

To: Councillors Stevens (Chairman),
Lovelock, McElligott, McKenna, Page,
Steele and Terry

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Your Ref:

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21 September 2016

Your contact is: Peter Driver - Committee Services

NOTICE OF MEETING - AUDIT AND GOVERNANCE COMMITTEE - 29 SEPTEMBER 2016

A meeting of the Audit & Governance Committee will be held on Thursday 29 September 2016 at 6.30pm in the Council Chamber, Civic Offices, Reading. The Agenda for the meeting is set out below.

AGENDA

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3. APPROVAL OF THE 2015/16 ACCOUNTS, EY AUDIT MEMORANDUM AND AUDIT OPINION (ISA 260)	6

This report seeks, in accordance with the Accounts & Audit Regulations, the approval of the Council's accounts by the end of September, which will conclude the accounts and audit process for 2015/16.

4. FUTURE AUDIT ARRANGEMENTS - APPOINTMENT OF PUBLIC SECTOR AUDIT APPOINTMENTS LTD	9
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This report presents the latest position on the requirement in the Local Audit & Accountability Act 2014 for the Council to eventually appoint its own auditor.

CIVIC OFFICES EMERGENCY EVACUATION: If an alarm sounds, leave by the nearest fire exit quickly and calmly and assemble on the corner of Bridge Street and Fobney Street. You will be advised when it is safe to re-enter the building.

5.	PUBLIC SECTOR INTERNAL AUDIT STANDARDS (SELF ASSESSMENT)	14
	This report informs the Committee of the results of a self-assessment carried out by the Chief Auditor against the Public Sector Internal Audit Standards.	
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	This report provides the Committee with an update on key findings from Internal Audit reports issued since the last quarterly progress report in July 2016.	
7.	BUDGET MONITORING REPORT	40
	This report updates the Committee on the Council's budget monitoring position to the end of July 2016.	
8.	TREASURY MANAGEMENT 2016/17 ACTIVITY TO AUGUST	46
	This report contains information about the Council's treasury activities to the end of August in 2016/17.	

AUDIT AND GOVERNANCE COMMITTEE MINUTES - 21 JULY 2016

Present: Councillor Stevens (Chair), Lovelock, McElligott, McKenna, Page, Steele & Terry.

Also in attendance:

Simon Warren	Interim Managing Director
Alan Cross	Head of Finance
Paul Harrington	Chief Auditor
Giorgio Framaliccio	Head of Planning, Development and Regulatory Services
Robin Pringle	Corporate Health & Safety Manager
Maria Grindley	Director and Engagement Lead, EY LLP
Simon Wilson	Summer Intern, EY LLP
Alan Witty	Engagement Senior Manager, EY LLP
Russell Dyer	Corporate Finance Business Partner

1. MINUTES

The Minutes of the meeting of 19 April 2016 were confirmed as a correct record and signed by the Chair.

2. HEALTH & SAFETY - ADDITIONAL SAFEGUARDS EMPLOYED FOLLOWING THE INCIDENT AT THE WILLOWS AND REVISED HEALTH, SAFETY AND STAFF WELLBEING STRATEGY 2016-19

The Director of Environment and Neighbourhood Services submitted a report outlining actions that had been taken and additional safeguards put in place reflecting the learning points from the Willows case, as discussed at the meeting on 19 April 2016 (Minute 17 refers).

The report explained that following identification of Legionella bacteria in the water system at the Willows Care Home, a range of further safeguards had been put in place across all buildings within the Council's portfolio. The report detailed the procedures and processes which were in place and the actions taken to reduce the risks of any such incident recurring.

The following documents were attached to the report:

Appendix 1 Spreadsheet of Health & Safety spot audits of high risk Council buildings
Appendix 2 Legionella Control Flowchart

The following documents had been circulated separately:

Appendix 3 Property Management and Compliance Guide
Appendix 4 Health & Safety Competency Flow Chart
Appendix 5 Health, Safety & Staff Wellbeing Strategy and Action Plan

In discussion the Chief Auditor confirmed that there were three separate streams of audit activity on Health and Safety and further assurance on compliance were expected to be included in the Internal Audit update report to the Committee in September 2016.

Resolved:

AUDIT AND GOVERNANCE COMMITTEE MINUTES - 21 JULY 2016

- (1) That the actions taken and additional safeguards put in place in relation to the Willows case be noted; and
- (2) That the revised Health, Safety and Staff Wellbeing Strategy covering the period 2016-2019 be noted.

3. BUDGET MONITORING 2016/17

The Head of Finance submitted a report on Budget Monitoring that had been considered by the Policy Committee at its meeting on 18 July 2016 and was presented for information.

The report described significant budget pressures, particularly in Children's Services, which was projecting an overspend of £3.635m, representing an 11.7% variance.

The Committee discussed the report and the impacts of wider national policy and economic context on the Council's budget position.

Resolved: That the report be noted.

4. DRAFT OUTTURN POSITION 2015/16

The Head of Finance submitted a report on the draft outturn position for the 2015-16 accounts for the Council that had been considered by Policy Committee on 13 June 2016 and was presented for information.

The following documents were attached to the report:

Appendix A Section 106 receipts that Policy Committee had agreed were to be applied in 2015/16

Appendix B Final Accounts Process

Appendix C General Debtor Arrears

Resolved: That the report be noted.

5. EXTERNAL AUDITORS UPDATE

Alan Witty, Engagement Senior Manager at EY, the Council's external auditor, submitted a report on progress with the 2015/16 audit plan.

The report explained that the EY team had continued to meet regularly with key officers as part of the ongoing audit process. These meetings had enabled the EY team to develop an understanding of the Council's financial processes and to select the samples of income and expenditure they would use for audit purposes.

The report stated that EY's IT team would shortly conclude work on reviewing the controls around the Council's main financial systems. Initial draft findings had been shared with the Head of Finance for review, following which the report would be finalised.

Initial Housing Benefit testing had identified a number of potential errors, which would be reviewed to assess their implications for EY's certification work.

AUDIT AND GOVERNANCE COMMITTEE MINUTES - 21 JULY 2016

The Committee thanked EY for their proactive engagement and welcomed their intention to report to each meeting of the Committee.

Resolved: That the report be noted.

6. INTERNAL AUDIT ANNUAL ASSURANCE REPORT

The Chief Auditor submitted a report presenting, at Appendix 1, the Internal Audit Annual Assurance Report, as required by the Accounts and Audit regulations and the Public Sector Internal Audit Standards.

The report gave the Chief Auditor's opinion on the overall adequacy and effectiveness of the organisation's governance arrangements, risk management and internal control environment, drawing attention to any issues particularly relevant to the preparation of the Annual Governance Statement. It also drew out key themes arising from the work of the Audit Team during the 2015/2016 financial year, and compared the audit work undertaken with that planned, summarising the performance of the Internal Audit function against its performance measures and targets.

The report explained that detailed audit reports had been issued to the relevant Service Managers on the results of individual audits throughout the year, and to the relevant Directors and Heads of Service where unsatisfactory internal control had been identified. In addition, quarterly reports had been issued to, and discussed with, the Corporate Management Team (CMT) and the Audit & Governance Committee in order to report on standards of internal control, to provide appropriate focus on weaknesses and to progress remedial action where necessary.

The Annual Assurance Opinion for 2015/16 stated that the Internal Audit Team had concluded that the system of internal control was satisfactory and processes to identify and manage risk were in place.

Resolved: That the assurance opinion given by the Chief Auditor be noted.

7. ANNUAL GOVERNANCE STATEMENT 2015/16 AND IMPLEMENTATION PLAN

The Head of Finance submitted a report presenting the draft 2015/16 Annual Governance Statement.

The report explained that the Council was responsible for ensuring that financial management was adequate and effective and that the Council had a sound system of internal control, which facilitated the effective exercise of the Council's functions, including arrangements for the management of risk. The AGS was a record of the overall effectiveness of governance arrangements within the Authority; it reflected the latest guidance from CIPFA/SOLACE on a strategic approach to governance and demonstrated how the key governance requirements had been met.

The Head of Finance outlined two suggested amendments to the draft, in response to comments the auditor had made, and Cllr Lovelock raised a point that should be clarified. It was explained that other points may arise before the absolute final version is published with the accounts after the September committee.

The following documents were attached to the report:

Appendix 1 Draft Annual Governance Statement (AGS) 2015/16

Appendix 2 AGS Implementation plan for 2016/17

Resolved:

- (1) That, subject to (2) below, the draft Annual Governance Statement for 2015/16 be received and approved for publication with the Council's accounts; and
- (2) That the Interim Managing Director and Head of Finance, in consultation with the Leader of the Council and Chair of the Audit & Governance Committee, be authorised to make any necessary amendments that are needed before final publication.

8. AUDIT AND INVESTIGATIONS QUARTERLY REPORT

The Chief Auditor submitted a report giving an update on key findings emanating from Internal Audit reports issued since the previous quarterly progress report in April 2015. Attached to the report at Appendix A were the internal audit assurance definitions and priority ratings of recommendations.

The report set out a summary of the audit reports and an assurance finding for audits carried out of the following service areas:

- Electronic Document & Record Management
- Leisure income
- Katesgrove Primary School

Resolved: That the report be noted.

9. TREASURY OUTTURN REPORT 2015/16 & RELATED UPDATE

The Head of Finance submitted a report presenting, at Appendix 1, the Annual Treasury Outturn Report 2015/16.

The report explained that the Treasury Outturn report was intended to explain how the Council had tried to minimise net borrowing costs over the medium term, ensure it had enough money available to meet its commitments, ensure reasonable security of money lent and invested, maintain an element of flexibility to respond to changes in interest rates, and manage treasury risk overall. It also outlined some current treasury and related issues likely to impact the Council during 2016/17, the establishment of the Municipal Bonds Agency, and the developing treasury position in the context of the Council's finances and the referendum vote on leaving the European Union.

A Cross gave a presentation at the meeting summarising key treasury management issues.

AUDIT AND GOVERNANCE COMMITTEE MINUTES - 21 JULY 2016

Resolved: That the annual Treasury Outturn Report for 2015/16 be noted.

10. STRATEGIC RISK REGISTER - QUARTER ONE

The Chief Auditor submitted a schedule updating the Committee on the Q1 status of the Council's 2016/17 Strategic Risk Register, in line with the requirements of the Council's Risk Management Strategy.

Entries within the Register reflected the risks identified by the Corporate Management Team thereby strengthening their strategic perspective, management response and controls. The inclusion of risks within any level of risk register did not necessarily mean there was a problem but reflected the fact that officers were aware of potential risks and had devised strategies for the implementation of mitigating controls.

Each entry within the register was scored based on an assessment of their impact and likelihood, to provide an assessment of the residual level of risk. Plans were in place to mitigate the risks identified in the Strategic Risk Register.

Resolved: That the Q1 status of the Council's 2016/17 Strategic Risk Register be noted.

(The meeting started at 6.30pm and closed at 7.57pm).

READING BOROUGH COUNCIL
REPORT BY HEAD OF FINANCE

AT THE TIME OF DESPATCH WE HAD YET TO RECEIVE THE DRAFT ISA260 FROM THE AUDITOR - AN UPDATE WILL FOLLOW WHEN THIS BECOMES AVAILABLE. THE DRAFT ACCOUNTS ARE ON THE WEBSITE BUT MAY NEED UPDATING IF THERE ARE AGREED AUDIT ADJUSTMENTS

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	29 September 2016	AGENDA ITEM:	3
TITLE:	APPROVAL OF 2015/16 ACCOUNTS, EY AUDIT MEMORANDUM & AUDIT OPINION (ISA260)		
LEAD COUNCILLOR:	CLLR STEVENS	AREA COVERED:	CHAIR OF AUDIT & GOVERNANCE
SERVICE:	FINANCIAL	WARDS:	BOROUGHWIDE
AUTHOR:	ALAN CROSS	TEL:	2058 / 9372058
JOB TITLE:	HEAD OF FINANCE	E-MAIL:	Alan.Cross@reading.gov.uk

1. PURPOSE AND SUMMARY OF REPORT

- 1.1 In accordance with the Accounts & Audit Regulations, the Committee, on behalf of Council is required to approve the Council's accounts by the end of September.
- 1.2 As part of the annual external audit process of the Council's accounts, EY produce an Audit Memorandum (ISA260) to those charged with Corporate Governance prior to issuing their opinion.
- 1.3 EY have PROVISIONALLY indicated that subject to the approval of the accounts by the Committee, the receipt by them of a Management Representation letter, the receipt by the Committee of the Report to those Charged with Governance they will be in a position to issue an unqualified audit report on the (amended) Council's accounts, thus concluding the accounts audit process for 2015/16. This report sets out these documents, though for reasons of size the formal accounts have not been printed as part of the agenda.
- 1.4 However, EY are separately required to issue a value for money opinion, that includes factors related to financial stability. EY have indicated that this opinion will be qualified.
- 1.5 EY will be present at the meeting to deal with questions relating to their audit.

2. RECOMMENDATION

2.1 Audit & Governance Committee are requested to note:

- a) the Management Representations letter from the Head of Finance
- b) EY's (ISA 260) Report to those charged with governance

2.2 Audit & Governance Committee are requested, on behalf of Council to approve the final accounts for 2015/16, noting that in doing so EY will be in a position to issue an unqualified opinion on the accounts.

2.3 Audit & Governance Committee are requested to note the qualified VFM opinion and actions the Council has agreed to pursue arising from the audit (TO FOLLOW) on behalf of Council.

3. POLICY CONTEXT

3.1 Each year as part of the annual external audit process the Council's External Auditor produce a report addressed to those charged with governance prior to issuing their Audit Opinion. This is the first year of EY's appointment as auditor.

3.2 The Report is submitted to the Audit & Governance Committee as part of its duties on behalf of Council. Given the democratic nature of the Council it is possibly too simplistic to suggest the Committee is solely responsible for governance, and we suggest that Council as a whole as well as the Administration have some governance responsibilities too, as of course does the Corporate Management Team. To reflect this, the Annual Governance Report is signed by the Leader and Managing Director.

3.3 The general financial position was reported to the Committee at its July meeting, and the Council's draft accounts were signed off at the end of June by the Head of Finance and placed on the website. As is normal in the course of the audit we have agreed a small number of changes to the draft accounts. As part of the process, the Council's Section 151 Officer is required to submit a Management Representations letter to the External Auditor, and this is attached for the information of the Committee.

4. OPINION AND AUDIT MEMORANDUM / MANAGEMENT REPRESENTATIONS LETTER

4.1 Attached to this covering report are

- Management Representations Letter
- EY's Audit Memorandum (ISA 260) to those charged with governance (to follow)

4.2 Implementing External Audit Recommendations

EY's letter includes

4.3 {PARAGRAPH TO FOLLOW ONCE ISA 260 received}

4.4 EY Audit Differences

EY's Report sets out the more significant issues that have arisen in their audit and a small number of audit adjustments we have made to the draft accounts as a consequence of their work. The required adjustments are largely technical or presentational ones. There have been no changes to the council's available balances and resources as a consequence of EY's audit.

[possible comments to follow related to audit differences]

4.3 EY

The committee will be aware that prior to its abolition the Audit Commission decided to appoint EY as auditor for the 2015/16 & 2016/17 accounts, an appointment that has subsequently been extended by DCLG to include 2017/18.

5. FINANCIAL IMPLICATIONS

5.1 None, directly from this report.

5.2 As indicated above and in EY's report, a number of adjustments have been made to the accounts since June, but overall these have had no significant impact on the General Fund Balance.

5.3 The final accounts with the audit report will as usual be published on the Council's website.

6. LEGAL IMPLICATIONS

6.1 The process being followed is in line with the Accounts & Audit Regulations.

7. CONTRIBUTION TO STRATEGIC AIMS / COMMUNITY ENGAGEMENT /EQUALITY IMPACT ASSESSMENT

7.1 None directly from the report.

8. BACKGROUND PAPERS

8.1 None.

**READING BOROUGH COUNCIL
REPORT BY HEAD OF FINANCE**

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	29 September 2016	AGENDA ITEM:	4
TITLE:	FUTURE AUDIT ARRANGEMENTS - APPOINTMENT OF PUBLIC SECTOR AUDIT APPOINTMENTS LTD		
LEAD COUNCILLOR:	CLLR STEVENS	AREA COVERED:	CHAIR OF AUDIT & GOVERNANCE
SERVICE:	FINANCIAL	WARDS:	BOROUGHWIDE
AUTHOR:	ALAN CROSS	TEL:	2058 / 9372058
JOB TITLE:	HEAD OF FINANCE	E-MAIL:	Alan.Cross@reading.gov.uk

1. PURPOSE AND SUMMARY OF REPORT

- 1.1 Further to the report in April 2016, this report explains the latest position in relation to the requirement in the Local Audit & Accountability Act 2014 for the Council to eventually appoint its own external auditor.
- 1.2 Following the approval of Public Sector Audit Appointments Limited (PSAA) as the appointing person under the Act, this report recommends that to ensure the Council gets the best price for its independent external audit, and can minimise the work involved locally that PSAA is asked to assist the Council in finding an auditor, and authorises the Head of Finance to progress arrangements, reporting to Council in due course.

2. RECOMMENDATION

- 2.1 Audit & Governance Committee are requested to note that the Government have recently appointed Public Sector Audit Appointments Limited (PSAA) as an appointing person under the provisions of the Local Audit and Accountability Act 2014 (the 2014 Act) and the Local Audit (Appointing Person) Regulations 2015.
- 2.2 Audit & Governance Committee confirms its recommendation to ask PSAA to assist the Council in finding an Auditor for 2018/19 and beyond, and delegates to the Head of Finance authority to make arrangements to progress the process once PSAA publish the timetable.

2.3 Audit & Governance Committee note that a meeting of Council will need to confirm the audit appointment in due course.

3. POLICY CONTEXT

3.1 In April the Committee resolved that it supported in principle a proposal that we ask Public Sector Appointments Ltd to assist with the appointment of an external auditor for the 2018/19 and subsequent accounts.

4. BACKGROUND

4.1 The previous Secretary of State decided to abolish the Audit Commission and give local authorities the power to appoint their own auditor. During the passage of the legislation through parliament, the Local Government Association argued that there should be a facility for authorities to club together at a national level to make appointments.

4.2 Public Sector Audit Appointments Ltd (PSAA) was set up initially as part of the transitional arrangements associated with the Audit Commission's abilities to manage the run off of the contracts let by the Commission, but with the intention that in due course it would apply to be able to let future contracts. PSAA sits within the LGA Group, and currently works from the LGA's offices.

4.3 The Government has recently confirmed PSAA's appointment in the latter role, and PSAA wrote to chief financial officers in August as in the Appendix. Whilst the timetable is not yet certain, the appendix indicates "opt in" decisions will be invited before December. The appendix outlines the process thereafter leading to a formal appointment of an auditor for 2018/19 during the second half of calendar year 2017 (as the legal deadline to appoint is 31 December before the 1 April in the year the appointment commences)

5. FINANCIAL IMPLICATIONS

5.1 None, directly from this report, save that in principle the decision should ensure a value for money independent audit appointment in due course

6. LEGAL IMPLICATIONS

6.1 The proposal significantly simplifies the process the Council would need to undertake to appoint an auditor. Were the Council to choose to do this independently, we would need to set up an auditor panel (including an independent chair and other independent members (in the majority)), run our own procurement and follow various other tightly specified procedures.

- 6.2 By asking PSAA to do this, the only thing the Council will need to do in due course is formally confirm the appointment. That is a reserved function of Council,

- 7. CONTRIBUTION TO STRATEGIC AIMS / COMMUNITY ENGAGEMENT /EQUALITY IMPACT ASSESSMENT

- 7.1 None directly from the report.

- 8. BACKGROUND PAPERS

- 8.1 Communication from PSAA received by e-mail in Appendix
- 8.2 Local Audit & Accountability Act 2014 & Local Audit (Appointing Persons) Regulations 2015

Appendix

17 August 2016

Subject: PSAA has been specified by DCLG as the appointing person for auditor appointments at principal local government bodies

Dear Mr Cross

I am writing to you with updated information on the position on local auditor appointment requirements, following recent developments.

Local auditor appointments

Last month, the Secretary of State for Communities and Local Government confirmed that Public Sector Audit Appointments Limited (PSAA) has been specified as an appointing person under the provisions of the Local Audit and Accountability Act 2014 (the 2014 Act) and the Local Audit (Appointing Person) Regulations 2015. This means that PSAA will make auditor appointments to relevant principal local government bodies that choose to opt into the national appointment arrangements we are developing, for audits of the accounts from 2018/19.

Current auditor appointments are made under the audit contracts previously let by the Audit Commission and now managed by PSAA under transitional arrangements. These audit contracts will end with the completion of the 2017/18 audits for principal local government bodies including police and fire bodies, and the completion of the 2016/17 audits for NHS bodies.

A top priority for PSAA in developing the new scheme will be to ensure we are able to make independent auditor appointments at the best possible prices. We will also endeavour to appoint the same auditors to bodies which are involved in formal collaboration or joint working initiatives.

We are currently working on the details of the scheme, including a timetable, and will provide further information as soon as possible.

Timetable

Over the next few months all principal authorities will need to decide how their auditors will be appointed under the new requirements. They may make their auditor appointment themselves, or in conjunction with other bodies. Or principal local

government bodies can take advantage of the national collective scheme that PSAA is developing, which should pay dividends in terms of quality, cost, responsiveness and convenience.

New appointments, for the 2018/19 accounts for principal local government bodies, must be made under the provisions of the 2014 Act and confirmed by 31 December 2017.

The date by which principal local government bodies will need to opt into the appointing person arrangement is not yet finalised. The aim is to award contracts to audit firms by June 2017, giving six months to consult on appointments with authorities before the 31 December 2017 deadline. We anticipate that invitations to opt in will be issued before December 2016.

The Local Audit (Appointing Person) Regulations 2015 require that a principal authority may only make the decision to opt into the appointing person arrangement by the members of the authority meeting as a whole, except where the authority is a corporation sole, in which case the decision may be made by the holder of the office.

More information

We will provide further updates as soon as we can.

Information is available on our website on the [specified appointing person arrangements](#) and on the [transition to local auditor appointment](#) more generally. A [prospectus for the new scheme](#) is also available on the website.

If you have a specific enquiry please contact us at generalenquiries@psaa.co.uk.

Yours sincerely

Jon Hayes
Chief Officer

READING BOROUGH COUNCIL

REPORT BY (HEAD OF FINANCE)

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	29 SEPTEMBER 2016	AGENDA ITEM:	5
TITLE:	PUBLIC SECTOR INTERNAL AUDIT STANDARDS (SELF-ASSESSMENT)		
LEAD COUNCILLOR:	Councillor STEVENS	PORTFOLIO:	AUDIT & GOVERNANCE
SERVICE:	FINANCE	WARDS:	N/A
LEAD OFFICER:	PAUL HARRINGTON	TEL:	9372695
JOB TITLE:	CHIEF AUDITOR	E-MAIL:	Paul.harrington@reading.gov.uk

1. PURPOSE OF REPORT AND EXECUTIVE SUMMARY

1.1 The purpose of this report is to inform the Audit & Governance Committee the results of the self-assessment carried out by the Chief Auditor against the Public Sector Internal Audit Standards (PSIAS). The PSIAS encompass the mandatory elements of the Chartered Institute of Internal Auditors (CIIA) International Professional Practices Framework (IPPF). Areas of non or partial compliance have been identified as part of the assessment, and a Quality Assurance and Improvement Programme (QAIP) has been produced that shows how these will be addressed.

1.2 The PSIAS contain a detailed checklist of over 200 questions which has been used as the basis for the self-assessment. It is designed to assess the performance of internal audit against the following categories:

- Code of Ethics - integrity, objectivity, confidentiality and competency
- Attribute Standards
 - Purpose, authority and responsibility
 - Independence and objectivity
 - Proficiency and due professional care
 - Quality assurance and improvement programme
- Performance Standards
 - Managing the internal audit activity
 - Nature of work
 - Engagement planning
 - Performing the engagement
 - Communicating results
 - Monitoring progress
 - Communicating the acceptance of risks

- 1.3 The Chartered Institute of Public Finance Accountants (CIPFA) has developed a comprehensive checklist for assessing compliance with the PSIAS and the Local Government Application Note which the Chief Auditor has completed.
- 1.4 Attached in appendix 1 is the action plan following the self-assessment.

2. RECOMMENDED ACTION

- 2.1 The Audit & Governance Committee notes the actions required for improvement in appendix 1.
- 2.2 Chief Auditor to arrange an external assessment completed via a peer review in 2017, the results of which will be reported to the Audit and Governance Committee.

3. PUBLIC SECTOR INTERNAL AUDIT STANDARDS

- 3.1 The Public Sector Internal Audit Standards (PSIAS) came into effect on 1 April 2013. Compliance with these is a requirement of the Audit and Accounts Regulations and should underpin the Internal Audit arrangements within the Council. The Chief Auditor is expected to report on conformance with the PSIAS annually.
- 3.2 CIPFA's Local Government Application Note has been developed as the sector-specific requirements for local government organisations within the UK Public Sector Internal Audit Framework.
- 3.3 The Code of Ethics promotes an ethical, professional culture. It does not supersede or replace internal auditors own professional bodies codes of ethics or those of the employing organisation. Internal auditors must also have regard to the Committee on Standards in Public Life's Seven Principles of Public Life, namely selflessness, integrity, objectivity, accountability, openness, honesty and leadership.
- 3.4 The Standards define internal auditing as *'An independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes'*.
- 3.5 The Standards refer to a 'Chief Audit Executive' which, for Reading Borough Council, is deemed to be the Chief Auditor. The Standards also refer to a 'Board' which, for Reading Borough Council, is deemed in most cases to be the Audit and Governance Committee on behalf of the Council.

- 3.6 The Chief Auditor must report functionally to the Board. In practice this means the Audit and Governance Committee (as the Board) will be involved in:
- Approving the internal audit charter
 - Approving the risk based internal audit plan
 - Receiving communications from the Chief Auditor on the internal audit activity's performance relative to its plan and other matters
 - Making appropriate enquiries of management and the Chief Auditor to determine whether there are inappropriate scope or resource limitations
 - Approving any significant additional (internal audit) consulting services not already included in the audit plan, prior to any engagement being accepted
 - To receive feedback for the Chief Auditor's performance appraisal
- 3.7 The published PSIAS also included some examples of functional reporting to the Board which are not typically seen as the responsibility of an Audit Committee in a Local Authority and would not be done by the Audit and Governance Committee e.g.:
- Approving decisions regarding the appointment and removal of the Chief Auditor
 - Approving the remuneration of the Chief Auditor
 - Approving the Internal Audit Budget and resource plan
- 3.8 The Chief Auditor undertakes periodic reviews of the quality of internal audit work completed and also reviews all draft and final reports issued. In delivering the Internal Audit Service, the planning, conducting and reporting on reviews have been completed in conformance with the requirements of the PSIAS and our self-assessment demonstrates compliance with the standards.
- 3.9 The Head of Finance (Sec 151 Officer) and Managing Director also periodically review Internal Audit work and discuss issues as necessary with the Chief Auditor through regular one-to-one meetings.
- 3.10 The PSIAS require an external assessment to be completed once every 5 years by a qualified, independent assessor or assessment team from outside the organisation. External assessments can be in the form of a full external assessment, or a self-assessment with independent external validation. An independent assessor or assessment team means not having either a real or an apparent conflict of interest and not being a part of, or under the control of, the organisation to which the internal audit activity belongs.
- 3.11 Quotations for an external assessment provided by an external organisation (e.g. CIPFA, CMIIA, PWC etc.) range from £8k to £20k. Given the small team, we do not believe that such expense would offer value for money, especially given budget constraints. It is therefore the intention of the Chief Auditor to arrange an external assessment completed via peer review in 2017, the results of which will be reported to the Corporate Management Team (CMT) and the Audit and Governance Committee.

4. CONTRIBUTION TO STRATEGIC AIMS

- 4.1 Audit Services aims to assist in the achievement of the strategic aims of the Authority by bringing a systematic disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

5. COMMUNITY ENGAGEMENT AND INFORMATION

- 5.1 A professional, independent and objective internal audit service is one of the key elements of good governance, as recognised throughout the UK public sector.

6. LEGAL IMPLICATIONS

- 6.1 Legislation dictates the objectives and purpose of the internal audit service the requirement for an internal audit function is either explicit or implied in the relevant local government legislation. Section 151 of the Local Government act 1972 requires every local authority to '*make arrangements for the proper administration of its financial affairs*' and to ensure the one of the officers has responsibility for the administration of those affairs. In England, more specific requirements are detailed in the Accounts and audit Regulations, in that authorities must '*maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with proper internal audit practices*'.

7. FINANCIAL IMPLICATIONS

- 7.1 There may be a financial implication depending on the route preferred to complete an external assessment. The level of finance required will depend upon the scope and who the Audit and Governance committee agrees to perform the external assessment.

8. BACKGROUND PAPERS

- 8.1 Regulation 4 of the Accounts and Audit Regulations 2011
Public Sector Internal Audit Standards - applying the Institute of Internal Auditors International Standards to the UK Public Sector
Local Government application Note

Summary of Compliance against the
Public Sector Internal Audit Standards

Section	Standard	Compliant				Total
		Yes	Partial	No	N/A	
1	Definition of Internal Auditing	3				3
2	Code of Ethics	13				13
3	Attribute Standards					
3.1	Purpose, Authority and Responsibility	19	2	2		23
3.2	Independence and Objectivity	30	2		4	36
3.3	Proficiency and Due Professional Care	19	2			21
3.4	Quality Assurance and Improvement Programme	22			8	30
4	Performance Standards					
4.1	Managing the Internal Audit Activity	44	2		1	47
4.2	Nature of Work	27	2			29
4.3	Engagement Planning	58			1	59
4.4	Performing the Engagement	21	2			23
4.5	Communicating Results	50	1		4	55
4.6	Monitoring Progress	4				4
4.7	Communicating the Acceptance of Risks	2				2
Total		310	12	2	18	342

**Public Sector Internal Auditing Standards
Action Plan - Partial Compliance**

Standard	Comment	Action	Responsible Officer
3.1 Purpose, Authority and Responsibility			
Does the internal audit charter define the nature of assurance services provided to the organisation, as well as assurances provided to parties external to the organisation?	The internal audit charter defines the nature of assurances services provided to RBC, but needs to reflect the work undertaken for BFC.	The Internal Audit Charter will be refreshed to reflect these requirements and brought to CMT and the Audit & Governance Committee for sign off.	Chief Auditor
Does the chief audit executive (CAE) periodically review the internal audit charter and present it to senior management and the board for approval?	Reviewed and updated in 2009 and 2013. Needs to be refreshed.	The Internal Audit Charter will be refreshed to reflect these requirements and brought to CMT and the Audit & Governance Committee for sign off.	Chief Auditor
3.2 Independence and Objectivity			
Is feedback sought from the chair of the audit committee for the CAE's performance appraisal?	Scrutiny and feedback is received at quarterly meetings of the A&G on the service provision of the internal audit service.	The Chair of the Audit Committee will be requested for feedback/observations to feed into the appraisal process.	Head of Finance
If there have been any assurance engagements in areas over which the CAE also has operational responsibility, have these engagements been overseen by someone outside of the internal audit activity?	The Chief Auditor has line management responsibility for Insurance.	Future audits in this area will be overseen by someone outside of internal audit (head of finance) or will be undertaken by a neighbouring authority.	Head of Finance

Standard	Comment	Action	Responsible Officer
3.3 Proficiency and Due Professional Care			
Do internal auditors have sufficient knowledge of the appropriate computer-assisted audit techniques that are available to them to perform their work, including data analysis techniques?	All auditors have access to Excel and associated corporate training programs. Internal Auditors also use a data analysis tool (IDEA) to extract and test data.	The IT Auditor must provide Auditors with in-house training on the new version of IDEA and the applications for continuous auditing.	ICT Auditor
Do internal auditors undertake a programme of continuing professional development?	This is a requirement but in recent times CPD has been very limited due to lack of funds. Cheap options have been attended. Reading journals count towards CPD access to webinars etc.	Undertake ICT needs assessment to establish whether Auditors have sufficient knowledge of IT related risks and controls.	Chief Auditor
4.1 Managing the Internal Audit Activity			
Has the CAE carried out an assurance mapping exercise as part of identifying and determining the approach to using other sources of assurance?	Assurances are obtained from the Council's External Auditor, Ofsted and other inspection agencies, including peer reviews.	The Chief Auditor to carry out an assurance mapping exercise as part of identifying and determining the approach to using other sources of assurance	Principal Auditor
Are the policies and procedures regularly reviewed and updated to reflect changes in working practices and standards?	Health & Safety and office procedures are up to date (2015). Audit Carter needs refreshing in addition to the anti-fraud and corruption strategy. The audit manual was last refreshed in 2013.	Anti-Fraud & Corruption strategy and Audit manual to be refreshed to reflect changes in working practices.	Senior Auditor

Standard	Comment	Action	Responsible Officer
4.2 Nature of Work			
Has the internal audit activity evaluated the design, implementation and effectiveness of the organisation's ethics-related objectives, programmes and activities?	Individual audit assignments are linked to council values. Consistency and compliance to standards are considered during audit reviews Specific reviews have been conducted in the past on whistleblowing, code of conduct, gifts & hospitality etc.	The Chief Auditor to consider the value and proportionality of the amount of work required to assess the following assignments in future audit plans: <ul style="list-style-type: none"> • Organisation performance monitoring and accountability • Ethics related programmes and activities 	Chief Auditor
Has the internal audit activity evaluated the potential for fraud and also how the organisation itself manages fraud risk?	Auditors have consideration of fraud when performing assignments (requirement in audit manual). Anti-Fraud and Corruption Policy (2002) Policy needs reviewing to take account of any changes from the Fraud Act 2006	Refresh the Anti-Fraud and Corruption Policy to take account of any changes from the Fraud Act 2006	Principal Auditor
4.4 Performing the engagement			
Has the CAE developed and implemented retention requirements for all types of engagement records?	Document retention policy written 2013. Audit reports and working papers are retained for 3 years, plus current year. Since we've moved from audit management software to electronic files in folders, Document retention needs to be checked and old files deleted.	A review of electronic records will be undertaken to ensure compliance with the services document retention policies.	Principal Auditor
Are the retention requirements for engagement records consistent with the organisation's own guidelines as well as any relevant regulatory or other requirements?	Document retention policy written 2013. Audit reports and working papers are retained for 3 years, plus current year. Since we've moved from audit management software to electronic files in folders, Document retention needs to be checked and old files deleted.	A review of electronic records will be undertaken to ensure compliance with the services document retention policies.	Principal Auditor

Standard	Comment	Action	Responsible Officer
4.5 Communicating Results			
Do internal auditors report that engagements are 'conducted in conformance with the PSIAS' only if the results of the QAIP support such a statement?	The annual assurance report makes this declaration, but	Individual Audit reports to include a paragraph to declare engagements are conducted in accordance in conformance with the Public Sector Internal Audit Standards	Senior Auditor

**Public Sector Internal Auditing Standards
Action Plan - No Compliance**

Standard	Comment	Action	Responsible Officer
3.1 Purpose, Authority and Responsibility			
Does the internal audit charter also: k) Define the role of internal audit in any fraud-related work? l) Set out the existing arrangements within the organisation's anti-fraud and anti-corruption policies, to be notified of all suspected or detected fraud, corruption or impropriety?	Internal audits role in fraud-related work is explicit in the Council's Financial Procedural Rules The Council's anti-fraud & corruption policy and Financial Procedural Rules require the Chief Auditor to be informed of suspected fraud and irregularities	The Internal Audit Charter will be refreshed to reflect these requirements and brought to CMT and the Audit & Governance Committee for sign off.	Chief Auditor

**Public Sector Internal Auditing Standards
Action Plan - Not Applicable**

Standard	Comment	Action	Responsible Officer
3.2 Independence and Objectivity			
<p>Does the board:</p> <p>e) approve decisions relating to the appointment and removal of the CAE</p>	<p>Such actions are not constitutionally permissible to be undertaken by Audit & Governance Committee (Local Authorities (Standing Orders) (England) Regulations 2001)</p>	<p>To continue to follow existing County Council Standing Orders and procedures in the appointment and dismissal of the Chief Auditor</p>	N/A
<p>Have any instances been discovered where an internal auditor has used information obtained during the course of duties for personal gain?</p>	<p>There have been no known instances where an internal auditor has used information for personal gain</p>	N/A	N/A
<p>If there has been any real or apparent impairment of independence or objectivity, has this been disclosed to appropriate parties (depending on the nature of the impairment and the relationship between the CAE and senior management/the board as set out in the internal audit charter)?</p>	<p>There have been no known instances of real or apparent impairment of independence or objectivity.</p>	N/A	N/A
<p>If there has been any real or apparent impairment of independence or objectivity relating to a proposed consulting services engagement, was this disclosed to the engagement client before the engagement was accepted?</p>	<p>There have been no known instances of real or apparent impairment of independence or objectivity.</p>	N/A	N/A

Standard	Comment	Action	Responsible Officer
3.4 Quality Assurance and Improvement Programme			
Has the CAE considered the pros and cons for the different types of external assessment (i.e. 'full' or self-assessment plus 'independent validation')?	The requirement for an external Assessment (to be undertaken every 5 years) is new. The PSIAS took effect from 1 April 2013; as such there is no requirement to have completed an external assessment until 31 March 2018.	The Chief Auditor will present a paper to CMT and the Audit & Governance Committee (Board) exploring the options, form, timing and scope of the external assessment. This will need to provide VFM and the likely scenario will be to commission a peer review.	Chief Auditor
Has the CAE discussed the proposed form of the external assessment and the qualifications and independence of the assessor or assessment team with the board?	As above	As above	Chief Auditor
Has the CAE agreed the scope of the external assessment with an appropriate sponsor, such as the chair of the audit committee, the CFO or the chief executive?	As above	As above	Chief Auditor
Has the CAE agreed the scope of the external assessment with the external assessor or assessment team?	As above	As above	Chief Auditor
<p>Has the assessor or assessment team demonstrated its competence in both areas of professional practice of internal auditing and the external assessment process?</p> <p>Competence can be determined in the following ways: a) experience gained in organisations of similar size b) complexity c) sector (ie the public sector) d) industry (ie local government), and e) technical experience.</p> <p>Note that if an assessment team is used, competence needs to be demonstrated across the team and not for each individual member.</p>	As above	As above	Chief Auditor

Standard	Comment	Action	Responsible Officer
How has the CAE used his or her professional judgement to decide whether the assessor or assessment team demonstrates sufficient competence to carry out the external assessment?	As above	As above	Chief Auditor
Does the assessor or assessment team have any real or apparent conflicts of interest with the organisation? This may include, but is not limited to, being a part of or under the control of the organisation to which the internal audit activity belongs.	As above	As above	Chief Auditor
Has the CAE reported any instances of non-conformance with the PSIAS to the board?	As above	As above	Chief Auditor
4.1 Managing the Internal audit Activity			
Where an external internal audit service provider acts as the internal audit activity, does that provider ensure that the organisation is aware that the responsibility for maintaining and effective internal audit activity remains with the organisation?	Internal audit is not provided by an external service provider.	N/A	N/A

Standard	Comment	Action	Responsible Officer
4.5 Communicating Results			
<p>Where any non-conformance with the PSIAS has impacted on a specific engagement, do the communication of the results disclose the following:</p> <p>a) The principle or rule of conduct of the Code of Ethics or Standard(s) with which full conformance was not achieved?</p> <p>b) The reason(s) for non-conformance?</p> <p>c) The impact of non-conformance on the engagement and the engagement results?</p>	Occasion has not arisen whereby non-conformance with PSIAS has impacted on an engagement.	N/A	N/A
Where a qualified or unfavourable annual internal audit opinion is given, are the reasons for that opinion stated?	Occasion has not arisen whereby a qualified or unfavourable annual internal audit opinion is given.	N/A	N/A

**READING BOROUGH COUNCIL
HEAD OF FINANCE**

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	29 September 2016	AGENDA ITEM:	6
TITLE:	AUDIT & INVESTIGATIONS QUARTERLY PROGRESS REPORT		
LEAD COUNCILLOR:	COUNCILLOR STEVENS	PORTFOLIO:	FINANCE
SERVICE:	FINANCE	WARDS:	N/A
LEAD OFFICER:	PAUL HARRINGTON	TEL:	9372695
JOB TITLE:	CHIEF AUDITOR	E-MAIL:	Paul.Harrington@reading.gov.uk

1. EXECUTIVE SUMMARY

1.1 This report provides the Audit & Governance Committee with an update on key findings emanating from Internal Audit reports issued since the last quarterly progress report in July 2016.

1.2 The report aims to:





- Provide a high level of assurance, or otherwise, on internal controls operated across the Council that have been subject to audit.
- Advise of significant issues where controls need to improve to effectively manage risks.
- Track progress on the response to audit reports and the implementation of agreed audit recommendations

2. RECOMMENDED ACTION

2.1 The Audit & Governance Committee are requested to consider the report.

3. ASSURANCE FRAMEWORK

3.1 Where appropriate each report we issue during the year is given an overall assurance opinion. The opinion stated in the audit report provides a brief objective assessment of the current and expected level of control over the subject audited. It is a statement of the audit view based on the terms of reference agreed at the start of the audit; it is not a statement of fact. The opinion should be independent of local circumstances but should draw attention to any such problems to present a rounded picture. The audit assurance opinion framework is as follows:

Substantial	 GREEN	Substantial assurance can be taken that arrangements to secure governance, risk management and internal control, within those areas under review, are suitably designed and applied effectively. Few matters require attention and are compliance or advisory in nature with low impact on residual risk exposure.
Reasonable	 YELLOW	We can give reasonable assurance that arrangements to secure governance, risk management and internal control, within those areas under review, are suitably designed and applied effectively. Some matters require management attention in control design or compliance with low to moderate impact on residual risk exposure until resolved.
Limited	 AMBER	Limited assurance can be taken that arrangements to secure governance, risk management and internal control within those areas under review, are suitably designed and applied effectively. More significant matters require management attention with moderate impact on residual risk exposure until resolved.
No assurance	 RED	There is no assurance that arrangements to secure governance, risk management and internal control, within those areas under review, are suitably designed and applied effectively. Action is required to address the whole control framework in this area with high impact on residual risk exposure until resolved.

3.2 Grading of recommendations

3.2.1 In order to assist management in using our reports, we categorise our recommendations according to their level of priority as follows:

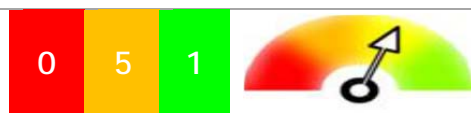
Priority	Current Risk
High	Poor key control design or widespread non-compliance with key controls. Plus a significant risk to achievement of a system objective or evidence present of material loss, error or misstatement.
Medium	Minor weakness in control design or limited non-compliance with established controls. Plus some risk to achievement of a system objective
Low	Potential to enhance system design to improve efficiency or effectiveness of controls. These are generally issues of good practice for management consideration

3.4.2 The assurance opinion is based upon the initial risk factor allocated to the subject under review and the number and type of recommendations we make.

3.4.3 It is management's responsibility to ensure that effective controls operate within their service areas. However, we undertake follow up work to provide independent assurance that agreed recommendations arising from audit reviews are implemented in a timely manner. We intend to follow up those audits where we have given limited or 'no' assurance.

4. HIGH LEVEL SUMMARY OF AUDIT FINDINGS

4.1 Accounts Payable



4.1.1 Since the introduction of Oracle Fusion there have been some significant implementation issues and in general the Council has not adjusted all of the accounts payable business processes to take full advantage of Fusion's functionality and improve financial controls and processes.

4.1.2 Currently the Accounts Payable Team has a number of manual processes, which are inefficient. Invoices are processed manually, including printing off electronic invoices received by email and supplier set up is a time consuming manual process given the volume of new suppliers set up daily on the system.

4.1.3 Supplier categorisation also needs to be improved to provide better quality management information on categories of spend and to limit the number of suppliers on the system to a manageable level.

4.1.4 Since September 2015 the Council has undertaken an improvement program with Oracle to deal with a number of outstanding implementation issues, with the introduction of a more robust Purchase to Pay (P2P). A new business process was mapped with services and then the new process was launched with a variety of training, support and communications. The correct use of the P2P process is essential for good governance and improved efficiency.

4.1.5 Enhancements of Fusion functionality together with revisions to finance and business processes are in train or are being planned.

4.2 MOSAIC Finance Payments



4.2.1 Mosaic is the Adult and Children Social care system, but also includes a substantial finance module to support the successful delivery of these services. The purpose of the review was to establish that the financial information held on Mosaic and Oracle Fusion reflects an accurate picture of the expenditure on social care.

4.2.2 The audit did not find formal written procedures for financial processes in either system (Mosaic Finance and Oracle Fusion). In particular there did not seem to be any clear guidance on Mosaic financial reporting. There is an acknowledgment that a major issue is the quality of financial data and being able to report accurately. It has also been recognised that the standard reports in Mosaic require a great deal of manual intervention.

- 4.2.3 The Mosaic finance module is used to manage the social care purchasing system (for both adults & children. It creates purchase orders and issues them to suppliers; as well as paying scheduled contracted block and other care service payments. Oracle Fusion pays the invoices in accordance with supplier requirements and shows the expenditure on designated codes, but only holds information on expenditure in arrears after services have been supplied, but does not currently show future commitment.
- 4.2.4 Financially what is in the Oracle Fusion system can be traced back to activity in Mosaic regarding expenditure and vice versa.
- 4.2.5 A review of the physical processes around the creation of invoices and set up of suppliers in Mosaic found no significant issues, however testing of the timeliness of payments highlighted a number of issues in the area of personal budgets around the processing of adjusted invoices and the time taken to process some invoices from issue date to payment. Alteration and amendments to payments were also examined and it was noted that there were a lot of adjustments after the event, but that there was an audit trail that justified these changes. The need for credit notes to adjust invoices and amendments for correct accounting for VAT payments between the systems added to the delay as both require a great deal of manual intervention to achieve satisfactory resolution. The process of identifying and correcting payments is also time consuming and means that establishing a fixed reconciliation point is problematic.
- 4.2.6 Testing of the commitment and budgeting options for personal budgets in Mosaic did not produce confidence that the figures in the system accurately represented committed expenditure as a whole and there were multiple cases where purchase orders and their commitments had not been closed or where orders or variations to orders were retrospective creating potential overpayments with regards to invoices and payment in Fusion. The records in Fusion often show considerable amendment and adjustment for expenditure coding and payment amounts which reflected the delays and difficulties in getting accurate information.
- 4.2.7 The reason for the limited number of recommendations and positive assurance opinion is due to recognition that Mosaic and Fusion interfaces require development and although inefficient, manual interventions provide the basis for reasonable financial reporting. To help drive improvements CMT have agreed that Fusion will be the main reporting resource. Data will be brought in from Mosaic to allow comprehensive management reports to be produced (allowing actuals and commitments data all in one place, and work on this has subsequently begun). Oversight for both the finance module of Mosaic and Fusion sits with the Finance System Team manager. An additional temporary resource has been brought in to provide day to day support to Mosaic and as part of this role will be training the Finance system team to support Mosaic (Finance) and they in turn will be producing procedural notes.

4.3 Right to Buy

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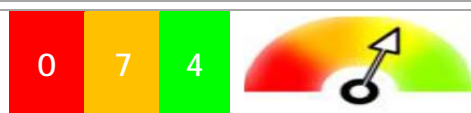
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- 4.3.1 The Government introduced increased discounts to tenants wishing to buy their home under the Right to Buy (RTB) scheme almost four years ago. The Council has experienced a large rise in applications to the scheme when the discount was first increased; however this has now slowed down due to the escalating house prices in Reading. Often significant officer time is taken up processing applications which do not complete due to tenants being unable to afford the purchase price, even after the discount has been applied.
- 4.3.2 The RTB scheme is lucrative to potential fraudsters and is considered as an area of emerging fraud risk by the CIPFA Counter Fraud Centre. With the national average value of a RTB fraud £64k per property, it lends itself to money laundering and encourages sub-letting/non-residency in order to take advantage of the scheme. If undetected it permanently deprives the Local Authority of that property for future use.
- 4.3.3 This is a recognised area for improvement, with verification processes currently under review and following our recommendations the service is putting in place additional measures to provide more rigorous checks.
- 4.3.4 In the majority of cases, the required statutory timescales are met for processing applications, with the necessary documentation sent to tenants. Property valuations are carried out in-house by an appropriately qualified individual, with the discount calculated appropriately and consistently.
- 4.3.5 Regular reconciliations are conducted to ensure the correct sale proceeds are recognised in the Council's financial system and evidence such as CHAPS¹ receipt, workflow process or record of telephone conversation are now to be retained to evidence that sale proceeds and rent checks have been conducted prior to RTB completion.

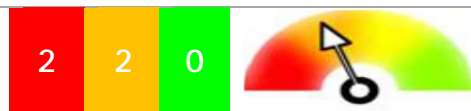
¹ Clearing House Automated Payment System

4.4 School Expansion Programme



- 4.4.1 In common with many other local authorities, Reading Borough Council is facing a significant increased demand for primary school places. In order to be able to cater for the increase in numbers, the Council has initiated a major building programme for either a new school or development and extension of a number of existing schools.
- 4.4.2 An audit review of the scheme was carried out in 2013/14 at an early stage of the building programme which noted that there were robust governance arrangements, procurement processes were generally sound and that adequate programme and financial management processes and controls existed.
- 4.4.3 The purpose of this review was principally to update the position and provide assurance that a satisfactory control framework continues to operate for the scheme(s).
- 4.4.4 The School Expansion Programme represented a major (£64 million) capital programme project for RBC and is currently forecast to be delivered to time and budget. Given the scale and scope of the programme this represents a significant achievement for those officers and parties involved. Although we made a few recommendations in respect of the existing programme, generally we found good governance and programme structure in place. A number of recommendations (lessons learnt) were made for consideration in respect of any future construction programmes.

4.5 Sec 106 Contributions



- 4.5.1 Whilst reconciling financial data at year-end, Section 106 contributions for two developments, totalling £42,000, could not be accounted for by the Council. An immediate investigation identified that a member of staff was re-directing funds into a non-RBC bank account. The officer in question had substituted the Council's official bank account details with his personal bank account details in letters sent to developers instructing them to make payment.
- 4.5.2 Running parallel to the criminal investigation (see paragraph 6.5), the Head of Planning, Development & Regulatory Services commissioned an urgent Internal Audit review of the control processes covering the receipt and accounting of Section 106 contributions. The purpose of the review was to examine the procedures associated with collecting S106 receipts, and did not examine the allocation or use of S106 contributions.

- 4.5.3 The audit highlighted inherent weaknesses in the administration of the billing and collection of developer S106 contributions. There was a lack of clarity over the extent of supervision of the monitoring officer, with limited checks being undertaken on transactions. Letters (word documents) were being used to request contributions from developers, which were not being verified/checked or approved by a senior officer. This was further compounded by the absence of independent checks/reconciliations to periodically verify the receipt of contributions against what was expected. There was insufficient segregation of duties.
- 4.5.4 Although existing documented procedures cover the start-to-end process, procedures did not provide sufficient operational detail specifically on roles and tasks covering the income collection and receipting process. This enabled tasks being assigned to the one individual without sufficient monitoring and managerial supervision, or separation of duties.
- 4.5.5 Amended procedures detailing operational steps and standards, control requirements and workflow processes are now being prepared for discussion with internal audit and the Head of Finance. Once agreed, these procedures will be issued to staff along with appropriate training provided and staff will be required to sign to confirm they have received and understood the new procedures.
- 4.5.6 The service has recently experienced a wholesale change in the key personnel as part of broader resource issues and more recently a restructure of the Planning Service has taken place. Whilst it is acknowledged that structures and roles can change, it is important that roles and responsibilities remain clear and where possible a separation of duties exist. It is recognised that job descriptions and procedures need to clearly specify supervisory responsibilities and how this relates to the administration or monitoring of S106 monies. The Head of Service has since confirmed that roles will be made clearer and that job descriptions for staff directly involved in undertaking or supervising work on S106 are being re-written to include reference to carrying out duties in accordance with procedures. At the time of writing the Head of Planning, Development and Regulatory Service is consulting staff on a number of organisational changes including the introduction of a new S106/Community Infrastructure Levy (CIL) officer role and changes to the administrative officers' role to include relevant S106 /CIL tasks.
- 4.5.7 Consideration is being given to either exploring the use of the Council's Corporate Debtors system (which is managed separately from the Planning Service) or acquiring a comparative system which enforces greater separation of duties between the initiation and actual recovery of contributions and to provide an audit trail of income due and received.

5. AUDIT REVIEWS 2016/2017

5.1 The table below details those audit reviews in progress and the reviews planned for the next quarter. Any amendments to the plan to reflect new and emerging issues or changes in timing have been highlighted.

Audit Title	Timing	Start Date	Draft Report	Final Report
MOSAIC (Finance Payments)	Q1	Mar 16	July 16	Aug 16
Creditors (Accounts Payable)	Q1	Dec 15	Apr 16	Aug 16
Nursing & Residential Care Packages	Q1	Mar 16	June 16	
School Places Capital programme	Q1	Mar 16	May 16	Aug 16
Right to Buy	Q1	Apr-16	Jun 16	Aug 16
Leisure (Income Collection)	Q1	Apr 16	Jun 16	Jun 16
MOSAIC/Oracle Fusion End of year reconciliation	Q1	May 16	Aug 16	
Overtime	Q1	Jun 16		
Health & Safety Review	Q1	May 16	Sep 16	
Information Governance & Data Protection	Q1	Jun 16	Sep 16	
Electronic Document and Records Management	Q1	Apr 16	May 16	Jun 16
Troubled Families (Grant Sign Off)	Q2	Sep 16	-	
Pinch Point (Grant Certification)	Q2	-	-	
LTP Capital Settlement (Grant Certification)	Q2	-	-	
Integrated Discharge Scheme	Q2	Aug 16		
Access to Records	Q2	May-16		
MASH (Multi-Agency Safeguarding Hub)	Q2			
Use of cash vouchers & cash accounts	Q2	Jun-16	Sep 16	
Sec 106 contributions*	Q2	Jun 16	Aug 16	Sep 16
RBC childcare settings*	Q2	Sep 16		
Pupil Premium Funding	Q3	Aug 16		
Caversham Nursery School	Q3	Oct 16		
Cranbury College	Q3	Nov 16		
Manor Primary School	Q3	Oct 16		
Corporate Buildings H&S	Q3			
Housing & Communal areas Buildings H&S	Q3			
Bed and Breakfast Placements	Q3			
Key financial system reconciliations	Q3			
Financial Assessments of Adult Care (follow up)	Q3			
Extra Care Housing	Q3			

Audit Title	Timing	Start Date	Draft Report	Final Report
eTendering	Q4			
Mosaic (Data Quality)	Q3			
Looked After Children	Q3			
Troubled Families (Grant Sign Off)	Q3	-	-	
Early Years	Q4			
Reading Girls School (Follow up)	Q4			
Micklands Primary School	Q4	Nov 16		
Moorlands Primary School	Q4	Jan 17		
The Hill Primary School	Q4			
The Ridgeway Primary School	Q4			
Corporate Governance Overview	Q4	-	-	
Foster Care & Adoption Allowances (follow up)	Q4			
General Ledger	Q4	-	-	
Creditors (Accounts Payable)	Q4	-	-	

*Audits added in-year following specific request

6. INVESTIGATIONS (April 2015 - March 2016)

6.1 Benefit Investigations

- 6.1.1 Whilst the Council no longer investigates Housing Benefit fraud one case has been referred back to investigations team by the DWP, the total overpaid benefit for this case was £13,600.
- 6.1.2 The investigation officers are also now looking at referrals from Council Tax in relation to possible criminal offences under the Council Tax Support regulations. Investigations receive on average 22 referrals per week from the service and at present have 25 ongoing investigations.
- 6.1.3 The Council Tax Support overpayment figure as at Aug 2016 is £16,121, which includes one prosecution. In this period 9 claimants investigated have been subject to Administration Penalties², with the total fines imposed amounting to £6,407.

² We offer an administrative penalty in circumstances where it is felt that it would be more suitable to dispose of the matter without criminal proceedings being initiated.

6.2 Fraud & Error Reduction Incentive Scheme

- 6.2.1 Investigation officers are working very closely with Housing Benefit teams on the Fraud & Error Reduction Incentive Scheme (FERIS). The scheme is a DWP initiative and provides financial incentives (approximately £6.5k per month) to local authorities who reduce fraud and error in their Housing Benefit cases. A schedule of planned visits (40 per month) on current Housing Benefit claimants are undertaken to ensure claimant details held are accurate and up-to-date.
- 6.2.2 Investigation officers will look at any referrals coming from this work where the unreported change affects the rate of Council Tax support awarded.

6.3 Housing Tenancy

- 6.3.1 Since 1 April 2016 Investigation officers have investigated 21 cases of housing tenancy fraud and have assisted in the return to stock of 3 Council properties.
- 6.3.2 It is difficult to quantify the financial implications of these types of investigations, however the RBC agreed figure of £15,000 is considered to be the average cost for retaining a family in temporary accommodation. Using this figure (3x £15,000) in the region of £45,000 could have been saved as a result of tenancy investigations.
- 6.3.3 We are working alongside a Financial Investigator in connection to a previous Housing Tenancy fraud case in which the defendant was found guilty at trial in 2015. An application under the Proceeds of Crime Act (POCA) has progressed through initial stages and there is an application on file for hearing this year at Reading Crown Court. The application is in respect of the defendant had benefitted to the sum of £122,500. In addition to this, compensation amounts to £90,000.
- 6.3.4 However this is a very complex case, the decisions on amounts and payments (if any) we will not know until the Court has considered all arguments, but we are hoping to get a decision from the Crown Court later this year.
- 6.3.5 Investigation officers have been working with Housing to undertake a rolling programme of tenancy Audits (58 visits to date), which has led to further investigations into potential non-residency for 5 tenancies, with one property in the final stages of returning back to RBC stock.
- 6.3.6 The investigations officers also work closely with housing colleagues on succession/accession applications. Since April 2016 we've reviewed 19 such cases, with six referred back to Housing for further review.
- 6.3.7 As part of the ongoing joint work we are doing with Housing services. Since April 2016 investigation staff have assisted in the verification and checking of 586 Home choice applications. There were 6 cases in which SPD /CTRS issues were identified. These cases have resulted in a CTRS overpayment of £3,760.

6.4 Blue Badge investigations

6.4.1 In the period April 2016 through to August 2016, we have received a total of 8 case referrals, 2 Blue Badges have been seized and removed from circulation.

6.5 Sec 106 Fraud

6.5.1 As detailed in section 4.5 officers undertook an investigation into missing sec 106 contributions. Enquiries and subsequent evidence identified that a member of the Planning Team was re-directing funds into a bank account which was not managed by RBC. The officer in question had substituted the Council's official bank account details with his personal bank account details in letters sent to developers instructing them to make payment.

6.5.2 Section 106 contributions for two developments, totalling £42,000, were fraudulently diverted into his personal bank account.

6.5.3 From our examination of records relating to S106 contributions due, two further cases, were identified where the S106 Monitoring Officer had attempted to get the developer(s) to pay outstanding S106 contributions directly into his account. Neither was successful as they were inadvertently thwarted by staff.

6.5.4 The investigation also revealed that the officer wrote to customers who had made enquiries for section 106 searches offering to carry out the service for a fee of £50; however it was unclear how many customers had made this payment.

6.5.5 Following a detailed investigation the officer was arrested, charged with offences under the fraud act and later sentenced for two years.

6.5.6 The Court has agreed to an order under the Proceeds of Crime Act, which is being pursued by the Crown Prosecution Service.

7. CONTRIBUTION TO STRATEGIC AIMS

- 7.1 Audit Services aims to assist in the achievement of the strategic aims of the authority by bringing a systematic disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes contributing to the strategic aim of remaining financially sustainable.

8. COMMUNITY ENGAGEMENT AND INFORMATION

- 8.1 N/A

9. LEGAL IMPLICATIONS

- 9.1 Legislation dictates the objectives and purpose of the Internal Audit service the requirement for an internal audit function is either explicit or implied in the relevant local government legislation.

- 9.2 Section 151 of the Local Government act 1972 requires every local authority to “make arrangements for the proper administration of its financial affairs” and to ensure that one of the officers has responsibility for the administration of those affairs.

- 9.3 In England, more specific requirements are detailed in the Accounts and Audit Regulations, in that authorities must “maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with proper internal audit practices”.

- 9.4 The Internal Audit Service works to best practice as set out in Public Sector Internal Audit Standards Issued by the Relevant Internal Audit Standard Setters. This includes the requirement to prepare and present regular reports to the Committee on the performance of the Internal Audit service.

11. FINANCIAL IMPLICATIONS

- 11.1 N/A

12. BACKGROUND PAPERS

- 12.1 N/A

READING BOROUGH COUNCIL
REPORT BY HEAD OF FINANCE

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	29 SEPTEMBER 2016	AGENDA ITEM:	7
TITLE:	BUDGET MONITORING 2016/17		
LEAD COUNCILLOR:	COUNCILLORS	PORTFOLIO:	FINANCE
SERVICE:	LOVELOCK/ PAGE FINANCIAL	WARDS:	BOROUGHWIDE
LEAD OFFICER:	ALAN CROSS	TEL:	01189372058 (x72058)
JOB TITLE:	HEAD OF FINANCE	E-MAIL:	Alan.Cross@reading.gov.uk

1. EXECUTIVE SUMMARY

- 1.1 This report set out the budget monitoring position for the Council to the end of July 2016.

2. RECOMMENDED ACTION

- 2.1 To note that based on the position at the end of July 2016 budget monitoring forecasts an overspend of around £6.8m.

3. BUDGET MONITORING

- 3.1 The results of the Directorate budget monitoring exercises are summarised below.

	Emerging Variances £000	Remedial Action £000	Net Variation £000	% variance budget
Environment & Neighbourhood Services	1,436	(839)	597	1.9%
Childrens, Education & Early Help Services/	5,870	(189)	5,681	16.8%
Adults Care and Health Services inc. Public Health	3,781	(2,993)	725	1.8%
Corporate Support Services	0	0	0	0
Directorate Sub total	10,934	(4,021)	7,003	4.5
Treasury	(169)	0	(169)	-
Total	10,765	(4,021)	6,834	4.5

3.2 Environment & Neighbourhood Services

Despite increasing this year's budget for Bed and Breakfast costs, there is a significant risk for the budget to be exceeded based on current trend (higher numbers but lower unit cost than budgeted), even with the mitigations planned being put in place. Forecasting outturn at this stage of the year is extremely challenging as this is a demand led budget with a range of factors impacting beyond our control. Demand does not follow predictable patterns. However, projections are being recast regularly based on latest actual figures and an assessment of demand forecasts and project delivery plans. Currently there are 170 households in B&B which is 45 more than predicted in the budget A forecast overspend of £250k is reported based on this rising to around 200 households by the financial year end. This is being closely monitored as numbers fluctuate.

Services directly delivered within Economic & Cultural Development generate significant levels of income to offset operational costs and this is the key unpredictable variable in delivering to budget. At this early stage in the financial year it is impossible to accurately predict income trends, however, based on the information currently available a potential income shortfall of £310k is reported this month relating to known pressures, offset with £40k savings. Officers will be reviewing any opportunities to compensate for these pressures through alternative income streams in the coming months to mitigate these pressures.

Overall, the Directorate is reporting pressures of £597k this month, but we remain hopeful mitigating actions across the Directorate are identified and implemented to offset, including a specific review of the income pressures in Economic & Cultural Development.

3.3 Children, Education & Early Help Services

The 2016/17 budget included a net £1m addition to manage anticipated demand pressures based upon projections in October last year. Demand pressures have increased beyond that predicted month on month since then. There has been a further increase in the cost of the demand pressure on the service of £0.9m since the last report. Overall the overspend on placements and paying for children in other settings is now around £2.4m.

The new structure to ensure caseloads were manageable by staff was agreed in February for Children's Social Care and was launched in late August following consultation. This had an additional estimated unfunded cost (including agency costs associated with the change) of £1.4m which accounts for a significant element of the underlying overspend. With regard to agency and staffing, the position is currently being reviewed in detail but on the basis of a current assessment of progress it has been identified that, whilst increasing, recruitment of permanent staff is below that which was anticipated and modelled adding an additional £0.9m pressure. There remains a significant risk that this £2.3m pressure may increase further in future months due to continuing problems recruiting permanent staff and keeping social worker caseloads manageable.

In addition flowing from the recent OFSTED report the RAG rating of in year savings of £545k within children's social care has now been rated as red and the forecast overspend has been increased accordingly. The service will need to bring forward a post OFSTED Improvement Plan which will have additional costs that have yet to be agreed. The arrival of a Commissioner may also lead to a need for further costs. These improvement costs are subject to further work and discussion and are not included at this stage.

With regard to other services areas there continues to be a pressure on Education with regard to home to school transport unachieved savings of £0.5m.

Whilst the above represents the position with regard to the general fund, we are also forecasting a £3.6m pressure on the high needs block funded by the Dedicated Schools Grant that has been reported to Schools Forum, most recently in July.

3.4 Adult Care & Health Services

During the last month the forecast Directorate overspend has reduced by £323k (from £1,048k to £725k). The major change has been the successful review of the earlier predicted overspend in Public Health which has identified a package of options to allow spending to be in line with the grant, albeit with a number of risks associated with this linked to the demand led nature of some of the services.

Adults continue to experience demand pressure in excess of available budgets in both residential and community based services. There are a number of transformation and deficit reduction projects currently being run in order to ensure that the service achieves savings targets, but to achieve this there are also transformation costs that are also having to be absorbed.

A key issue to note is the current dispute with the two local CCG's around Continuing Health Care Funding. The current prediction is if cases that the Council is currently funding (that the Council believes should be CHC funded) were CHC funded, then the current predicted overspend could be reversed and a small underspend would be predicted.

3.5 Corporate Support Services

At the end of July the Directorate is currently forecasting a breakeven position after the savings proposed at Policy committee on the 19th July are taken account of. The areas of risk/concern relate to child care lawyers and the housing benefit subsidy claim.

Child care lawyers expenditure associated directly with current demand pressures in children's services have been reviewed. At this stage it appears that pressures can be managed within available budgets, however this is being carefully monitored and any change to this forecast will be reported in future months.

The remaining area of concern is the housing benefit subsidy claim where there is still a risk that this may result in a pressure in the current year. Due to this the Directorate is currently reviewing mitigating actions.

4. TREASURY MANAGEMENT

- 4.1 The review of the capital financing budget has identified a potential under spend of £169k. In terms of treasury activity, we have arranged up to £60m of temporary borrowing during the year (with £120m borrowed from various other local authorities (or similar) for various periods to manage the cash flow), and this should ensure we have enough cash available until at least the autumn. The impact of this has been to reduce the average interest rate we are paying from 3.6% to around 3.4%. The forecast incorporates our latest estimates of the capital programme and it's financing for the year.

5. SUMMARY GENERAL FUND POSITION

- 5.1 The General Fund Balance at the end of 2015/16 was £5.6m. As indicated in the table above, assuming remedial action highlighted is carried out, there is now expected to be a net overspend on service revenue budgets of £7.0m.
- 5.2 The pressure on service directorate budgets is very slightly offset by a favourable treasury position (see para 4.1), so there is an overall £6.8m over spend forecast.
- 5.3 The Council's Financial Position Report explains that £18.6m further savings will be brought forward during the autumn. Some of these savings measures will have a part year impact in this financial year to reduce the current overspend. However, the impact of this cannot be confidently estimated now.

6. CAPITAL PROGRAMME 2016/17

To the end of July, £10m of the programme had been spent. The total programme is now £97m of which £78m supports the General Fund. Capital spending is normally weighted to the latter part of the year, though with the need to complete significant parts of the school building programme by September we are expecting a greater proportion earlier in the year.

7. HRA

- 7.1 Operational budgets (for repairs and management costs) at this stage in the year appear to be broadly on track and no significant variances have been identified.
- 7.2 An initial review of the likely HRA capital financing position for 2016/17 has identified those costs should be around £250k under spent, and an initial consideration of the prospect for rent income, suggests that actual income should be at least £100k better than budget, amongst other reasons because of continuing good control of rent arrears.

8. RISK ASSESSMENT

- 8.1 There remain considerable risks associated with delivering the Council's budget and this was subject to an overall budget risk assessment. At the current time those risks are being reviewed as part of budget monitoring and can be classed as follows:

- Demand for children’s social care;
- High use of agency staffing;
- Pressures on pay costs in some areas to recruit staff or maintain services;
- In year reductions in grant;
- Demand for adult social care;
- On-going work with Health to determine shares of funding for vulnerable people
- As indicated above the risk of a need for additional costs from the OFSTED Improvement Plan and the Children’s Services Commissioner
- Increased requirement for childcare solicitors linked to activity on the above;
- Homelessness, and the risk of a need for additional bed & breakfast accommodation;
- Demand for special education needs services;
- Housing Benefit Subsidy does not fully meet the cost of benefit paid

9. BUDGET SAVINGS RAG STATUS

9.1 The RAG status of savings and income generation proposals included in the 2016/17 budget are subject to a monthly review. The RAG status in terms of progress is summarised below:

	£000	%
Red	2,175	18
Amber	7,184	59
Green	2,772	23
Total	<u>12,131</u>	<u>100</u>

9.2 The RAG status of budget savings supplements the analysis in budget monitoring above, and the red risks do not represent additional pressures to those shown above.

10. COUNCIL TAX & BUSINESS RATE INCOME

10.1 We have set targets for tax collection, and the end of July 2016 position is:

Council Tax	2016/17 £000	Previous Year’s Arrears £000	Total £000
Target	32,770	1,117	33,887
Actual	32,874	807	33,861
Variance	104 above	310 below	26 below

10.2 For 2016/17 as a whole the minimum target for Council Tax is 96.5%, (2015/16 collection rate 96.8%). At the end of May 2016, collection for the year was 37.86% compared to a target of 38.18%, and collection is slightly behind 2015/16 (38.16% by end of July 2015).

10.3 Business Rates Income to the end of July 2016

	2016/17	2016/17

Business Rates	£000	%
Target	42,006	36.1
Actual	40,644	34.93
Variance	1,362 below	1.17% below

The target for 2016/17 as a whole is 98.50%. By comparison, at the end of May 2015, 35.58% of rates had been collected.

11. OUTSTANDING GENERAL DEBTS

11.1 The Council's outstanding debt total as at 31 July 2016 stands at £4.717m in comparison to the 31st March figure of £3.861m. This shows an increase of £0.856m, but this includes large amounts due from other public sector bodies and we note that £2.652m of the balance as at 31 July 2016 is greater than 151 days old.

12. CONTRIBUTION TO STRATEGIC AIMS

12.1 The delivery of the Council's actual within budget overall is essential to ensure the Council meets its strategic aims.

13. COMMUNITY ENGAGEMENT AND INFORMATION

13.1 None arising directly from this report.

14. LEGAL IMPLICATIONS

14.1 The Local Government Act 2003 places a duty on the Council's Section 151 Officer to advise on the robustness of the proposed budget and the adequacy of balances and reserves.

14.2 With regard to Budget Monitoring, the Act requires that the Authority must review its Budget "from time to time during the year", and also to take any action it deems necessary to deal with the situation arising from monitoring. Currently Budget Monitoring reports are submitted to Policy Committee regularly throughout the year and therefore we comply with this requirement.

15. FINANCIAL IMPLICATIONS

15.1 The main financial implications are included in the report.

16. EQUALITY IMPACT ASSESSMENT

16.1 None arising directly from the report. An Equality Impact Assessments was undertaken and published for the 2016/17 budget as a whole.

17. BACKGROUND PAPERS

17.1 Budget Working & monitoring papers, save confidential/protected items.

**READING BOROUGH COUNCIL
REPORT BY HEAD OF FINANCE**

TO:	AUDIT & GOVERNANCE COMMITTEE		
DATE:	29 SEPTEMBER 2016	AGENDA ITEM:	8
TITLE:	TREASURY MANAGEMENT 2016/17 ACTIVITY TO AUGUST		
LEAD COUNCILLOR:	CLLR STEVENS	AREA COVERED:	CHAIR OF AUDIT & GOVERNANCE
SERVICE:	FINANCIAL	WARDS:	BOROUGHWIDE
AUTHOR:	ALAN CROSS	TEL:	2058/ 9372058
JOB TITLE:	HEAD OF FINANCE	E-MAIL:	Alan.Cross@reading.gov.uk

1. EXECUTIVE SUMMARY

- 1.1 This report sets out for the Committee information about the Council's treasury activities to the end of August in 2016/17. The report is based on a template provided by Arlingclose, the Council's treasury advisor, for Q1 activity updated to cover developments in July & August. There will be a short presentation at the Committee meeting to accompany this report.

2. RECOMMENDED ACTION

- 2.1 Audit & Governance Committee is asked to note progress in implementing the 2016/17 treasury strategy.

3. Background

- 3.1 The Council's Treasury Management Strategy for 2016/17 is underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, which includes the requirement for:

- The creation and maintenance of a Treasury Management Policy Statement, which sets out the policies and objectives of the Council's treasury management activities.
- The creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives.
- The receipt by the Council of an annual strategy report for the year ahead and an annual review report of the previous year.

- The delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

3.2 Treasury management in this context is defined as:

“The management of the local Council’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.”

In addition to the annual strategy and annual review reports, the Code of Practice recommends that councillors should receive at least one interim report during the year.

Practically in Reading we meet these requirements by providing a brief update as part of each budget monitoring report, and this “mid year” report, presented at the end of September, reporting activity to the end of August. This report therefore ensures the Council meets CIPFA’s recommendations.

3.3 The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk and is intended to explain how, so far during 2015/16

- *the Council tried to minimise net borrowing costs over the medium term*
- *we ensured we had enough money available to meet our commitments*
- *we ensured reasonable security of money we have lent and invested*
- *we maintained an element of flexibility to respond to changes in interest rates*
- *we managed treasury risk overall*

The remainder of this report has been prepared based on a template provided by Arlingclose Limited, the Council’s treasury advisor.

3.4 External Context

3.4.1. As we entered 2016, there was a significant uncertainty about the outlook for global growth. The slowdown in the Chinese economy and the knock-on effects for both trading partners and commodity prices, the uncertainty over the outcome of the US presidential election (no clear candidate or party being identified as an outright winner) and the impending referendum on the UK’s future relationship with the EU, all resulted in nervousness and a shaky start for financial markets.

- 3.4.2. Data released in the April-June quarter showed UK GDP at 2% year/year to March 2016 and annual inflation at 0.3% in May. Core inflation remained subdued as a consequence of weak global price pressures, past movements in sterling and restrained domestic price growth. Internationally, a modest pace of growth in the UK's main trading partners remained the most likely prospect.
- 3.4.3. Fluctuations in the opinion polls on the EU referendum prompted pronounced volatility in exchange rates, gilts, corporate bonds and equities as the result became increasingly uncertain. Immediately prior to the result, financial market sentiment shifted significantly in favour of a "Remain" outcome, a shift swiftly reversed as the actual result came in. The vote to leave the EU sent shockwaves through the domestic, European and global political spectrum, with stock markets, the pound and gilt yields all sharply lower. An immediate political impact was the resignation of Prime Minister David Cameron.
- 3.4.4. Between 23 June and 1 July the sterling exchange rate index fell by 9% and short-term volatility of sterling against the dollar increased significantly. Worldwide, markets reacted very negatively with a big initial fall in equity prices. Government bond yields also fell sharply by 20-30 bp across all maturities (i.e. prices rose) as investors sought safe haven from riskier assets. The 10-year benchmark gilt yield fell from 1.37% to 0.86%.
- 3.4.5. Yet, a week on from the result the overall market reaction, although significant, was less severe than some had feared. The 5-year CDS for the UK (the cost of insuring against a sovereign default) rose from 33.5 basis points to 38.4 basis points. The FTSE All Share index, having fallen sharply by 7% from 3,481 points on 23rd June to 3,237 after the result, had subsequently recovered and risen to 3,515 by the end of the month.
- 3.4.6. The Bank of England sought to reassure markets and investors. Governor Mark Carney's speeches on 24 and 30 June in response to the referendum result stressed that the Bank was ready to support money market liquidity and raised the likelihood of a cut in policy rates 'in the summer'. The door was also left open for an increase in the Bank's asset purchase facility (QE). The Governor noted that the Bank would weigh the downside risks to growth against the upside risks to inflation from fall in the value of sterling.

3.5 Local Context

- 3.5.1. At 31/3/2016 the Council's underlying need to borrow for capital purposes as measured by the Capital Financing Requirement (CFR) was £466.5m (including £32.8m PFI related liabilities), while usable reserves and working capital (which are the underlying resources available for investment) were

£69.3m (net balance sheet value). The Council had £318.4m of borrowing and £12m of investments.

- 3.5.2. The Council's current strategy is to maintain borrowing and investments below their underlying levels, referred to as internal borrowing, subject to normally holding a minimum investment balance of £10m.
- 3.5.3. The Council has an increasing CFR over the remainder of the decade due to the capital programme, but minimal investments. Borrowing of just over to £100m is expected to be needed over the 3 year forecast period.

4 Borrowing Strategy to the end of August

- 4.1 At 31/8/2016 the Council held £354.4m of loans (a net increase of £36m on 31/3/2016). The Council expects to borrow at least £60m (net) in 2016/17. The Council may also expect some additional sums to pre-fund future years' requirements and in doing so will not exceed the authorised limit for borrowing of £410m.
- 4.3 The Council's chief objective when borrowing continues to be striking an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.
- 4.4 Affordability and the "cost of carry" remained important influences on the Council's borrowing strategy alongside the consideration that, for any borrowing undertaken ahead of need, the proceeds would have to be invested in the money markets at rates of interest significantly lower than the cost of borrowing. As short-term interest rates have remained, and are likely to remain for a significant period, lower than long-term rates, we have concluded that it is more cost effective in the short-term to borrow short-term loans rather than long term ones.
- 4.5 Temporary and short-dated loans borrowed from the markets, from other local authorities, has also remained affordable and attractive. £129m of such loans were borrowed, and a further £45m with start dates in the autumn, at an average rate of 0.41%. Maturity periods have range from 1 day to 9 months and the totals include the replacement of maturing loans.

Borrowing Activity in 2016/17

	Balance on 01/04/2016 £m	Maturing Debt £m	New Borrowing £m	Balance on 31/08/2016 £m	Notes
Short Term Borrowing ¹	14.6	93.1	129.1	50.6	
Short / Long Term Borrowing - PWLB Variable	4.8	0	0	4.8	
Long Term Borrowing - PWLB - Fixed (Market)	269.1	5.0*	0	269.1 5.0	*Barclays LOBO £5m changed to fixed term borrowing
Long Term Borrowing - Market (LOBO)	30.0	-5.0*	0	25.0	
TOTAL BORROWING	318.5	93.1	129.1	354.5	
Other Long Term Liabilities (PFI)	32.8			32.8	
TOTAL EXTERNAL DEBT	351.3	93.1	129.1	387.3	
Increase/ (Decrease) in Borrowing £m				36.0	

4.6 LOBOs: The Council holds £25m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. No LOBO options were exercised by banks, but as £20m of LOBOs have options during 2016/17, the Council acknowledges there is an element of refinancing risk even though in the current interest rate environment lenders are unlikely to exercise their options.

4.7 Barclays LOBOs: In June Barclays Bank informed the Council of its decision to cancel all the embedded options within standard LOBO loans. This effectively converts the £5m Barclays LOBO loan the Council has to fixed rate loans removing the uncertainty on both interest cost and maturity date. This waiver has been done by 'deed poll'; it is irreversible and transferable by Barclays to any new lender.

4.8 Debt Rescheduling:

The premium charge for early repayment of PWLB debt remained relatively expensive for the loans in the Council's portfolio and therefore unattractive for debt rescheduling activity. No rescheduling activity was undertaken as a consequence.

¹ Loans with maturities less than 1 year.

5 Investment Activity

- 5.1 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2016/17, to the end of August the Council's investment balances has ranged between £0 and £55.9 million, excluding the longer term CCLA Property Fund Investment (which was increased from £12m to £15m at the end of April).
- 5.2 The Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles.
- 5.3 The transposition of European Union directives into UK legislation places the burden of rescuing failing EU banks disproportionately onto unsecured local Council investors through potential bail-in of unsecured bank deposits.
- 5.4 Given the increasing risk and continued low returns from short-term unsecured bank investments, it is the Council's aim to diversify into more secure and/or higher yielding asset classes. The Council's surplus cash is currently invested in External Property Funds and money market funds.

Investment Activity in 2016/17

Investments	Balance on 01/04/2016 £m	Investments Made £m	Maturities/ Investments Sold £m	Balance on 31/08/2016 £m
Short term Investments	0	0	0	0.0
Call Accounts	1.0	Changes Daily, Sometime Weekly		6.7
Long term Investments (Pooled funds) - CCLA Property Fund	12.0	3.0	0.0	15.0
Money Market Funds	0	(net) 17.2	0	17.2
TOTAL INVESTMENTS	13.0	25.9	0	38.9
Increase/ (Decrease) in Investments £m				25.9

- 5.5 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 2016/17.

5.6 Counterparty credit quality was assessed and monitored with reference to credit ratings (the Council’s minimum long-term counterparty rating for institutions defined as having “high credit quality” is A- across rating agencies Fitch, S&P and Moody’s); credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

5.7 Credit Risk

The table below shows counterparty credit quality as measured by credit ratings and the percentage of the investment portfolio exposed to bail-in risk.

Date	Value Weighted Average - Credit Risk Score	Value Weighted Average - Credit Rating	Time Weighted Average - Credit Risk Score	Time Weighted Average - Credit Rating	Investments exposed to bail-in risk %
31/03/2016	5.67	A	5.67	A	100%
30/06/2016	4.68	A+	4.68	A+	100%

Scoring:

-Value weighted average reflects the credit quality of investments according to the size of the deposit

-Time weighted average reflects the credit quality of investments according to the maturity of the deposit

-AAA = highest credit quality = 1

-D = lowest credit quality = 26

-Aim = A- or higher credit rating, with a score of 7 or lower, to reflect current investment approach with main focus on security

5.8 Counterparty Update

Various indicators of credit risk reacted negatively to the result of the referendum on the UK’s membership of the European Union. UK bank credit default swaps saw a modest rise but bank share prices fell sharply, on average by 20%, with UK-focused banks experiencing the largest falls. Non-UK bank share prices were not immune although the fall in their share prices was less pronounced.

5.9 Fitch downgraded the UK’s sovereign rating by one notch to AA from AA+, and Standard & Poor’s downgraded its corresponding rating by two notches to AA from AAA. Fitch, S&P and Moody’s have a negative outlook on the UK. S&P took similar actions on rail company bonds guaranteed by the UK Government.

5.10 Moody’s affirmed the ratings of nine UK banks and building societies and revised the outlook to negative for those banks and building societies that it perceived to be exposed to a more challenging operating environment arising from the ‘leave’ outcome.

- 5.11 There was no immediate change to Arlingclose's credit advice on UK banks and building societies as a result of the referendum result. Our advisor believes there is a risk that the uncertainty over the UK's future trading prospects will bring forward the timing of the next UK recession. In the coming weeks and months Arlingclose will review all UK based institutions, and it is likely that, over time, will advise shortening durations on those institutions considered to be most affected.
- 5.12 Fitch upgraded the long-term rating of ING Bank from A to A+ based on Fitch's view of the bank's solid and stable financial metrics and its expectation that that the improvement in earnings will be maintained. Fitch also upgraded Svenska Handelsbanken's long-term rating from AA- to AA reflecting the agency's view that the bank's earnings and profitability will remain strong, driven by robust income generation, good cost efficiency and low loan impairments.

Cash Balances

- 5.13 The average cash balances were £29.5m during the period. The UK Bank Rate had been maintained at 0.5% since March 2009, prior to being cut to 0.25% in August and is now forecast to remain at these low levels or fall further. Short-term money market rates have remained at relatively low levels (see Table 1 in Appendix 2). New deposits were made at an average rate of 1.56%. Investments in Money Market Funds generated an average rate of 0.33%.
- 5.14 The Bank Rate may be cut further towards zero in the coming months, which will in turn lower the rates short-dated money market investments with banks and building societies. As the majority of the Council's surplus cash continues to be invested in short-dated money market instruments, it will most likely result in a fall in investment income over the year.

6 Compliance with Prudential Indicators

The Council confirms compliance with its Prudential Indicators for 2016/17, which were set in as part of the Council's Treasury Management Strategy Statement in February 2016

Treasury Management Indicators

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

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed will be:

	2016/17	2017/18	2018/19
Upper limit on fixed interest rate exposure	120%	120%	120%
Actual	105.8%		
Upper limit on variable interest rate exposure	50%	50%	50%
Actual	5.1%		

Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Instruments that mature during the financial year are classed as variable rate.

Maturity Structure of Borrowing: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Upper	Lower	Actual 31/8/16
Under 12 months	25%	0%	14.4%
12 months and within 24 months	25%	0%	0.9%
24 months and within 5 years	25%	0%	2.5%
5 years and within 10 years	25%	0%	2.5%
10 years and above	100%	40%	79.7%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Principal Sums Invested for Periods Longer than 364 days: The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end will be:

	2016/17	2017/18	2018/19
Limit on principal invested beyond year end	£20m	£20m	£15m
Actual	£0m	N/A	

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average or credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1,

AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment.

	Target Maximum	Actual
Portfolio average score	6.0	4.68

Liquidity: The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three month period, without additional borrowing.

	Target	Actual (liquid at 31/08/16)
Total cash available within 3 months	At least £10m	£23.8m

7 Outlook for the remainder of 2016/17

Following the UK's vote to leave the European Union, the economic outlook for the UK has immeasurably altered. It will to a large extent be dependent on the nature of the future relationship negotiated with the EU, particularly in relationship to trade. The negotiations crucially hinge on domestic politics which, at the end of the June quarter, which have been unsettled themselves.

The domestic outlook is uncertain, but likely to be substantially weaker in the short term than previously forecast. Arlingclose has changed its central case for the path of Bank Rate over the next three years. Arlingclose believes any currency-driven inflationary pressure will be looked through by Bank of England policymakers. The likely path for Bank Rate is downwards and the central case is 0.25%, but there is a 40% possibility of that the rate is cut to zero.

	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
Official Bank Rate													
Upside 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
Arlingclose Central Case	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
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

In addition, Arlingclose believes that the Government and the Bank of England have both the tools and the willingness to use them to prevent any immediate market-wide problems leading to bank insolvencies. The cautious approach to credit advice means that the banks currently on the Council's counterparty list have sufficient equity buffers to deal with any localised problems in the short term.

Operationally we mainly intend, given the benign outlook above to borrow short term as needed to maintain liquidity, though anticipate participating in the initial bond issue(s) of the Municipal Bond Agency.

Appendix 1

Prudential Indicators 2016/17

The Local Government Act 2003 requires the Council to have regard to CIPFA's *Prudential Code for Capital Finance in Local Authorities* (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

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

Capital Expenditure and Financing	2015/16 Actual £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m
General Fund	71.3	78.0	44.7	31.5
HRA	12.4	15.9	10.7	7.5
Total Expenditure	83.7	93.8	54.7	39.0
Capital & Other Receipts	13.6	11.1	8.3	7.6
Government Grants	27.8	21.0	16.9	4.4
S106	7.2	1.5	0.8	0.5
Borrowing	35.0	63.6	29.4	26.5
Total Financing	83.7	97.2	54.7	39.0

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

Capital Financing Requirement	31.03.16 Actual £m	31.03.17 Estimate £m	31.03.18 Estimate £m	31.03.19 Estimate £m
General Fund	273.2	323.4	342.1	358.7
HRA	193.3	193.3	191.9	188.0
Total CFR	466.5	516.7	534.0	546.7

The CFR is forecast to rise by £80m over the next three years as capital expenditure financed by debt outweighs resources put aside for debt repayment.

This has increased from previously published forecasts, as it now includes an initial assessment of the borrowing needed to finance the Council's company Himes for Reading. The estimate will need to be refined in the next few months. The forecast suggests we will need to change the authorised limit for borrowing for future years.

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

Debt	31.03.16 Actual £m	30.03.17 Estimate £m	31.03.18 Estimate £m	31.03.19 Estimate £m
Borrowing (already done)	318.4	330.4	291.2	286.4
Future Estimated Borrowing	9.5	32.4	97.5	113.2
PFI liabilities	32.8	32.2	31.3	30.4
Total Debt	360.7	395.0	420.0	430.0

Total debt is expected to remain below the CFR during the forecast period. Actual debt levels are monitored against the Operational Boundary and Authorised Limit for External Debt, below.

Operational Boundary for External Debt: The Operational Boundary is based on the Council's estimate of most likely, i.e. prudent, but not worst case scenario for external debt.

Operational Boundary	2016/17 £m	2017/18 £m	2018/19 £m
Borrowing	400	400	400
Other long-term liabilities	40	40	40
Total Debt	440	440	440

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

Authorised Limit	2016/17 £m	2017/18 £m	2018/19 £m
Borrowing	400	400	400
Other long-term liabilities	40	40	40
Total Debt	440	440	440

Total debt at 31/8/2016 was £354.4m, well below the above limit.

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

Ratio of Financing Costs to Net Revenue Stream	2016/17 Estimate %	2017/18 Estimate %	2018/19 Estimate %
General Fund	7.5	10.1	12.4
HRA	25.4	26.0	26.5

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

Incremental Impact of Capital Investment Decisions	2016/17 Estimate £	2017/18 Estimate £	2018/19 Estimate £
Increase in Band D Council Tax (In year)	14.56	6.50	2.23
Increase in Band D Council Tax (On-Going)	61.17	25.88	9.36
Increase in Average Weekly Housing Rents	0.22	0.29	0.0

Money Market Data and PWLB Rates

The average, low and high rates correspond to the rates during the financial year rather than those in the tables below.

Please note that the PWLB rates below are Standard Rates. Authorities (including Reading) are eligible for the Certainty Rate can borrow at a 0.20% reduction.

Table 1: Bank Rate, Money Market Rates

Date	Bank Rate	O/N LIBID	7-day LIBID	1-month LIBID	3-month LIBID	6-month LIBID	12-month LIBID	2-yr SWAP Bid	3-yr SWAP Bid	5-yr SWAP Bid
01/4/2016	0.50	0.36	0.36	0.39	0.46	0.61	0.88	0.78	0.83	0.98
30/4/2016	0.50	0.36	0.36	0.38	0.47	0.62	0.90	0.86	0.95	1.13
31/5/2016	0.50	0.35	0.37	0.39	0.46	0.61	0.89	0.82	0.92	1.09
30/6/2016	0.50	0.35	0.36	0.39	0.43	0.55	0.80	0.49	0.49	0.60
Average	0.50	0.36	0.36	0.38	0.46	0.60	0.86	0.77	0.83	0.98
Maximum	0.50	0.36	0.37	0.39	0.47	0.62	0.90	0.88	0.99	1.20
Minimum	0.50	0.35	0.36	0.37	0.40	0.50	0.73	0.49	0.49	0.58
Spread	--	0.01	0.01	0.02	0.07	0.12	0.17	0.39	0.50	0.62

Table 2: PWLB Borrowing Rates - Fixed Rate, Maturity Loans (Standard Rate)

Change Date	Notice No	1 year	4½-5 yrs	9½-10 yrs	19½-20 yrs	29½-30 yrs	39½-40 yrs	49½-50 yrs
01/4/2016	125/16	1.33	1.82	2.51	3.24	3.33	3.19	3.15
30/4/2016	165/16	1.37	1.95	2.65	3.34	3.40	3.25	3.21
31/5/2016	205/16	1.36	1.93	2.56	3.22	3.27	3.11	3.07
30/6/2016	249/16	1.17	1.48	2.09	2.79	2.82	2.61	2.57
Low		1.09	1.41	2.05	2.76	2.79	2.59	2.56
Average		1.31	1.79	2.46	3.17	3.23	3.07	3.03
High		1.40	2.00	2.71	3.40	3.46	3.31	3.28

Table 3: PWLB Borrowing Rates - Fixed Rate, Equal Instalment of Principal (EIP) Loans (Standard Rate)

Change Date	Notice No	4½-5 yrs	9½-10 yrs	19½-20 yrs	29½-30 yrs	39½-40 yrs	49½-50 yrs
01/4/2016	125/16	1.50	1.86	2.54	2.99	3.25	3.34
30/4/2016	165/16	1.59	1.99	2.68	3.11	3.34	3.42
31/5/2016	205/16	1.58	1.97	2.58	2.99	3.23	3.30
30/6/2016	249/16	1.24	1.51	2.11	2.55	2.79	2.86
Low		1.24	1.51	2.11	2.55	2.79	2.86
Average		1.48	1.83	2.48	2.91	3.15	3.23
High		1.59	1.99	2.68	3.11	3.34	3.42

Table 4: PWLB Variable Rates

	1-M Rate	3-M Rate	6-M Rate	1-M Rate	3-M Rate	6-M Rate
	Pre-CSR	Pre-CSR	Pre-CSR	Post-CSR	Post-CSR	Post-CSR
1/4/2016	0.61	0.65	0.67	1.51	1.55	1.57
30/4/2016	0.61	0.65	0.67	1.51	1.55	1.57
31/5/2016	0.65	0.66	0.70	1.55	1.56	1.60
30/6/2016	0.64	0.62	0.62	1.54	1.52	1.52
Low	1.51	1.52	1.52	0.61	0.62	0.62
Average	1.53	1.55	1.57	0.63	0.65	0.67
High	1.55	1.56	1.60	0.65	0.66	0.70

Please note post CSR rates are standard rates