AUDIT COMMITTEE

Venue:	**Town Hall, Moorgate Street, Rotherham. S60 2TH**	**Date:**	**Wednesday, 5 February 2014**
		Time:	**4.00 p.m.**

A G E N D A

1. To determine if the following matters are to be considered under the categories suggested in accordance with the Local Government Act 1972.

2. To determine any item which the Chairman is of the opinion should be considered as a matter of urgency.

3. Minutes of the previous meeting held on 18th December, 2013 (herewith) (Pages 1 - 3)

4. KPMG Grants Report 2012/13 (report herewith) (Pages 4 - 13)

5. Review of Progress Against the Internal Audit Plan for the nine months ending 31st December, 2013 (report herewith) (Pages 14 - 25)

6. Prudential Indicators and Treasury Management and Investment Strategy 2014/15 to 2016/17 (report herewith) (Pages 26 - 53)

AUDIT COMMITTEE
18th December, 2013

Present:- Councillor Sangster (in the Chair); Councillors Gilding and Sharman.

Apologies for absence:- Apologies were received from Councillors Kaye and Sims.

P18. MINUTES OF THE PREVIOUS MEETING

Consideration was given to the minutes of the previous meeting of the Audit Committee held on 30th October, 2013.

Resolved:- That the minutes of the previous meeting be approved as a correct record for signature by the Chairman.

P19. CORPORATE RISK REGISTER

Consideration was given to a report presented by Colin Earl, Director of Internal Audit and Asset Management, which provided details of the Council's current Corporate Risk Register. The summary set out the risks associated with the Council's most significant priorities and projects and actions being taken to mitigate these risks.

The Council's key current risks continued to relate to the financial pressures faced by the Council and the implications of the coalition Government's Welfare Reforms. The report summarised the management actions that were being taken to mitigate these and other risks in the register.

The risk score on the priority relating to achieving economic growth remained high in recognition of the continuing weak economic conditions.

The risk register summary also showed risks in descending inherent risk order, to emphasize the most significant risks faced by the Authority. The top risks requiring close monitoring were:-

- Managing Government budget reductions - unable to maintain key services due to budgetary limits.
- Welfare Reforms.
- Delivering effective Children's Services within budget.
- Digital Region.
- Economic Growth.

An initial assessment had also been made of the Council's liabilities relating to aged insurance claims was made by the Municipal Mutual Insurance Company administrators in early 2013. This indicated a potential liability for the Council of up to £1.32m, which had been provided for in the Council's budget. Current indications were that there may be a further small increase in the liability during 2013/14.

The former risk relating to the implementation of the Localism Act had now been removed as the Council had successfully responded to relevant requirements. Any specific future risks would be included as separate items as appropriate.

Discussion ensued on the impact of welfare reform on Rotherham and on reputational risk and an update was provided on the current position with Digital Region and the progress being made to secure appropriate banking arrangements for the Council.

The Committee also noted the benchmarking activity being undertaken by KPMG, which would provide comparisons of risk by various Local Authorities. This information would be available in 2014.

Resolved:- (1) That the Corporate Risk Register summary attached at Appendix A be noted.

(2) That the current assessment of the Council's top corporate risks be noted.

(3) That any further risks or opportunities that it was felt should be added to the risk register be identified.

P20. ANNUAL REVIEW - INSURANCE AND RISK MANAGEMENT PERFORMANCE

Further to Minute No. 34 of the meeting of the Audit Committee held on 19th December, 2012, consideration was given to a report presented by Colin Earl, Director of Internal Audit and Asset Management, which set out details of the numbers and cost of insurance claims made against the Council.

It was noted that the Council continued to have a very good and improving record in most areas. Proactive Risk Management measures were helping to reduce the number of claims made against the Council and effective monitoring and inspection systems were enabling the Council to successfully defend many claims that were received.

The report highlighted areas where risk management action was helping to achieve the greatest savings in support of the Council's Medium Term Financial Strategy.

Reference was made to the summary of claims received by the Council over the past ten years, relating to the five main areas of insurance risk

On average, the Council had paid £1.42m per year on insurance claims over the last ten years. The need to continue to invest in reducing the costs of accidents via improved management systems, work environment and training could not be overstated.

The Committee welcomed this report and the work taking place to improve performance.

Resolved:- That the generally very good performance in relation to the management of risk and minimisation of insurance claims costs be noted.

P21. ASSESSMENT OF CURRENT LOCAL GOVERNMENT RISKS - KPMG AUDIT COMMITTEE INSTITUTE

Consideration was given to a report, presented by Colin Earl, Director of Internal Audit and Asset Management, stating that, during November 2013, the Chairman and the Vice-Chairman of the Audit Committee attended a KPMG Audit Committee Institute event on current local government issues. The event was designed to indicate to Audit Committee Members some of the key current issues that they may need to be aware of in fulfilling their responsibilities.

Reference was made to the key issues raised at the event and provided assurance to the Audit Committee about the arrangements in place at this Council in the areas highlighted by KPMG. This assurance showed that the Council had substantially got in place appropriate arrangements in the areas that were covered:-

- Transparency of Financial Reporting.
- Learning the Lessons from Public Interest Reports.
- Welfare Reforms.
- Fraud Risk.
- Public Health.
- Financial Management and Prospects: “A Brilliant Authority”.

The Committee noted that there were no significant risks associated with Public Health integration.

Resolved:- (1) That publication of the ‘’Audit Committee Institute Local Government Programme’’ be noted.

(2) That the Council’s position in the key areas covered and the future proposed actions be noted.

P22. DATE AND TIME OF THE NEXT MEETING

Resolved:- That the next meeting take place on Wednesday, 22nd January, 2014 at 4.00 p.m.

 Agenda Item 4

ROTHERHAM BOROUGH COUNCIL – REPORT TO MEMBERS

1.	**Meeting:**	**Audit Committee**
2.	**Date:**	**5 February 2014**
3.	**Title:**	**KPMG Grants Report 2012/13**
4.	**Directorate:**	**Resources**

5. Summary

The report advises Audit Committee of the matters arising from the external audit of the Council's 2012/13 government grants and returns (KPMG report attached as Appendix 1).

6. Recommendations

That Audit Committee notes:

- **the external auditor's report**
- **the sustained good performance of the Council in both preparing and submitting its 2012/13 grant claims and returns and reduced fees for carrying out grant certification work**

7. Proposals and Details

In agreement with our external auditor, KPMG annually provides feedback on the effectiveness of the Council's arrangements for preparing and submitting government grant claims and returns (see KPMG's report attached).

This report summarises KPMG's key findings from the certification work they have carried out in 2012/13.

The main findings are:

- KPMG were required to audit 5 claims and returns in 2012/13 with an aggregate value of £208m and issued a qualification certificate for one return and unqualified certificates for the remaining four grants and returns.

  The Housing and Council Tax Benefit claim was qualified for four separate issues, two of which have no impact on the subsidy, one which is awaiting a response from the system suppliers and one qualification issue which could reduce subsidy entitlement by £4k - this is dependent on the conclusion reached by the Department of Work and Pensions (DWP). Independent to this was a small adjustment to reduce subsidy entitlement by £4k which represents 0.004% of the claim value (£112m). **KPMG have commented that this grant is a very complex and high value grant and the relatively low number and value of amendments / qualification issues represents good performance at preparing this grant claim relative to other local authorities**.

- **The Council has good arrangements in place to ensure the efficient and effective preparation and submission of claims and returns and which supports the audit process**. In particular, working papers are of a good standard and officers responded promptly to audit queries.

These positive findings demonstrate that the Council continues to maintain the high standard achieved in recent years.

As a result of the Audit Commission changing its fee regime for certifying grants and returns, the Council's indicative grant fee for 2012/13 was set at £25k (£47k 2011/12). The actual fee charged varied from the original indicative amount due to changes in the following requirements:

- The Local Transport plan – Major Projects grant was not included in the original indicative figure resulting in an increase of £2k; and
- The Audit Commission removed the necessity for further testing in respect of the Pooling of Housing Capital Receipts, National Non-Domestic Rates and the Teachers' Pension returns resulting in a reduction of £2k.

Keeping audit fees at this low level is a direct result of this Council continuing to prepare substantially accurate and complete claims within agreed timeframes and with good supporting working papers. This enables KPMG to place assurance on the Council's arrangements and therefore keep the audit fees for carrying out their grant certification work to a minimum.

8. Finance

The reduction in fees for carrying out grant certification work is a welcome contribution to the budget savings the Council is being required to make.

9. Risks and Uncertainties

There are no outstanding risks or uncertainties as all the 2012/13 claims and returns have been certified and submitted.

10. Policy and Performance Agenda Implications

Sustaining the good performance identified by the external auditor in the way in which the Council prepares and submits government claims and returns should maintain their accuracy and quality thereby helping to secure the anticipated fee savings in 2013/14.

11. Background Papers and Consultation

External Auditor's Grants Report 2012/13

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Simon Tompkins, Finance Manager, extension 54513
simon.tompkins@rotherham.gov.uk

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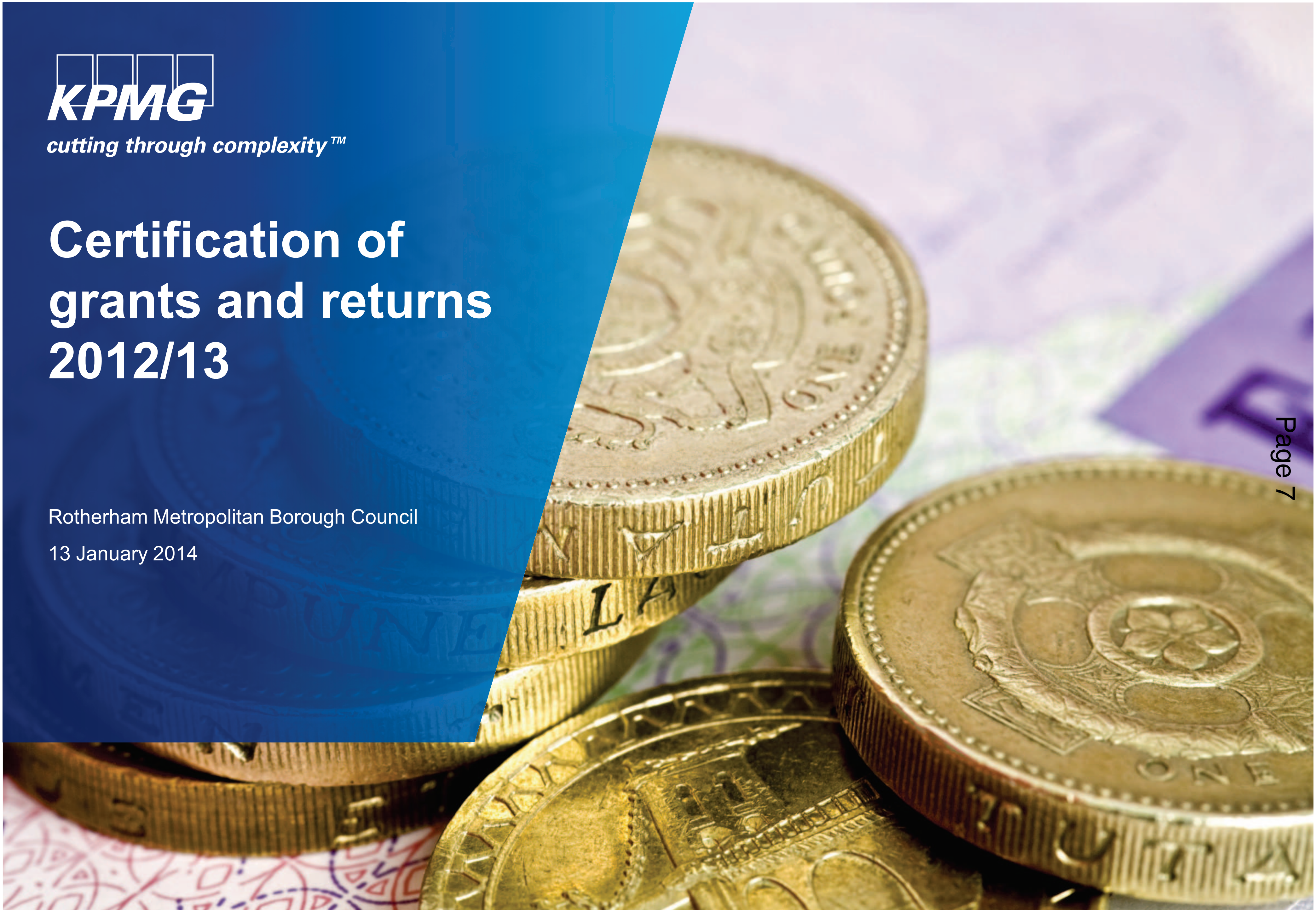
Certification of grants and returns 2012/13

Rotherham Metropolitan Borough Council

13 January 2014



Contents

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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Stephen Clark, who is the engagement leader to the Authority (telephone 0113 231 3543, e-mail stephen.clark@kpmg.co.uk who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees (telephone 0161 236 4000, e-mail trevor.rees@kpmg.co.uk) who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 0303 444 8330.

Headlines

Introduction and background	**This report summarises the results of work on the certification of the Council's 2012/13 grant claims and returns.** ■ For 2012/13 we certified: – One claim with a total value of £6.352m; and – Four returns with a total value of £201.235m.	
Certification results	**We issued a qualified certificate for one return and unqualified certificates for the remaining four grants and returns** ■ The Housing & Council Tax Benefit claim was qualified for four separate issues, two of which have no impact on the subsidy, one of which is awaiting a response from the system suppliers. The final qualification issue could reduce subsidy entitlement by £4k, however that will depend on the conclusion reached by the Department for Work and Pensions (DWP). Separate to this there is a small adjustment to reduce subsidy entitlement by £4k which represents 0.004% of the claim value. ■ This compares to no qualifications from 6 grants and returns in 2011/12.	**Pages 3 - 4**
Audit adjustments	**Adjustments were necessary to one of the Council's returns as a result of our certification work this year.** ■ As mentioned above the Housing & Council Tax Benefits claim was amended to reduce subsidy claimed by £4k.	**Pages 3 - 4**
The Council's arrangements	**The Council has good arrangements for preparing its grants and returns and supporting our certification work** ■ Working papers are generally clear and easy to follow, and very few errors have been found. ■ Officers respond efficiently and effectively to any queries we raise on grant and returns. ■ The Authority's arrangements to prepare its grants and return contribute to an efficient certification process.	**Pages 3 - 4**
Fees	**The Audit Commission changed its fee regime for certifying grants and returns in 2012/13, and set an indicative fee for the Council of £24,650. Our actual fee for the certification of grants and returns was £24,899.** ■ The increase in fee from the indicative amount is due to the requirement to certify the Local Transport Plan: Major Projects grant which was not included in the original figure.	**Page 5**

Summary of certification work outcomes

Overall, we certified 5 grants and returns:

- **4 were unqualified with no amendment;**
- **1 required a qualification to our audit certificate.**

Detailed comments are provided overleaf.

Detailed below is a summary of the key outcomes from our certification work on the Council's 2012/13 grants and returns, showing where either amendments were made as a result of our work or where we had to qualify our audit certificate.

A qualification means that issues were identified concerning the Council's compliance with a scheme's requirements that could not be resolved through adjustment. In these circumstances, it is likely that the relevant grant paying body will require further information from the Council to satisfy itself that the full amounts of grant claimed are appropriate.

	Comments overleaf	Qualified certificate	Significant adjustment	Minor adjustment	Unqualified certificate
Housing & Council Tax Benefit	1	●		●	
Pooling of Housing Capital Receipts					●
National Non Domestic Rates return					●
Teachers' Pensions return					●
Local Transport Plan: Major Projects					●
		1		1	4

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Summary of certification work outcomes

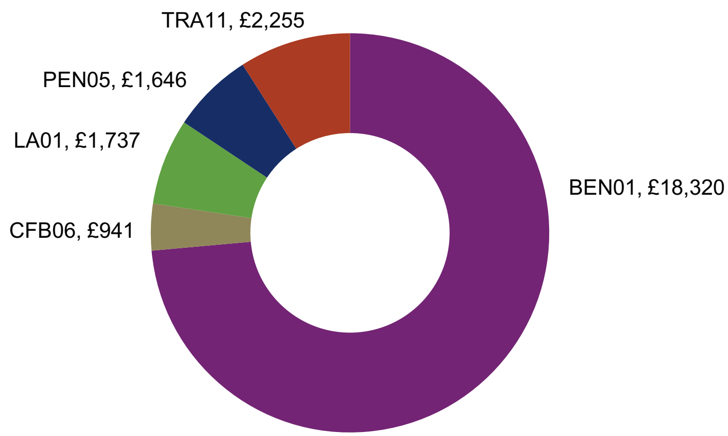
This table summarises the key issues behind the adjustment and qualification that were identified on the previous page.

Ref	Summary observations	Amendment
1	**Housing & Council Tax Benefit** •Detailed testing of Rent Rebates identified cases where benefit had been overpaid due to the claimant's weekly working hours being input incorrectly (and subsequently an additional earnings disregard being applied incorrectly). An extrapolated error was calculated for this issue and included within the qualification letter. Should the Department for Work and Pensions (DWP) choose to adopt this extrapolated error to the subsidy entitlement, there would be a small reduction of £4k. •Detailed testing of Rent Rebates also identified a case where we were unable to determine whether benefit had been correctly granted due to a number of unexplained movements in weekly benefit rate. A query had been raised with Northgate however no response had been received by the deadline for certification, and therefore this was included in the qualification letter. •A further issue was identified with a Rent Rebate case where benefit had been underpaid as an additional earnings disregard had only been applied in part. This was included on the qualification letter for information only, and will have no impact on subsidy. •Detailed tested of Rent Rebates, Rent Allowances, and Council Tax Benefits identified cases where expenditure had been incorrectly classified as backdated expenditure. An extrapolated error was calculated for this issue and included within the qualification letter. Should the DWP choose to adopt this extrapolated error there will be no change to subsidy as the backdated expenditure cells are for information only. •This is a very complex and high value grant (£112m) and the relatively low number and value of amendments/qualification issues represents good performance at preparing this grant claim relative to other local authorities.	-£4k

Fees

Our overall fee for the certification of grants and returns is slightly higher than the original estimate due to an additional grant requiring certification

Breakdown of certification fees 2012/13



Breakdown of fee by grant/return	2012/13 (£)	2011/12 (£)
BEN01 – Housing and Council Tax Benefit	18,320	34,815
CFB06 – Pooling of Housing Capital Receipts	941	2,285
LA01 – National Non Domestic Rates return	1,737	2,985
PEN05 – Teachers' Pensions return	1,646	3,360
TRA11 – Local Transport Plan: Major Schemes	2,255	0
Other claims not certified in 2012/13	0	3,745
Total fee	**24,899**	**47,190**

The Audit Commission changed its fee regime for certifying grants and returns in 2012/13. It set an indicative fee for the Council of £24,650. Based on the actual work we carried out the actual fee we charged was higher than the indicative fee. The actual fee varied from the indicative fee for the following reasons

- The Local Transport Plan: Major Schemes grant was not included in the initial original Audit Commission calculation, so additional fee of £2,255 was required;
- In 2010/11, the base year for this year's fee, Pooling of Housing Capital Receipts, National Non-Domestic Rates and the Teachers' Pension Return all required part A and B testing. For 2012/13, only part A testing was required. This has led to a fee reduction of £2,006.

The fee has reduced in comparison to 2011/12 by £22,291.

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ROTHERHAM BOROUGH COUNCIL – REPORT TO AUDIT COMMITTEE

1.	**Meeting:**	**Audit Committee**
2.	**Date:**	**5th February 2014**
3.	**Title:**	**Review of Progress Against the Internal Audit Plan for the nine months ending 31st December 2013**
4.	**Directorate:**	**Environment and Development Services**

5. Summary.

This report contains a summary of Internal Audit work and performance for the nine months ending 31st December 2013. The report shows that the service continues to perform at a high level across all indicators. One piece of work undertaken has led to the recovery of £20,000 on behalf of the Council.

Like many services within the Council, Internal Audit is diminishing in size. However, by using a risk based approach to planning and efficient management of our resources, we expect to be able to fulfil our minimum statutory responsibilities to give an opinion on the Council's internal control environment and to complete the work on fundamental accounting systems expected by the external auditor for the 2013/14 financial year.

Based upon the work undertaken in the period, we were able to confirm that the Council's control environment was adequate and was operating satisfactorily.

6. Recommendations.

The Audit Committee is asked to:

- **note the performance of the Internal Audit Service during the period**
- **note the key issues arising from the work done in the period**

7. Proposals and Details.

7.1 Background

This report summarises the main activities of the Internal Audit service for the first nine months of 2013/14. The report is presented to the Audit Committee to enable the Committee to fulfil its responsibility to oversee the work of Internal Audit. The report summarises:

- performance against key service benchmarks
- planned audit reports issued during the period, highlighting the overall conclusion/opinion for each audit
- the number of high priority recommendations made
- the proportion of recommendations agreed / not agreed
- a summary of responsive work undertaken
- an analysis of use of audit resources
- a summary of key service developments during the period.

7.2 Performance Indicators.

7.2.1 Our performance against a number of indicators is summarised in the table below:

Performance Indicator	2011/12 Actual	2012/13 Actual	2013/14 Target	April to Dec 2013
Draft reports issued within 15 days of field work being completed.	94%	93%	95%	95%
Percentage of 3 star (fundamental control weakness) recommendations agreed.	100%	100%	100%	100%
Chargeable Time/Gross Time.	62%	65%	63%	62%
Audits completed within planned time.	94%	93%	95%	89%
Percentage of Audit Plan completed.	84%	78%	85%	82%*
Cost per Chargeable Day.	£271	£275	£265	£268
Client Satisfaction Survey.	100%	100%	100%	100%

** extrapolated from performance to date*

7.2.2 Overall our performance against the targets agreed with Audit Committee is very good. Client satisfaction continues to be excellent, our performance on chargeable time is within 1% of target and the percentage of the Audit Plan completed is 82% at this stage. Although our performance in completing audits within planned time is slightly below target, we do expect this position to improve by the end of the financial year.

7.3 Planned Audit Reports and Recommendations.

7.3.1 **Appendix A** shows the audit reports issued during the first nine months of the year. Audit work in most areas indicated that satisfactory control arrangements were in place and that these arrangements were operating effectively during the period under review. Notwithstanding this, our work shows that there are opportunities to strengthen arrangements in some areas. Implementation of Internal Audit's recommendations for improvement will reduce the Council's exposure to risks.

7.3.2 Significant audit issues reported in the period included the following:

a) CYPS – Budget setting & monitoring and procurement at a secondary school

During the audit of a secondary school we identified that budget setting and monitoring arrangements were unsatisfactory and had resulted in the management reporting an inaccurate financial position during the 2012/13 year to its Governing Body. We concluded the overall control environment to be inadequate owing to the number of fundamental control weaknesses found. We have made a number of recommendations to address these weaknesses.

b) CYPS – Schools Catering Service

During a review of the Schools Catering Service we conducted a series of visits to school kitchens to evaluate the income cashing up / paying-in and reconciliation procedures in connection with the operation of a dinner money collection system.

Examination of procedures and controls in connection with the income system gave rise to a number of weaknesses including:

- the control of cash including a potential lack of separation of duties
- inadequate safe insurance
- a general absence of audit trails for transactions.

This has been reported to Education Catering Services management.

d) EDS: Treatment of VAT

During an audit of the Parks and Green Spaces Service we found that VAT had not been correctly accounted for on sales of food at catering facilities, which has resulted in an underpayment of VAT. A further significant VAT error was noted during an audit of the Local Land Charges function. The latest position on this is that the VAT errors highlighted by our report have been corrected and notified to HM Revenues & Customs. A review is also currently on-going to determine the extent of any similar errors within Land Charges and Parks and Green Spaces, with a view to examining the whole of EDS in due course.

7.4 Responsive Audits.

7.4.1 **Appendix B** summarises responsive work carried out in the period, which can be categorised into two main areas:

- investigative work
- requests for advice and assistance.

7.4.2 A total of 127 auditor days have been spent on responsive work to date, representing approximately 11% of available resources. Examples of the more significant areas examined in the period include: -

a) EDS: Investigation into an overspend on a civil engineering project

Following a request from the Capital Strategy and Asset Review Team (CSART), we investigated a significant capital overspend on a contract that involved emergency repair works to one of the Council's reservoirs. We found a number of budgetary control and contract management weaknesses and a subsequent failure to comply with the Council's Financial Regulations and Contract Standing Orders.

During our investigation we also identified that the cost of the works had not been fully verified in accordance with the contract and as a result we found potential overpayments to the contractor. A separate report has been issued and the recommendations accepted by management. **Since our report was issued overpayments totalling £20K (incl. VAT) have been identified and repaid to the Authority by the contractor.**

b) CYPS: Investigation of allegation of fraudulently claimed overtime

Following a request from HR & Payroll we conducted an investigation into an allegation that a member of staff at one of the Council's Children's Homes had been claiming for overtime shifts that had not been worked. We found insufficient evidence to indicate overtime had been claimed fraudulently. However a number of control weaknesses were found relating to the attendance recording system. We have made recommendations to improve controls in this area.

c) CYPS: Investigation into missing cash

Following a request from CYPS management we conducted an investigation at an Academy School into an amount of dinner money belonging to the RMBC Schools Catering Service that had gone missing whilst in transit from the kitchen to the administration office. All staff involved in cash handling were interviewed, although one member of staff went off sick prior to the interview. The same member of staff subsequently resigned their employment.

d) <u>CYPS: Investigation into allegations of financial issues at a secondary school, raised by a whistle-blower</u>

Internal Audit investigated the validity of financial issues at a secondary school that were raised by a whistle-blower. The audit confirmed that income due to the delegated school budget had been wrongly paid into the voluntary school fund and that consequently VAT had not been promptly and properly accounted for and paid over to HM Revenues and Customs.

e) <u>CYPS: Investigation into accusations of inappropriate use of funds by a secondary school, raised by anonymous letter</u>

Following the publication of an article in the *Rotherham Advertiser,* the Authority received anonymous letters containing accusations that a secondary school's voluntary school funds had been used to buy gifts for school staff and purchase goods for the personal use of the Head Teacher. Our work confirmed that purchases were made to reward staff for good OFSTED inspection and exam results. In the absence of a written constitution it was not possible to form an opinion as to whether this expenditure was consistent with the objectives or purposes of the fund. As a consequence the school had exposed itself to reputation damage. During the audit it was noted that a significant sum of money generated from letting the school's sports facilities was paid into the Private School Fund, instead of properly being paid into the school's Delegated Budget. Internal Audit made recommendations to address the issues.

g) <u>EDS – Investigation into cash shortfall</u>

Following concerns raised by a senior manager over a cash shortfall, we conducted an investigation into the 'cashing-up' and banking transactions over the period concerned, including interviewing members of staff. There was insufficient evidence to indicate theft, however we have agreed with senior management a programme of improvements to procedures to minimise future risk.

h) <u>NAS – Investigation into allegations of financial abuse</u>

We provided assistance with an investigation being undertaken by Adult Social Services and South Yorkshire Police into allegations of financial abuse of an elderly man with learning difficulties by a carer employed by a contractor. Insufficient evidence was found to support the allegations made; however, NAS management is working with the contractor to improve controls and procedures.

7.5 Analysis of Use of Audit Resources

7.5.1 The Audit Plan presented to the Audit Committee on 24th April 2013 identified the time available for internal audit during the year, the expected number of chargeable audit days and expected usage of available time. An analysis of the actual use of audit resources compared to the profiled budget at the end of December 2013 has been undertaken and is shown at **Appendix C**.

7.5.2 There have been 131 days fewer than expected at this stage of the year and this is mainly due to two instances of long term sickness (one due to an operation) and the profiling of time available for term-time staff (with more days lost during April to December). The position should improve over the final quarter of the year. Only 31 days have been lost to the planned programme of work as a result of lower demand (by 100 days) for investigations and responsive work.

7.5.3 Overall, we will be able to do sufficient work to fulfil our minimum statutory requirements.

7.6 Summary of Key Service Developments During the Period

7.6.1 The following significant developments have arisen during the period:

a) We have secured income generating work to fulfil the requirement for a 'Responsible Officer' function at Wingfield Academy, to provide assurance to Governors and the Academy on the adequacy of financial procedures and controls, based on an agreed programme of work.

8. Finance.

There are no direct financial implications arising from this report.

9. Risks and Uncertainties.

Failure to deliver an effective internal audit function would weaken the Council's internal control arrangements and increase the risk of erroneous and / or irregular activities.

10. Policy and Performance Agenda Implications.

The strength of Internal Audit impacts upon the Council's internal control environment. A sound control environment is part of good governance, which is wholly related to the achievement of the objectives in the Council's Corporate Plan.

11. Background Papers and Consultation.

Detailed audit reports.

Contact Names:
Colin Earl, Director of Audit and Asset Management x22033
Marc Bicknell, Chief Auditor x23297

Appendices:

Appendix A: Summary of Planned Audits Completed: Apr – Dec 2013

Appendix B: Summary of Internal Audit Responsive Work: Apr – Dec 2013

Appendix C: Analysis of Use of Audit Resources: Apr – Dec 2013

Appendix A

Summary of Planned Audits Completed: April – December 2013

Area Audited	Number of Recs Made	Number of Recs Agreed	Variance	Number of 3 * Recs Made	Number of 3 * Recs Agreed	Opinion Adequate/ Inadequate
Resources Directorate.						
Carbon Reduction Scheme	1	1	0	0	n/a	Adequate
Members' Allowances and Expenses	2	*	*	0	0	Adequate
ICT						
Application Controls	5	*	*	0	n/a	Adequate
Children and Young People's Services Directorate						
Aston Fence Primary School	8	8	0	0	n/a	Adequate
Aughton Primary School	8	8	0	0	n/a	Adequate
Thorpe Hesley Junior School	14	14	0	0	n/a	Adequate
Woodsetts Primary School	28	*	*	0	n/a	Adequate
Ferham Primary School	20	20	0	0	n/a	Adequate
Brampton Ellis Infant School	15	15	0	0	n/a	Adequate
Winterhill Private School Fund	4	4	0	0	n/a	Adequate
St Ann's Primary School	24	24	0	0	n/a	Adequate
Bramley Grange Primary School	20	20	0	0	n/a	Adequate
Troubled Families Grant	n/a	n/a	n/a	n/a	n/a	Adequate
Wingfield Responsible Officer	4	**	**	0	n/a	Adequate
Cherry Tree House Children's Home Liberty House Respite Centre	9	**	**	0	n/a	Adequate
Schools Catering Service	23	**	**	0	n/a	Inadequate
Children's Social Care: North Locality Team	8	8	0	0	n/a	Adequate
Fostering and Adoption Service: Imprest Accounts	7	7	0	0	n/a	Adequate
Rawmarsh Children's Centre	5	*	*	0	n/a	Adequate
Wath Victoria Children's Centre	9	**	**	0	n/a	Adequate
Wath Comprehensive School	12	*	*	0	n/a	Inadequate
Neighbourhoods and Adult Services Directorate						
Provision of Adult Social Care for the Elderly (Independent Sector)	11	*	*	0	n/a	Adequate
Licensing Income	8	*	*	0	n/a	Adequate
Supporting People	1	*	*	0	n/a	Adequate
Addison Road Day Centre	6	*	*	0	n/a	Adequate
Environment and Development Services Directorate						
Civic Theatre	10	10	0	0	n/a	Adequate
Local Land Charges	7	7	0	0	n/a	Adequate
Business Centres	1	1	0	0	n/a	Adequate

Appendix A

Summary of Planned Audits Completed: April – December 2013

Area Audited	Number of Recs Made	Number of Recs Agreed	Variance	Number of 3 * Recs Made	Number of 3 * Recs Agreed	Opinion Adequate/ Inadequate
Bus Service Operators Grant	n/a	n/a	n/a	n/a	n/a	Adequate
BDR Waste PFI	0	0	0	0	n/a	Adequate
Thrybergh Country Park	10	10	0	0	n/a	Adequate
Clifton Park	11	11	0	0	n/a	Adequate
Markets Income	5	5	0	0	n/a	Adequate
AFS Fire and Security Contract	2	2	0	0	n/a	Adequate
Home to School Transport	9	**	**	0	n/a	Adequate
Treatment of Waste (non-commercial)	5	*	*	0	n/a	Adequate
Blue Badge Scheme	3	*	*	0	n/a	Inadequate
Contracts						
EDS Design and Projects Team Final Accounts System	9	9	0	0	n/a	Adequate
Fundamental Systems						
Creditors System	6	6	0	0	n/a	Adequate

* Internal Audit Report issued – Awaiting formal response.
**Draft report issued – Awaiting response

Appendix B

Summary of Internal Audit Responsive Work: April – December 2013

Description
Resources Directorate
Advice provided on the competitive procurement requirements of Contract Standing Orders regarding the award of contracts to 'in house' providers.
Assisted Financial Services in issuing taxation guidance to managers when assessing the 'employment status' of contractors.
Advice provided on the payment arrangements regarding the Fund for Change scheme.
Advice provided on the disposal of obsolete Council paying-in books and general guidance on the Council's 'Retention of Data' policy.
We reviewed and commented on the controls in place to process requests to make changes to a creditor's bank account details.
Children and Young People Services Directorate
Investigation into an allegation of fraudulent claims for overtime by an employee at a Children's Home.
Advice provided to a school that was considering the use of an auction website to buy and sell items.
Investigation into missing cash at a secondary school.
Investigation into a 'Confidential Reporting' (whistle-blowing) case at a secondary school that alleged income due to the school's delegated budget had been diverted into its private fund
Investigation following allegations that a secondary school's funds had been used to purchase gifts for staff and goods for the personal use of the head teacher.
Advice provided to schools that were considering the purchase and download of 'i-tunes' for students' use.
Advice provided to schools regarding the payment of travel expenses to Governors.
Environment and Development Services Directorate
Investigation into the budgetary control and contract administration arrangements following a significant overspend on a civil engineering project and follow-up review of contract payments.
Advice and guidance provided on income reconciliation procedures.
Advice provided on a new electronic authorisation system for processing contract payments.
Investigation into the validity of additional payments to two members of staff employed at a Council depot.
Review of the process applied to the sale of Council-owned land, following a complaint from a member of the public.
Advice provided to ICT to assist in its review of the Council's ICT Security Policy.
Advice provided on the proposal to install cash payment machines to replace the cashiering function at several sites across the Borough.
Advice provided on fees for the use of Herringthorpe Stadium.
Advice provided on Contract Standing Orders in respect of the procurement of temporary modular buildings and classrooms.
Investigate concerns into a shortfall of cash identified during the routine 'cashing-up' and banking process
Advice provided on disposal of assets to ensure compliance with Financial Regulations

Appendix B

Summary of Internal Audit Responsive Work: April – December 2013

Description
Neighbourhoods and Adult Services Directorate
Advice provided to the Commissioning Team on inclusion of a reference to the Council's Anti-Money Laundering policy in contract documentation.
Advice provided on Contract Standing Orders regarding exemption from seeking competitive tenders for external insulation of non-traditional properties.
Assistance with an investigation by Adult Social Services and South Yorkshire Police into allegations of financial abuse of an elderly man with learning difficulties by a carer employed by a contractor.
Advice provided to the Corporate Procurement Team on the tender documentation and tender evaluation model for the re-tender of the corporate cash collection contract.

Appendix C

Analysis of use of Audit Resources April – December 2013

Analysis of use of Audit Resources

	Budget 2013/14	Profiled Budget (Periods 1- 9)	Actual (Periods 1 – 9)	Variance
Gross Days Available	**2614**	**1961**	**1894**	**-67**
Less				
Vacancy	0	0	0	0
Leave (Annual / Statutory / Other)	364	273	312	+39
Elections	0	0	0	0
Sickness	73	55	107	+52
Service Development	30	23	31	+8
Professional Training and CPD	122	92	46	-46
Management and Supervision	193	145	151	+6
Admin and Clerical	60	45	72	+27
Professional Meetings	0	0	0	0
Less	**842**	**633**	**719**	**+86**
Gross Audit Days Available	**1772**	**1328**	**1175**	**-153**
Less				
2012/13 Work Brought Forward / Follow Up Work	65	49	27	-22
Less	**65**	**49**	**27**	**-22**
Net Audit Days Available for 2013 / 2014	**1707**	**1279**	**1148**	**-131**
Responsive Audits	303	227	127	-100
Planned Audits	1404	1052	1021	-31

There are a number of variances between budget and actual in relation to the number of audit days available. The most significant of which are: -

- The gross days available has reduced by 67 days due to: (i) a member of staff moving to a term-time only contract, which has created a small budget saving for the Council and (ii) another two members of staff that work 'term-time' only, having a disproportionate amount of school holidays (non-working time) during the 9 months to December 2013, than in the period Jan – Mar 2014.
- Annual Leave is higher than the profiled budget at the end of period 9 (Dec 2013) because most members of staff use most of their leave during the summer months and use further leave around Christmas. In addition three members of staff purchased additional leave (13 days in total) in accordance with RMBC terms and conditions.

Appendix C

Analysis of use of Audit Resources April – December 2013

- Sickness absence is higher than expected (by 52 days) mainly as a result of two instances of protracted illness, one that required hospital treatment.
- Time spent on professional training is below budget. This follows last year's decision to place increased emphasis on low-cost "on the job" training due to the high costs associated with external professional training and the result of ongoing budget pressures. As a consequence there has been a need to focus on delivery of the plan and scale back training opportunities.
- Time spent on responsive work remains under budget as Internal Audit has been able to quickly conclude investigations. This also reflects the effectiveness of our risk-based planning approach that has reduced the amount of 'unexpected' requests for work.

 Agenda Item 6

ROTHERHAM BOROUGH COUNCIL – REPORT TO MEMBERS

1.	**Meeting:**	**Audit Committee**
2.	**Date:**	**5 February 2014**
3.	**Title:**	**Prudential Indicators and Treasury Management and Investment Strategy 2014/15 to 2016/17**
4.	**Directorate:**	**Resources**

5. Summary

In accordance with the Prudential Code for Capital Finance, the Secretary of State's Guidance on Local Government Investments, the CIPFA Code of Practice for Treasury Management in Local Authorities and with Council policy, the Director of Financial Services is required, prior to the commencement of each financial year to seek the approval of the Council to the following:

i. The Prudential Indicators and Limits for 2014/15 to 2016/17 (Appendix A)
ii. A Minimum Revenue Provision (MRP) Statement which sets out the Council's policy on MRP (Appendix A)
iii. An Annual Treasury Management Strategy in accordance with the CIPFA Code of Practice on Treasury Management including the Authorised Limit (Appendix B)
iv. An Investment Strategy in accordance with the Department for Communities and Local Government (CLG) investment guidance (Appendix B)

6. Recommendations

Audit Committee is asked to consider the proposed Cabinet recommendations to Council:

1. **Approve the prudential indicators and limits for 2014/15 to 2016/17 contained in Appendix A to the report**

2. **Approve the Minimum Revenue Provision Statement contained in Appendix A which sets out the Council's policy on MRP**

3. **Approve the Treasury Management Strategy for 2014/15 to 2016/17 and the Authorised Limit Prudential Indicator (Appendix B)**

4. **Approve the Investment Strategy for 2014/15 to 2016/17 (Appendix B – Section (e) and Annex B1)**

7. Proposals and Details

The Director of Financial Services has delegated authority to carry out treasury management activities on behalf of the Council. This report is produced in order to comply with the CIPFA Code of Practice for Treasury Management in Local Authorities, the CIPFA Prudential Code for Capital Finance in Local Authorities and the CLG Investment Guidance.

The Council's 2013/14 Treasury Management Strategy was approved by Council on 6 March 2013, whilst a Mid Year report which updated the 2013/14 approved indicators was approved by Council on 11 December 2013. This report updates the currently approved indicators for the period 2013/14 to 2015/16 and introduces new indicators for 2016/17.

The Strategy was drawn up in association with the Council's treasury management advisors, Capita Asset Services, part of The Capita Group plc.

7.1 Background

During 2009 three key documents were published, the first two of which resulted in the main from the impact of the Icelandic banking issues:

- the Audit Commission report 'Risk and Return',
- the CLG Select Committee report on local authority investments; and,
- CIPFA's revised Prudential Code.

In addition CIPFA fully revised its guidance on Treasury Management and published the following two documents towards the end of 2009:

- Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes; and,
- Treasury Management in the Public Services – Guidance Notes for Local Authorities including Police Authorities and Fire Authorities

In March 2010 CLG confirmed changes to the Capital Finance system which included revisions to CLG's Investment Guidance. These were in line with the outcomes from the publications & reports issued (and referred to above) and take account of the changes to CIPFA's Code of Practice and Guidance Notes.

During 2011 CIPFA published updates to the Treasury Management Code of Practice, the Treasury Management Guidance Notes and the Prudential Code. These incorporated minor revisions to the previous guidance.

This report is fully reflective of the changes to guidance issued by CIPFA and the CLG.

7.2. Review of the Currently Approved Investment Strategy

Following the events of October 2008 and in light of the current and on-going economic & financial climate, the Director of Financial Services took a series of actions to evaluate the Council's Investment Strategy and manage the treasury management function.

The Council's investment policy's continuing primary governing principle is the **security** of its investments, although yield or return on investments is also a consideration.

The revised operational guidelines enhanced the weighting towards 'security' even further at the expense of yield or return. Although seeking to minimise investment default risk, it does not eliminate it. Eliminating risk altogether is only possible if the Council only invested any surplus funds with the Bank of England's Debt Management Office (DMO).

These actions were reinforced within the currently approved strategy whereby the criteria for choosing counterparties were tightened. We continue to operate the treasury management guidelines well within the boundaries set by the approved selection criteria so as to minimise the risks inherent in operating a treasury management function during volatile and adverse economic and financial conditions. To this end, the Council has continued to invest any surplus funds primarily with the Bank of England's Debt Management Office.

In addition, investment levels over the last 12 months remain low as market conditions still dictate that it continues to be prudent to defer borrowing plans and to fund on-going capital commitments through the use of the Council's internal cash-backed resources.

Actual returns on investment opportunities remain subdued when compared to previous years but have been effectively and prudently managed by significantly reducing expected capital financing costs by delaying borrowing plans. This has enabled the Council to stay within its capital financing budget cash limit and for budget savings to be put forward in support of both the Council's 2013/14 and 2014/15 revenue budget. This is a significant achievement given the difficult economic and financial conditions prevailing throughout the current financial year.

Counterparty List

At the present time the Council's counterparty list for investments uses the following criteria:

	Fitch	Moody's	Standard & Poor's	Money Limit	Time Limit
Upper Limit Category	F1+/AA-	P-1/Aa3	A-1+/AA-	£20m	5years
Middle Limit Category	F1/A-	P-1/A3	A-1/A-	£10m	364 days
Lower Limit Category *	All Building Soc's ranked 1 to 10 All Building Soc's ranked 11 to 20			£5m £1m	6 months 3 months
Debt Management Office	-	-	-	Unlimited **	6 months
Money Market Funds ***	-	-	-	£20m	n/a
UK Single Tier & County Councils	-	-	-	£20m	5 years
The Council's Bankers	-	-	-	£10m	364 days

The above money limits are exclusive of bank balances held by schools

* Based on maximum of 20% of the investment portfolio

** Provides maximum flexibility

*** Based on maximum of 20% of the investment portfolio

Taking into account the current market conditions and future economic and financial outlook, whilst retaining sufficient flexibility to react to changing market conditions, it is proposed to retain the currently approved criteria.

In essence, the counterparty list provides the Council with the opportunity to maximise security of any invested funds by allowing all funds to be placed with the DMO and UK Single Tier and County Councils and reducing the maximum level and time of investments that can be placed with financial institutions that do not meet all the upper limit credit rating criteria.

The Co-operative Bank is undergoing a restructuring to strengthen its financial position and as part of the restructuring strategy the bank will be withdrawing from providing banking services to Local Authorities. For individual authorities this takes place at the time contracts run out which in the Council's case is the end of March 2015. To ensure the transfer between provider runs smoothly it is suggested the Council should re-tender for its banking services early with a new contract start before the end of 2014. Specific reference to the Co-operative Bank has therefore been removed in the above table of criteria for selecting counterparties. A general reference allows for the eventuality that the new provider also does not meet the Council's minimum investment criteria and an exception for day-to-day banking is required. Progress reports on the tendering of banking services will be presented to Members in due course.

7.3 Prudential Indicators

7.3.1 Capital Expenditure, Capital Financing Requirement & Affordability

The Prudential Indicators submitted for approval are summarised as:

	2013/14 Revised	2014/15 Estimated	2015/16 Estimated	2016/17 Estimated
Capital Expenditure	£82.395m	£59.348m	£42.030m	£32.439m
Capital financing requirement	£754.447m	£749.856m	£761.685m	£750.984m
Authorised limit for external debt (RMBC)	£774.908m	£765.376m	£762.910m	£761.685m
Operational boundary for external debt (RMBC)	£617.775m	£614.912m	£619.925m	£617.585m
Authorised limit for external debt (Former SYCC)	£96.121m	£96.121m	£96.121m	£86.709m
Operational boundary for external debt (Former SYCC)	£96.121m	£96.121m	£96.121m	£86.709m

	2013/14 Revised	2014/15 Estimated	2015/16 Estimated	2016/17 Estimated
Ratio of financing costs to net revenue stream – Non HRA	8.18%	9.14%	8.59%	8.10%
Ratio of financing costs to net revenue stream – HRA	18.17%	17.52%	16.06%	15.32%
Incremental impact of capital investment decisions on the Band D Council Tax	£3.46	£6.69	£4.06	£4.35
Incremental impact of capital investment decisions on housing rents levels	£0.03	£0.13	£0.00	£0.00

It should be noted that only schemes in the Council's approved capital programme are included in the indicators as listed and that there may be further schemes pending approval. Any additional approvals will normally have to be funded from unsupported borrowing as all identified available resources have been allocated. This would impact on the prudential indicators above.

It should further be noted that the impact on Band D Council Tax, as shown in the table above, indicates the impact of the Council's capital investment plans as already budgeted for within the proposed Budget for 2014/15 and the Council's Medium Term Financial Strategy, **and does not indicate additional requirements of Rotherham council tax payers**.

7.3.2 Treasury Management Prudential Indicators and Limits on Activity

There are four treasury prudential indicators, the purpose of which is to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. The indicators submitted for approval are shown below.

The limits for interest rate exposures are consistent with those approved within the Mid Year report on the 2013/14 Strategy; in line with the requirements of the new Code the maturity structure detail has been updated and extended; and the investment limits beyond 364 days have been maintained to reflect the continued investment strategy.

RMBC	2014/15	2015/16	2016/17
Interest rate Exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rate debt based on fixed net debt	100%	100%	100%
Limits on variable interest rate debt based on variable net debt	30%	30%	30%

RMBC Maturity Structure of fixed interest rate borrowing 2014/15		
	Lower	**Upper**
Under 12 months	0%	35%
12 months to 2 years	0%	35%
2 years to 5 years	0%	40%
5 years to 10 years	0%	40%
10 years to 20 years	0%	45%
20 years to 30 years	0%	50%
30 years to 40 years	0%	50%
40 years to 50 years	0%	55%
50 years and above	0%	60%

RMBC Maximum Funds invested > 364 days			
	1 to 2 years	2 to 3 years	3 to 5 years
Funds invested > 364 days	£m 10	£m 8	£m 6

Former SYCC	2014/15	2015/16	2016/17
Interest Rate Exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	30%	30%	30%

Maturity Structure of fixed interest rate borrowing 2014/15		
	Lower	**Upper**
Under 12 months	0%	50%
12 months to 2 years	0%	70%
2 years to 5 years	0%	100%
5 years to 10 years	0%	100%

7.4 Minimum Revenue Provision Policy

Communities & Local Government Regulations require Full Council to approve a Minimum Revenue Provision Statement in advance of each financial year. The policy put forward for approval is set out in section 12 of Appendix A.

8. Finance

Treasury Management forms an integral part of the Council's overall financial arrangements.

The assumptions supporting the capital financing budget for 2014/15 and for the future years covered by the MTFS of the Council have been reviewed in light of the current economic and financial conditions and the revised future years' capital programme.

The proposed Treasury Management and Investment Strategy is not forecasted to have any further revenue consequences other than those identified and planned for in both the Council's 2014/15 Revenue Budget and approved MTFS.

9. Risks and Uncertainties

The proposed Treasury Management and Investment Strategy seeks to minimise the risks inherent in operating a Treasury Management function during these difficult economic and financial conditions.

Operational Treasury Management guidelines will continue to be kept in place and reviewed to ensure they are appropriate given the circumstances faced, supported by regular monitoring to ensure that any risks and uncertainties are addressed at an early stage and hence kept to a minimum.

10. Policy and Performance Agenda Implications

Effective Treasury Management will assist in delivering the Councils' policy and performance agenda.

11. Background Papers and Consultation

Audit Committee – 13 February & 30 October 2013
Cabinet – 20 February & 27 November 2013
Council – 6 March & 11 December 2013
CIPFA – The Prudential Code for Capital Finance in Local Authorities
CIPFA – Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes
CIPFA – Treasury Management in the Public Services – Guidance Notes for Local Authorities including Police Authorities and Fire Authorities
CLG Investment Guidance – March 2010
The Local Government Act 2003

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Appendix A

PRUDENTIAL INDICATORS 2014/15 TO 2016/17

Introduction

1. The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code and prepare and publish prudential indicators. Each indicator either summarises the expected activity or introduces limits upon the activity, and reflects the underlying capital programme. This report updates currently approved indicators and introduces new indicators for 2016/17.

2. Within this overall prudential framework there is a clear impact on the Council's treasury management activity, either through borrowing or investment activity. As a consequence the Treasury Management Strategy for 2014/15 to 2016/17 is included as Appendix B to complement these indicators. Some of the prudential indicators are shown in the Treasury Management Strategy to aid understanding.

The Capital Expenditure Plans

3. The Council's capital expenditure plans are summarised below and this forms the first of the prudential indicators. A certain level of capital expenditure is grant supported by the Government; any decisions by the Council to spend above this level will be considered unsupported capital expenditure. This unsupported capital expenditure needs to have regard to:

    - Service objectives (e.g. strategic planning);
    - Stewardship of assets (e.g. asset management planning);
    - Value for money (e.g. option appraisal)
    - Prudence and sustainability (e.g. implications for external borrowing and whole life costing);
    - Affordability (e.g. implications for the council tax and rents)
    - Practicality (e.g. the achievability of the forward plan).

4. The revenue consequences of capital expenditure, particularly the unsupported expenditure, will need to be paid for from the Council's own revenue resources.

5. This capital expenditure can be paid for immediately (by applying capital resources such as capital receipts, capital grants etc., or revenue resources), but if these resources are insufficient any residual expenditure will add to the Council's borrowing need.

6. The key risks to the plans are that the level of Government support has been estimated and is therefore subject to change. Similarly some of estimates for other sources of funding, such as capital receipts, may also be subject to change over this timescale. For example, anticipated asset sales resulting from the Council's on-going asset rationalisation programme may be deferred due to the on-going impact of the current economic & financial conditions on the property market.

7. The Council is asked to approve the summary capital expenditure projections below. This forms the first prudential indicator:

	2013/14 Revised £m	**2014/15 Estimated £m**	**2015/16 Estimated £m**	**2016/17 Estimated £m**
Children & Young People's Services	21.108	10.948	6.307	3.257
Env & Dev Services	24.420	14.239	7.239	0.650
Neighbourhoods & Adult Services – Non HRA	4.786	3.156	1.950	1.897
Resources	2.389	0.957	0.470	0.470
Total Non-HRA	**52.703**	**29.300**	**15.966**	**6.274**
HRA	29.692	30.048	26.064	26.165
Total HRA	**29.692**	**30.048**	**26.064**	**26.165**
Total expenditure	**82.395**	**59.348**	**42.030**	**32.439**
Capital receipts	1.815	0.782	0.332	0.332
Capital grants, capital contributions & sources other capital funding	69.371	50.967	31.939	30.937
Total financing	**71.186**	**51.749**	**32.271**	**31.269**
Net financing need for the year	**11.209**	**7.599**	**9.759**	**1.170**

8. Other long term liabilities - the above financing need excludes other long-term liabilities, such as PFI and leasing arrangements which already include borrowing instruments.

<u>The Capital Financing Requirement (the Council's Borrowing Need)</u>

9. The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. The capital expenditure above which has not immediately been paid for will increase the CFR.

10. Following accounting changes the CFR includes any other long term liabilities (e.g. PFI schemes) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of scheme include a "borrowing facility" and so the Council is not required to separately

borrow for this scheme. The Council will have £127.405m within the CFR at 1 April 2014 in respect of such schemes.

11. The Council is asked to approve the CFR projections below:

	2013/14 Revised £m	2014/15 Estimated £m	2015/16 Estimated £m	2016/17 Estimated £m
CFR – General Fund	449.637	442.210	454.039	443.338
CFR – HRA	304.810	307.646	307.646	307.646
Total CFR	**754.447**	**749.856**	**761.685**	**750.984**
Movement in CFR	**-0.589**	**-4.591**	**11.829**	**-10.701**
Movement in CFR represented by:				
Net financing need for the year (above)	11.209	7.599	9.759	1.170
Net financing need for the year (OLTL - Waste PFI)	0.000	0.000	13.518	0.000
Less General Fund MRP/VRP and other financing movements	11.798	12.190	11.448	11.871
Movement in CFR	**-0.589**	**-4.591**	**11.829**	**-10.701**

MRP Policy Statement

12. The Council is required to pay off an element of the accumulated General Fund capital spend each year through a revenue charge (the Minimum Revenue Provision - MRP). In addition, it is also allowed to make additional voluntary payments (VRP) where it is prudent to do so.

13. CLG Regulations require Full Council to approve an MRP Statement in advance of each year. Detailed rules have been replaced by a single duty to charge an amount of MRP which the Council considers ‘prudent’. The Director of Financial Services will, where it is prudent to do so, use discretion to review the overall financing of the capital programme and the opportunities afforded by the regulations to maximise the benefit to the Council whilst ensuring it meets its duty to charge a ‘prudent’ provision. To provide maximum flexibility into the future the recommended MRP policy has been amended to include the use of the annuity method in addition equal instalments method.

    The Council is recommended to approve the following MRP policy in relation to the charge for the 2014/15 financial year:

    (a) The MRP charge in relation to borrowing for capital expenditure incurred prior to 2007/08 will be unaffected by the regulations;

    (b) The MRP charge in relation to capital expenditure incurred since 2007/08 where the expenditure is funded by both supported and unsupported borrowing will be calculated using the expected useful life of the asset at the point the asset is brought into use. The calculation of the provision will be either the annuity method or the equal instalments method depending on which is most appropriate; and

(c) The MRP charge in relation to capital expenditure incurred since 2007/08 where the expenditure is funded by a ‘capitalisation directive’ (e.g. equal pay) will be calculated on the basis of the specified period(s) set down within the regulations. The calculation of the provision will be either the annuity method or the equal instalments method depending on which is most appropriate.

14. No MRP charge is currently required for the HRA. With the move to self-financing, the HRA will be required to charge depreciation on its assets, which will be a revenue charge. To alleviate the impact of this charge falling on the tenants, new HRA regulations will allow the Major Repairs Allowance to be used as a proxy for depreciation for the first five years.

15. Repayments included in annual PFI or finance leases are applied as MRP.

Affordability Prudential Indicators

16. The previous sections cover those prudential indicators that are used to monitor the impact the capital programme has on the Council’s borrowing position.

17. Within this framework prudential indicators are used to assess the affordability of the capital investment plans. Further indicators are used to provide an indication of the impact the capital programme has on the overall Council’s finances. The Council is asked to approve the following indicators.

18. **Actual and Estimates of the ratio of financing costs to net revenue stream** – This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream of the Council. The trend reflects the Council’s prioritisation of its capital investment plans.

19. The estimates of financing costs include all current commitments, the proposals contained in the proposed 2014/15 Revenue Budget and updated future years’ Capital Programme. The “non HRA” figures from 2014/15 onwards also reflect the changes to Council funding brought about by Local Government Reform which increases the level of general grant funding included within the Net Revenue Stream.

Ratio of financing costs to Net Revenue Stream				
	2013/14 Revised %	2014/15 Estimated %	2015/16 Estimated %	2016/17 Estimated %
Non-HRA	8.18	9.14	8.59	8.10
HRA	18.17	17.52	16.06	15.32

20. **Estimates of the incremental impact of capital investment decisions on the Council Tax** – This indicator identifies the revenue costs associated with proposed changes to the capital programme compared to the Council's existing commitments and current plans.

Only schemes in the Council's approved capital programme are included in the indicators and there may be further schemes pending approval. Any additional approvals will normally have to be funded from unsupported borrowing as all identified available resources have been allocated. This would impact on the prudential indicators above.

The impact on Band D Council Tax, as shown in the table below, indicates the impact of the Council's capital investment plans as already budgeted for within the proposed Budget for 2014/15 and the Council's Medium Term Financial Strategy, **and does not indicate additional requirements of Rotherham council tax payers**.

Incremental impact of capital investment decisions on the Band D Council Tax				
	Revised 2013/14 £	Proposed Budget 2014/15 £	Projection 2015/16 £	Projection 2016/17 £
Council Tax – Band D	3.46	6.69	4.06	4.35

For each financial year the impact at Band A is £2.31, £4.46, £2.71 and £2.90 respectively.

21. **Estimates of the incremental impact of capital investment decisions on Housing Rent levels** – Similar to the Council tax calculation, this indicator identifies the revenue cost of proposed changes in the housing capital programme compared to the Council's existing approved commitments and current plans expressed in terms of the impact on weekly rent levels.

Incremental impact of capital investment decisions on the Housing Rent levels				
	Revised 2013/14 £	Proposed Budget 2014/15 £	Projection 2015/16 £	Projection 2016/17 £
Weekly Housing Rent levels	0.03	0.13	0.00	0.00

Appendix B

TREASURY MANAGEMENT STRATEGY 2014/15 – 2016/17

1. Treasury Management is an important part of the overall financial management of the Council's affairs. The prudential indicators in Appendix A consider the affordability and impact of capital expenditure decisions, and set out the Council's overall capital framework. The Treasury Management Strategy considers the effective funding of these decisions. Together they form part of the process which ensures the Council meets balanced budget requirement under the Local Government Finance Act 1992. There are specific treasury prudential indicators included in this Strategy which require Member approval.

2. The Council's treasury activities are strictly regulated by statutory requirements and a professional code of practice (the CIPFA Code of Practice on Treasury Management – revised November 2009). The Council adopted the Code of Practice on Treasury Management (Cabinet, March 2004) and adopted the revisions to the Code in March 2010.

3. The Council's constitution (via Financial Regulations) requires an annual strategy to be reported to Council outlining the expected treasury activity for the forthcoming 3 years. A key requirement of this report is to explain both the risks, and the management of the risks, associated with the treasury service. A further report is produced after the year-end to report on actual activity for the year, and a new requirement of the revision of the Code is that there is a mid-year monitoring report.

4. This Strategy covers:

   (a) The Council's debt and investment projections;
   (b) The Council's estimates and limits to borrowing activity;
   (c) The expected movement in interest rates;
   (d) The Council's borrowing and debt strategy
   (e) The Council's investment strategy;
   (f) Treasury Management prudential indicators and limits on activity;
   (g) Treasury performance indicators
   (h) Policy on the use of external service advisers

(a) Debt and Investment Projections 2014/15 – 2016/17

5. The borrowing requirement comprises the expected movement in the CFR and any maturing debt which will need to be re-financed. The table below shows this effect on the treasury position over the next three years for both the Council and the ex-SYCC debt that the Council administers on behalf of the other South Yorkshire local authorities. The table also highlights the expected level of investment balances.

RMBC	2013/14 Revised £m	2014/15 Estimated £m	2015/16 Estimated £m	2016/17 Estimated £m
External Debt				
Borrowing at 1 April	488.437	487.507	482.424	480.084
Expected change in debt	-0.930	-5.083	-2.340	-10.868
Other long-term liabilities (OLTL) at 1 April	129.338	127.405	125.617	137.501
Expected change in OLTL	-1.933	-1.788	11.884	-2.126
Borrowing at 31 March	614.912	608.041	617.585	604.591
CFR – the borrowing need	754.447	749.856	761.685	750.984
Under/(over) borrowing	139.535	141.815	144.100	146.393
Investments				
Total Investments at 1 April	15.479	20.000	10.000	10.000
Investment change	4.521	-10.000	0.000	0.000
Total Investments 31 March	20.000	10.000	10.000	10.000
Net borrowing	594.912	598.041	607.585	594.591

Ex SYCC	2013/14 Revised £m	2014/15 Estimated £m	2015/16 Estimated £m	2016/17 Estimated £m
External Debt				
Borrowing at 1 April	96.121	96.121	96.121	86.709
Expected change in debt	0.000	0.000	-9.412	-10.000
Borrowing at 31 March	96.121	96.121	86.709	76.709
Investments				
Total Investments at 1 April	0.000	0.000	0.000	0.000
Investment change	0.000	0.000	0.000	0.000
Total Investments 31 March	0.000	0.000	0.000	0.000
Net borrowing	96.121	96.121	86.709	76.709

(b) <u>Limits to Borrowing Activity</u>

6. Within the prudential indicators there are a number of key indicators to ensure the Council operates its activities within well defined limits

7. For the first of these the Council needs to ensure that its total borrowing net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2014/15 and the following two financial years. This allows some flexibility for limited early borrowing for future years.

RMBC	2013/14 Revised £m	2014/15 Estimated £m	2015/16 Estimated £m	2016/17 Estimated £m
Borrowing	614.912	608.041	617.585	604.591
Investments	20.000	10.000	10.000	10.000
Net Borrowing	594.912	598.041	607.585	594.591
CFR	754.447	749.856	761.685	750.984
CFR less Net Borrowing	**159.535**	**151.815**	**154.100**	**156.393**

8. The Director of Financial Services reports that the Council has complied with this indicator in the current year and does not envisage difficulties for the future. This view takes into account approved commitments and existing plans.

9. A further two prudential indicators control or anticipate the overall level of borrowing. These are:

10. **The Authorised Limit for External Debt** – This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all council's plans, or those of a specific council, although no control has yet been exercised.

    The Council is asked to approve the following Authorised Limit for RMBC:

Authorised Limit for External Debt (RMBC)	2013/14 Revised £m	2014/15 Estimated £m	2015/16 Estimated £m	2016/17 Estimated £m
Borrowing	645.570	637.971	625.409	624.184
Other long term liabilities	129.338	127.405	137.501	135.375
Total	774.908	765.376	762.910	759.559

Separately, the Council is also limited to a maximum HRA CFR through the HRA self-financing regime. This limit remains unchanged until there is any change in Government legislation.

HRA Debt Limit	2013/14 Revised £m	2014/15 Estimated £m	2015/16 Estimated £m	2016/17 Estimated £m
Total	336.623	336.623	336.623	336.623

The Council is also asked to approve the following Authorised Limit for the former SYCC:

Authorised Limit for External Debt (Former SYCC)	**2013/14 Revised £m**	**2014/15 Estimated £m**	**2015/16 Estimated £m**	**2016/17 Estimated £m**
Borrowing	96.121	96.121	96.121	86.709
Other long term liabilities	0.000	0.000	0.000	0.000
Total	96.121	96.121	96.121	86.709

11. **The Operational Boundary for External Debt** –This is the limit beyond which external borrowing is not normally expected to exceed. In most cases this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual borrowing.

    The Council is asked to approve the following Operational Boundary for RMBC:

Operational Boundary for External Debt (RMBC)	**2013/14 Revised £m**	**2014/15 Estimated £m**	**2015/16 Estimated £m**	**2016/17 Estimated £m**
Borrowing	488.437	487.507	482.424	480.084
Other long term liabilities	129.338	127.405	137.501	135.375
Total	617.775	614.912	619.925	615.459

The Council is also asked to approve the following Operational Boundary for the former SYCC:

Operational Boundary for External Debt (Former SYCC)	**2013/14 Revised £m**	**2014/15 Estimated £m**	**2015/16 Estimated £m**	**2016/17 Estimated £m**
Borrowing	96.121	96.121	96.121	86.709
Other long term liabilities	0.000	0.000	0.000	0.000
Total	96.121	96.121	96.121	86.709

12. Borrowing in Advance of Need - The Council has some flexibility to borrow funds in advance for use in future years. The Director of Financial Services may do this under delegated powers where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or help meet budgetary constraints. Whilst the Director of Financial Services will adopt a prudent approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme or to fund debt maturities.

13. Risks associated with any advance borrowing activity will be subject to appraisal in advance and subsequent reporting through the mid-year and annual reporting mechanism.

14. Debt Rescheduling - As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. These savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

15. The reasons for any rescheduling to take place will include:

- The generation of cash savings and/or discounted cash flow savings;
- Helping to fulfill the treasury strategy; and,
- Enhancing the balance of the portfolio (amending the maturity profile and/or the balance of volatility.

(c) <u>Expected Movement in Interest Rates</u>

16. The Bank Rate, currently 0.50%, underpins investment returns and is not expected to start increasing until the second quarter of 2015. This is despite inflation being around the Monetary Policy Committee inflation target and unemployment approaching 7% at which point the Bank of England had indicated it may consider increasing the rate. The outlook for borrowing rates continues to be uncertain and difficult to predict. Short-term rates to one-year are expected to remain at current levels. The outlook for long-term interest rates continues to be favourable in the near future but is expected to become less so.

17. This challenging outlook has several key treasury management implications:

- Investment returns are likely to remain relatively low during 2014/15
- Borrowing interest rates are currently attractive but are less likely to remain so. The timing of any borrowing will therefore be monitored carefully.
- There will remain a cost of carrying capital – any borrowing undertaken that results in an increase in investments will incur an incremental cost as the cost of borrowing is greater than the likely investment return.

(d) Borrowing and Debt Strategy 2014/15 – 2016/17

18. The Council is currently maintaining an under-borrowed position. This means that the CFR has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is high and will be maintained for the borrowing excluding the HRA reform settlement.

19. The uncertainty over future interest rates increases the inherent risks associated with treasury activity. As a result the Council will continue to take a prudent approach to its treasury strategy.

20. The Director of Financial Services, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the forecast above. It is likely shorter term fixed rates may provide lower cost opportunities in the short to medium term.

(e) Investment Strategy 2014/15 – 2016/17

21. The primary objectives of the Council's investment strategy are:

    - Firstly to safeguard the timely repayment of principal and interest (security);
    - Secondly to ensure adequate liquidity; and,
    - Thirdly to produce an investment return (yield)

22. As part of this Strategy Members need to consider and approve security and liquidity benchmarks in addition to yield benchmarks which are currently widely used to assess investment performance and have previously been reported to Members. The proposed benchmarks are set down in Annex B2.

23. The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle the Council will ensure:

    - It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the Specified and Non-Specified investment sections of Annex B1.

    - It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested as set out in Annex B1.

24. The Director of Financial Services will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council

for approval as necessary. These criteria are different to those which are used to select Specified and Non-Specified investments.

25. The rating criteria use the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution will fall outside the lending criteria. This is in compliance with a CIPFA Treasury Management Panel recommendation in March 2009 and the CIPFA Treasury Management Code of Practice.

26. Credit rating information is supplied by our treasury advisors on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty list. Any rating changes, rating watches (notification of a likely change) and rating outlooks (notification of a possible long term change) are provided to officers almost immediately after they occur and this information is considered before any dealing.

27. The criteria for providing a portfolio of high quality investment counterparties (both Specified and Non-Specified investments) is:

- **Banks –** the Council will use banks which are rated by at least two rating agencies and have at least the following Fitch, Moody's and Standard and Poors' ratings (where rated):

	Fitch	Moody's	Standards & Poor's
Short-term	F1	P-1	A-1
Long-term	A-	A3	A-
Viability	bb+	n/a	n/a
Support	3	n/a	n/a
Financial Strength	n/a	C	n/a

  To allow for the day to day management of the Council's cash flow the Council's bankers, **currently the Co-operative Bank plc** will also be retained on the list of counterparties if ratings fall below the above minimum criteria.

- **Building Societies** – the Council will use the top 20 Building Societies ranked by asset size but restricted to a maximum of 20% of the investment portfolio

- **Money Market Funds** – AAA – restricted to a maximum of 20% of the investment portfolio

- **UK Government** – Debt Management Office

- **UK Single Tier & County Councils** – (i.e. Metropolitan Districts, London Boroughs, County Councils, Unitary Authorities)

A limit of 35% will be applied to the use of Non-Specified investments within the investment portfolio, excluding day to day cash management through the Council's own bank, currently the Co-operative Bank plc.

28. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market and sovereign information will continue to be applied before making any specific investment decision from the agreed portfolio of counterparties.

29. The time and monetary limits for institutions on the Council's Counterparty List are as follows and represent no change from those currently approved (these will cover both Specified and Non-Specified Investments):

	Fitch	Moody's	Standard & Poor's	Money Limit	Time Limit
Upper Limit Category	F1+/AA-	P-1/Aa3	A-1+/AA-	£20m	5years
Middle Limit Category	F1/A-	P-1/A3	A-1/A-	£10m	364 days
Lower Limit Category *	All Building Soc's ranked 1 to 10 All Building Soc's ranked 11 to 20			£5m £1m	6 mths 3 mths
Debt Management Office	-	-	-	Unlimited **	6 months
Money Market Funds ***	-	-	-	£20m	n/a
UK Single Tier & County Councils	-	-	-	£20m	5 years
Council's Bankers	-	-	-	£10m	364 days

The above money limits are exclusive of bank balances held by schools

* Based on maximum of 20% of the investment portfolio

** Provides maximum flexibility

*** Based on maximum of 20% of the investment portfolio

30. The proposed criteria for Specified and Non-Specified investments and monitoring of counterparties are shown in Annex B1 for Member approval.

31. In the normal course of the Council's cash flow operations it is expected that both Specified and Non-specified investments will be utilised for the control of liquidity as both categories allow for short term investments.

32. The use of longer term instruments (greater than one year from inception to repayment) will fall in the Non-specified investment category. These instruments will only be used where the Council's liquidity requirements are safeguarded. This will also be limited by the long term investment limits.

(f) <u>Treasury Management Prudential Indicators and Limits on Activity</u>

33. There are four further treasury activity limits the purpose of which are to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However if these are set to be too restrictive they will impair the opportunities to reduce costs. The limits are:

- Upper limits on fixed interest rate exposure – This identifies a maximum limit for fixed interest rates based upon the fixed debt position net of fixed interest rate investments.

- Upper limits on variable interest rate exposure – as above this limit covers a maximum limit on variable interest rates based upon the variable debt position net of variable interest rate investments.

- Maturity structures of borrowing – These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

- Total funds invested for greater than 364 days – These limits are set to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

For the purposes of these indicators the Council's market debt is treated as fixed. Whilst a percentage of the debt may be subject to variation on specific call dates each year, over the Strategy period any such variations are thought unlikely and the debt can be regarded as fixed.

34. The activity limits (prudential indicators) for Member approval are as follows:

RMBC	2014/15	2015/16	2016/17
Interest rate Exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rate debt based on fixed net debt	100%	100%	100%
Limits on variable interest rate debt based on variable net debt	30%	30%	30%

RMBC Maturity Structure of fixed interest rate borrowing 2014/15		
	Lower	**Upper**
Under 12 months	0%	35%
12 months to 2 years	0%	35%
2 years to 5 years	0%	40%
5 years to 10 years	0%	40%
10 years to 20 years	0%	45%
20 years to 30 years	0%	50%
30 years to 40 years	0%	50%
40 years to 50 years	0%	55%
50 years and above	0%	60%

RMBC Maximum Funds invested > 364 days			
	1 to 2 years	2 to 3 years	3 to 5 years
Funds invested > 364 days	£m 10	£m 8	£m 6

Former SYCC	**2014/15**	**2015/16**	**2016/17**
Interest Rate Exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on total debt	100%	100%	100%
Limits on variable interest rates based on total debt	30%	30%	30%

Former SYCC Maturity Structure of fixed interest rate borrowing 2014/15		
	Lower	**Upper**
Under 12 months	0%	50%
12 months to 2 years	0%	70%
2 years to 5 years	0%	100%
5 years to 10 years	0%	100%

(g) <u>Treasury Performance Indicators</u>

35. The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking. The results of the following two indicators will be reported in the Treasury Annual Report for 2014/15:

- Debt – Borrowing - Average rate of borrowing for the year compared to average available
- Investments – Internal returns above the 7 day London Interbank Bid rate (LIBID) which is the rate at which a bank is willing to borrow from other banks

(h) <u>Policy on the use of external service advisors</u>

36. The Council uses Capita Asset Services a subsidiary of The Capita Group plc as its treasury management advisors.

37. The company provides a range of services which include:

- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments; and,
- Credit rating/market information service comprising the three main credit rating agencies.

38. Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the Council recognises that responsibility for treasury management decisions remains with the Council at all times. The service is provided to the Council under a contractual agreement which is subject to regular review.

Annex B1

Treasury Management Practice (TMP) 1 (5) – Credit and Counterparty Risk Management

1. Overview

The Office of the Deputy Prime Minister (now CLG) issued Revised Investment Guidance in March 2010, and this forms the structure of the Council's policy below.

The key intention of the Guidance is to maintain the current requirement for councils to invest prudently, and that priority is given to security and liquidity before yield.

In order to facilitate this objective the guidance requires this Council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. This Council has adopted the Code will apply its principles to all investment activity.

In accordance with the Code, the Director of Financial Services has reviewed and prepared its treasury management practices. This part, TMP 1(5), covering investment counterparty policy requires approval each year.

2. Annual Investment Strategy

The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of its annual treasury strategy for the following year, covering the identification and approval of the following:

- The guidelines for investment decision making, particularly non-specified investments.
- The principles to be used to determine the maximum periods for which investments can be made.
- The specified investments the Council may use.
- The non-specified investments the Council may use.

This strategy is to be approved by full Council.

The investment policy proposed for the Council is detailed in the paragraphs below.

2.1 Strategy Guidelines

The main strategy guidelines are contained in the body of the treasury strategy statement.

2.2 Specified Investments

These investments are sterling investments of not more than one-year maturity. If they are for a longer period then the Council must have the right to be repaid within 12 months if it wishes.

These are low risk assets where the possibility of loss of principal or investment income is small.

These would include the following investment categories:

1. The UK Government Debt Management Office.

2. UK Single Tier & County Councils – (i.e. Metropolitans District, London Boroughs, County Councils, Unitary Authorities)

3. Money Market Funds that have been awarded AAA credit ratings by Standard and Poor's, Moody's or Fitch rating agencies and restricted to 20% of the overall investment portfolio

4. A bank or a building society that has been awarded a minimum short-term rating of F1 by Fitch, P-1 by Moody's and A-1 by Standard and Poor's rating agencies. For Building Societies investments will be restricted to 20% of the overall investment portfolio and:

   - a maximum of £5m for a period not exceeding 6 months if the society is ranked in the top 10 by asset size; or
   - a maximum of £1m and a period not exceeding 3 months if the society is ranked 11 to 20 by asset size.

2.3 Non-Specified Investments

Non-specified investments are any other type of investment not defined as specified above.

The criteria supporting the selection of these investments and the maximum limits to be applied are set out below.

Non specified investments would include any sterling investments with:

1. A bank that has been awarded a minimum long term credit rating of AA- by Fitch, Aa3 by Moody's and AA- by Standard & Poor's for deposits with a maturity of greater than 1 year.

2. The Council's own bank, currently the Co-operative Bank plc, if ratings fall below the above minimum criteria.

3. A Building Society which is ranked in the top 20 by asset size. Investments will be restricted to 20% of the overall investment portfolio and:

- a maximum of £5m for a period not exceeding 6 months if the Society is ranked in the top 10 by asset size; or
- a maximum of £1m and a period not exceeding 3 months if the Society is ranked 11 to 20 by asset size.

3 The Monitoring of Investment Counterparties

The credit rating of counterparties will be monitored regularly. The Council receives credit rating information from the Council Treasury Management advisors on a daily basis, as and when ratings change, and counterparties are checked promptly.

On occasions ratings may be downgraded after the date on which an investment has been made. It would be expected that a minor downgrading would not affect the full receipt of the principal and interest.

Any counterparty failing to meet the minimum criteria will be removed from the list immediately by the Director of Financial Services, and new counterparties will be added to the list if and when they meet the minimum criteria.

Annex B2

Security, Liquidity and Yield Benchmarking

These benchmarks are targets and so may be exceeded from time to time with any variation reported, with supporting reasons in Mid-Year & Annual Treasury Reports.

1. **Security and liquidity** – these benchmarks are already intrinsic to the approved treasury strategy through the counterparty selection criteria and some of the prudential indicators, e.g. the maximum funds which may be invested for more than 364 days, the limit on the use of Non-specified investments, etc.

1.1 Security – Security is currently evidenced by the application of minimum criteria to investment counterparties, primarily through the use of credit ratings supplied by the three main credit rating agencies. Whilst this approach embodies security considerations, benchmarking the levels of risk is more subjective and therefore problematic.

One method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council's investment strategy.

Credit Rating	1 year	2 years	3 years	4 years	5 years
AAA	0.00%	0.02%	0.06%	0.10%	0.13%
AA	0.02%	0.04%	0.14%	0.28%	0.40%
A	0.09%	0.25%	0.44%	0.62%	0.83%
BBB	0.21%	0.61%	1.07%	1.61%	2.13%

The Council's minimum long term rating criteria (over one year) is "AAA" meaning the average expectation of default for a three year investment in a counterparty with a "AAA" long term rating would be 0.06% of the total investment (e.g. for a £1m investment the average potential loss would be £600).

The Council's minimum long term rating criteria (up to one year) is "BBB" and the average expectation of default for such an investment would be 0.21% (e.g. for a £1m investment the average loss would be £2,100).

These are only averages but do act as a benchmark for risk across the investment portfolio.

The Council's maximum security risk benchmark for the estimated maximum portfolio during 2014/15 is 0.09% which means that for every £1m invested the average potential loss would be £900. This position remains unchanged from 2013/14.

The Council's Treasury advisers maintain a continuous review of the risk position by the inclusion the Council's daily investment position within their online model.

1.2 Liquidity – This is defined as "having adequate, though not excessive cash resources, borrowing arrangements, overdrafts or standby facilities to enable the Council at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives" (CIPFA Treasury Management Code of Practice). The Council seeks to maintain:

- Bank overdraft - £10m
- Liquid, short term deposits of at least £3m available with a week's notice.

The availability of liquidity and the inherent risks arising from the investment periods within the portfolio is monitored using the Weighted Average Life (WAL) of the portfolio. This measures the time period over which half the investment portfolio would have matured and become liquid

A shorter WAL generally represents less risk and in this respect the benchmark to be used for 2014/15 is:

- 0.08 years which means that at any point in time half the investment portfolio would be available within 28 days.

2. **Yield** – These benchmarks are currently widely used to assess investment performance and the Council's local measure of yield is:

- Internal returns above the 7 day London Interbank Bid rate (LIBID) which is the rate at which a bank is willing to borrow from other banks