return	2019/20 Actual	2020/21 Forecast	2021/22 Forecast
Treasury management investments	2.1%	1.6%	1.6%
Service investments: Loans	0%	3.0%	3.0%
Service investments: Shares	0	0	0
Commercial investments: Property	6.8%	6.4%	6.3%
ALL INVESTMENTS	4.8%	4.7%	4.7%

29 **Other indicators:** The MHCLG guidance lists other indicators and the Council has selected the indicators below as appropriate.

Indicator	**2019/20 Actual**	**2020/21 Forecast**	**2021/22 Forecast**
Debt to net service expenditure ratio	0%	0%	0%
Commercial income to net service expenditure ratio	35%	31%	32%
Benchmarking of returns – ratio of property income yield to IPD property yield index averaged over 5 year period	130%	130%	130%
Income net of direct cost return target	6.8%	6.4%	6.3%
Operating overheads of property section attributable to commercial property as a proportion of net property income	6.8%	6.5%	6.4%
Average Vacancy levels	1%	3%	2%
Tenant over 5%	5	5	5
Weighted Average Unexpired Lease Term (WAULT)	9yr	9yr	9yr
Bad debts written off	£0	£200,000	£200,000