South Somerset District Council

Notice of Meeting

Audit Committee

Making a difference where it counts

Thursday 28 February 2013

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, **Anne Herridge** on Yeovil (01935) 462570
Email: anne.herridge@southsomerset.gov.uk

This Agenda was issued on Wednesday 20 February 2013

Ian Clarke, Assistant Director (Legal & Corporate Services)

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

Audit Committee Membership

Chairman	Derek Yeomans
Vice-Chairman	Ian Martin
John Calvert	Roy Mills
John Dyke	Terry Mounter
Marcus Fysh	John Richardson
Tony Lock	Colin Winder

South Somerset District Council – Corporate Aims

Our key aims are: (all equal)

- Jobs – We want a strong economy which has low unemployment and thriving businesses
- Environment – We want an attractive environment to live in with increased recycling and lower energy use
- Homes – We want decent housing for our residents that matches their income
- Health and Communities – We want communities that are healthy, self-reliant and have individuals who are willing to help each other

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.

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:

Internal Audit Activity

1. To approve the Internal Audit Charter and annual Internal Audit Plan;

2. To receive quarterly summaries of Internal Audit reports and seek assurance from management that action has been taken;

3. To receive an annual summary report and opinion, and consider the level of assurance it provides on the council's governance arrangements;

4. To monitor the action plans for Internal Audit reports assessed as "partial" or "no assurance;"

5. To consider specific internal audit reports as requested by the Head of Internal Audit, and monitor the implementation of agreed management actions;

6. To receive an annual report to review the effectiveness of internal audit to ensure compliance with statutory requirements and the level of assurance it provides on the council's governance arrangements;

External Audit Activity

7. To consider and note the annual external Audit Plan and Fees;

8. To consider the reports of external audit including the Annual Audit Letter and seek assurance from management that action has been taken;

Regulatory Framework

9. 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;

10. To review the Annual Governance Statement (AGS) and monitor associated action plans;

11. To review the Local Code of Corporate Governance and ensure it reflects best governance practice. This will include regular reviews of part of the Council's Constitution and an overview of risk management;

12. To receive reports from management on the promotion of good corporate governance;

Financial Management and Accounts

13. 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;

14. To provide a scrutiny role in Treasury Management matters including regular monitoring of treasury activity and practices. The committee will also review and recommend the Annual Treasury Management Strategy Statement and Investment Strategy, MRP Strategy, and Prudential Indicators to Council;

15. To review and recommend to Council changes to Financial Procedure Rules and Procurement Procedure Rules;

Overall Governance

16. The Audit Committee can request of the Assistant Director – Finance and Corporate Services (S151 Officer), the Assistant Director – Legal and Corporate Services (the Monitoring Officer), or the Chief Executive (Head of Paid Services) a report (including an independent review) on any matter covered within these Terms of Reference;

17. The Audit Committee will request action through District Executive if any issue remains unresolved;

18. The Audit Committee will report to each full Council a summary of its activities.

Meetings of the Audit Committee are held monthly including at least one meeting with the Council's external auditor, although in practice the external auditor attends more frequently.

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 28 February 2013

Agenda

Preliminary Items

1. To approve as a correct record the Minutes of the previous meeting held on 22 November 2012

2. Apologies for Absence

3. Declarations of Interest

In accordance with the Council's current Code of Conduct (adopted July 2012), which includes all the provisions relating to Disclosable Pecuniary Interests (DPI), personal and prejudicial interests, Members are asked to declare any DPI and also any personal interests (and whether or not such personal interests are also "prejudicial") in relation to any matter on the agenda for this meeting. A DPI is defined in The Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012 (SI 2012 No. 1464) and Appendix 3 of the Council's Code of Conduct. A personal interest is defined in paragraph 2.8 of the Code and a prejudicial interest is defined in paragraph 2.9.

4. Public Question Time

Items for Discussion ***Page Number***

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5. 2012/13 SWAP Internal Audit Quarter 3 Update Report

Head of Service: *Gerry Cox, Head of Internal Audit Partnership*
Lead Officer: *Andrew Ellins, Audit Manager*
Contact Details: *andrew.ellins@southwestaudit.gov.uk or (01935) 462378*

Purpose of the Report

This report has been prepared for the Audit Committee to review the progress made on the 2012-13 Annual Internal Audit Plan.

Recommendation

To note the progress made.

Background

The Audit Committee agreed the 2012/13 Internal Audit Plan at its February meeting. This is the third quarterly update report to inform the Audit Committee of progress against the plan for April 2012 to January 2013.

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*

APPENDIX A

SWAP
SOUTH WEST AUDIT PARTNERSHIP
Delivering Audit Excellence

South Somerset District Council

Report of Internal Audit Activity

Quarter 3 Update, 2012/13

Internal Audit ▪ Risk ▪ Special Investigations ▪ Consultancy

Contents

The contacts at SWAP in connection with this report are:

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Audit Manager
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Our audit activity is split between:

- **Operational Audit**
- **Key Controls, Finance**
- **Key Controls, Income**
- **Governance, Fraud & Corruption Audit**
- **IT Audit**
- **Special Reviews**

Role of Internal Audit

The Internal Audit service for South Somerset District Council is provided by the South West Audit Partnership (SWAP). SWAP has 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 in February 2012.

Internal Audit provides an independent and objective opinion on the Authority's control environment by evaluating its effectiveness. Primarily the work includes;

- Operational Audit Reviews
- Annual Review of Key Financial System Controls
- Annual Review of Main Income Stream System Controls
- Cross Cutting Fraud and Governance Reviews
- IT Audit Reviews
- Other Special or Unplanned Reviews

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 Directors, Assistant Directors, Service Managers and External Audit. This year's Audit Plan was reported to the Audit Committee at its meeting in February 2012.

Audit assignments are undertaken in accordance with this Plan to assess current levels of governance, control and risk.

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

Quarter 3 Outturn:

Audit Assignments undertaken in the Quarter

- **Operational Audits**

Internal Audit Work Programme

The schedule provided at Appendix B contains a list of all audits as agreed in the Annual Audit Plan 2012/13. It is important that Members are aware of the status of all audits and that this information helps them place reliance on the work of Internal Audit and its ability to complete the plan as agreed.

Each completed assignment includes its respective "control assurance" opinions 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.

Operational Audits

Operational Audits are a detailed evaluation of a Service's 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.

In Quarter 3 there were no Operational audits planned as we undertake the Key Financial audits in this quarter (see page 3 below).

- Energy Management

Energy Management was at draft report stage in Qtr2 and has since reached final report stage. We were able to provide reasonable assurance as no significant risks were unmanaged.

Quarter 3 Outturn:

Audit Assignments undertaken in the Quarter

- **Key Controls; Finance**

Key Controls, Finance Audits

Key Control Audits are completed to assist the External Auditor in their assessment of the Council's financial control environment. It is essential that all key controls identified by the External Auditors are operating effectively to provide management with the necessary assurance that there is a satisfactory framework on internal control. The Key Control Audits provide assurance over the main financial systems;

Audit	Assurance Provided
Capital Accounting	★★★ Substantial
Council Tax and NNDR	★★ Reasonable
Creditors	★★ Reasonable
Debtors	★★ Reasonable
Housing and Council Tax Benefits	★★★ Substantial
Main Accounting	Discussion Document
Payroll	★★ Reasonable
Treasury Management	★★★ Substantial

These audits are always undertaken in Qtr 3 and are the main focus of our work in this quarter.

In all there were only 8 recommendations for improvement, most of which are minor and overall the key financial systems continue to be well controlled. The Main Accounting audit has found some areas for improvement but at the time of this report these had yet to be agreed with management. A verbal update will be available at the Committee meeting.

Quarter 3 Outturn:

Audit Assignments undertaken in the Quarter

- **Key Controls; Main Income Stream Audits**

Key Controls, Main Income Stream Audits

These other Key Control Audits have been performed as South Somerset considers these Services to have a significant impact on the Councils ability to meet its overall budget. These are areas of high and in many cases volatile income streams where poor internal controls could result in material losses.

In Quarter 3 there were two (out of the annual plan of nine) key income stream audits planned;

- Licensing Income
- Homelessness Prevention Income

The Licensing Income audit and the Homelessness Prevention Income audit are not yet to Final as we give priority to completing the Financial Key Controls Audits (see Page 3 above). Thus far we have no concerns to raise and a verbal update can be provided at the Committee Meeting (this report has been produced 3 weeks before the Meeting).

- Wincanton Sports Centre

This was a Qtr2 audit but was still in progress when we last reported - Wincanton Sports Centre received partial assurance in 2011/12 and the Audit Committee rightly have sought assurance that the risks identified are now being managed and the improved controls recommended by audit have been implemented and are operating effectively. We are now pleased to report that most of the issues previously found have been addressed and reasonable assurance has now been provided.

Quarter 3 Outturn:

Audit Assignments undertaken in the Quarter

- **Governance, Fraud and Corruption Audits**

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. 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 of our Client sites.

There are four governance, fraud and corruption reviews in progress and an update will provided in the final quarterly update report;

- Treasury Management Strategies
- TENS Risk Management System
- Non-Compliance with EU Procurement Rules
- Contracts Fraud

- **Information Systems**

Information Systems

Information Systems – IT audits provide the Authority with assurance with regards to their compliance with industry best practice. As with Operational Audits, an audit opinion is given.

The SWAP IT Manager has met with the SSDC ICT Manager to identify IT Risks that would benefit from audit assurance. Audits will be undertaken in Qtr4, once agreed with the S151 Officer.

Quarter 3 Outturn:

Audit Assignments undertaken in the Quarter

- **Special Reviews**

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

Special Reviews

At the request of the Assistant Director – Health and Well-Being and in agreement with the Section 151 Officer, SWAP undertook an independent investigation to provide assurance that the Council had acted fairly and demonstrated an adequate duty of care following an accusation by a member of staff that she felt she was the victim of bullying and harassment.

SWAP reported their findings to the Strategic Director – Place and Performance as the Management representative leading the review for the Council.

Future Planned Work

This is detailed in Appendix B and is subject to any changes in agreement with the S151 officer.

Quarter 3 Outturn:

Conclusions

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 of Appendix C.

The Committee will be aware that in May 2012, SWAP were pleased to provide an Audit Opinion for the Annual Governance Statement for 2011/12 that gave Comprehensive Assurance. Our approach to the audits for 2012/13 reflects this positive assurance and we are seeking to undertake more challenging and cross-cutting reviews rather than traditional service reviews that we have done over recent years, given that these areas have now proven themselves to have adequate and often good internal controls. We shall continue to give ongoing assurance on key controls, but similarly we can do this with less resource than we have previously.

We are continuing to add value by making recommendations for improvement, although we are finding that the key controls are operating effectively and it is rare that we cannot give reasonable or substantial assurance over the areas reviewed. This indicates a good internal control environment in the Council.

A list of all audits planned for 2012/13 and their status at the end of Quarter 3 are detailed in Appendix B.

South Somerset District Council Audit Plan Progress 2012/13 - Qtr 3 Update **APPENDIX B**

Audit Type	Audit Title	Quarter	Status	Opinion	No. of recs	⬅ Major - Recommendations - Minor ➡				
						5	4	3	2	1
Follow-Up	Register of Interests - Members Related Parties	Qtr 1	Complete	Non-Opinion	0	0	1	2	0	0
Governance	Boden Mill Site & Chard Regeneration Scheme Statement of Accounts	Qtr 1	Complete	Non-Opinion	0	0	0	0	0	0
Governance	Yeovil Crematorium and Cemetery Annual Return	Qtr 1	Complete	Non-Opinion	0	0	0	0	0	0
Governance	Data Security Breaches	Qtr 1	Discussion Document	Reasonable	17	0	0	9	8	0
Governance	Fraud and Corruption - Creditors	Qtr 1	Final	Reasonable	5	0	0	5	0	0
Key Income	Goldenstones	Qtr 1	Final	Reasonable	5	0	0	4	1	0
Operational	Yeovil Crematorium and Cemetery	Qtr 1	Discussion Document	Reasonable	9	0	1	3	5	0
Key Income	Workplace Nursery Income	Qtr 2	Final	Reasonable	2	0	0	2	0	0
Key Income	Plant Nursery Income	Qtr 2	Final	Reasonable	5	0	0	4	1	0
Operational	Debt Management	Qtr 2	Deferred			0	0	0	0	0
Operational	Energy Management	Qtr 2	Final	Reasonable	4	0	0	4	0	0
Operational	Development Control	Qtr 2	Final	Reasonable	12	0	0	10	2	0
Key Income	Wincanton Sports Centre Income	Qtr 2	Draft	Reasonable	8	0	0	7	1	0
Governance	Non-compliance with EU rules	Qtr 2	In Progress			0	0	0	0	0
Governance	Fraud and Corruption - Contracts	Qtr 2	Discussion Document			0	0	0	0	0
Special Review	Housing Team Bullying & Harrasment Claim	Qtr 2	Complete	Non-Opinion	0	0	0	0	0	0
Key Income	Licensing Income	Qtr 3	Draft			0	0	0	0	0
Follow-Up	Housing Benefit Fraud	Qtr 3	Discussion Document			0	0	0	0	0
Governance	Treasury Management Strategies	Qtr 3	In Progress			0	0	0	0	0
Governance	TEN Risk Management System	Qtr 3	In Progress			0	0	0	0	0
Key Income	Homelessness Income	Qtr 3	In Progress			0	0	0	0	0
Key Control, Finance	Capital Accounting	Qtr 3	Final	Substantial	0	0	0	0	0	0
Key Control, Finance	Council Tax and NNDR	Qtr 3	Final	Reasonable	3	0	0	3	0	0
Key Control, Finance	Creditors	Qtr 3	Final	Reasonable	1	0	0	1	0	0
Key Control, Finance	Debtors	Qtr 3	Final	Reasonable	1	0	0	1	0	0
Key Control, Finance	Housing and Council Tax Benefits	Qtr 3	Final	Substantial	1	0	0	0	1	0
Key Control, Finance	Main Accounting	Qtr3	Draft			0	0	0	0	0
Key Control, Finance	Payroll	Qtr 3	Final	Reasonable	2	0	0	2	0	0
Key Control, Finance	Treasury Management	Qtr 3	Final	Substantial	0	0	0	0	0	0
Operational	Lean Process Post Review	Qtr 4	Deferred			0	0	0	0	0
Governance	Remote and Mobile Working	Qtr 4	In Progress			0	0	0	0	0
Governance	Asset Management Planning	Qtr 4	In Progress			0	0	0	0	0
Governance	Fraud and Corruption - Expenses	Qtr 4	In Progress			0	0	0	0	0
Key Income	Car Parks Income	Qtr 4	In Progress			0	0	0	0	0
Key Income	Octagon Theatre Income	Qtr 4	In Progress			0	0	0	0	0
Key Income	Section 106 Agreements Income	Qtr 4	In Progress			0	0	0	0	0
Key Income	Careline Income	Qtr 4	In Progress			0	0	0	0	0

Audit Framework Definitions

Control Assurance Definitions

Substantial	★★★ I am able to offer substantial 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 – 28th February 2013

6. 2013/14 SWAP Internal Audit Plan

Head of Service: *Gerry Cox, Head of Internal Audit Partnership*
Lead Officer: *Andrew Ellins, Audit Manager*
Contact Details: *andrew.ellins@southwestaudit.gov.uk or (01935) 462378*

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 the Internal Audit Plan for April 2013 to March 2014.

Background

The Total number of audit days planned for 2013-14 remains at 419 days.

As last year, 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 the plan will have to remain flexible to address new and emerging risks faced by the Council.

SWAP also have recommended ‘Themed’ audits following Risk Management Facilitation Meetings with representatives of South West Councils where common emerging risks were identified in order to seek to compare and contrast best practice.

Key Control Audits - This 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 them 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 8 annual audits planned:

Capital Accounting
Creditors
Debtors
Housing and Council Tax Benefits
Main Accounting
NNDR
Payroll
Treasury Management

Governance, Fraud and Corruption Audits – This 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 or could be subject to fraud. 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 11 reviews planned:

Troubled Families
Fighting Fraud Locally
NNDR – Managing New Risks and Liabilities
Debt Management
Asset Management - Leasing
Unofficial Voluntary Funds
Corporate Procurement Cards
Use of Cash Collection Contractors; Banking (Loomis) and Bailiffs
Resource Centre – Contract Compliance
Boden Mill and Chard Regeneration Scheme Statement of Accounts
Yeovil Crematorium and Cemetery Annual Return

IT Audits – IT 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 will liaise with the I.T. Manager to identify specific I.T. related risks. There will be at least 2 specialist reviews:

Mobile and Remote Working (SWAP IT Themed audit)
To be Agreed

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. The S151 Officer has requested on-going assurance that the key income streams are well controlled and opportunities for losses are minimised and opportunities for increased income are maximised. There are 10 audits planned:

Careline Income
Car Parks Income
Goldenstones Income
Homelessness Prevention Income
Licensing Income
Octagon Theatre Income
Plant Nursery Income
Section 106 Agreements Income
Wincanton Sports Centre Income
To Be Agreed

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 15 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.

Appendix A – List of the Audits Planned for 2013-14.

Financial Implications

There are no financial implications associated with these recommendations.

Background Papers: *None*

SSDC Proposed Internal Audit Plan 2013-14

Follow-Up Audits	
2012-13 Audits receiving Partial Assurance	15.00
Total	**15.00**
Key Control Audits	
Capital Accounting	10.00
Council Tax and NNDR	15.00
Creditors	10.00
Debtors	10.00
Housing and Council Tax Benefits	15.00
Main Accounting	15.00
Payroll	10.00
Treasury Management	10.00
Total	**95.00**
Governance, Fraud and Corruption Audits	
Boden Mill and Chard Regeneration Scheme Statement of Accounts	3.00
Yeovil Crematorium and Cemetery Annual Return	5.00
Troubled Families	15.00
Fighting Fraud Locally	15.00
Corporate Procurement Cards	15.00
Use of Cash Collection Contractors: Banking (Loomis) and Bailiffs	15.00
Resource Centre - Contract Compliance	15.00
NNDR - Managing New Risks and Liabilities	15.00
Debt Management	15.00
Asset Management - Leasing	15.00
Unofficial Voluntary Funds	15.00
Total	**143.00**
IT Audits	
Mobile and Remote Working	15.00
TBA	15.00
Total	**30.00**
Operational Audits	
Careline Income	10.00
Car Parks Income	10.00
Goldenstones Income	10.00
Homelessness Prevention Income	10.00
Licensing Income	10.00
Octagon Theatre Income	10.00
Plant Nursery Income	5.00
Section 106 Agreements Income	5.00
Wincanton Sports Centre Income	10.00
TBA	15.00
Total	**95.00**
Follow-Up Audits	**15.00**
Key Control Audits	**95.00**
Governance, Fraud and Corruption Audits	**143.00**
IT Audits	**30.00**
Operational	**95.00**
TOTAL AUDIT TIME	***378.00***
Corporate Meetings	12.00
Corporate Advice	9.00
External Audit (Grant Thornton)	3.00
General Advice	12.00
Waste and Recycling (County Wide)	5.00
Total Plan Days	***419.00***

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7. Internal Audit Charter – Annual Review

Head of Service: *Gerry Cox, Head of Internal Audit Partnership*
Lead Officer: *Andrew Ellins, Audit Manager*
Contact Details: *andrew.ellins@southwestaudit.gov.uk or (01935) 462378*

Purpose of the Report

The Audit Manager will verbally update members on the Audit Charter, there is a planned change due on 1 April 2013, therefore the Charter will remain unchanged for now.

Recommendation

To note the update.

Background

The Audit Committee agreed the Audit Charter at its meeting in February 2012. The Charter is required to be reviewed annually.

Financial Implications

There are no financial implications associated with this update.

Background Papers: *None*

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8. Certification of Claims and Returns

Portfolio Holder *Cllr Tim Carroll*
Director: *Donna Parham, Assistant Director – Finance and Corporate Services*
Lead Officer: *Donna Parham*
Contact Details: *donna.parham@southsomerset.gov.uk or (01935) 462225*

Purpose of the report

This report introduces the annual report from our external auditors Grant Thornton on their findings from signing off of claims and returns for 2011/12.

Recommendations

The Audit Committee is asked to:

(1) Note the contents of the Certification of Claims and Returns 2011/12.

Introduction

The Certification of Claims and Returns Report is included within the remit of the Audit Committee under its terms of reference as follows:

"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 has been taken"

"To consider the reports of external audit and inspection agencies and seek assurance from management that action has been taken"

Grant Claims

The external auditors certify two key claims/ returns for SSDC. These are:

- Housing and Council Tax Benefit Scheme;
- National Non-Domestic Rates (NNDR) Return.

The report from Grant Thornton is attached at Appendix A. As was the case in the previous year the Housing and Council Tax Benefit scheme was given a qualified opinion. This was because of errors found in claims once tested. However, the report outlines that "the claim is complex and many local authorities have amendments and qualification letters issues".

The error on the NNDR return was caused through a software fault. Our supplier has now confirmed that this has been fixed. An action plan has been agreed to improve this position in future years and the plan is outlined on page 10 of the Grant Thornton report.

Financial Implications

None as a consequence of this report but the audit has meant that further funds have been returned to SSDC.

Background Papers

Housing Benefit Subsidy Claim
National Non-Domestic Rates Return.

Grant Thornton

South Somerset District Council

Certification work report 2011/12

January 2013

Contents

1 Executive Summary

Introduction

1.1 Grant Thornton, as the Council's auditors and acting as agents of the Audit Commission, is required to certify the claims submitted by the Council. This certification typically takes place some three to eight months after the claim period and represents a final but important part of the process to confirm the Council's entitlement to funding.

1.2 Grant Thornton and the Audit Commission have certified two claims and returns for the financial year 2011/12 relating to expenditure of £92 million.

1.3 This report summarises our overall assessment of the Council's management arrangements in respect of the certification process and draws attention to significant matters in relation to individual claims.

Approach and context to certification

Arrangements for certification for claims and returns:

- below £125,000 - no certification
- above £125,000 and below £500,000 - agreement to underlying records
- over £500,000 - agreement to underlying records and assessment of control environment. Where full reliance cannot be placed, detailed testing.

1.4 We provide a certificate on the accuracy of grant claims and returns to various government departments and other agencies. Arrangements for certification are prescribed by the Audit Commission, which agrees the scope of the work with each relevant government department or agency, and issues auditors with a Certification Instruction (CI) for each specific claim or return.

1.5 Appendix A sets out an overview of the approach to certification work, the roles and responsibilities of the various parties involved and the scope of the work we perform.

Key messages

1.6 The National Non Domestic Rates return was completed by the Audit Commission prior to our appointment as the Council's auditors on 1 November. The findings set out in this report therefore represent the some of the results of your previous auditors' work.

1.7 A summary of both claims and returns subject to certification and details of our certification fee is provided at Appendix B. The key messages from our review are summarised in Exhibit One, and set out in detail in the next section of the report.

Exhibit One: Summary of Council performance

Aspect of certification arrangements	Key Message
Submission and certification	Both claims were submitted on time to audit and they were certified within the required deadline.
Accuracy of claim forms submitted to the auditor Amendments and qualifications	Both claims were amended and one of these was qualified as well. The auditor amended the non-domestic rates return because of errors in interest payable and write offs to decrease the amount payable to the national pool. The housing benefit and council tax benefit claim was amended and a qualification letter was issued. This claim is complex and many local authorities have amendments and qualification letters issued.
Supporting working papers	Staff in the finance section, revenues and benefits have been very helpful during our certification work. There was additional time spent on certification of the non-domestic rates return because the system reports did not identify write offs and interest payments processed in March 2012.

The way forward

1.8 We have made a number of recommendations to address the key messages above and other findings arising from our certification work at Appendix C.

1.9 Implementation of the agreed recommendations will assist the council in compiling accurate and timely claims for certification. This will reduce the risk of penalties for late submission, potential repayment of grant and additional fees.

Acknowledgements

1.10 We would like to take this opportunity to thank Council officers for their assistance and co-operation during the course of the certification process.

Grant Thornton UK LLP

January 2013

2 Results of our certification work

Key messages

2.1 We and the Audit Commission have certified two claims and returns for the financial year 2011/12 relating to expenditure of £92 million.

2.2 The Council's performance in preparing claims and returns is summarised in Exhibit Two.

Exhibit Two: Performance against key certification targets

Performance measure	Target	Achievement in 2011-12		Achievement in 2010-11		Direction of travel
		No.	%	No.	%	
Total claims/returns		2		3		
Number of claims submitted on time	100%	2	100	3	100	→
Number of claims certified on time	100%	2	100	3	100	→
Number of claims certified with amendment	0%	2	100	2	66	→
Number of claims certified with qualification	0%	1	50	1	33	→

2.3 This analysis of performance shows that:

- the number of claims that required certification has reduced. The Department no longer requires the audit certification of disabled facilities grants.
- the two claims that we certified required amendments and there was one qualification letter.

2.4 Details on the certification of all claims and returns are included at Appendix B.

2.5 Where we have identified significant matters or opportunities for improvement in the compilation of claims and returns, these are summarised below and recommendations are included in the action plan at Appendix C.

2.6 We charged a total fee of £7,716 to complete the certification of the housing benefit and council tax benefit and to complete this report in 2011-12. In addition, your previous auditors the Audit Commission, charged a fee of £15,646 giving a total fee of £23,362 against an indicative budget of £30,167, as communicated in the fee letter of 8 April 2011. Details of fees charged for specific claims and returns are included at Appendix B.

Significant findings

2.7 The following significant findings were identified in relation to the management arrangements and certification of individual grant claims and returns:

Certification of Housing Benefit and Council Tax Benefit

2.8 The certification instruction is issued by the Audit Commission with the agreement of the relevant paying department (in this case the Department for Work and Pensions). It sets out the number of benefit cases that we are required to test in our initial sample. For South Somerset District Council the initial sample was 60 cases.

2.9 The certification instruction also prescribes additional testing when errors have been found in the initial sample or when errors found in previous years audit testing suggest a high-risk of error in the current year. We found errors in the initial samples and the Council reviewed an additional 650 cases. We reviewed the Council's work and confirmed its findings.

2.10 The Council amended the claim by £139, increasing the amount the Department for Work and Pensions (DWP) owes to the Council. There were a number of underpayments and overpayments to claimants. We issued a qualification letter and the DWP could apply the error rates, which the Council has estimated would increase subsidy by up to £3,401. This is because the Council errors receive 100% subsidy provided the total Local Authority errors remain below the threshold set by the DWP.

2.11 The following issues were identified from the audit.

- One incorrect classification of Non HRA Rent Rebate (i.e. bed and breakfast) between expenditure up to and including the cap and above cap, due to a housing benefit software error in 2010/11, for which the final subsidy claim was amended.
  In 2011/12, the benefits system Northgate amended these errors, and so in effect "double counted" the error. In order to rectify this a manual adjustment was required in 2011/12 so that the correct subsidy position for these claims across the two years was reflected in the final claim. The impact on the subsidy claim is to increase subsidy due to the Council by £139.
- incorrect start date for one Non HRA claim resulting in overpaid expenditure. The Council completed 100% testing of all 134 claims of this type and confirmed this was an isolated error and the subsidy claim was amended for this error. The Council amended the claim.

2.12 The following errors were identified during the audit and reported in the qualification letter. For each bullet point the extended sample size was 60:

- Incorrect calculation of claimants' weekly earned income resulting in five claimants being overpaid, three claimants being underpaid, four claimants had no impact upon entitlement, and for one further claimant, benefit paid had been incorrectly classified as an overpayment (under/overpayments ranged from £1 - £39 for any individual claimant).
- Incorrect calculation of claimants' state retirement pension resulting in three claimants being overpaid, 15 claimants being underpaid, and four claimants had no impact upon entitlement (under/overpayments ranged from £1 - £205 for any individual claimant).

- Incorrect calculation of claimants' child and working tax credits resulting in 11 claimants being overpaid, nine claimants being underpaid, and 10 claimants had no impact upon entitlement (under/overpayments ranged from £1 - £180 for any individual claimant).
- Incorrect calculation of claimants' paymaster general office pension resulting in one claimant being overpaid, and six claimants being underpaid (under/overpayments ranged from £1 - £105 for any individual claimant).
- Incorrect calculation of claimants' entitlement using a notional income resulting in one claimant being overpaid, and two claimants being underpaid (under/overpayments ranged from £2 - £11 for any individual claimant).

Certification of National Non Domestic Rates NNDR3

2.13 The control totals from the revenues system were incorrect for interest refunds and costs of collection because of an error with the computer system. Where the Council had made interest payments or written off debts in the period between the billing run (early March 2012) and the end of the year – 31 March, the system had incorrectly assigned these adjustments to the following financial year 2012/13.

2.14 For interest refunds the Council had used the financial ledger as the source of the figure for the NNDR3 return which was correct but did not agree to the print out from the revenues system. After contacting the system supplier the Council was able to provide a further schedule of interest payments made during March to prove the figure in the NNDR3 return.

2.15 However, the Council had used the revenues system to provide the debts written off in the cost of collection. This figure was incorrect because it did not take into account the debts written off in March 2012, of £119,948. The required adjustment increased the costs of collection. There was a further adjustment required (reducing the costs of collection) because the provision for bad debts was based on the arrears at 31 March 2012 (which had included debts which had already been written off). The net effect was to reduce the amount the Council had to pay over to the National Pool by £55,765.

A Approach and context to certification

Introduction

In addition to our responsibilities under the Code of Audit Practice, we also act as agents for the Audit Commission in reviewing and providing a certificate on the accuracy of grant claims and returns to various government departments and other agencies.

The Audit Commission agrees with the relevant grant paying body the work and level of testing which should be completed for each grant claim and return, and set this out in a grant Certification Instruction (CI). Each programme of work is split into two parts, firstly an assessment of the control environment relating to the claim or return and secondly, a series of detailed tests.

In summary the arrangements are:

- for amounts claimed below £125,000 - no certification required
- for amounts claimed above £125,000 but below £500,000 - work is limited to certifying that the claim agrees to underlying records of the Council
- for amounts claimed over £500,000 - an assessment of the control environment and certifying that the claim agrees to underlying records of the Council. Where reliance is not placed on the control environment, detailed testing is performed.

Our certificate

Following our work on each claim or return, we issue our certificate. The wording of this depends on the level of work performed as set out above, stating either the claim or return is in accordance with the underlying records, or the claim or return is fairly stated and in accordance with the relevant terms and conditions. Our certificate also states that the claim has been certified:

- without qualification;
- without qualification but with agreed amendments incorporated by the Council; or
- with a qualification letter (with or without agreed amendments incorporated by the Council).

Where a claim is qualified because the Council has not complied with the strict requirements set out in the certification instruction, there is a risk that grant-paying bodies will retain funding claimed by the Council or, claw back funding which has already been provided or has not been returned. In addition, where claims or returns require amendment or are qualified, this increases the time taken to undertake this work, which impacts on the certification fee.

Certification fees

Each year the Audit Commission sets a schedule of hourly rates for different levels of staff, for work relating to the certification of grant claims and returns. When billing the Council for this work, we are required to use these rates. They are shown in the table below.

Role	2011/12	2010/11
Engagement lead	£325	£325
Manager	£180	£180
Senior auditor	£115	£115
Other staff	£85	£85

B Details of claims and returns certified for 2011-12

Claim or return	Value (£)	Amended?	Amendment Amount (£)	Qualified?	Fee 2010/11 (£)	Fee 2011/12 (£)	Comments
Housing benefit and council tax benefit scheme	£53,548,544	Yes	increased by £139 to £53,548,683	Yes	£26,079	£19,767	The fee varies from year to year depending on the complexity of the cases sampled. In 2009/10 the fee was £28,970. Additional time was spent on the qualification letter but the helpfulness of the Council's housing benefit lead has allowed us to conclude efficiently on the additional testing she needed to undertake.

Claim or return	Value (£)	Amended?	Amendment Amount (£)	Qualified?	Fee 2010/11 (£)	Fee 2011/12 (£)	Comments
National non-domestic rates return	£38,775,898	Yes	Decreased by £55,765 to £38,720,133	No	£1,560	£2,980	All tests have to be carried out at least once every three years. Limited tests (Tests A) had been carried out in 2009/10 and 2010/11 but 2011/12 was the third year in which all tests in Sections A and B of the Certification Instruction had to be performed. The return was amended for errors in interest refunds and write-offs.
Disabled facilities	Not applicable			Not applicable	£365	NIL	CLG no longer requires this claim to be audited.
Reporting to those charged with Governance	Not applicable			Not applicable	£383	£615	Additional requirements to report the results of the certification work, particularly housing benefit
Total	**£92,324,442**				**£28,387**	**£23,362**	The certification fee for 2011/12 was estimated at £30,167 in the fee letter dated April 2011 and in the Annual Governance Report in September 2012.

C Action plan

Claim or return	Recommendation	Priority (L/M/H)	Management response & implementation details
Housing benefit and council tax benefit	Communicate the findings of this certification work with benefit assessors so that the correct figures are input for earned income, pensions and tax credits.	High	The findings and impact of the audit were explained to the assessors at a team meeting in December. Sample testing of earned income and pensions is being done and will be ongoing. Sample testing of tax credits will start by the 21st January and, as with the other testing, will be ongoing.
Housing benefit and council tax benefit	Ensure that any amendments in the 2011/12 claim are not double counted in 2012/13.	Medium	This will be done prior to the submission of the final claim for 2012/13. The claim needs to be submitted by 30th April 2013.
National Non Domestic Rates – NNDR 3	Ensure that interest payments and write offs which are processed in the revenues system in March are included in the form NNDR3	High	The discrepancies with the interest and write off totals was identified as a software issue. Our supplier has confirmed that the problem has been fixed. We will not be able to test this until after rollover at the beginning of April 2013.

Audit Committee – 28 February 2013

9. Planned Audit Fee for 2012/13

Portfolio Holder: *Cllr Tim Carroll*
Director: *Donna Parham, Assistant Director – Finance and Corporate Services*
Lead Officer: *Donna Parham*
Contact Details: *donna.parham@@southsomerset.gov.uk or (01935) 462225*

Purpose of the report

This report introduces the planned audit fee for 2012/13.

Recommendations

The Audit Committee is asked to:

(1) Note the contents of the Planned Audit Fee Letter 2012/13.

Introduction

The Planned audit fee letter is included within the remit of the Audit Committee under its terms of reference as follows:

"To consider and note the annual external Audit Plan and fees".

The Planned Audit Fee Letter

The letter attached outlines the scale and scope of the work that SSDC's external auditor Grant Thornton will carry out over the coming year.

Financial Implications

A budget of £81,650 is allocated in 2013/14 to fund this work. The budget will not be sufficient if there is further work required for instance additional testing on benefit claims.

Background Papers

None

Grant Thornton

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7 November 2012

Dear Mark

Planned audit fee for 2012/13

We are delighted to have been appointed by the Audit Commission as auditors to the Council and look forward to providing you with a high quality external audit service for at least the next five years. We look forward to developing our relationship with you over the coming months, ensuring that you receive the quality of external audit you expect and have access to a broad range of specialist skills where you would like our support.

The Audit Commission has set its proposed work programme and scales of fees for 2012/13. In this letter we set out details of the audit fee for the Council along with the scope and timing of our work and details of our team.

Scale fee

The Audit Commission defines the scale audit fee as "the fee required by auditors to carry out the work necessary to meet their statutory responsibilities in accordance with the Code of Audit Practice. It represents the best estimate of the fee required to complete an audit where the audited body has no significant audit risks and it has in place a sound control environment that ensures the auditor is provided with complete and materially accurate financial statements with supporting working papers within agreed timeframes."

For 2012/13, the Commission has independently set the scale fee for all bodies. The Council's scale fee for 2012/13 is £64,801. which compares with the audit fee of £108,001for 2011/12, a reduction of 40%.

Further details of the work programme and individual scale fees for all audited bodies are set out on the Audit Commission's website at: www.audit-commission.gov.uk/scaleoffees1213.

The audit planning process for 2012/13, including the risk assessment, will continue as the year progresses and fees will be reviewed and updated as necessary as our work progresses.

Scope of the audit fee

Our fee is based on the risk based approach to audit planning as set out in the Code of Audit Practice and work mandated by the Audit Commission for 2012/13. It covers:

- our audit of your financial statements
- our work to reach a conclusion on the economy, efficiency and effectiveness in your use of

resources (the value for money conclusion)
- our work on your whole of government accounts return.

Value for money (VFM) conclusion

Under the Audit Commission Act, we must be satisfied that the Council has adequate arrangements in place to secure economy, efficiency and effectiveness in its use of resources, focusing on the arrangements for:

- securing financial resilience; and
- prioritising resources within tighter budgets.

We undertake a risk assessment to identify any significant risks which we will need to address before reaching our value for money conclusion. We will assess the Council's financial resilience as part of our work on the VFM conclusion and a separate report of our findings will be provided.

Our planning to date has not identified any additional work which we are required to undertake to support our VFM conclusion. We will continue to assess the Council's arrangements and discuss any additional work required during the year.

Certification of grant claims and returns

The Audit Commission has replaced the previous schedule of hourly rates for certification work with a composite indicative fee. This composite fee, which is set by the Audit Commission, is based on actual 2010/11 fees adjusted to reflect a reduction in the number of schemes which require auditor certification and incorporating a 40% fee reduction. The composite indicative fee grant certification for the Council is £16,850.

Billing schedule

Our fees are billed quarterly in advance. Given the timing of our appointment we will raise a bill for two quarter's in December 2012 with normal quarterly billing thereafter. Our fees will be billed as follows:

Main Audit fee	**£**
December 2012	32,401
March 2013	16,200
June 2013	16,200
Scale fee	64,801
Grant Certification	
June 2013	16,850
Total	**81,651**

Outline audit timetable

We will undertake our audit planning and interim audit procedures in December, January and February. Upon completion of this phase of our work we will issue our detailed audit plan setting out our findings and details of our audit approach. Our final accounts audit and work on the VFM conclusion will be completed in June, July and August 2012 and work on the whole of government accounts return in September 2013.

Phase of work	Timing	Outputs	Comments
Audit planning and interim audit	December 2012 to February 2013	Audit plan	The plan summarises the findings of our audit planning and our approach to the audit of the Council's accounts and VFM.
Final accounts audit	June to Sept 2013	Report to those charged with governance	This report will set out the findings of our accounts audit and VFM work for the consideration of those charged with governance.
VFM conclusion	Jan to Sept 2013	Report to those charged with governance	As above
Financial resilience	Jan to Sept 2013	Financial resilience report	Report summarising the outcome of our work.
Whole of government accounts	September 2013	Opinion on the WGA return	This work will be completed alongside the accounts audit.
Annual audit letter	October 2013	Annual audit letter to the Council	The letter will summarise the findings of all aspects of our work.
Grant certification	June to November 2013	Grant certification report	A report summarising the findings of our grant certification work

Our team

The key members of the audit team for 2012/13 are:

	Name	Phone Number	E-mail
Engagement Lead	Simon Garlick	0117 305 7878	simon.p.garlick@uk.gt.com
Engagement Manager	Peter Lappin	0117 305 7865	peter.lappin@uk.gt.com
Audit Executive	Sophie Harcombe	0117 305 7875	sophie.harcombe@uk.gt.com

Additional work

The scale fee excludes any work requested by the Council that we may agree to undertake outside of our Code audit. Each additional piece of work will be separately agreed and a detailed project specification and fee agreed with the Council.

Quality assurance

We are committed to providing you with a high quality service. If you are in any way dissatisfied, or would like to discuss how we can improve our service, please contact me in the first instance. Alternatively you may wish to contact John Golding, our Public Sector Assurance regional lead partner (john.golding@uk.gt.com) .

Yours sincerely

Simon Garlick
For Grant Thornton UK LLP

Audit Committee – 28 February 2013

10. Treasury Management Presentation

Portfolio Holder	*Cllr Tim Carroll*
Director:	*Donna Parham, Assistant Director – Finance and Corporate Services*
Lead Officer:	*Donna Parham*
Contact Details:	*donna.parham@southsomerset.gov.uk or (01935) 462225*

Purpose of the Report

Mark Swallow from Arlingclose will be attending the meeting to give a presentation on current issues including:

- The current economic situation,
- Credit worthiness;
- Investment advice and
- The interest rate environment.

He will also be looking at our current investment portfolio in terms of risk and reward.

Audit Committee – 28 February 2013

11. Treasury Management Strategy Statement and Investment Strategy 2013/14

Executive Portfolio Holder:	*Councillor Tim Carroll*
Assistant Director:	*Donna Parham, Assistant Director – Finance and Corporate Services*
Service Manager:	*Amanda Card, Finance Manager*
Lead Officer:	*Karen Gubbins, Principal Accountant – Exchequer*
Contact Details:	*donna.parham@southsomerset.gov.uk or (01935) 462225*

Purpose of the Report

This report has been prepared for Audit Committee who has been tasked with the scrutiny of treasury management and to recommend to full Council the Treasury Management Strategy Statement and Investment Strategy for 2013/14.

Recommendation

To recommend the Treasury Management Strategy Statement and Investment Strategy for 2013/14 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 (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the CLG's Investment Guidance.

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 2013/14 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 and is split into the following main areas:

- Background
- Balance Sheet and Treasury Position
- Outlook for Interest Rates
- Borrowing Requirement and Strategy
- Investment Policy and Strategy
- Balanced Budget Requirement
- 2013/14 MRP Statement
- Monitoring and Reporting on Treasury Management
- Other Items

Financial Implications

The revised strategy will achieve the budget for new investments in 2013/14. If members would prefer to accept a more risk averse strategy we will be unable to achieve the Treasury Management Interest budget because the Authority will be restricted to counterparties who offer lower rates of return. In addition, there would be less diversification within the Council's portfolio, ultimately concentrating all risks within a select few counterparties.

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

Appendix 1

South Somerset District Council
Treasury Management Strategy Statement and Investment Strategy 2013/14

Contents

Appendices

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") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the CLG's Investment Guidance.

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 adopts the key recommendations of CIPFA's Treasury Management in the Public Services: Code of Practice (the Code), as described in Section 5 of the Code.

1.4 Accordingly, the Council will create and maintain, as the cornerstones for effective treasury management:-

- A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities

- Suitable treasury management practices (TMPs), setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

1.5 Full Council will receive reports on its treasury management policies, practices and activities including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close.

1.6 The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to Audit Committee and for the execution and administration of treasury management decisions to the Assistant Director (Finance and Corporate Services) who will act in accordance with the organisation's policy statement and TMPs and CIPFA's standard of Professional Practice on Treasury Management.

1.7 The Council nominates Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

1.8 This 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. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

1.9 This Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

1.10 The Council's primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yield earned on investments remain important but are secondary considerations.

1.11 The Council's borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council transparency and control over its debt.

1.12 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:

	31/03/13 Estimate £'000	**31/03/14 Estimate £'000**	**31/03/15 Estimate £'000**	**31/03/16 Estimate £'000**
CFR	9,381	9,447	9,332	9,234
Usable Capital Receipts	(30,399)	(29,057)	(29,077)	(29,161)
Balances & Reserves	(8,077)	(6,278)	(6,461)	(6,215)
Net Balance Sheet Position	**(29,095)**	**(25,888)**	**(26,206)**	**(26,142)**

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 underlying need to borrow 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 2013/14 is nil and for interest receipts is £316,300

3. Outlook for Interest Rates

3.1 The Arlingclose interest rate forecast continues its theme of the last few years, that is, that interest rates will remain low for even longer. The forecast is for official UK interest rates to remain at 0.5% until 2016 given the bleak outlook for economic growth and the extension of austerity measures announced in the Chancellor's Autumn Statement. Until there is a credible resolution of the problems that stalk the Eurozone – and that resolution requires full-scale fiscal union which faces many significant political hurdles – then the UK's safe haven status and minimal prospect of increases in official interest rates will continue to combine and support the theme within the forecast.

3.2 The economic and interest rate forecast provided by the Authority's treasury management advisor is attached at Appendix C. The Authority will reappraise its strategies from time to time in response to evolving economic, political and financial events.

4. Borrowing Requirement and Strategy

4.1 Treasury management and borrowing strategies in particular continue to be influenced not only by the absolute level of borrowing rates but also the relationship between short and long term interest rates. The interest rate forecast provided in appendix C indicates that an acute difference between short and longer term interest rates is expected to continue. This difference creates a "cost of carry" for any new longer term borrowing where the proceeds are temporarily held as investments because of the difference between what is paid on the borrowing and what is earned on the investment. Whilst the cost of carry can be assumed to be a reasonably short term issue since borrowing is often for longer dated periods (anything up to 50 years) it cannot be ignored against a backdrop of uncertainty and affordability constraints in the Authority's wider financial position.

4.2 As indicated in the following table, the authority has a gross borrowing requirement of £9m in 2013/14 but has sufficient balances and reserves to avoid the need for external borrowing. By essentially lending its own surplus funds to itself the Authority is able to minimise borrowing costs and reduce overall treasury risk by reducing the level of its external investment balances.

	31/03/13 Estimate £'000	31/03/14 Estimate £'000	31/03/15 Estimate £'000	31/03/16 Estimate £'000
Capital Financing Requirement (CFR)	9,381	9,447	9,332	9,234
Less: Existing Profile of Borrowing and Other Long Term Liabilities	(268)	(334)	(219)	(121)
Cumulative Maximum External Borrowing Requirement	(9,113)	(9,113)	(9,113)	(9,113)
Capital Receipts, Balances & Reserves	(38,476)	(35,335)	(35,538)	(35,376)
Cumulative Net Borrowing Requirement (Investments/ Call on capital receipts)	**(38,476)**	**(35,335)**	**(35,538)**	**(35,376)**

4.3 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.

4.4 In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Council will keep under review the following borrowing options:

- Internal
- PWLB loans
- Borrowing from other local authorities
- Borrowing from institutions such as the European Investment Bank
- Commercial Banks
- Capital Markets (stock issues, commercial paper and bills)
- Structured finance
- Leasing

4.5 The Council will undertake a financial options appraisal before any borrowing is made.

4.6 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.

4.7 The cost of carry has resulted in an increased reliance upon shorter dated and variable rate borrowing. This type of borrowing injects volatility into the debt portfolio in terms of interest rate risk but is counterbalanced by its affordability and alignment of borrowing costs with investment returns. The Authority's exposure to shorter dated and variable rate borrowing is kept under regular review by reference to the difference or spread between variable rate and longer term borrowing costs. A significant narrowing in the spread (e.g. by 0.50%) will result in an immediate and formal review of the borrowing strategy to determine whether the exposure to shorter dated and variable rates is maintained or altered.

5. Investment Policy and Strategy

Annual Investment Strategy

5.1 In accordance with Investment Guidance issued by the CLG and best practice this Authority's primary objective in relation to the investment of public funds remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yields earned on investments is important but are secondary considerations.

5.2 The Authority and its advisors remain on a heightened state of alert for signs of credit or market distress that might adversely affect the Authority.

5.3 Investments are categorised as 'Specified' or 'Non Specified' investments within the investment guidance issued by the CLG.

5.4 Specified investments are sterling denominated investments with a maximum maturity of one year. They also meet the "high credit quality" as determined by the Authority and are not deemed capital expenditure investments under Statute. Non specified investments are, effectively, everything else. The types of investments that will be used by the Authority and whether they are specified or non-specified are as follows:

Investment	Specified	Non-Specified
Term deposits with banks and building societies	✓	✓
Term deposits with other UK local authorities	✓	✓
Investments with Registered Providers	✓	✓
Certificates of deposit with banks and building societies	✓	✓
Gilts	✓	✓
Treasury Bills (T-Bills)	✓	×
Bonds issued by Multilateral Development Banks	✓	✓
Local Authority Bills	✓	×
Commercial Paper	✓	×
Corporate Bonds	✓	✓
AAA-Rated Money Market Funds	✓	×
Other Money Market and Collective Investment Schemes	✓	✓
Debt Management Account Deposit Facility	✓	×

5.5 Registered Providers (RPs) have been included within specified and non-specified investments for 2013/14. Investments with RPs will be analysed on an individual basis and discussed with Arlingclose prior to investing.

5.6 The Authority and its advisors, Arlingclose Ltd, select countries and financial institutions after analysis and ongoing monitoring of:

- Published credit ratings for financial institutions. The minimum credit rating for non-UK sovereigns is AA+ (or equivalent). For specified investments the minimum long term rating for counterparties is A- (or equivalent).
- Credit Default Swaps (where quoted)
- Economic fundamentals (for example Net Debt as a percentage of GDP)
- Sovereign support mechanisms
- Share Prices
- Corporate developments, news, articles, markets sentiment and momentum
- Subjective overlay

Any institution can be suspended or removed should any of the factors identified above give rise to concern. The Countries and institutions that meet the criteria for investments are included in Appendix D

5.7 Authority's Banker – The Council banks with National Westminster Bank. At the current time, it does meet the Authority's minimum credit criteria. Even if the credit rating falls below the Authority's minimum criteria, Natwest will continue to be used for short term liquidity requirements (overnight) and business continuity arrangements.

Investment Strategy

5.8 With short term interest rates low for some time, an investment strategy will typically result in a lengthening of investment periods, where cash flow permits, in order to lock in higher rates of acceptable risk adjusted returns. The problem in the current environment is finding an investment counterparty providing acceptable levels of counterparty risk.

5.9 In order to diversify an investment portfolio largely invested in cash, investments will be placed with a range of approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return. Maximum investment levels with each counterparty will be set to ensure prudent diversification is achieved.

5.10 Money Market Funds (MMFs) will be utilised but good treasury management practice prevails and whilst MMFs provide good diversification the Authority will also seek to diversify any exposure by utilising more than one MMF. The Authority will also restrict its exposure to MMFs with lower levels of funds under management and will not exceed 0.5% of the net asset value of the MMF. In the case of Government MMFs, the Council will ensure exposure to each Fund does not exceed 2% of the net asset value of the Fund.

5.11 The Authority has evaluated the use of Pooled Funds and determined the appropriateness of their use within the investment portfolio. Pooled funds enable the Authority to diversify the assets and the underlying risk in the investment portfolio and provide the potential for enhanced returns.

5.12 Investments in pooled funds will be undertaken with advice from Arlingclose Ltd. The Authority's current investments in Pooled Funds are listed in Appendix E; their performance and continued suitability in meeting the Authority's investment objectives are regularly monitored.

5.13 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. The Council's current level of investments is shown at Appendix A.

5.14 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)

Policy on use of financial Derivatives

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

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

5.17 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

5.18 The local authority will only use derivatives after seeking expertise, a legal opinion and ensuring officers have the appropriate training for their use.

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. 2012/13 MRP Statement

Background:

7.1 CLG's Guidance on Minimum Revenue Provision (issued in 2010) places a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Secretary of State and local authorities are required to "have regard" to such Guidance under section 21(1A) of the Local Government Act 2003.

7.2 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.

MRP Options:

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

Option 1 – Regulatory Method:

7.4 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:

7.5 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:

7.6 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 Instalments: 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.

7.7 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.

7.8 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.

7.9 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.

7.10 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.

Option 4 - Depreciation Method:

7.11 The deprecation 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 2013/14:

7.12 It is proposed that for 2013/14 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.

7.13 MRP in respect of leases brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.

8. <u>Monitoring and Reporting on Treasury Management</u>

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) ensures 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 Management Advisors

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
- 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.

APPENDIX A

EXISTING PORTFOLIO PROJECTED FORWARD

	31/03/12 Actual £'000	31/03/13 Estimate £'000	31/03/14 Estimate £'000	31/03/15 Estimate £'000
External Borrowing: *Long-term liabilities* • *Finance Leases*	383	259	251	80
Total External Debt	**389**	**259**	**251**	**80**
Investments: *Managed in-house* • Deposits and monies on call and Money Market Funds	25,710	38,910	39,077	39,161
• Supranational bonds	13,203	0	0	0
Total Investments	**38,913**	**38,910**	**39,077**	**39,161**
(Net Borrowing Position)/ Net Investment position	**38,524**	**38,651**	**38,826**	**39,081**

APPENDIX B

PRUDENTIAL INDICATORS 2013/14 TO 2015/16

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 2012/13, 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 Tax. The approved expenditure for 2012/13 and the estimates of capital expenditure to be incurred for 2013/14 and future years are:

	2012/13 Approved £'000	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**	**2015/16 Estimate £'000**
Approved capital schemes	3,526	1,259	(44)	(84)
Reserve schemes	1,279	1,062	0	0
New Schemes for 2013/14 start	533	881	370	0
Total Expenditure	**5,338**	**3,202**	**326**	**(84)**

The figures in the later years are showing income streams. This is due to income already budgeted from previously approved schemes. This will change 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 2013/14 and future years, and the approved figures for 2012/13 are:

Portfolio	2012/13 Approved £'000	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Financing Costs*	(397)	(220)	(165)	(177)
Net Revenue Stream	16,577	17,955	19,153	18,341
%*	**(2.4)**	**(1.2)**	**(0.9)**	**(1.0)**

*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.

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:

	2012/13 Approved £'000	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Opening CFR	9,506	9,381	9,447	9,332
Capital Expenditure	3,526	3,598	447	0
Capital Receipts*	(3,117)	(2,140)	(326)	84
Grants/Contributions*	(409)	(1,458)	(121)	(84)
MRP	(125)	(96)	(115)	(99)
Additional Leases taken on during the year	0	163		
Closing CFR	**9,381**	**9,447**	**9,332**	**9,234**

*Figures in brackets denote financing through receipts or reserves.

As a result of agreeing a capital programme year by year, and the fact that we have an identified income stream from the Crewkerne Aqua Centre Loan Repayment and the repayment of capital from the Goldenstones 10 year plan, the current position is showing an abnormal contribution to capital receipts year 2015/16 (as opposed to the usual funding from capital receipts).

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.

	2012/13 Approved £'000	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Net Borrowing*	(36,014)	(38,910)	(39,077)	(39,161)
CFR	9,381	9,447	9,332	9,234

*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.

	2012/13 % Limit	2013/14 % Limit	2014/15 % Limit	2015/16 % Limit
Fixed	80	80	80	80
Variable	100	100	100	100

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

	2012/13 % Limit	2013/14 % Limit	2014/15 % Limit	2015/16 % Limit
Fixed	100	100	100	100
Variable	100	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	2012/13 Approved £'000	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Between 1-2 years	25,000	25,000	25,000	25,000
Between 2-3 years	20,000	20,000	20,000	20,000
Between 3-4 years	10,000	10,000	10,000	10,000
Between 4-5 years	10,000	10,000	10,000	10,000
Over 5 years	5,000	5,000	5,000	5,000

The estimates are considerably higher than the actual balances held in previous years 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 – Credit Risk:

The Council considers security, liquidity and yield, in that order, when making investment decisions.

Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk.

The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution and its sovereign
- Sovereign support mechanisms
- Credit default swaps (where quoted)
- Share prices (where available)
- Economic Fundamentals, such as a country's net debt as a percentage of its GDP
- Corporate developments, news articles, markets sentiment and momentum
- Subjective overlay

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

Prudential Indicator 8 - 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 31/03/2012	**£'000**
Borrowing	0
Other Long-term Liabilities	389
Total	**389**

Prudential Indicator 9 - 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. 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.

	2012/13 Approved £'000	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Borrowing	11,000	11,000	11,000	11,000
Other Long-term Liabilities	1,000	1,000	1,000	1,000
Total	**12,000**	**12,000**	**12,000**	**12,000**

Prudential Indicator 10 – 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.

	2012/13 Approved £'000	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Borrowing	9,200	9,200	9,200	9,200
Other Long-term Liabilities	800	800	800	800
Total	**10,000**	**10,000**	**10,000**	**10,000**

Prudential Indicator 11 - 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	2011/12 % Actual	2012/13 % Actual	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 12 - 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	**2012/13 Approved £**	**2013/14 Estimate £**	**2014/15 Estimate £**	**2015/16 Estimate £**
Decrease in Band D Council Tax	0.34	0.47	0.67	0.67

Prudential Indicator 13 - 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 18th April 2002.

APPENDIX C

Arlingclose's Economic and Interest Rate Forecast

	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16
Official Bank Rate													
Upside risk			0.25	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	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
3-month LIBID													
Upside risk	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	0.75
Central case	0.40	0.40	0.40	0.45	0.45	0.50	0.50	0.50	0.55	0.55	0.55	0.60	0.60
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
1-yr LIBID													
Upside risk	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	0.75
Central case	0.85	0.90	0.95	0.95	1.00	1.00	1.00	1.00	1.10	1.10	1.10	1.10	1.10
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
5-yr gilt													
Upside risk	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00
Central case	0.95	0.95	0.95	0.95	1.00	1.00	1.00	1.00	1.10	1.10	1.10	1.20	1.20
Downside risk	-0.25	-0.25	-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	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.00	1.00
Central case	2.00	2.00	2.05	2.05	2.05	2.05	2.10	2.10	2.10	2.20	2.20	2.20	2.20
Downside risk	-0.25	-0.25	-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	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00
Central case	2.90	2.90	2.90	2.90	3.00	3.00	3.00	3.00	3.10	3.10	3.10	3.10	3.10
Downside risk	-0.25	-0.25	-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	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00
Central case	3.35	3.35	3.35	3.40	3.40	3.40	3.50	3.50	3.50	3.50	3.60	3.60	3.60
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

Underlying Assumptions:

- UK growth is unlikely to return to above trend for the foreseeable future. Q3 GDP was strong at 0.9% but this momentum is unlikely to be sustained in Q4 or in 2013. The rebalancing from public-sector driven consumption to private sector demand and investment is yet to manifest, and there is little sign of productivity growth. Further contraction in the Eurozone, including Germany's powerful economy, and slower forecast growth in the emerging economies (Brazil/Mexico/India) are exacerbating the weakness.

- Consumer Price Inflation has fallen to 2.7 % from a peak of 5.2%. Near term CPI is likely to be affected by volatility in commodity prices and its decrease towards the 2% target is expected to be slower than previously estimated. Real wage growth (i.e. after inflation) is forecast to remain weak.

- The fiscal outlook for bringing down the structural deficit and stabilise debt levels remains very challenging. Weakened credibility of the UK reining its levels of debt poses a risk to the AAA status, but recent history (US, France) suggests this may not automatically result in a sell-off in gilts.

- In the absence of large, unexpected decline in growth, QE is likely to remain on hold at £375bn for now. The availability of cheaper bank borrowing and subsequently for corporates through the Funding for Lending Scheme (FLS) is a supporting factor.

- The US Federal Reserve's shift in its rate guidance from a date-based indication to economic thresholds (6.5% unemployment, inflation 1 – 2 years out projected to remain below 2.5%, longer term inflation expectations remain well anchored) is likely to increase market uncertainty around the highly volatile US employment data releases.

- The Eurozone is making slow headway which has curtailed some of the immediate risks although peripheral countries continue to struggle. Fully-fledged banking and fiscal union is still some years away.
- In the US, the issues of spending cuts, reducing the budget deficit and raising the country's debt ceiling remain unresolved. A failure to address these by March 2013 could lead to a similar showdown and risks a downgrade to the US sovereign credit rating by one or more agencies.
- A reversal in market risk sentiment from current "risk on" to "risk off" could be triggered by economic and/or political events – impending Italian and German elections, US debt ceiling impasse, difficulty surrounding Cyprus' bailout, and contagion returning the haunt the European peripheral nations – could inject renewed volatility into gilts and sovereign bonds.

APPENDIX D

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 and subsequent amendments.

"Specified" Investments identified for the Council's use are:

- Deposits in the DMO's Debt Management Account Deposit Facility
- Deposits with UK local authorities (including Police 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)
- Commercial Paper
- 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 and subsequent amendments.

*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: A3 (Moody's) or A- (S&P) or A-(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 (including Police Authorities)	No limit
Term Deposits/Call Accounts/CDs	UK	Counterparties rated at least A- Long Term and F1 Short Term (or equivalent)	See following table
Term Deposits/Call Accounts/CDs	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+	See following table
Gilts	UK	DMO	No limit
T-Bills	UK	DMO	No limit
LA-Bills	UK	Other UK Local Authorities	No limit
Commercial Paper		Counterparties rated at least A- Long Term and F1 Short Term (or equivalent)	(6,000,000
Bonds issued by multilateral development banks		(For example, European Investment Bank/Council of Europe, Inter American Development Bank)	N/A
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)	Will not exceed 0.5% of the net asset value of the MMF
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	£6,000,000

Under the new proposal our Current Counterparty list would be 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	HSBC Bank Plc	£6,000,000	
Term Deposits/Call Accounts	UK	Nationwide Building Society	£6,000,000	
Term Deposits/Call Accounts	UK	Natwest (RBS Group)	£6,000,000	£6,000,000
Term Deposits/Call Accounts	UK	Royal Bank of Scotland (RBS) Group	£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	£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	

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	Finland	Pohjola	£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	Netherlands	Bank Nederlandse Gemeenten	£6,000,000	
Term Deposits/Call Accounts	Singapore	DBS Bank Ltd	£6,000,000	
Term Deposits/Call Accounts	Singapore	Oversea-Chinese Banking Corporation (OCBC)	£6,000,000	
Term Deposits/Call Accounts	Singapore	United Overseas Bank (UOB)	£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:

Instrument	Maximum maturity	Max %/£M of portfolio	Capital expenditure?	Example
Term deposits with banks, building societies which meet the specified investment criteria (on advice from TM Adviser)	2 years	70% in aggregate	No	
Term deposits with local authorities	2 years	70% in aggregate	No	
CDs and other negotiable instruments with banks and building societies which meet the specified investment criteria (on advice from TM Adviser)	5 years	70% in aggregate	No	
Deposits with registered providers	10 years	£5m	No	
Gilts	10 years	70% in aggregate	No	
Bonds issued by multilateral development banks	10 years	70% in aggregate	No	EIB Bonds, Council of Europe Bonds etc.
Sterling denominated bonds by non-UK sovereign governments	10 years	70% in aggregate	No	
Money Market Funds and Collective Investment Schemes	These funds do not have a defined maturity date	50% of portfolio	No	Investec Target Return Fund; Elite Charteris Premium Income Fund; LAMIT; M&G Global Dividend Growth Fund
Corporate and debt instruments issued by corporate bodies	10 years	£10m	No	

purchased from 01/04/12 onwards				
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 and subsequent amendments	These funds do not have a defined maturity date	£2M	Yes	Way Charteris Gold Portfolio Fund; Aviva Lime Fund

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.

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 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 Instrument)	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

Audit Committee – 28 February 2013

12. Treasury Management Performance to December 2012

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

Purpose of Report

1. To review the treasury management activity and the performance against the Prudential Indicators for the nine months ended 31st December 2012.

Recommendations

2. The Audit Committee are asked to:
   - Note the Treasury Management Activity for the nine-month period ended 31st December 2012.
   - Note the position of the individual prudential indicators for the nine-month period ended 31st December 2012.

The Investment Strategy for 2012/13

3. The Treasury Management Strategy for 2012/13 has been underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2011, which includes the requirement for determining a treasury strategy on the likely financing and investment activity for the forthcoming financial year.

4. The Code also recommends that members are informed of Treasury Management activities at least twice a year. This report therefore ensures this authority is embracing Best Practice in accordance with CIPFA's recommendations.

5. Treasury management is defined as: "The management of the local authority's investments and 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."

6. With short term interest rates remaining lower for even longer than anticipated, our investment strategy will typically result in the lengthening of investment periods, where cash flow permits, in order to lock into higher rates of acceptable risk adjusted returns. The problem in the current environment is finding an investment counterparty providing acceptable levels of counterparty risk.

7. In order to diversify the authority's investment portfolio which is largely invested in cash, investments will be placed with a range of approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return.

8. Money Market Funds (MMFs) will be utilised but good treasury management practice prevails and whilst MMFs provide good diversification the Authority will also seek to diversify any exposure by utilising more than one MMF. The Authority

will also restrict its exposure to MMFs with lower levels of funds under management and it will not exceed 0.5% of the net asset value of the MMF. In the case of Government MMFs, the Council will ensure exposure to each Fund does not exceed 2% of the net asset value of the Fund.

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).

Interest Rates 2012/13

10. Base rate began the financial year and remains at 0.5%.

11. Our advisors are forecasting that rates will remain low for an extended period, as shown below:

	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16
Official Bank Rate													
Upside risk			0.25	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	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

Investment Portfolio

12. The table below shows the Council's overall investments as at 31st December 2012:

	Value of Investments at 01.04.12 £	Value of Investments at 31.12.12 £	Fixed/ Variable Rate
Investments advised by Arlingclose			
Euro Sterling Bonds	4,182,407		Fixed
World Bonds	3,035,190	3,022,352	Fixed
Certificates of Deposit		8,501,418	Variable
Money Market Fund (Variable Net Asset Value)		1,000,000	Variable
Euro Sterling Bonds	5,985,000	5,985,000	Variable
Total	**13,202,597**	**18,508,770**	
Internal Investments			
Short Term Deposits (Banks)	8,000,000	22,000,000	Variable
Short Term Deposits (Other LA's)	14,000,000	8,000,000	Variable
Short Term Deposits (DMADF)			Variable
Money Market Funds (Constant Net Asset Value) & Business Reserve Accounts	3,710,000	3,500,000	Variable
Total	**25,710,000**	**33,500,000**	
TOTAL INVESTMENTS	**38,912,597**	**52,008,770**	

Note:
Variable Net Asset Value (VNAV) Money Market Funds - where there is greater than 12 month history of a consistent £1 Net Asset Value although there is a risk you may receive less than the £1 you originally invested. This is monitored closely by Arlingclose before they recommend the use of the fund.
Constant Net Asset Value (CNAV) Money Market Funds – where £1 is invested you receive £1 back on withdrawal.

Returns for 2012/13

13. The returns to 31st December 2012 are shown in the table below:

	Actual Income £'000	% Rate of Return
Investments advised by Arlingclose		
Euro Sterling Bonds (Fixed)	5	
World Bonds (Fixed)	17	
Certificate of Deposits (CDs)	23	
Payden Money Market Fund (VNAV)	3	
Euro Sterling Bonds (Variable)	37	
Total	**85**	**0.81**
Internal Investments		
Short Term Deposits	179	
Money Market Funds (CNAV) & Business Reserve Accounts	35	
Total	**214**	**0.77**
Other Interest		
Miscellaneous Loans	8	
Total	**8**	
TOTAL INCOME TO 31st DECEMBER 2012	**307**	**0.78**
PROFILED BUDGETED INCOME	**380**	
FORECAST DEFICIT FOR YEAR END	**128,030**	
BENCHMARK RATE OF RETURN		**0.43**

14. The table above shows investment income for the year to date compared to the profiled budget. The annual budget is set at £507,030. Current estimates are predicting an underachievement of income to the value of £128,030. This shortfall will be covered by the Treasury Management Reserve, the balance of which is £500,000.

15. 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 the collection of council tax and business rates.

Investments

16. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2012/13. New investments can be made with the following institutions:
    - Other Local Authorities;
    - AAA-rated Money Market Funds;
    - Certificates of Deposit (CDs) and Term Deposits with UK Banks and Building Societies systemically important to the UK banking system and deposits with select non-UK Banks (Australian, Canadian and American);
    - T-Bills and DMADF (Debt Management Office);
    - Bonds issued by Multilateral Development Banks, such as the European Investment Bank;
    - Pooled funds (collective investment schemes) meeting the criteria in SI 2004 No 534 and subsequent amendments.

17. The graph shown in Appendix A shows the performance of the in-house Treasury team in respect of all investments for the quarter ending 31st December 2012 in comparison to all other clients of Arlingclose.

18. The graph shows that SSDC is in a satisfactory position in terms of the risk taken against the return on investments.

Borrowing

19. An actual overall borrowing requirement (CFR) of £9.4 million was identified at the beginning of 2012/13. As interest rates on borrowing exceed those on investments the Council has used its capital receipts to fund capital expenditure. As at 31st December 2012 the Council had no external borrowing.

Breakdown of investments as at 31st December 2012

Date Lent	Counterparty	Amount	Rate	Maturity Date
31-Jan-12	Nottingham City Council	2,000,000	0.80%	29-Jan-13
13-Mar-12	Corby Borough Council	2,000,000	0.80%	12-Mar-13
9-Nov-12	Bank of Scotland	1,000,000	1.15%	11-Feb-13
4-Dec-12	Barclays Bank Plc	1,000,000	0.52%	20-Mar-13
31-May-12	Newcastle City Council	3,000,000	0.72%	30-May-13
12-Dec-12	Barclays Bank Plc	1,000,000	0.98%	12-Dec-13
04-Oct-12	Nationwide Building Society	1,000,000	0.49%	11-Jan-13
06-Jul-12	Commonwealth Bank of Australia	5,000,000	0.52%	7-Jan-13
09-Oct-12	Barclays Bank Plc	1,000,000	0.50%	17-Jan-13
12-Jul-12	National Australia Bank	2,000,000	0.55%	14-Jan-13
06-Nov-12	IPA SCB TD Incoming (Santander)	1,000,000	0.83%	6-Feb-13
02-Aug-12	National Australia Bank	1,000,000	0.55%	2-Aug-13
05-Nov-12	Bank of Scotland	2,000,000	1.60%	7-May-13
12-Oct-12	Bank of Scotland	1,000,000	1.35%	7-Jan-13
12-Oct-12	Canadian Imperial Bank of Commerce	1,000,000	0.50%	11-Oct-13
15-Nov-12	IPA SCB TD Incoming (Santander)	1,000,000	0.82%	15-Feb-13
07-Nov-12	Barclays Bank Plc	1,000,000	1.05%	7-Nov-13
12-Nov-12	Nationwide Building Society	1,000,000	0.80%	12-Aug-13
28-Nov-12	Birmingham City Council	1,000,000	0.50%	30-Sep-13
29-Nov-12	IPA SCB TD Incoming (Santander)	1,000,000	0.82%	5-Mar-13
	Santander Plc Business Reserve	3,000,000	0.60%	
	Bank of Scotland Business Reserve	500,000	0.50%	
	Payden Money Market Fund*	1,000,000	1.34%	
	International Bank for Reconstruction and Development (the World Bank)	2,014,080	0.84%	10-Dec-13
	International Bank for Reconstruction and Development (the World Bank)	1,008,272	0.71%	10-Dec-13
	Eurobond Floating Rate Note	5,985,000	SONIA+ 0.35%	18-Mar-14
	Certificate of Deposit	1,500,227	0.83%	14-Jan-13
	Certificate of Deposit	3,000,891	0.97%	2-Aug-13
	Certificate of Deposit	2,000,151	0.50%	14-Feb-13
	Certificate of Deposit	2,000,149	0.47%	18-Mar-13
		52,008,770		

** Note: Money Market Funds are instant access accounts so the rate displayed is a daily rate*

Prudential Indicators – Quarter 3 monitoring

Background:

20. In March 2012, Full Council approved the indicators for 2012/13, as required by the Prudential Code for Capital Finance in Local Authorities. The Local Government Act 2003 allowed 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:

	2012/13 Original Estimate £'000	Expected Outturn £'000	2012/13 Variance £'000	Reason for Variance
Approved capital schemes	4,059	4,434	375	Slippage from previous years makes up the majority of the variance as well as new allocations in year and transfers into the main programme from the reserve schemes
Reserves	1,279	3,407	2,128	The variance is due to slippage from last financial year into this financial year and new allocation of monies
Total Expenditure	**5,338**	**7,841**	**2,503**	

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 of financing capital costs compared to the revenue income stream to support these costs. This shows how much of the revenue budget is committed to the servicing of finance.

Portfolio	2012/13 Original Estimate £'000	Expected Outturn £'000	2012/13 Variance £'000	Reason for Variance
Financing Costs*	(397)	(254)	143	We are currently predicting an underachievement of

				investment income of £128k
Net Revenue Stream	16,577	17,039	462	Carry forwards of £497k and £74k for Evening/Sunday Car parking charges built into the budget less budget savings of £139k for 13/14 offered for 12/13 returned to general balances
%*	**(2.4)**	**(1.5)**	**0.9**	

*figures in brackets denote income through receipts and reserves

24. The financing costs include interest payable, 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:

	2012/13 Revised Estimate £'000	**Expected Outturn £'000**	**2012/13 Variance £'000**	**Reason for Variance**
Opening CFR	9,506	9,506	0	
Capital Expenditure	4,059	7,873	3,814	See explanations for indicator 1 above
Capital Receipts*	(3,650)	(4,434)	(784)	Slippage of schemes approved in previous years
Grants/Contributions*	(409)	(3,439)	(3,030)	Reprofiling of income expected in future years
Minimum Revenue Position (MRP)	(125)	(124)	1	Roundings
Additional Finance Leases	0	0	0	
Closing CFR	**9,381**	**9,382**	**1**	

*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.

	2012/13 Revised Estimate £'000	2012/13 Qtr 3 Actual £'000	2012/13 Variance £'000	Reason for Variance
Net Borrowing	(36,014)	(51,458)	(15,444)	The estimate is a prediction of the year end balance whilst quarter 3 is always higher as we are 9 months into the 10 month council tax collection cycle
CFR	9,381	9,382	1	

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.

	2012/13 % Limit	2012/13 Qtr 3 Actual %	2012/13 Variance %	Reason for Variance
Fixed	80	5.8	(73.5)	Within limit
Variable	100	94.2	(6.5)	Within limit

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

	2012/13 % Limit	2012/13 Qtr 3 Actual %	2012/13 Variance %	Reason for Variance
Fixed	100	0	100	SSDC currently has no borrowing
Variable	100	0	100	SSDC 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	2012/13 Maximum Limit £'000	2012/13 Qtr 3 Actual £'000	2012/13 Expected Outturn £'000	Reason for Variance
Between 1-2 years	25,000	5,985	0	Within limit
Between 2-3 years	20,000	0	0	Within limit
Between 3-4 years	10,000	0	0	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. The purpose of this treasury indicator is to highlight a situation where the Council is planning to borrow in advance of need.

	2012/13 Estimate £'000	2012/13 Qtr 3 Actual £'000	2012/13 Variance £'000	Reason for Variance
Outstanding Borrowing (at nominal value)	0	0	0	
Other long-term liabilities (at nominal value)	196	258	62	Additional Leases taken out since setting the budget
Gross Debt	**196**	**258**	**62**	
Less: Net Investments	**(36,014)**	**(51,458)**	**(15,444)**	
Net Debt	**(35,818)**	**(51,200)**	**(15,382)**	

The figures above described as net debt actually represent net investments.

Prudential Indicator 8 – Credit Risk:

34. The Council considers security, liquidity and yield, in that order, when making investment decisions.

Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk.

The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution and its sovereign

- Sovereign support mechanisms
- Credit default swaps (where quoted)
- Share prices (where available)
- Economic Fundamentals, such as a country's net debt as a percentage of its GDP
- Corporate developments, news articles, markets sentiment and momentum
- Subjective overlay

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

Prudential Indicator 9 - Actual External Debt:

35. 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 31/03/2012	**£'000**
Borrowing	0
Other Long-term Liabilities (Finance Leases)	383
Total	**383**

Prudential Indicator 10 - Authorised Limit for External Debt:

36. 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.

	2012/13 Estimate £'000	**2012/13 Qtr 3 Actual £'000**	**2012/13 Variance £'000**	**Reason for Variance**
Borrowing	11,000	0	(11,000)	SSDC currently has no external borrowing
Other Long-term Liabilities (Finance Leases)	1,000	258	(742)	Within limit
Total	**12,000**	**258**	**(11,742)**	

Prudential Indicator 11 – Operational Boundary for External Debt:

37. 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.

	2012/13 Estimate £'000	2012/13 Qtr 3 Actual £'000	2012/13 Variance £'000	Reason for Variance
Borrowing	9,200	0	(9,200)	SSDC currently has no external borrowing
Other Long-term Liabilities (Finance Leases)	800	258	(542)	Within limit
Total	**10,000**	**258**	**(9,742)**	

Prudential Indicator 12 - Maturity Structure of Fixed Rate borrowing:

38. 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	2011/12 Upper Limit %	2011/12 Lower Limit %	2011/12 Qtr 3 Actual %	2011/12 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 13 - Incremental Impact of Capital Investment Decisions:

39. 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	2012/13 Original Estimate £
Decrease in Band D Council Tax	0.34

Prudential Indicator 14 - Adoption of the CIPFA Treasury Management Code:

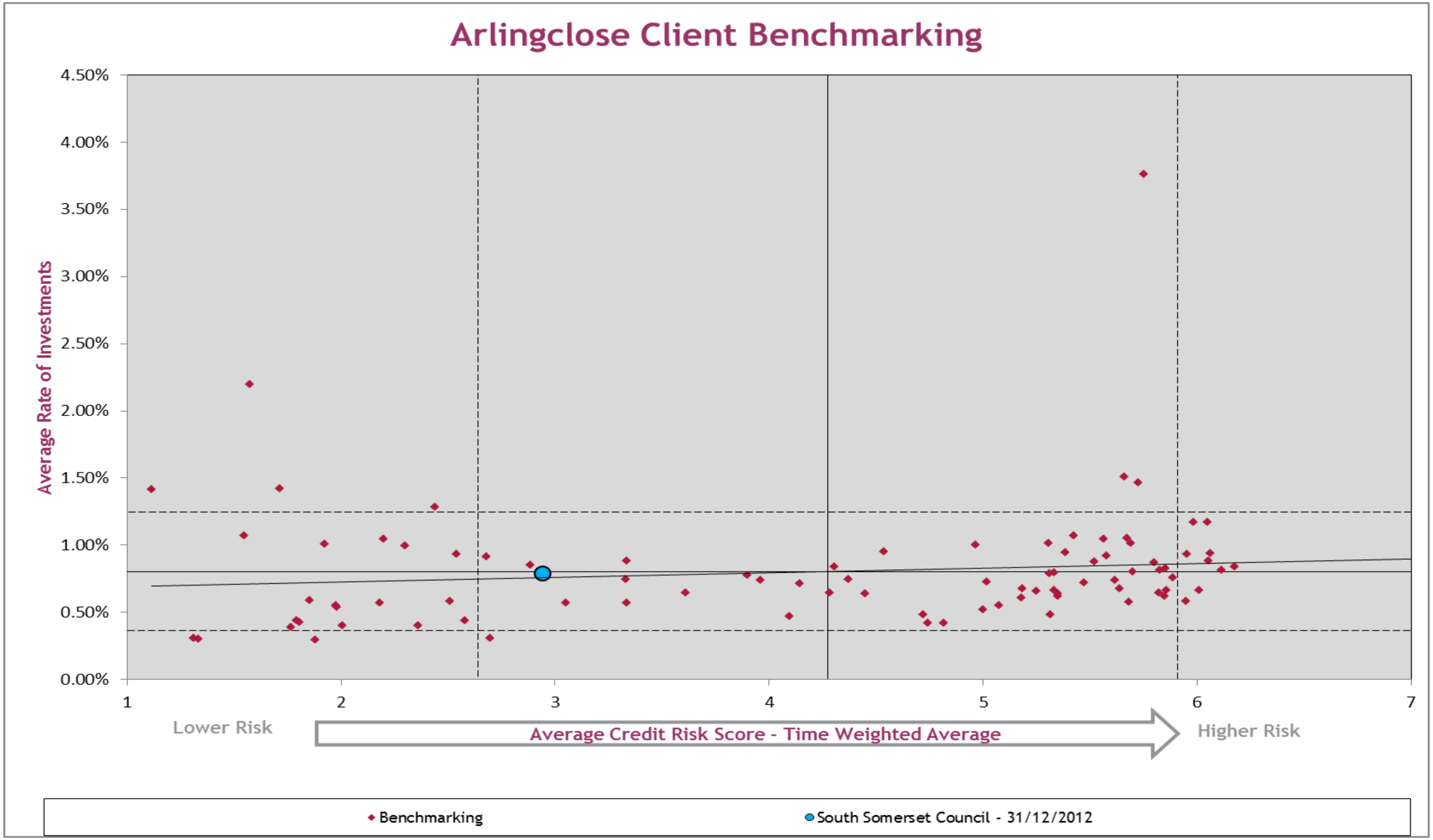
40. This indicator demonstrates that the Council has adopted the principles of best practice.

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 18th April 2002.

Conclusion

41. 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*


Arlingclose Client Benchmarking
4.50%
4.00%
3.50%
3.00%
2.50%
2.00%
1.50%
1.00%
0.50%
0.00%
Average Rate of Investments
1
2
3
4
5
6
7
Lower Risk
Average Credit Risk Score - Time Weighted Average
Higher Risk
Benchmarking
South Somerset Council - 31/12/2012

Audit Committee – 28 February 2013

13. Audit Forward Plan

Assistant Director: *Donna Parham – Finance and Corporate Services*
Lead Officer: *Anne Herridge, Committee Administrator*
Contact Details: *anne.herridge@southsomerset.gov.uk or (019350 462570*

Purpose of the Report

This report informs Members of the agreed Audit Committee Forward Plan.

Recommendation

Members are asked to:-

Comment upon and note the proposed Audit Committee Forward Plan as attached at Appendix A.

Audit Committee Forward Plan

The forward plan sets out items and issues to be discussed over the coming few months and is reviewed annually.

Background Papers: *None*

Audit Committee – 28 February 2013

Audit Committee Forward Plan

Appendix A

Meeting Date	Agenda Item	Lead Officer
28 Mar 13	Risk Management Update	Gary Russ
28 Mar 13	Health, Safety & Welfare – Annual Report	Pam Harvey
25 Apr 13	Accounting policies for 2012/13 Accounts	Amanda Card
	Register of staff interests – Annual Review	Ian Clarke
23 May 13	2012/13 Annual Governance Statement	Donna Parham
	Review of Internal Audit	Donna Parham
	Internal Audit Plan – Review 2012/13	Andrew Ellins
27 Jun 13	Approve Annual Treasury Management Activity Report 2012/13 with recommendation to Full Council	Karen Gubbins
	External Audit – Audit of financial controls 2012/13	Donna Parham

14. Date of Next Meeting

The next scheduled meeting of the Audit Committee will be held on Thursday, 28 March 2013 at 10.00 a.m. in the Main Committee Room, Council Offices, Brympton Way, Yeovil.
