Reading Borough Council
Working better with you

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

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13 November 2017

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NOTICE OF MEETING – AUDIT AND GOVERNANCE COMMITTEE – 21 NOVEMBER 2017

A meeting of the Audit & Governance Committee will be held on Tuesday 21 November 2017 at **6.30pm** in the Council Chamber, Civic Offices, Reading. The Agenda for the meeting is set out below.

AGENDA

***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.*

At this point, the following motion will be moved by the Chairman:

"That, pursuant to Section 100A of the Local Government Act 1972 (as amended) members of the press and public be excluded during consideration of the following item on the agenda, as it is likely that there would be disclosure of exempt information as defined in the relevant Paragraphs of Part 1 of Schedule 12A (as amended) of that Act"

7. **EQUAL PAY UPDATE** To Follow

WEBCASTING NOTICE

Please note that this meeting may be filmed for live or subsequent broadcast via the Council's website. At the start of the meeting the Chair will confirm if all or part of the meeting is being filmed. You should be aware that the Council is a Data Controller under the Data Protection Act. Data collected during a webcast will be retained in accordance with the Council's published policy.

Members of the public seated in the public gallery will not ordinarily be filmed by the automated camera system. However, please be aware that by moving forward of the pillar, or in the unlikely event of a technical malfunction or other unforeseen circumstances, your image may be captured. **Therefore, by entering the meeting room, you are consenting to being filmed and to the possible use of those images and sound recordings for webcasting and/or training purposes**.

Members of the public who participate in the meeting will be filmed, unless they have given prior notice that they do not consent to this.

Please speak to a member of staff if you have any queries or concerns.

AUDIT AND GOVERNANCE COMMITTEE MINUTES – 28 SEPTEMBER 2017

Present: Councillors Stevens (Chairman), Duveen, Lovelock, McElligott, McKenna, Page, Rodda, Steele & Terry.

Also in attendance:

Kirsty Anderson	Income & Assessment Manager
Alan Cross	Head of Finance
Maria Grindley	Director and Engagement Lead, EY LLP
Paul Harrington	Chief Auditor
Anthony Kearns	Principal Auditor
Peter Lewis	Strategic Finance Director
Peter Sloman	Chief Executive
Sharon Warner	Income & Assessment Team Leader
Alan Witty	EY LLP

11. MINUTES

The Minutes of the meeting of 18 July 2017 were confirmed as a correct record and signed by the Chairman.

12. ACCOUNTS 2016/17

Peter Lewis, Strategic Finance Director, submitted a report stating that, at this stage, it had not been possible to sign off the accounts as a true and fair view of the Council's finances. This consequently meant that the Council's external auditors, EY, had been unable to issue an audit opinion.

The report set out the ongoing and intended actions by officers of the Council to improve the quality of financial processes and systems in order to deliver a true and fair view in the future. It was now intended that the 2016/17 accounts would be revised, signed off and audited either alongside the accounts for 2017/18 or before if possible. Therefore, it was now essential to address the improvements needed to the systems, processes and skills as soon as possible to maximise the chance of securing unqualified accounts for 2017/18. It was, however, acknowledged that to move from the current situation to unqualified accounts within this accounting year would be a tough challenge, but there was strong commitment within the Finance Team to achieving this outcome. The report contained a table, which briefly described the actions underway or planned to rectify the deficiencies in the 2016/17 accounts and ensure that they were not repeated in 2017/18. A further detailed action plan would be developed to identify any additional actions and/or resources required.

Resolved:

(1) **That the actions underway or planned to rectify the deficiencies in the 2016/17 accounts and ensure that they were not repeated in 2017/18, as described in the table at paragraph 3.4 of the report, be endorsed;**

(2) **That a further detailed action plan being developed to identify any additional actions and/or resources required be endorsed, and that**

the Committee be updated regularly of the progress being made to achieve the objectives set out in the plan.

13. HOUSING BENEFIT SUBSIDY

Kirsty Anderson, Income & Assessment Manager, submitted a report providing an update on the actions that had been taken by the Housing Benefits Service to mitigate error and losses as a result of the complex subsidy regime. The report also provided details of the further actions and activity carried out within the service to increase monitoring of thresholds. Further options to mitigate risk were being explored, including increasing the level of checks carried out across the Assessment Team and benchmarking with other neighbouring authorities. Currently, there was a recruitment exercise being carried out to appoint two additional Housing Benefit Officers to provide additional resource to administer the scheme. The report stated that the Local Government Association (LGA) had been contacted to encourage them to lobby the Government over the very serious concerns the Council had about the current arrangements for the Housing Benefit Subsidy scheme (and its audit). There had been no response from the LGA to the Council's correspondence as yet.

The report highlighted that the External Audit of the 2016/17 Housing Benefit Claim was in progress and had identified some error levels that could impact on the subsidy loss. Given the volume of claims being checked, it was expected that errors would be identified. The latest indication was that there would be an improvement on the previous year but due to the complex nature of the claims there could still be a significant loss to the authority. On a positive note, the Internal Audit team had reviewed the service, and had been able to validate and evidence that there had been an overall improvement in the service in both quality and training, as well as the business processes of the team.

Resolved:

(1) That the action taken by the Benefits Team to mitigate against future risks be endorsed as set out in paragraph 4.1 of the report;

(2) That the increased monitoring activities being undertaken by the Benefits Team be endorsed as reasonable actions to take in the circumstances.

14. INTERNAL AUDIT QUARTERLY PROGRESS REPORT

Paul Harrington, Chief Auditor, submitted a report providing the Committee with an update on key findings emanating from Internal Audit reports and investigations issued since the last quarterly progress report in July 2017. The report set out a summary of the audit reports in respect of Child Sexual Exploitation, Mosaic/Fusion end of year reconciliation, Housing Benefit Subsidy, Council Wide Savings - Governance, Bus Subsidy Grant, Local Transport Capital Grant 2016/17 and Pot Hole Action Fund Grant 16/17. The report also contained a table showing the audit reviews currently in progress and those planned for the next quarter.

Resolved: That the report be noted.

15. INTERNAL AUDIT EXTERNAL QUALITY ASSESSMENT (EQA)

Paul Harrington, Chief Auditor, submitted a report on the requirement for the Council's Internal Audit service to undergo an external quality assessment at least once every 5 years as part of Internal Audit's Quality Assurance Framework. The report provided the Committee with information on the result of the external quality assessment undertaken in July 2017. The assessment report produced by CIPFA, which was appended to the Chief Auditor's report, showed that the Council's Internal Audit function 'generally conforms' to the requirements of the Public Sector Internal Audit Standards and the associated Chartered Institute of Public Finance and Accountancy (CIPFA) advisory note. The Assessor concluded that: *"Reading Borough Council has a professional and well-respected internal audit service that is effective and not only follows best practice, but is itself a good example of best practice in local government internal audit"*.

The report stated that from the evidence reviewed as part of the external quality assessment, no areas of non-compliance with the standards had been identified, nor were any significant areas of partial non-compliance identified, that would affect the overall scope or operation of the internal audit activity. One minor area of partial compliance and some issues relating to the Audit and Governance committee had been identified, and some recommendations had been made to address these issues.

Resolved: That the outcome of the External Quality Assessment of the Council's Internal Audit Service be welcomed, which gave assurance that the quality and effectiveness of the Service was meeting the requirements of the Public Sector Internal Audit Standards and operating in accordance with the CIPFA Advisory Note associated with the Standards and was praised as an example of best practice in local government internal audit.

16. BUDGET MONITORING 2017/18

The Strategic Finance Director submitted a report on Budget Monitoring that had been considered by the Policy Committee at its meeting on 25 September 2017 and was presented for information. The Committee noted that, based on the position at the end of July 2017, budget monitoring forecasted an overspend of around £1.781m, and that plans to address this position, if it persisted, would be presented regularly to the Policy Committee.

Resolved: That the report be noted.

17. ANNUAL GOVERNANCE STATEMENT 2016/2017 – UPDATED ACTION PLAN

The Strategic Finance Director submitted a report on the 2016/17 Annual Governance Statement (AGS), which had attached an updated action plan. The Council was required to prepare and publish an AGS each year as an accompaniment to the authority's financial statements. The Council was responsible for ensuring that its financial management was adequate and effective and that it 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. Overall, 10 headline actions had been identified, all of which had been or were in the process of being implemented.

Resolved: That the updated Action Plan associated with the Annual Governance Statement for 2016/17 be noted.

(The meeting started at 7.00pm and closed at 8.30pm).

READING BOROUGH COUNCIL

REPORT BY DIRECTOR OF FINANCE

TO:	**AUDIT & GOVERNANCE COMMITTEE**		
DATE:	**21 NOVEMBER 2017**	**AGENDA ITEM:**	**4**
TITLE:	**Annual Governance Statement 2016/2017 - Updated Action Plan**		
LEAD COUNCILLOR:	**Councillor Lovelock**	**PORTFOLIO:**	AUDIT & GOVERNANCE
SERVICE:	**FINANCE**	**WARDS:**	N/A
	Peter Lewis	**TEL:**	0118 9373263
JOB TITLE:	**Director of Finance**	**E-MAIL:**	**Peter.lewis@reading.gov.uk**

1. EXECUTIVE SUMMARY

1.1 The Council is responsible for ensuring that financial management is adequate and effective and that there is a sound system of internal control, which facilitates the effective exercise of the Council's functions. It is also essential that there are effective arrangements for the management of risk.

1.2 The Accounts and Audit Regulations require local authorities to prepare and publish an Annual Governance Statement (AGS) each financial year, which accompanies the Authority's financial statements. This was presented to the Audit and Governance Committee in July 2017 along with an action plan to address the governance challenges identified. A further report was presented in September 2017, updating the Committee on the actions taken to that date.

1.3 This report updates the Committee on the further progress made against the action plan; the details are appended. Discussions are underway with the Chief Auditor to identify how he can, in future, offer assurance to the Committee about progress being made and when it would be appropriate to sign off the actions.

RECOMMENDATION

It is recommended that the Committee considers, and comments on, the progress being made against the action plan and also indicates any further requirement for information to assure themselves of continued improvements.

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No.	**Management Action**	**How implemented**	**Progress**	**Due date**	**Status**	**Responsible Officer**	**Monitoring Comments**
1.	Prepare and agree a robust and deliverable Medium Term Financial Strategy for the period 2017/18 to 2019/20	Development of a robust MTFS for 2017/18 to 2019/20	Revised MTFS being presented to Policy Committee on 17 July 2017, with further work on robustness and delivery planned	July 2017	Reports prepared for Committee showing balanced positions for 2017/18 and 2018/19. More work required to balance 2019/20	Director of Finance	A revised and more robust budget for 2017/18, including a MTFS to 2020, was presented to, and agreed by, the Policy Committee in July 2017. There is now in place a robust savings monitoring regime overseen by the Delivery Unit and the Corporate Programme Delivery Group. Budget monitoring is showing pressures emerging in 2017/18 that need to be mitigated. These pressures will have an impact in 2018/19 and beyond so additional work is required to prepare the refreshed 2018/19 budget and MTFS (extended to 2020/21) ready for consideration by members in early 2018. In addition a Corporate Plan for 2018-21 is being developed in parallel with the budget preparations.
2.	Prepare and deliver a robust savings monitoring programme to ensure that savings are delivered and/or adjusted according to a strong governance process	Implementation of a more robust budget and savings monitoring regime overseen by the Corporate Programme Delivery Group	Corporate Programme Delivery Group now oversees robust savings monitoring regime. Changes to the proposals are monitored and controlled.	May 2017	Implemented and now embedding	Head of Customer Services	There is a process for robust savings monitoring overseen by the Delivery Unit and the Corporate Programme Delivery Group (CPDG). This has been in place since May 2017 and has been improved each month. There is now more independent investigation into each saving by the Delivery Unit and more

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							scrutiny at CPDG and at the individual Directorate Steering groups. This has driven up the standard of scrutiny and the quality and regularity of information being supplied from directorates. There is a clear expectation that where savings cannot be delivered then mitigating actions are put forward. The recent Internal Audit review of this area was encouraging with only minor recommendations. The first 6 months review of progress on savings shows a positive trend upwards in delivery of existing savings.
3.	Put in place a robust regime for the reconciliation of control accounts on an ongoing basis	EY recommended that a centrally held list of reconciliations should be kept, so this should be implemented by creating (and keeping up to date) such a list	Most reconciliations have been done to 31 March 2017 but the list has not yet been established	List in place and status recorded of all reconciliations by 31 Aug 2017	In progress – list being started	Head of Finance (with Chief Technical Accountant)	Relevant Officers have been instructed to send reconciliations to the Finance Service each month from September 2017 onwards within 1 month of the month end. The initial systems covered by this are the Council Tax, Business Rates, Housing Rent and General Debt Income streams and Payroll Expenditure. An initial review of the reconciliations received has identified various historic reconciliation issues that the Finance Service will be working with relevant colleagues to resolve

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							or clear from the accounts and reconciliation to ensure that the overall process becomes robust and any historic imbalances have been addressed. The reconciliation processes will be reviewed and where necessary more fully documented. In addition, the same process will include the Council's VAT Control Account, some key Oracle Fusion Controls and the most significant Grant Control Accounts, as well as Banking related processes (see 8c below). The schedule will be periodically considered by Senior Finance Managers and the Officer Due Diligence Group.
4.	Ensure that Children's Services has an appropriate level of resources and that there are processes in place to monitor the resource allocated to the service and the achievement of service improvements required	Additional resources have been added to the Finance Team supporting Children's Services. This includes the appointment of the Interim Directorate Accountant from the end of November 2016, secondment of the Senior Analyst to the	DCEEH DMT have a clearer understanding of the Children's Services budgets and the implementation of the MTFS for Children's Services was completed with the full involvement of DMT. The accounts closure process has impacted the process of the introduction of further improvements. Now	June September 2017	Partly achieved, further improvements depend upon Team resourcing Started in July but	Director of Finance	New temporary Senior Accountant has now been appointed increasing the level of resources within Team. DMT now demonstrate a strong understanding and ownership of budgets within the Directorate Performance Meetings. Finance assists decision making with DMT by providing robust, accurate and timely information to assist in the process. There is improved budget monitoring and clear

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		Team from March 2017 and now access to an Interim Senior Analyst. This was to enable improved monitoring of the Children's Services budgets. As well as overall improvements to monitor budgets and improving the relationship between Children's Services and Finance. Key monitoring piece of work is LAC Modelling and the development of the MOSAIC system.	closure has been completed the improvements can gather pace again.		slower progress than anticipated		understanding of Children's Services budgets and key high risk areas, and the factors impacting on these areas. The LAC monitoring of CSE children and the activity data are now used in the budget monitoring process. Recent changes in the type of cases being dealt with have introduced another cost factor that is now being analysed for impact. The current level of LAC placements, taking account of these new factors, will be profiled to assess the impact on future years of the MTFS. A strategy has now been developed for SEND to be implemented and to reduce the pressure on the High Needs budget. Finance has improved the monitoring for schools with deficits and are implementing loan agreements.
5.	Further develop the financial culture of the Council	A revised budget management handbook will be made available and it is planned to have some training sessions	Revised handbook was published in April 2017. Training sessions are being planned for November 2017.	April 2017 November 2017	Complete In planning	Director of Finance	The budget manager training pilot took place on 18 October and was well received. Training for all budget managers then took place in week commencing 6 November; 142 budget managers were trained over the ten available

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		to launch and embed it. CMT will further scrutinise financial information and seek to lead by example in terms of the culture.	CMT already scrutinises finance and performance information, but will undertake more intense investigation to ensure that expenditure is delivered in line with the budget.	June 2017 (first monitoring for 2017/18)	Commenced		sessions. The planned restructure of the Finance Team will also prepare for a different cultural environment where there is more self-service by budget managers; consultation on the new structure commenced on 2 November 2017. Detailed scrutiny of the budget position for 2017/18 takes place monthly at CMT meetings; Directorate Steering Groups sessions now present the opportunity for more detailed scrutiny. Remedial action are required to seek to ensure that, overall, spend remains within budget.
6.	Children's Services: Meet the objectives within the Learning and Improvement plan for Children's Services following the Ofsted Inspection in June 2016	A detailed action plan has been prepared, that is overseen by an independently chaired Improvement Board (CSIB) reporting quarterly to ACE Committee	Actions are being delivered in accordance with various action plans and monitoring regimes.	Various to 31/3/18 and beyond	In progress	Director of Children's, Education & Early Help Services	Monitored monthly at CSIB. Key headlines are that of 39 actions 21 are rag rated as green i.e. making good progress; 9 are amber i.e. some delays with mitigation and 9 are red i.e. out of timescale or presenting risk. All red actions have clear plans and are being actively worked and tracked.
7.	Replacement of agency and interim staff with permanently	Staff in post on permanent appointments wherever	Recruitment Drive underway in Children's Services to attract and retain SW and	30 September 2017	In progress	Head of Legal and Democratic Services	Since the recruitment drive was launched in June 2017, there have been 28 staff recruited, with 4 due to start in November. Six of

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	employed staff	possible	management staff. In other areas, initial scoping work has been done and there would be little in the way of realisable savings.				these are people who have been working with RBC through Agencies. This shows that they are now encouraged to convert to directly employed. There have been 4 internal appointments. Of the 28, 5 are Service Managers, 9 are Team Managers and 1 is an Assistant Team Manager. Still to be recruited at the end of October are: • 3 Team Managers • 3 Assistant Team Managers • 2 Higher Specialist Social Worker • 29 Social Workers Learning & Development is a key focus with managers having individual development plans and a Talent Programme being developed. All the permanent Service Managers have recently undergone a Skills Assessment with an external partner, Learning & Workforce Development and the Service Consultant. Reflective supervision training is being delivered. These aim to develop the managers and front line staff and assist in retaining the permanent staff.

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8a.	Internal Controls: *General Ledger* – detailed action plan in response to Internal Audit findings to be completed and delivered.	Action Plan has been drafted for review setting out in detail how each recommendation will be addressed in the short and medium term	Actions contained within the action are being progressed; the highest priority recommendations are being addressed in the shortest timescale	August 2017 for high priority October 2017 for medium and low priority	Actions underway – all short term target dates met	Financial Systems Manager	Two of the three Priority 1 issues have now been fully addressed: – a daily log of interface files process is kept and reviewed; originating teams are informed of daily file values (item 1 on report) - internal audit have been provided with access to Fusion data table contents (item 3 on report) The final Priority 1 issue related to the control of journals and this has been thoroughly investigated. The principle that a different control arrangement is required has been agreed by the Head of and Director of Finance. An interim process by which all non-interface journals are viewed by a panel of senior finance staff prior to posting into the ledger is in place. Work is actively being under taken in conjunction with Oracle to implement a process of journal control and view within Fusion itself. Internal Audit is due to undertake a follow up review shortly.
8b.	Internal Controls: *Accounts Payable* – detailed action plan in response to Internal Audit findings to be	Specialist Payments Team Change Manager to be appointed.	Interim Accounts Payable Change Manager Appointed	5 June 2017	Recruitment Completed Manager in Post	Director of Finance	Postholder making a positive impact. Full Audit Response submitted to IA with all Amber then Green tasks prioritised (no red).

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	completed and delivered	Change Manager to review AP Audit Management Action Plan and complete Management Response, Response Person and Target Date Create detailed supporting implementation plan that addresses all points raised and integrates solutions with introduction of upcoming supplier portal	Documents reviewed by Change Manager and commented Summary top level run through completed with Accounts Payable team Balance of actions o/s	8 June 2017 9 June 2017 9 June 2017	Completed Known remedial actions will be factored into (currently in draft) audit milestone plan Completed	Accounts Payable Change Manager	Audit response reviewed and accepted by Internal Audit. Ongoing review to identify any further (non-audit) AP process improvements. This work has currently identified a further 8 areas for change to enhance or streamline existing processes. There is a milestone report that contains • All AP Remedial audit actions agreed upon. • The Supplier Portal implementation Project actions. • The Invoice Scanning Project Implementation actions From this report 11 Actions are now fully completed 3 Actions commenced 15 actions are in varying degrees of progress Main areas of focus at this time are the rollout of the supplier portal and the scanning automation.
8c.	Internal Controls: *Bank Reconciliation* – regular completion	A revised properly structured procedure will be	Considerable work was done to identify the weaknesses of the existing process	Process in place from July with suitable "back	Work in Progress. Work has	Head of Finance	A revised Bank Reconciliation Process has been designed, and some necessary system and processing changes ordered to

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	of timely reconciliations throughout the year	put in place to complete the bank reconciliation, with proper "walk through" possible Bank account reconciliation completed in timely way and reviewed by a senior officer on a monthly basis, within the month	(substantially by the Treasury & VAT officer, under the guidance of the then Interim Chief Accountant This has identified the need to change the	entries" for months up to July 2017	proceeded more slowly than the aspiration because officers involved have had to deal with other work, notably external audit queries		enable us to be able to regularly complete a balanced bank reconciliation. These changes will require work by our Civica System supplier and an early December date for this is planned. In the meantime we continue to successfully check daily that all receipts in the bank account are processed by the Civica (cash) system, so we know we do not have unallocated cash receipts. As RBC predominantly initiates payments through the Oracle Fusion Payments module or Payroll, we should therefore have control at transaction level. The new bank reconciliation process essentially brings these together, and allows for the "timing differences" to reconcile the Oracle Fusion bank position with the actual bank account. With regard to historic reconciliations, we are clearing known unreconciled items so that the historic unreconciled balance is removed.
8d.	Internal Controls: *Information Governance & data protection* Improve	Revised procedures, improved training and awareness	Ongoing training to staff and improved breach reporting procedures has meant that more mitigation is	Dec 17	In progress	Head of Legal & Democratic Services	Ongoing face to face Data Protection training currently being delivered to all staff. Teams who process and hold sensitive data a high priority. A need to target

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	governance structures to mitigate risk of breach of data protection legislation		in place. Work is underway to ensure that the Council is compliant with the new General Data Protection Regulation (GDPR) when it comes into force in May 2018				staff who work at offsite locations. Working with Learning and Development to further develop E-learning packages Covering Information Governance including the GDPR. The GDPR project team are working through the changes to be introduced and a data audit survey has been rolled out to all staff. The project team have started to hold monthly drop in sessions for staff to help awareness of the new regulation. A short presentation to Senior Leadership Group means they are now aware of the scale of changes introduced by the GDPR. All contracts with suppliers, contractors and providers will need varying in line with the GDPR New software (Data leakage protection), to detect inappropriate email content, is imminent Document marking software is already in place

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8e.	Internal Controls: *Subject Access Requests* Under the Data Protection Act 1998, individuals have a right to access information held about them. A consistent policy and procedure should be applied to subject access requests.	Different routes of access have been merged into a single route, which will be co-ordinated and monitored via Legal Service A new policy and procedure has been implemented and key officers are being trained by Legal Services	Training has been delivered to key service areas and teams who are likely to come in contact with SARs.	31 March 17	Complete	Head of Legal & Democratic Services	The new procedure is working well with all routes of access being co-ordinated by Legal Services. The GDPR imposes new requirements on local authorities dealing with SARs and we will need to make amendments to our processes in light of this. Internal Audit review is shortly to commence.
8f.	Internal Controls: *Electronic Document & Records Management* - Internal processes to collect and manage the transportation of paper documents for scanning must provide sufficient guarantees that documents will be safely accounted for and protect the Council from the risk of data loss	The Business Systems Support Team is progressing with the work to redesign the overall service provision including the arrangements for the secure transfer of hard copy documents	A range of process and procedure improvements have been implemented to increase in internal controls and safeguards. Choice of courier used is to be reviewed. Individual information Asset Owners will need to periodically assure themselves that arrangements for transfer of documents are appropriate for the nature of the data they include.	31 Dec 2017	In Progress	Head of Customer Services	Internal controls and process improvements in place. Royal Mail courier contract is now in place, with transition to be completed by the due date of 31 Dec 2017 Information asset owners engaged and consulted on proposed changes to processes and supplier. Internal Audit follow up review is underway.

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8g.	Internal Controls: *Accounts receivable* All services raise invoices promptly and provide sufficient details on invoices to improve collection performance	Refreshed procedures are being written up to accurately reflect the procedures we have in place for raising, monitoring and chasing of unpaid invoices. These procedures will be re-launched and shared with other service areas, to ensure the quality of information provided on invoices is improved.	We are currently working on a proposal to recommend with the validation from internal audit, a significant change to the way invoices are being raised currently. Whereby directorates/services would forward details of potential invoices to Income & Recovery for the team to then raise centrally. This could have several potential advantages for the Council and could improve the efficiency and effectiveness of income collection and recovery. This proposal is to be further investigated and presented to CMT for discussion in the near future.	31 January 2018 for the review	In progress	Head of Customer Services / Head of Finance	This project has now commenced with a series of workshops to set out the new process and determine which areas of invoicing might benefit from change. A detailed project plan is in place and options will be presented to CMT for discussion at the end of November.
8h.	Internal Controls: *Nursing & residential care packages* > Improve audit trails to provide	Alternative support options are consider and tried in some cases before requests for long	These are clearly recorded; an audit of the panel proformas and decision log will be completed to ensure compliance with the	Ongoing	Green	Director of Adult Care & Health Services	The Department has introduced a formalised short term intervention team at the social care front door to manage demand. This team focusses on providing timely interventions such as assistive

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	better evidence of placement decisions made by the Adult Funding Panel Improve procedures to ensure care packages are reviewed annually to comply with statutory review process	term placements are made, an example being the rehab beds at The Willows. There is a clear audit trail for those individuals presented at panel, out of panel decisions also have an audit trial – these decisions relate mainly to hospital discharges. Evidence for placement and justification for decision is clearly recorded. The panel has representation from commissioning who contribute to the decision making process. Reviews are recorded in MOSAIC, this generates a review date.	process annually. Review project in place to support compliance with reviews. Reports run for managers to review evidence of performance.	Ongoing	Amber		technology, equipment and rehabilitation services. This aims to prevent services users coming in to statutory services earlier than they need to including being placed too early in residential settings. The impact of this team will be closely monitored over the next quarter to understand the impact on service user numbers and budget. The Department has established a pre-funding eligibility panel process currently being introduced to maximise monitor the use of universal community options, assistive technology and Public Health commissioned services to support residents to remain at home as long as possible. The Pre Eligibility Panel also provides information of the current market availability to ensure workers are well informed to consider effective commissioning options. The Pre Eligibility Panel requires staff to complete a proforma referencing all the pre work they have completed for a case which is checked for quality and completeness prior to being formalised at Panel. and reduce reliance upon home care. A Resources Eligibility Panel meets

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		Managers run reports from MOSAIC to monitor performance and compliance.					weekly, chaired by the Head of ASC or the DASS, to provide a robust approach to decision making in relation to eligibility and applying consistency in the approach to how care and support needs are met. 132 cases were considered by the Panel from 23.8.17 to date which would have cost 35,675 per week, however after consideration of eligibility the total cost committed was 17,687, though this includes deferred cases. DMT have requested a number of priority performance indicator reports be prepared to enable maintaining of the timeliness of assessments and work throughout. A specialist Review Team has been created to support completion of Reviews and reduce reliance upon statutory services The Team considered all universal community options, or where care and support is required through home care, then support through the use of Direct Payments is enabled to so the service user has control over their care and support. We are currently establishing data

Annual Governance Statement 2016/17 Implementation Plan							
No.	**Management Action**	**How implemented**	**Progress**	**Due date**	**Status**	**Responsible Officer**	**Monitoring Comments**
							collection on spreadsheets where this cannot be captured in Mosaic. 9 reviews completed since 01.09.2017 have elicited 35K FYE. Work is underway corporately/departmentally to review the Reports required from MOISAC to monitor and Manage the throughput of work.
8i.	Internal Controls: *Corporate Governance* Improve a number of corporate governance processes, update key documents and communicate to staff on starting employment with the Council or on a regular basis during their employment	The Officers Code of Conduct will be reviewed and updated to ensure it reflects current practice and requirements Review Code of Corporate Governance Use of NetConsent to roll out key policies and procedures	Code of Conduct currently being updated (June 2017). It will be considered at CMT before going on to LJF and Personnel Committee for formal approval.	30 September 2017	Ongoing	Head of Legal and Democratic Services	A draft revised Code of Conduct has been finalised and will be put before CMT for approval before going to LJF and Personnel Committee following trade union agreement. Implementation of the new Code will be through Netconsent (software to track individual staff review to ensure compliance). In addition new Anti-Fraud and Money Laundering Policies have been drafted and approval processes are underway, ultimately ending with Policy Committee in January 2018. A revised Corporate Governance Code of Practice is yet to be drafted although it intended to be presented to the Audit and Governance Committee in April (or May) 2018.

Annual Governance Statement 2016/17 Implementation Plan							
No.	**Management Action**	**How implemented**	**Progress**	**Due date**	**Status**	**Responsible Officer**	**Monitoring Comments**
8j.	Internal Controls: *Strengthen and embed the processes for the management of risk.* Current deployment is not robust enough for risk management to be a key influence in decision making	Develop the current directorate risk registers specifying the owner of each action	Risk action plan updated for 2017/18. Directorate risk registers programmed in for quarterly discussion at DMTs. Strategic Risk Register programmed in for quarterly review at CMT. Level 4 Risk Management training, supplied by Council's insurers being scheduled for senior officers.	1st April 2017 31 Dec 2017	Complete Ongoing	Director of Finance	22 staff have been invited to Level 4 Risk Training and 19 have accepted, split between 2 courses on 30/10/17 and 15/11/17. New reformatted risk register has been agreed by CMT. The new format introduces risk appetite and aims to better inform those responsible for managing risks. A risk workshop has been arranged for 28 Nov 2017, which will be externally facilitated. Risk register in new format will be presented to CMT in early Jan and then to A&G on 27 Jan 2018. All directorate risk registers have been reviewed quarterly (Q1 & Q2), with the exception of DENS.
8k.	Internal Controls: *Compliance* An appropriate set of governance arrangements exist yet these are not followed rigorously which then allows weaknesses in internal controls	Attention will be paid to professional practice and compliance to drive up standards, as well as cultural change efforts in terms of the operation of the Council.	Through the development of the AGS and actions plans such as this one, plus an appropriate focus on discipline and good governance then improvements will be made. More formal interventions in terms of organisational development will be required in due course.	May 2017 September 2017	Developing and ongoing Requires planning	Director of Finance	AGS action plan is now in place and is being actively monitored by the Due Diligence Group. Those responsible for the actions identified above are both implementing the actions and updating the action plan. Action leads are attending the Due Diligence Group on a periodic basis. The recently implemented Directorate Steering Groups are reviewing overall performance and adherence to standards and will start to have some impact in

Annual Governance Statement 2016/17 Implementation Plan							
No.	**Management Action**	**How implemented**	**Progress**	**Due date**	**Status**	**Responsible Officer**	**Monitoring Comments**
							governance terms. Overall, the mood of the organisation is being changed through a range of interventions, including the Chief Executive staff briefings. The Chief Auditor is now considering how he might be able to offer assurance to the Director of Finance and the Audit and Governance Committee about the impact of the actions so that they can be signed off at future meetings.
9.	Develop a clear and consistent strategy or procedure for advising new and existing staff of their responsibility to declare interests and register gifts of hospitality	Designation of officers in each Directorate to hold registers. Recommunication of expectations on staff.	Each Director will be asked to nominate an individual in their area to hold the register. There will be communication and NetConsent approval to remind all staff of what to declare, why and to whom.	31 October 2017	Ongoing	Head of Legal, HR & Democratic Services	Approval given at CMT for implementation. HR to:- a) update guidance notes in line with revised Code of Conduct and CMT report – guidance notes have been incorporated into Code of Conduct b) Draft short questionnaire which confirms staff understand key conduct obligations including gifts, hospitality and interests. To take no longer than 30mins to complete and a week will be given for completion otherwise computer access will be blocked. c) There will be an e-mail to staff communicating the fact it's going to happen and why. There will be appropriate

Annual Governance Statement 2016/17 Implementation Plan							
No.	**Management Action**	**How implemented**	**Progress**	**Due date**	**Status**	**Responsible Officer**	**Monitoring Comments**
							communications with staff and arrangements to implement this via NetConsent (software that monitors staff that have engaged with the policy). The new register of interests will be monitored quarterly at DMTs and published accordingly.
10.	Align performance reporting processes to ensure CMT is fully sighted on organisational health and performance	New framework in place and embedded with regular review meetings scheduled for 2017/18	Regular meetings are in place for reporting and performance however, it is proposed to review and refresh framework during 17/18.	End July 2017	Ongoing	Head of Customer Services	New meeting arrangements were put in place from 1/8/17. This includes new directorate steering groups which involve meetings of DMT's & corporate senior management. New directors reports on performance have been put in place reporting into CMT. Meetings are in place; these focus attention on processes, systems and performance for each single directorate. Each director is held accountable for progress and performance. The Delivery Unit prepares the information in a consistent form. Proposals are being developed for the creation of a centralised performance and data function – to give insight to inform policy.

READING BOROUGH COUNCIL

REPORT BY STRATEGIC DIRECTOR OF FINANCE

TO:	**AUDIT & GOVERNANCE COMMITTEE**		
DATE:	**21 NOVEMBER 2017**	**AGENDA ITEM:**	**5**
TITLE:	**ACCOUNTS 2016/17**		
LEAD COUNCILLOR:	**Councillor Lovelock**	**PORTFOLIO:**	**LEADERSHIP**
SERVICE:	**FINANCE**	**WARDS:**	**N/A**
	Peter Lewis	**TEL:**	**0118 9373263**
JOB TITLE:	**Director of Finance**	**E-MAIL:**	**Peter.lewis@reading.gov.uk**

1. EXECUTIVE SUMMARY

1.1 The Committee was due to receive both the accounts for 2016/17 in September and a report on those accounts from the Council's external auditors, EY. As explained at that time, it was not possible to deliver either due to significant challenges experienced in the preparation of the accounts.

1.2 This report sets out the ongoing and future actions by officers of the Council to deliver the 2016/17 accounts and to improve the quality of financial processes and systems in order to deliver a true and fair view in the future.

2. RECOMMENDED ACTION

2.1 The Committee is requested to consider the current and future actions set out in this report and indicate their support for them, amended as required.

3. BACKGROUND AND PROCESS

3.1 The Committee received a report in September 2017 stating that it was not possible to present, at that time, a set of signed off and audited accounts for the financial year 2016/17. That report set out the issues that had prevented the successful completion of the accounts.

3.2 Since then, significant effort has been committed to addressing the deficiencies in the accounts and this report summarises the actions taken to date and those planned. In undertaking these actions, attention is also being paid to preparations for the completion of the 2017/18 accounts, which must be undertaken by 31 May 2018 with the audit complete by 31 July 2018.

3.2 While there remains strong commitment within the Finance Team to delivering improved accounts for audit, it is recognised that to move from the current situation to unqualified accounts within this accounting year is a tough challenge.

3.3 One of the first and arguably most important actions to be undertaken was to significantly bolster the resources dedicated to the task of improving the accounts. Other actions have also been initiated to seek to deliver the 2016/17 closedown and to improve processes in 2017/18. The table below briefly sets out the actions underway or planned at the current time.

No.	Comments and Actions	Intended Impact	Underway / Future
1	Fundamental restructure of the Finance Function, to fit with the Chief Executive's proposals for strengthening Corporate Support Services	Improve clarity of roles, capability and capacity within the Function to ensure that both financial and management accounting activity, along with technical tasks, are carried out correctly	U – in consultation phase; due to end 1 Dec.
2	Health check of the Fusion (the main financial ledger) system	Ensure that the system is working as intended, and particularly that the set-up is efficient so maximising system tasks and reducing manual tasks	U – contractor selected; in mobilisation period. Will commence after Fusion upgrade.
3	Recruitment of additional interim technical accountancy capacity	To work with interim Chief Accountant to improve the accounting processes within the wider organisation (e.g. Collection fund accounting)	U – 4 interims now in place and 1 under recruitment
4	Recruitment of permanent Chief Accountant	Seasoned professional required to drive up technical accounting standards and embed them throughout Finance and elsewhere as needed.	U – Chief Accountant commences on 2 Jan 2018. Already engaged in review of structure.

5	Implement new year-end software designed by CIPFA with EY	Implementing the system will both drive improvements in process and structure of the accounts, and it will enable easier production of the accounts in a tighter timeframe next year	U – implementation starts on 14 November.
6	Version 3 of the 2016/17 accounts presented to EY for technical review	Version 2 was reviewed by EY prior to September 2017; corrections were needed and these were done for version 3 by end September. After quality assurance by RBC interims, EY will undertake a technical review to identify any further improvements needed.	U – EY review commences w/c 13 November
7	Reconciliations - per the AGS action plan, a list of reconciliations has been prepared and a review of them is underway. New software will be introduced for bank reconciliation and 2017/18 to date will be reconciled.	Reconciliations are a fundamental part of our control framework. They have not been carried out, in full, for 2017/18 to date and once brought up to date, will be completed on a routine basis.	U
8	Journals – previous EY audit work showed that evidence underpinning journals was not adequate. Evidence is being attached to journals in the Fusion system, focusing on the EY sample initially.	Good quality evidence will be presented for EY audit to give assurance that transactions on the accounts are sound. EY have indicated that they will do some early sample checks to advise on the adequacy of evidence.	U
9	Debtors and creditors – EY were not able to draw samples due to lack of detailed breakdowns of debtor and creditor balances and impact on control account reconciliations.	It was identified during the external audit that officers had difficulty in breaking down in detail balances held in Oracle. This will require further investigatory work on source systems that feed the Oracle General ledger. Once this is completed, then EY can draw their samples and test transactions. This area is very important as it is the one with most potential to affect the outturn position.	U

10	Correct issues identified during the 16/17 audit and address these for the 17/18 financial year.	Preparation for the valuation of assets is underway for the 17/18 year end. Review of the fixed assets spreadsheet for 2017/18 is underway. We are also working with RTL to align financial years and accounting treatments if possible.	F and U
11	Implement new processes to ensure that inadequate practice identified in 2016/17 is amended for the later part of 2017/18	To improve the standard of accounting practice as a foundation for the remainder of 2017/18 and beyond	F with some U
12	Interim Directorate Accountant for DACHS secured for the remainder of the financial year	Required to improve management accounting and support to the directorate in controlling budgets in challenging circumstances	U – commenced in post on 2 October

3.5 While EY are unable to undertake formal audit work during this period, contact is being maintained with EY colleagues to seek guidance and advice where possible. Particularly, where they are able to undertake some informal review then EY are doing so in order to offer some assurance or further guidance. We are grateful for this support.

3.6 The target remains for the 2016/17 accounts to be ready for audit before the end of December and for the audit to commence in January 2018. Work to prepare for the 2017/18 closure of accounts will overlap with this action plan. The Committee will be updated on progress at each meeting.

READING BOROUGH COUNCIL
REPORT BY DIRECTOR OF FINANCE

TO:	**AUDIT & GOVERNANCE COMMITTEE**		
DATE:	**21 NOVEMBER 2017**	**AGENDA ITEM:**	**6**
TITLE:	**TREASURY MANAGEMENT 2017/18 ACTIVITY TO SEPTEMBER**		
RESPONSIBLE 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

This report sets out for the Committee information about the Council's treasury activities to the end of September in 2017/18. The report is largely based on a template provided by Arlingclose, the Council's treasury advisor, for activity in the first half of the financial year.

2. RECOMMENDED ACTION

2.1 Audit & Governance Committee is asked to note progress in implementing the 2017/18 treasury strategy, and the key issues emerging.

2.2 Audit & Governance Committee is asked to note the Council intends to opt up (to continue) to be treated as a Professional Client in MIFID 2 as set out in paragraphs 4.1-4.3 of the report.

3. Background

3.1 The Council's Treasury Management Strategy for 2017/18 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 authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

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. This report therefore ensures the Council meets CIPFA's recommendations. There were no significant breaches of Treasury Management Policies or Prudential Indicators during the half year.

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

- *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

Economic backdrop: Commodity prices fluctuated over the period to September 2017 with oil falling below $45 a barrel before inching back up to $58 a barrel. UK Consumer Price Inflation (CPI) index rose with the data print for August showing CPI at 2.9%, its highest since June 2013 as the fall in the value of sterling following the June 2016 referendum result continued to feed through into higher import prices. The new inflation measure CPIH, which includes owner occupiers' housing costs, was at 2.7%.

3.5 The unemployment rate fell to 4.3%, its lowest since May 1975, but the squeeze on consumers intensified as average earnings grew at 2.5%, below the rate of inflation. Economic activity expanded at a much slower pace as evidenced by Q1 and Q2 GDP growth of 0.2% and 0.3% respectively. With the dominant services sector accounting for 79% of GDP, the strength of consumer spending remains vital to growth, but with household savings falling and real wage growth negative, there are concerns that these will be a constraint on economic activity in the second half of calendar 2017.

3.6 The Bank of England made no change to monetary policy at its meetings in the first half of the financial year. The vote to keep Bank Rate at 0.25% narrowed to 5-3 in June highlighting that some MPC members were more concerned about rising inflation than the risks to growth. Although at September's meeting the Committee voted 7-2 in favour of keeping Bank Rate unchanged, the MPC changed their rhetoric, implying a rise in Bank Rate in "the coming months". The Council's treasury advisor Arlingclose was not convinced the UK's economic outlook justified such a move at this stage, but the Bank's interpretation of the data seems to have shifted, and the rate was increased to 0.25% in November.

3.7 In contrast, near-term global growth prospects improved. The US Federal Reserve increased its target range of official interest rates in June for the second time in 2017 by 25bps (basis points) to between 1% and 1.25% and, despite US inflation hitting a soft patch with core CPI at 1.7%, a further similar increase is expected in its December 2017 meeting. The Fed also announced confirmed that it would be starting a reversal of its vast Quantitative Easing programme and reduce the $4.2 trillion of bonds it acquired by initially cutting the amount it reinvests by $10bn a month.

3.8 Geopolitical tensions escalated in August as the US and North Korea exchanged escalating verbal threats over reports about enhancements in North Korea's missile programme. The provocation from both sides helped wipe off nearly $1 trillion from global equity markets but benefited safe-haven assets such as gold, the US dollar and the Japanese yen. Tensions remained high, with North Korea's threat to fire missiles towards the US naval base in Guam, its recent missile tests over Japan and a further testing of its latent nuclear capabilities.

3.9 Prime Minister Theresa May called an unscheduled General Election in June, to resolve uncertainty but the surprise result has led to a minority Conservative government in coalition with the Democratic Unionist Party. This clearly results in an enhanced level of political uncertainty. Although the potential for a so-called hard Brexit is diminished, lack of clarity over future trading partnerships, in particular future customs agreements with the rest of the EU block, is denting business sentiment and investment. The reaction from the markets on the UK election's outcome was fairly muted, business confidence now hinges on the progress (or not) on Brexit negotiations, the ultimate 'divorce bill' for the exit and whether new trade treaties and customs arrangements are successfully concluded to the UK's benefit.

3.10 In the face of a struggling economy and Brexit-related uncertainty, Arlingclose expects the Bank of England to take only a very measured approach to any monetary policy tightening. Any increase will be gradual and limited as the interest rate backdrop will have to provide substantial support to the UK economy through the Brexit transition; illustrated by the 0.25% increase in November.

3.11 Financial markets: Government Bond (Gilt) yields displayed significant volatility over the six-month period with the appearing change in sentiment in the Bank of England's outlook for interest rates, the push-pull from expectations of tapering of Quantitative Easing (QE) in the US and Europe and from geopolitical tensions, which also had an impact. The yield on the 5-year gilts fell to 0.35% in mid-June, but then rose to 0.80% by the end of September. The 10-year gilts similarly rose from their lows of 0.93% to 1.38% at the end of the quarter, and those on 20-year gilts from 1.62% to 1.94%.

3.12 The FTSE 100 nevertheless powered away reaching a record high of 7548 in May but dropped back to 7377 at the end of September. Money markets rates have remained low: 1-month, 3-month and 12-month LIBID rates have averaged 0.25%, 0.30% and 0.65% over the period from January to 21st September.

3.13 Credit background: UK bank credit default swaps continued their downward trend, reaching three-year lows by the end of June. Bank share prices have not moved in any particular pattern.

3.14 There were a few credit rating changes during the quarter. The significant change was the downgrade by Moody's to the UK sovereign rating in

September from Aa1 to Aa2 which resulted in subsequent downgrades to sub-sovereign entities including local authorities. Moody's downgraded Standard Chartered Bank's long-term rating to A1 from Aa3 on the expectation that the bank's profitability will be lower following management's efforts to de-risk their balance sheet. The agency also affirmed Royal Bank of Scotland's and NatWest's long-term ratings at Baa1, placed Lloyds Bank's A1 rating on review for upgrade, revised the outlook of Santander UK plc, and Nationwide and Coventry building societies from negative to stable but downgraded the long-term rating of Leeds BS from A2 to A3.

3.15 Ring-fencing, which requires the larger UK banks to separate their core retail banking activity from the rest of their business, is expected to be implemented within the next year. In May, following Arlingclose's advice, the Authority reduced the maximum duration of unsecured investments with Bank of Scotland, HSBC Bank and Lloyds Bank from 13 months to 6 months as until banks' new structures are finally determined and published, the different credit risks of the 'retail' and 'investment' banks cannot be known for certain.

3.16 The new EU regulations for Money Market Funds were finally approved and published in July and existing funds will have to be compliant by no later than 21st January 2019. The key features include Low Volatility NAV (LVNAV) Money Market Funds which will be permitted to maintain a constant dealing NAV, providing they meet strict new criteria and minimum liquidity requirements. MMFs will not be prohibited from having an external fund rating (as had been suggested in draft regulations). Arlingclose expects most of the short-term MMFs it recommends to convert to the LVNAV structure and awaits confirmation from each fund.

4. Regulatory Updates

4.1 MiFID II: Local authorities are currently treated by regulated financial services firms as professional clients who can "opt down" to be treated as retail clients instead. However, from 3rd January 2018, as a result of the second Markets in Financial Instruments Directive (MiFID II), local authorities will be treated as retail clients who can "opt up" to be professional clients, subject to meeting certain criteria. Regulated financial services firms include banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments. In order to opt up to professional, the authority must have an investment balance of at least £10 million and the person authorised to make investment decisions on behalf of the authority must have at least one year's relevant professional experience. In addition, the firm must assess that that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved. Formally, the delegation to make such decisions in Reading rests with the Chief Finance Officer (currently the Interim Director of Finance), though in practice most day to day transactional decisions are approved and signed off by the Head of Finance or another senior finance manager all of whom have many years' experience at various levels of local authority treasury activities. Whilst some of those postholders are due to change over the next year, it is expected that the relevant senior finance staff will continue to meet the criteria.

4.2 The main additional protection for retail clients is a duty on the firm to ensure that the investment is "suitable" for the client. Local authorities are not protected by the Financial Services Compensation Scheme nor are they eligible to complain to the Financial Ombudsman Service whether they are retail or professional clients. It is also likely that retail clients will face an increased cost and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice (several of which are regularly used by the Council). The Authority has not opted down to retail client status in the past as the costs (from potential loss of were considered to outweigh the benefits.

4.3 As the Council normally meets all the conditions to opt up to professional status and intends to do so in order to maintain the current MiFID status. Committee members may recall that we normally aim to operate with a minimum £10m balance but from January will increase this norm to £15m to provide some headroom above the minimum MIFID 2 limit (as potentially breaches of the limit have to be reported to the regulator.

4.4` CIPFA Consultation on Prudential and Treasury Management Codes

In February 2017 CIPFA canvassed views on the relevance, adoption and practical application of the Treasury Management and Prudential Codes and after reviewing responses launched a further technical consultation on changes to the codes in August with a September deadline for responses.

4.5 The proposed changes to the Prudential Code include the production of a new high-level Capital Strategy report to a Council meeting which will cover the basics of the capital programme and treasury management. The prudential indicators for capital expenditure and the (statutory) authorised borrowing limit would be included in this report but other (more technical) indicators may in future be delegated to another committee. There consultation proposal suggested dropping certain prudential indicators, notably those related to the Housing Revenue Account. However local indicators are recommended for ring fenced funds (including the HRA) and for group accounts. Other proposed changes include applying the principles of the Code to subsidiaries.

4.6 Proposed changes to the Treasury Management Code include the potential for non-treasury investments such as commercial investments in properties in the definition of “investments” as well as loans made or shares brought for service purposes. Another proposed change is the inclusion of financial guarantees as instruments requiring risk management and addressed within the Treasury Management Strategy (TMS). Approval of the technical detail of the TMS may be delegated to a committee rather than needing approval of Council. There are also plans to drop or alter some of the current treasury management indicators. The Head of Finance submitted a brief response largely modelled on the Arlingclose response though arguing that bearing in mind the significance of HRA borrowing in many authorities it would be more sensible to retain HRA indicators to ensure consistency of approach rather than strongly recommend local indicators.

4.7 CIPFA has indicated that it intends to publish the two revised Codes towards the end of 2017 for implementation in 2018/19, although we understand the actual publication date will now be in 2018. CIPFA plans to put transitional arrangements in place for reports that are required to be approved before the start of the 2018/19 financial year, though these have not been set out in detail yet.

4.8 Furthermore, the Department of Communities and Local Government (DCLG) and CIPFA wish to have a more rigorous framework in place for the treatment of commercial investments as soon as is practical. As this report was being finalised DCLG published a consultation paper revising its Investment Guidance and the MRP guidance. The investment guidance covers a wider range of activity including property investment and LA company investment, and some aspects of the MRP guidance appear on an initial read to have been tightened, but it is too early to advise on the impact of these proposed changed.

5. Local Context

5.1 On 31st March 2017, the Council had net borrowing of £326m arising from its historic revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in table 1 below.

Table 1: Balance Sheet Summary

	31.3.17 Actual £m
General Fund CFR	303.2
HRA CFR	190.0
Total CFR	**493.2**
Less: Other debt liabilities (mainly PFI Related)	-31.0
Borrowing CFR	**462.2**
Less: Usable reserves	-82.2
Less: Working capital	-55.9
Net borrowing	**324.1**

5.2 The Council's current strategy is to maintain borrowing and investments below their underlying levels implied by the CFR, sometimes known as "internal borrowing", in order to reduce risk and minimise interest costs. The treasury management position as at 30th September 2017 and the change over the period is show in table 2 below.

Table 2: Treasury Management Summary

	31.3.17 Balance £m	Movement £m	30.9.17 Balance £m	30.9.17 Rate %
Long-term borrowing Short-term borrowing	297.4 56.0	-3.3 +11.0	294.1 67.0	3.66% 0.39%
Total borrowing	**353.4**	**+7.7**	**361.1**	**3.05%**
Long-term investments – CCLA Property Fund Money Market Funds / Call Account	15.0 12.2	0.0 19.1	15.0 31.3	c.4.50% 0.18%
Total investments	**27.2**	**19.1**	**46.3**	**c.1.60%**
Net borrowing	**326.2**	**13.4**	**314.8**	

Overall we needed £11.4m less net borrowing at 30 September compared to the March year end. This is mainly because of the Council's general cash income within the year is front loaded, with expenditure more evenly spread, so by mid-year the need to borrow reduces. This position switches round markedly in the final quarter of the year. The increase in cash held as investments reflects the timing of borrowing.

5.3 Borrowing Strategy during the half year

At 30/9/2017 the Council held £359.15m of loans, (an increase of £5.75m on 31/3/2017), as part of its strategy for funding previous years' capital programmes. The 30th September 2017 borrowing position is show in table 3 below.

Table 3: Borrowing Position

	31.3.17 Balance £m	Movement £m	30.9.17 Balance £m	30.9.17 Weighted average rate %	30.9.17 Weighted average maturity years
Long Term					
Public Works Loan Board	267.4	(3.3)	264.1	3.60	29.7
Banks (LOBO)	25.0	0.0	25.0	4.21	*55.4
Banks (Fixed)	5.0	0.0	5.0	3.99	38.2
Short Term					
Local authorities	56.0	11.0	67.0	0.39	0.2
Total borrowing	**353.4**	**7.7**	**361.1**	**3.05**	**26.1**

*to final maturity, assuming options not called

The Council's chief objective when borrowing has been to strike 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.

5.4 Only short term borrowing has been taken (almost) exclusively from other local authorities for period of up to 9 months to benefit from short term interest rates and the treasury advisor's (and largely market) view that UK interest rates will remain at low levels for some years to come. Therefore, in furtherance of our strategic objectives, no new long term borrowing (over one year) was undertaken, whilst existing loans were allowed to mature without replacement. This strategy has enabled the Council to keep net capital financing costs (including allowing for foregone investment income) about £250k below budget (as reported in Budget Monitoring) and reduce overall treasury risk.

5.5 The "cost of carry" analysis performed by the Council's treasury management advisor Arlingclose did not provide a compelling case for there being value in borrowing in advance for future years' planned expenditure and therefore none was taken.

5.6 The Council continues to hold £25m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as 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 banks exercised their option during the first half of 2017/18. The Director and Head of Finance are considering (with Arlingclose's help) the possibility that £10m of these loans might be restructured next year, if a solution can be identified that would produce a budget saving without materially increasing treasury risk

5.7 Leasing & PFI

There was no significant activity on lease or PFI schemes during the period.

5.8 Investment Activity

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held and borrowed money held to facilitate the effective management of cashflow. During the first half of 2017/18 the Council's investment balance ranged between £19m and £70million due to timing differences between income and expenditure. The overall investment movement during the half year is shown in table 4 below.

Table 4: Investment Position

	31.3.17 Balance £m	**Movement £m**	**30.9.17 Balance £m**	**30.9.17 Weighted average rate %**	**30.9.17 Weighted average days to maturity**
Money Market Funds	10.2	11.2	21.5	0.15	1
Call Accounts	1.9	7.9	9.8	0.18	1
Pooled Funds (CCLA Property Fund)	15.0	0.0	15.0	9.07	n/a*
Total investments	**27.1**		**46.3**		

*The CCLA Property Fund is a longer term investment, so "Weighted Average Maturity" is not really meaningful (though there is a monthly opportunity to buy/sell units)

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

5.10 To achieve these objectives, and given the increasing risk and falling returns from short-term unsecured bank investments, the Council has mainly held its cash balances in money market funds, which have a similar, and sometimes higher yield. The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in table 5 below.

Table 5: Investment Benchmarking

	Credit Score	Credit Rating	*Bail-in Exposure	Rate of Return
31.03.2017	4.91	A+	100%	0.84%
30.06.2017	4.92	A+	100%	3.34%
30.09.2017	4.92	A+	100%	3.01%
Similar LAs	**4.8**	**A+**	**70%**	**1.46%**
All LAs	**4.44**	**AA-**	**65%**	**1.12%**

*Bail in exposure provides an indication of the capital losses the Council may incur, in the (low risk) scenario that the banking institutions to whom money has been lent failed.

The better credit score and reduced bail in exposure achieved by other authorities reflect that some of them have money lent to other local authorities, which both improves the credit score and reduced the bail in exposure.

5.11 The Council's £15m of externally managed pooled property fund investment generated a dividend returns of £356k in the half year. This income to the budget helped support services in year. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives are regularly reviewed. Investment in this fund is planned to be maintained for several years to allow time for capital growth to outstrip the 7% bid/offer margin when (most of) our units were purchased.

6. Other Investment Activity – Property Investments

6.1 Although not currently classed as treasury management activities and therefore not covered by the CIPFA Code, the Council also bought £24m of investment property in 2016/17, and held a further £1.9m (restated balance sheet value) at the start of the year. Further investments have been investigated, but none yet made during 2017/18.

6.2 These non-treasury investments generated c.£737k of investment income for the Council after taking account of direct costs and MRP, representing a rate of return of c.6.1% annual return. This is higher than the return earned on treasury investments, but reflects the additional risks to the Council of holding such investments.

6.3 Assuming CIPFA's proposed amendments to the Treasury Management Code are adopted in the revised Code from 2018/19, these will henceforth need to be included in the expanded definition of "investments".

6.4 Performance Report

The Council primarily measures the financial performance of its treasury management activities in terms of its impact on the revenue budget, where there is an underspend as reported in budget monitoring.

The Prudential Indicator that measures treasury costs as a percentage of the overall budget also serves as a measure. The estimate at the start of the year and forecast for the year as a whole are as in Table 6 below. A comparison with 2016/17 provides an indication of the impact of capital financing costs on the overall budget over time.

Table 6: Performance on the Funding Cost Indicator

Ratio of Financing Costs to Net Revenue Stream	**2016/17 February Revised %**	**2016/17 Actual %**	**2017/18 (February) Budget Estimate %**	**2017/18 (Mid Year) Forecast Outturn %**
General Fund	7.5	**7.0**	10.1	8.0
HRA	25.4	**25.0**	25.9	24.7

Prudential Code Compliance Report

7.1 We can report that all treasury management activities undertaken during the first half of 2017/18 complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy, save the cash position for seven days in the half year as explained in 7.3 below. Compliance with specific investment limits is demonstrated in table 7 below.

Table 7: Investment Limits

Figures in £m	H1 Maximum	30.9.17 Actual	2017/18 Limit	Complied
Any single bank with A- or better credit rating (subject to duration advice) or other Local Authorities	13.6	9.8	20	✓
Any group of funds under the same management	**As MMF below**		**20**	✓
Registered Providers (of Social Housing with A- credit rating or better)	**0**	**0**	**5**	✓
Unsecured investments with Building Societies	**0**	**0**	**10**	✓
Money Market Funds	**20 (in one fund)**	**21.5 (over 2 funds)**	**20**	✓
CCLA Property Fund	**15**	**15**	**20**	✓

7.2 Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 8 below.

Table 8: Debt Limits

	H1 Maximum	30.9.17 Actual	2017/18 Operational Boundary	2017/18 Authorised Limit	Complied
Borrowing	372.0	361.1	460	470	✓
PFI & finance leases	**31.0**	**c.30.6**	**40**	**40**	✓
Total debt	**403.0**	**391.7**	**500**	**510**	✓

Since the operational boundary is intended as a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

7.3 Treasury Management Indicators

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

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average 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. Unrated investments are assigned a score based on their perceived risk.

	30.9.17 Actual	2017/18 Target	Complied
Portfolio average credit	4.92	Below 6.0	✓

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. The minimum is normally £10m, though when this was indicator was introduced, it was recognised that there may be brief periods when this might be breached. During the half year there were two such brief periods in April and May between salary payment day and the month end. At the time the Council could easily have borrowed to avoid the technical breach, but as the borrowing was not otherwise required, but was not undertaken. As indicated above, when MIFID 2 comes in, we are likely to have to report such breaches so may consider borrowing instead. The normal minimum is being increased to £15m to allow some headroom above the MIFID 2 £10m minimum.

	30.9.17 Actual	2017/18 Target	Complied
Total cash available within 3 months	£31.3m	£10m	✓
Minimum in the 6 month period	£4.7m		✓

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 was:

	30.9.17 Actual	2017/18 Limit	Complied
Upper limit on fixed interest rate exposure	99.6%	110%	✓
Upper limit on variable interest rate exposure	13.7%	15%	✓

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

7.4 **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 were:

	30.9.17 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	19.3%	25%	0%	✓
12 months and within 24 months	1.3%	25%	0%	✓
24 months and within 5 years	3.9%	25%	0%	✓
5 years and within 10 years	6.1%	25%	0%	✓
10 years and above	69.2%	100%	40%	✓

During the half year the under 12 month maturity peaked at 21.5% of borrowing in early August. Taking account of our present debt maturity structure, if we persist with the present "short term" strategy we can have temporary borrowing of up to about £96m before the 25%<12 month limit would be breached. This will need to be carefully monitored towards the end of the financial year on the present forecast cash flow (and will may need recalibration if the LOBO restructure mentioned in paragraph 5.6 above proceeds. Given the low prospect of LOBO's options being called (and the Council's ability to replace them with PWLB loans at a much lower rate), LOBO's have been assumed to run significantly beyond a year.

7.6 **Principal Sums Invested for Periods Longer than 364 days:** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The Council has not made such investments for some time.

8. Outlook for the remainder of 2017/18

8.1 The UK economy faces a challenging outlook as the minority government continues to negotiate the country's exit from the European Union. Both consumer and business confidence remain subdued. Household consumption growth, the driver of UK GDP growth, has softened following a contraction in real wages. Savings rates are at an all-time low and real earnings growth (i.e after inflation) struggles in the face of higher inflation.

8.2 The Bank of England’s Monetary Policy Committee changed its rhetoric, implying a rise in Bank Rate in "the coming months" towards the end of the half year. Our advisor, Arlingclose was not convinced the UK’s economic outlook wholly justified such a move at this stage, but the Bank’s interpretation of the data has shifted, and the bank rate was increased by 0.25% to 0.5% at the beginning on November.

8.3 Arlingclose will be reviewing its forecast (which had anticipated a continuation of a 0.25% rate, possibly as far as 2020 (though with upside risk of 0.25%-0.5% from December 2017). In the longer term market Arlingclose’s central case is for gilt yields to remain broadly stable in the across the medium term, but there may be near term volatility due to shifts in interest rate expectations.

8.4 The Bank Rate increase was so well signalled that it would have been a major shock had it not been introduced, and we understand that the 10-year treasury yields in fact nudged downwards shortly after the BoE’’s announcement. One comment we have seen says that “over time the rate rise may ease the pressure on banks and pension funds, whilst also increasing the cost of debt; however, 3-year forecasts only show rates moving to 1.0%. The BoE decision reflects an erosion of economic slack and an increase in domestically generated inflation (as opposed to imported inflation which the BoE has so far been able to ‘*look through*’)”.