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RUSHMOOR BOROUGH COUNCIL

LICENSING AND GENERAL PURPOSES COMMITTEE

at the Council Offices, Farnborough on
Monday, 28th November, 2016 at 7.00 pm

To:

Cllr A. Jackman (Chairman)
Cllr M.L. Sheehan (Vice-Chairman)

Cllr Sophia Choudhary
Cllr Liz Corps
Cllr A.H. Crawford
Cllr B. Jones
Cllr S.J. Masterson
Cllr M.D. Smith
Cllr L.A. Taylor
Cllr Jacqui Vosper
Cllr J.E. Woolley

Enquiries regarding this agenda should be referred to the Committee Administrator, Kathy Flatt, Democratic and Customer Services, Tel. (01252 398829) or email kathy.flatt@rushmoor.gov.uk.

A G E N D A

1. **MINUTES –** (Pages 1 - 4)

   To confirm the Minutes of the Meeting held on 26th September, 2016 (copy attached).

2. **APPOINTMENT OF EXTERNAL AUDITOR –** (Pages 5 - 14)

   To consider the Head of Financial Services' Report No. FIN1625 (copy attached), which seeks approval to recommend to the Council that Rushmoor opts in to the appointing person arrangements made by Public Sector Audit Appointments (PSAA) for the appointment of external auditors and authorises the Head of Financial Services to sign the notice of acceptance on behalf of the authority, subject to the Council decision.

3. **ANNUAL AUDIT LETTER –** (Pages 15 - 38)

   To consider the Annual Audit Letter for Rushmoor Borough Council (copy attached), to be presented by Mr. Andrew Brittain, Executive Director of Ernst & Young LLP, the Council's external auditors.

4. **TREASURY MANAGEMENT OPERATIONS MID-YEAR REPORT 2016/17 –** (Pages 39 - 54)

   To consider the Head of Financial Services' Report No. FIN1617 (copy attached), which sets out the main activities of the Treasury Management Operations during the first half of 2016/17.

PUBLIC PARTICIPATION AT MEETINGS

Members of the public may ask to speak at the meeting on any of the items on the agenda by writing to the Committee Administrator at the Council Offices, Farnborough by 5.00 pm three working days prior to the meeting.

LICENSING AND GENERAL PURPOSES COMMITTEE

Meeting held on Monday, 26 September 2016 at the Council Offices, Farnborough at 7.00 pm.

Voting Members

Cllr A. Jackman (Chairman)
Cllr M.L. Sheehan (Vice-Chairman)

Cllr Sophia Choudhary
Cllr Liz Corps
Cllr A.H. Crawford
Cllr S.J. Masterson
Cllr L.A. Taylor
Cllr J.E. Woolley

Apologies for absence were submitted on behalf of Councillor Barry Jones, Councillor Mike Smith and Councillor Jacqui Vosper.

14. **MINUTES**

The Minutes of the Meeting held on 27th June, 2016 were approved and signed by the Chairman.

15. **INTERNAL AUDIT - AUDIT UPDATE**

The Committee received the Audit Manager's Report No. AUD1602, which provided an overview of the internal audit work undertaken from March to August, 2016.

It was noted that an audit of capital projects that had been deferred over the previous three financial years had been carried out to identify reasons for the slippage and to ascertain if any trends had been highlighted. The key findings from the audit were:

- slippage of projects happened each year, with 44% of projects in 2013/14 and 56% of projects in 2014/15 slipped;

- 48 projects had slipped over the three year period with seven of these having slipped for more than three financial years;

- the majority of the slipped projects related to building works/ improvements, highways work/improvement or sports/recreational facilities; and

- external conditions had contributed to the majority of the slippages sampled (e.g. requiring external agreement or external funding).

The Committee was advised that no recommendations had been made as actions identified in the previous audit of capital projects would help to address the findings within the 2015/16 audit. A follow-up on the recommendations would be carried out later in the year and reported to the Committee.

In respect of audit follow-up work, the Committee noted that these had been carried in respect of: financial grants; parking management system; planning enforcement; eXpress system (elections); and, IT network security. This work had shown that progress had been made in implementing the audit recommendations. A follow-up had also been carried out on the mobile devices audit, although one high priority recommendation in respect of security had not yet been fully implemented and would be referred back to the Directors' Management Board for further discussion on a way forward.

The Committee was advised of current work in respect of Public Sector Internal Audit Standards which had come into effect in April, 2013, setting down areas of internal audit work which were expected in order to be compliant with the standards. The Internal Audit team was currently carrying out a self-assessment against the standards and the results would be reported to the next meeting of the Committee.

During discussion, Members raised questions regarding the reasons for the slippage of projects and staffing resources for the projects.

RESOLVED: That the Audit Manager's Report No. AUD1602 be noted.

16. **STATEMENT OF ACCOUNTS AND AUDIT RESULTS REPORT 2015/16**

The Committee considered the Head of Financial Services' Report No. FIN1620 which sought approval for the Council's Statement of Accounts for 2015/16 and set out the external auditor's Audit Results Report.

The Committee was advised that the Statement of Accounts for 2015/16 had been prepared in line with CIPFA's 'Code of Practice on Local Authority Accounting' for 2015/16, under International Financial Reporting Standards and in accordance with the Accounts and Audit (England) Regulations, 2015. The Council's Annual Governance Statement, which had been approved by the Committee on 27th June 2016, was required to be published alongside the Statement of Accounts by 30th September, 2016 and was included in Appendix A to the Report.

On behalf of the Committee, the Chairman welcomed Mr. Andrew Brittain and Mr. Adrian Balmer who were attending to present the findings of the Council's Auditors, Ernst & Young, in carrying out audit work in relation to the 2015/16 financial year. The audit was now complete and an unqualified audit opinion was issued. The external auditors also concluded that the Council had put in place proper arrangements to secure value for money in its use of resources and the audit certificate was issued at the meeting alongside the audit opinion.

Mr. Brittain advised that there was currently one unadjusted audit difference, which was an extrapolated error. Details of this were set out in Appendix B to the Audit Results Report. The error was not considered to be material to the audit opinion. The auditors sought the Committee's approval of management's rationale as to why the correction had not been made. This was included in the draft Letter of

Representation from the Council, which had been circulated to the Committee for approval.

A limited number of casting and consistency errors had been identified. These had been corrected during the course of the audit work and details were provided in Appendix A to the Audit Results Report. It was noted that these amendments did not have an impact on useable reserves.

Mr. Balmer advised the Committee on the responsibilities of the Council in preparing and publishing its Statement of Accounts and Annual Governance Statement as well as putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. Mr. Balmer also spoke on the purpose and scope of an audit, including audit risks identified during the planning phase of the audit, and which had been previously reported to the Committee in the Audit Plan. The Audit Results Report also set out: audit procedures performed and the assurance gained and issues arising from this work during the audit; other matters which were significant to the Council in overseeing its financial reporting process; control themes and observations; a request for written representations; Whole of Government Accounts return; and, a value for money conclusion.

Mr. Brittain thanked the Council for its help and support in allowing Ernst & Young to complete the audit.

RESOLVED: That

(i) the Auditor's Audit Results Report, as appended to the Head of Financial Services' Report No. FIN1620, be noted;

(ii) the financial statements for 2015/16 be approved;

(iii) the letter of representation, as circulated at the meeting, be approved; and

(iv) the Chairman be authorised to sign page 13 of the Statement of Accounts 2015/16, attached as Appendix A to the Report, to certify the Committee's approval.

The meeting closed at 7.32 pm.

CLLR A. JACKMAN (CHAIRMAN)

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AGENDA ITEM NO. 2

LICENSING AND GENERAL PURPOSES COMMITTEE
28TH NOVEMBER 2016

HEAD OF FINANCIAL SERVICES' REPORT NO. FIN1625

APPOINTMENT OF EXTERNAL AUDITOR

SUMMARY AND RECOMMENDATIONS:

SUMMARY: Following the demise of the Audit Commission, new arrangements were needed for the appointment of external auditors. The Local Audit and Accountability Act 2014 requires authorities to either opt in to the appointing person regime or to establish an auditor panel and conduct their own procurement exercise.

Appointment of auditors for the 2018/19 financial year is required by 31 December 2017.

RECOMMENDATIONS: That Licensing and General Purposes Committee (i) recommends to Full Council that Rushmoor opts in to the appointing person arrangements made by Public Sector Audit Appointments (PSAA) for the appointment of external auditors and (ii) authorises the Head of Financial Services to sign the notice of acceptance on behalf of the authority, subject to the Full Council decision.

1. INTRODUCTION

1.1 When the Government closed the Audit Commission it novated external audit contracts to Public Sector Audit Appointments Limited (PSAA) on 1 April 2015. The audits were due to expire following conclusion of the audits of the 2016/17 accounts, but could be extended for a period of up to three years by PSAA, subject to approval from the Department for Communities and Local Government.

2. BACKGROUND

2.1 In October 2015, the Secretary of State confirmed that the transitional provisions would be amended to allow an extension of the contracts for a period of one year. This meant that for the audit of the 2018/19 accounts it would be necessary for authorities either to undertake their own procurements or to opt in to the appointed person regime.

2.2 PSAA was originally established to operate the transitional arrangements following the closure of the Audit Commission and is a company limited by guarantee incorporated by the Local Government Association in August 2014. In July 2016, the Secretary of State for Communities and Local Government specified PSAA as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015. This means that PSAA can make auditor appointments for audits of the accounts from 2018/19 of principal authorities that choose to opt into its arrangements

2.3 All Local Authorities have now received an invitation to opt-in to the PSAA arrangements for a national scheme to appoint external auditors. A copy of the invitation is attached at Appendix A. The decision must be taken in accordance with the Regulations, i.e. by the Members of the authority meeting as a whole, and notice has to be given to PSAA of an authority's intention to opt-in by 9 March 2017.

2.4 The main advantages of using PSAA are set out below; these can also be viewed as the disadvantages if the Council was to decide to undertake its own procurement.

- Assure timely auditor appointments
- Manage independence of auditors
- Secure highly competitive prices
- Save on procurement costs
- Save time and effort needed on auditor panels
- Focus on audit quality
- Operate on a not for profit basis and distribute any surplus funds to scheme members.

3. DETAILS OF THE PROPOSAL

General

3.1 It is likely that a sector wide procurement conducted by PSAA will produce better outcomes for the Council than any procurement that the Council could manage itself, or with a limited number of partners. Use of the PSAA will also be less resource intensive than establishing an auditor panel and conducting our own procurement.

3.2 Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in must be made by Full Council (authority meeting as a whole). To comply with this regulation Licensing and General Purposes Committee is asked to make the recommendation above to Council.

Alternative Options

3.3 To establish an Auditor Panel and conduct our own procurement. This is not recommended as it will be a far more resource intensive process and, without the bulk buying power of the sector-led procurement, would be likely to result in a more costly service.

Consultation

3.4 This Council is a member of the Society of District Council Treasurers, which has conducted consultation via its PSAA Advisory Board, and has consulted widely with Local Authority Section 151 Officers.

4. IMPLICATIONS

Risks

4.1 As set out in the report, use of PSAA minimises the risks inherent in undertaking our own procurement.

Legal Implications

4.2 The process as set out above and the recommendation should ensure compliance with the Local Audit and Accountability Act 2014.

Financial and Resource Implications

4.3 If PSAA is not used some additional resource may be needed to establish an auditor panel and conduct our own procurement. Until the procurement exercise is completed, it is not possible to estimate the final audit fee for the audit of accounts from 2018/19, although it should be remembered that the audit fees were significantly reduced during the transition arrangements from those previously payable via the Audit commission. It is also expected that economies of scale will mean that procuring via PSAA would be significantly less than procuring individually or through any smaller group of authorities.

5. CONCLUSIONS

5.1 Two courses of possible action in relation to the provision of external audit services have been discussed in this report. A sector wide procurement conducted by PSAA will produce better outcomes for the Council than any procurement the Council could manage itself, or with a limited number of partners.

CONTACT DETAILS:

Report Author: Martin Dawson Martin.Dawson@Rushmoor.gov.uk 01252 398441
Head of Service: Amanda Fahey Amanda.Fahey@Rushmoor.gov.uk 01252 398440

BACKGROUND DOCUMENTS:
PSAA Prospectus & PSAA – Appointing Person – Frequently Asked Questions
http://www.psaa.co.uk/supporting-the-transition/appointing-person/

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27 October 2016

Email: appointingperson@psaa.co.uk

Andrew Lloyd
Rushmoor Borough Council
Rushmoor Council Offices
Farnborough Road
Farnborough Hampshire GU14 7JU

Copied to: Amanda Fahey, Head of Financial Services, Rushmoor Borough Council
Ann Greaves, Solicitor to the Council, Rushmoor Borough Council

Dear Mr Lloyd

Invitation to opt into the national scheme for auditor appointments

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

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

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

I need to highlight two things:

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

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

Yours sincerely

Jon Hayes, Chief Officer

PSAA, 3rd floor, Local Government House, Smith Square, London, SW1P 3HZ
T 020 7072 7445 www.psaa.co.uk Company number: 09178094

Appointing an external auditor

Information on the national scheme

Public Sector Audit Appointments Limited (PSAA)

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

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

The national scheme for appointing local auditors

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

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

What the appointing person scheme will offer

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

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

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

Using the scheme will avoid the need for you to:

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

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

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

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

High quality audits

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

We will:

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

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

Procurement strategy

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

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

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

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

Auditor appointments and independence

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

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

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

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

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

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

Fee scales

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

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

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

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

Opting in

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

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

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

Timetable

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

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

Enquiries

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

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

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Rushmoor Borough Council

Annual Audit Letter for the year ended 31 March 2016

October 2016

Ernst & Young LLP

Building a better working world

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Contents

In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued ''Statement of responsibilities of auditors and audited bodies 2015-16'. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk)

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

The 'Terms of Appointment from 1 April 2015' issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities. 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 Steve Varley, 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.

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Rushmoor Borough Council (the Council) following completion of our audit procedures for the year ended 31 March 2016.

Below are 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 2016 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

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	The Council is below the specified audit threshold of £350 million. 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 26 September 2016
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 26 September 2016

In January 2017 we will also issue a report to those charged with governance of the Council summarising the certification work we have undertaken.

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

Andrew Brittain

Executive Director
For and on behalf of Ernst & Young LLP

Purpose

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 2015/16 Audit Results Report to the 26 September 2016 Licensing and General Purposes 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

Responsibilities of the Appointed Auditor

Our 2015/16 audit work has been undertaken in accordance with the Audit Plan that we issued in February 2016 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- Expressing an opinion:
  - On the 2015/16 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 thy 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 you Whole of Government Accounts return. The Council is below the specified audit threshold of £350 million. 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. 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.

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's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an unqualified audit report on 26 September 2016.

Our detailed findings were reported to the 26 September 2016 Licensing and General Purposes Committee.

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

Significant Risk	Conclusion
Management override of controls As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement. For local authorities the potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.	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. Our review of accounting estimates has found that estimates are reasonable, and there was no indication of bias in the calculation of the estimates. 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.
IPSAS 16 and IFRS 13 – Fair Value Measurement Changes to IPSAS 16 and IFRS 13 with respect to Investment Properties and Fair Value valuation	We reviewed the Council's assessment of the impact of IPSAS 16 and IFRS 13 on Surplus Assets and/or Investment Properties and noted no issues We tested a sample of assets classified as Investment Properties and agreed with the

respectively came into effect for the financial year15-16. The new IPSAS 16 standard could have changed the classification of an Investment Property if the property was used to facilitate the delivery of services or production of goods as well as to earn rental income or capital appreciation or both. The Council had approximately £26 m of Investment Property as at 31/03/15 and so any re-assessment to comply with IPSAS 16 or IFRS 13 could have potentially resulted in a material re-classification between Investment Properties and Other Land and Buildings.	classification. We completed an assessment of the property valuation expert commissioned to undertake the valuation. This did not identify any issues.

Other Key Findings	Conclusion
Debtors Existence As part of our testing of Debtors we identified an error in our existence testing of Debtors. We were unable to obtain supporting evidence for one of our samples selected. This was an old historical debtor from 1999/2000 which had not been provided against. It is good practice to regularly review old historical balances in relation to debtors and to ascertain the likelihood of recovering such money. We reported this is an uncorrected error within our Audit Results Report as an extrapolated error.	We have recommended that a process of review is conducted to ensure that historical debts are supported by adequate documentation and suitably reviewed for recoverability. Where documentation is not available to support the existence of the Debtor then the balance should be considered for write off and suitably approved. Key officers have accepted the recommendation and are currently undertaking a review of historical debtors to assess the impact and to take the appropriate action. The outcome of this review will be reported by management to Those Charged with Governance in due course.

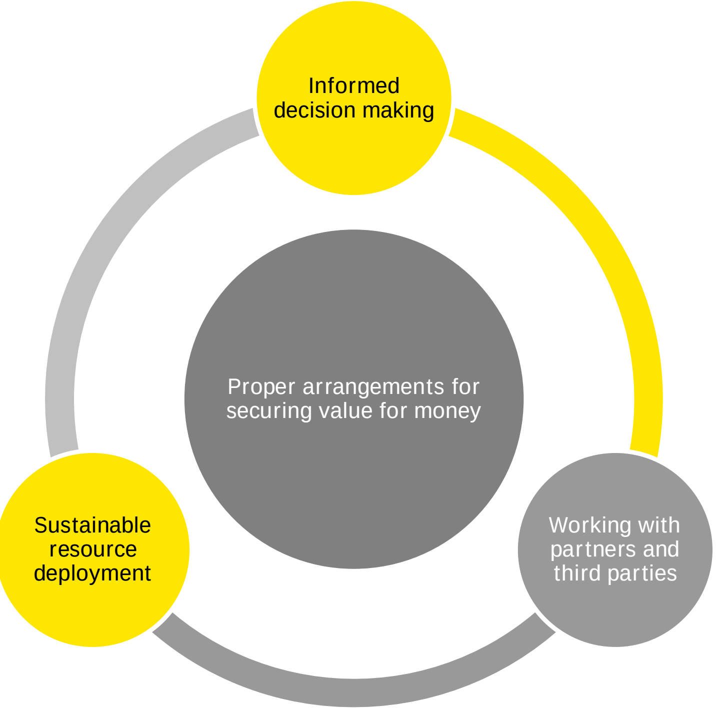
Value for Money

Value for Money

We are required to consider whether the Council has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on 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.



We issued an unqualified value for money conclusion on 26 September 2016.

Our audit did not identify any significant matters in relation to the Council.

Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

The Council is below the specified audit threshold of £350 million. Therefore, we did not 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.

Objections Received

We did not receive any objections to the 2015/16 financial statements from member of the public.

Other Powers and Duties

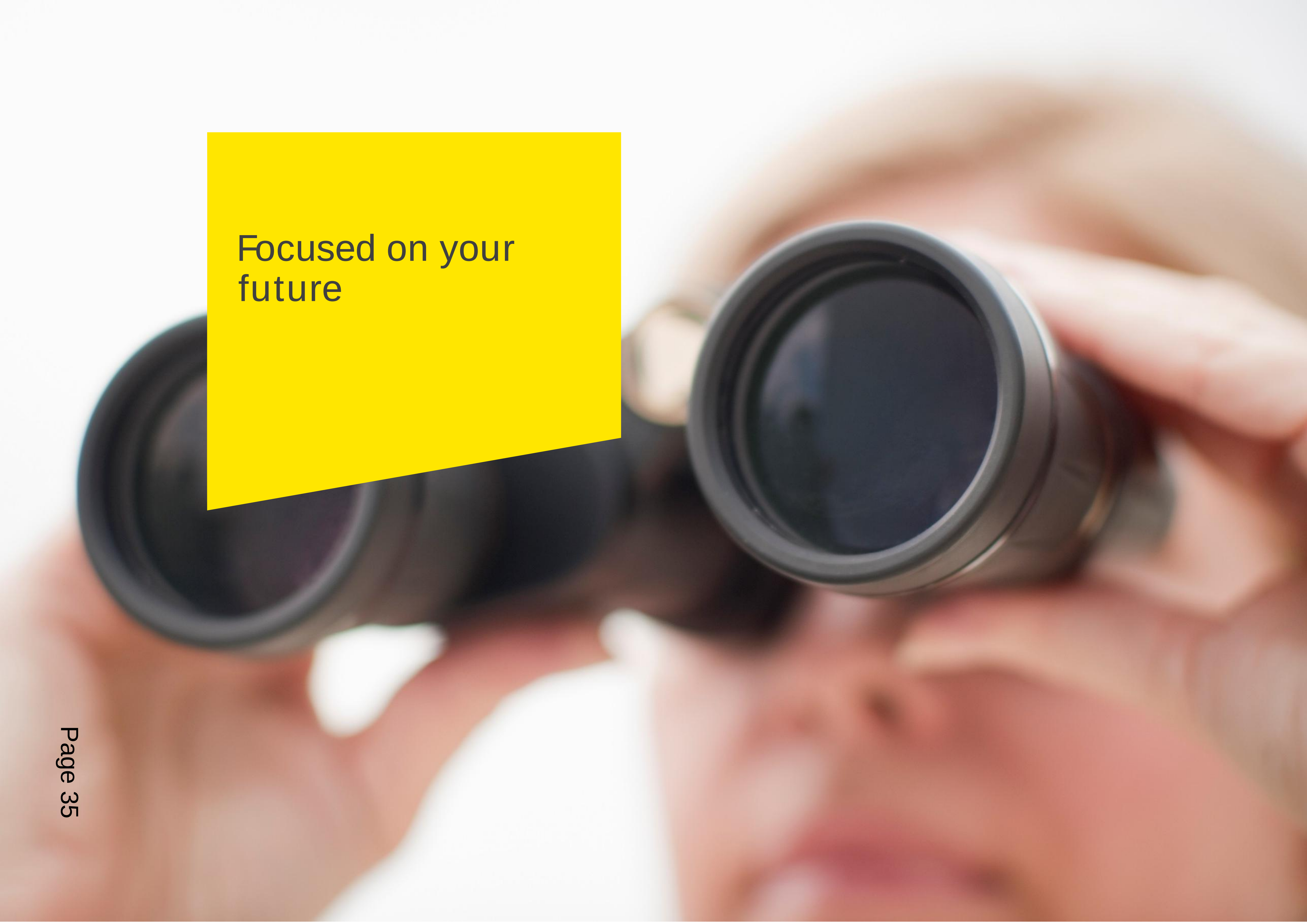
We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the Licensing and General Purposes Committee on 26 September 2016. 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

We have adopted a fully substantive approach and have therefore not tested the operation of controls.



Focused on your future

Focused on your future

Area	Issue	Impact
Faster close	From the 2017/18 financial year, the deadline for preparing the Council's financial statements will move to 31 May from 30 June. In addition, the deadline for completing the statutory audit will move to 31 July from 30 September.	The faster closedown timetable requires the Council to adjust its timetable for preparing the accounts, as well as the budget setting process and the timing of committee meetings. It requires upfront planning to identify areas of the accounts that can be prepared earlier, before the 31 March, and there will be a need to establish robust basis for estimations across a wider number of entries in the financial statements. For the 2016/17 audit, we are working with officers to bring our work forward to support the transition ahead of the new deadlines in 2017/18.
Appointment of auditors	The current audit contracts expire on the completion of the 2017/18 audit. The expiry of contracts also marks the end of the current mandatory regime for auditor appointments. After this, the Council can exercise choice about whether it decides to opt in to the authorised national scheme, or whether to make other arrangements to appoint its own auditors. In July 2016, the Secretary of State for Communities and Local Government specified Public Sector Audit Appointments limited (PSAA) as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015. PSAA will be able to appoint an auditor to relevant authorities that choose to opt into its national collective scheme.	Appointment of auditors for the 2018/19 financial year is required by 31 December 2017. The council should consider whether they intend to opt into the appointed person scheme to appoint your auditors from 2018/19 or if the council should make its own arrangements following the legislative requirements.

EY | Assurance | Tax | Transactions | Advisory

Ernst & Young LLP

ED None

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

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

ey.com

AGENDA ITEM NO. 4

LICENSING & GENERAL PURPOSES **HEAD OF FINANCIAL SERVICES**
28TH NOVEMBER 2016 **REPORT NO. FIN1626**

TREASURY MANAGEMENT OPERATIONS MID-YEAR REPORT 2016/17

SUMMARY AND RECOMMENDATIONS:

SUMMARY: This report sets out the main activities of the Treasury Management Operations during the first half of 2016/17.

RECOMMENDATION:

Note the contents of the report in relation to the activities carried out during the first half of 2016/17.

1 INTRODUCTION

1.1 The Treasury Management Strategy for 2016/17 is underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2011, which includes the requirement for determining a treasury strategy on the likely financing and investment activity for the forthcoming financial year. The Code also recommends that members are informed of Treasury Management activities at least twice a year. This report therefore ensures this authority is embracing best practice in accordance with CIPFA's recommendations.

1.2 This report sets out the main activities of the Treasury Management Operations during the first half of 2016/17, provides an update on the current economic conditions affecting Treasury Management decisions and a forward look for the remainder of 2016/17.

1.3 Appendix A shows the actual prudential indicators relating to capital and treasury activities for the first half of 2016/17 and compares these to the indicators set in the Annual Treasury Management Strategy for the year, which was approved by Council in February 2016.

2 TREASURY MANAGEMENT ADVICE

2.1 The Council receives independent treasury advisory services from Arlingclose Ltd. Arlingclose provide treasury advice to 25% of UK local authorities including technical advice on debt and investment management, and long-term capital financing. They advise on investment trends, developments and opportunities consistent with the Council's Treasury Management Strategy.

2.2 With the exception of pooled funds all investment activity is carried out by the Council's own treasury team with advice from Arlingclose Ltd, as outlined in paragraph 2.1 above, and having due regard to information from other sources such as the financial press and credit-rating agencies.

2.3 Pooled funds are managed at the discretion of the external fund managers associated with each fund. It should however be noted that whilst the funds are externally managed, the decision as to whether to invest lies solely with the Council in accordance with its Treasury Management Strategy.

2.4 Officers involved in treasury activities have attended an Arlingclose workshop on investment security, liquidity and yield during the 6 months to 30th September 2016.

3 ECONOMIC BACKGROUND

Comment provided by Arlingclose

3.1 **UK Economy:** The preliminary estimate of Q2 2016 GDP showed reasonably strong growth as the economy grew 0.7% quarter-on-quarter, as compared to 0.4% in Q1 and year/year growth running at a healthy pace of 2.2%. However, the UK economic outlook changed significantly on 23rd June 2016. The surprise result of the referendum on EU membership prompted forecasters to rip up previous projections and dust off worst-case scenarios. Growth forecasts had already been downgraded as 2016 progressed, as the very existence of the referendum dampened business investment, but the crystallisation of the risks and the subsequent political turmoil prompted a sharp decline in household, business and investor sentiment.

3.2 The repercussions of this plunge in sentiment on economic growth were judged by the Bank of England to be severe, prompting the Monetary Policy Committee to initiate substantial monetary policy easing at its August meeting to mitigate the worst of the downside risks. This included a cut in Bank Rate to 0.25%, further gilt and corporate bond purchases (QE) and cheap funding for banks (Term Funding Scheme) to maintain the supply of credit to the economy.

3.3 The minutes of the August meeting also suggested that many members of the Committee supported a further cut in Bank Rate to near-zero levels (the Bank, however, does not appear keen to follow peers into negative rate territory) and more QE should the economic outlook worsen.

3.4 In response to the Bank of England's policy announcement, money market rates and bond yields declined to new record lows. Since the onset of the financial crisis over eight years ago, Arlingclose's rate outlook has progressed from 'lower for longer' to 'even lower for even longer' to, now, 'even lower for the indeterminable future'.

3.5 **Market reaction**: Following the referendum result gilt yields fell sharply across the maturity spectrum on the view that Bank Rate would remain extremely low for the foreseeable future. The yield on the 10-year gilt fell from 1.37% on 23rd June to a low of 0.52% in August, a quarter of what it was at the start of 2016. The 10-year gilt yield has since risen to 0.69% at the end of September. The yield on 2- and 3-year gilts briefly dipped into negative territory intra-day on 10th August to -0.1% as prices were driven higher by the Bank of England's bond repurchase programme. However, both yields have since recovered to 0.07% and 0.08% respectively.

3.6 The fall in gilt yields was reflected in the fall in PWLB borrowing rates. It should be noted that after an initial sharp drop, equity markets appeared to have shrugged off the result of the referendum and bounced back despite warnings from the IMF on the impact on growth from 'Brexit' as investors counted on QE-generated liquidity to drive risk assets. The most noticeable fall in money market rates was for very short-dated periods (overnight to 1 month) where rates fell to between 0.1% and 0.2%.

3.7 **Interest Rate Forecast**: The Arlingclose central case for the path of the Bank Rate over the next three years is for the Bank Rate to remain at 0.25%, with a 25% possibility of a drop to close to zero, with a small chance of a reduction below zero.

4. BORROWING ACTIVITY IN 2016/17

4.1 Prior to the start of the current financial year the Council had made use of a revolving infrastructure fund from the Local Enterprise Partnership (LEP) by borrowing £3 million to progress the Aldershot regeneration schemes, and £1.7 million for Ball Hill SANG. An element of the borrowing for Aldershot regeneration schemes had been spent in 2015/16 meaning that the Council had raised its Capital Financing Requirement to £1.4m at the commencement of 2016/17. Further expenditure in relation to the borrowing from the Local Enterprise Partnership is planned for the current year, although only minor amounts had been committed in the first half-year.

4.2 Significant capital expenditure was incurred in the first half year in relation to the acquisition of income yielding investment properties, which were not listed in the Council's original capital budget for the year 2016/17. Cabinet approval of these acquisitions was made within the first half-year of 2016/17.

4.3 In order to raise sufficient cash to accommodate these purchases the Council has negotiated some short-term borrowing at low interest rates within the first half year of 2016/17, and may incur some additional borrowing within the second half of the year to continue to service capital expenditure.

4.4 The Council's Authorised Limit for borrowing was set at £15m in the Annual Treasury Management Strategy Statement (TMSS) for 2016/17, approved by Full Council in February 2016. This limit was set as it was foreseen in the TMSS that there was a need to progress expenditure on Invest to Save schemes (as part of the 8-Point Plan) and strategic projects such as regeneration schemes (TMSS Full Council 25 February 2016 Appendix B page 16). This capital expenditure on the "Invest to Save" schemes was estimated to be £8.5m, although the Council has now approved a number of these schemes within the first half-year 2016/17 to the total value of £17m. A figure twice in value compared to the TMSS projection.

4.5 These additional Invest to Save scheme approvals have an effect on the Prudential Indicators approved in the TMSS for 2016/17. The Head of Financial Services is considering these effects and will include revisions to the 2016/17 Prudential Indicators as part of the TMSS reporting for 2017/18 that will be considered by Full Council in late February 2017.

5. INVESTMENT ACTIVITY IN 2016/17

5.1 The Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles. The graph at Appendix B has been produced by Arlingclose and demonstrates that during the six months to 30th September 2016 the Council's returns on total investment portfolio were 2.6%. This represents an increase against the returns generated during the previous financial year (2015/16 1.9%). The current half-year performance is amongst the highest when benchmarked against the average of 0.86% yield for 133 local authority clients. The marked improvement has been achieved in relation to the Council's pooled funds' holding (which includes movements on the capital value of pooled funds). A small number of other Councils with similar sized internal and external portfolios are marked on the graph to enable performance comparison.

5.2 **Pooled Funds**

Pooled Fund Capital Growth - As these are long-term investments (3-5 year window) Finance staff monitor the capital value of these investments on a monthly basis. Two of the pooled funds (Payden & CCLA) provide for good capital growth. Columbia Threadneedle has now returned near par to the price that the Council originally paid to acquire the fund. The UBS fund is currently priced only marginally below the Council's original purchase price. Aberdeen Asset Management Absolute continue to be below their original fund price.

Arlingclose have confirmed that "we review all our advised funds regularly, and if we think the fund manager is under performing, or the fund holdings are no longer suitable for clients, then we will advise you to sell".

Pooled Fund Income Returns – The income returned by fund for the period to 30th September 2016 is analysed below (all percentage returns quoted below are measured at 12-month running averages):

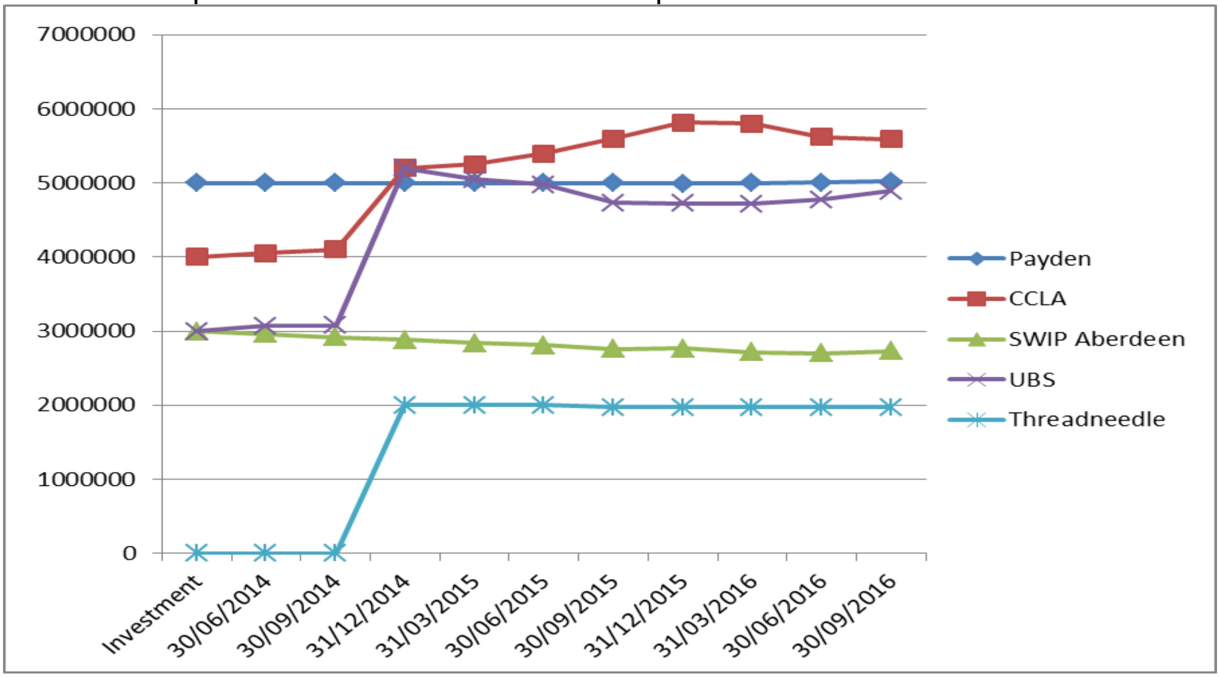
- £5 million investment with Payden & Rygel's Sterling Reserve Fund. The Fund seeks to provide capital security, liquidity and income through investment in Sterling denominated investment-grade debt securities. The fund has provided a 0.84% income return performance.

- £5 million investment with CCLAs Local Authorities' Mutual Investment Trust. The fund has provided a 5.55% income return performance.

- £3 million investment with Aberdeen Asset Management Absolute Return Fund. This fund aims for a target total return of 3-5% from a combination of investment income or capital appreciation. The fund has provided a 2.23% income return performance.

- £5 million investment in the UBS Multi-Asset Income Fund. This Fund follows a strategy of reducing volatility exposure levels by spreading investments across a diversified range of asset classes. The fund has provided a 3.44% income return performance.

- £2 million investment in the Columbia Threadneedle Strategic Bond Fund. This Fund aims to provide income and capital appreciation through investment grade and high yield bonds. The fund has provided a 4.36% income return performance.



5.3 **Bonds** – debt instruments in which an investor lends money for a specified period of time at a fixed rate of interest. **Covered Bonds** are conventional bonds that are backed by a separate group of loans (usually prime residential mortgages). When the covered bond is issued, it is over collateralised, with the pool of assets being greater than the value of the bond. During the first half year 2016/17, the Council had not negotiated any additional bond investments in excess of continuation of its investment in the following covered bonds held at the commencement of the half-year. The Council holds the following bonds (listed at their nominal value):

- £1 million Bank of Scotland at fixed rate of 0.957% (until Nov 16)
- £1 million Yorkshire BS at a fixed rate of 1.33% (until Apr 18)
- £1 million Yorkshire BS at a fixed rate of 1.18% (until Apr 18)
- £2 million Leeds BS at a fixed rate of 1.47% (until Dec 18)
- £1 million Leeds BS at Libor + 0.27% (until Feb 18)

Bank and Building Society Investments

- An amount of £1 million is invested into Lloyds Bank at a rate of 1.05% (until Apr 2017)

- An amount of £1 million is invested into Bank of Scotland at a rate of 0.90% (until Jan 2017)
- An amount of £1 million is invested into the Nationwide BS at a rate of 0.71% (until Oct 2016)

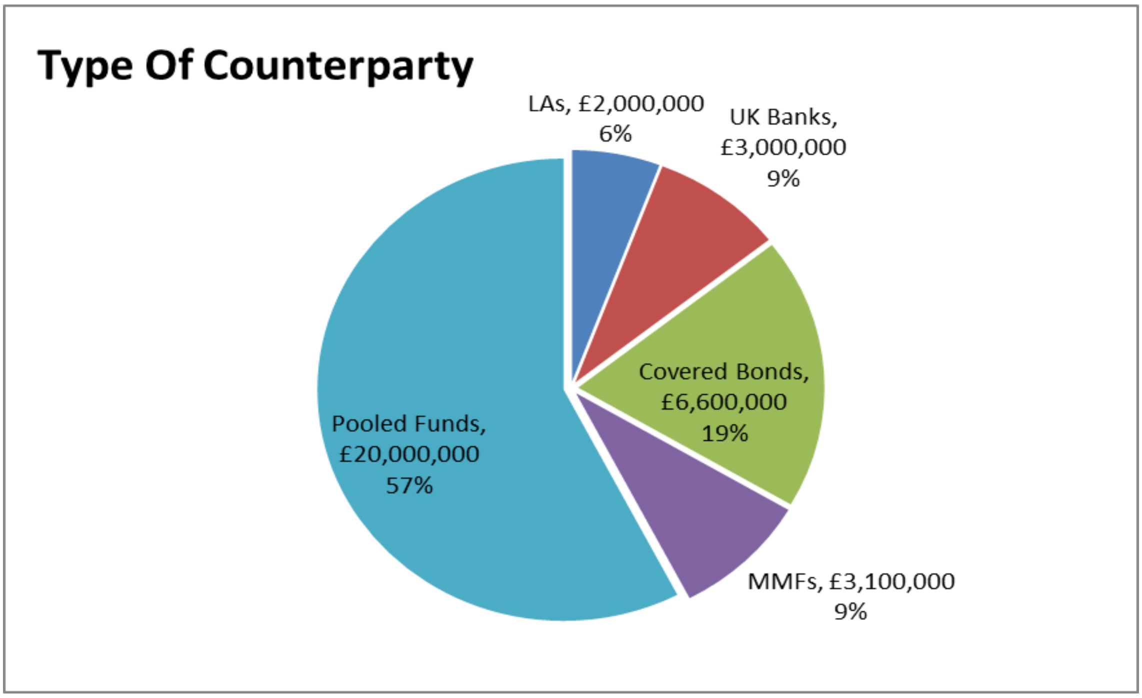
Other Investments – The Council continues to maintain some diversity in its portfolio by holding the following in institutions other than UK banks:

- £2 million at a fixed rate of 1% with Dumfries and Galloway Council (redemption Aug 17)
- Various temporary investments across a range of approved unsecured banks and building society counterparties all for durations of 6 months or less at rates ranging between 0.39% - 0.44% (as measured towards the end of the first half-year 2016/17). These temporary investments assist the Council to achieve essential cash liquidity on a daily basis.

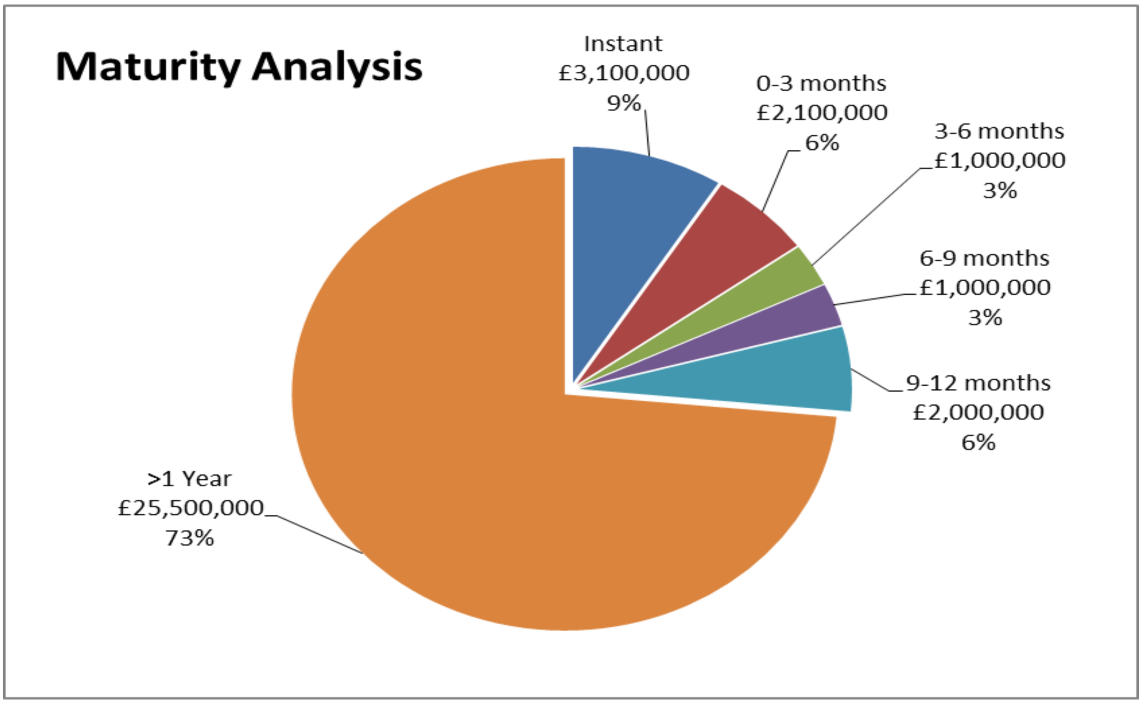
5.4 **All Investments –** The table that follows summarises deposit/investment activity during the 6-month period to 30th September 2016. Overall, there was a decrease of £4.3m invested during the period.

Investment Counterparty	Balance at 01/04/16 £m	Investments Made £m	Maturities/ Investments Sold £m	Balance at 30/09/16 £m	Avg Rate % and Avg Life (yrs)
UK Local Authorities	2.0	-	-	2.0	1% 9 - 12mths
UK Banks and Building Societies (unsecured): Short-term Long-term	3.0 -	2.0 -	(2.0) -	3.0 -	0.8% 3 – 6mths
Foreign Banks	2.2	-	(2.2)	-	-
Covered Bonds	6.6	-	-	6.6	0.96% - 1.47% (1mth– 2 Yrs. 3 mths)
AAA-rated Money Market Funds and short-term bank investments	5.2	Activity in & out on a daily basis, resulting in a net reduction in the period	(2.1)	3.1	Varies daily <0.42%
Pooled Funds: • Payden • CCLA • SWIP Aberdeen • UBS Multi Asset • Threadneedle	5.0 5.0 3.0 5.0 2.0	- - - - -		5.0 5.0 3.0 5.0 2.0	0.84% 5.55% 2.23% 3.44% 4.36%
TOTAL INVESTMENTS	38.8	-	(4.3)	34.7	
Increase/ (Decrease) in Investments £m		-	(4.3)		

5.5 The following pie charts illustrate the spread of investments by counterparty along with a maturity analysis. These illustrate continued diversity.



Maturity Analysis for ALL INVESTMENTS as at 30th September 2016	Amount invested £	% of total investments
Instant	3,100,000	9
0-3 months	2,100,000	6
3-6 months	1,000,000	3
6-9 months	1,000,000	3
9-12 months	2,000,000	6
> 1 year	25,500,000	73
Total for all duration periods	**34,700,000**	**100**



6 CREDIT RISK (Credit Score Analysis)

6.1 Counterparty credit quality is assessed and monitored by reference to credit ratings. Credit ratings are supplied by rating agencies Fitch, Standard & Poor's and Moody's. Arlingclose assign values between 1 and 26 to credit ratings in the range AAA to D, with AAA being the highest credit quality (1) and D being the lowest (26). Lower scores mean better credit quality and less risk.

6.2 The advice from Arlingclose is to aim for an A-, or higher, average credit rating, with an average score of 7 or lower. This reflects the current investment approach with its focus on security. The scores are weighted according to the size of our deposits (value-weighted average) and the maturity of the deposits (time-weighted average).

6.3 The table below summarises the Council's internal investment credit score for deposits during the 6-month period to 30th September 2016. The Council's scores fall comfortably within the suggested credit parameters. This represents good credit quality deposits on the grounds of both size and maturity. When comparing performance between quarters, quarter 2 reflects an improved credit risk score from the position in quarter 1.

Date	Value Weighted Average – Credit Risk Score	Value Weighted Average – Credit Rating	Time Weighted Average – Credit Risk Score	Time Weighted Average – Credit Rating
Q4 2015/16	3.02	AA	1.50	AAA
Q1 2016/17	4.74	A+	5.45	A+
Q2 2016/17	2.88	AA	1.57	AA+

6.4 **Interest Rate Exposure**: This indicator is set to monitor the Council's exposure to the effects of changes in interest rates. The indicator calculates the relationship between the Council's net principal sum outstanding on its borrowing to the minimum amount it has available to invest. The upper limits on fixed and variable rate interest rate exposures expressed as the amount of net principal borrowed is shown in the table that follows.

At 30th September 2016 the Council's total net position on principal sums invested amounts to £34.7m (investments) offset by £10.3m (borrowing) resulting in a (net) amount of £24.4m.

Interest Rate Exposure	2016/17 Approved Limit	End of Q2 2016/17 Actual
Upper limit on fixed interest rate exposure – represented by the maximum permitted net outstanding principal sum borrowed at fixed rate – Note that a negative indicator represents net investment	-£27m	-£27m

Upper limit on variable interest rate exposure – represented by the maximum permitted net outstanding principal sum borrowed at variable rate – Note that a negative indicator represents net investment	-£19m	-£19m

As the Council still has more funds available to invest than its total borrowing the above indicators result in negative figures.

6.5 **Maturity Structure of Borrowing**: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing are given in the table below:

	Upper	Lower	End of Q2 2016/17 Actual Performance
Under 12 months	100%	0%	60%
12 months and within 24 months	100%	0%	15%
24 months and within 5 years	100%	0%	21%
5 years and within 10 years	100%	0%	4%
10 years and above	100%	0%	-

At 30th September 2016, the Council's external borrowing amounts to £10m. The maturity duration percentage are related to the tiered repayment structure for the M3 LEP.

6.6 **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 investments. Performance against the limits on the total principal sum invested to final maturities beyond the period end is:

	2016/17 Approved Limit	End of Q2 2016/17 Actual Performance
Limit on principal invested beyond year end at any one time	£50m	£25m

7 COUNTERPARTY UPDATE

7.1 All three credit ratings agencies have reviewed their ratings in the six months to reflect the loss of government support for most financial institutions and the potential for varying loss given defaults as a result of new bail-in regimes in many countries. Despite reductions in government support, many institutions have seen upgrades due to an improvement in their underlying strength and an assessment that the level of loss given default is low. The Council continues to invest only in counterparties recommended by Arlingclose.

8 FORWARD LOOK

8.1 Advice from Arlingclose continues to ensure that the Council should focus on diversification of risk, spreading smaller amounts over an increasing number of counterparties. The Council currently uses 18 different counterparties compared with an average of 16 used by Arlingclose's 139 local authority clients.

8.2 Arlingclose are also in the knowledge that the Council has acquired over £16m of significant income yielding property assets in Q2 2016/17 and have provided advice on retention of an element of investments whilst borrowing is incurred.

8.3 In addition to continuing to spread risk by investing in a diverse range of counterparties, the Council's in-house team also continues to evaluate the opportunity for future investment options if sufficient cash becomes available. A range of potential options as specified in the current year's TMSS paragraph 5.6 (Full Council 25 February 2016 Agenda item 6 (2)) could be considered.

8.4 However, the Council's situation regarding its overall holding of investments and borrowing has changed with some significance during the first half-year 2016/17. These changes are due in the main to the approved acquisition of income yielding investment properties in the first half-year, which were not included in the Council's original capital budget for 2016/17.

8.5 Treasury management decision making is now progressing to incurring some specific external borrowing to service the Council's capital expenditure plans, whilst retaining existing investments for as long as possible.

9 BUDGETED INCOME & OUTTURN

9.1 The UK Bank Rate has been reduced to 0.25% (from 0.5%) and the Council's advisors central case estimate is for the Bank Rate to remain at 0.25%, but there is a 40% possibility of a drop to close to zero, with a small chance of a reduction below zero . The Council's full year 2016/17 budgeted investment income interest is now estimated to be £768,000, compared to the original budget for the year of £850,000. In addition, borrowing interest costs for the current year are estimated to be £12,000, compared to a zero original budget for 2016/17. This information was contained in the Cabinet report "Revenue Monitoring first half-year 2016/17" for 15 November 2016. The reduction in overall net investment/borrowing yield is directly related to the Council's decision to acquire a number of investment properties in the first half of the current year.

10 CONCLUSIONS

10.1 2016/17 continues to present challenges for treasury management. The Council's treasury team has concentrated as always on the security of deposits/investments while having regard to the returns available. It is estimated that the Council's increased capital expenditure in the current year will raise the level of external borrowing at the end of the year.

10.2 Further capital expenditure in 2017/18 and future years will require progressive redemption of the Council's investments as borrowing increases. Every effort is being made to retain the higher yielding investments for as long as possible, as their redemption in the future to raise cash for capital purposes will cause significant revenue effects in relation to the loss of investment income. The Council continues to seek to diversify its investments in order to maximise returns and to safeguard the Council's treasury management position.

10.3 The Treasury and Prudential indicators were set in February 2016 as part of the Council's Treasury Management Strategy. The Council can confirm that it has complied with its Treasury and Prudential Indicators for 2016/17.

AMANDA FAHEY
HEAD OF FINANCIAL SERVICES

Background papers:

CIPFA Prudential Code 2011 (Printed edition 2013)

CIPFA Code of Practice -'Treasury Management in the Public Services'

Loans and Investments records

Contact: Amanda Fahey, Head of Financial Services, x8440

1.1 **Prudential Indicators**

Estimates of Capital Expenditure: The Council's planned capital expenditure and financing is summarised as follows.

Capital Expenditure and Financing	2016/17 Estimate £m	2016/17 Projected £m	2017/18 Estimate £m	2018/19 Estimate £m
General Fund	8.802	27.500	5.317	1.150
Total Expenditure	**8.802**	**27.500**	**5.317**	**1.150**
Capital Receipts	5.477	18.840	3.470	(0.037)
Capital Grants & Contributions	2.575	0.655	1.097	0.437
Revenue	0.750	0.550	0.750	0.750
Prudential Code Borrowing	-	7.455	-	-
Total Financing	**8.802**	**27.500**	**5.317**	**1.150**

Capital expenditure in 2016/17 is now estimated to be significantly higher when compared to the original estimate. Detail of this increase can be obtained by reference to Cabinet report 15 November 2016 "Capital Programme Monitoring" agenda item 2 (2).

Estimates of Capital Financing Requirement:
The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose.

Capital Financing Requirement	31.03.17 Estimate £m	31.03.17 Projected £m	31.03.18 Estimate £m	31.03.19 Estimate £m
General Fund	4.3	4.3	15.0	29.9
Total CFR	**4.3**	**4.3**	**15.0**	**29.9**

The CFR amounts provided above are provided in relation to the TMSS for 2016/17 incorporating items within the 8-Point Plan with regard to "Invest to Save" schemes.

Gross Debt and the Capital Financing Requirement: In order to ensure that over the medium term debt will only be for a capital purpose, the Council should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.

Debt	31.03.17 Estimate £m	31.03.17 Projected £m	31.03.18 Estimate £m	31.03.19 Estimate £m
Borrowing	4.1	4.1	3.4	2.6
Total Debt	**4.1**	**4.1**	**3.4**	**2.6**

During 2016/17, the Council is expecting to continued make use of a revolving infrastructure fund from the Local Enterprise Partnership (M3 LEP).

Operational Boundary for External Debt: The operational boundary is based on the Council's estimate of most likely, i.e. prudent, but not worst-case scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, Private Finance Initiative and other liabilities that are not borrowing but form part of the Council's debt.

Operational Boundary	2016/17 Estimate £m	2016/17 Projected £m	2017/18 Estimate £m	2018/19 Estimate £m
Borrowing	5.0	5.0	5.0	5.0
Total Debt	**5.0**	**5.0**	**5.0**	**5.0**

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.

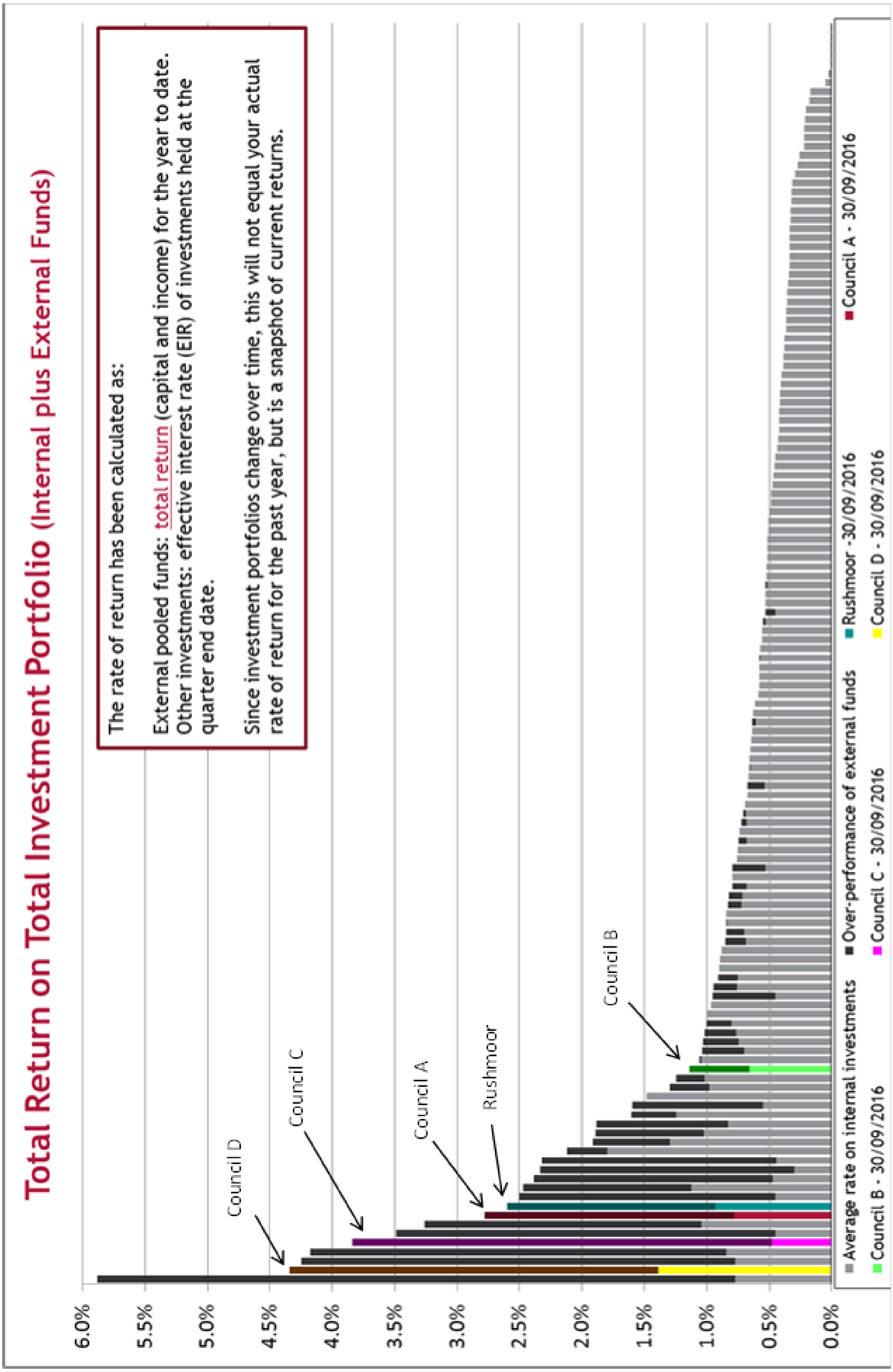
Authorised Limit	2016/17 Estimate £m	2016/17 Projected £m	2017/18 Estimate £m	2018/19 Estimate £m
Borrowing	14.0	14.0	18.0	20.0
Other long-term liabilities	1.0	1.0	1.0	1.0
Total Debt	**15.0**	**15.0**	**19.0**	**21.0**

Ratio of Financing Costs to Net Revenue Stream: This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Ratio of Financing Costs to Net Revenue Stream	**2016/17 Estimate %**	**2016/17 Projected %**	**2017/18 Estimate %**	**2018/19 Estimate %**
General Fund	-7	-7	-5	-5

Incremental Impact of Capital Investment Decisions: This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax levels. The incremental impact is the difference between the total revenue budget requirement of the current approved capital programme and the revenue budget requirement arising from the capital programme proposed.

Incremental Impact of Capital Investment Decisions	**2016/17 Estimate £**	**2016/17 Projected £**	**2017/18 Estimate £**	**2018/19 Estimate £**
General Fund - increase in annual band D Council Tax	4.75	4.75	2.67	2.55



Total Return on Total Investment Portfolio (Internal plus External Funds)
The rate of return has been calculated as:
External pooled funds: total return (capital and income) for the year to date.
Other investments: effective interest rate (EIR) of investments held at the quarter end date.
Since investment portfolios change over time, this will not equal your actual rate of return for the past year, but is a snapshot of current returns.
6.0%
5.5%
5.0%
4.5%
4.0%
3.5%
3.0%
2.5%
2.0%
1.5%
1.0%
0.5%
0.0%
Council D
Council C
Council A
Rushmoor
Council B
Average rate on internal investments
Over-performance of external funds
Rushmoor - 30/09/2016
Council A - 30/09/2016
Council B - 30/09/2016
Council C - 30/09/2016
Council D - 30/09/2016

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