

South Somerset District Council

Notice of Meeting



Audit Committee

Making a difference where it counts

Thursday 24th February 2011

10.00 a.m.

**Main Committee Room,
Council Offices,
Brympton Way,
Yeovil,
Somerset BA20 2HT**

The public and press are welcome to attend.

Disabled Access is available at this meeting venue.



If you would like any further information on the items to be discussed, please ring the Agenda Co-ordinator, **Andrew Blackburn** on Yeovil (01935) 462462
email: andrew.blackburn@southsomerset.gov.uk

This Agenda was issued on Wednesday, 16th February 2011

Ian Clarke, Assistant Director (Legal & Corporate Services)



2007-2008
*Neighbourhood and
Community Champions:
The Role of Elected Members*
2006-2007
*Improving Rural Services
Empowering Communities*
2005-2006
Getting Closer to Communities

This information is also available on our
website: www.southsomerset.gov.uk



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Audit Committee Membership

Chairman Derek Yeomans
Vice-Chairman Ian Martin

Mike Best John Richardson
John Calvert Peter Roake
John Hann Alan Smith
Roy Mills Colin Winder

South Somerset District Council – Corporate Aims

Our key aims are: (all equal)

- Increase economic vitality and prosperity
- Enhance the environment, address and adapt to climate change
- Improve the housing, health and well-being of our citizens
- Ensure safe, sustainable and cohesive communities
- Deliver well managed, cost effective services valued by our customers

Members' Questions on Reports prior to the Meeting

Members of the Committee are requested to contact report authors on points of clarification prior to the Committee meeting.

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Information for the Public

The purpose of the Audit Committee is to provide independent assurance of the adequacy of the risk management framework and the associated control environment, independent scrutiny of the authority's financial and non-financial performance, to the extent that it affects the authority's exposure to risk and weakens the control environment and to oversee the financial reporting process.

The Audit Committee should review the Code of Corporate Governance seeking assurance where appropriate from the Executive or referring matters to management on the scrutiny function.

The terms of reference of the Audit Committee are:

1. To approve the Strategic and Annual Internal Audit Plans;
2. To receive summaries of Internal Audit reports and seek assurance from management that action has been taken.
3. To consider the reports of external audit and inspection agencies and seek assurance from management that action has been taken.
4. To consider the effectiveness of SSDC's risk management arrangements, the control environment and associated anti-fraud and corruption arrangements and seek assurance from management that action is being taken.
5. To review the annual Statement of Internal Control and monitor associated action plans.
6. To review the SSDC's Code of Corporate Governance and ensure it is kept up to date and reflects best practice. This will include regular reviews of the Council's Constitution and an overview of the risk management.
7. To receive reports from management on the promotion of good corporate governance.
8. To review and approve the annual Statement of Accounts, external auditor's opinion and reports to members and monitor management action in response to issues raised.

Meetings of the Audit Committee are held monthly including at least one meeting with the Council's external auditor.

Agendas and minutes of this committee are published on the Council's website at www.southsomerset.gov.uk

The Council's Constitution is also on the web site and available for inspection in council offices.

Further information can be obtained by contacting the agenda co-ordinator named on the front page.

Audit Committee

Thursday 24th February 2011

Agenda

Preliminary Items

1. To approve as a correct record the Minutes of the previous meeting held on 27th January 2011
2. Apologies for Absence
3. Declarations of Interest

In accordance with the Council's Code of Conduct, which includes all the provisions of the statutory Model Code of Conduct, members are asked to declare any personal interests (and whether or not such an interest is "prejudicial") in any matter on the agenda for this meeting. A personal interest is defined in paragraph 8 of the Code and a prejudicial interest is defined in paragraph 10.

4. Public Question Time

Items for Discussion

Page Number

- | | | |
|-----|--|----|
| 5. | 2010/11 Internal Audit Quarterly Update Report | 1 |
| 6. | Internal Audit Plan 2011-12 | 15 |
| 7. | Internal Audit Charter Annual Review..... | 18 |
| 8. | Treasury Management Performance to December 2010 | 22 |
| 9. | Treasury Management Strategy Statement and Investment Strategy
2011/12..... | 32 |
| 10. | Accounting Policies for 2010/11 Statement of Accounts | 64 |
| 11. | Date of Next Meeting | 83 |

Audit Committee – 24th February 2011

5. 2010/11 Internal Audit Quarterly Update Report

Strategic Director: Mark Williams, Chief Executive
Assistant Director: Donna Parham, Finance and Corporate Services
Lead Officer: Andrew Ellins, Audit Manager
Contact Details: andrew.ellins@southwestaudit.gov.uk

Purpose of the Report

This report has been prepared for the Audit Committee to review the progress made on the 2010-11 Annual Internal Audit Plan.

Recommendation

To note the progress made.

Background

The Audit Committee agreed the 2010/11 Internal Audit Plan at its February meeting. An update was provided in August (for quarter one) and November (for quarter two) and this report provides the latest position (for quarter three).

Appendix A - Detailed Quarterly Report
Appendix B - Annual Audit Plan Progress Table
Appendix C - Audit Assurance Definitions

Financial Implications

There are no financial implications associated with these recommendations.

Background Papers: None



South Somerset District Council

Report of Internal Audit Activity

Quarter 3, 2010/11

Contents

The contacts at SWAP in connection with this report are:

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Summary	2
Internal Audit Work Programme:	3
Operational Audits	4
Key Control Audits	5
Governance, Fraud and Corruption	5
Managed Audits	6
Additional Reviews	6
Future Planned Work	7
Conclusions	7

Our audit activity is split between:

- **Operational Audit**
- **Key Control Audits**
- **Governance, Fraud & Corruption**
- **Managed Audits**
- **Additional Reviews**

Role of Internal Audit

The Internal Audit service for South Somerset District Council is provided by South West Audit Partnership (SWAP). SWAP adopted and works to the Standards of the Institute of Internal Auditors, but also follows the CIPFA Code of Practice for Internal Audit. The Partnership is also guided by the Internal Audit Charter approved by the Audit Committee at its meeting on 25th February 2010. Primarily the work includes;

- Plan of Operational Reviews
- Annual Review of Key Income Streams (Key Control Audits)
- Annual Review of Key Financial System Controls (Managed Audits)
- Annual review of key governance and fraud controls

Overview of Internal Audit Activity

Internal Audit work is largely driven by an Annual Audit Plan. This is approved by the Section 151 Officer, following consultation with the Management Board and External Auditors. This year's Audit Plan was reported to this Committee at its meeting in February 2010. The Annual Audit Plan for next year (2011-12) will be presented to this Committee in a separate report at this meeting.

Quarter 3 Outturn:

We rank our recommendations on a scale of 1 to 5, with 1 being minor or administrative concerns to 5 being areas of major concern requiring immediate corrective action

Internal Audit Work Programme

The schedule provided at [Appendix B](#) contains a list of all audits as agreed in the Annual Audit Plan 2010/11. This allows Members to monitor the progress of all audits in the plan.

Each assignment completed to at least draft report status includes its respective “control assurance” opinion together with the number and relative ranking of recommendations that have been raised with management. The assurance opinion ratings have been determined in accordance with the Internal Audit “Audit Framework Definitions” as shown in [Appendix C](#).

Where assignments record that recommendations have been made to reflect that some control weaknesses have been identified as a result of audit work, these are considered to represent a less than significant risk to the Council’s operations. However, in such cases, the Committee can take assurance that improvement actions have been agreed with management to address these.

Quarter 3 Outturn:

Completed Audit Assignments In The Period

Operational Audits

Operational Audits are a detailed evaluation of a service or functions control environment. A risk evaluation matrix is devised and controls are tested. Where weaknesses or areas for improvement are identified, actions are agreed with management and target dated.

Quarter 3 is when the Managed Audits are all conducted and governance reviews undertaken. As a result, only one operational review was completed since the last audit committee meeting. This review of Asset Management had nine recommendations of which only one was a high priority.

The lead auditor concluded that 'The 2009 report provided only Partial Assurance because a number of serious control weaknesses were identified, the results of this follow up review show that improvements have been made. However there are areas that still need to be documented and controls that need further improvement to fully mitigate risks. The Uniform system is still not being used to appropriately manage the property elements of the commercial asset.

The audit received reasonable assurance.

- Asset Management

An operational review of Tourist Information Centers (TIC's) was originally planned, however, at the request of the Client this review has been dropped from the Audit Plan. This service is currently undergoing significant change due to the budget cuts and it was felt inappropriate to undertake a review at this time.

Quarter 3 Outturn:

Completed Audit Assignments In The Period

Key Control Audits

Key Control Audits provide independent annual assurance that key income streams are adequately controlled and the Council are not exposed to risks that could impact on its ability to meet its overall objectives.

There was only one Key Control review in Quarter 3 due to resources being prioritised on the managed audits and governance reviews.

The lead auditor concluded that 'Improvements have been made to the service to enhance the control framework within the Centre and to address the high to medium risks identified in the previous audit review. Some minor control issues have also been identified but are not significant enough to undermine the integrity of; or materially impact on; the service. As such these have not been included in the action plan but nonetheless, have been discussed with Management to address; together with the findings reported below.'

- Yeovil Recreational Centre

Governance, Fraud and Corruption Audits

Governance, Fraud and Corruption Audits focus primarily on key risks relating to cross cutting areas that are controlled and/or impact at a Corporate rather than Service specific level. Since the last quarterly report there have been two governance audits completed and a further two that are at Draft stage but not yet agreed with Management and will therefore be reported upon in the next quarterly report to this committee.

Two separate reviews of register of interests were performed. The Members review found that this area was well controlled and comprehensive assurance was provided with only one low priority recommendation. The review over the staff register could only provide partial assurance although the lead auditor conclude 'South Somerset District Council have demonstrated their compliance with the Local Government Act through the guidance given in the Staff Code of Conduct. They also have a robust procedure for dealing with any complaints, but there are weaknesses in the recording of interests and a lack of a uniform approach across the services.'

- Register of Interests—Staff
- Register of Interests—Members

Quarter 3 Outturn:

Completed Audit Assignments In The Period

Managed Audits

Managed Audits are completed to assist the External Auditor in their assessment of the Council's financial control environment. These are scheduled each year to be carried out between October and the end of December. Nine managed audits were completed as planned. The plan ([Appendix B](#)) shows ten managed audits, however, in agreement with the Section 151 Officer the review of Budgetary Control was undertaken as an element of the Main Accounting audit.

I am pleased to report that of the nine managed audits completed, four received reasonable assurance and five received comprehensive assurance. In total there were just seven recommendations and only one medium/high priority action was required.

- Capital Accounting
- Council Tax
- Creditors
- Debtors
- Housing Benefits
- Main Accounting (including Budgetary Control)
- NNDR
- Payroll
- Treasury Management

Additional Reviews

Additional Reviews are adhoc reviews, normally non-opinion requested by the Section 151 Officer. There have been two more reviews started since the last report to this committee but both are still in progress and will be reported in the next quarterly audit report.

We keep our audit plans under regular review, so as to ensure we are auditing the right things at the right time.

Future Planned Work

This is detailed in [Appendix B](#) subject to any changes agreed by the Section 151 Officer.

Conclusions

For those audits still required by the client SWAP are on target to complete those audits as planned. For the audits completed to report stage each report contains an action plan with a number of recommendations which are given service priorities. Definitions of these priorities can be found in the Categorisation of recommendations section in [Appendix C](#).

So far this year SWAP has provided 103 recommendations for improvement where weaknesses in control were identified. For the last quarter we are pleased to report that no very high priority actions were identified and only two high actions requiring priority management attention were reported. Furthermore, only one partial assurance was given for the audits completed in this quarter which is an indication that the audited areas are well controlled within the scope covered in each review. In particular all of the managed audits received reasonable assurance or greater.

APPENDIX B

Client	Directorate/Service	Audit Area	Quarter	Status	Opinion	No. of recs	◀ Major - Recommendations - Minor ▶				
							5	4	3	2	1
SSDC	Additional Review	Air Control Industries Site & Chard Regeneration Scheme Statement of Accounts	Qtr1	Complete	Non-Opinion	0	0	0	0	0	0
SSDC	Key Control Audits	Car Parks	Qtr1	Complete	Reasonable	11	0	2	9	0	0
SSDC	Operational Audits	Catering	Qtr1	Complete	Reasonable	11	0	0	11	0	0
SSDC	Operational Audits	Childcare Nursery	Qtr1	Complete	Reasonable	10	0	0	6	4	0
SSDC	Governance, Fraud & Corruption	Data Quality - Performance Indicators	Qtr1	Complete	Reasonable	4	0	0	4	0	0
SSDC	Key Control Audits	Goldenstones	Qtr1	Complete	Reasonable	12	0	0	12	0	0
SSDC	Governance, Fraud & Corruption	Health & Safety - Internal Awareness and Training	Qtr1	Complete	Reasonable	3	0	0	1	2	0
SSDC	Key Control Audits	Homelessness	Qtr1	Complete	Reasonable	17	0	0	13	4	0
SSDC	Additional Review	Yeovil Cemetery & Crematorium Annual Return	Qtr1	Complete	Non-Opinion	0	0	0	0	0	0
SSDC	Operational Audits	Asset Management Follow-Up	Qtr2	Complete	Reasonable	9	0	1	4	4	0
SSDC	Operational Audits	Building Control	Qtr2	Complete	Reasonable	7	0	2	5	0	0
SSDC	ICT - Security	Corporate back up routines	Qtr2	Complete	Reasonable	2	0	0	2	0	0
SSDC	Governance, Fraud & Corruption	Equalities and Diversity Impact Assessments	Qtr2	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Key Control Audits	Licensing	Qtr2	Complete	Reasonable	3	0	0	2	1	0
SSDC	Governance, Fraud & Corruption	Performance - NI 179 Efficiency Statements	Qtr2	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Governance, Fraud & Corruption	Performance - NI 188 Use of Natural Resources	Qtr2	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Operational Audits	VAT	Qtr2	Complete	Reasonable	2	0	0	1	1	0
SSDC	Managed Audits	Budgetary Control	Qtr3	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Managed Audits	Capital Accounting	Qtr3	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Managed Audits	Council Tax	Qtr3	Complete	Reasonable	1	0	0	1	0	0
SSDC	Managed Audits	Creditors	Qtr3	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Managed Audits	Debtors	Qtr3	Complete	Reasonable	1	0	0	1	0	0
SSDC	Governance, Fraud & Corruption	Fees and Charges	Qtr3	In Progress		0	0	0	0	0	0
SSDC	Governance, Fraud & Corruption	Gifts & Hospitality - Register of Interests (Members)	Qtr3	Final	Comprehensive	1	0	0	0	1	0
SSDC	Governance, Fraud & Corruption	Gifts and Hospitality - Register of Interests (Officers)	Qtr3	Final	Partial	3	0	0	3	0	0
SSDC	Managed Audits	Housing Benefits	Qtr3	Complete	Comprehensive	0	0	0	0	0	0

APPENDIX B

Client	Directorate/Service	Audit Area	Quarter	Status	Opinion	No. of recs	◀ Major - Recommendations - Minor ▶				
							5	4	3	2	1
SSDC	Managed Audits	Main Accounting	Qtr3	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Managed Audits	NNDR	Qtr3	Complete	Reasonable	4	0	1	3	0	0
SSDC	Managed Audits	Payroll	Qtr3	Complete	Reasonable	1	0	0	1	0	0
SSDC	Governance, Fraud & Corruption	Risk Management (Risk Registers including Major Projects)	Qtr3	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Tourism (TIC's)	Qtr3	Dropped	N/A	0	0	0	0	0	0
SSDC	Managed Audits	Treasury Management	Qtr3	Complete	Comprehensive	0	0	0	0	0	0
SSDC	Key Control Audits	Yeovil Recreation Centre	Qtr3	Final	Reasonable	1	0	0	1	0	0
SSDC	Governance, Fraud & Corruption	Business Continuity - Major Partnerships & Contracts	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Care Line	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Choice Based Lettings	Qtr4	Created		0	0	0	0	0	0
SSDC	Operational Audits	Corporate Policy & Performance	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Countryside & Rights of Way	Qtr4	Created		0	0	0	0	0	0
SSDC	ICT - Security	Firewall Change Management	Qtr4	Created		0	0	0	0	0	0
SSDC	Governance, Fraud & Corruption	Income Collection (Analytical Review including Budgets and Methods of Payment)	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Innovation Centre (Key Controls)	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Additional Review	Innovation Centre - Operational Review	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Octagon Theatre	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Key Control Audits	Octagon Theatre - Production Company Contracts	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Operational Audits	Printing & Copying	Qtr4	Created		0	0	0	0	0	0
SSDC	Operational Audits	Section 106 & Commuted Sums Follow-Up	Qtr4	Created		0	0	0	0	0	0
SSDC	Operational Audits	Streetscene	Qtr4	Deffered	N/A	0	0	0	0	0	0
SSDC	ICT - Security	Threat Protection	Qtr4	In Progress		0	0	0	0	0	0
SSDC	Special Review	Whistleblow	Qtr4	In Progress	Non-Opinion	0	0	0	0	0	0
						103	0	6	80	17	0

Audit Framework Definitions

Control Assurance Definitions

Comprehensive	▲ ★ ★ ★	I am able to offer comprehensive assurance as the areas reviewed were found to be adequately controlled. Internal controls are in place and operating effectively and risks against the achievement of objectives are well managed.
Reasonable	▲ ★ ★ ★	I am able to offer reasonable assurance as most of the areas reviewed were found to be adequately controlled. Generally risks are well managed but some systems require the introduction or improvement of internal controls to ensure the achievement of objectives.
Partial	▲ ★ ★ ★	I am able to offer Partial assurance in relation to the areas reviewed and the controls found to be in place. Some key risks are not well managed and systems require the introduction or improvement of internal controls to ensure the achievement of objectives.
None	▲ ★ ★ ★	I am not able to offer any assurance. The areas reviewed were found to be inadequately controlled. Risks are not well managed and systems require the introduction or improvement of internal controls to ensure the achievement of objectives.

Categorisation Of Recommendations

When making recommendations to Management it is important that they know how important the recommendation is to their service. There should be a clear distinction between how we evaluate the risks identified for the service but scored at a corporate level and the priority assigned to the recommendation. No timeframes have been applied to each Priority as implementation will depend on several factors, however, the definitions imply the importance.

Priority 5: Findings that are fundamental to the integrity of the unit's business processes and require the immediate attention of management.

Priority 4: Important findings that need to be resolved by management.

Priority 3: The accuracy of records is at risk and requires attention.

Priority 2: Minor control issues have been identified which nevertheless need to be addressed.

Priority 1: Administrative errors identified that should be corrected. Simple, no-cost measures would serve to enhance an existing control.

Definitions of Risk

Risk	Reporting Implications
Low	Issues of a minor nature or best practice where some improvement can be made.
Medium	Issues which should be addressed by management in their areas of responsibility.
High	Issues that we consider need to be brought to the attention of senior management.
Very High	Issues that we consider need to be brought to the attention of both senior management and the Audit Committee.

Audit Committee – 24th February 2011

6. Internal Audit Plan 2011-12

Strategic Director: Mark Williams, Chief Executive
Assistant Director: Donna Parham, Finance and Corporate Services
Lead Officer: Andrew Ellins, Audit Manager
Contact Details: andrew.ellins@southwestaudit.gov.uk

Purpose of the Report

This report has been prepared for the Audit Committee to provide them with details of the audits planned for the next financial year.

Recommendation

To agree to the Internal Audit Plan for 2011-12.

Background

The total number of audit days planned for 2011-12 is 459 days, which is a reduction on the current year of 111 days. This reduction was requested in order to reduce the cost of the internal audit service as part of the Council's budget cuts.

Historically audit plans have been derived from 4 year Strategic Plans. However, this plan has been pulled together with a view to providing assurance to both officers and members of the current and imminent risks faced by the Authority in an ever changing risk environment. The plan is only indicative to facilitate the planning of audit resources. We anticipate that, as the real impact of recently announced budget cuts bite, the plan will have to remain flexible to address new and emerging risks faced by the Council.

To ensure that to the best of our ability we have covered the necessary risks, the Audit Manager and the Section 151 Officer have liaised with Assistant Directors and Heads of Service and together, whilst also considering audits already undertaken in recent years, have produced the plan below.

Key Control Audits - The Key Control process focuses primarily on key risks relating to the Council's major financial systems. It is essential that all key controls identified by the External Auditors are operating effectively to provide management with the necessary assurance. To this end we have liaised with the Audit Commission representatives and included any requirements they have in providing them necessary assurance, in line with the International Auditing Standards, that they are required to audit against. There are 9 annual audits planned;

- Capital Accounting
- Council Tax
- Creditors
- Debtors
- Housing Benefit
- Main Accounting
- NNDR
- Payroll
- Treasury Management

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Key Income Control Audits - The Key Income Control Audits provide independent annual assurance that key income streams are adequately controlled and the Council are not exposed to risks that could impact on its ability to meet its overall objectives. There are 10 annual audits planned;

- Careline Income
- Car Parks Income
- Goldenstones Income
- Homelessness Income
- Licensing Income
- Octagon Theatre Income
- Section 106 Agreements Income
- Wincanton Sports Centre Income
- Workplace Nursery Income
- Yeovil Recreation Centre Income

Governance Audits – The Governance Audit process focuses primarily on key risks relating to cross cutting areas that are controlled and/or impact at a corporate rather than service specific level. It also provides an annual assurance review of areas of the Council that are inherently higher risk. This work will, in some cases, enable SWAP to provide management with added assurance that they are operating best practice as we will be conducting these reviews at all our Client Sites. We fully consulted with each of our Client Section 151 Officers and with them, or their representatives at the SWAP Management Board, we carried out a Control and Risk Self Assessment workshop to identify the major risks facing their organisations for the coming year. There are 17 reviews planned for 2011-12;

- ACI Site & Chard Regeneration Scheme Statement of Accounts
- Annual Governance Statement Review
- Contract Management - Monitoring and Compliance with SO's
- Fees and Charges
- Health & Safety - Safeguarding Staff and Clients
- Information Governance
- Managing Complaints
- Managing with Reduced Resources
- Maximising Income (Opportunity Comparisons)
- Members Interests - Related Parties
- MTFP Process
- Partnership Arrangements
- Scheme of Delegation
- Threat from Fraud or Corruption (Analytical Review)
- Threat from Fraud or Corruption (Policy Review)
- Yeovil Cemetery and Crematorium Annual Return
- Yeovil Town Centre Bank Account

IT Audits – IS Reviews are completed to provide the Authority with assurance with regards to their compliance with industry best practice. SWAP has a specialist Computer Audit Manager who has met with the I.T. Manager and identified specific I.T. related risks. There are 3 specialist reviews planned for 2011-12;

- Gov Connect
- PCI Compliance
- ICT Service Management and Governance

Operational Audits - Operational audits are a detailed evaluation of a service or functions control environment. A risk evaluation matrix is devised and controls are

tested. Where weaknesses or areas for improvement are identified, actions are agreed with management and target dated. There are 9 audits planned for 2011-12;

- Car Loans
- Pest Control
- Housing Benefits Fraud
- Legal Services
- Play and Youth Facilities
- Property Services
- Streetscene - Workshop
- Streetscene - Enforcement
- Waste & Recycling

Follow Up Audits – Internal Audit follow up on all Audits being given a ‘Partial or No Assurance’ level to ensure that agreed actions to mitigate risks have been implemented. We have provisionally planned 25 days to do follow-up reviews.

Advice and Meetings - Internal Audit are risk experts and as well as undertaking planned audits are always glad to assist officers where they seek advice on managing their risks. Similarly, to enable effective governance Internal Audit work closely with the Audit Commission and with the Section 151 Officer and the Audit Committee through regular liaison meetings and progress reporting.

Financial Implications

There are no financial implications associated with these recommendations.

Background Papers: *None*

7. Internal Audit Charter Annual Review

Strategic Director: Mark Williams, Chief Executive
Assistant Director: Donna Parham, Finance and Corporate Services
Lead Officer: Andrew Ellins, Audit Manager
Contact Details: andrew.ellins@southwestaudit.gov.uk

Purpose of the Report

This report has been prepared for the Audit Committee to review the Internal Audit Charter and approve any changes.

Recommendation

To agree to the revised Internal Audit Charter as attached at pages 19-21.

Background

The Audit Committee agrees the Internal Audit Charter annually. It was last reviewed by this Committee on 25th February 2010. This year the Charter has been updated to reflect the move away from an historic 4 year strategic audit plan;

“The annual plan will be developed with reference to the risks the organisation will be facing in the forthcoming year, whilst providing a balance of current and on-going risks, reviewed on a cyclical basis. The plan will be reviewed on a quarterly basis to ensure it remains current and addresses new and emerging risks.”

Financial Implications

There are no financial implications associated with these recommendations.

Background Papers: None

Internal Audit Charter

Purpose

The purpose of this Charter is to set out the nature, role, responsibility, status and authority of internal auditing within the South Somerset District Council, and to outline the scope of internal audit work.

Approval

This Charter was approved by the Audit Committee on 26 February, 2004 and the Council on 18 March, 2004 and is reviewed each year to confirm it remains accurate and up to date. It was last reviewed by the Audit Committee on 24 February, 2011.

Provision of Internal Audit Services

The internal audit service is provided by the South West Audit Partnership (SWAP) on a 5 year contract expiring on 31 March, 2015. This charter should be read in conjunction with the Trading Agreement, which forms part of the legal agreement between the SWAP partners.

The budget for the provision of the internal audit service is determined by the Council, in conjunction with the SWAP Partnership Board. The general financial provisions are laid down in the legal agreement, including the level of financial contribution by the Council, and may only be amended by unanimous agreement of the Partnership Board. The budget is based on an audit needs assessment that was carried out when determining the Council's level of contribution to SWAP. This is reviewed each year by the Assistant Director (Finance and Corporate Services) in consultation with the Head of Internal Audit Partnership.

Role of Internal Audit

Internal audit is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Responsibilities of Management and of Internal Audit

Management

Management is responsible for determining the scope, except where specified by statute, of internal audit work and for deciding the action to be taken on the outcome of, or findings from, their work. Management is responsible for ensuring SWAP has:

- the support of management and the Council; and
- direct access and freedom to report to senior management, including the Chief Executive and the Audit Committee.

Management is responsible for maintaining internal controls, including proper accounting records and other management information suitable for running the Authority. Management is also responsible for the appropriate and effective management of risk.

Internal Audit

Internal audit is responsible for operating under the policies established by management in line with best practice.

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Internal audit is responsible for conducting its work in accordance with the Code of Ethics and Standards for the Professional Practice of Internal Auditing as set by the Institute of Internal Auditors. Internal Audit also complies with the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom.

Internal audit is not responsible for any of the activities which it audits. Members of SWAP will not assume responsibility for the design, installation, operation or control of any procedures. Members of SWAP who have transferred in to the department from other areas of South Somerset District Council will not be asked to review any aspects of their previous department's work until six months has passed since they left that area.

Relationship with the External Auditors/Other Regulatory Bodies

Internal Audit will co-ordinate its work with others wherever this is beneficial to the organisation.

Status of Internal Audit in the Organisation

The Head of the Internal Audit Partnership is responsible to the SWAP Management Board and the Partnership Board. The Head of Internal Audit Partnership and the Group Audit Manager also report to the Assistant Director (Finance and Corporate Services), as Section 151 Officer, and reports to the Audit Committee as set out below.

Appointment or removal of the Head of Internal Audit Partnership is the sole responsibility of the Partnership Board.

Scope and authority of Internal Audit work

There are no restrictions placed upon the scope of internal audit's work. Members of SWAP engaged on internal audit work are entitled to receive and have access to whatever information or explanations they consider necessary to fulfil their responsibilities to senior management. In this regard, internal audit may have access to any records, personnel or physical property of South Somerset District Council.

Internal audit work will normally include, but is not restricted to:

- reviewing the reliability and integrity of financial and operating information and the means used to identify, measure, classify and report such information;
- evaluating and appraising the risks associated with areas under review and make proposals for improving the management of risks;
- appraise the effectiveness and reliability of the enterprise risk management framework and recommend improvements where necessary;
- assist management and Members to identify risks and controls with regard to the objectives of the Council and its services;
- reviewing the systems established by management to ensure compliance with those policies, plans, procedures, laws and regulations which could have a significant impact on operations and reports, and determining whether South Somerset District Council is in compliance;
- reviewing the means of safeguarding assets and, as appropriate, verifying the existence of assets;

- appraising the economy, efficiency and effectiveness with which resources are employed;
- reviewing operations or programmes to ascertain whether results are consistent with established objectives and goals and whether the operations or programmes are being carried out as planned.
- reviewing the operations of the council in support of the council's anti-fraud and corruption policy.
- at the specific request of management, internal audit may provide consultancy services provided:
 - the internal auditors independence is not compromised
 - the internal audit service has the necessary skills to carry out the assignment, or can obtain such skills without undue cost or delay
 - the scope of the consultancy assignment is clearly defined and management have made proper provision for resources within the annual audit plan
 - management understand that the work being undertaken is not internal audit work.

Planning and Reporting

SWAP will submit to the Audit Committee, for information, an annual internal audit plan, setting out the recommended scope of their work in the period.

The annual plan will be developed with reference to the risks the organisation will be facing in the forthcoming year, whilst providing a balance of current and on-going risks, reviewed on a cyclical basis. The plan will be reviewed on a quarterly basis to ensure it remains current and addresses new and emerging risks.

SWAP will carry out the work as agreed, report the outcome and findings, and will make recommendations on the action to be taken as a result to the appropriate manager and Director. SWAP will report at least two times a year to the Audit Committee. SWAP will also report a summary of their findings, including any persistent and outstanding issues, to the Audit Committee on a regular basis.

Internal audit reports will normally be by means of a brief presentation to the relevant manager accompanied by a detailed report in writing. The detailed report will be copied to the relevant line management, who will already have been made fully aware of the detail and whose co-operation in preparing the summary report will have been sought. The detailed report will also be copied to the Assistant Director (Finance and Corporate Services), the Chief Executive Officer and to other relevant line management.

The Head of Internal Audit will submit an annual report to the Audit Committee providing an overall opinion of the status of risk and internal control within the council, based on the internal audit work conducted during the previous year.

In addition to the reporting lines outlined above, the Head of Internal Audit Partnership and the Group Audit Manager have the unreserved right to report directly to the Leader of the Council, The Chairman of the Audit Committee, the Chief Executive Officer or the External Audit Manager.

Revised February 2011

8. Treasury Management Performance to December 2010

Strategic Director: Mark Williams, Chief Executive
Assistant Director: Donna Parham, Finance and Corporate Services
Service Manager: Amanda Card, Finance Manager
Lead Officer: Karen Gubbins, Principal Accountant - Exchequer
Contact Details: karen.gubbins@southsomerset.gov.uk or (01935) 462456

Purpose of the Report

1. To review the treasury management activity and the performance against the Prudential Indicators for the nine months ended 31st December 2010.

Recommendations

2. The Audit Committee are asked to:
 - note the Treasury Management Activity for the nine-month period ended 31st December 2010;
 - note the position of the individual Prudential Indicators for the nine-month period ended 31st December 2010.

Summary of Investment Strategy for 2010/11

3. The Council's strategy for investments is based upon minimising risk and safeguarding the capital sum. There is a reliance on the investment income receivable in maintaining a balanced revenue budget and therefore the long-term strategy is to maintain stability by having a significant amount invested in fixed rate of return investment instruments.
4. Our minimum rating is A+ long term (or equivalent). Following the guidance from our advisors, Arlingclose we are keeping investments to a rolling programme of 12 months where cash flow permits.
5. The sum invested in longer dated securities at fixed rates of interest at the end of December represented 26% of the total portfolio. The sum invested in longer dated securities at variable rates of interest at the end of December represented 12% of the total portfolio. Investments made in longer dated securities comprise EuroSterling bonds and a Corporate bond; these investments have all been made following advice from our treasury advisers.
6. The Treasury Management Strategy Statement and Annual Investment Policy were both approved by Council on 18th March 2010. The strategy identified that the overall investment portfolio should, subject to current economic conditions, include investments in the following ranges:-

	%
Fund Managers and pooled managed funds.	0% - 25%
Term deposits (up to 2 years).	0% - 75%
3 – 5 year cash deposits.	0% - 25%
1 – 5 year callable deposits.	0% - 15%
1 – 5 year EuroSterling/Corporate Bonds.	10% - 75%

7. The table below compares the investment portfolio at 31st December 2010 to the investment strategy:-

	£'m	%	Strategic aim
Pooled Managed Funds and business reserve accounts	4.89	10.04	0% - 25%
Term deposits (up to 2 year)	25.00	51.35	0% - 75%
3 – 5 year cash deposits.	0	0	0% - 25%
1 – 5 year callable deposits.	0	0	0% - 15%
1 – 5 year EuroSterling/Corporate Bonds.	18.80	38.61	10% - 75%
	48.69	100.00	

The above table shows that the current investment portfolio broadly reflects the strategy.

Interest Rates 2010/11

8. Base rate began the financial year and remains at 0.5%.
9. Our advisors are forecasting that rates will continue at 0.5% during the remainder of this financial year with a likelihood of increasing by 0.25% in September 2011.

	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13
Official Bank Rate										
Upside risk	-	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.50	0.50	0.50	0.75	1.00	1.25	1.50	2.00	2.50	2.75
Downside risk	-	-	-	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50

Investment Portfolio

10. The total amount of investments has increased since 1st April due to the fact we are now nine months into the ten month council tax collection cycle.
11. The table below shows the Council's overall investments as at 31st December 2010:

	Value of Investments at 01.04.10 £	Value of Investments at 31.12.10 £	Fixed/ Variable Rate
Investments advised by Arlingclose			
Euro Sterling Bonds	9,850,072	7,561,574	Fixed
Corporate Bonds	5,336,559	5,243,425	Fixed
Euro Sterling Bonds	2,000,630	6,000,000	Variable
Total	17,187,261	18,804,999	
Internal Investments			
Short Term Deposits	19,000,000	25,000,000	Variable
Money Market Funds & Business Reserve Accounts	2,960,000	4,890,000	Variable
Total	21,960,000	29,890,000	
TOTAL INVESTMENTS	39,147,261	48,694,999	

AC

Returns for 2010/11

12. The returns to 31st December 2010 are shown in the table below:

	Actual Income £'000	% Rate of Return
Investments advised by Arlingclose		
Euro Sterling Bonds (Fixed)	363	
Corporate Bonds	175	
Euro Sterling Bonds (Variable)	33	
Total	571	3.81%
Internal Investments		
Short Term Deposits	245	
Money Market Funds & Business Reserve Accounts	38	
Total	283	1.27%
Other Interest		
Miscellaneous Loans	110	
Total	110	
TOTAL	964	
PROFILED BUDGETED INCOME	1011	
SHORTFALL	47	
BENCHMARK RATE OF RETURN		0.41%

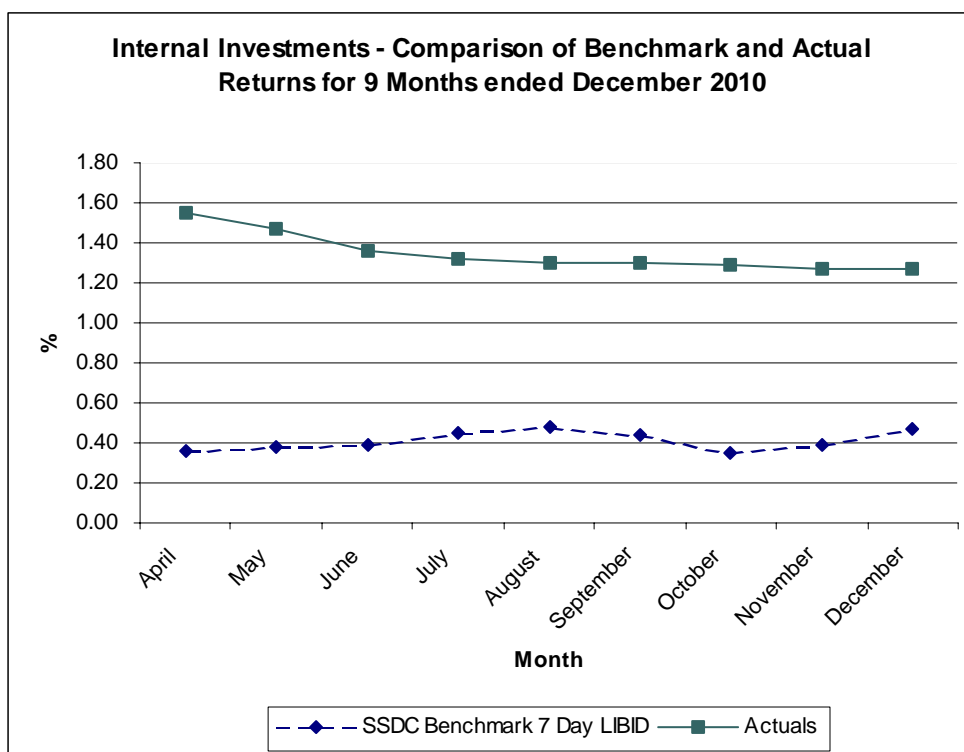
13. The table above shows investment income for the first nine months of the year compared to the profiled budget. The figures show a shortfall under budget of £47,000. We currently estimate that the position at the end of the financial year will be an adverse variance in the order of £67,000.

14. The outturn position is affected by both the amount of cash we have available to invest and the interest base rate set by the Bank of England. Balances are affected by the timing of capital expenditure and council tax and business rate collection.

15. The original Treasury Management budget of £1,347,620 was derived by forecasting an average rate of return of 2.74%. The actual interest rate received for nine months to the end of December was 2.23%.

Internal Investments (Short Term)

16. The graph below shows the In-house performance in respect of short-term investments as at 31st December 2010.



17. The current benchmark set for the in house team is the 7-day LIBID (London Interbank Bid) rate, which is the rate used for quick benchmarking by the CIPFA benchmarking club.

18. The above graph shows that the internal investments returns are consistently outperforming the benchmark by around 80 basis points. This is due to a large amount of our investment portfolio being in longer dated securities such as Eurobonds and Corporate Bonds as well as maintaining a rolling programme of 12 month term deposits where cash flow permits.

Borrowing

19. An actual overall borrowing requirement (CFR) of £9.6 million was identified at the beginning of 2010/11. As interest rates on borrowing exceed those on investments the Council has used its capital receipts to fund capital expenditure. As at 31st December 2010, the Council had no external borrowing.

AC

Prudential Indicators – Quarter 1 monitoring

Background:

20. In March 2010, Full Council approved the indicators for 2010/11, as required by the Prudential Code for Capital Finance in Local Authorities. The Local Government Act 2003 allows local authorities to determine their own borrowing limits provided they are affordable and that every local authority complies with the code.

Prudential Indicator 1 - Capital Expenditure:

21. The revised estimates of capital expenditure to be incurred for the current year compared to the original estimates are:

	2010/11 Original Estimate £'000	Expected outturn £'000	2010/11 Variance £'000	Reason for Variance
Approved capital schemes	9,301	8,828	(473)	Decrease arises from the reprofiling of expenditure to future years
Reserves	1,111	2,667	1,556	Slippage from 2009/10 accounts for the majority of the variance as well as an increase in the amount of money allocated to the affordable housing scheme
Total Expenditure	10,412	11,495	1,083	

22. The above table shows that the overall estimate for capital expenditure has increased.

Prudential Indicator 2 - Ratio of Financing Costs to Net Revenue Stream:

23. A comparison needs to be made between financing capital costs and the revenue income stream to support these costs. This shows how much of the revenue budget is committed to the servicing of finance.

Portfolio	2010/11 Revised Estimate £'000	Expected outturn £'000	2010/11 Variance £'000	Reason for Variance
Financing Costs	(1,368)	(1,074)	(294)	Interest rates forecast to stay lower for longer than originally anticipated
Net Revenue Stream	20,310	20,682	372	The budget has increased due to the approval of the carry forwards from 2009/10
%*	(6.7)	(5.2)		

24. The financing costs include interest payable and notional amounts set aside to repay debt less interest on investment income. The figure in brackets is due to investment income outweighing financing costs significantly for SSDC but is nevertheless relevant since it shows the extent to which the Council is dependent on investment income.

Prudential Indicator 3 - Capital Financing Requirement:

25. The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. Estimates of the year-end capital financing requirement for the authority are:

	2010/11 Original Estimate (Restated) £'000	Expected outturn £'000	2010/11 Variance £'000	Reason for Variance
Opening CFR	9,558	9,558	0	
Capital Expenditure	9,301	8,828	(473)	See explanations for indicator 1 above
Capital Receipts*	(7,116)	(4,447)	2,669	Reduced requirement to draw on Capital receipts due to extra grants being received as well as reprofiling of expenditure to future years
Grants/Contributions*	(2,185)	(4,381)	(2,196)	Additional grant money received: £1.3m towards Park Homes, £470k towards the Eco Town and £448k Housing Grant
Minimum Revenue Position (MRP)	(206)	(206)	0	
Closing CFR	9,352	9,352	0	

*Figures in brackets denote income through receipts or reserves.

Prudential Indicator 4 – Net external Borrowing compared to the medium term Capital Financing Requirement:

26. The Council is also required to ensure that any medium term borrowing is only used to finance capital and therefore it has to demonstrate that the net external borrowing does not, except in the short term exceed the total of capital financing requirements over a three year period.

	2010/11 Original Estimate (Restated) £'000	2010/11 Qtr 3 Actual £'000	2010/11 Variance £'000	Reason for Variance
Net Borrowing	(34,802)	(48,376)	(13,574)	Capital receipts totalling £422.5k have been received but not yet spent and we are nine months into the ten month Council Tax collection cycle
CFR	9,352	9,352	0	See explanations for indicator 3 above

27. The figures above in brackets described as net borrowing actually represent net investments. Our net borrowing is forecast to remain as net investment for the foreseeable future and therefore will not at any time be in excess of the capital financing requirement.

Prudential Indicator 5 - Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:

28. The Council must set three years of upper limits to its exposure to the effects of changes in interest rates. As a safeguard, it must ensure that its limit would allow it to have up to 100% invested in variable rate investments to cover against market fluctuations. For this purpose, term deposits of less than 365 days are deemed to be variable rate deposits. Fixed rate deposits are investments in Eurobonds, Corporate Bonds and term deposits exceeding 365 days.

	2010/11 % Limit	2010/11 Qtr 3 Actual %	2010/11 Variance %	Reason for Variance
Fixed	80	26	54	Within limit
Variable	100	74	26	Within limit

29. The Council must also set limits to reflect any borrowing we may undertake.

	2010/11 % Limit	2010/11 Qtr 3 Actual %	2010/11 Variance %	Reason for Variance
Fixed	100	0	100	SDDC currently has no borrowing
Variable	100	0	100	SDDC currently has no borrowing

30. The indicator has been set at 100% to maximise opportunities for future debt as they arise.

Prudential Indicator 6 - Upper Limit for total principal sums invested over 364 days:

31. SSDC must also set upper limits for any investments of longer than 364 days. The purpose of this indicator is to ensure that SSDC, at any time, has sufficient liquidity to meet all of its financial commitments.

Upper Limit for total principal sums invested over 364 days	2010/11 Maximum Limit £'000	2010/11 Qtr 3 Actual £'000	2010/11 Expected Outturn £'000	Reason for Variance
Between 1-2 years	25,000	2,137	3,209	Within limit
Between 2-3 years	20,000	1,071	6,000	Within limit
Between 3-4 years	10,000	7,136	1,136	Within limit
Between 4-5 years	10,000	0	0	Within limit
Over 5 years	5,000	0	0	Within limit

32. The table above shows that the Council adopts a policy of safeguarding its investments by minimising investments that are redeemable more than five years ahead.

Prudential Indicator 7 - Actual External Debt:

33. This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities (this represents our finance leases). This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2010	£'000
Borrowing	0
Other Long-term Liabilities	445
Total	445

Prudential Indicator 8 - Authorised Limit for External Debt:

34. This limit represents the maximum amount that SSDC may borrow at any point in time during the year. If this limit is exceeded the Council will have acted ultra vires. It also gives the Council the responsibility for limiting spend over and above the agreed capital programme. A ceiling of £12 million was set for each year.

	2010/11 Estimate £'000	2010/11 Qtr 3 Actual £'000	2010/11 Variance £'000	Reason for Variance
Borrowing	11,450	0	(11,450)	SSDC currently has no borrowing
Other Long-term Liabilities	550	239	(311)	Within limit
Total	12,000	239	(11,761)	

Prudential Indicator 9 – Operational Boundary for External Debt:

35. The operational boundary sets the limit for short term borrowing requirements for cash flow and has to be lower than the previous indicator, the authorised limit for external debt. A ceiling of £10 million for each of the next three years was set.

	2010/11 Estimate £'000	2010/11 Qtr 3 Actual £'000	2010/11 Variance £'000	Reason for Variance
Borrowing	9,500	0	(9,500)	SSDC currently has no borrowing
Other Long-term Liabilities	500	239	(261)	Within limit
Total	10,000	239	(9,761)	

Prudential Indicator 10 - Maturity Structure of Fixed Rate borrowing:

36. This indicator is relevant when we borrow, then we can take a portfolio approach to borrowing in order to reduce interest rate risk. This indicator is shown as the Council has set limits in anticipation of future borrowing.

Maturity structure of fixed rate borrowing	2010/11 Upper Limit %	2010/11 Lower Limit %	2010/11 Qtr 3 Actual %	2010/11 Variance %	Reason for Variance
Under 12 months	100	0	0	Not applicable	
12 months and within 24 months	100	0	0	Not applicable	
24 months and within 5 years	100	0	0	Not applicable	
5 years and within 10 years	100	0	0	Not applicable	
10 years and within 20 years	100	0	0	Not applicable	
20 years and within 30 years	100	0	0	Not applicable	
30 years and within 40 years	100	0	0	Not applicable	
40 years and within 50 years	100	0	0	Not applicable	
50 years and above	100	0	0	Not applicable	

Prudential Indicator 11 - Incremental Impact of Capital Investment Decisions:

37. SSDC must show the effect of its annual capital decisions for new capital schemes on the council taxpayer. Capital spend at SSDC is financed from additional receipts so the figure below actually shows the possible decreases in council tax if all capital receipts were invested rather than used for capital expenditure.

Incremental Impact of Capital Investment Decisions	2010/11 Original Estimate £
Decrease in Band D Council Tax	0.20

Prudential Indicator 12 - Adoption of the CIPFA Treasury Management Code:

38. This indicator demonstrates that the Council has adopted the principles of best practice.

Adoption of the CIPFA Code of Practice in Treasury Management
The Council approved the adoption of the CIPFA Treasury Management Code at its Council meeting on 18 th April 2002.

Conclusion

39. The council is currently within all of the Prudential Indicators and is not forecast to exceed them.

Background Papers: *Prudential Indicators Working Paper, Treasury Management Strategy Statement*

9. Treasury Management Strategy Statement and Investment Strategy 2011/12

Strategic Director: Mark Williams, Chief Executive
Assistant Director: Donna Parham, Finance and Corporate Services
Service Manager: Amanda Card, Finance Manager
Lead Officer: Karen Gubbins, Principal Accountant – Exchequer
Contact Details: karen.gubbins@southsomerset.gov.uk or (01935) 462456

Purpose of the Report

This report has been prepared for Audit Committee who have been tasked with the scrutiny of treasury management and to recommend to full Council the Treasury Management Strategy Statement and Investment Strategy for 2011/12.

Recommendation

To recommend the Treasury Management Strategy Statement and Investment Strategy for 2011/12 to full Council;

Background

The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis.

CIPFA has defined Treasury Management as:

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

The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Specific treasury management risks are identified in the Council's approved Treasury Management Practices. The risks include:

- Liquidity Risk (Adequate cash resources)
- Market or Interest Rate Risk (Fluctuations in the value of investments).
- Inflation Risks (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risks (Impact of debt maturing in future years).
- Legal & Regulatory Risk (Compliance with statutory and regulatory requirements).

The Local Government Act 2003 requires the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy; this sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The proposed strategy for 2011/12 takes into account the Council's current treasury position and the approved Prudential Indicators and draws upon the forecasts for interest rates provided by the Council's treasury advisers.

The Strategy is attached at Appendix 1 (pages 35-63) and is split into the following main areas:

- Background
- Balance Sheet and Treasury Position
- Outlook for Interest Rates
- Borrowing Requirement and Strategy
- Debt Rescheduling
- Investment Policy and Strategy
- Balanced Budget Requirement
- 2011/12 MRP Statement
- Reporting
- Other Items

Financial Implications

There are no financial implications in accepting this report and the associated recommendations.

Background Papers: *Cipfa Treasury Management Code of Practice*
Arlingclose Technical Paper – Revisions to the TM Code and Prudential Code
Treasury Management Practices

Treasury Management Strategy Statement and Investment Strategy 2011/12

Contents

- 1. Background**
- 2. Balance Sheet and Treasury Position**
- 3. Outlook for Interest Rates**
- 4. Borrowing Requirement and Strategy**
- 5. Investment Policy and Strategy**
- 6. Balanced Budget Requirement**
- 7. 2011/12 MRP Statement**
- 8. Reporting**
- 9. Other Items**

Appendices

- A. Current and Projected Portfolio Position
- B. Prudential Indicators
- C. Interest Rate Outlook: The Council's, Arlingclose's
- D. Specified Investments for use by the Council
- E. Non- Specified Investments for use by the Council
- F. Glossary of Terms

1. Background

1.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") requires local authorities to determine the Treasury Management Strategy Statement (TMSS). This statement also incorporates the Investment Strategy. Together, these cover the financing and investment strategy for the forthcoming financial year.

1.2 CIPFA has defined Treasury Management as:

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

1.3 The Council is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification, monitoring and control of risk is an important and integral element of its treasury management activities. The main risks to the Council's treasury activities are:

- Liquidity Risk (Adequate cash resources)
- Market or Interest Rate Risk (Fluctuations in the value of investments)
- Inflation Risk (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risk (Impact of debt maturing in future years)
- Legal & Regulatory Risk (Compliance with statutory and regulatory requirements)

2. Balance Sheet and Treasury Position

2.1 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The estimates, based on the current Revenue Budget and Capital Programmes, are set out below:

	31/03/11 Estimate £'000	31/03/12 Estimate £'000	31/03/13 Estimate £'000	31/03/14 Estimate £'000
CFR	9,352	9,226	9,164	9,134
Usable Capital Receipts	(28,473)	(30,434)	(28,266)	(27,205)
Balances & Reserves	(5,925)	(5,667)	(5,672)	(5,700)
Net Balance Sheet Position	(25,046)	(26,875)	(24,774)	(23,771)

2.2 The Council's level of physical debt and investments is linked to these components of the Balance Sheet. The current portfolio position is set out at Appendix A. Market conditions, interest rate expectations and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position.

- 2.3 As the CFR represents the level of borrowing (currently nil) for capital purposes and revenue expenditure cannot be financed from borrowing, net physical external borrowing should not exceed the CFR other than for short term cash flow requirements.
- 2.4 It is permissible under the Prudential Code to borrow in advance of need up to the level of the estimated CFR over the term of the Prudential Indicators. Where this takes place the cash will form part of the invested sums until the related capital expenditure is incurred. This being the case net borrowing should not exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years other than in the short term due to cash flow requirements.
- 2.5 The estimate for interest payments in 2011/12 is nil and for interest receipts is £799,620.

3. Outlook for Interest Rates

- 3.1 The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, is attached at Appendix C. The Council will reappraise its strategy from time to time and, if needs be, realign it in line with market conditions and expectations for future interest rates.

4. Borrowing Requirement and Strategy

- 4.1 The CFR represents the cumulative capital expenditure of the local authority that has not been financed. To ensure that this expenditure will ultimately be financed, local authorities are required to make a Minimum Revenue Provision for Debt Redemption (MRP) from within the Revenue budget each year.
- 4.2 Capital expenditure not financed from internal resources (i.e. Capital Receipts, Capital Grants and Contributions, Revenue or Reserves) will produce an increase in the CFR (the underlying need to borrow) and in turn produce an increased requirement to charge MRP in the Revenue Account.
- 4.3 Physical external borrowing may be greater or less than the CFR, but in accordance with the Prudential Code, the Council will ensure that net external borrowing does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years.
- 4.4 The cumulative estimate of the maximum long-term borrowing requirement is estimated by comparing the projected CFR with the profile of the current portfolio of external debt and long term liabilities over the same financial horizon, as follows:

	31/03/11 Estimate £'000	31/03/12 Estimate £'000	31/03/13 Estimate £'000	31/03/14 Estimate £'000
Capital Financing Requirement (CFR)	9,352	9,226	9,163	9,134
Less:				
Existing Profile of Borrowing and Other Long Term Liabilities	239	113	50	21
Cumulative Maximum External Borrowing Requirement	9,113	9,113	9,113	9,113
Balances & Reserves	0	0	0	0
Cumulative Net Borrowing Requirement (Call on capital receipts)	9,113	9,113	9,113	9,113

- 4.5 The Council's strategy is to maintain maximum control over any potential long term borrowing activities as well as flexibility on its loans portfolio. Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimize borrowing costs over the medium to longer term (should SSDC decide to borrow). A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the Council's Prudential Indicators.
- 4.6 In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Council will keep under review the following borrowing options:
- PWLB loans
 - Borrowing from other local authorities
 - Borrowing from institutions such as the European Investment Bank and directly from Commercial Banks
 - Borrowing from the Money Markets
 - Local authority stock issues
 - Local authority bills
 - Structured finance

The outlook for borrowing rates:

- 4.7 Following the CSR announcement which increased the cost of new local authority fixed rate loans to 1% above the cost of the Government's borrowing, the PWLB remains an attractive source of borrowing, given the transparency and control that its facilities continue to provide. The types of PWLB borrowing that are considered appropriate for a low interest rate environment are:
- Variable rate borrowing
 - Medium-term Equal Instalments of Principal (EIP) or Annuity Loans
 - Long-term Maturity loans, where affordable.
- 4.8 Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term and maintaining stability. The differential between debt costs and investment earnings, despite long term borrowing rates being at low levels, remains acute and this is expected to remain a feature during 2011/12. The "cost of carry" associated with medium- and long-term borrowing compared to temporary investment returns means that new fixed rate borrowing could entail additional short-

term costs. The use of internal resources in lieu of borrowing may again, in 2011/12, be the most cost effective means of financing capital expenditure.

- 4.9 The Council will undertake a financial options appraisal before any borrowing is made.
- 4.10 For any borrowing that may be undertaken in advance of need the Council will adopt the same rigorous policies and approach to the protection of capital as it does for the investment of its surplus balances.

5. Investment Policy and Strategy

Background

- 5.1 Guidance from CLG on Local Government Investments in England requires that an Annual Investment Strategy (AIS) be set.

Investment Policy

- 5.2 To comply with the CLG's guidance, the Council's general policy objective is to invest its surplus funds prudently. The Council's investment priorities are:

- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield which is commensurate with security and liquidity.

The CLG's Guidance on investments reiterates security and liquidity as the primary objectives of a prudent investment policy. The speculative procedure of borrowing purely in order to invest is unlawful.

- 5.3 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the CLG Guidance. Potential instruments for the Council's use within its investment strategy are contained in Appendix D.
- 5.4 Changes to the investment strategy for 2011/12 include:
- AAA-rated Variable Net Asset Value (VNAV) Money Market Funds
 - Treasury Bills
 - Local Authority Bills
 - Term deposits in Sweden
 - Maximum duration for new deposits 2 years
- 5.5 The Council's current level of investments is shown at Appendix A.

Investment Strategy

- 5.6 The UK Bank Rate has been maintained at 0.5% since March 2009, and it is anticipated to remain at low levels throughout 2011/12. Short-term money market rates are likely to remain at very low levels which will have a significant impact on investment income. The Medium Term Financial Plan has been updated to reflect the impact of long term low interest rates to ensure that the security of the sums invested remains paramount.

5.7 The Assistant Director (Finance and Corporate Services), under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported to the Audit Committee on a quarterly basis.

Investments managed in-house:

5.8 The Council's shorter term cash flow investments are made with reference to the outlook for the UK Bank Rate and money market rates.

5.9 In any period of significant stress in the markets, the default position is for investments to be made with the Debt Management Office or UK Treasury Bills (The rates of interest from the DMADF are below equivalent money market rates, but the returns are an acceptable trade-off for the guarantee that the Council's capital is secure)

5.10 The table below shows the strategic approach to treasury management and the overall portfolio should include investments within the following ranges dependant on overall economic conditions:

	%
Fund Managers and pooled managed funds	0% - 25%
Term Deposits (up to 2 years)	0% - 75%
3 – 5 year cash deposits	0% - 25%
1 – 5 year callable deposits	0% - 15%
1 – 10 year Eurosterling/Corporate Bonds	0% - 75%

5.11 This approach aims to promote a diverse mix of investments with funds placed aiming to give some measure of certainty and stability. The main aim however will be to minimise risk.

5.13 The Council selects countries and institutions within them, for the counterparty list after analysis and careful monitoring of:

- Credit Ratings (minimum long-term A+ for counterparties; AA+ for countries)
- Credit Default Swaps (where quoted)
- GDP; Net Debt as a Percentage of GDP
- Sovereign Support Mechanisms / potential support from a well-resourced parent institution
- Share Price (where quoted)
- Macro-economic indicators
- Corporate developments, news and articles, market sentiment

The Council and its Treasury Advisors, Arlingclose, will continue to analyse and monitor these indicators and credit developments on a regular basis and respond as necessary to ensure security of the capital sums invested.

5.14 To protect against a prolonged period of low interest rates and to provide certainty of income, 2-year deposits and longer-term secure investments will be actively considered within the limits the Council has set for Non-Specified Investments (see Appendix D). The longer-term investments will be likely to include:

- **Supranational bonds (bonds issued by multilateral development banks):** Even at lower yields likely to be in force, the return on these bonds will provide certainty of income against an outlook of low official interest rates.
- **Term Deposits with counterparties rated at least A+ (or equivalent)**

Investments managed externally

5.15 Currently the Council has no externally managed funds. However the following may be used once fully evaluated and with advice from Arlingclose;

5.16 Funds managed on a segregated basis: the Council will continue to evaluate funds managed externally. Fund Managers may be able to add value through the use of investments contained in Appendix D

5.17 Collective Investment Schemes (Pooled Funds): The Council will continue to evaluate the use of Pooled Funds and determine the appropriateness of their use within the investment portfolio. Pooled funds enable the Council to diversify the assets and the underlying risk in the investment portfolio and provide the potential for enhanced returns.

6. Balanced Budget Requirement

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

7. 2011/12 MRP Statement

Background:

7.1 For many years local authorities were required by Statute and associated Statutory Instruments to charge to the Revenue Account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the Revenue Account was referred to as the Minimum Revenue Provision (MRP). In practice MRP represents the financing of capital expenditure from the Revenue Account that was initially funded by borrowing.

7.2 In February 2008 the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [Statutory Instrument 2008/414] were approved by Parliament and became effective on 31 March 2008. These regulations replaced the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations required a local authority to determine each financial year an amount of MRP which it considers to be prudent. Linked to this new regulation, the Department of Communities and Local Government (CLG) produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.

7.3 The CLG Guidance recommends that before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by the Full Council.

- 7.4 The broad aim of the Policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure which gave rise to the debt provides benefits. In the case of borrowing supported by Revenue Support Grant, the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant. Where a local authority's overall CFR is £nil or a negative amount there is no requirement to charge MRP.
- 7.5 The move to International Financial Reporting Standards (IFRS) has meant that many Operating Leases have had to be reclassified as Finance Leases and been brought on Balance Sheet. Where this is the case, such items are classed in accounting terms as a form of borrowing. CLG has therefore proposed amending the Capital Finance Regulations to ensure that the impact on the Revenue account is neutral, with MRP for these items matching the principal repayment embedded within the lease agreement.

MRP Options:

- 7.6. Four options for prudent MRP provision are set out in the CLG Guidance. Details of each are set out below:

Option 1 – Regulatory Method:

- 7.7 This method replicates the position that would have existed under the previous Regulatory environment. MRP is charged at 4% of the Authority's underlying need to borrow for capital purposes, however this option allows a historical adjustment to take place that is beneficial to some authorities. This method can only be used for supported expenditure.

Option 2 – CFR Method:

- 7.8 This method simplifies the calculation of MRP by basing the charge solely on the authority's CFR but excludes the technical adjustments included in Option 1. The annual MRP charge is set at 4% of the CFR at the end of the preceding financial year. This method can only be used for supported expenditure.

Option 3 – Asset Life Method:

- 7.9 Under this method MRP is determined by the life of the asset for which the borrowing is undertaken. This can be calculated by either of the following methods:
- (a) Equal Installments: where the principal repayment made is the same in each year,
or
 - (b) Annuity: where the principal repayments increase over the life of the asset.
The annuity method has the advantage of linking MRP to the benefits arising from capital expenditure, where these benefits are expected to increase over the life of the asset.
- 7.10 MRP commences in the financial year following that in which the expenditure is incurred or, in the year following that in which the relevant asset becomes operational. This enables an MRP "holiday" to be taken in relation to assets which take more than one year to be completed before they become operational.

- 7.11 The estimated life of the asset will be determined in the year that MRP commences and cannot be revised. However, additional repayments can be made in any year which will reduce the level of payments in subsequent years.
- 7.12 If no life can be reasonably attributed to an asset, such as freehold land, the life is taken to be a maximum of 50 years. In the case of freehold land on which a building or other structure is constructed, the life of the land will be treated as equal to that of the structure, where this would exceed 50 years.
- 7.13 In instances where central government permits revenue expenditure to be capitalised, the Statutory Guidance sets out the number of years over which the charge to revenue must be made.
- 7.14 MRP in respect of Operating Leases brought on Balance Sheet under IFRS falls under Option 3.

Option 4 - Depreciation Method:

- 7.15 The depreciation method is similar to that under Option 3 but MRP is equal to the depreciation provision required in accordance with proper accounting practices to be charged to the Income and Expenditure account

MRP Policy for 2011/12:

- 7.16 It is proposed that for 2011/12 the Council adopts Option 3 – Asset Life Method. Option 3 enables the calculation of MRP to be aligned with the life of the asset. If it is ever proposed to vary the terms of this MRP Statement during the year, a revised statement will be made to Council at that time.

8. Reporting on Treasury Management

The scrutiny of the treasury management function is carried out by the Audit Committee who then make recommendations to Full Council. The Assistant Director (Finance and Corporate Services) will report to Council/Audit Committee on treasury management activity / performance as follows:

- (a) Audit Committee will be responsible for the scrutiny of treasury management activity and practices.
- (b) Audit Committee will review the Treasury Management Strategy Statement, Investment Strategy, MRP Statement, and Prudential Indicators twice per year and recommend them to Council for Approval
- (c) Audit Committee will monitor Treasury Management activity quarterly and annually and will approve the Treasury Management Practices on an annual basis
- (d) Full Council will receive the Treasury Management Strategy Statement, Investment Strategy, MRP Statement, and Prudential Indicators prior to the start of the financial year and a mid year review against the strategy approved for the year.
- (e) The Council will produce an outturn report on its treasury activity no later than 30th September after the financial year end.

9. Other Items

Training

CIPFA's revised Code requires the Assistant Director (Finance and Corporate Services) to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities.

Officers tasked with treasury management responsibilities are engaged in regular financial and treasury training through attendance at selective seminars/workshops and treasury courses.

Treasury Consultants

The CLG's Draft revisions to its Guidance on local government investments recommend that the Investment Strategy should state:

- Whether and, if so, how the authority uses external contractors offering information, advice or assistance relating to investment and;
- How the quality of any such service is controlled.

The Council appointed Arlingclose as its Treasury Advisers in 2005. The provision of treasury advisory services was formally re-tendered in autumn 2009 and Arlingclose was reappointed. Among the various services received is **advice** on capital financing, borrowing and investments appropriate to the Council's individual circumstances and objectives.

The Council monitors the service through measuring:

- The timeliness of advice
- The returns from investments
- The accuracy of technical advice
- Regular market testing
- Regular internal meetings to discuss performance
- Measurement through CIPFA's benchmarking club
- Direct access to a nominated advisor
- The quality and content of training courses

However, this doesn't divest the Council from its responsibility of its treasury decisions.

Publication

The CLG's Draft revisions to its Guidance on local government investments recommend that the initial strategy and any revised strategy should, when approved, be made available to the public free of charge, in print or online.

The Council makes available online its Treasury Management Strategies within the finance section of the website. This includes both the initial strategy as well as any revisions. Should any member of the public request a printed copy, this would be provided free of charge.

EXISTING PORTFOLIO PROJECTED FORWARD

	31/03/10 £'000	31/03/11 Estimate £'000	31/03/12 Estimate £'000	31/03/13 Estimate £'000	31/03/14 Estimate £'000
External Borrowing:	0	0	0	0	0
Long-term liabilities					
- Finance Leases	445	239	113	50	21
Total External Debt	445	239	113	50	21
Investments:					
<i>Managed in-house</i>					
• Deposits and monies on call and Money Market Funds	21,960	20,870	27,560	28,609	34,585
• Supranational bonds	11,851	13,526	9,209	7,101	1,101
• Corporate bonds	5,337	5,243			
Total Investments	39,148	39,639	36,769	35,710	35,686
(Net Borrowing Position)/ Net Investment position	38,703	39,400	36,656	35,660	35,665

PRUDENTIAL INDICATORS 2010/11 TO 2012/13

Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators.

Net Borrowing and the Capital Financing Requirement:

This is a key indicator of prudence. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that the net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

The Assistant Director Finance and Corporate Services reports that the authority had no difficulty meeting this requirement in 2010/11, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

Prudential Indicator 1 - Capital Expenditure:

This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council. The actual expenditure for 2009/10 and the estimates of capital expenditure to be incurred for the current and future years are:

	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Approved capital schemes	6,446	8,828	5,034	1,850	403
Investments	0	0	0	0	0
Reserves	1,932	2,667	1,168	803	600
New Schemes for 2010/11 start	0	0	307	0	0
Total Expenditure	8,378	11,495	6,509	2,653	1,003

The figures in the later years are lower at this stage but will increase as anticipated capital projects are approved. Additional capital expenditure will also occur if new capital receipts are received and used to finance projects currently on the reserve list, as per the capital strategy.

Prudential Indicator 2 - 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. This shows how much of the revenue budget is committed to the servicing of finance.

Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2009/10 are:

Portfolio	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Financing Costs*	(2,218)	(1,074)	(673)	(383)	(208)
Net Revenue Stream	19,765	20,682	17,345	16,356	16,255
%*	(11.2)	(5.2)	(3.9)	(2.3)	(1.3)

*Figures in brackets denote income through receipts or reserves.

The financing costs include interest payable, notional amounts set aside to repay debt, less, interest on investment income. The figures are in brackets due to investment income outweighing financing costs significantly for SSDC. This shows the extent that the Council is dependent on investment income.

The percentages are falling as the revenue stream increases, i.e. the budget requirement is becoming larger and the investment income smaller as more capital is spent.

Prudential Indicator 3 - Capital Financing Requirement:

The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. Estimates of the year-end capital financing requirement for the authority are:

	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Opening CFR	9,738	9,558	9,352	9,226	9,164
Capital Expenditure	6,446	8,828	5,034	1,850	403
Capital Receipts*	(4,353)	(4,447)	(1,370)	(885)	342
Grants/Contributions*	(2,093)	(4,381)	(3,664)	(965)	(61)
MRP	(180)	(206)	(126)	(62)	(30)
Closing CFR	9,558	9,352	9,226	9,164	9,134

*Figures in brackets denote income through receipts or reserves.

The capital financing requirement has changed due to the way we need to account for leases.

Prudential Indicator 4 – Net external Borrowing compared to the medium term Capital Financing Requirement:

The Council is also required to ensure that any medium term borrowing is only used to finance capital and therefore it has to demonstrate that the net external borrowing does not, except in the short term exceed the total of capital financing requirements over a three year period.

	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Net Borrowing*	(38,198)	(48,376)	(46,434)	(44,266)	(43,205)
CFR	9,558	9,352	9,226	9,164	9,134

*The figures in brackets show the estimated level of investments we currently have.

Prudential Indicator 5 - Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:

The Council must set three years of upper limits to its exposure to the effects of changes in interest rates. As a safeguard, it must ensure that its limit would allow it to have up to 100% invested in variable rate investments to cover against market fluctuations. Overall the authority is aiming to keep within the following exposure to fixed rates as and when market conditions improve.

	2009/10 % Actual	2010/11 % Probable Outturn	2011/12 % Limit	2012/13 % Limit	2013/14 % Limit
Fixed	38.7	26.3	80	80	80
Variable	61.3	73.7	100	100	100

The Council must also set limits to reflect any borrowing we may undertake.

	2009/10 % Actual	2010/11 % Probable Outturn	2011/12 % Limit	2012/13 % Limit	2013/14 % Limit
Fixed	0	0	100	100	100
Variable	0	0	100	100	100

The indicator has been set at 100% to maximise opportunities for future debt as they arise.

Prudential Indicator 6 - Upper Limit for total principal sums invested over 364 days:

The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested.

Upper Limit for total principal sums invested over 364 days	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Between 1-2 years	8,604	3,209	25,000	25,000	25,000
Between 2-3 years	3,296	6,000	20,000	20,000	20,000
Between 3-4 years	2,001	1,136	10,000	10,000	10,000
Between 4-5 years	1,160	0	10,000	10,000	10,000
Over 5 years	0	0	5,000	5,000	5,000

The estimates are considerably higher than the actual balances held in 2009/10 and 2010/11 to ensure the Council has sufficient flexibility to deal with any unexpected events. **The overall limit for maturities of greater than 364 days will not exceed 70% of the portfolio.**

Prudential Indicator 7 - Actual External Debt:

This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2010	£'000
Borrowing	0
Other Long-term Liabilities	445
Total	445

Prudential Indicator 8 - Authorised Limit for External Debt:

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

This limit represents the maximum amount that SSDC may borrow at any point in time during the year. If this limit is exceeded the Council has acted ultra vires. It also gives the Council the responsibility for limiting spend over and above the agreed capital programme. The results for 2009/10 and 2010/11 show that this limit has not been used. A £9.1m borrowing requirement has been identified to finance the capital programme and further borrowing may be undertaken to increase our borrowing to this level if and when it is the most cost effective way of funding SSDC's requirements. A ceiling of £12 million for each of the next three years is recommended, to allow flexibility to support new capital projects over and above the identified borrowing requirement.

The move to local authorities implementing International Financial Reporting Standards (IFRS) has had implications for the Capital Financing Requirement components on the Balance Sheet. Analysis of the Council's leases against IFRS implications have resulted in the related assets and liabilities being brought onto the Council's balance sheet.

	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Borrowing	0	0	11,600	11,600	11,600
Other Long-term Liabilities	445	239	400	400	400
Total	445	239	12,000	12,000	12,000

Prudential Indicator 9 – Operational Boundary for External Debt:

The Operational Boundary sets the limit for short term borrowing requirements for cash flow and has to be lower than the previous indicator, the authorised limit for external debt. A ceiling of £10 million is recommended for each of the next three years. The table overleaf shows that SSDC's current borrowing is well within this limit. This indicator more than covers the capital financing requirement.

The Assistant Director (Finance and Corporate Services) has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next Council meeting.

	2009/10 Actual £'000	2010/11 Probable Outturn £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Borrowing	0	0	9,700	9,700	9,700
Other Long-term Liabilities	445	239	300	300	300
Total	445	239	10,000	10,000	10,000

Prudential Indicator 10 - Maturity Structure of Fixed Rate borrowing:

This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. The maturity of borrowing is determined by reference to the earliest date on which the lender can require payment.

Maturity structure of fixed rate borrowing	2009/10 % Actual	2010/11 % Probable Outturn	Lower Limit %	Upper Limit %
Under 12 months	0	0	0	100
12 months and within 24 months	0	0	0	100
24 months and within 5 years	0	0	0	100
5 years and within 10 years	0	0	0	100
10 years and within 20 years	0	0	0	100
20 years and within 30 years	0	0	0	100
30 years and within 40 years	0	0	0	100
40 years and within 50 years	0	0	0	100
50 years and above	0	0	0	100

As the council doesn't have any fixed rated external borrowing at present the above upper and lower limits have been set to allow flexibility to borrow within any of the maturity bands.

Prudential Indicator 11 - Incremental Impact of Capital Investment Decisions:

SSDC must show the effect of its annual capital decisions for new capital schemes on the council taxpayer. Capital spend at SSDC is financed from additional receipts so the figures below actually show the possible decreases in council tax if all capital receipts were invested rather than used for capital expenditure.

Incremental Impact of Capital Investment Decisions	2009/10 Approved £	2010/11 Approved £	2011/12 Estimate £	2012/13 Estimate £	2013/14 Estimate £
Decrease in Band D Council Tax	0.92	0.20	0.20	0.20	0.20

Prudential Indicator 12 - Adoption of the CIPFA Treasury Management Code:

This indicator demonstrates that the Council has adopted the principles of best practice.

Adoption of the CIPFA Code of Practice in Treasury Management

The Council approved the adoption of the CIPFA Treasury Management Code at its Council meeting on 18 th April 2002.
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Arlingclose's Economic and Interest Rate Forecast

	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13
Official Bank Rate											
Upside risk	-	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.50	0.50	0.50	0.75	1.00	1.25	1.50	2.00	2.50	2.75	2.75
Downside risk	-	-	-	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
1-yr LIBID											
Upside risk	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.50	1.75	2.00	2.25	2.50	2.75	3.00	3.25	3.50	3.50	3.50
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
5-yr gilt											
Upside risk	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	2.00	2.25	2.75	3.25	3.50	3.75	4.00	4.00	4.00	4.00	4.00
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
10-yr gilt											
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50
Central case	3.50	3.75	3.75	4.00	4.25	4.50	4.75	4.75	4.75	4.75	4.75
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
20-yr gilt											
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50
Central case	4.25	4.50	4.75	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
50-yr gilt											
Upside risk	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	4.25	4.25	4.50	4.75	4.75	4.75	4.75	4.50	4.50	4.50	4.50
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25

- The recovery in growth is likely to be slow and uneven.
- The initial reaction to the CSR is positive, but implementation risks remain.
- The path of base rates reflects the fragility of the recovery and the significantly greater fiscal tightening of the emergency budget. With growth and underlying inflation likely to remain subdued, the Bank will stick to its lower for longer stance on policy rates.
- Uncertainty surrounding Eurozone sovereign debt and the risk of contagion will remain a driver of global credit market sentiment.

Underlying Assumptions

- The framework and targets announced in the Comprehensive Spending Review (CSR) to reduce the budget deficit and government debt will be put to the test; meeting the 2010 borrowing target of £149bn will be crucial to the gilt market's confidence in the credibility of the deficit reduction plans.
- Despite Money Supply being weak and growth prospects remaining subdued, the MPC has gravitated towards increasing rates in the new year as global inflation continues to rise along with household inflation.
- Consumer Price Inflation is stubbornly above 3% and is likely to spike above 4% in the first quarter of 2011 as a result of VAT, Utilities and Rail Fares.

- Unemployment remains near a 16 year high, at just over 2.5 Million, and is set to increase as the Public Sector shrinks. Meanwhile employment is growing but this is mainly due to part time work, leaving many with reduced income
- Recently announced Basel III capital/liquidity rules and extended timescales are positive for banks. Restructuring of UK banks' balance sheets is ongoing and expected to take a long time to complete. This will be a pre-condition for normalisation of credit conditions and bank lending.
- Mortgage repayment, a reduction in net consumer credit and weak consumer confidence are consistent with lower consumption and therefore the outlook for growth.
- The US Federal Reserve downgraded its outlook for US growth; the Fed is concerned enough to signal further QE through asset purchases. Industrial production and growth in the Chinese economy are showing signs of slowing. Both have implications for the global economy.

Specified and Non Specified Investments

Specified Investments identified for use by the Council

Specified Investments will be those that meet the criteria in the CLG Guidance, i.e. the investment

- is sterling denominated
- has a maximum maturity of 1 year
- meets the “high” credit criteria as determined by the Council or is made with the UK government or is made with a local authority in England, Wales, Scotland or Northern Ireland or a parish or community council.
- the making of which is not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate).

“Specified” Investments identified for the Council’s use are:

- Deposits in the DMO’s Debt Management Account Deposit Facility
- Deposits with UK local authorities
- Deposits with banks and building societies
- *Certificates of deposit with banks and building societies
- *Gilts : (bonds issued by the UK government)
- *Bonds issued by multilateral development banks
- Treasury-Bills (T-Bills)
- Local Authority Bills (LA Bills)
- AAA-rated Money Market Funds with a Constant Net Asset Value (CNAV)
- AAA-rated Money Market Funds with a Variable Net Asset Value (VNAV)
- Other Money Market Funds and Collective Investment Schemes– i.e. credit rated funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573.

1. ** Investments in these instruments will be on advice from the Council’s treasury advisor.*

2. *The use of the above instruments by the Council’s fund manager(s) will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.*

For credit rated counterparties, the minimum criteria will be the lowest equivalent short-term and long-term ratings assigned by various agencies which may include Moody's Investors Services, Standard & Poor's, Fitch Ratings.

Long-term minimum: A1 (Moody's) or A+ (S&P) or A+(Fitch)

Short-term P-1 (Moody's) or A-1 (S&P) or F1 (Fitch).

The Council will also take into account information on corporate developments of and market sentiment towards investment counterparties.

New specified investments will be made within the following limits:

Instrument	Country/ Domicile	Counterparty	Maximum Counterparty Limits %/£m
Term Deposits	UK	DMADF, DMO	No limit
Term Deposits/Call Accounts	UK	Other UK Local Authorities	No limit
Term Deposits/Call Accounts	UK	Counterparties rated at least A+ Long Term and F1 Short Term (or equivalent)	
Term Deposits/Call Accounts	Non-UK	Counterparties rated at least A+ Long Term and F1 Short Term (or equivalent) in select countries with a Sovereign Rating of at least AA+	
Gilts	UK	DMO	No limit
T-Bills	UK	DMO	No limit
LA-Bills	UK	Other UK Local Authorities	No limit
Bonds issued by multilateral development banks		(For example, European Investment Bank/Council of Europe, Inter American Development Bank)	
AAA-rated Money Market Funds	UK/Ireland/ Luxembourg domiciled	CNAV MMFs VNAV MMFs (where there is greater than 12 month history of a consistent £1 Net Asset Value)	
Other MMFs and CIS	UK/Ireland/ Luxembourg domiciled	Pooled funds which meet the definition of a Collective Investment Scheme per SI 2004 No 534 and subsequent amendments	

Our Current Counterparty list is as follows:

Instrument	Country	Counterparty	Maximum Counterparty Limit %/£m	Maximum Group Limit (if applicable) %/£
Term Deposits	UK	DMADF, DMO	No limit	
Term Deposits/Call Accounts	UK	Other UK Local Authorities	No limit	
Term Deposits/Call Accounts	UK	Santander UK Plc (Banco Santander Group)	£6,000,000	
Term Deposits/Call Accounts	UK	Bank of Scotland (Lloyds Banking Group)	£6,002,000	£9,002,000
Term Deposits/Call Accounts	UK	Lloyds TSB (Lloyds Banking Group)	£6,000,000	
Term Deposits/Call Accounts	UK	Barclays Bank Plc	£6,000,000	
Term Deposits/Call Accounts	UK	Clydesdale (This is part of the NAB group which has a combined limit of £6m)	£6,000,000	£6,000,000
Term Deposits/Call Accounts	UK	HSBC Bank Plc	£6,000,000	
Term Deposits/Call Accounts	UK	Nationwide Building Society	£6,000,000	
Term Deposits/Call Accounts	UK	Royal Bank of Scotland	£6,000,000	
Term Deposits/Call Accounts	UK	Standard Chartered Bank	£6,000,000	
Term Deposits/Call Accounts	Australia	Australia and NZ Banking Group	£6,000,000	
Term Deposits/Call Accounts	Australia	Commonwealth Bank of Australia	£6,000,000	
Term Deposits/Call Accounts	Australia	National Australia Bank Ltd (National Australia Bank Group)	See Clydesdale above	£6,000,000
Term Deposits/Call Accounts	Australia	Westpac Banking Corp	£6,000,000	
Term Deposits/Call Accounts	Canada	Bank of Montreal	£6,000,000	

Instrument	Country	Counterparty	Maximum Counterparty Limit %/£m	Maximum Group Limit (if applicable) %/£
Term Deposits/Call Accounts	Canada	Bank of Nova Scotia	£6,000,000	
Term Deposits/Call Accounts	Canada	Canadian Imperial Bank of Commerce	£6,000,000	
Term Deposits/Call Accounts	Canada	Royal Bank of Canada	£6,000,000	
Term Deposits/Call Accounts	Canada	Toronto-Dominion Bank	£6,000,000	
Term Deposits/Call Accounts	Finland	Nordea Bank Finland	£6,000,000	
Term Deposits/Call Accounts	France	BNP Paribas	£6,000,000	
Term Deposits/Call Accounts	France	Credit Agricole CIB (Credit Agricole Group)	£6000,000	£6,000,000
Term Deposits/Call Accounts	France	Credit Agricole SA (Credit Agricole Group)	£6,000,000	
Term Deposits/Call Accounts	France	Societe Generale	£6,000,000	
Term Deposits/Call Accounts	Germany	Deutsche Bank AG	£6,000,000	
Term Deposits/Call Accounts	Netherlands	ING Bank NV	£6,000,000	
Term Deposits/Call Accounts	Netherlands	Rabobank	£6,000,000	
Term Deposits/Call Accounts	Sweden	Svenska Handelsbanken	£6,000,000	
Term Deposits/Call Accounts	Switzerland	Credit Suisse	£6,000,000	
Term Deposits/Call Accounts	US	JP Morgan	£6,000,000	

NB Any existing deposits outside of the current criteria will be reinvested with the above criteria on maturity.

Non-Specified Investments determined for use by the Council

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use:

	In-house use	Use by fund managers	Maximum maturity	Max % of portfolio	Capital expenditure?
<ul style="list-style-type: none"> ▪ Deposits with banks and building societies ▪ Certificates of deposit with banks and building societies 	<p>✓</p> <p>✓</p>	<p>✓</p>	5 yrs	70% in aggregate	No
<ul style="list-style-type: none"> ▪ Gilts ▪ Bonds issued by multilateral development banks ▪ Bonds issued by financial institutions guaranteed by the UK government ▪ Sterling denominated bonds by non-UK sovereign governments 	<p>✓ (on advice from treasury advisor)</p>	<p>✓</p>	10 years	70% in aggregate	No
Money Market Funds and Collective Investment Schemes which are not credit rated	<p>✓ (on advice from treasury advisor)</p>	<p>✓</p>	These funds do not have a defined maturity date	50%	No
Government guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies (e.g. govt bonds issued by HBOS / RBS / Nationwide, etc)	<p>✓</p>	<p>✓</p>	10 years	£15m	Yes

	In-house use	Use by fund managers	Maximum maturity	Max % of portfolio	Capital expenditure?
Non-guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	✓	✓	10 years	£5m	Yes
Collective Investment Schemes (Pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No 534 or SI 2007 No 573	✓ (on advice from treasury advisor)	✓	These funds do not have a defined maturity date	£5m	Yes

Investments which constitute capital expenditure will not in aggregate exceed £20m.

1. In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.
2. The use of the above instruments by the Council's fund manager(s) will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.

Glossary of Terms

Balances and Reserves	Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.
Bank Rate	The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.
Bond	A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The price of a bond may vary during its life.
Capital Expenditure	Expenditure on the acquisition, creation or enhancement of capital assets
Capital Financing Requirement (CFR)	The Council's underlying need to borrow for capital purposes representing the cumulative capital expenditure of the local authority that has not been financed.
Capital growth	Increase in the value of the asset (in the context of a collective investment scheme, it will be the increase in the unit price of the fund)
Capital receipts	Money obtained on the sale of a capital asset.
Credit Rating	Formal opinion by a registered rating agency of a counterparty's future ability to meet its financial liabilities; these are opinions only and not guarantees.
Collective Investment Schemes	Funds in which several investors collectively hold units or shares. The assets in the fund are not held directly by each investor, but as part of a pool (hence these funds are also referred to as 'Pooled Funds'). Unit Trusts and Open-Ended Investment Companies are types of collective investment schemes / pooled funds.
Corporate Bonds	Corporate bonds are bonds issued by companies. The term is often used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.
Corporate Bond Funds	Collective Investment Schemes investing predominantly in bonds issued by companies and supranational organisations.
CPI	Consumer Price Index. (This measure is used as the Bank of England's inflation target.)
Credit default swaps	Financial instrument for swapping the risk of debt default; the buyer effectively pays a premium against the risk of default.
Diversification / diversified exposure	The spreading of investments among different types of assets or between markets in order to reduce risk.
ECB	European Central Bank

Federal Reserve	The US central bank. (Often referred to as “the Fed”)
Floating Rate Notes	A bond issued by a company where the interest rate paid on the bond changes at set intervals (generally every 3 months). The rate of interest is linked to LIBOR and may therefore increase or decrease at each rate setting
Gilt	Is a fixed rate security issued as debt and repaid at a future date.
IFRS	International Financial Reporting Standards
Income Distribution	The payment made to investors from the income generated by a fund; such a payment can also be referred to as a ‘dividend’
Maturity	The date when an investment or borrowing is repaid
Money Market Funds (MMF)	Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity.
Minimum Revenue Provision	An annual provision that the Authority is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets
Non-Specified Investments	Term used in the Communities and Local Government Guidance and Welsh Assembly Guidance for Local Authority Investments. It includes any investment for periods greater than one year or those with bodies that do not have a high credit rating, use of which must be justified.
Pooled funds	See Collective Investment Schemes (above)
Prudential Code	Developed by CIPFA as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice
Prudential Indicators	Indicators determined by the local authority to define the its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators
PWLB	Public Works Loans Board. It is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.
Revenue Expenditure	Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges
SI (Statutory Instrumeny)	Is the principal form in which delegated or secondary legislation is made in Great Britain.
SORP	Statement of Recommended Practice for Accounting (Code of Practice on Local Authority Accounting in the United Kingdom).

Specified Investments	Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than 1 year. UK government, local authorities and bodies that have a high credit rating.
Supranational Bonds	Instruments issued by supranational organisations created by governments through international treaties (often called multilateral development banks). The bonds carry a AAA rating in their own right. Examples of supranational organisations are the European Investment Bank, the International Bank for Reconstruction and Development.
Supported Capital Expenditure	The financing element of Capital expenditure that is grant funded by Central Government
Treasury Management Code	CIPFA's Code of Practice for Treasury Management in the Public Services
Temporary Borrowing	Borrowing to cover peaks and troughs of cash flow, not to fund spending.
Term Deposits	Deposits of cash with terms attached relating to maturity and rate of return (interest)
Unsupported Capital Expenditure	The financing of Capital expenditure is financed internally through the revenue budget
Yield	The measure of the return on an investment instrument

10. Accounting Policies for 2010/11 Statement of Accounts

Strategic Director: Mark Williams, Chief Executive
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Purpose of the Report

To request that members of the Audit Committee approve the Accounting Policies for 2010/11 so that the Statement of Accounts 2010/11 can be prepared on this bases.

Recommendation

That members approve the Accounting Policies, paying particular attention to the key accounting policy changes as a result of moving towards International Financial Reporting Standards.

Background

It is a statutory requirement for all local authority financial statements to be IFRS compliant by 2010/11. In order to prepare IFRS compliant accounts by 2010/11, the Council needs to revise its accounting policies.

The introduction of IFRS will significantly change the way that local authority accounts are prepared and a large number of areas will be subject to different accounting treatments. The proposed Accounting Policies are attached in Appendix 1 (pages 66-82).

Key Accounting Policy Changes

The key accounting policy changes impacting on the Council are outlined below:

Property, Plant & Equipment

- **Component Accounting**

IFRS places a greater emphasis on component accounting. Where components of an asset are significant in value in relation to the total value of the asset as a whole, and they have substantially different economic lives, they should be recognised separately.

There is no requirement to apply these changes retrospectively and instead components should be recognised separately as and when they are replaced.

- **Investment Property**

Under IFRS, investment property is defined as a property that is held exclusively for revenue generation or for the capital gains that the asset is expected to generate. In this respect, the asset is not used directly to deliver the Council's services. Investment properties are initially measured at cost and thereafter at market value.

- **Non-Current Assets Held For Sale (new)**

Assets meeting this classification are those where the value of the asset will be recovered through selling the asset rather than through usage. To be classed as such the asset must meet the following criteria:

- Be available for immediate sale in its present condition.
- Its sale must be highly probable.
- Management expects the sale to take place within twelve months.

Assets held for sale are to be valued at the lower of their existing balance sheet value or their estimated sale price less costs to sell.

Government and Grants & Other Capital Contributions

Under the current SORP arrangements, grants received by the Council towards capital expenditure are held in a Government/ Capital Contributions account and written off to Revenue over the life of the asset the grant was used to purchase.

Under IFRS, all such grants are to be treated as revenue income as soon as any conditions relating to the grant have been met.

Leases & Lease Type Arrangements

Leases can be classified as either finance or operating leases. If a lease transfers substantially all the risks and rewards incidental to ownership it will be classified as a finance lease regardless of its legal form.

For assets leased under a finance lease, the asset value should be recognised as either an asset or a liability in the Balance Sheet as appropriate and the annual payments consist of an amount of interest plus an amount to clear the relevant debtor or creditor. Leases that do not meet the definition of finance leases are accounted for as operating leases and the income or expenditure is either credited, or charged to, service revenue accounts on a straight-line basis over the term of the lease

Under IFRS, the land and buildings elements of a lease of land and buildings require separate identification for both lease classification and subsequent valuation. In most cases, the land element of a lease will be an operating lease.

Employee Benefits

A new requirement under IFRS is that the Council must make an accrual in its accounts at year end for any annual leave and flexible working entitlement earned but not taken by employees at the end of the financial year.

Financial Implications

There are no financial implications in accepting this report and the associated recommendations.

Background Papers: *Audit Committee – 28th January 2010 - Preparation of 2010/11 Statement of Accounts and IFRS*
Audit Committee – 27th January 2011 - Preparation of 2010/11 Statement of Accounts and IFRS
Statement of Accounts 2008/09
Statement of Accounts 2009/10

1. General Principles

The Statement of Accounts summarises the Council's transactions for the 2010/11 financial year and its position at the year-end of 31 March 2011. The Authority is required to prepare an annual Statement of Accounts by the Accounts and Audit Regulations 2003, which those regulations require to prepare in accordance with proper accounting practices. These practices primarily comprise the Code of Practice on Local Authority Accounting in the United Kingdom 2010/11 and the Best Value Accounting Code of Practice 2010/11, supported by International Financial Reporting Standards (IFRS) and statutory guidance issued under section 12 of the 2003 Act.

The accounting convention adopted is principally historical cost, modified by the evaluation of certain categories of non-current assets and financial instruments.

2. Accruals of Income and Expenditure

Activity is accounted for in the year that it takes place, not simply when cash payments are made or received. In particular:

- Fees, charges and rents due from customers are accounted for as income at the date the Council provides the relevant goods or services.
- Supplies are recorded as expenditure when they are consumed – where there is a gap between the date supplies are received and their consumption, they are carried as inventories on the Balance Sheet.
- Works are charged as expenditure when they are completed, before which they are carried as works in progress on the balance sheet.
- Interest payable on borrowings and receivable on investments is accounted for on the basis of the effective interest rate for the relevant financial instrument rather than the cash flows fixed or determined by the contract.
- Where income and expenditure has been recognised but cash has not been received or paid, a debtor or creditor for the relevant amount is recorded in the balance sheet. The largest estimate of this nature is the amount accrued in respect of housing benefit subsidy. This calculation is based upon the pre-audited return. Where it is doubtful that debts will be settled, the balance of debtors is written down and a charge is made to revenue for the income that might not be collected.
- Income and expenditure are credited and debited to the relevant revenue account, unless they properly represent capital receipts or capital expenditure.

3. Receipts and Payments in Advance

Receipts in advance represent income received in the current year in respect of fees and charges (including our proportion of Council Tax) for the forthcoming years. They are included as a liability (within Creditors) on the Balance Sheet.

Payments in Advance represent amounts paid in the current year in respect of goods and services for the forthcoming years. They are included as an asset (within Debtors) on the Balance Sheet.

4. Cash and Cash Equivalents

Cash is represented by cash in hand and deposits with financial institutions repayable without penalty on notice of not more than 24 hours.

Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. SSDC will include deposits in Money Market Funds and Business Reserves in Cash Equivalents.

In the Cash Flow Statement, cash and cash equivalents are shown net of the bank overdrafts that are repayable on demand and form an integral part of the Authority's cash management.

5. Prior Period Adjustments, Changes in Accounting Policies and Estimates and Errors

Prior period adjustments may arise as a result of a change in accounting policies or to correct a material error. Changes in accounting estimates are accounted for prospectively, i.e. in the current and future years affected by the change and do not give rise to a prior period adjustment.

Changes in accounting policies are only made when required by proper accounting practices or the change provides more reliable or relevant information about the effect of transactions, other events and conditions on the Authority's financial position or financial performance. When a change is made, it is applied retrospectively (unless stated otherwise) by adjusting the opening balances and comparative amounts for the prior period as if the new policy had always been applied.

Material errors discovered in prior period figures are corrected retrospectively by amending opening balances and comparative amounts for the prior period.

6. Charges to Revenue for Non-Current Assets

Service revenue accounts, support services and trading accounts are debited with the following amounts to record the real cost of holding fixed assets during the year:

- Depreciation attributable to the assets used by the relevant service.
- Revaluation and impairment losses attributable used by the service where there are no accumulated gains in the Revaluation Reserve against which they can be written off.
- Amortisation of intangible fixed assets attributable to the service.

The Council is not required to raise council tax to cover depreciation, revaluation and impairment losses or amortisations. However, it is required to make an annual provision from revenue to contribute towards the reduction in its overall borrowing requirement.

Depreciation, revaluation and impairment losses and amortisations are therefore replaced by the contribution to the General Fund Balance, by way of an adjusting transaction with the Capital Adjustment Account in the Movement in Reserves Statement for the difference between the two.

7. Employee Benefits

Benefits Payable During Employment

Short-term employee benefits are those due to be settled within 12 months of the year-end. They include benefits such as wages and salaries, paid annual leave and paid sick leave and non-monetary benefits (e.g. cars) for current employees and are recognised as an expense for service in the year in which employees render service to the Authority. An accrual is made for the cost of holiday entitlements (or any form of leave, e.g. time off in lieu) earned by employees but not taken before the year-end which employees can carry forward to the next financial year. The accrual is made at the wage and salary rates applicable in the following accounting year, being the period in which the employee takes the benefit. The accrual is charged to Surplus and Deficit on the Provision of Services, but then reversed out through the Movement in Reserves Statement so that holiday benefits are charged to revenue in the financial year in which the holiday absence occurs.

Termination Benefits

Termination benefits are amounts payable as a result of a decision by the Authority to terminate an officer's employment before the normal retirement date or an officer's decision to accept voluntary redundancy and are charged on an accruals basis to the Non Distributed Costs line in the Comprehensive Income and Expenditure Statement when the Authority is demonstrably committed to the termination of the employment of an officer or group of officers or making an offer to encourage voluntary redundancy. Where termination benefits involve the enhancement of pension, statutory provisions require the General Fund balance to be charged with the amount payable by the Authority to the pension fund or pensioner in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, appropriations are required to and from the Pensions Reserve to remove the notional debits and credits for pension enhancement termination benefits and replace them with debits for the cash paid to the pension fund and pensioners and any such amounts payable but unpaid at the year end.

Post Employment Benefits

Employees of the Authority are members of the Local Government Pensions Scheme administered by Somerset County Council, which provides defined benefits to members (retirement lump sums and pensions) earned as employees worked for the Authority.

The Local Government Pension Scheme is accounted for as a defined benefits scheme:

The liabilities of the Somerset County Council pension scheme attributable to the Council are included in the balance sheet on an actuarial basis using the projected unit method i.e. an assessment of the future payments that will be made in relation to the retirement benefits earned to date by employees, based on assumptions about mortality rates, employee turnover rates, etc, and projections of projected earnings for current employees.

- Liabilities are discounted to their value at current prices, using a discount rate based on the yield on the iBoxx AA, rated over the 15 year Corporate Bond Index.
- The assets of the Somerset County Council pension fund attributable to the Council are included in the balance sheet at their fair value on a current bid price

(estimate bid values have been used on pre-2008/09 valuations based on mid market values where current bid prices are not available).

- The change in net pension liability is analysed into seven components:
 - Current service cost – the increase in liabilities as a result of years service earned this year is allocated to the Comprehensive Income and Expenditure Statement to the services for which the employees worked.
 - Past service costs – the increase in liabilities arising from current year decisions whose effect relates to years of service earned in earlier years is debited to the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement as part of Non Distributed Costs.
 - Interest cost – the expected increase in the present value of liabilities during the year as they move one year closer to being paid is debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.
 - Expected return on assets – the annual investment return on the fund assets attributable to the Council, based on an average of the expected long-term return is credited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.
 - Gains/losses on settlements and curtailments – the result of actions to relieve the Council of liabilities or events that reduce the expected future service or accrual of benefits of employees is debited or credited to the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement as part of Non Distributed Costs.
 - Actuarial gains and losses – changes in the net pension liability that arise because events have not coincided with assumptions made in the last actuarial valuation or because the actuaries have updated their assumptions are debited or credited to the Statement of Total Recognised Gains and Losses.
 - Contributions paid to the Somerset County Council pension fund – cash paid as employer’s contributions to the pension fund in settlement of liabilities; not accounted for as an expense.

In relation to retirement benefits, statutory provisions require the General Fund balance to be charged with the amount payable by the Authority to the pension fund or directly to the pensioners in the year, not the amount calculated according the relevant accounting standards. In the Movement in Reserves Statement, this means that there are appropriations to and from the Pensions Reserve to remove the notional debits and credits for retirement benefits and replace them with debits for the cash paid to the pension fund and pensioners and any such amounts payable but unpaid at the year-end. The negative balance that arises on the Pensions Reserve thereby measure the beneficial impact to the General Fund of being required to account for retirement benefits on the basis of cash flows rather than as benefits are earned by employees.

Discretionary Benefits

The Council also has restricted powers to make discretionary awards of retirement benefits in the event of early retirements. Any liabilities estimated to arise as a result of an award to any member of staff are accrued in the year of the decision to make the award and accounted for using the same policies as are applied to the Local Government Pension Scheme.

8. Events after the Balance Sheet Date

Events after the Balance Sheet date are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the Statement of Accounts is authorised for issue. Two types of events can be identified:

- Those that provide evidence of conditions that existed at the end of the reporting period – the Statement of Accounts is adjusted to reflect such events
- Those that are indicative of conditions that arose after the reporting period – the Statements of Accounts is not adjusted to reflect such events, but where a category of events would have a material effect, disclosure is made in the notes of the nature of the events and their estimated financial effect.

Events taking place after the date of authorisation for issue are not reflected in the Statement of Accounts.

9. Financial Instruments

Financial Liabilities

Financial liabilities are recognised on the Balance Sheet when the Authority becomes party to the contractual provisions of a financial instrument and are initially measured at fair value and carried at their amortised cost. Annual charges to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest payable are based on the carrying amount of the liability, multiplied by the effective rate of interest of the instrument. The effective interest rate is the rate that exactly discounts estimated future cash payments over the life of the instrument to the amount at which it was originally recognised.

This means that the amount presented in the Balance Sheet is the outstanding principal repayable and interest charged to the Comprehensive Income and Expenditure Statement is the amount payable for the year in the loan agreement.

Gains and losses on the repurchase or early settlement of borrowing are credited and debited to Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement in the year of repurchase/settlement. However, where repurchase has taken place as part of a restructuring of the loan portfolio that involves the modification or exchange of existing instruments, the premium or discount is respectively deducted from or added to the amortised cost of the new or modified loan and the write-down to the Comprehensive Income and Expenditure Statement is spread over the life of the loan by an adjustment to the effective interest rate.

Where premiums and discounts have been charged to the Comprehensive Income and Expenditure Statement, regulations allow the impact on the General Fund Balance to be spread over future years. The Council has a policy of spreading the gain or loss over a minimum period equal to the outstanding term on the loan or 10 years (if shorter) against which the premium was payable or discount receivable when it was repaid. The reconciliation of amounts charged to the Comprehensive Income and Expenditure Statement to the net charge required against the General Fund Balance is managed by a transfer to or from the Financial Instruments Adjustment Account in the Movement in Reserves Statement.

Financial Assets

Financial assets are classified into two types:

- Loans and receivables - assets that have fixed or determinable payments but are not quoted in an active market
- Available-for-sale assets - assets that have a quoted market price and/or do not have fixed or determinable payments

Loans and Receivables

Loans and receivables are recognised on the Balance Sheet when the Authority becomes a party to the contractual provisions of a financial instrument and are initially measured at fair value and carried at their amortised cost. Annual credits to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest receivable are based on the carrying amount of the asset multiplied by the effective rate of interest for the instrument. This means that the amount presented in the Balance Sheet is the outstanding principal receivable and interest credited to the Comprehensive Income and Expenditure Statement is the amount receivable for the year in the loan agreement.

However, the Council has made a number of car loans, bicycle loans and loans for learning to members of staff at less than market rates (soft loans). When soft loans are made, a loss is recorded in the Comprehensive Income and Expenditure Statement (debited to the appropriate service) for the present value of the interest that will be foregone over the life of the instrument, resulting in a lower amortised cost than the outstanding principal. Interest is credited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement at a marginally higher effective rate of interest than the rate receivable from the members of staff, with the difference serving to increase the amortised cost of the loan in the Balance Sheet. Statutory provisions require that the impact of soft loans on the General Fund Balance is the interest receivable for the financial year. The reconciliation of amounts debited and credited to the Comprehensive Income and Expenditure Statement to the net gain required against the General Fund Balance is managed by a transfer to, or from, the Financial Instruments Adjustment Account in the Movement in Reserve Statement.

Where assets are identified as impaired because of a likelihood arising from a past event that payments due under the contract will not be made, the asset is written down and a charge made to the relevant service (for receivables specific to that service) or the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement. The impairment loss is measured as the difference between the carrying amount and the present value of the revised future cash flows discounted at the asset's original effective interest rate.

Any gains and losses that arise on the de-recognition of the asset are credited or debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.

Available-for-sale Assets

Available-for-sale assets are recognised on the Balance Sheet when the Authority becomes a party to the contractual provision of a financial instrument and are initially measured and carried at fair value. Where the asset has fixed or determinable payments, annual credits to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest receivable are based on the amortised cost of the asset multiplied by the effective rate of interest for the instrument. Where there are no fixed or determinable payments, income is credited to

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the Comprehensive Income and Expenditure Statement when it becomes receivable by the Council.

Assets are maintained in the Balance Sheet at fair value. All assets currently held by the Council are instruments with quoted market prices and the value is based on market price.

Changes in fair value are balanced by an entry in the Available-for-Sale Reserve and the gain/loss is recognised in the Surplus or Deficit on Revaluation of Available-for Sale Financial Assets. The exception is where impairment losses have been incurred - these are debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement, along with any net gain/loss for the asset accumulated in the Available-for-Sale Reserve.

Where assets are identified as impaired because of a likelihood arising from a past event that payments due under the contract will not be made, the asset is written down and a charge made to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement. If the asset has fixed or determinable payments, the impairment loss is measured as the difference between the carrying amount and the present value of the revised future cash flows discounted at the asset's original effective interest rate. Otherwise the impairment loss is measured as any shortfall of fair value against the acquisition cost of the instrument (net of any principal repayment and amortisation).

Any gains and losses that arise on the de-recognition of the asset are credited or debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement, along with any accumulated gains/losses previously recognised in the Available-for-Sale Reserve.

10. Government Grants and Contributions

Whether paid on account, by instalments or in arrears, government grants and third party contributions and donations are recognised as due to the Authority when there is reasonable assurance that:

The authority will comply with the conditions attached to the payments, and
The grants or contributions will be received.

Amounts recognised as due to the Council are not credited to the Comprehensive Income and Expenditure Statement until conditions attached to the grant or contribution have been satisfied. Conditions are stipulations that specify that the future economic benefits or service potential embodied in the asset acquired using the grant or contribution are required to be consumed by the recipient as specified, or future economic benefits or service potential must be returned to the transferor.

Monies advanced as grants and contributions for which conditions have not been satisfied are carried in the Balance Sheet as creditors. When conditions are satisfied, the grant or contribution is credited to the relevant service line (attributable revenue grants and contributions) or Taxation and Non-Specific Grant Income (non-ringfenced revenue grants and all capital grants) in the Comprehensive Income and Expenditure Statement.

Where capital grants are credited to the Comprehensive Income and Expenditure Statement, they are reversed out of the General Fund Balance in the Movement in Reserves Statement. Where the grant has yet to be used to finance capital expenditure, it is posted to the Capital Grants Unapplied reserve. Where it has been applied, it is posted to the Capital Adjustment Account. Amounts in the Capital Grants Unapplied

reserve are transferred to the Capital Adjustment Account once they have been applied to fund capital expenditure.

Area Based Grant (ABG) is a general grant allocated by central government directly to local authorities as additional revenue funding. ABG is non-ringfenced and is credited to Taxation and Non-Specific Grant Income in the Comprehensive Income and Expenditure Statement.

11. Intangible Fixed Assets

Expenditure on non-monetary assets that do not have physical substance but are controlled by the Council as a result of past events (e.g. software licences) are capitalised at cost when they are expected that future economic benefits or service potential will flow from the intangible asset to the Authority.

Intangible assets are measured initially at cost. Amounts are only revalued where the fair value of the assets held by the Authority can be determined by reference to an active market. In practice, not intangible asset held by the Council meets this criterion, and they are therefore carried at amortised cost. The depreciable amount of an intangible asset is amortised over its useful life to the relevant service line(s) in the Comprehensive Income and Expenditure Statement. An asset is tested for impairment whenever there is an indication that the asset might be impaired – any losses recognised are posted to the relevant service line(s) in the Comprehensive Income and Expenditure Statement. Any gain or loss arising on the disposal or abandonment of an intangible asset is posted to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement.

Where expenditure on intangible assets qualifies as capital expenditure for statutory purposes, amortisation, impairment losses and disposal gains and loss are not permitted to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and (for any sale proceeds greater than £10,000) the Capital Receipts Reserve.

12. Inventories and Long Term Contracts

Inventories are included in the Balance Sheet at the lower of cost and net realisable value. The cost of inventories is assigned using the [FIFO/weighted average] costing formula.

Long term contracts are accounted for on the basis of charging the Surplus and Deficit on the Provision of Services with the value of works and services received under the contract during the financial year.

13. Investment Property

Investment properties are those that are used solely to earn rentals and/or for capital appreciation. The definition is not met if the property is used any way to facilitate the delivery of services or productions of goods or is held for sale.

Investment properties are measured initially at cost and subsequently at fair value, based on the amounts at which the asset could be exchanged between knowledgeable parties at arm's-length. Properties are not depreciated but are revalued annually according to market conditions at the year-end. Gains and losses on revaluation are posted to the Financing and Investment Income and Expenditure line in the

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Comprehensive Income and Expenditure Statement. The same treatment is applied to gains and losses on disposal.

Rentals received in relation to investment properties are credited to the Financing and Investment Income line and result in a gain for the General Fund Balance. However, revaluation and disposal gains and losses are not permitted by statutory arrangements to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and (for any sale proceeds greater than £10,000) the Capital Receipts Reserve.

14. Leases

Leases are classified as finance leases where the terms of the lease transfer substantially all the risks and rewards incidental to ownership of the property, plant or equipment from the lessor to the lessee. All other leases are classified as operating leases.

Where a lease covers both land and buildings, the land and building elements are considered separately for classification.

The Authority as Lessee

Finance Leases

Property, plant and equipment held under finance leases is recognised on the Balance Sheet at the commencement of the lease at its fair value measured at the lease's inception (or the present value of the minimum lease payments, if lower). The asset recognised is matched by a liability for the obligation to pay the lessor. Initial direct costs of the Authority are added to the carrying amount of the asset. Premiums paid on entry into a lease are applied to writing down the lease liability. Contingent rents are charged as expenses in the periods in which they are incurred.

Lease payments are apportioned between:

- a charge for the acquisition of the interest in the property, plant and equipment – applied to write down the lease liability, and
- a finance charge (debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement).

Property, plant and equipment recognised under finance leases are accounted for using the policies applied generally to such assets, subject to depreciation being charged over the lease term if this is shorter than the asset's estimated useful life (where ownership of the asset does not transfer to the authority at the end of the lease period)

The Authority is not required to raise council tax to cover depreciation or revaluation and impairment losses arising on leased assets. Instead, a prudent annual contribution is made from revenue funds towards the deemed capital investment in accordance with statutory requirements. Depreciation and revaluation and impairment losses are therefore substituted by revenue contributions in the General Fund Balance, by way of an adjusting transaction with the Capital Adjustment Account in the Movement in Reserves Statement for the difference between the two.

Operating Leases

Rentals paid under operating leases are charged to the Comprehensive Income and Expenditure Statement as an expense of the services benefitting from use of the leased property, plant or equipment. Charges are made on a straight-line basis over the life of the lease.

The Authority as Lessor

Finance Lease

Where the Authority grants a finance lease over a property of an item of plant or equipment, the relevant asset is written out of the Balance Sheet as a disposal. At the commencement of the lease, the carrying amount of the asset in the Balance Sheet (whether Property, Plant and Equipment or Assets Held for Sale) is written off the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement as part of the gain or loss on disposal. A gain, representing the Authority's net investment in the lease, is credited to the same line in the Comprehensive Income and Expenditure Statement as part of the gain or loss on disposal (i.e. netted off against the carrying value of the asset at the time of disposal), matched by a lease (long-term debtor) asset in the Balance Sheet.

Lease rentals are apportioned between:

- a charge for the acquisition of the interest in the property – applied to write down the lease debtor (together with premiums received), and
- a finance charge (credited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement).

The gain credited to the Comprehensive Income and Expenditure Statement on disposal is not permitted by statute to increase the General Fund Balance and is required to be treated as a capital receipt. Where a premium has been received, this is posted out of the General Fund Balance to the Capital receipts Reserve in the Movement in Reserves Statement. Where the amount due in relation to the lease asset is to be settled by the payment of rentals in future financial years, this is posted out of the General Fund Balance to the Deferred Capital Receipts Reserve in the Movement in Reserves Statement. When the future rentals are received, the element for the capital receipt for the disposal of the asset is used to write down the lease debtor. At this point, the deferred capital receipts are transferred to the Capital Receipts Reserve.

The written-off value of disposals is not a charge against council tax, as the cost of fixed assets is fully provided for under separate arrangements for capital financing. Amounts are therefore appropriated to the Capital Adjustment Account from the General Fund Balance in the Movement in Reserves Statement.

Operating Leases

When the Authority grants an operating lease over a property or an item of plant or equipment, the asset is retained in the Balance Sheet. Rental income is credited to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement. Credits are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a premium paid at the commencement of the lease). Initial direct costs incurred in negotiating and arranging the

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lease are added to the carrying amount of the relevant asset and charges as an expense over the lease term on the same basis as rental income.

15. Overheads and Support Services

The costs of overheads and support services are charged to those that benefit from the supply or service in accordance with the costing principles of the CIPFA Best Value Accounting Code of Practice (BVACOP) 2010/11. The total absorption costing principal is used where the full cost of overheads and support services are shared between users in proportion to the benefits received with the exception of:

- Corporate and Democratic Core – costs relating to the Council's status as a multi-functional democratic organisation.
- Non Distributed Costs – the cost of discretionary benefits awarded to employees retiring early and impairment losses on Assets Held for Sale

These two cost categories are defined in BVACOP and accounted for as separate headings in the Comprehensive Income and Expenditure Statement, as part of Net Expenditure on Continuing Services.

16. Property, Plant and Equipment

Assets that have physical substance and are held for use in provision of services or for administrative purposes and that are expected to be used during more than one financial year are classified as Property, Plant and Equipment.

Recognition

Expenditure on the acquisition, creation or enhancement of Property, Plant and Equipment is capitalised on an accruals basis, provided that it is probable that the future economic benefits or service potential associated with the item will flow to the authority and the cost of the item can be measured reliably. Expenditure that maintains but does not add to an asset's potential to deliver future economic benefits or service potential (i.e. repairs and maintenance) is charged as an expense when it is incurred. There are two exceptions to this:

- The expenditure incurred is below £10,000, except Capital Grants where the limit is £1,000. In such cases expenditure is charged direct to the revenue accounts.
- The asset is acquired through an operating lease when rental payments are charged to the revenue account.

Measurement

Assets are initially measured at cost, comprising all expenditure that is directly attributable to bringing the asset into working condition for its intended use (such as purchase price; any costs attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management).

Assets are then carried in the Balance Sheet using the following measurement basis:

- Infrastructure, community assets and assets under construction – depreciated historical cost
- All other assets – fair value, determined as the amount that would be paid for the asset in existing use (existing use value – EUV).

Where there is no market based evidence of fair value because of the specialist nature of an asset, depreciated replacement cost (DRC) is used as an estimate of fair value.

Assets included in the balance sheet at fair value are re-valued sufficiently regularly to ensure that their carrying amount is not materially different from their fair value at the year end, but as a minimum every five years. Increases in valuations are matched by credits to the Revaluation Reserve to recognise unrealised gains. Exceptionally, gains might be credited to the Comprehensive Income and Expenditure Account where they arise from the reversal of a loss previously charged to a service.

Where decreases in value are identified, they are accounted for by:

- Where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against the balance (up to the amount of the accumulated gains)
- Where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the Comprehensive Income and Expenditure Statement.

The Revaluation Reserve contains revaluation gains recognised since 1 April 2007 only, the date of its formal implementation. Gains arising before that date have been consolidated into the Capital Adjustment Account.

Capital expenditure incurred in enhancing assets or increasing their useful life is classed as enhancing expenditure.

Assets which have been significantly enhanced are brought forward in the five-year rolling programme to ensure that the independent valuer can correctly assess their new carrying value, this ensures that any potential overstatement only reflects a short timing difference between the enhancement taking place and the valuer assessing its impact on the asset's carrying value.

Impairment

Assets are assessed at each year-end as to whether there is any indication that an asset may be impaired. Where indications exist and any possible differences are estimated to be material, the recoverable amount of the asset is estimated and, where this is less than the carrying amount of the asset, an impairment loss is recognised for the shortfall.

Where impairment losses are identified, they are accounted for by:

- Where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains)
- Where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the Comprehensive Income and Expenditure Statement.

Where an impairment loss is reversed subsequently, the reversal is credited to the relevant service line(s) in the Comprehensive Income and Expenditure Statement, up to the amount of the original loss, adjusted for depreciation that would have been charged if the loss had not been recognised.

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Depreciation

Depreciation is provided for on all assets with a determinable finite life (except for investment properties), by allocating the value of the assets in the balance sheet over the periods expected to benefit from their use.

Depreciation is calculated on the following bases:

- Dwellings and other buildings – straight-line allocation over the life of the property as estimated by the valuer. Vehicles, plant and equipment - straight-line allocation over the life of the asset.
- Infrastructure – straight-line allocation over the life of the asset.

The following standard estimated lives are used for newly acquired assets:

	Years
Sports and Leisure Centres	40
Public Conveniences	50
Vehicles	10
Cremators	10
Office Buildings	60

Where an asset includes a number of components with significantly different asset lives, these components are then treated as separate assets and depreciated over their own useful economic lives. See Component Accounting Policy.

Revaluation gains are also depreciated, with an amount equal to the difference between current value depreciation charged on assets and the depreciation that would have been chargeable based on their historical cost being transferred each year from the Revaluation Reserve to the Capital Adjustment Account.

Assets that are sold during the year are treated as if sold on 31 March and the service accounts receive a full year's charge for depreciation as appropriate. Assets acquired during the year attract no charge.

Disposals and Non-current Assets Held for Sale

When it becomes probable that the carrying amount of an asset will be recovered principally through a sale transaction rather than through its continuing use, it is reclassified as an Asset Held for Sale. The asset is revalued immediately before reclassification and then carried at the lower of this amount and fair value less costs to sell. Where there is a subsequent decrease to fair value less costs to sell, the loss is posted to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement. Gains in fair value are recognised in the Surplus or Deficit on Provision of Services. Depreciation is not charged on Assets Held for Sale.

If assets no longer meet the criteria to be classified as Assets Held for Sale, they are reclassified back to back to non-current assets and valued at the lower of their carrying amount before they were classified as held for sale; adjusted for depreciation, amortisation or revaluations that would have been recognised had they not been classified as Held for Sale, and their recoverable amount at the date of the decision not to sell.

Assets that are to be abandoned or scrapped are not reclassified as Assets Held for Sale.

When an asset is disposed of or decommissioned, the carrying amount of the asset in the Balance Sheet (whether Property, Plant and Equipment or Assets Held for Sale) is written off to the Other Operating Expenditure line in the Comprehensive Income and

Expenditure Statement as part of the gain or loss on disposal. Receipts from disposals are credited to the Comprehensive Income and Expenditure Statement also as part of the gain or loss on disposal (i.e. netted off against the carrying value of the asset at the time of disposal). Any revaluation gains in the Revaluation Reserve are transferred to the Capital Adjustment Account.

Amounts in excess of £10,000 received from disposals are categorised as capital receipts and credited to the Capital Receipts Reserve, which can then only be used for new capital investment or set aside to reduce the Council's underlying need to borrow (the capital financing requirement). Receipts are appropriated to the Reserve from the General Fund Balance in the Movement in Reserves Statement. If the proceeds are £10,000 or less, they are not treated as capital receipts but are instead credited to revenue.

The written off value of disposals is not a charge against council tax, as the cost of fixed assets is fully provided for under separate arrangements for capital financing. Amounts are appropriated to the Capital Adjustment Account from the General Fund Balance in the Movement in Reserves Statement.

A proportion of receipts relating to housing disposals is payable to the Government. In practice this relates only to mortgage repayments, 75% of which must be paid over to the Government.

17. Component Accounting

Components of non-current assets do not always have the same useful lives and may depreciate or wear out at different rates throughout their life. Therefore, it is appropriate to depreciate each significant component separately over its useful life, in order that the Comprehensive Income & Expenditure Account is fairly charged with the consumption of economic benefits of those assets.

Where a significant component is expected to wear out more quickly than the overall asset, it is depreciated over a shorter period of time and any subsequent expenditure on restoring or replacing the component is capitalised (with any carrying amount of the replaced component being written off to the Comprehensive Income and Expenditure Statement).

From 1st April 2010, components will be recognised when an asset is enhanced, acquired or re-valued. Where a component is replaced or restored, the carrying amount of the old component is derecognised.

- Land and individual buildings will be valued separately.
- Assets are deemed to be material and considered for componentisation when the cost or value in the Balance Sheet is at least £500,000 (approximately 1% of the authority's non current assets).
- Each asset will be reviewed individually by the valuer to determine whether any part of a material asset has a differing useful life or method of depreciation. The assets will be reviewed by the following:
 - Sub Structure
 - Superstructure (frame, upper floors, roof, stairs, external walls, windows, external doors, internal walls, partitions, internal doors)
 - Internal finishes (walls, floors and ceilings)
 - Fixtures (sanitary, water, disposal equipment)

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- Engineering services (heating, air treatment, gas installations, lifts, protective, communications)
- External works

- Where component spend is worth 20% of the total cost value of the asset it is deemed to be significant. Where information is not readily available to determine the value of components, a best estimate will be accounted for and detail of how the estimate was arrived at, in liaison with relevant professional advice, will be documented.

18. Provisions, Contingent Liabilities and Contingent Assets

Provisions

Provisions are made where an event has taken place that gives the Council an obligation that probably requires settlement by transfer of economic benefits or service potential, and a reliable estimate can be made of the amount of the obligation. For instance, the Council may be involved in a court case that could eventually result in the making of a settlement or the payment of compensation.

Provisions are charged to the appropriate service line in the Comprehensive Income and Expenditure Statement in the year that the authority becomes aware of the obligation, and are measured at the best estimate at the balance sheet date of the expenditure required to settle the obligation, taking into account relevant risks and uncertainties.

When payments are eventually made, they are charged to the provision carried in the balance sheet. Estimated settlements are reviewed at the end of each financial year; where it becomes less than probable that a transfer of economic benefits will now be required (or a lower settlement than anticipated is made), the provision is reversed and credited back to the relevant service.

Where some or all of the payments required to settle a provision is expected to be recovered from another party (e.g. from an insurance claim), this is only recognised as income for the relevant service if it is virtually certain that reimbursement will be received if the authority settle the obligation.

Contingent Liabilities

A contingent liability arises where an event has taken place that gives the authority a possible obligation whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the Council's control. Contingent liabilities also arise in circumstances where a provision would otherwise be made but either it is not probable that an outflow of resources will be required or the amount of the obligation cannot be measured reliably.

Contingent liabilities are not recognised in the Balance Sheet but disclosed in a note to the accounts.

19. Reserves

The Council sets aside specific amounts as reserves for future policy purposes or to cover contingencies. Reserves are created by appropriating amounts out of the General Fund Balance in the Movement in Reserves Statement. When expenditure to be financed from a reserve is incurred, it is charged to the appropriate service in that year to score against the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement. The reserve is then appropriated back to the

General Fund Balance in the Movement in Reserves Statement so that there is no net charge against council tax for the expenditure.

Certain reserves are kept to manage the accounting processes for non-current assets, financial instruments, retirement and employee benefits and do not represent usable resources for the Authority.

20. Revenue Expenditure Funded from Capital Under Statute

Expenditure incurred during the year that may be capitalised under statutory provisions but does not result in the creation of non-current assets has been charged as expenditure to the relevant service in the Comprehensive Income and Expenditure Statement in the year. Where the Council has determined to meet the cost of this expenditure from existing capital resources, a transfer in the Movement in Reserves Statement from the General Fund Balance to the Capital Adjustment Account then reverses out the amounts charged so there is no impact on the level of council tax.

21. VAT

The Council does not include VAT as part of income or expenditure, whether of a capital or revenue nature except where it is not able to recover VAT.

22. Related Party Transactions

The Authority is required to disclose material transactions with related parties – bodies or individuals that have the potential to control or influence the Council or to be controlled or influenced by the Council.

The materiality of the transaction has been considered before justifying inclusion in the statements. Transactions disclosed elsewhere in the statement of accounts are not cross referenced in the note. Disclosure is only required where the Council has gone beyond providing financial assistance to having a relationship with the assisted organisation that allows it to exert control over the organisation's financial and operational policies.

23. The Collection Fund

Billing authorities in England are required by statute to establish and maintain a separate fund for the collection and distribution of amounts due in respect of council tax and national non-domestic rates (NNDR).

There is no requirement for a separate Collection Fund Balance Sheet as balances are distributed across the Balance Sheets of the billing authority, the Government and precepting authorities.

Further details on the Collection Fund use can be found within the notes to the Collection Fund in the Statement of Accounts.

24. Accounting for Council Tax

The collection of Council Tax income is in substance an agency arrangement, the cash collected by the Council from council tax debtors belongs proportionately to the Council and the major preceptors. There will be therefore a debtor/creditor position between the Council and each major preceptor to be recognised since the net cash paid to each

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major preceptor in the year will not be its share of the cash collected from council taxpayers.

The Council Tax income included in the Taxation and Non Specific Grant Income line in the Comprehensive Income and Expenditure Statement shall be the accrued income for the year. This is calculated by taking the demand on the Collection Fund plus the authority's share of the carry forward surplus/deficit on the Collection Fund as at the 31st March 2010. This amount is then adjusted for the authority's share of the surplus/deficit of 31st March 2009 that has not been distributed or recovered in the current year.

The difference between the income included in the Taxation and Non Specific Grant Income line in the Comprehensive Income and Expenditure Statement and the amount required by regulation to be credited to the Collection Fund shall be taken to the Collection Fund Adjustment Account and included as a reconciling item in the General Fund in the Movement in Reserves Statement.

25. Accounting for National Non-Domestic Rates

The Council, as an agent on behalf of Central Government carries out the collection of National Non-Domestic Rates (NNDR). Cash collected from NNDR taxpayers by the Council (net of the cost of collection allowance) belongs to the Government and the amount not yet paid to the Government at the Balance Sheet date shall be included in the Balance Sheet as a creditor; similarly, if the cash paid to the Government exceeds the cash collected from NNDR taxpayers (net of the cost of collection allowance), the excess shall be included in the Balance Sheet as a debtor.

NNDR debtor and creditor balances with NNDR taxpayers and the impairment allowance for doubtful debts are not assets and liabilities of the Council and are not recognised in the Council's Balance Sheet.

Audit Committee – 24th February 2011

11. Date of Next Meeting

The next meeting of the Audit Committee is scheduled to take place on 24th March 2011 at 10.00 a.m. in the Main Committee Room, Council Offices, Brympton Way, Yeovil.
