Members of the Audit Committee:
(Councillors R P Lillis (Chairman), K Mills (Vice Chairman),
P Pilkington, N Thwaites, R Thomas, R Woods, T Venner)

Our Ref: Democratic Services

Contact: Clare Rendell c.rendell@tauntondeane.gov.uk

Date 24 November 2017

THE PRESS AND PUBLIC ARE WELCOME TO ATTEND THE MEETING
THIS DOCUMENT CAN BE MADE AVAILABLE IN LARGE PRINT, BRAILLE, TAPE FORMAT OR IN OTHER LANGUAGES ON REQUEST

Dear Councillor

I hereby give you notice to attend the following meeting:

AUDIT COMMITTEE

Date: **Monday 4 December 2017**

Time: **2.00 pm**

Venue: **Council Chamber, Council Offices, Williton**

Please note that this meeting may be recorded. At the start of the meeting the Chairman will confirm if all or part of the meeting is being recorded.

You should be aware that the Council is a Data Controller under the Data Protection Act. Data collected during the recording will be retained in accordance with the Council's policy.

Therefore unless you advise otherwise, by entering the Council Chamber and speaking during Public Participation you are consenting to being recorded and to the possible use of the sound recording for access via the website or for training purposes. If you have any queries regarding this please contact Committee Services on 01643 703704.

Yours sincerely

BRUCE LANG
Proper Officer

RISK SCORING MATRIX

Report writers score risks in reports uses the scoring matrix below

Risk Scoring Matrix

Likelihood	5	Almost Certain	Low (5)	Medium (10)	High (15)	Very High (20)	Very High (25)
	4	Likely	Low (4)	Medium (8)	Medium (12)	High (16)	Very High (20)
	3	Possible	Low (3)	Low (6)	Medium (9)	Medium (12)	High (15)
	2	Unlikely	Low (2)	Low (4)	Low (6)	Medium (8)	Medium (10)
	1	Rare	Low (1)	Low (2)	Low (3)	Low (4)	Low (5)
			1	2	3	4	5
			Negligible	Minor	Moderate	Major	Catastrophic
			Impact				

Likelihood of risk occurring	Indicator	Description (chance of occurrence)
1. Very Unlikely	May occur in exceptional circumstances	< 10%
2. Slight	Is unlikely to, but could occur at some time	10 – 25%
3. Feasible	Fairly likely to occur at same time	25 – 50%
4. Likely	Likely to occur within the next 1-2 years, or occurs occasionally	50 – 75%
5. Very Likely	Regular occurrence (daily / weekly / monthly)	> 75%

- Mitigating actions for high ('High' or above) scoring risks are to be reflected in Service Plans, managed by the Group Manager and implemented by Service Lead Officers;

- Lower scoring risks will either be accepted with no mitigating actions or included in work plans with appropriate mitigating actions that are managed by Service Lead Officer.

AUDIT COMMITTEE - AGENDA

4 December at 2.00 pm

Council Chamber, West Somerset House, Williton

1. Apologies for Absence

2. Minutes

Minutes of the Meeting of the Committee held on 25 September 2017 – **SEE ATTACHED**.

3. Declarations of Interest

To receive and record any declarations of interest in respect of any matters included the Agenda for consideration at this Meeting.

4. Public Participation

The Chairman to advise the Committee of any items on which members of the public have requested to speak and advise those members of the public present of the details of the Council's public participation scheme.

For those members of the public wishing to speak at this meeting there are a few points you might like to note.

A three-minute time limit applies to each speaker and you will be asked to speak before Councillors debate the issue. There will be no further opportunity for comment at a later stage. Your comments should be addressed to the Chairman and any ruling made the Chair is not open to discussion. If a response is needed it will be given either oral at the meeting or a written reply made within five working days of the meeting.

5. Audit Committee Action Plan

To update the Audit Committee on the progress of resolutions and recommendations from previous meetings.

6. Audit Committee Forward Plan

To review the Audit Committee Forward Plan 2018 – **SEE ATTACHED.**

7. Grant Thornton External Audit – Annual Audit Letter 2016-2017

To consider Report No WSC 135/17 to be presented by Rebecca Usher, Audit Manager from Grant Thornton – **SEE ATTACHED**

The purpose of the report is to summarise the key findings from the external audit work carried out in respect of the 2016/2017 financial year and details the actual audit fees charged.

8. SWAP Internal Audit – Progress Update 2017-2018

To consider Report No WSC 136/17 to be presented by Alastair Woodland, Audit Manager, South West Audit Partnership – **SEE ATTACHED**.

The purpose of the report is to update Members on the Internal Audit Plan 2017-2018 progress and bring to their attention any significant findings identified through our work.

9. Treasury Management Update

To consider Report No WSC 137/17 to be presented by Steve Plenty, Senior Corporate Accountant – **SEE ATTACHED**.

The purpose of the report is to provide Members with an update on the Treasury Management activity of the Council for the first six months of 2017-2018. It focuses on a review of the Council's borrowing and investment activities.

10. New Data Protection Legislation

The Corporate Strategy and Performance Officer will attend to present to Members the details of the new General Data Protection Regulations due to be introduced in May 2018.

11. Transformation Project Update

The Transformation Programme Manager will attend to update Members on the progress being made on the Transformation Project.

COUNCILLORS ARE REMINDED TO CHECK THEIR POST TRAYS

The Council's Vision:

To enable people to live, work and prosper in West Somerset

The Council's Corporate Priorities:

- Local Democracy:
  Securing local democracy and accountability in West Somerset, based in West Somerset, elected by the people of West Somerset and responsible to the people of West Somerset.

- New Nuclear Development at Hinkley Point
  Maximising opportunities for West Somerset communities and businesses to benefit from the development whilst protecting local communities and the environment.

The Council's Core Values:

- Integrity
- Respect
- Fairness
- Trust

AUDIT COMMITTEE

Minutes of the Meeting held on 25 September 2017 at 2.00 pm in the Council Chamber, Williton

Present

Councillor K Mills – Vice Chairman (In the Chair)
Councillor P Pilkington
Councillor R Thomas
Councillor N Thwaites
Councillor R Woods
Councillor T Venner

Members In Attendance

Councillor M Chilcott

Officers In Attendance

Corporate Strategy and Performance Officer (R Doyle)
Finance Manager (J Nacey)
Principal Corporate Accountant (S Plenty)
Democratic Services Officer (C Rendell)

Also In Attendance

Rebecca Usher, Manager, Grant Thornton
Alastair Woodland, Assistant Director, South West Audit Partnership (SWAP)

A.16 Apologies for Absence

Apologies were received from the Chairman (Councillor R Lillis) and Peter Barber, Manager, Grant Thornton.

A.17 Minutes

(Minutes of the Meeting of the Audit Committee held on 20 June 2017, circulated with the Agenda)

RESOLVED that the Minutes of the Audit Committee held on 20 June 2017, be confirmed as a correct record.

A.18 Declarations of Interest

Name	Minute No.	Member of	Personal or Prejudicial	Action Taken
Cllr P Pilkington	All	Timberscombe Parish Council	Personal	Spoke and voted
Cllr R Thomas	All	Minehead Town Council	Personal	Spoke and voted
Cllr N Thwaites	All	Dulverton Town Council	Personal	Spoke and voted
Cllr T Venner	All	Minehead Town Council	Personal	Spoke and voted
Cllr M Chilcott	All	SCC	Personal	Spoke

A.19 Public Participation

No members of the public had requested to speak on any item on the Agenda.

A.20 Audit Committee Action Plan

(Copy of the Audit Committee Action Plan circulated with the Agenda).

There were three recorded actions from the last meeting on 20 June 2017, all of which had been resolved.

During the discussion of this item the following points were made:-

- Members of the Committee requested an explanation, why the date of the meeting was changed and why several of the reports were distributed after the agenda was compiled.
  The Finance Manager apologised and explained this was due to the delay in the Accounts being audited.
- Members queried why the item on the Transformation Project had been pushed back to the December Audit Committee when the original request was made in March.
  It was deemed that the June and September meetings were too soon for the Transformation Team to give a proper update to the Committee.

RESOLVED that the Action Plan be noted.

A.21 Audit Committee Forward Plan

(Copy of the Audit Committee Forward Plan circulated with the Agenda).

RESOLVED that the Audit Committee Forward Plan, with the requested amendments, be noted.

A.22 Grant Thornton External Audit – Audit Findings Report

(Report No. WSC 95/17, circulated with the Agenda).

The purpose of the report was to outline the findings from the audit of the Statement of Accounts and arrangements to secure Value for Money. This also incorporated a review of the financial resilience of the Council.

The Unaudited Statement of Accounts 2016-2017 was signed off by the Council's Section 151 Officer in June 2017.

The external audit review had been completed and the auditor had indicated their intention to issue an ‘unqualified opinion’ for the Statement of Accounts, which showed a true and fair view of the Council’s financial position and performance.

The auditor had also reviewed the arrangements to secure economy, efficiency and effectiveness in the use of resources and provided an opinion in the form of a value for money (VFM) conclusion. Last year the Auditor provided a ‘qualified except for’ VFM conclusion due to the financial challenges the Council faced. This year they had provided an ‘unqualified’ VFM conclusion that recognised the progress in delivering savings but also reiterated the need for transformation savings included in the Medium Term Financial Plan.

In the Executive Summary, the Auditors had identified two non-material adjustments. One related to a classification error of £346,000 of grant income, which management had adjusted for in the final version of the financial statements. The second adjustment related to an error that was identified in a sample testing of revenue expenditure funded from the capital under statue, where one item selected related to 2015-2016.

Within the Audit Findings, it was reported that in the audit plan the overall materiality was £425,000, which was 1.8% of gross revenue expenditure from the 2015-2016 financial statements. During the course of the audit and upon receipt of the 2016-2017 financial statements, it was considered whether this level remained appropriate. The materiality had been adjusted to £409,000 which represented 1.8% of the reported 2016-2017 gross revenue expenditure.

There were five Internal Controls highlighted within the Findings. These were:-

- IT Security Policy and lack of review and acknowledgment by staff;
- No proactive reviews of user access in the Active Directory;
- PPE Valuations;
- Register of Interests; and
- Purchase Orders.

Details of Adjusted Misstatements, Unadjusted Misstatements and Disclosure Changes were also given to the Committee.

During the discussion of this item the following points were made:-

- Members queried the missing Register of Interests reported by the auditors. Was this illegal behaviour which related to the Code of Conduct?
  The Finance Manager explained the different rules and what was classed as illegal.
- Members queried the sample used and how was it carried out.
  The Audit Manager explained the process.
- Members queried why £346,000 was missed out of the report.
  The Audit Manager explained that this was not included because the bottom line had not changed.
- The IT Security Policy was considered along with the relevance of the policy with data breaches that had been reported. Access and security were very different in each Authority.
  Work would be carried out to review and combine the two policies for West Somerset Council (WSC) and Taunton Deane Borough Council (TDBC).

- The EDF settlement was mentioned and although the agreement was not ‘set in stone’, it appeared that WSC was performing better.
  EDF and the Valuation Office Agency had set a figure for the agreement but this could vary and was dependant on the results of the outage.

RESOLVED that Members noted the report from the External Auditor on the Council’s Statement of Accounts and supported the action plan in the report.

A.23 Grant Thornton External Audit – Progress and Update Report

(Report No. WSC 106/17, circulated with the Agenda).

The purpose of the report was to provide an update on the work carried out by the external auditors in 2016-2017 and any emerging national issues.

The Audit Manager outlined the report, which provided an update on the work undertaken to date and included the status of all the planned audit work for the Council. Additionally, the report shared headlines on some national issues that might have an impact upon the Council.

During the discussion of this item the following point was made:-

- Members queried the use of Social Enterprises.
  Research had been carried out on how to develop Social Enterprises for Local Government to help raise money.

RESOLVED that the update report was noted.

A.24 SWAP Internal Audit – Progress Update 2017/2018

(Report No. WSC 96/17, circulated with the Agenda).

The purpose of the report was to update Members on the Internal Audit Plan 2017-2018 progress and bring to their attention any significant findings identified through the work.

The Associate Director for SWAP presented the report and informed the Committee on the changes to the Audit Plan that had occurred since the last update in June 2017.

These were:-

- Due to the refurbishment work at The Deane House, SWAP had been requested to push the Development Control review back from quarter 2 to quarter 4.
- Due to the partial assurance on the Data Protection Act 1998 and the General Data Protection Regulations (GDPR), SWAP had utilised some of the follow up contingency days to programme a review in for quarter 4 which evaluated progress being made on the recommendations and additional requirements contained within the GDPR.

In addition there were also two follow up audits in relation to the Somerset Building Control Partnership (SBCP) and Homelessness.

The SBCP was a partnership between the four Somerset District Councils and had commenced operations in April 2016.

Partial assurance had been given to this review and details of the weaknesses had been reported to the Committee in March 2017.

Since then, SWAP had undertaken a follow up review and could report that eleven of the twelve recommendations made had been implemented. The one recommendation that could not be actioned was due to a coding error and was caused by the online payment system which did not force applicants to enter the district information on the online form. This issue had been resolved and it was expected that the final recommendation would be implemented by the end of September 2017.

The Homelessness final report was issued in October 2016. Partial assurance was given in relation to the areas that had been reviewed and the controls that had been found to be in place. Some key risks were not well managed and systems required the introduction or improvement of internal controls to ensure the achievement of objectives.

A total of eleven recommendations had been made.

Seven of the agreed actions had been assessed as ‘complete’. Two of the agreed actions that were ‘in progress’ were now overdue and therefore revisions to the implementation dates had been agreed.

One of these was a priority four recommendation to ensure the control was in place to mitigate major health and safety risks. When this was reviewed, it had been identified that there was one tenant in a property with a gas oven that did not have a valid gas safety certificate. Whilst an updated control was in place, the weakness here was in relation to human error. The control put in place needed to be enhanced further to ensure all gas appliances were covered, not just gas boilers.

During the discussion of this item the following points were made:-

- Concern was raised on the progress made on the new data protection policy. The Auditor had stated that work should have commenced 12-18 months prior to May 2018, when the policy should be in place.
  Officers had produced a GDPR action plan and attended training, so were able to offer assurance to Members that the work would be completed and in place for May 2018.
- Concern was raised on the gas safety work that had been reported. It had proven difficult to find a gas engineer to inspect properties in the area. Members queried if there was a list of contractors available.
  The Audit Manager confirmed that the Deane DLO would be used in the future. The Finance Manager advised Members that there was a list of contractors and that officers had been told to find the best value for money when selecting a service provider.
- Members noted the ‘Substantial’ result given for the accounts.

RESOLVED that the significant findings and progress made in delivery of the 2017-2018 Internal Audit Plan be noted.

A.25 <u>Approval of the Statement of Accounts</u>

(Report No. WSC 97/17, circulated with the Agenda).

The purpose of the report was to review and approve the audited Statement of Accounts.

The Statement of Accounts for 2016-2017 was required to be approved by the Audit Committee and signed by the Section 151 Officer and the Chairman of the Audit Committee. The Statement of Accounts document was attached to the report for the information of Members.

The Statement of Accounts for 2016-2017 had been prepared on an International Financial Reporting Standards basis in line with the Chartered Institute of Public Finance Accountancy Code of Practice on Local Authority Accounting in the UK 2016-2017.

In 2016-2017 there had been a significant change in the Code of Practice to accounting requirements which meant that income and expenditure had to be reported in the same format that management accounts were presented to the Committee. This also meant that the 2015-2016 figures had to be reinstated in the same format for a comparative purpose. The format change had not affected the outturn figures.

The Finance Manager presented the report and gave an overview of the four main statements contained within the Statement of Accounts under the following headings:-

- Comprehensive Income and Expenditure Statement;
- Movement in Reserves Statement;
- Balance Sheet; and
- Cash Flow Statement.

There were also supplementary statements related to the Collection Fund, which dealt with the collection and distribution of Council Tax and Business Rates.

The report provided the Council's financial position as at 31 March 2017, with comparisons with 31 March 2016. The net assets had remained fairly static at negative £916,000. This would have been a much healthier positive position were it not for the £2,890,000 increase in the Pension Deficit that was reported during the year. The increase in the liability was a result of a change in actuarial assumptions.

During the discussion of this item the following points were made:-

- Members queried if the Council had to use the new format for Income and Expenditure?
  No, this was up to each Council to decide which format they used. This meant there was no continuity between the Councils.
- The Principal Finance Officer advised Members that the system produced the figures in the two different formats and hoped that the new format would be logical for those that were involved in budget monitoring.
- The Finance Manager advised the Committee that the budgets did not appear in the Statement of Accounts compared to the Outturn Report.
- Members praised the Finance Team and the work involved in producing the

Accounts. This was credit to the officers because the issue of pension deficit was out of their control.

- Members queried investments and internal borrowing.
  The majority used was from the CIM funds and this was held in store and other funds were invested in low risk schemes. A breakdown was given in the report.
- Members stated that only external borrowing was reported.
- Members queried if it was possible for the pension deficit to be capitalised.
  The Department of Communities and Local Government had been consulted about this point, but the Council had been told that this was not possible.
- Members queried the external borrowing rates and if these could be used in the future.
  The Finance Manager gave information on Arling Close and the procedures the Finance Team followed.
- Members queried how a deficit could be deemed as a reserve.
  Information was given on how the accounts were presented.
- Did the Government provide pension protection schemes?
  Protection was given to private companies but not the public sector.
- Information was given on the measures taken to protect the pension fund.
- Members requested clarification on the term ‘unqualified’.

RESOLVED that:-

a) Members noted the Auditor’s unqualified opinion on the Statement of Accounts;

b) Members approved the 2016-2017 Statement of Accounts and

c) The Chairman of the Committee be requested to sign the Statement of Accounts.

A.26 Overdue High Priority SWAP Audit Actions

(Report No. WSC 98/17, circulated with the Agenda).

The purpose of the report was to provide the Audit Committee with a position statement on the SWAP audit recommendations for WSC, which were assessed as high and very high priority, where the agreed action was overdue.

The Corporate Strategy and Performance Officer presented the report and highlighted the Priority four and five audit actions that affected WSC, where the agreed remedial action was overdue. There were six priority four actions which were overdue but zero overdue priority five recommendations.

The six priority four actions were:-

- Contract Management Bribery – The Procurement function was not limited enough;
- Contract Management Bribery – No assurance that the contract standing orders and the anti-bribery policy was embedded within the Council;
- Asset Management – Strategy linked to corporate priorities;
- Asset Management – Development of a new Asset Management Plan;
- Creditors 2016-2017 Final Report – Changes to the standing data;
- User and Access Management Final Report – Approval of Physical Access.

During the discussion of this item the following point was made:-

- Members were disappointed that the Corporate Strategy and Performance Officer had to chase officers for the outcomes of the priority four actions.
- Members requested that a column be added to the table to show the Implementation Date and suggested the layout of the table be improved.
- Members queried the result for the Creditors Final Report 2016-2017 and the key control for standing data of existing suppliers.
  The Finance Manager apologised because the relevant officer had not responded by the time the report was published.
- Members requested that the two priority actions on Contract Management Bribery be actioned in time for the next meeting because these actions were already 18 months overdue.

RESOLVED that the overdue actions be reviewed.

A.27 Corporate Governance Action Plan Update

(Report No. WSC 99/17, circulated with the Agenda).

The purpose of the report was to provide an update on the progress made on the Annual Governance Statement (AGS) Action Plan.

The AGS was a statutory document which provided assurance on the governance arrangements in place within the Council.

The AGS included an action plan which addressed any new governance issues identified by the Corporate Governance Officers Group and relied on reports from internal and external audit.

There were two actions now planned for 2017-2018. These were:-

- Review the approach to the Risk Management culture; and
- To prepare the Corporate Governance process for Transformation and the possibility of a new Council.

During the discussion of this item the following points was made:-

- Members queried how far both Councils could progress with the Transformation Project whilst the Government made their decision.
  The Councils would carry on with the assumption of the decision on implementing the New Council being approved.

RESOLVED that the progress in relation to completion of the actions identified within the Annual Governance Statement be noted.

A.28 Corporate Risk Management Update

(Report No. WSC 100/17, circulated with the Agenda).

The purpose of the report was to update the Audit Committee on the corporate risks which were managed by the Joint Management Team (JMT).

The Corporate Risk Register was a 'live' document which highlighted the key corporate risks that the Council faced. This was a joint register between TDBC and WSC and was formally reviewed by JMT on a regular basis as part of the Corporate Performance Review.

These regular reviews ensured that new strategic-level risks could be recognised; continued risks could be re-assessed and risks which were no longer considered important could be removed.

Risks which were managed at a corporate level were those which had a significant risk to the delivery of a corporate priority or which were cross-cutting risks that did not naturally sit with a single department or team.

There were currently fourteen strategic risks identified and approved by JMT. Eleven joint risks, one WSC risk and two TDBC specific risks.

During the discussion of this item the following points were made:-

- The Corporate Strategy and Performance Officer advised the Committee that Data Protection had been added to the report after it had been published.
- It was confirmed that the Data Protection policy applied to the Town and Parish Councils too.
- Members queried why Universal Credit was still included under the risk for Welfare Reforms.
  Universal Credit was still deemed as a new benefit and so the risks were still relevant.
- Members queried how they were made aware that all the corporate risks were included.
  Officers should discuss all relevant risks and recommend to Members what should be reported. The risks on the register were updated regularly.
- Members queried why Gypsies were only a risk in Taunton Deane and not West Somerset.
  Gypsies had only been recognised as a risk within Taunton Deane due to recent behaviour. This would be added as a risk to both Councils.

RESOLVED that the Committee:-

a) Noted the current position in relation to the identification of risks and the corporate risks that had been tracked; and

b) Requested that all the necessary corporate risks, of which they were aware, were detailed in the report.

A.29 WSC Going Concern Assessment

(Report No. WSC 107/17, circulated with the Agenda).

The purpose of the report was to inform the Audit Committee of the Assistant Director - Strategic Finance and Section 151 Officer's assessment of the Council as a 'going concern' for the purposes of producing the Statement of Accounts for 2016-2017.
The concept of a 'going concern' assumed that an Authority, its functions and services,

would continue in operational existence for the foreseeable future. This assumption underpinned the accounts drawn up under the local authority Code of Accounting Practice and was made because local authorities carried out functions essential to the local community and were themselves revenue-raising bodies.

If the assessment determined that the Council was not a 'going concern', particular care would be needed in the valuation of assets, inventories and property, plant and equipment might not be realisable at the book values and provisions might be needed for closure costs or redundancies.

The main factors which underpinned the assessment were:-

- The Council's current financial position;
- The Council's projected financial position;
- The Council's governance arrangements; and
- The regulatory and control environment applicable to the Council as a local authority.

The challenges the Council faced whilst setting a balanced budget and still providing an appropriate level of services to the public, were well documented. The Council had in recent years been extremely susceptible to volatility in its Business Rates funding position in particular with Hinkley Point B power station valuations and its significant changes in the rateable value which had caused large variations to the Council's annual funding.

The financial overview in the draft Statement of Accounts for 2016-2017 included reference to the Council's balance sheet on 31 March 2017 and concluded that it was robust. Factors which gave rise to this assessment included:-

- Review of debts owed to the Council;
- An assessment of the Council's net worth;
- The adequacy of risk-assessed provisions for doubtful debts;
- The range of reserves set aside to help manage expenditure; and
- An adequate risk-assessed General Fund Reserve to meet unforeseen expenditure.

It was considered that the Council remained a 'going concern' until at least September 2018. However, risk and uncertainty remained in view of the reliance upon a stable Business Rates position for Hinkley Point. A large reduction in Business Rates would require emergency measures to secure the financial viability of the Council in the short term and render the Council financially unviable in the medium to long term.

During the discussion of this item the following points were made:-

- Members commented that the accounts had been precarious but looked better for the next year.
- Concern was raised on the future of the Transformation Project.
  Information on the Transformation project agreement was given to Members.

RESOLVED that Members noted the assessment made of the Council's status as a 'going concern' for a basis for preparation of the 2016-2017 Statement of Accounts.

(The meeting closed at 4.32pm)

AUDIT COMMITTEE ACTION PLAN

Date/Minute Number	Action Required	Action Taken
25 September 2017 **A26 – Overdue High Priority SWAP Audit Actions**	**<u>RESOLVED:-</u>** Request was made by Members to add a column in the table to show the Implementation Date and suggested the layout of the table be improved.	The table would be improved ready for the meeting scheduled for the 19 March 2018.
25 September 2017 **A26 – Overdue High Priority SWAP Audit Actions**	**<u>RESOLVED:-</u>** Request was made by Members that the two priority actions on Contract Management Bribery be actioned in time for the next meeting because these actions were already 18 months overdue.	This would be followed up at the meeting scheduled for the 19 March 2018.

West Somerset Council - Audit Committee – Forward Plan 2018

Meeting	DRAFT AGENDA ITEMS	LEAD OFFICER
19 March 2018	Grant Thornton External Audit – Audit Update Grant Thornton External Audit – Audit Plan SWAP Internal Audit – Progress Report 2017/18 SWAP Internal Audit - Audit Plan 2018/19 and Audit Charter Corporate Risk Management Update Corporate Governance Action Plan Summary of Overdue Level 4/5 Actions Powys Counter Fraud Partnership – Update Report Forward Plan	Rebecca Usher Rebecca Usher Alastair Woodland Alastair Woodland Richard Doyle Richard Doyle Richard Doyle Heather Tiso
19 June 2018 - TBC	Grant Thornton External Audit - Audit Fees Grant Thornton External Audit - Audit Update SWAP Internal Audit – Audit Plan 2017/18 Outturn SWAP Internal Audit – Annual Report Review of Effectiveness of Internal Audit 2017/18 Treasury Management Outturn Report Annual Governance Statement 2016/17 Forward Plan	Rebecca Usher Rebecca Usher Alastair Woodland Alastair Woodland Richard Doyle Steve Plenty Richard Doyle
30 July 2018 - TBC	Grant Thornton External Audit – Audit Findings Report Approval of the Statement of Accounts Assessment of Going Concern Status Forward Plan	Rebecca Usher Jo Nacey Jo Nacey
17 Sept 2018 - TBC	Grant Thornton External Audit – Progress & Update Report SWAP Internal Audit – Progress Update 2017/18 Summary of Overdue Level 4/5 Actions Corporate Governance Action Plan Update Corporate Risk Management Update Forward Plan	Rebecca Usher Alastair Woodland Richard Doyle Richard Doyle Richard Doyle
3 Dec 2018 - TBC	Grant Thornton External Audit – Annual Audit Letter 2017/18 Grant Thornton External – Audit Update SWAP Internal Audit – Progress Report 2016/17 6-Month Review of Treasury Management Activity Forward Plan	Rebecca Usher Rebecca Usher Alastair Woodland Steve Plenty

Report Number: WSC 135/17

West Somerset Council

Audit Committee – 4th December 2017

External Audit – Annual Audit Letter for Year Ended 31 March 2017

This matter is the responsibility of Cabinet Member Mandy Chilcott

Report Author: (Jo Nacey, Financial Services Manager)

1 **Purpose of the Report**

1.1 To summarise the key findings from the external audit work carried out in respect of the 2016/17 financial year and details the actual audit fees charged.

1.2 The Annual Audit Letter for 2016/17 confirms that:

- The Auditors have issued an unqualified opinion in respect of the Statement of Accounts for 2016/17;
- The Auditors were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2017;
- The fees charged for 2016/17 were £42,525 in respect of the statutory audit.

2 Recommendations

2.1 That Members are requested to note the report.

3 Risk Assessment (if appropriate)

Risk Matrix

Description	Likelihood	Impact	Overall
The details of any specific risks are contained within the body of the External Auditors report.			

Risk Scoring Matrix

Likelihood	5	Almost Certain	Low (5)	Medium (10)	High (15)	Very High (20)	Very High (25)
	4	Likely	Low (4)	Medium (8)	Medium (12)	High (16)	Very High (20)
	3	Possible	Low (3)	Low (6)	Medium (9)	Medium (12)	High (15)
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	1	Rare	Low (1)	Low (2)	Low (3)	Low (4)	Low (5)
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			Negligible	Minor	Moderate	Major	Catastrophic
			Impact				

Likelihood of risk occurring	**Indicator**	**Description (chance of occurrence)**
1. Very Unlikely	May occur in exceptional circumstances	< 10%
2. Slight	Is unlikely to, but could occur at some time	10 – 25%
3. Feasible	Fairly likely to occur at same time	25 – 50%
4. Likely	Likely to occur within the next 1-2 years, or occurs occasionally	50 – 75%
5. Very Likely	Regular occurrence (daily / weekly / monthly)	> 75%

4 Background and Full details of the Report

4.1 The Council's external audit function is undertaken by Grant Thornton. The external auditors, as part of their work, provide an Annual Update Letter which summarises their findings and provides an update regarding the actual audit fees. The Annual Udit Letter is attached to this report.

5 Links to Corporate Aims / Priorities

5.1 None in relation to this report.

6 Finance / Resource Implications

6.1 The Annual Audit Letter confirms that the external auditors have issued an unqualified opinion in respect of the Council's Statement of Accounts for 2016/17, which means that no material errors were identified and the Accounts were produced to a good standard.

6.2 The auditors have also confirmed that they were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources.

7 Legal Implications

7.1 The Council has a statutory duty to produce financial statements.

8 Environmental Impact Implications

8.1 None in respect of this report.

9 Safeguarding and/or Community Safety Implications

9.1 None in respect of this report.

10 Equality and Diversity Implications

10.1 None in respect of this report.

11 Social Value Implications

11.1 None in respect of this report.

12 Partnership Implications

12.1 None in respect of this report.

13 Health and Wellbeing Implications

13.1 None in respect of this report.

14 Asset Management Implications

14.1 None in respect of this report.

15 Consultation Implications

15.1 None in respect of this report.

Democratic Path:

- **Audit Committee – Yes**
- **Full Council – No**

Reporting Frequency: ☐ **Once only** ☐ **Ad-hoc** ☐ **Quarterly**

X Twice-yearly ☐ **Annually**

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The Annual Audit Letter for West Somerset District Council

Year ended 31 March 2017

October 2017

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Executive summary

Purpose of this letter

Our Annual Audit Letter (Letter) summarises the key findings arising from the work we have carried out at West Somerset District Council (the Council) for the year ended 31 March 2017.

This Letter provides a commentary on the results of our work to the Council and its external stakeholders, and highlights issues we wish to draw to the attention of the public. In preparing this letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice (the Code) and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'.

We reported the detailed findings from our audit work to the Council's Audit Committee (as those charged with governance) in our Audit Findings Report on 25 September 2017.

Our responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on the Council's financial statements (section two)
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money conclusion) (section three).

In our audit of the Council's financial statements, we comply with International Standards on Auditing (UK and Ireland) (ISAs) and other guidance issued by the NAO.

Our work

Financial statements opinion

We gave an unqualified opinion on the Council's financial statements on 26 September 2017.

Value for money conclusion

We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2017. We reflected this in our audit opinion on 26 September 2017.

Certificate

We certified that we had completed the audit of the accounts of West Somerset District Council in accordance with the requirements of the Code on 26 September 2017.

Certification of grants

We also carry out work to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. Our work on this claim is not yet complete and will be finalised by 30 November 2017. We will report the results of this work to the Audit Committee in our Annual Certification Letter.

Working with the Council

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Council's staff.

Grant Thornton UK LLP
October 2017

Audit of the accounts

Our audit approach

Materiality

In our audit of the Council's accounts, we applied the concept of materiality to determine the nature, timing and extent of our work, and to evaluate the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for our audit of the Council's accounts to be £0.409 million, which is 1.8% of the Council's gross revenue expenditure. We used this benchmark, as in our view, users of the Council's accounts are most interested in how it has spent the income it has raised from taxation and grants during the year.

We also set a lower level of specific materiality for members' allowances, auditors' remunerations and senior officer remuneration.

We set a lower threshold of £20,000, above which we reported errors to the Audit Committee in our Audit Findings Report.

The scope of our audit

Our audit involves obtaining enough evidence about the amounts and disclosures in the financial statements to give reasonable assurance they are free from material misstatement, whether caused by fraud or error. This includes assessing whether:

- the Council's accounting policies are appropriate, have been consistently applied and adequately disclosed;
- significant accounting estimates made by the Assistant Director – Strategic Finance are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the narrative report and annual governance statement to check they are consistent with our understanding of the Council and with the accounts included in the Statement of Accounts on which we gave our opinion.

We carry out our audit in line with ISAs (UK and Ireland) and the NAO Code of Audit Practice. We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach was based on a thorough understanding of the Council's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

Audit of the accounts

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of property, plant and equipment The Council revalues its assets on a rolling basis over a five year period. The Code requires that the Council ensures that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements.	• Review of management's processes and assumptions for the calculation of the estimate. • Review of the competence, expertise and objectivity of any management experts used. • Review of the instructions issued to valuation experts and the scope of their work • Discussions with the Council's valuer about the basis on which the valuation was carried out, challenging the key assumptions. • Review and challenge of the information used by the valuer to ensure it was robust and consistent with our understanding. • Testing of revaluations made during the year to ensure they were input correctly into the Council's asset register • Evaluation of the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value.	We reviewed the work of the new valuer and did not identify any issues. We did note that there were £108k of assets that have not been revalued since 2010/11 and that management have not satisfied themselves that there was no significant difference between the carrying value in the FAR and the fair value. We have determined that as the majority of assets were revalued in 2016/17, this is not likely to lead to a material misstatement but note that it is a Code requirement for all Land and Buildings assets to be revalued within a 5 year cycle. We have raised this as a control issue for management to resolve in 2017/18.
Valuation of pension fund net liability The Council's pension fund net liability, as reflected in its balance sheet ,represents a significant estimate in the financial statements.	• Identifying the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessing whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement. • Review of the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation. • Gaining an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made. • Review of the consistency of the pension fund net liability disclosures in notes to the financial statements with the actuarial report from your actuary.	We did not identify any issues to report to Audit Committee.

Audit of the accounts

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Going Concern We had determined that there was a doubt over the completeness and adequacy of the going concern disclosures in the accounts. This was based, at the date of our audit plan, on our review of the Medium Term Financial Plan (MTFP) submitted to Members in February 2017. This highlighted a £900k budget deficit in 2018/19 with no substantive plans in place at address this gap. The proposed New Council with Taunton Deane Borough Council is not expected until April 2019, therefore the gap would remain irrespective of the progress with the New Council. However, subsequent to our initial review, a revaluation of the Hinkley B site has been completed by the Valuation Office (VO). EDF appealed this valuation and following further negotiation agreed on a revised valuation of £21m, significantly more than the £8m used in the February 2017 MTFP. This revised valuation is now reflected in the updated MTFP, which was presented to members in August 2017.	• Review of management's assessment of going concern assumptions and supporting information	We have reviewed the new MTFP to ensure that only the new NDR income has been changed from the MTFP we reviewed in February 17. We have also obtained the VO valuation report to confirm the revised valuation of Hinkley B. We note that this revision to the MTFP leaves a budget shortfall of £130k in 2018/19. Based on the current level of reserves and cash holdings maintained by the Council, we concur with the Council's own assessment that concludes it is a going concern with no material uncertainties, as long as the Transformation savings included in the MTFP are achieved.

Audit of the accounts

Audit opinion

We gave an unqualified opinion on the Council's accounts on 26 September 2017, in advance of the 30 September 2017 national deadline.

The Council made the accounts available for audit in line with the agreed timetable, and provided a good set of supporting working papers. The finance team responded promptly and efficiently to our queries during the audit.

Issues arising from the audit of the accounts

We reported the key issues from our audit of the accounts of the Council to the Council's Audit Committee on 25 September 2017.

Annual Governance Statement and Narrative Report

We are required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website with the draft accounts in line with the national deadlines.

Both documents were prepared in line with the relevant guidance and were consistent with the supporting evidence provided by the Council and with our knowledge of the Council.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice (the Code), following the guidance issued by the NAO in November 2016 which specified the criterion for auditors to evaluate:

In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the key risks where we concentrated our work.

We identified one key risk for West Somerset District Council and the work we performed are set out in table overleaf.

Overall VfM conclusion

We are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2017.

Value for Money

Table: Value for money risk

Risk identified	Work carried out	Findings and conclusions
Medium term financial position, including the implementation of Joint Management and Shared Services (JMASS) and transformation The Council has a balanced financial plan for 2017/18. However, there was a cumulative shortfall of £3.9 million for the subsequent four years of the plan reported to Members in February 2017 when we completed our VFM risk assessment. A subsequent revaluation of Hinkley B's rateable value has led to a material revision of the MTFP, which was resubmitted to Council in August 2017 and showed a revised cumulative £0.8 million shortfall over the four year 2018-2021 period. In order to achieve financial savings and efficiencies, the Council has a shared services agreement with Taunton Deane Borough Council and has completed the implementation and full integration of the workforce. This has already delivered significant financial savings. However, further efficiencies are required, both in terms of utilisation of staff and in the transformation of services. The two councils have proposed to work together as a new Council from 2019 and are awaiting a decision from the Secretary of State.	We reviewed the Council's original and revised medium term financial plan, including the assumptions that underpin the plan – particularly the revised Hinkley B rateable valuation. We reviewed how the Council is progressing the Joint Management and Shared Services arrangement, with a particular emphasis on the transformation of services, as well as reviewing the progress on the proposal to create a new Council.	For 2016/17 the Council budgeted for a breakeven position on its revenue budget. The 2016/17 outturn was a £217k underspend which provides assurance that the Council has good arrangements in place for setting and delivering a realistic and achievable budget. In the current climate of needing to make further savings to secure the longer term financial position of the Council this is very important. We reviewed the medium term financial plan (MTFP) that was presented to the Council in February 2017 and the adequacy of the assumptions used to prepare the MTFP, in particular the planned sources of rates revenue from the Hinkley B power station remaining at the level of the 2010 valuation of £8m. Management, at the time, felt it was more prudent, given the history of appeals against the 2010 valuation, to assume no change in the valuation, even though an updated valuation of £29m have been issued by the Valuation Office (VO) in September 2016. We concluded that the assumptions used by management were appropriate for the current circumstances at the date of our initial review. In March 2017, the Valuation Office (VO) completed a review of the revaluation of the Hinkley B power station, in consultation with EDF, that resulted in a reduction of the 2017 valuation to £21m. This still represents a significant increase in the rateable value of the property from 2010, and a significant budget increase in NDR income expected for the Council, which had not been budgeted in the MTFP submitted in Feb 2017. As a result the Council updated its MTFP in August 2017. We reviewed this updated MTFP and the supporting evidence of the Hinkley B revaluation to ensure that the new calculations were robust. The Council is still reporting a cumulative £0.8 million budget shortfall in the years 2018-2021, this represents a much improved position into the medium term although full financial balance is predicated on and the 'one council' proposal being realised. We have reviewed the current progress of the creation of the new Council and note that the consultation has now been completed with a final decision expected from central government later this year. We do, however, note that the future longer term financial position of the Council is still predicated on the savings expected from the implementation of the New Council. Alternatives include implementation of greater shared working arrangements with Taunton Deane Borough Council or cuts to services. **Whilst significant pressures remain we conclude that, overall, the Council has demonstrated it has appropriate arrangements in place for sustainable resource deployment. Continued close in year monitoring and timely corrective action will be needed to ensure budgets are delivered and service transformation implemented.**

Appendix A: Reports issued and fees

We confirm below our final fees charged for the audit and provision of non-audit services.

Fees

	Proposed fee £	Actual fees £	2015/16 fees £
Statutory audit of Council	42,525	42,525	42,525
Housing Benefit Grant Certification	8,963	TBC	6,996
Total fees (excluding VAT)	**51,488**	**TBC**	**49,521**

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA)

Reports issued

Report	Date issued
Audit Plan	24 February 2017
Audit Findings Report	26 September 2017
Annual Audit Letter	2 October 2017

Fees for other services

Service	Fees £
Audit related services: • Harbour Accounts	**0**
Non-audit services - none	**0**

Non- audit services

- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The table above summarises all other services which were identified.
- We have considered whether other services might be perceived as a threat to our independence as the Council's auditor and have ensured that appropriate safeguards are put in place, as reported in our Audit Findings Report.

Report Number: WSC 136/17

Presented by: Alastair Woodland, Assistant Director
Author of the Report: Alastair Woodland, Assistant Director
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Report to a Meeting of: Audit Committee
To be Held on: 4th December 2017

INTERNAL AUDIT PLAN 2017-18 PROGRESS UPDATE

1. PURPOSE OF REPORT

1.1 To update members on the Internal Audit Plan 2017-18 progress and bring to their attention any significant findings identified through our work.

2. CONTRIBUTION TO CORPORATE PRIORITIES

2.1 Delivery of the corporate objectives requires strong internal control. The attached report provides a summary of the audit work carried out to date this year by the Council's internal auditors, South West Audit Partnership.

3. RECOMMENDATIONS

3.1 Members are asked to note progress made in delivery of the 2017/18 internal audit plan and note the significant findings.

4. RISK ASSESSMENT (IF APPLICABLE)

4.1 Any organisation needs to have a well-established and systematic risk management framework in place to identify and mitigate the risks it may face. WSC has a risk management framework, and within that, individual internal audit reports deal with the specific risk issues that arise from the findings. These are translated into mitigating actions and timetables for management to implement. The most significant findings are reported to this committee in terms of significant corporate risks or in terms of high priority findings at an individual service level.

5. BACKGROUND INFORMATION

This report summarises the work of the Council's Internal Audit Service and provides:

- Details of any new significant weaknesses identified during internal audit work completed since the last report to the committee in September 2017.

- A schedule of audits completed during the period, detailing their respective assurance opinion rating, the number of recommendations and the respective priority rankings of these.

6. FINANCIAL/RESOURCE IMPLICATIONS

6.1 There are no specific finance issues relating to this report.

7. COMMENTS ON BEHALF OF SECTION 151 OFFICER

7.1 No Specific comments.

8. EQUALITY & DIVERSITY IMPLICATIONS

8.1 There are no direct implications from this report.

9. CRIME AND DISORDER IMPLICATIONS

9.1 There are no direct implications from this report.

10. CONSULTATION IMPLICATIONS

10.1 There are no direct implications from this report.

11. ASSET MANAGEMENT IMPLICATIONS

11.1 There are no direct implications from this report.

12. ENVIRONMENTAL IMPACT IMPLICATIONS

12.1 There are no direct implications from this report.

13. HEALTH & WELLBEING

13.1 There are no direct implications from this report.

14. LEGAL IMPLICATIONS

14.1 There are no specific legal issues relating to this report.

SOUTH WEST AUDIT PARTNERSHIP

Delivering Audit Excellence

West Somerset Council

Report of Internal Audit Activity

2017/18 Plan Progress November 2017

Internal Audit ▪ Risk ▪ Special Investigations ▪ Consultancy

Contents

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SWAP work is completed to comply with the International Professional Practices Framework of the Institute of Internal Auditors and the CIPFA Code of Practice for Internal Audit in England and Wales.

Internal Audit Plan Progress 2017/18

Our audit activity is split between:

- **Operational Audit**
- **Governance Audit**
- **Key Control Audit**
- **IT Audit**
- **Grants**
- **Other Reviews**

Role of Internal Audit

The Internal Audit service for West Somerset Council is provided by South West Audit Partnership Limited (SWAP). SWAP is a Local Authority Controlled Company. SWAP has adopted and works to the Standards of the Institute of Internal Auditors, further guided by interpretation provided by the Public Sector Internal Audit Standards (PSIAS), and also follows the CIPFA Code of Practice for Internal Audit. The Partnership is also guided by the Internal Audit Charter approved by the Audit and Governance Committee at its meeting in March 2017.

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

- Operational Audit Reviews
- Cross Cutting Governance Audits
- Annual Review of Key Financial System Controls
- IT Audits
- Grants
- Other Special or Unplanned Review

Internal Audit work is largely driven by an Annual Audit Plan. This is approved by the Section 151 Officer, following consultation with the Corporate Management Team and External Auditors. This year's Audit Plan was reported to this Committee and approved by this Committee at its meeting in March 2017.

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

Internal Audit Plan Progress 2017/18

Outturn to Date:

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

Internal Audit Work

The schedule provided at **Appendix B** contains a list of all audits as agreed in the Annual Audit Plan 2017/18. It is important that Members are aware of the status of all audits and that this information helps them place reliance on the work of Internal Audit and its ability to complete the plan as agreed.

Each completed assignment includes its respective "assurance opinion" rating together with the number and relative ranking of recommendations that have been raised with management. In such cases, the Committee can take assurance that improvement actions have been agreed with management to address these. The assurance opinion ratings have been determined in accordance with the Internal Audit "Audit Framework Definitions" as detailed in **Appendix A** of this document.

Overall good progress is being made on the Audit Plan 2017-18. Current progress as at the end of November can be seen from **Appendix B.**

As agreed with this Committee where a review has a status of 'Final' and has been assessed as 'Partial' or 'No Assurance', I will provide further detail to inform Members of the key issues identified. Since the September 2017 update, there is one Partial Assurance review I need to bring to your attention; this being in relation to Car Parking Maintenance. Whilst this review was given partial assurance, it did not identify any corporate level risks. Further details on these reviews can be found in **Appendix C.**

Internal Audit Plan Progress 2017/18

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

Approved Changes to the Audit Plan

The audit plan for 2017/18 is detailed in **Appendix B**. Inevitably changes to the plan will be required during the year to reflect changing risks and ensure the audit plan remains relevant to West Somerset Council. Members will note that, where necessary, any changes to the plan throughout the year will have been subject to agreement with the appropriate Service Manager and the Audit Client Officer.

Since September 2017 there have been no changes to the Internal Audit Plan 2017-18.

Internal Audit Definitions — APPENDIX A

At the conclusion of audit assignment work each review is awarded a "Control Assurance Definition";

- **Substantial**
- **Reasonable**
- **Partial**
- **No Assurance**

Audit Framework Definitions

Control Assurance Definitions

Substantial	△★★★	I am able to offer substantial assurance as the areas reviewed were found to be adequately controlled. Internal controls are in place and operating effectively and risks against the achievement of objectives are well managed.
Reasonable	△★★☆	I am able to offer reasonable assurance as most of the areas reviewed were found to be adequately controlled. Generally, risks are well managed, but some systems require the introduction or improvement of internal controls to ensure the achievement of objectives.
Partial	△★☆☆	I am able to offer Partial assurance in relation to the areas reviewed and the controls found to be in place. Some key risks are not well managed, and systems require the introduction or improvement of internal controls to ensure the achievement of objectives.
No Assurance	▲☆☆☆	I am not able to offer any assurance. The areas reviewed were found to be inadequately controlled. Risks are not well managed, and systems require the introduction or improvement of internal controls to ensure the achievement of objectives.

Non-Opinion/Advice – In addition to our opinion based work we will provide consultancy services. The "advice" offered by Internal Audit in its consultancy role may include risk analysis and evaluation, developing potential solutions to problems and providing controls assurance. Consultancy services from Internal Audit offer management the added benefit of being delivered by people with a good understanding of the overall risk, control and governance concerns and priorities of the organisation.

Internal Audit Definitions APPENDIX A

Recommendation are prioritised from 1 to 5 on how important they are to the service/area audited. These are not necessarily how important they are to the organisation at a corporate level.

Each audit covers key risks. Each audit a risk assessment is undertaken whereby with management risks for the review are assessed at the Corporate inherent level (the risk of exposure with no controls in place) and then once the audit is complete the Auditors assessment of the risk exposure at Corporate level after the control environment has been tested. All assessments are made against the risk appetite agreed by the SWAP Management Board.

Audit Framework Definitions

Categorisation of Recommendations

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

- Priority 5: Findings that are fundamental to the integrity of the unit's business processes and require the immediate attention of management.
- Priority 4: Important findings that need to be resolved by management.
- Priority 3: The accuracy of records is at risk and requires attention.
- Priority 2: Minor control issues have been identified which nevertheless need to be addressed.
- Priority 1: Administrative errors identified that should be corrected. Simple, no-cost measures would serve to enhance an existing control.

Definitions of Risk

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

Internal Audit Work Plan APPENDIX B

Audit Type	Audit Area	Quarter	Status	Opinion	No of Rec	1 = Minor ↔ 5 = Major Recommendation 1	2	3	4	5	Comments
FINAL											
Governance, Fraud & Corruption	Compliance with IR35	Q1	Final	Reasonable	4	0	0	4	0	0	
Follow Up	Licensing Follow Up	Q1	Final	Follow Up	4	0	0	4	0	0	Reported June 2017
Follow Up	Building Control follow up	Q1	Final	Follow Up	1	0	0	1	0	0	Reported September 2017
Follow Up	Homelessness Follow Up	Q1	Final	Follow Up	4	0	0	3	1	0	Reported September 2017
Operational Audit	Parking maintenance	Q1	Final	Partial	6	0	0	3	3	0	Details in Appendix C
Operational Audit	Grants - DFG & Other	Q2	Final	Reasonable	7	0	1	6	0	0	
DRAFT											
Governance, Fraud & Corruption	Organised Crime - Compliance Checklist	Q2	Drafting								
Follow Up	User Access Management follow up	Q2	Drafting								
Key Control	Discretionary Payments - Housing	Q3	Draft	Reasonable							
IN PROGRESS											
Governance, Fraud & Corruption	Transformation	Q1, Q2, Q3, Q4	In Progress								
Key Control	Main Accounting	Q3	In Progress								

Internal Audit Work Plan APPENDIX B

Audit Type	Audit Area	Quarter	Status	Opinion	No of Rec	1 = Minor ↔ 5 = Major Recommendation 1	2	3	4	5	Comments
Key Control	Creditors	Q3	In Progress								
Key Control	Debtors	Q3	In Progress								
Governance, Fraud & Corruption	Business Rate Avoidance	Q3	In Progress								
Governance, Fraud & Corruption	Culture & Ethics Survey	Q4	In Progress								
NOT STARTED											
Operational Audit	Development Control	Q4									
ICT	Cyber Security	Q4									
ICT	Back Ups	Q4									
Key Control	System Parameter testing Civica	Q4									
Governance, Fraud & Corruption	GDPR	Q4									
Governance, Fraud & Corruption	Procurement Analysis	Q4									

Summary of Key Audit Findings APPENDIX C

Audit Assignments completed since the September 2017 update:

These are actions that we have identified as being high priority and that we believe should be brought to the attention of the Audit Committee.

Summary of Audit Findings and High Priority Service Findings

The following information provides a brief summary of each audit review finalised since the last Committee update in September 2017. Each audit review is displayed under the relevant audit type, i.e. Operational; Key Control; Governance; Fraud & Corruption; ICT, Follow Up and Special Review.

Since the September 2017 update, there is one 'Partial' Assurance audit opinion that I need to bring to your attention.

Operational Audits

Operational audits are a detailed evaluation of a Service's control environment. A risk matrix is devised, and controls are tested that mitigate those risks. Where weaknesses or areas for improvement are identified, actions are agreed with management and target dated.

Car Parking Maintenance – Partial Assurance Audit

The objective of this review was to ensure that the Parking Maintenance Plan takes into consideration the commitments within the Growth Agenda; that money is spent wisely, and health and safety risks are controlled effectively.

This is the first time that car parking maintenance has been looked at since Taunton Deane Borough Council and West Somerset Council decided to align services under one management structure.

Testing has identified a key concern with regards to Management's knowledge of the car parking maintenance budget for West Somerset. While we have identified there is a sufficient budget for high priority repairs to be undertaken, during the course of this audit we were provided with three different figures that varied by £66.6k.

Summary of Key Audit Findings

APPENDIX C

Audit Assignments completed since the September 2017 update:

These are actions that we have identified as being high priority and that we believe should be brought to the attention of the Audit Committee.

Operational Audits Continued

Further concerns were established with regards to the car parking strategies for each district. While there are strategies in place for each Council, the document for West Somerset is out of date and the version for Taunton Deane is being updated by Parsons Brinkerhoff. A lack of direction does not help focus car park maintenance activities across both districts.

Concerns were also identified with regards to the failure to utilise the corporate risk management approach and an inadequate methodology for the assessment of risks to car parks. Current processes are based on a subjective assessment of health and safety.

While Parking Maintenance Plans are in place for each district, they require updates. A further detailed and accurately costed Programme of Works is needed for the Orchard Multi-Storey Car Park in Taunton.

As with all Partial and No Assurance reviews, a follow up audit will be scheduled to confirm appropriate action has been taken to address the weaknesses identified.

Report Number: WSC 137/17

West Somerset Council

Audit Committee – 4th December 2017

Treasury Management Update – 30th September 2017

This matter is the responsibility of Cabinet Member Mandy Chilcott

Report Author: (Steve Plenty, Senior Corporate Accountant)

1 **Purpose of the Report**

1.1 To provide Members with an update on the Treasury Management activity of the Council for the first six months of 2017/18. It focuses on a review of the Council's borrowing and investment activities.

2 Recommendations

2.1 To note the Treasury Management position as at 30th September 2017 (Appendix A attached to this report).

3 Risk Assessment (if appropriate)

Risk Matrix

Description	Likelihood	Impact	Overall
The Council fails to maintain an adequate system of internal control.	2	3	6
The Council has an approved Treasury Management Strategy Statement and effective management practices to ensure compliance	1	2	2

Risk Scoring Matrix

Likelihood	5	Almost Certain	Low (5)	Medium (10)	High (15)	Very High (20)	Very High (25)
	4	Likely	Low (4)	Medium (8)	Medium (12)	High (16)	Very High (20)
	3	Possible	Low (3)	Low (6)	Medium (9)	Medium (12)	High (15)
	2	Unlikely	Low (2)	Low (4)	Low (6)	Medium (8)	Medium (10)
	1	Rare	Low (1)	Low (2)	Low (3)	Low (4)	Low (5)
			1	2	3	4	5
			Negligible	Minor	Moderate	Major	Catastrophic
			Impact				

Likelihood of risk occurring	Indicator	Description (chance of occurrence)
1. Very Unlikely	May occur in exceptional circumstances	< 10%
2. Slight	Is unlikely to, but could occur at some time	10 – 25%
3. Feasible	Fairly likely to occur at same time	25 – 50%
4. Likely	Likely to occur within the next 1-2 years, or occurs occasionally	50 – 75%
5. Very Likely	Regular occurrence (daily / weekly / monthly)	> 75%

4 Background and Full details of the Report

4.1 On 22nd February 2017 the Council approved the Treasury Management Strategy Statement, Minimum Revenue Policy and Annual Investment Strategy for 2017/18 in line with the CLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

4.2 The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals. These reports are required to be adequately scrutinised by committee before being recommended to the Council. This role is undertaken by the Audit Committee.

5 Links to Corporate Aims / Priorities

5.1 None in relation to this report.

6 Finance / Resource Implications

6.1 Investment income is predicted to be £0.004m below the budget of £0.032m for the financial year 2017/18.

6.2 The Council currently has no external loans and is not predicting the need to borrow externally for the remainder of the 2017/18 financial year, however finance officers will continue to monitor this closely.

7 Legal Implications

7.1 The Section 151 Officer has a legal requirement to ensure appropriate arrangements are in place to adequately control the Council's resources.

8 Environmental Impact Implications

8.1 None in respect of this report.

9 Safeguarding and/or Community Safety Implications

9.1 None in respect of this report.

10 Equality and Diversity Implications

10.1 None in respect of this report.

11 Social Value Implications

11.1 None in respect of this report.

12 Partnership Implications

12.1 None in respect of this report.

13 Health and Wellbeing Implications

13.1 None in respect of this report.

14 Asset Management Implications

14.1 None in respect of this report.

15 Consultation Implications

15.1 None in respect of this report.

Democratic Path:

- **Audit Committee – Yes**
- **Full Council – Yes**

Reporting Frequency: **X Once only** ☐ **Ad-hoc** ☐ **Quarterly**

☐ **Twice-yearly** ☐ **Annually**

List of Appendices

Appendix A	Treasury Management Update – 30th September 2017

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Treasury Management Update
Six Months Ended 30th September 2017

1. Introduction

The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that Authorities report on the performance of the treasury management function at least twice yearly (mid-year and at year end).

The Council's treasury management strategy for 2017/18 was approved at a meeting of Full Council on 22nd February 2017 which can be accessed on the website at the following address:
https://www.westsomersetonline.gov.uk/Council---Democracy/Council-Meetings/Full-Council/Full-Council---22-February-2017

The Authority has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

2. External Context

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

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

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

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

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

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

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

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

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

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

There were a few credit rating changes during the quarter. The significant change was the downgrade by Moody's to the UK sovereign rating in September from Aa1 to Aa2 which resulted in subsequent downgrades to sub-sovereign entities including local authorities. Moody's downgraded Standard Chartered Bank's long-term rating to A1 from Aa3 on the expectation that the bank's profitability will be lower following management's efforts to de-risk their balance sheet. The agency also affirmed Royal Bank of Scotland's and NatWest's long-term ratings at Baa1, placed Lloyds Bank's A1 rating on review for upgrade, revised the outlook of Santander UK plc, and Nationwide and Coventry building societies from negative to stable but downgraded the long-term rating of Leeds BS from A2 to A3. The agency downgraded long-term ratings of the major Canadian banks on the expectation of a more challenging operating environment and the ratings of the large Australian banks on its view of the rising risks from their exposure to the Australian housing market and the elevated proportion of lending to residential property investors.

S&P also revised Nordea Bank's outlook to stable from negative, whilst affirming their long-term rating at AA-. The agency also upgraded the long-term rating of ING Bank from A to A+.

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

The new EU regulations for Money Market Funds were finally approved and published in July and existing funds will have to be compliant by no later than 21st January 2019. The key features include Low Volatility NAV (LVNAV) Money Market

Funds which will be permitted to maintain a constant dealing NAV, providing they meet strict new criteria and minimum liquidity requirements. MMFs will not be prohibited from having an external fund rating (as had been suggested in draft regulations). Arlingclose expects most of the short-term MMFs it recommends to convert to the LVNAV structure and awaits confirmation from each fund.

Low Volatility Net Asset Value (LVNAV) money market funds are similar to Constant Net Asset Value (CNAV) funds in the following ways:

- LVNAV's will be able to invest in securities rated AAA – A, the same as CNAV's
- The maximum weighted average maturity will remain at 60 days.

A LVNAV fund will differ from a CNAV fund in the following ways:

- NAV tolerance for an LVNAV fund will be 99.8p whereas in a current CNAV fund it is 99.5p. In Layman's terms this means that to be priced at £1, the fund price will need to be between 99.8p and 100.2p instead of between 99.5p and 100.5p. Effectively the 'band' in which the price has to fall for it to be still priced at £1 has been narrowed.
- Daily liquidity requirements for an LVNAV fund will be 10%, instead of the 0% for a current CNAV fund. In other words, the fund has to hold 10% of its assets overnight. This will likely effect the return of the LVNAV fund as overnight investments tend to yield less than long dated investments.
- Weekly liquidity requirements for a LVNAV fund will be 30%, as opposed to the current 20% allowed for a CNAV fund.
- Sponsor support will also be banned for a LVNAV fund, which is not the case for CNAV funds. This means that if a LVNAV fund is in 'distress', the sponsor company (Amundi, Standard Life, Investec to name a few) cannot put their own money in to help the fund out.

Due to the heightened liquidity requirements, a LVNAV fund is likely to yield slightly less than the current CNAV fund and it is estimated that it will be approximately 5bp less, although this will have to be seen.

3. MiFID II

Local authorities are currently treated by regulated financial services firms as professional clients who can "opt down" to be treated as retail clients instead. But from 3rd January 2018, as a result of the second Markets in Financial Instruments Directive (MiFID II) local authorities will be treated as retail clients who can "opt up" to be professional clients, providing that they meet certain criteria. Regulated financial services firms includes banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments. In order to opt up to professional, the authority must have an investment balance of at least £10 million, and the person authorised to make investment decisions on behalf of the authority must have at least one year's relevant professional experience. In addition, the firm must assess that that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved.

The main additional protection for retail clients is a duty on the firm to ensure that the investment is "suitable" for the client. However, local authorities are not protected by the Financial Services Compensation Scheme and are not eligible to complain to the Financial Ombudsman Service, whether they are retail or professional clients It is also likely that the authority will face an increased cost and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and financial advice. The Authority has declined to opt down to retail client status in the past as the costs were thought to outweigh the benefits.

The Council expects to meet the conditions to opt up to professional status and intends to do so in order to maintain their current MiFID status.

CIPFA Consultation on Prudential and Treasury Management Codes

In February 2017 the Chartered Institute of Public Finance and Accountancy (CIPFA) canvassed views on the relevance, adoption and practical application of the Treasury Management and Prudential Codes and after reviewing responses launched a further consultation on changes to the codes in August 2017. A final decision on changes is expected in December 2017.

The proposed changes to the Prudential Codes include the production of a new high level Capital Strategy report to full council which will cover the basics of the capital programme and treasury management. The prudential indicators for capital expenditure and the authorised borrowing limit would be included in this report but other indicators may be delegated to another committee. There are plans to drop certain prudential indicators, however local indicators are recommended for ring fenced funds (including the HRA) and for group accounts.

Proposed changes to the Treasury Management Code include the potential for currently non-treasury investments such as commercial investments in properties, loans made or shares brought for service purposes and financial guarantees to be brought under the Treasury Management Strategy. Approval of the Treasury Management Strategy may be delegated to a committee rather than needing approval of the full council. There are plans to drop or alter some of the current treasury management indicators.

CIPFA intends to publish the two revised Codes towards the end of 2017 for implementation in 2018/19, although CIPFA plans to put transitional arrangements in place for reports that are required to be approved before the start of the 2018/19 financial year. The Department of Communities and Local Government (DCLG) and

CIPFA wish to have a more rigorous framework in place for the treatment of commercial investments as soon as is practical. It is understood that DCLG will be revising its Investment Guidance (and its MRP guidance) for local authorities in England; however there have been no discussions with the devolved administrations yet.

4. Local Context

On 31st March 2017, the Council's underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in the table below.

Balance Sheet Summary

	31.3.17 Actual £000
General Fund CFR	5,347
Less: Usable reserves	(6,840)
Less: Working capital	(13,932)
Net Investments	**(15,425)**

The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep interest costs low.

The treasury management position as at 30th September 2017 and the change in the first six months of 2017/18 is shown in table below.

Treasury Management Summary

	31.03.17 Balance £000	Movement £000	30.09.17 Balance £000	30.09.17 Rate %
Long-term borrowing	0	0	0	N/A
Short-term borrowing	0	0	0	N/A
Total borrowing	**0**	**0**	**0**	
Long-term investments	499	(499)	0	N/A
Short-term investments	12,392	1,241	13,633	0.29
Cash and cash equivalents	4,097	1,438	5,535	0.13
Total investments	**16,988**	**2,180**	**19,168**	**0.23**
Net Investments	**16,988**	**2,180**	**19,168**	

5. Borrowing Strategy during the half year

At 30th September 2017 the Council held no external loans, this position remains unchanged from that reported at 31 March 2017 as part of the Treasury Management Outturn Report. The Council does not expect to borrow externally in the remainder of 2017/18.

Borrowing Activity in 2017/18

	Balance on 01/04/2017 £000	MRP £000	Maturing Debt £000	New Borrowing £000	Balance on 30/09/2017 £000
CFR	5,347	(143)	0	0	5,204

6. Investment Activity

The Council holds invested funds on its own behalf with a separate fund in respect of the Section 106 Agreement it has with EDF relating to the building of Hinkley C Nuclear Power Station representing income received in advance of expenditure plus balances and reserves held. Cash flow forecasts indicate that during 2017/18 the Council's investment balances would range between £15.89m and £22.16m combining the General Fund and the Section 106 'Hinkley Funds'.

Investment Position

	31.03.17 Balance £000	Movement £000	30.09.17 Balance £000	30.09.17 Average Rate %
Banks & building societies (unsecured)	376	559	935	0.11
Covered bonds (secured)	3,000	(500)	2,500	0.57
Government (incl. local authorities)	3,635	965	4,600	0.22
Money Market Funds	9,874	1,259	11,133	0.10
Total investments	**16,885**	**2,283**	**19,168**	

Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's main objective when investing money is the security of capital. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2017/18.

Credit Risk

The table below shows counterparty credit quality as measured by credit ratings and the percentage of the in-house investment portfolio exposed to bail-in risk. This is an extract from Arlingclose's quarterly investment benchmarking.

Investment Benchmarking

	Average Credit Score	Average Credit Rating	Bail-in Exposure	Average Credit Rating – Time Weighted	Rate of Return
31.03.2017	2.95	AA	24%	AAA	0.23%
30.06.2017	3.03	AA	24%	AA+	0.19%
30.09.2017	3.27	AA	29%	AA+	0.18%
Similar LAs	4.39	AA-	65%	AA-	1.43%
All LAs	4.44	AA-	64%	AA-	1.12%

Scoring:
-Value weighted average reflects the credit quality of investments according to the size of the deposit
-Time weighted average reflects the credit quality of investments according to the maturity of the deposit
-AAA = highest credit quality = 1
- D = lowest credit quality = 26
-Aim = A- or higher credit rating, with a score of 7 or lower, to reflect current investment approach with main focus on security

Budgeted Income and Expenditure

The average cash balances were £19.68m during the period. The UK Bank Rate had been maintained at 0.5% since March 2009 until August 2016, when it was cut to 0.25%.

New investments on an unsecured basis with banks over the 6-month period were made at an average rate of 0.11%. Investments in Money Market Funds generated an average rate of 0.22%, investments with the Debt Management Office (DMO) generated an average of 0.10%, and investments placed in Covered Floating Rate Notes generated an average of 0.57%.
The Authority's budgeted investment income for the year is £0.032m with forecast returns predicted to be £0.028m. Investment income in respect of Hinkley S106 funds are ring-fenced and added to the S106 Account.

Compliance Report

The Assistant Director – Strategic Finance is pleased to report that all treasury management activities undertaken during the first half of 2017/18 complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in the table below.

Investment Limits

	Maximum	30.09.17 Actual	2017/18 Limit	Complied
Any single organisation, including Supernational and Sovereign Agencies, except the UK Government and UK Local Authorities	£2m	£2m	£2m	✓
UK Government	£11.13m	£11.13m	Unlimited	✓
Any group of organisations under the same ownership (Except UK Government)	£2m	£2m	£2m per Group	✓
Any group of pooled funds under the same management	£0m	£0m	£2m per Manager	✓
Negotiable instruments held in a broker's nominated account	£3m	£2.5m	£5m per Broker	✓
Foreign Banks (Excluding Supernational Organisations)	£2m	£2m	£2m per Country	✓
Registered providers	£0m	£0m	£5m in Total	✓
Loans to unrated corporates	£0m	£0m	£2m in Total	✓
Money Market Funds	£6m	£4.6m	£10m in Total	✓

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

Debt Limits

	Maximum £m	30.09.17 Actual £m	2017/18 Operational Boundary £m	2017/18 Authorised Limit £m	Complied
Borrowing	0	0	12	24	✓
Total Debt	**0**	**0**	**12**	**24**	✓

Treasury Management Indicators 2017/18

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

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	30.09.17 Actual	2017/18 Target	Complied
Portfolio average credit rating	AA	A-	✓

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

	30.09.17 Actual	2017/18 Target	Complied
Total cash available within 3 months	17.7m	3.5m	✓

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

	30.09.17 Actual %	2017/18 Limit %	Complied
Upper limit on fixed interest rate exposure	58	100	✓
Upper limit on variable interest rate exposure	42	100	✓

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

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

	30.09.17 Actual %	Upper Limit %	Lower Limit %	Complied

Under 12 months	0	100	0	✓
12 months and within 24 months	0	100	0	✓
24 months and within 5 years	0	100	0	✓
5 years and within 10 years	0	100	0	✓
10 years and above	0	100	0	✓

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

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

	2017/18 £m	**2018/19 £m**	**2019/20 £m**
Actual principal invested beyond year end	0.5	0.0	0.0
Limit on principal invested beyond year end	6.0	6.0	6.0
Complied	✓	✓	✓

7. Outlook for the remainder of 2017/18

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

The Bank of England's Monetary Policy Committee has changed its rhetoric, implying a rise in Bank Rate in "the coming months". Arlingclose is not convinced the UK's economic outlook justifies such a move at this stage, but the Bank's interpretation of the data seems to have shifted.

This decision is still very data dependant and Arlingclose is, for now, maintaining its central case for Bank Rate at 0.25% whilst introducing near-term upside risks to the forecast as shown below. Arlingclose's central case is for gilt yields to remain broadly stable in the across the medium term, but there may be near term volatility due to shifts in interest rate expectations.

	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
Official Bank Rate													
Upside risk	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**
Downside risk	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25

Prudential Indicators 2017/18

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

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

Capital Expenditure and Financing	**2016/17 Actual £000**	**2017/18 Estimate £000**
Steam Coast Trail Project	294	102
Asset Disposal / Demolition Costs	29	67
Play Spaces	17	
Transformation		470
Disabled Facilities Grants	244	332
Hinkley Impact Mitigation Projects	1,016	2,218
S106 General Schemes		50
Affordable Housing		124
Capital Sustainability		64
Superfast Broadband		70
Other Schemes	67	105
Total Capital Expenditure	**1,667**	**3,602**
Capital Receipts	(23)	(773)
Capital Grants	(545)	(439)
Revenue Contributions	(9)	(122)
S106 General	(74)	(50)
S106 Hinkley	(1,016)	(2,218)
Total Capital Financing	**(1,667)**	**(3,602)**

Estimates of Capital Financing Requirement: The Capital Financing Requirement (CFR) measures the Authority's underlying need to borrow for a capital purposes.

Capital Financing Requirement	**31.03.17 Actual £m**	**31.03.18 Estimate £m**	**31.03.19 Estimate £m**	**31.03.20 Estimate £m**
General Fund	5,347	5,204	5,061	4,918

The CFR is forecast to fall over the next three years as capital expenditure financed by debt (currently forecast to be £nil) is outweighed by resources put aside for debt repayment.

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

Debt	**31.03.17 Actual £000**	**30.09.17 Actual £000**	**31.03.18 Estimate £000**	**31.03.19 Estimate £000**	**31.03.20 Estimate £000**
Borrowing	0	0	0	0	0

Total debt is expected to remain below the CFR during the forecast period.

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

Ratio of Financing Costs to Net Revenue Stream	**2016/17 Actual %**	**2017/18 Estimate %**	**2018/19 Estimate %**	**2019/20 Estimate %**
General Fund	-0.53	-0.38	1.39	1.39

The actual ratio for 2016/17 and the estimated ratio for 2017/18 are negative due to the Council having no debt to service (no interest to pay on borrowing) and a capital programme which does not impact on the revenue budget.

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

Incremental Impact of Capital Investment Decisions	**2017/18 Estimate £**	**2018/19 Estimate £**	**2019/20 Estimate £**
General Fund – Increase in annual Band D Council Tax	0	0	0

Adoption of the CIPFA Treasury Management Code: The Authority adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* in March 2012.