Audit and Governance Committee

Members are asked to attend a private training session at 6 pm in the Civic Suite immediately before the meeting

Meeting: Monday, 17th March 2014 at 6.30 pm in Civic Suite, North Warehouse, The Docks, Gloucester, GL1 2EP

Membership:	Cllrs. Wilson (Chair), Hobbs (Vice-Chair), McLellan, Noakes, Llewellyn, Porter and Gilson
Contact:	Parvati Diyar Democratic Services Officer 01452 396192 Parvati.Diyar@gloucester.gov.uk

AGENDA	
1.	**APOLOGIES** To receive any apologies for absence.
2.	**DECLARATIONS OF INTEREST** To receive from Members, declarations of the existence of any disclosable pecuniary, or non-pecuniary, interests and the nature of those interests in relation to any agenda item. Please see Agenda Notes.
3.	**MINUTES** (Pages 7 - 18) To approve as a correct record the minutes of the meeting held on 25 November 2013.
4.	**MINUTES OF SPECIAL AUDIT AND GOVERNANCE COMMITTEE** (Pages 19 - 20) To approve as a correct record the minutes of the special meeting held on 27 January 2014.

5.	**PUBLIC QUESTION TIME (15 MINUTES)** To receive any questions from members of the public provided that a question does not relate to: • Matters which are the subject of current or pending legal proceedings, or • Matters relating to employees or former employees of the Council or comments in respect of individual Council Officers
6.	**PETITIONS AND DEPUTATIONS (15 MINUTES)** To receive any petitions and deputations provided that no such petition is in relation to: • Matters relating to individual Council Officers, or • Matters relating to current or pending legal proceedings
7.	**RESPONSE TO INTERNAL AUDIT REPORT RECOMMENDATIONS - RESPONSE REPAIRS CONTRACT** To receive the report of the Asset Manager, as requested by the Committee, relating to the implementation of agreed internal audit recommendations. **Please note that this document will be published as a separate supplement to the agenda when it is available.**
8.	**STREETCARE MONITORING SHEET MARCH 2014** (Pages 21 - 30) To receive the Streetcare Contract Monitoring sheet provided by the Head of Neighbourhood Services, as requested by the Committee, relating to the implementation of agreed internal audit recommendations.
9.	**AUDIT AND GOVERNANCE COMMITTEE ACTION PLAN** (Pages 31 - 34) To consider the Action Plan.
10.	**KPMG CERTIFICATION OF GRANTS AND RETURNS 2012/13** (Pages 35 - 42) To receive the report of Darren Gilbert, KPMG.
11.	**EXTERNAL AUDIT PLAN 2013/14** (Pages 43 - 72) To receive the report of Darren Gilbert, KPMG.
12.	**BUDGET MONITORING - MONTH 9** To receive the report of the Director of Resources which informs Members of the predicted

	year-end financial position based on an analysis of the year to date. **Please note that this document will be published as a separate supplement to the agenda when it is available.**
13.	**TREASURY MANAGEMENT UPDATE - QUARTER 3 REPORT 2013/14** (Pages 73 - 88) To receive the report of the Director of Resources which updates Members on treasury management activities for the period 1 October 2013 to 31 December 2013.
14.	**TREASURY MANAGEMENT STRATEGY 2014/15** (Pages 89 - 122) To receive the report of the report of the Director of Resources which sets out the Council's Treasury Management Strategy, the Prudential Indicators and Treasury activities.
15.	**INTERNAL AUDIT PLAN - 2013/14 MONITORING REPORT** (Pages 123 - 134) To receive the report of the Audit, Risk and Assurance Manager which informs Members of the audits completed as part of the approved Internal Audit Plan 2013/14.
16.	**INTERNAL AUDIT PLAN 2014/15** (Pages 135 - 142) To receive the report of the Audit, Risk and Assurance Manager which presents to Members for their consideration and approval, the Internal Audit Plan 2014/15.
17.	**UPDATE ON PEER REVIEW** To receive the report of the Chief Executive. **Please note that this document will be published as a separate supplement to the agenda when it is available.**
18.	**REVIEW OF TERMS OF REFERENCE FOR THE AUDIT AND GOVERNANCE COMMITTEE** (Pages 143 - 158) To receive the report of the Head of Legal and Policy Development which sets out proposed revisions to the Terms of Reference for the Committee.
19.	**REVIEW OF FREQUENCY OF AUDIT AND GOVERNANCE COMMITTEE MEETINGS** To receive the report of the Audit, Risk and Assurance Manager which looks at the current frequency of Audit and Governance Committee meetings and makes recommendations for the frequency of future meetings. **Please note that this document will be published as a separate supplement to the agenda when it is available.**

20.	**AUDIT AND GOVERNANCE COMMITTEE WORK PROGRAMME** (Pages 159 - 162) To consider the Committee's Work Programme.
21.	**DATE OF NEXT MEETING** Thursday, 26 June 2014 at 6.30pm.

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Julian Wain
Chief Executive

Date of Publication: Friday, 7 March 2014

NOTES

Disclosable Pecuniary Interests
The duties to register, disclose and not to participate in respect of any matter in which a member has a Disclosable Pecuniary Interest are set out in Chapter 7 of the Localism Act 2011.

Disclosable pecuniary interests are defined in the Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012 as follows –

Interest	Prescribed description
Employment, office, trade, profession or vocation	Any employment, office, trade, profession or vocation carried on for profit or gain.
Sponsorship	Any payment or provision of any other financial benefit (other than from the Council) made or provided within the previous 12 months (up to and including the date of notification of the interest) in respect of any expenses incurred by you carrying out duties as a member, or towards your election expenses. This includes any payment or financial benefit from a trade union within the meaning of the Trade Union and Labour Relations (Consolidation) Act 1992.
Contracts	Any contract which is made between you, your spouse or civil partner or person with whom you are living as a spouse or civil partner (or a body in which you or they have a beneficial interest) and the Council (a) under which goods or services are to be provided or works are to be executed; and (b) which has not been fully discharged
Land	Any beneficial interest in land which is within the Council's area. For this purpose "land" includes an easement, servitude, interest or right in or over land which does not carry with it a right for you, your spouse, civil partner or person with whom you are living as a spouse or civil partner (alone or jointly with another) to occupy the land or to receive income.
Licences	Any licence (alone or jointly with others) to occupy land in the Council's area for a month or longer.
Corporate tenancies	Any tenancy where (to your knowledge) – (a) the landlord is the Council; and (b) the tenant is a body in which you, your spouse or civil partner or a person you are living with as a spouse or civil partner has a beneficial interest
Securities	Any beneficial interest in securities of a body where – (a) that body (to your knowledge) has a place of business or land in the Council's area and (b) either –

i. The total nominal value of the securities exceeds £25,000 or one hundredth of the total issued share capital of that body; or

ii. If the share capital of that body is of more than one class, the total nominal value of the shares of any one class in which you, your spouse or civil partner or person with whom you are living as a spouse or civil partner has a beneficial interest exceeds one hundredth of the total issued share capital of that class.

For this purpose, "securities" means shares, debentures, debenture stock, loan stock, bonds, units of a collective investment scheme within the meaning of the Financial Services and Markets Act 2000 and other securities of any description, other than money deposited with a building society.

NOTE: the requirements in respect of the registration and disclosure of Disclosable Pecuniary Interests and withdrawing from participating in respect of any matter where you have a Disclosable Pecuniary Interest apply to your interests and those of your spouse or civil partner or person with whom you are living as a spouse or civil partner where you are aware of their interest.

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Agendas and reports can be viewed on the Gloucester City Council website: www.gloucester.gov.uk and are available to view five working days prior to the meeting date.

For further details and enquiries about this meeting please contact Penny Williams, 01452 396125, penny.williams@gloucester.gov.uk.

For general enquiries about Gloucester City Council's meetings please contact Democratic Services, 01452 396126, democratic.services@gloucester.gov.uk.

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FIRE / EMERGENCY EVACUATION PROCEDURE

If the fire alarm sounds continuously, or if you are instructed to do so, you must leave the building by the nearest available exit. You will be directed to the nearest exit by council staff. It is vital that you follow their instructions:

- You should proceed calmly; do not run and do not use the lifts;
- Do not stop to collect personal belongings;
- Once you are outside, please do not wait immediately next to the building; gather at the assembly point in the car park and await further instructions;
- Do not re-enter the building until told by a member of staff or the fire brigade that it is safe to do so.

Gloucester City Council

AUDIT AND GOVERNANCE COMMITTEE

MEETING : Monday, 25th November 2013

PRESENT : Cllrs. Wilson (Chair), Hobbs (Vice-Chair), McLellan, Noakes and Porter

Others in Attendance

Councillor Wood, Cabinet Member for Performance and Resources
Peter Gillett, Corporate Director of Resources
Terry Rodway, Audit, Risk and Assurance Manager
Sue Mullins, Head of Legal and Policy Development
Jon Topping, Head of Finance
Andrew Cummings, Management Accountant
Stephanie Payne, Audit, Risk Management and Value for Money Officer
Sarah Tilling, Financial Project Supervisor
Richard Webb, Asset Manager
Ross Cook, Head of Neighbourhood Services
Parvati Diyar, Democratic Services Officer

APOLOGIES : Cllrs. Llewellyn and Gilson

63. DECLARATIONS OF INTEREST

Councillor Porter declared a personal interest as a Member of the Aspire Trust Board.

64. MINUTES

The minutes of the meeting held on 23 September 2013 were confirmed as a correct record and signed by the Chair.

65. PUBLIC QUESTION TIME (15 MINUTES)

There were no questions from members of the public.

66. PETITIONS AND DEPUTATIONS (15 MINUTES)

There were no petitions or deputations.

67. RESPONSE TO INTERNAL AUDIT REPORT RECOMMENDATIONS - CLIENT MONITORING OF PAYROLL SYSTEM

The Audit, Risk and Assurance Manager introduced the Financial Project Supervisor who had been invited to attend the meeting to provide Members with an update in relation to the implementation of audit recommendations relating to the payroll system. Members were reminded that this item was a result of a recommendation from a previous meeting of the Audit and Governance Committee.

The main areas of weakness identified were that there was an unsatisfactory level of assurance on the confirmation of the establishment by Group Managers, review of exception reports, reconciliation of the payroll to actual payments made and client monitoring of the payroll service level agreement (SLA).

The Financial Project Supervisor advised that following the issues picked up by Internal Audit, progress had been made addressing the issues.

An email had been sent to all Managers requesting them to review their establishment list. In addition to this, the SAP system allowed Managers to check staff at any point and they were expected to log into the SAP system regularly. The SAP system provided visual structures and was more transparent than the previous payroll system. HR would be meeting with Managers on a regular basis and structures would be discussed at these sessions to further emphasise the requirement on Managers.

It was identified that no exception reports were being provided and these were now in place and being checked monthly by the HR team. The current reports provide variance details from last pay to current pay. Further expansion of the reporting available would be investigated to produce a Gross to Net report for HR through the use of the Council's new software.

The Financial Project Supervisor confirmed that all reconciliations on payroll control accounts were now up to date and in balance. Following the audit the County Council provided additional reports that had allowed Finance to better identify payment details and this had enabled them to reconcile more simply.

Since the audit, some scoping had been undertaken to remove any uncertainty around who provided which part of the service detailed in the SLA. Moving payroll into HR had given a clear point of contact for officers and had allowed HR to better see the whole picture.

Currently a value for money review of the payroll service is being carried out by a member of the Audit and Assurance team. The SLA is currently under review to ensure more clear and defined targets and performance monitoring are in place. This area of work had not yet been completed but the intention was to ensure the findings of the value for money review were included.

The Financial Project Supervisor commented that the aim was to have a revised and agreed SLA in place by the end of the financial year so the Council could move forward into 2014/15 with improved assurance and confidence.

The Chair enquired on the move of payroll from Finance to HR. The Corporate Director of Resources commented that although some services had been moved to the County Council, it was always the intention to move the residual payroll function and client monitoring of the SLA from Finance to HR.

In response to a question from Councillor Porter, the Corporate Director of Resources advised that whilst some teething problems had arisen during the transition period following the move to the County Council's SAP payroll system, it was important to work to make a success of the current arrangements. Alternative provision however would be benchmarked as part of the value for money review.

The Audit, Risk and Assurance Manager advised Members that a follow up audit would be undertaken to ensure all audit recommendations had been carried out. As previously agreed, any Rank 1 recommendations not implemented by the agreed date would be reported to the Committee.

Members thanked the Financial Project Supervisor for her attendance.

RESOLVED that the report be noted.

68. RESPONSE TO INTERNAL AUDIT REPORT RECOMMENDATIONS - RESPONSE REPAIRS CONTRACT

The Audit, Risk and Assurance Manager introduced the Asset Manager who had been invited to provide Members with an update in relation to the implementation of audit recommendations relating to the client monitoring of the Response Repairs Contract. Members were reminded that this item was a result of a recommendation from a previous meeting of the Audit and Governance Committee.

The Asset Manager provided an update. He advised that the original contract dated back to August 2012 and was not operational until March 2013. During this period problems had arisen with the Contractor which had led to a lack of trust between both parties.

A preferred course of action had been identified to ensure value for money was being achieved and improvements had been made to contract standing orders. The audit recommendations had been accepted and actions agreed to implement them.

The Committee raised their concerns regarding the delays in work in view of the fact the Contractor had been appointed in 2012. If the contract was not fit for purpose this should be remedied as a matter of urgency.

The Corporate Director of Resources advised that the contract had been put into place by the Asset Manager's predecessor. The Asset Manager would ensure future contracts were dealt with appropriately.

Members thanked the Asset Manager for his attendance.

RESOLVED that the Asset Manager would provide a further update at the next meeting of the Audit and Governance Committee in March 2014.

69. ACTION PLAN

The Corporate Director of Resources presented the updated action plan.

Councillor Noakes noted the improved layout and suggested that the completed items should have a date against it once it has been finalised. She added that dates which had not been achieved should remain in brackets against the revised target date.

Councillors Porter and McLellan commented that they had been unable to attend the Treasury Management Training held on 23 September 2013. The Corporate Director of Resources said he would repeat this event in 2014.

The Vice Chair asked why the purchase of software with a modern stock control facility at the Guildhall still had an amber status. He was advised that the newly appointed Manager was currently reviewing the existing processes and this item had an amber status as the target date was 31 March 2014 although it may not be completed by this date. Councillor Wood advised that a Working Group had been set up to look at the progress at the Guildhall. It was suggested that if no progress had been made by the target date, the Guildhall Manager be invited to provide an update at a future meeting of the Committee.

Councillor Porter commented on the combined heat and power installation at GL1 which had not worked correctly since its initial installation due to a problem with the main gas unit. He believed this item should be a red status. The Corporate Director of Resources said he would investigate this matter with the Asset Manager who would then email the Committee with an update.

In response to a query from the Chair regarding the Fixed Asset Register, the Corporate Director of Resources confirmed that the system upgrade was due to be completed week commencing 2 December 2013. The upgrade was necessary before the register could be implemented. The Head of Finance commented that the project to move from the Excel based asset register would commence on 1 December 2013. He did not want the implementation to be rushed and therefore the installation would not take place until he and Internal Audit were fully confident the asset register had been fully tested and reconciled. If this was not completed by year end it would be implemented in the new financial year. This had been agreed with external audit.

RESOLVED that the action plan be noted.

70. ANNUAL GOVERNANCE STATEMENT ACTION PLAN 2013-14

The Committee received a report on the Annual Governance Statement Action Plan 2013/14, which had been prepared by the Corporate Governance Group advising Members of the action taken.

The Corporate Director of Resources commented that all actions within the report now had green status and target dates for completion had now been included.

The Corporate Director of Resources provided an update on the restructure of Financial Services. He advised that Jon Topping, the Head of Finance had started in September and Andrew Cummings had been appointed as Management Accountant and the further restructure of Financial Services was underway.

The Interim Finance Change Manager had now completed the handover with the Head of Finance and would be finishing at the end of November 2013. He is currently undertaking some project work to support elements of finance work. The Project Accountant would be undertaking technical work until May to help cover the vacant post.

RESOLVED that the action taken on the Annual Governance Statement Action Plan 2013/14 be endorsed.

71. FINANCIAL SERVICES IMPROVEMENT PLAN

The Head of Finance presented the Financial Services Improvement Plan which detailed the progress undertaken by the Finance Team.

Members noted that following a handover with the Interim Finance Change Manager, the Head of Finance would now be the formal owner of the Improvement Plan.

In response to a question from the Chair, the Head of Finance confirmed that monthly meetings with Managers and budget holders would be held to ensure budget monitoring processes were being implemented.

Councillor Porter enquired about the £9k manual journal which had been required to balance the reconciliation. He was advised that this item had been reconciled and the matter was now complete.

In relation to the Fixed Asset Register whereby no resources had been allocated to deliver the project which was estimated to take three months, the Head of Finance referred Members to the discussion on the action plan and advised that action would be taken as soon as the system upgrade had been completed.

The Corporate Director of Resources advised that the Management Accountant was reviewing approval levels for different areas of spend. He confirmed that all invoices had now been coded.

Councillor Noakes suggested that it would be helpful to have completed target dates included on the Improvement Plan if an item had been closed.

RESOLVED that the Financial Services Improvement Plan be noted.

72. TREASURY MANAGEMENT UPDATE - QUARTER 2 REPORT 2013/14

The Committee considered a report by the Corporate Director of Resources fulfilling one of the requirements of the revised Code of Practice for Treasury Management in November 2011 recommending that Members should be updated on treasury management activities at least twice a year, but preferably quarterly. The report covered Quarter 2 from 1 July to 30 September 2013.

The Committee was advised that investment rates available in the market had continued at historically low levels and had fallen further during the quarter as a result of the Funding for Lending Scheme. The average level of funds available for investment purposes during the quarter was £8.5m.

No borrowing had been undertaken during the quarter and to minimise investment risk, the Council had reduced external investments to minimise new external borrowing. This had been achieved by reducing the overall debt liability by repaying £5,000,000 of external debt however this policy would require ongoing monitoring.

The Council had not borrowed in advance of need during the quarter ended 30 September 2013 and had no intention to borrow in advance in 2013/14.

The Corporate Director of Resources commented that the Co-operative Bank was due to announce an opt out of providing services to local authorities. The City Council would take the opportunity to procure a new bank and a suggestion had been made to carry out a joint procurement with other district council's which would save on costs. The Corporate Director of Resources and the Head of Finance would be meeting with the Co-operative Manager and would seek financial or other support to fund any potential transitional costs.

RESOLVED that the report be noted and approval is given for any changes it may require to the prudential indicators.

73. RISK MANAGEMENT ANNUAL REPORT 2013

The Committee considered a report by the Audit, Risk and Assurance Manager which provided Members with an update on the Council's risk management activities from the past year and also future planned actions.

The Officer Risk Management Champion presented the report and advised that Councillor Llewellyn had been appointed as the new Member Risk Management Champion, replacing Councillor Wood who previously held the post.

It was noted that during the Officer Risk Management Champion's maternity leave her role was covered by a member of the Audit and Assurance team to ensure the continuity of risk management support within the Council was undertaken.

The strategic risk register was under review by the Gloucester Leadership Team (GLT) which included Group Manager sessions on a monthly basis. Service risk registers were also being reviewed by GLT and as at October 2013, the majority of service business plans and risk registers had been presented to GLT for review. The remaining seven service areas are scheduled for review.

Ongoing workshops have been offered to officers and managers. Risk Management training was offered to Members in February 2013 however the session had been cancelled due to low take up. It was anticipated to promote Member risk management workshop scheduled for 8 January 2014.

The Audit, Risk and Assurance Manager advised that currently six Members had confirmed their attendance on the workshop in January and asked if the Chair of the Committee could encourage Members to attend. The Chair advised that he would make an announcement at the next Council meeting scheduled for Thursday, 28 November 2013. The Audit, Risk and Assurance Manager would confirm whether it was a statutory requirement for Members to attend. It was noted that the email regarding the workshop would be re-submitted to all Members.

In response to a question from Councillor McLellan, Councillor Wood advised that the Terms of Reference for the Member Risk Management Champion were imprecise but the main role was to work in association with the Officer Risk Management Champion and ensure risks were managed in the appropriate manner.

RESOLVED that the risk management process undertaken to date and the planned future work be endorsed.

74. INTERNAL AUDIT PLAN 2013/14 - MONITORING REPORT

The Committee considered a report by the Audit, Risk and Assurance Manager informing Members of the audits completed as part of the approved Internal Audit Plan 2013/14.

At the previous meeting of the Committee, Members received an update from the Markets Manager on the implementation of internal audit recommendations. It was agreed that a further update would be provided at the next meeting. The Audit, Risk and Assurance Manager advised that the Markets Manager had now left the Council's employment and therefore the audit would be undertaken when a replacement was in post and would be reported to the Committee at its meeting in March.

The Vice Chair acknowledged that no Manager was currently in post but believed this should not prohibit the audit to be undertaken. The Audit, Risk and Assurance Manager confirmed that the audit would now be carried out in January 2014.

The Audit, Risk and Assurance Manager referred to Appendix A of the report which detailed the lists of audits completed during September 2013 to October 2013.

The Committee noted that the audit recommendation for the Streetcare Contract – Client Monitoring had been given an unsatisfactory level of assurance. The Head of Neighbourhood Services provided an update. He welcomed the report and advised the audit recommendations had been taken on board and a number of actions were now in place. Amey had recently taken over Enterprise and the consultation on the realignment of Neighbourhood Services had been completed. A number of issues in the report had been superseded by other changes and were being monitored in a different way.

Councillor McLellan referred to the possible overpayment of £280k. It was noted that this referred to the method of calculation of the Annual Contract Sum. Amey had been asked to confirm if this calculation was correct.

Councillor Porter expressed his disappointment with the report and believed the Council should recover the £280k from Amey. The Head of Neighbourhood Services reassured Members that all issues identified within the report were now being addressed. The Interim Finance Change Manager was currently identifying any potential overpayment.

The Head of Neighbourhood Services commented that under the new staffing structure, there would be a split of roles between contract management and service delivery. One of the recommendations was to formalise the Strategic Streetcare Partnership meetings and it was now proposed that the Group would receive quarterly monitoring reports.

It was agreed that the Head of Neighbourhood Services would provide an update at the Audit & Governance Committee in March.

RESOLVED that the audit work undertaken to date and the assurance given on the adequacy of internal controls operating in the systems audited be endorsed.

75. COMMITTEE ON STANDARDS IN PUBLIC LIFE - ANNUAL REPORT 2012-13

The Committee considered a report by the Monitoring Officer informing them about the work of the Committee on Standards in Public Life during 2012/13 and to identify any changes to be made to the Council's governance arrangements in light of the report.

The Monitoring Officer referred to the two key areas of relevance, one of which included the number of areas within the Standards in Public Life report which were relevant to the work of the Audit and Governance Committee. The report reached four main conclusions and recommended eight best practice points. Reference was made regarding ethical issues which should feature regularly on the agendas of the boards of public bodies and, where appropriate, on risk registers.

The second area of relevance related to the description and guidance to the Seven Principles of Public Life which had been amended.

RESOLVED:

1. **That the contents of the Annual Report 2012-13 of the Committee on Standards in Public Life, set out in Appendix A be noted.**

2. **That the current position and proposed actions in relation to the best practice points identified in paragraph 3.3.5 of the report be noted and approved.**

and RECOMMENDED:

3. **That the Council's Code of Conduct for Members be amended to reflect the updated Seven Principles of Public Life, as set out in paragraph 3.3.6 of the report.**

76. REGULATION OF INVESTIGATORY POWERS ACT 2000 (RIPA) - ANNUAL REVIEW OF PROCEDURAL GUIDE

The Committee considered a report by the Chief Executive requesting Members to review and update the Council's procedural on RIPA and requesting that last year's use by the Council of its RIPA powers be noted.

The Head of Legal and Policy Development advised that no activity had occurred during the last year and therefore the Council had not made use of its RIPA powers. This was mainly due to the change restricting RIPA authorisations for directed surveillance to offences which carried a maximum custodial sentence of 6 months or more.

The Council received its most recent inspection by the Office of Surveillance Commissioners (OSC) on 27 July 2012. The suggestions for amendment and improvement arising from the inspection had been incorporated into the draft Procedural Guide as shown at Appendix 1. A further minor change related to a job title change for the RIPA Co-ordinator.

RESOLVED:

1. **That the proposed changes to the Council's RIPA Procedural Guide and the Council's use of its RIPA powers in the last year be noted.**

and RECOMMENDED:

2. **That the changes to the Procedural Guide at Appendix 1 be approved.**

77. REVIEW OF TERMS OF REFERENCE FOR AUDIT AND GOVERNANCE COMMITTEE

The Committee considered a report by the Head of Legal and Policy Development requesting that a Working Group of the Committee reviews the Terms of Reference for the Committee and identifies any changes to the Terms of Reference that should be recommended to the Constitutional and Electoral Working Group and Council.

The Head of Legal and Policy Development commented that it was good practice for a Working Group to be formed to consider the frequency of Committee meetings due to the volume of business at recent meetings. The next meeting of the Committee is scheduled for 17 March 2014 and this would be too late for any changes to the Committee's Terms of Reference to be included in this year's Constitutional review.

It was noted that the updated CIPFA guidance on the review of the effectiveness of the audit committee was anticipated later this month or early December.

RESOLVED:

1. **That a Working Group be formed comprising of at least three members of the Committee to review the Terms of Reference for the Committee.**

2. **That the Working Group be instructed to consider and make recommendations on the frequency of Audit and Governance Committee meetings.**

3. **Subject to the CIPA guidance, the Working Group would consist of the Chair, Vice Chair and Councillor Porter.**

78. UPDATE ON THE PEER REVIEW

The Corporate Director of Resources updated Members on the peer review.

He advised that the peer challenge would be held from 11 to 13 December 2013 inclusive. The challenge would concentrate on the following five key headings:

- Understanding of local context and priority setting
- Financial planning and viability
- Political and managerial leadership
- Governance and decision making
- Organisational capacity

The Peer Team would consist of the following:

- Steve Packham - Chief Executive, Chelmsford City Council
- Gerald Almeroth - Strategic Director for Resources, London Borough of Sutton
- William Nunn - Conservative member, former Leader of Breckland Council
- Sir Stephen Houghton CBE - Labour member, Barnsley Council
- Chris Bowron – Programme Member, Peer Support, LGA

The Peer Challenge Team would be allocated a base room for the duration of their visit, which would be located on the 4th Floor in close proximity to the Chief Executive's office. A Corporate Support Officer would provide any assistance they require.

GLT had been asked to complete a self assessment which would be submitted along with other documentation requested by the Team.

A proposed list of officers/Members/focus groups which the Peer Team would interview during the review had been drafted. This would consist of Group Leaders, Cabinet Members, GLT, the Head of Legal and Policy Development, The Audit, Risk and Assurance Manager and Senior Managers. Frontline staff focus group would involve a cross section of staff and key partners including Gloucester City Homes, Amey, Aspire Sports & Cultural Trust, the Dean of Gloucester, the Chief Executive at the County Council would also be interviewed.

The Peer Team would present their findings on the final day of the review.

RESOLVED that the report be noted.

79. SERVICE RISK REGISTERS

The Audit, Risk and Assurance Manager advised he did not have any additional information to add following the last meeting. As stated in the Risk Management Annual Report, Service Risk Registers continued to be reviewed by the Gloucester Leadership Team (GLT).

The Committee agreed that this item should no longer be included as a standing item.

RESOLVED that the report be noted.

80. WORK PROGRAMME

The Corporate Director of Resources presented the proposed work programme for the Audit and Governance Committee.

The Committee were advised that due to the size of recent agendas, an additional meeting of the Audit and Governance Committee would be arranged with the external auditors, KPMG for late January or early February 2014.

The Committee agreed to this proposal.

RESOLVED:

1. **That the Audit and Governance Committee Work Programme be noted.**

2. **That the Corporate Director of Resources would liaise with the Democratic Services Officer and identify potential dates for an additional meeting.**

81. DATE OF NEXT MEETING

Monday, 17 March 2014 at 6.30pm.

Time of commencement: 18:30 hours
Time of conclusion: 20:35 hours

Chair

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AUDIT AND GOVERNANCE COMMITTEE

MEETING : Monday, 27th January 2014

PRESENT : Cllrs. Hobbs (Vice-Chair, in the Chair), McLellan, Noakes, Llewellyn, Porter, Wood and Ms T Westcott of KPMG LLP (UK)

Others in Attendance
Ms T Westcott, Manager, KPMG LLP (UK)
Peter Gillett, Corporate Director of Resources (Gloucester City)
Jon Topping, Head of Financial Services (Gloucester City)
Terry Rodway, Audit, Risk and Assurance Manager (Gloucester City)

APOLOGIES : Cllrs. Wilson and Gilson, Mr D Gilbert of KPMG LLP (UK)

82. DECLARATIONS OF INTEREST

There were no declarations of interest.

83. PUBLIC QUESTION TIME (15 MINUTES)

There were no questions from members of the public.

84. PETITIONS AND DEPUTATIONS (15 MINUTES)

There were no petitions or deputations.

85. UPDATE ON PEER REVIEW

The Director of Resources updated the Committee on behalf of the Chief Executive. As the first draft of the Peer Review report had only just been received, it was proposed that the report be considered at the next meeting of the Committee to allow further analysis of the document. The Committee agreed and requested that a Members' Briefing on the subject be emailed before the next meeting.

RESOLVED:
(1) That the update be deferred to the meeting on 17 March 2014.
(2) That an electronic Members' Briefing be issued before the next meeting on 17 March 2014.

86. KPMG ANNUAL AUDIT LETTER 2012/13

Ms T Westcott, Manager of KPMG LLP (UK) presented the Committee with the Annual Audit Letter 2012/13 dated October 2013.

Ms Westcott drew Members' attention to the 'Headlines' in the Annual Audit Letter. She confirmed that KPMG LLP (UK) were satisfied that the Council had proper arrangements for securing financial resilience and that it secured economy, efficiency, and effectiveness. In particular, the Annual Audit Letter recognised an improvement in the quality of Gloucester City Council's accounts. Ms Westcott commented on the recommendations relating to fixed assets and noted the Council's plans to implement a new system to address this issue. Ms Westcott also gave a breakdown of the audit fees set out in Appendix 3.

Members were pleased to learn of the improved position.

The Committee discussed the following matters:-

- **The reason for the variation between the Audit Commission's scale fee of £85,400 and the actual final fee charged for 2012/13 of £139,500**. Ms Westcott clarified the position and confirmed that KPMG LLP (UK) would be reviewing the future fee in light of the Council's improved position and that a reduction was anticipated.
- **The reason why Aspire's assets were not included in the 'Review of Community and Intangible Assets'.** Ms Westcott explained that KPMG LLP (UK) believed that Aspire's relationship with the City Council had changed following a full review.

RESOLVED: That the Annual Audit Letter for 2012/13 be noted.

87. DATE OF NEXT MEETING

Monday 17 March 2014 at 18.30 hours.

Time of commencement: 18:30 hours
Time of conclusion: 18:50 hours

Chair

G A A P

Gloucestershire Audit & Assurance Partnership
The Audit & Assurance Service for
GCC & SDC

Monitoring Sheet – March 2014 - Streetcare Contract Monitoring incl. Recycling Credits and waste incentives

Rec No.	Risk	Recommendation	Rank	Accepted/ Not Accepted	Action to be Taken	Owner	Current Status	Target Date	RAG
1	Contract conditions and specifications highlighted in the Contract Review report may not be accepted and implemented promptly resulting in poor service and additional costs.	The draft Contract Review report performed by the Environmental Service Manager should be finalised and agreed by the Communities and Public Spaces Manager and Corporate Director Services & Neighbourhoods.	1	Accepted	It was recognized at the time of the contract review that it could not be completed in the time available and hence was left draft. Where an action plan was not produced as the review had not been completed at that stage, a number of the recommendations have been implemented as advised below.	Ross Cook	3/3/14 – A review of the draft report has now been completed and the key areas for further work identified. A meeting has taken place (26 Feb) between Neighbourhood Management, Business Improvement and Audit & Assurance to discuss the Action Plan (see Recommendations 2 and 3 below)	Original Target Date – 28 February 2014 Completed – 26 February 2014	
2	Contract conditions and specifications highlighted in the Contract Review report may not be accepted and implemented promptly resulting in poor service and additional costs.	Where actions in the Report have been identified an owner should be formally assigned, expected implementation dates noted and regular progress to implementation provided to Neighbourhood Services management.	1	Accepted	A number of the recommendations made in the contract review have already begun to be implemented, these include: introduction of KPIs, work schedules and method statements. Some of the recommendations can only be fully implemented once the savings have been realized and work patterns altered to accommodate the reduced resource.	Ross Cook / Lloyd Griffiths/ Meyrick Brentnall	3/3/14 - As detailed in (1) above, an Action Plan has now been developed and officers (roles) have been identified for each action. Do to the recent realignment of roles within Neighbourhood Management, we have a couple of positions to be filled through external recruitment and so the final target dates will be subject to these appointments being made. The Action Plan focuses on – Review of the Output Specification and finalising Method Statements Agreement of the Payment and Performance Mechanism Ongoing review of the Service Delivery Plan Clarification of roles of Monitoring Meetings (already completed) Contract Variations (see Recommendation 4 below) Review of Risk Register Supply and Sharing of Information	An agreed timescale will be implemented following consideration of the final report and actions required. Date for completion of Action Plan – 31 March 2014	

3	Not all contractual conditions and specifications have been fully implemented and monitored resulting in poor service and increased costs.	A detailed review of the Contract should be performed and a gap analysis produced detailing all the conditions and specifications detailing whether and how they are being achieved. Any identified gaps should then be implemented.	1	Accepted	When the review of the contract is completed, any identified gaps will form part of the agreed Action Plan.	Gordon Buchanan, Environmental Service Manager.	3/3/14 – As detailed in 2 above, the review has been completed and a draft Action Plan developed. Each Action will be assigned to a named officer. The Review of the Output Specification and Method Statements will be assigned to a relevant officer within Neighbourhood Management – Waste and Recycling – Lloyd Griffiths Grounds Maintenance – Dave Pritchett City Centre Cleansing – Ismael Rhyman Street Cleansing – Vacant Post (Ross Cook to lead in interim) Trees and Hedges – Meyrick Brentnall	An agreed timescale will be implemented following consideration of the final report and actions required. Date for completion of Action Plan – 31 March 2014	
4	The contractual obligations on Enterprise to deliver the service and associated costs may not be fully known resulting in Contract breaches going undetected and overcharge for services. Changes made to service delivery may not be fully known resulting in increased and possible duplicated costs.	The following work should be performed to ensure all Service Change Requests and Contract Variations are fully documented, accounted for and approved: • Separate central records of all Service Change Requests and Contract Variations should be set-up and maintained by the Environmental Service Manager; • Service Change Requests and Contract Variations should be sequentially numbered to ensure they can all be accounted for; • Service Change Requests and Contract Variations should be agreed and approved by the Environmental Service Manager or above and appropriate	1	Accepted	This recommendation was made by the Environmental Service Manager in the contract review. There have not been any variations since this review any future variations will be carried out in a clear and consistent manner and in line with Recommendation 4.	Ross Cook / Lloyd Griffiths / Meyrick Brentnall (Contract Variations and Adoptions)	3/3/14 – Adoptions – Meyrick Brentnall is now responsible for adoptions and has already reviewed the process. An officer group has met to review the existing process and a suggested new process. This will be finalised and adopted by both the City Council and Amey 3/3/14 – Historic Adoptions and Contract Variations - Lloyd Griffiths has met with Phil Mathews from Amey and they have reviewed the schedule of outstanding contract variations regarding Street Cleansing and Grounds Maintenance, as a result of adoption of new areas of land. These will be included in the Annual Sum for either 2013/14 or 2014/15 (depending on when they were adopted). A new schedule of adoptions and variations has been developed and all agreed changes are added to this schedule and reviewed at the Partnership meeting 3/3/14 - Staff who deal with Amey on a daily basis have been advised of the need to ensure all Work Requests include the following information (Email to staff on 6/2/14). A new proforma has been developed and will be agreed at the Partnership meeting – • There must a reference number (these will be consecutively numbered for each financial year) • Nature of works • Location of works • Date works to be commenced • Date works to be completed	Original Target Date – Immediately Revised Target Date – 31 March 2014	

		Enterprise management. Legal should also be involved for any Contract Variations; • All original agreed and signed Service Change Requests should be held by the Environmental Service Manager and Contract Variations should be held with Legal Services with the signed Contract.					• Confirmed that the work is not within the existing contract • Confirmation as to whether the work can or cannot be prioritised by rescheduling existing resources If Not within contract and cannot be carried out by rescheduling resources. The following must be detailed – • Staff costs (must be included even if £0) • Material costs (including any contract uplift) • Whether the work is a one off (ad-hoc) i.e. repairing a fence, or • Whether there will be any ongoing costs, i.e. a new bin that needs emptying • If there are ongoing costs, the date when this to be included in the Annual Contract • Total value of works • Total value of annual ongoing costs • What Monitoring / KPIs are needed for the works or ongoing work The requests will be verified / signed off by – Officer requesting work Amey Officer to confirm work to be done Approved by – Lloyd Griffiths (Waste and Recycling / Flood), Meyrick Brentnall (Trees and Hedges), Neighbourhood Manager (Grounds or Streets) Ross Cook – in the absence of any of the above **All new processes are to be in place by 31 March 2014.**		
5	The various groups may not be fully aware of their purpose and responsibilities resulting in issues not being properly addressed.	Consideration should be given to agreeing a formal Terms of Reference for the quarterly Strategic Partnership Group.	3	Accepted	We will review the need to formulate a Terms of Reference.	Ross Cook	16/12/13 – Terms of Reference were discussed at the meeting held on 19 November and agreed.	At the next meeting of the Strategic Streetcare Partnership meeting – 19 November Completed – 19 November 2013	
6	Overpayments are made	Before certification and approval of the	1	Accepted	Recommendation to be implemented as detailed.	Ross Cook / Lloyd Griffiths.	3/3/14 – Discussions have taken place with Amey with regards to agreeing a timetable for the	Original Target Date - Immediately	

	resulting in financial losses and adverse publicity.	Annual Contract Sum checks should involve a thorough review of all costs and calculations detailed to confirm: • They are as per that detailed in the Contract; • Correctly calculated; • Indexation applied if appropriate and figures are substantiated to previous years Annual Contract Sum carried forwards and indices used in the calculations agree to the Labour & Supervision in Civil Engineering or equivalent; • Additional costs are fully substantiated and correctly applied with or without indexation.					completion of the Annual Sum discussions and sign off. A process has been discussed whereby the proposed Annual Sum, including all previously approved changes (see Recommendation 4 above) will be discussed between Amey, the Environmental Services Manager (Waste and Recycling), the Countryside and Land Manager (Trees and Hedges) and the relevant Neighbourhood Managers (Grounds and Streets) before a final recommendation is made to the Head of Neighbourhood Services to sign this off. It has been agreed that the draft Annual Sum will also be presented to the Strategic Streetcare Partnership meeting for information prior to signing. The draft Annual Sum for 2013/14 has been received and Lloyd Griffiths has reviewed variations and adoptions for inclusion. Final agreement of the Annual Sum for 2013/14 cannot be agreed until the conclusion of the discussions with regards to the Indexation Calculation. **All new processes are to be in place by 31 March 2014.**	Revised Target Date – 31 March 2014	
7	Overpayments are made resulting in financial losses and adverse publicity.	Discussions should be held with Enterprise to establish the reason why the Annual Contract Sum indexation calculation differs to the Contract and to establish if this change was correctly approved. Where it is proven that the change in the Contract stated Annual Contract Sum indexation calculation has not been approved then all the issued Annual	1	Accepted	This has been actioned and a response has been received from Enterprise. There are ongoing discussions as to how this will be dealt with. The method of calculation of the Annual Sum was signed of in 2010/11and there is no information available to confirm why this method was used. This method has subsequently been challenged and discussions are currently ongoing regarding the validity of this calculation method and the impacts on the annual cost.	Kevin Buckerfield, Finance Change Manager	A review of the calculation methods has been undertaken with a number of inconsistencies to the original contract. The areas which have been identified for discussion with Amey are. 1. Basis for baseline - no formal documents are available for the 2010 'soft reboot'; therefore, a number of contract extras may be being charged which should be considered as baseline. 2. The indexation base percentage increases are incorrect for the labour portion of the contract (56% of contract value) 3. No back-up of calculation to substantiate the 2012/13 increase value. 4. The cumulative impact upon the incorrect use of the baseline at 2010 is £400k, this has an annual ongoing impact of circa £100k	Audit Recommendation Date - 25/06/13 Original Target Date – 31 December 2013 Revised Target Date – 31 March 2014	

		Contract Sum documentation including all costs should be obtained, reviewed and any total over charge that has been determined is recovered.					(dependant upon the LG pay awards). 5. It is intended to arrange meetings with Amey for the last week in March to discuss progress. 6. The targeted completion date for this aspect of the exercise was End December - a meeting was held on the 15th January to discuss the results. 7. A final point for discussion is the methodology adopted, the monthly baseline amount at 2010 and it's impact beyond indexation. The re-boot was agreed by the previous Group Manger and appears to be in-correct; this could have a significant monetary value.		
8	Overpayments are made resulting in financial losses and adverse publicity.	A review of the costs quoted by Enterprise for the additional work included in the 2012/13 Annual Contract Sum should be undertaken to confirm the indexation calculation has been correctly applied to these costs. Other years Annual Contract Sum may need to be also reviewed depending on the outcome of the review.	2	Accepted	Agreed.	Kevin Buckerfield Finance Change Manager	A review of the contract extras is being undertaken and due for completion by the end of March 2014. A schedule of all contract extras since April 2008 has been prepared and investigatory work is ongoing to establish if those items should not have been charged as inclusive in the baseline cost. The value of these excluding VAT is £1.9 million for the five year period. Only a few instances of regular incurred fees have been applied an annual inflation increase (fly tipping, additional re-cycling etc.). Most of the charges are without sufficient supporting detail to establish validity; but these expenditure types will be put to Amey to demonstrate their non-inclusion in the baseline. A report to the Directors of Resources and Service and Neighbourhoods will be presented by the due date of End March. To include a schedule of potential duplicated payments for ad-hock services.	Audit Recommendation Date - 25/06/13 Revised Target Date – 31 March 2014	
9	Financial pressures may be placed on Enterprise that results in them not delivering the service and adverse publicity.	A timetable for the discussion and agreement of the Annual Contract Sum should be agreed with Enterprise that assists in the completion of these negotiations before the start of the financial year.	3	Accepted	Discussions have always commenced prior to the commencement of the relevant financial year but there often a number of factors that mean that the final figure cannot be agreed before April. A significant factor in the delay of confirming the Annual Sum over the last two years has been the numerous changes of the General Manager. An agreed timetable has now been put in place to minimise any future delays. The indices used to calculate the Annual Sum are not confirmed prior to April so there	Lloyd Griffiths	3/3/14 – Discussions have taken place with Amey with regards to agreeing a timetable for the completion of the Annual Sum discussions and sign off. A process has been discussed whereby the proposed Annual Sum, including all previously approved changes (see Recommendation 4 above) will be discussed between the Environmental Services Manager, the Countryside and Land Manager and the relevant Neighbourhood Managers before a final recommendation is made to the Head of Neighbourhood Services to sign this off. It has been agreed that the draft Annual Sum will also be presented to the Strategic Streetcare	Original Target Date – 31/07/13 Revised Target Date – 31 March 2014	

					will be an inevitable delay.		Partnership meeting for information. Final agreement of the Annual Sum for 2013/14 cannot be agreed until the conclusion of the discussions with regards to the Indexation Calculation. **All new processes are to be in place by 31 March 2014.**		
10	Enterprise Invoice requests for TUPE staff employers' pension contributions may be incorrectly calculated or contributions for ghost employees incorrectly claimed resulting in under/over payments by the Authority.	Contact Finance to establish the accuracy and appropriateness of the following: • Whether the employers' pension contribution level currently applied is correct; • VAT applied by Enterprise to the monthly employer pension contribution invoices; • What other checks are performed by the Interim Finance Change Manager on the pension invoices and supporting documentation and whether this is appropriate.	2	Accepted	These were previously checked by a former employee who is no longer with the Council and there does not appear to be any information confirming how these checks were being made. Checks have now been put in place and they will be carried out during the year.	Ross Cook	3/3/14 - A process for checking these invoices is now in place and has been implemented for the latest invoice. Amey have provided a list of current staff who are still in the GCC Pension Scheme and this was cross referenced to the list provided with the Pension Statement. The invoice is then referred back to Finance for them to check the calculation and the contribution levels. It is proposed that this level of check is carried out on a number of occasions during the year due to the minimal change of staffing in each year	Finance have been contacted. Information been requested from Amey to validate to invoices. Completed – 6 February 2014	
		Agree/confirm responsibility for verification and authorisation of pension invoices.		Accepted	Agreed	Ross Cook	3/3/14 – Checks on staffing are to be carried out by Neighbourhood Management. Checks on the accuracy of the invoice calculation to be verified by Finance.	Finance have been contacted. Information been requested from Amey to validate to invoices. Completed – 6 February 2014	
11	Overpayments are made resulting in financial losses and adverse publicity.	Enterprise should be advised of the identified overpayments by the Authority and recovery of these amounts sought.	2	Accepted	The Environmental Service Manager has already identified a number of overpayments and recouped these. Work will continue to identify other areas where overpayments may have occurred.	Ross Cook	3/3/14 – This has been discussed with Amey and a credit note received for an overpayment relating to the Sports Pavilion Attendance (where matches were cancelled). The issues discussed have been followed up by an Email (6 February) setting out the issues to be	A number of overpayments – Sports Pavilion Attendants and Legionella Monitoring have been identified and credit notes	

							resolved. Amey have now confirmed the overpayments have been made and we are finalising the values of the repayments / adjustment needed.	requested. Finance Change Manager reviewing historical invoices to identify overpayments. Target Date – 31 March 2014	
12	Unauthorised work may be instructed by Services areas resulting in incorrect and duplicate costs being incurred by the Authority.	A communication should be made to all appropriate Authority staff advising them that ad-hoc work required to be performed by Enterprise must be made through the Environmental Service Manager or his deputy. In addition Enterprise should be advised that they should not accept any orders for work unless they have been first approved by the Environmental Service Manager or his deputy. In addition all Enterprise invoices outside of the works order process e.g. pension costs, etc should be submitted to the Environmental Service Manager for approval or if appropriate delegated to the most suitable person.	2	Accepted	The Environmental Service Manager has prior to this audit already sought to try and rationalise the procedure for authorising ad-hoc work by advising other Services within the Council to consult him. This has resulted in a number of ad-hoc work not being authorised as they were deemed to already be within the contract. Some areas are not clear however and this relates back to Recommendation 1 and will be clarified on completion of the review. The Environmental Service Manager should check whether requested works are within the contract and a clear distinction should be made with regards to the "staffing / resources" and "materials". Discussions regarding Ad-hoc work should commence on the basis that they will be covered by existing resources and prioritized amongst other work. However, where works are needed to be carried out, then it must be clear as whether additional resources are being used and if so the cost of these resources. No Ad-hoc work should be authorized without a full breakdown of costs and a Purchase Order being raised.	Ross Cook / Lloyd Griffiths	3/3/14 – All key Services (Asset Management, Neighbourhood Management, Environmental Health and Countryside) who request work to be done by Amey have been advised of the need to get approval by the Head of Neighbourhood Services (or nominated Deputy). Full details of the proposed process is set out in Recommendation 4 above. **All new processes are to be in place by 31 March 2014.**	This will be picked up following the completion of the next stage of the review of our staffing structure – anticipated end of December Target Date – 31 March 2014	
13	The Authority may be overcharged for work resulting in the reduction in	A detailed breakdown of the costs particularly between labour and materials should be	2	Accepted	Agreed	Ross Cook	3/3/14 - Full details of the proposed process is set out in Recommendation 4 above. **All new processes are to be in place by 31 March 2014.**	Original Target Date – Immediately Revised Target Date –	

	other planned work and services and excessive costs.	provided by Enterprise for any additional costs so that they can be fully substantiated, agreed to the Contract and schedule of rates.						31 March 2014	
14	Profits made by Enterprise may not be shared with the Authority as per the Contract resulting in excessive costs being borne by the Authority and a reduction in services.	Quarterly accounts meetings as per the Contract should be held between Finance and Enterprise management to review a breakdown of costs of the Core Contract Services and to challenge spend. In addition profits over a set level stated in the Contract are confirmed and a portion distributed to the Authority. These meetings should be supported by a Terms of Reference and minuted.	2	Accepted	These are in place but need to be scheduled in throughout the year.	Ross Cook / Andrew Cummings (Finance)	3/3/14 - Andrew Cummings from Finance now attends the monthly Partnership Monitoring meetings and further discussions are taking place as to the ongoing attendance and specific discussions regarding financial aspects of the contract (ie whether this financial issues will be discussed as part of the main meeting or as a separate discussion and the frequency of these meetings, monthly or quarterly). In addition, Ross Cook and Andrew Cummings now meet on a monthly basis, to review the overall contract expenditure, and Andrew also meets with the relevant Service Managers to monitor and review specific spend.	Original Target Date - 1 March 2014	
15	Incorrect or invalid waste information is provided by Enterprise to the Authority resulting in reduced recycling credit and landfill incentive from Gloucestershire County Council.	The Environmental Service Manager should obtain the following information from Enterprise: • A sample of waste weighbridge tickets should be obtained from Enterprise to confirm the waste recycled and landfill tonnage figures on the Enterprise provided Recycling spreadsheet is correct;	2	Accepted	Copies of weigh bridge tickets are already forwarded to the Environmental Service Manager by County Council (the disposal authority). In addition a joint waste audit is carried out by County and the Environmental Service Manager on an annual basis where a representative number of waste tickets are checked. These tickets include those relating to how much recycling is taken by processors. The next audit is due on 4 September.	Gordon Buchanan, Environmental Service Manager.	16/12/13 – this had already been completed when the Audit was carried out.	Immediately – Audit carried out with County on 4/09/13	

		• The financial value of the waste recycled and compared to the Contract Assumed Recyclate Value at year end to determine if the Authority or Enterprise is due additional payments from each other.							
16	The Incorrect waste recycling value is included in the Annual Contract Sum indexation calculation resulting in over or underpayments to Enterprise.	Investigate the reason for the identified difference in the recyclate value recorded in the Annual Contract Sum for the 2011/12 and 2012/13 against the equivalent Assumed Recyclate Value documented in the Contract. In addition regularly reforecast the recyclate value as per the Contract.	2	Accepted	This has been queried with Enterprise. The sum does not apparently relate solely to the assumed recycling value. I am awaiting a response from the General Manager.	Kevin Buckerfield	The monthly contract calculation values include an estimated re-cycling value of £643k per annum. The exercise into the re-cycling values will be undertaken following the contract extras portion of the exercise. The 2013/14 indexation should not be agreed until resolution is found to the outstanding indexation overcharges.	Information has been received from Amey regarding this discrepancy, this is currently being considered by Finance Change Manager	
17	Invoices for recycling credits and incentives are raised late or incorrectly to Gloucestershire County Council resulting in poor cashflow, financial constraints placed on public services and adverse publicity.	The following actions should be implemented: • The Environmental Service Manager take on the responsibility for raising of invoices, review and management of the applicable Gloucestershire County Council debtor account; • Waste recycling credit and incentive invoices should be raised promptly and through one of the Gloucestershire	2	Accepted	Agreed.	Lloyd Griffiths	3/3/14 – Lloyd Griffiths has met with the County and identified all outstanding invoices. The backdated payments (due to us) have now been invoiced for and all other payments are being collected. Lloyd met with County again on 6/2/14 to review ensure no other payments are due and that all future payments / invoices will go through him..	Discussions are ongoing with Finance. A procedure will be put in place. Completed – 6 February 2014	

		County Council debtor ids in order to avoid any confusion in invoicing and payment arrangements; • Consider deleting the production and issue of the automated quarterly incentive invoices or establish whether the 4th quarter invoice can be suspended to allow a manual invoice to be produced in its place; • A thorough review the 2 Gloucestershire County Council waste debtor accounts should be undertaken to determine what has been invoiced and what is actually owed. Appropriate adjustments to the account and/or recover action should then be promptly undertaken.							

AUDIT AND GOVERNANCE COMMITTEE – 17 MARCH 2014

ACTION PLAN

MINUTE NO.	MATTER	CURRENT STATUS	RAG	TARGET DATE	OWNER
Actions arising from meeting held on 24 September 2012:					
17	Combined Heat and Power installation at GL1.	Included in action 23 from meeting of 24 June 2013.	**A**	31.03.14	RW
17	Purchase of software with a modern stock control facility at The Guildhall.	The stock control facility is part of a broader system requirement for the Guildhall operations. A new Manager has now been appointed at the Guildhall, who will review existing processes and systems and develop a business case for a new system as required. This will include stock control functionality.	**A**	31.03.14	SG
21	Internal Audit Plan 2012/13 – Fixed Asset Register to be in place.	Detailed spreadsheet in place. Currently evaluating a system linked to the financial ledger. Financial System upgrade to be completed December 2013. Once upgrade completed successfully project will commence for asset register transfer to ledger.	**A**	Priority	JB
Actions arising from meeting held on 26 November 2012:					
34	RIPA – annual update and external inspection report to be presented to the Committee each year.	Report due to come to Audit & Governance on 25.11.13 – **Action complete**	**Complete 25.11.13**	25.11.13	SM
35	Business Rates Pooling – annual report to be presented to the Committee.	Report due to come to Audit & Governance in June 2014	**G**	24.06.14	PG

MINUTE NO.	MATTER	CURRENT STATUS	RAG	TARGET DATE	OWNER
Actions arising from meeting held on 24 June 2013:					
23	Combined Heat and Power Installation.	Following investigative works it has been identified that the CHP plant at GL1 is not functioning correctly. In order to resolve this matter, officers will be employing the services of a third party expert (quotes are currently being sought) to identify what measures can be taken to improve the installation. We would anticipate that survey work will be completed by the end of November. Allowing for due process, procurement procedures and subject to budgetary provision, we believe that remediation/improvement works will be undertaken first quarter 2014.	**A**	31.03.14	RW
29	Internal Audit – Quarterly Monitoring Report – the Payroll Client Manager to be invited to the Committee	This item has been added to the agenda for the Audit & Governance Committee meeting on 25.11.13 – **Action complete**	**Complete 25.11.13**	25.11.13	TR
Actions arising from meeting held on 23 September 2013:					
46	Response to Internal Audit Report Recommendations – Markets – update to be provided at the next meeting.	This item is included in the Internal Audit Plan Monitoring Report due to come to Audit & Governance on 25.11.13 – **Action complete**	**Complete 25.11.13**	25.11.13	TR
52	Annual Governance Statement 2012/13 – Committee requested confirmed target / completion dates to be included in the Action Plan.	Report due to come to Audit & Governance on 25.11.13 – **Action complete**	**Complete 25.11.13**	25.11.13	PG

MINUTE NO.	MATTER	CURRENT STATUS	RAG	TARGET DATE	OWNER
Actions arising from meeting held on 25 November 2013:					
67	Response to Internal Audit Report Recommendations – Client Monitoring of Payroll System – Audit, Risk & Assurance Manager to undertake a follow up audit and report back to the Committee.	Follow-up audit planned for February 2014 with reporting of findings to Audit & Governance Committee on 17.03.14.	G	17.03.14	TR
68	Response to Internal Audit Report Recommendations – Response Repairs Contract – Asset Manager to provide further update at the Audit & Governance Committee in March 2014	This item has been added to the agenda for the Audit & Governance Committee meeting on 17.03.14.	G	17.03.14	RW/TR
69	The Corporate Director of Resources to arrange Treasury Management Training event	This has been arranged to take place before the Audit and Governance Committee on 26 June 2014.	G	26.03.14	PG
70	Annual Governance Statement Action Plan 2013/14 – need to amend to read '31 January 2014'	Appropriate amendment made.	G	27.01.14	PG/TR
74	Internal Audit Plan 2013/14 – Monitoring Report – Streetcare Contract – Head of Neighbourhood Services to provide verbal update at the meeting in March 2014	This item has been added to the agenda for the Audit & Governance Committee meeting on 17.03.14.	G	17.03.14	RC/TR
80	Work Programme – Additional meeting of the Committee to be held in late January / early February	Meeting has been arranged for Monday, 27 January 2014	G	27.01.14	PG

PLEASE NOTE: Rolling agenda items requested by the Committee have not been included above but have been included on the Audit and Governance Work Programme.

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KPMG

cutting through complexity™

Certification of grants and returns 2012/13

Gloucester City Council

February 2014

Contents

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Page 36

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

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

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Darren Gilbert, who is the engagement leader to the Authority (telephone 0292 046 8205 e-mail darren.gilbert@kpmg.co.uk who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees (telephone 0161 236 4000, e-mail trevor.rees@kpmg.co.uk) who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 0303 444 8330.

Headlines

Introduction and background	**This report summarises the results of work on the certification of the Authority's 2012/13 grant claims and returns.** ■ For 2012/13 we certified: – one grant with a total value of £53.9m; and – two returns with a total value of £47.3m.	-
Certification results	**We issued unqualified certificates for two grants and returns but qualification was necessary in one case.** ■ This represents an improvement on the results for 2011/12 where three grants and returns received qualified certificates. ■ We qualified our certificate relating to the Housing & Council Tax Benefits Scheme. This was because the Authority had not used the latest version of the Civica Open Revenues System to prepare the grant claim form.	**Page 3**
Audit adjustments	**Adjustments were necessary to one the Authority's grants and returns as a result of our certification work this year.** ■ Adjustments were required in relation to the Housing & Council Tax Benefit Scheme to correct a transposition error which occurred in the completion of the claim form and in response to a system error around the identification of expenditure above the LHA Cap. Payments made in relation to Rent Allowances, both HRA and Non-HRA, are subject to a cap on the weekly benefit value. Where the payment made by the Authority exceeds the cap, the expenditure over the cap attracts nil subsidy. The Civica system is designed in such a way that is should automatically split out any payments made over the cap. Despite this, we identified inaccuracies in the split applied which arose from a system error and resulted in an overstatement of expenditure over the cap. The cumulative impact of these adjustments was to increase the value of the subsidy claimed by £16,222.	**Page 3**
The Authority's arrangements	**The Authority has adequate arrangements for preparing its grants and returns and supporting our certification work and has made improvements since the prior year.** ■ We recognise that the Authority has improved the overall arrangements in relation to the preparation of grants and returns, including the identification of a single officer who is responsible for co-ordinating the process and certification work. ■ We have raised one recommendation in relation to the need to ensure that required software upgrades are fully implemented prior to the preparation of related grants.	**Pages 4-5**
Fees	**The Audit Commission changed its fee regime for certifying grants and returns in 2012/13, and set an indicative fee for the Authority of £13,400. Our actual fee for the certification of grants and returns was £12,617.** ■ The difference was due to changes in the level of work required to certify the Authority's grants and returns. ■ This represents a significant reduction compared to the certification fees charged for 2011/12 as a result of the change in the fee regime applicable to certification work.	**Page 4**

Summary of certification work outcomes

Overall, we certified three grants and returns:

- **two were unqualified with no amendment; and**
- **one required a qualification to our audit certificate.**

The table summarises the key issues behind the adjustments and qualifications.

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

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

	Comments below	Qualified certificate	Significant adjustment	Minor adjustment	Unqualified certificate
Housing & Council Tax Benefit	1	●	●	●	
Pooling of Housing Capital Receipts					●
National Non Domestic Rates return					●
		1	**1**	**1**	**2**

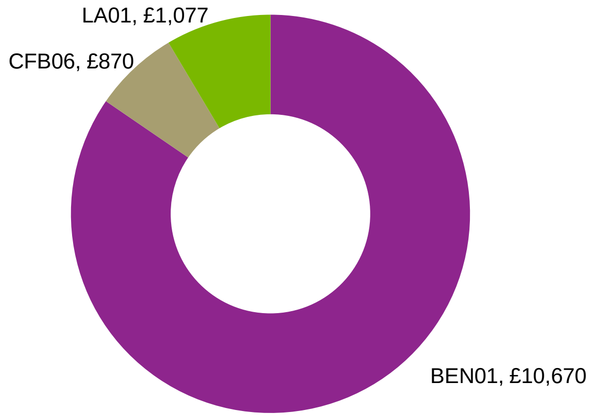
Ref	Summary observations	Amendment
1	**Housing & Council Tax Benefit** ▪ One minor amendment was required in order to correct a transposition error that had occurred during the preparation of the grant claim form. ▪ A more significant adjustment was required in order to account for a system error that we identified during the certification process. This error resulted in an incorrect split of expenditure above and below the LHA Cap which had incorrectly reduced the amount of subsidy claimed by the Authority. ▪ In addition to the amendments identified above, the grant certificate was qualified because the claim form was prepared using reports run from an out-dated version of the Civica Open Revenues System. This arose as a result of problems encountered during the implementation of an upgraded version of the software, so the Authority had to continue with the earlier version to prepare the claim form. Whilst these issues were subsequently resolved, and the software upgrade implemented, this was completed after the pre-audit claim form had been submitted. We were not able to quantify the impact that the installation of the upgrade would have had upon the subsidy claimed by the Authority.	+ £16,222

Fees

Our overall fee for the certification of grants and returns is significantly lower than the previous year and less than the original estimated fee.

Page 39

Breakdown of certification fees 2012/13



Breakdown of fee by grant/return

	2012/13 (£)	2011/12 (£)
BEN01 – Housing and Council Tax Benefit	10,670	21,594
CFB06 – Pooling of Housing Capital Receipts	870	1,983
LA01 – National Non Domestic Rates return	1,077	1,580
HOU01 – HRA Subsidy	-	6,656
Total fee	**12,617**	**31,813**

The Audit Commission changed its fee regime for certifying grants and returns in 2012/13. It set an indicative fee for the Authority of £13,400. Based on the actual work we carried out the actual fee we charged was lower than the indicative fee, at £12,617.

The main reasons for the fee being less than the indicative fee was that, in accordance with the Commission's three year cyclical approach, we did not undertake the detailed tested that was included in the original indicative fee for the National Non-Domestic Rates return.

We recognise that the Authority has improved the overall arrangements in relation to the preparation of grants and returns, including the identification of a single officer who is responsible for co-ordinating the process and certification work. In order to ensure that fees for future years are minimised it is essential that the Authority maintain a strong process in relation to the preparation of grants and returns going forward.

Recommendations

We have given each recommendation a risk rating and agreed what action management will need to take. We will follow up these recommendations during next year's audit.

Priority rating for recommendations		
❶ Issues that are fundamental and material to your overall arrangements for managing grants and returns or compliance with scheme requirements. We believe that these issues might mean that you do not meet a grant scheme requirement or reduce (mitigate) a risk.	❷ Issues that have an important effect on your arrangements for managing grants and returns or complying with scheme requirements, but do not need immediate action. You may still meet scheme requirements in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸ Issues that would, if corrected, improve your arrangements for managing grants and returns or compliance with scheme requirements in general, but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

Page 40

Issue	Implication	Recommendation	Priority	Comment	Responsible officer and target date
Housing & Council Tax Benefit					
System Versions The Authority completed the Housing & Council Tax Benefit Scheme claim form using an incorrect version of the Civica Open Revenues System (13.0.9 as opposed to 13.0.10). This arose as a result of problems encountered during the implementation of the upgrade in the test environment. As a result of this issue we were required to quality our certificate.	In relation to the 2012/13 year, it is likely that DWP will require further work to be undertaken in order to ascertain the impact of this issue. The completion of the claim form on an incorrect software version in future years will most likely result in qualification unless it is possible to calculate the full impact that would be had upon the entries to the form.	Review the events which resulted in the use of the incorrect software version in order to identify any lessons to be learned. Further to this, a timetable should be developed which ensures that any late software upgrades in future years will be capable of testing, resolution of issues, and full implementation prior to the completion of the grant form.	❶	We have reviewed the events that lead to the incorrect version of the software being used, and we will ensure that in future years the correct software releases will have been tested and applied before the grant claim form is completed.	**Responsible Officers:** Pauline Winters (Service Delivery Manager, Civica UK Ltd, Revenues & Benefits Service) Jon Topping (Gloucester City Council Head of Financial Services) **Target Date:** Ongoing

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External Audit Plan 2013/14

Gloucester City Council

March 2014

Contents

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Page 44

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

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

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Darren Gilbert, the appointed engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 03034448330.

Introduction

This document describes how we will deliver our audit work for Gloucester City Council.

Scope of this report

This document supplements our *Audit Fee Letter 2013/14* presented to you in June 2013. It describes how we will deliver our financial statements audit work for Gloucester City Council ('the Authority'). It also sets out our approach to value for money (VFM) work for 2013/14.

We are required to satisfy ourselves that your accounts comply with statutory requirements and that proper practices have been observed in compiling them. We use a risk based audit approach.

The audit planning process and risk assessment is an on-going process and the assessment and fees in this plan will be kept under review and updated if necessary.

Statutory responsibilities

Our statutory responsibilities and powers are set out in the *Audit Commission Act 1998* and the Audit Commission's *Code of Audit Practice*.

The *Code of Audit Practice* summarises our responsibilities into two objectives, requiring us to review and report on your:

- *financial statements (including the Annual Governance Statement):* providing an opinion on your accounts; and
- *use of resources:* concluding on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the value for money conclusion).

The Audit Commission's *Statement of Responsibilities of Auditors and Audited Bodies* sets out the respective responsibilities of the auditor and the Authority.

Structure of this report

This report is structured as follows:

- Section 2 includes our headline messages, including any key risks identified this year for the financial statements and Value for Money audit.
- Section 3 describes the approach we take for the audit of the financial statements.
- Section 4 provides further detail on the financial statements audit risks.
- Section 5 explains our approach to VFM work and sets out our initial risk assessment for the VFM conclusion.
- Section 6 provides information on the audit team, our proposed deliverables, the timescales and fees for our work.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

Headlines

This table summarises the headline messages. The remainder of this report provides further details on each area.

Page 46

Audit approach	Our overall audit approach is unchanged from last year. Our work is carried out in four stages and the timings for these, and specifically our on site work, have been agreed with the Corporate Director of Resources. Our audit strategy and plan remain flexible as risks and issues change throughout the year. We will review the initial assessments presented in this document throughout the year and should any new risks emerge we will evaluate these and respond accordingly.
Key financial statements audit risks	We have completed our initial risk assessment for the financial statements audit and have identified the following significant risks (which are areas that will attract particular focus during our audit): ■ Fixed asset register – Recent audits have highlighted weaknesses in the accounting for fixed assets and there is therefore a risk around the completeness and accuracy of data. The implementation of a new fixed asset register will require a detailed review and cleansing of the data currently held by the Council to ensure the information transferred is complete, accurate and fit-for-purpose. This exercise will be undertaken during 2013/14, although the new asset register is unlikely to be implemented for the 2013/14 audit; ■ LGPS triennial valuation – During the year, the Gloucestershire County Council Pension Fund has undergone a triennial valuation. There is a risk that the data provided to the actuary for the valuation exercise is inaccurate and that these inaccuracies affect the actuarial figures in the Council's accounts; and ■ Year end closedown and accounts preparation – The Council has made good progress in the last two years to improve the quality of accounts presented for audit, but there has historically been a large number of adjustments made between the draft and final versions of the accounts and there remains a need to demonstrate significant improvement in these arrangements. The Council needs to continue this direction of travel and ensure it produces a good quality set of draft financial statements for audit. It has made some key senior appointments in the Finance team to address this, thereby reducing its reliance on interim finance staff. These are described in more detail on pages 11 to 12. We will assess the Authority's progress in addressing these risk areas as part of our interim work and conclude this work at year end.

Headlines (continued)

VFM audit approach	We have completed our initial risk assessment for the VFM conclusion and have identified the following significant risks: ■ Contract monitoring – There is a risk that the Council is not carrying out effective contract monitoring to ensure that it pays the correct amount for services provided and that it obtains value for money from its contractors; ■ Savings plans – There is a risk that savings plans are not monitored effectively and that the Authority does not make the required savings in order to meet its budget; and ■ Budgetary control – The Council took steps last year to address weaknesses relating to its budgetary control arrangements. This process has continued during the year. Robust budgetary control and monitoring is key to delivering value for money, so we will follow up the recommendations made in our 2012/13 *Report to Those Charged with Governance (ISA 260 Report).* These are described in more detail on pages 17 to 18.
Audit team, deliverables, timeline and fees	There have been minimal changes to the audit team from last year. Our main year end audit is currently planned to commence on 21 July 2014. Upon conclusion of our work we will again present our findings to you in our *Report to Those Charged with Governance (ISA 260 Report)*. The planned fee for the 2013/14 audit is £115,000. This is a reduction of £24,500 from the position set out in our *Audit Fee Letter 2013/14*, although this reduction is still subject to determination by the Audit Commission.

Our audit approach

We undertake our work on your financial statements in four key stages during 2014:

- **Planning (January to March).**
- **Control Evaluation (March).**
- **Substantive Procedures (July to August).**
- **Completion (September).**

We have summarised the four key stages of our financial statements audit process for you below:

	Stage	Activity	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep
1	Planning	Update our business understanding and risk assessment.	○								
		Assess the organisational control environment.			○						
		Determine our audit strategy and plan the audit approach.			○						
		Issue our *Accounts Audit Protocol*.			○						
2	Control evaluation	Evaluate and test selected controls over key financial systems.			○						
		Review the internal audit function.			○						
		Review the accounts production process.			○						
		Review progress on critical accounting matters.			○						
3	Substantive procedures	Plan and perform substantive audit procedures.						○	○	○	
		Conclude on critical accounting matters.							○	○	
		Identify audit adjustments.							○	○	
		Review the Annual Governance Statement.							○	○	
4	Completion	Declare our independence and objectivity.									○
		Obtain management representations.									○
		Report matters of governance interest.						○			○
		Form our audit opinion.									○

Our audit approach – planning

During January to March 2014 we complete our planning work.

We assess the key risks affecting the Authority's financial statements and discuss these with officers.

We assess if there are any weaknesses in respect of central processes, including the Authority's IT systems, that would impact on our audit.

Page 49

Our planning work takes place from January to March 2014. This involves the following aspects:

Planning

- Update our business understanding and risk assessment.
- Assess the organisational control environment.
- Determine our audit strategy and plan the audit approach.
- Issue our *Accounts Audit Protocol*.

Business understanding and risk assessment

We update our understanding of the Authority's operations and identify any areas that will require particular attention during our audit of the Authority's financial statements.

We identify the key risks affecting the Authority's financial statements. These are based on our knowledge of the Authority, our sector experience and our ongoing dialogue with Authority staff. Any risks identified to date through our risk assessment process are set out in this document. Our audit strategy and plan will, however, remain flexible as the risks and issues change throughout the year. It is the Authority's responsibility to adequately address these issues. We encourage the Authority to raise any technical issues with us as early as possible so that we can agree the accounting treatment in advance of the audit visit.

We meet with the Finance team on a regular basis to consider issues and how they are addressed during the financial year end closedown and accounts preparation.

Organisational control environment

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would impact on our audit.

In particular risk management, internal control and ethics and conduct have implications for our financial statements audit. The scope of the work of your internal auditors also informs our risk assessment.

The Authority relies on information technology (IT) to support both financial reporting and internal control processes. In order to satisfy ourselves that we can rely on the use of IT, we consider and test selective controls over access to systems and data, system changes, system development and computer operations. Whilst we undertake some general IT controls work, we also focus on testing the specific applications and reports that are pivotal to the production of the financial statements.

Audit strategy and approach to materiality

Our audit is performed in accordance with International Standards on Auditing (ISAs) (UK and Ireland). The Engagement Lead sets the overall direction of the audit and decides the nature and extent of audit activities. We design audit procedures in response to the risk that the financial statements are materially misstated. The materiality level is a matter of judgement and is set by the Engagement Lead.

In accordance with ISA 320 '*Audit materiality*', we plan and perform our audit to provide reasonable assurance that the financial statements are free of material misstatement and give a true and fair view. Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements.

An indicative level of materiality for 2013/14 is £4.9 million. This is based on the prior year Statement of Accounts and on our understanding of the projected outturn for the current year. This figure is a guide only. The overriding objective is to preserve the true and fair view presented by the financial statements and we will consider any audit differences, individually and cumulatively, in that context. See appendix 3 for further details.

Our audit approach – planning (continued)

We will report on any significant matters arising from the work of the auditors of Gloucester City Homes Ltd and Gloucestershire Airport Ltd which we seek to rely on to support our audit of the Authority's group accounts.

We will issue our *Accounts audit protocol* following completion of our planning work.

Page 50

Group audit

In addition to the Authority we anticipate the following subsidiaries and joint ventures to be significant in the context of the group audit:

- Gloucester City Homes Ltd; and
- Gloucestershire Airport Ltd.

We will keep this area under review to ensure that the assessment of entities to be consolidated in the group accounts remains appropriate.

To support our audit work on the Authority's group accounts, we anticipate seeking to place reliance on the work of Baker Tilly and Hazlewoods who are the auditors to these bodies. We will liaise with them in order to confirm that their programme of work is adequate for our purposes and they satisfy professional requirements.

We will report the following matters in our *ISA 260 Report:*

- any deficiencies in the system of internal controls or instances of fraud which the subsidiary auditors identify;
- any limitations on the group audit, for example, where the our access to information may have been restricted; and
- any instances where our evaluation of the work the subsidiary auditors gives rise to concern about the quality of that auditor's work.

Accounts audit protocol

At the end of our planning work we will issue our *Accounts Audit Protocol*. This important document sets out our audit approach and timetable. It also summarises the working papers and other evidence we require the Authority to provide during our interim and final accounts visits.

We met with the Head of Financial Services to discuss mutual learning points from the 2012/13 audit. These will be incorporated into our work plan for 2013/14. We revisit progress against areas identified for development as the audit progresses.

Our audit approach – control evaluation

During March 2014 we will complete our interim audit work.

We assess if controls over key financial systems were effective during 2013/14. We work with your internal audit team to avoid duplication.

We work with your Finance team to enhance the efficiency of the accounts audit.

We will report any significant findings arising from our work to the Audit & Governance Committee.

Our interim visit on site will be completed during March. During this time we will complete work in the following areas:

Control Evaluation

- Evaluate and test controls over key financial systems identified as part of our risk assessment.
- Review the work undertaken by the internal audit function on controls relevant to our risk assessment.
- Review the accounts production process.
- Review progress on critical accounting matters.

Controls over key financial systems

We update our understanding of the Authority's key financial processes where our risk assessment has identified that these are relevant to our final accounts audit and where we have determined that this is the most efficient audit approach to take. We confirm our understanding by completing walkthroughs for these systems. We then test selected controls that address key risks within these systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Where our audit approach is to undertake controls work on financial systems, we seek to rely on any relevant work internal audit have completed to minimise unnecessary duplication of work. Our audit fee is set on the assumption that we can place reliance on their work. We have a joint working protocol and have met with the Head of Internal Audit to discuss the principles and timetables for the managed audit process for 2013/14.

Review of internal audit

Where we intend to rely on internal audit's work in respect of the key financial systems identified as part of our risk assessment, auditing standards require us to review aspects of their work. This includes re-performing a sample of tests completed by internal audit. We will provide detailed feedback to the Head of Internal Audit at the end of our interim visit.

Accounts production process

We raised a number of recommendations in our *ISA 260 Report 2012/13* relating to the accounts production process. The most significant of these were to:

- Review and rationalise the number of nominal ledger codes within the general ledger to ensure that this is more manageable for Finance.
- Make an adjustment each year between the Revaluation Reserve and the Capital Adjustment Account to ensure that, where assets are fully written down, there is no residual balance in the Revaluation Reserve.
- Undertake a detailed review of community and intangible assets to identify whether they meet the definition of capital expenditure as per the Authority's accounting policy and per the Code (for intangibles) and have been correctly classified (for infrastructure / community assets).

We will assess the Authority's progress in addressing our recommendations and in preparing for the closedown and accounts preparation.

Critical accounting matters

We will discuss the work completed to address the specific risks we identified at the planning stage. Wherever possible, we seek to review relevant workings and evidence and agree the accounting treatment as part of our interim work.

If there are any significant findings arising from our interim work we will present these to the Audit & Governance Committee in June 2014.

Our audit approach – substantive procedures

During July and August 2014 we will be on site for our substantive work.

We complete detailed testing of accounts and disclosures and conclude on critical accounting matters, such as specific risk areas. We then agree any audit adjustments required to the financial statements.

Page 52

We also review the Annual Governance Statement for consistency with our understanding.

We will present our *ISA 260 Report* to the Audit and Governance Committee in September 2014.

Our final accounts visit on site has been provisionally scheduled for the period 21 July to 11 August. During this time, we will complete the following work:

Substantive Procedures

- Plan and perform substantive audit procedures.
- Conclude on critical accounting matters.
- Identify and assess any audit adjustments.
- Review the Annual Governance Statement.

Substantive audit procedures

We complete detailed testing on significant balances and disclosures. The extent of our work is determined by the Engagement Lead based on various factors such as our overall assessment of the Authority's control environment, the effectiveness of controls over individual systems and the management of specific risk factors.

Critical accounting matters

We conclude our testing of key risk areas identified at the planning stage and any additional issues that may have emerged since.

We will discuss our early findings of the Authority's approach to address the key risk areas with the Head of Financial Services in April 2014, prior to reporting to the Audit & Governance Committee on 26 June 2014.

Audit adjustments

During our on site work, we will meet with the Head of Financial Services on a weekly basis to discuss the progress of the audit, any differences found and any other issues emerging.

At the end of our on site work, we will hold a closure meeting, where we will provide a schedule of audit differences and agree a timetable for the completion stage and the accounts sign off.

To comply with auditing standards, we are required to report uncorrected audit differences to the Audit and Governance Committee. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

Annual Governance Statement

We are also required to satisfy ourselves that your Annual Governance Statement complies with the applicable framework and is consistent with our understanding of your operations. Our review of the work of internal audit and consideration of your risk management and governance arrangements are key to this.

We report the findings of our final accounts work in our *ISA 260 Report*, which we will issue in September 2014.

Our audit approach – other

In addition to the financial statements, we also audit the Authority's Whole of Government Accounts pack.

We may need to undertake additional work if we receive objections to the accounts from local electors.

We will communicate with you throughout the year, both formally and informally.

Whole of government accounts (WGA)

We are required to review and issue an opinion on your WGA consolidation to confirm that this is consistent with your financial statements. The audit approach has been agreed with HM Treasury and the National Audit Office. Deadlines for production of the pack and issue of our opinion on the pack have not yet been confirmed.

Elector challenge

The Audit Commission Act 1998 gives electors certain rights. These are:

- the right to inspect the accounts;
- the right to ask the auditor questions about the accounts; and
- the right to object to the accounts.

As a result of these rights, in particular the right to object to the accounts, we may need to undertake additional work to form our decision on the elector's objection. The additional work could range from a small piece of work where we interview an officer and review evidence to form our decision, to a more detailed piece of work, where we have to interview a range of officers, review significant amounts of evidence and seek legal representations on the issues raised.

The costs incurred in responding to specific questions or objections raised by electors is not part of the fee. This work will be charged in accordance with the Audit Commission's fee scales.

Reporting and communication

Reporting is a key part of the audit process, not only in communicating the audit findings for the year, but also in ensuring the audit team are accountable to you in addressing the issues identified as part of the audit strategy. Throughout the year we will communicate with you through meetings with the finance team and the Audit and Governance Committee. Our deliverables are included on page 20.

Independence and objectivity confirmation

Professional standards require auditors to communicate to those charged with governance, at least annually, all relationships that may bear on the firm's independence and the objectivity of the audit engagement partner and audit staff. The standards also place requirements on auditors in relation to integrity, objectivity and independence.

The standards define 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case this is the Audit and Governance Committee.

KPMG LLP is committed to being and being seen to be independent. APB Ethical Standard 1 Integrity, Objectivity and Independence requires us to communicate to you in writing all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place, in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of the Engagement Lead and the audit team.

Appendix 1 provides further detail on auditors' responsibilities regarding independence and objectivity.

Confirmation statement

We confirm that as of date of this report in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Engagement Lead and audit team is not impaired.

Key financial statements audit risks

In this section we set out our assessment of the significant risks to the audit of the Authority's financial statements for 2013/14.

For each key risk area we have outlined the impact on our audit plan.

Page 54

Professional standards require us to consider two standard risks for all organisations. We are not elaborating on these standard risks in this plan but consider them as a matter of course in our audit and will include any findings arising from our work in our *ISA 260 Report*.

- Management override of controls – Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.
- Fraudulent revenue recognition – We do not consider this to be a significant risk for local authorities as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebut this risk and do not incorporate specific work into our audit plan in this area over and above our standard fraud procedures.

The table below sets out the significant risks we have identified through our planning work that are specific to the audit of the Authority's financial statements for 2013/14.

We will revisit our assessment throughout the year and should any additional risks present themselves we will adjust our audit strategy as necessary.

Key audit risks	Impact on audit
Fixed asset register **Audit areas affected** - Property, plant and equipment	**Risk** Recent audits have highlighted weaknesses in the accounting for fixed assets and there is therefore a risk around the completeness and accuracy of data. The implementation of a new fixed asset register will require a detailed review and cleansing of the data currently held by the Council to ensure the information transferred is complete, accurate and fit-for-purpose. This exercise will be undertaken during 2013/14, although the new asset register is unlikely to be implemented for the 2013/14 audit. **Our audit work** We will assess the controls the Council has in place around fixed asset recording and capital accounting to ensure appropriate processes are in place to monitor and regulate the Council's asset position. We will review the outcome of the data cleansing exercise being carried out by the Finance team and will take note of the findings from Internal Audit's review of the data transfer. We will carry out testing at year end on any specific areas of risk highlighted by the reviews.

Key financial statements audit risks (continued)

For each key risk area we have outlined the impact on our audit plan.

Page 55

Key audit risks	Impact on audit
LGPS Triennial Valuation **Audit areas affected** ■ Pension liability calculations and disclosures	**Risk** During the year, the Gloucestershire County Council Pension Fund has undergone a triennial valuation with an effective date of 31 March 2013 in line with the Local Government Pension Scheme (Administration) Regulations 2008. The share of pensions assets and liabilities for each admitted body is determined in detail, and a large volume of data is provided to the actuary to support this triennial valuation. The pension cost and net liability figures for the Authority to be included in the financial statements for 2013/14 will be based on the output of the triennial valuation rolled forward to 31 March 2014. For 2014/15 and 2015/16 the actuary will then roll forward the valuation for accounting purposes based on more limited data. There is a risk that the data provided to the actuary for the valuation exercise is inaccurate and that these inaccuracies affect the actuarial figures in the accounts. **Our audit work** We will complete testing to agree the data provided to the actuary back to the systems and reports from which it was derived, and to understand the controls in place to ensure the accuracy of this data.

Key financial statements audit risks (continued)

For each key risk area we have outlined the impact on our audit plan.

Key audit risks	Impact on audit
Closedown and accounts preparation **Audit areas affected** ▪ All areas of the financial statements	**Risk** The Council has made good progress in the last two years to improve the quality of accounts presented for audit, but there has historically been a large number of adjustments made between the draft and final versions of the accounts and there remains a need to demonstrate significant improvement in these arrangements. The Council needs to continue this direction of travel and ensure it produces a good quality set of draft financial statements for audit. It has made some key senior appointments in the Finance team to address this, thereby reducing its reliance on interim finance staff. **Our audit work** We will monitor closely the Council’s closedown plan and discuss with the Finance team how both the preparation of the financial statements and the support of our audit will be delivered. We will also consider the progress the Council has made to prepare and report its draft financial statements within the required 30 June deadline.

VFM audit approach

Our approach to VFM work follows guidance provided by the Audit Commission.

Page 57

Background to approach to VFM work

In meeting their statutory responsibilities relating to economy, efficiency and effectiveness, the Commission's *Code of Audit Practice* requires auditors to:

- plan their work based on consideration of the significant risks of giving a wrong conclusion (audit risk); and
- carry out only as much work as is appropriate to enable them to give a safe VFM conclusion.

To provide stability for auditors and audited bodies, the Audit Commission has kept the VFM audit methodology unchanged from last year. There are only relatively minor amendments to reflect the key issues facing the local government sector.

The approach is structured under two themes, as summarised below.

Specified criteria for VFM conclusion	Focus of the criteria	Sub-sections
The organisation has proper arrangements in place for securing **financial resilience**.	The organisation has robust systems and processes to: ▪ manage effectively financial risks and opportunities; and ▪ secure a stable financial position that enables it to continue to operate for the foreseeable future.	▪ Financial governance ▪ Financial planning ▪ Financial control
The organisation has proper arrangements for challenging how it **secures economy, efficiency and effectiveness**.	The organisation is prioritising its resources within tighter budgets, for example by: ▪ achieving cost reductions; and ▪ improving efficiency and productivity.	▪ Prioritising resources ▪ Improving efficiency and productivity

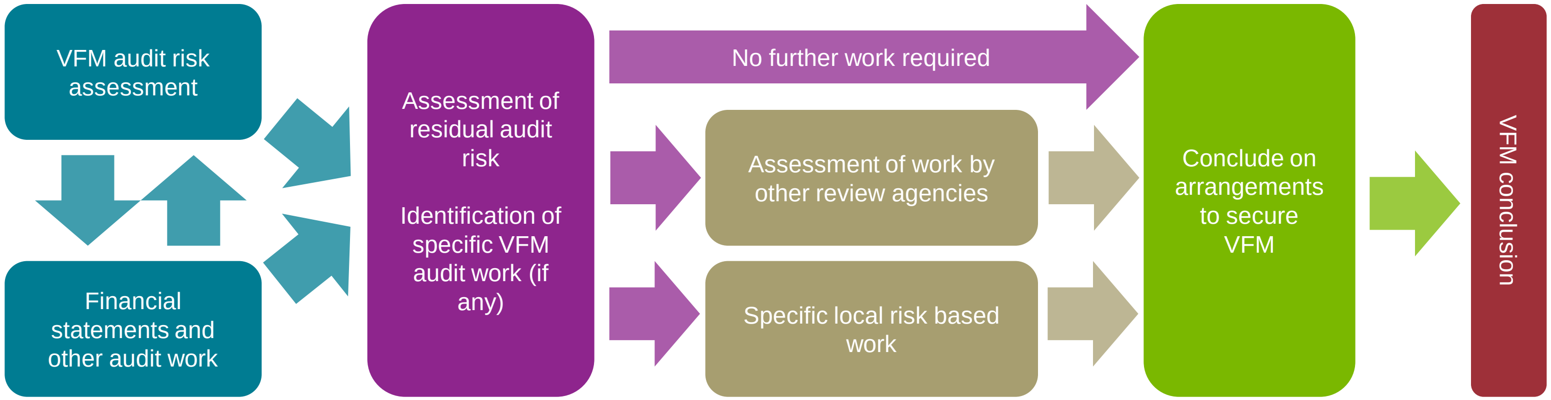
VFM audit approach (continued)

We will follow a risk based approach to target audit effort on the areas of greatest audit risk.

Page 58

Overview of the VFM audit approach

The key elements of the VFM audit approach are summarised below.



Each of these stages are summarised further below.

VFM audit stage	Audit approach
VFM audit risk assessment	We consider the relevance and significance of the potential business risks faced by all local authorities, and other risks that apply specifically to the Authority. These are the significant operational and financial risks in achieving statutory functions and objectives, which are relevant to auditors' responsibilities under the *Code of Audit Practice*. In doing so we consider: ■ the Authority's own assessment of the risks it faces, and its arrangements to manage and address its risks; ■ information from the Audit Commission's VFM profile tool and financial ratios tool; ■ evidence gained from previous audit work, including the response to that work; and ■ the work of other inspectorates and review agencies.

VFM audit approach (continued)

Our VFM audit will draw heavily on other audit work which is relevant to our VFM responsibilities and the results of last year's VFM audit.

We will then form an assessment of residual audit risk to identify if there are any areas where more detailed VFM audit work is required.

Page 59

VFM audit stage	Audit approach
Linkages with financial statements and other audit work	There is a degree of overlap between the work we do as part of the VFM audit and our financial statements audit. For example, our financial statements audit includes an assessment and testing of the Authority's organisational control environment, including the Authority's financial management and governance arrangements, many aspects of which are relevant to our VFM audit responsibilities. We have always sought to avoid duplication of audit effort by integrating our financial statements and VFM work, and this will continue. We will therefore draw upon relevant aspects of our financial statements audit work to inform the VFM audit.
Assessment of residual audit risk	It is possible that further audit work may be necessary in some areas to ensure sufficient coverage of the two VFM criteria. Such work may involve interviews with relevant officers and /or the review of documents such as policies, plans and minutes. We may also refer to any self assessment the Authority may prepare against the characteristics. To inform any further work we must draw together an assessment of residual audit risk, taking account of the work undertaken already. This will identify those areas requiring further specific audit work to inform the VFM conclusion. At this stage it is not possible to indicate the number or type of residual audit risks that might require additional audit work, and therefore the overall scale of work cannot be easily predicted. If a significant amount of work is necessary then we will need to review the adequacy of our agreed audit fee.
Identification of specific VFM audit work	If we identify residual audit risks, then we will highlight the risk to the Authority and consider the most appropriate audit response in each case, including: ■ considering the results of work by the Authority, inspectorates and other review agencies; and ■ carrying out local risk-based work to form a view on the adequacy of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources.

VFM audit approach (continued)

Where relevant, we may draw upon the range of audit tools and review guides developed by the Audit Commission.

We will conclude on the results of the VFM audit through our ISA 260 Report.

Page 60

VFM audit stage	Audit approach
Delivery of local risk based work	Depending on the nature of the residual audit risk identified, we may be able to draw on audit tools and sources of guidance when undertaking specific local risk-based audit work, such as: ■ local savings review guides based on selected previous Audit Commission national studies; and ■ update briefings for previous Audit Commission studies. The tools and guides will support our work where we have identified a local risk that is relevant to them. For any residual audit risks that relate to issues not covered by one of these tools, we will develop an appropriate audit approach drawing on the detailed VFM guidance and other sources of information.
Concluding on VFM arrangements	At the conclusion of the VFM audit we will consider the results of the work undertaken and assess the assurance obtained against each of the VFM themes regarding the adequacy of the Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources. If any issues are identified that may be significant to this assessment, and in particular if there are issues that indicate we may need to consider qualifying our VFM conclusion, we will discuss these with management as soon as possible. Such issues will also be considered more widely as part of KPMG's quality control processes, to help ensure the consistency of auditors' decisions.
Reporting	We will report on the results of the VFM audit through our *ISA 260 Report*. This will summarise any specific matters arising, and the basis for our overall conclusion. The key output from the work will be the VFM conclusion (i.e. our opinion on the Authority's arrangements for securing VFM), which forms part of our audit report.

VFM audit approach (continued)

We have identified a number of specific VFM risks.

We will carry out additional risk-based work in the following areas:

- **Contract monitoring**
- **Savings plans**
- **Budgetary control**

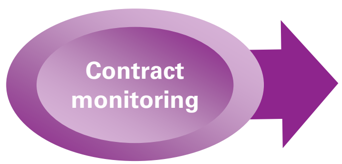
Page 61

In line with the risk-based approach set out on the previous page, we have

- assessed the Authority's key business risks which are relevant to our VFM conclusion;
- identified the residual audit risks for our VFM conclusion, taking account of work undertaken in previous years or as part of our financial statements audit;
- considered the results of relevant work by the Authority, the Audit Commission, other inspectorates and review agencies in relation to these risk areas; and
- concluded to what extent we need to carry out additional risk-based work.

Below we set out our preliminary findings in respect of those areas where we have identified a residual audit risk for our VFM conclusion,

We will report our final conclusions in our *ISA 260 Report 2013/14*.

Key VFM risk	Risk description and link to VFM conclusion	Audit work planned
	The Council has a number of contracts with third parties to provide services, such as neighbourhood services and IT. An Internal Audit review in 2012/13 identified that the Council had been overcharged on one of its contracts. There is a risk that the Council is not carrying out effective contract monitoring to ensure that it pays the correct amount for services provided and that it obtains value for money from its contractors. This is relevant to the economy, efficiency and effectiveness criteria of the VFM conclusion.	We will assess the arrangements in place to monitor the Council's contracts and ensure that the Council is achieving value for money. The Council is undertaking a detailed review of one of its major outsourcing contracts. We will note the outcomes of the work and feed it into our assessment.

VFM audit approach (continued)

Page 62

Key VFM risk	Risk description and link to VFM conclusion	Audit work planned
Savings plans	The savings plan target for the Authority for 2013/14 is £1.9m. This was built into the budget agreed by the Council and Cabinet at the start of the year. There is a risk that savings plans are not being monitored and that the Authority does not make the required savings in order to meet its budget. This is relevant to the financial resilience criteria of the VFM conclusion.	We will assess the arrangements the Council has in place to ensure a sound financial standing, specifically that its Medium Term Financial Plan has duly taken into consideration the potential funding reductions and that it is sufficiently robust to ensure that the Council can continue to provide services effectively. We will also review how the Council is planning and monitoring progress against its savings plans.
Budgetary control	The Council took steps last year to address weaknesses relating to its budgetary control arrangements. This process has continued during the year. Robust budgetary control and monitoring is key to delivering value for money, so we will follow up the recommendations made in our 2012/13 *Report to Those Charged with Governance (ISA 260 Report).* This is relevant to both the financial resilience and economy, efficiency and effectiveness criteria of the VFM conclusion.	We will review the budgetary control process to ensure it is operating effectively in the current financial year and to assess the progress made in implementing our prior year recommendations in this area.

Audit team

Your audit team has been drawn from our specialist public sector assurance department. With the exception of Rhys Hopkin, our audit team were all part of the Gloucester City Council audit last year.

Contact details are shown on page 1.

The audit team will be assisted by other KPMG specialists as necessary.

Darren Gilbert

Director

"My role is to lead our team and ensure the delivery of a high quality, valued added external audit opinion.

I will be the main point of contact for the Audit & Governance Committee and Chief Executive."

Tara Westcott

Senior Manager

"I provide quality assurance for the audit work and specifically any technical accounting and risk areas.

I will work closely with director to ensure we add value.

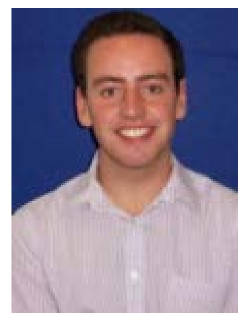
I will liaise with the Corporate Director of Resources and other Executive Directors."

Duncan Laird

Manager

"I am responsible for the management, review and delivery of the audit.

I will liaise with the Head of Finance and Head of Internal Audit."



Rhys Hopkin

Assistant Manager

"I will be responsible for the on-site delivery of our work and will supervise the work of our audit assistants."

Audit deliverables

At the end of each stage of our audit we issue certain deliverables, including reports and opinions.

Our key deliverables will be delivered to a high standard and on time.

We will discuss and agreed each report with the Authority's officers prior to publication.

Deliverable	Purpose	Committee dates
Planning		
External Audit Plan	■ Outlines our audit approach. ■ Identifies areas of audit focus and planned procedures.	**March 2014**
Control evaluation		
Interim Report	■ Details control and process issues. ■ Identifies improvements required prior to the issue of the draft financial statements and the year-end audit.	**June 2014**
Substantive procedures		
Report to Those Charged with Governance (ISA 260 Report)	■ Details the resolution of key audit issues. ■ Communicates adjusted and unadjusted audit differences. ■ Highlights performance improvement recommendations identified during our audit. ■ Comments on the Authority's value for money arrangements.	**September 2014**
Completion		
Auditor's Report	■ Provides an opinion on your accounts (including the Annual Governance Statement). ■ Concludes on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the VFM conclusion).	**September 2014**
Whole of Government Accounts	■ Provide our opinion on the Authority's WGA pack submission.	**September 2014**
Annual Audit Letter	■ Summarises the outcomes and the key issues arising from our audit work for the year.	**November 2014**

Audit timeline

We will be in continuous dialogue with you throughout the audit.

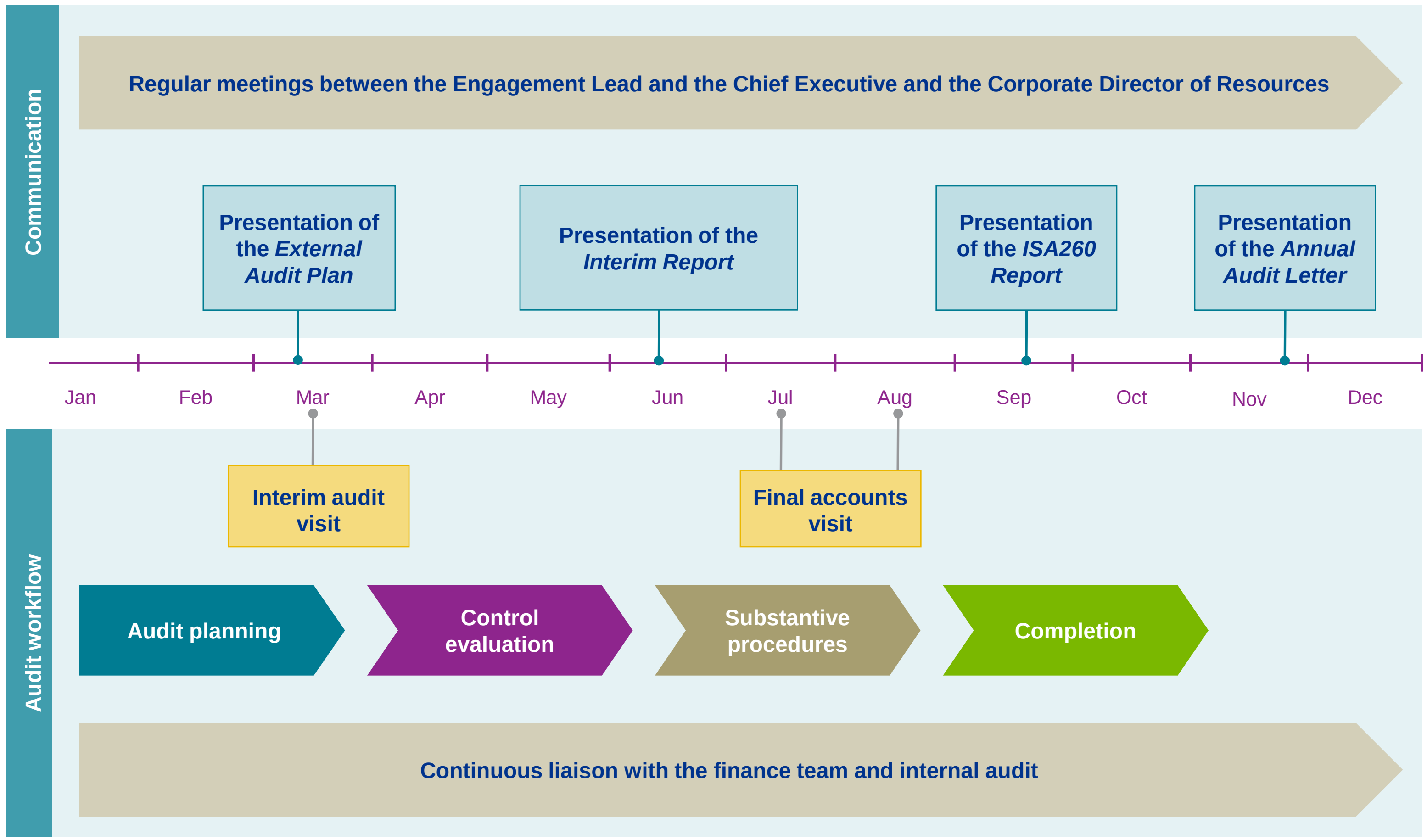
Key formal interactions with the Audit Committee are:

- **March – External Audit Plan;**
- **June – Interim Report;**
- **September – ISA 260 Report;**
- **November – Annual Audit Letter.**

We work with the finance team and internal audit throughout the year.

Our main work on site will be our:

- **Interim audit visit during March.**
- **Final accounts audit during July and August.**



Key: ● Audit Committee meetings.

Audit fee

The planned fee for the 2013/14 audit of the Authority is £115,000. We have reduced the fee from that set out in our *Audit Fee Letter 2013/14* issued in June 2013.

Our audit fee remains indicative and will be subject to determination by the Audit Commission. It is based on you meeting our expectations of your support.

Meeting these expectations will help the delivery of our audit within the proposed audit fee.

Audit fee

Our audit fee includes our work on the VFM conclusion and our audit of the Authority's financial statements.

The planned audit fee for 2013/14 is £115,000. This is a reduction of £24,500 on the final 2012/13 audit fee and the fee proposed originally in our *Audit Fee Letter 2013/14* in June 2013 (both of which were £139,500). This recognises the improvements made by the Council in the last 18 months, allowing us to plan for less audit work than previous years, but still reflecting the overall risk profile and the changes that are being made by the Council. The fee therefore remains higher than the Audit Commission's scale fee of £83,700.

The fee will be subject to determination by the Audit Commission.

Audit fee assumptions

The fee is based on a number of assumptions, including that you will provide us with complete and materially accurate financial statements, with good quality supporting working papers, within agreed timeframes. It is imperative that you achieve this. If this is not the case and we have to complete more work than was envisaged, we will need to charge additional fees for this work. In setting the fee, we have assumed:

- the improvements in financial reporting and the control environment that we anticipate from the changes the Council has made are delivered, sustained and are effective;
- you will inform us of any significant developments impacting on our audit;
- you will identify and implement any changes required under the *CIPFA Code of Practice on Local Authority Accounting in the UK 2013/14* within your 2013/14 financial statements;
- you will comply with the expectations set out in our *Accounts Audit Protocol*, including:
  - the financial statements are made available for audit in line with the agreed timescales;
  - good quality working papers and records will be provided at the start of the final accounts audit;
  - requested information will be provided within the agreed timescales;
  - prompt responses will be provided to queries and draft reports;
- internal audit meets appropriate professional standards;
- internal audit adheres to our joint working protocol and completes appropriate work on all systems that provide material figures for the financial statements and we can place reliance on them for our audit; and
- additional work will not be required to address questions or objections raised by local government electors or for special investigations such as those arising from disclosures under the Public Interest Disclosure Act 1998.

Meeting these expectations will help ensure the delivery of our audit within the agreed audit fee.

The Audit Commission requires us to inform you of specific actions you could take to reduce the audit fee. Future audit fees can be reduced if the Authority achieves an efficient and well-controlled financial closedown and accounts production process which complies with good practice and appropriately addresses new accounting developments and risk areas.

Changes to the audit plan

Changes to this plan and the audit fee may be necessary if:

- new significant audit risks emerge;
- additional work is required of us by the Audit Commission or other regulators; and
- additional work is required as a result of changes in legislation, professional standards or financial reporting requirements.

If changes to this plan and the audit fee are required, we will discuss and agree these initially with the Corporate Director of Resources.

Appendix 1: Independence and objectivity requirements

This appendix summarises auditors' responsibilities regarding independence and objectivity.

Independence and objectivity

Auditors are required by the Code to:

- carry out their work with independence and objectivity;
- exercise their professional judgement and act independently of both the Commission and the audited body;
- maintain an objective attitude at all times and not act in any way that might give rise to, or be perceived to give rise to, a conflict of interest; and
- resist any improper attempt to influence their judgement in the conduct of the audit.

In addition, the Code specifies that auditors should not carry out work for an audited body that does not relate directly to the discharge of the auditors' functions under the Code. If the Authority invites us to carry out risk-based work in a particular area, which cannot otherwise be justified to support our audit conclusions, it will be clearly differentiated as work carried out under section 35 of the Audit Commission Act 1998.

The Code also states that the Commission issues guidance under its powers to appoint auditors and to determine their terms of appointment. The Standing Guidance for Auditors includes several references to arrangements designed to support and reinforce the requirements relating to independence, which auditors must comply with. These are as follows:

- Auditors and senior members of their staff who are directly involved in the management, supervision or delivery of Commission-related work, and senior members of their audit teams should not take part in political activity.
- No member or employee of the firm should accept or hold an appointment as a member of an audited body whose auditor is, or is proposed to be, from the same firm. In addition, no member or employee of the firm should accept or hold such appointments at related bodies, such as those linked to the audited body through a strategic partnership.
- Audit staff are expected not to accept appointments as Governors at certain types of schools within the local authority.
- Auditors and their staff should not be employed in any capacity (whether paid or unpaid) by an audited body or other organisation providing services to an audited body whilst being employed by the firm.
- Firms are expected to comply with the requirements of the Commission's protocols on provision of personal financial or tax advice to certain senior individuals at audited bodies, independence considerations in relation to procurement of services at audited bodies, and area wide internal audit work.
- Auditors appointed by the Commission should not accept engagements which involve commenting on the performance of other Commission auditors on Commission work without first consulting the Commission.
- Auditors are expected to comply with the Commission's policy for the Engagement Lead to be changed on a periodic basis.
- Audit suppliers are required to obtain the Commission's written approval prior to changing any Engagement Lead in respect of each audited body.
- Certain other staff changes or appointments require positive action to be taken by Firms as set out in the standing guidance.

Appendix 2: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

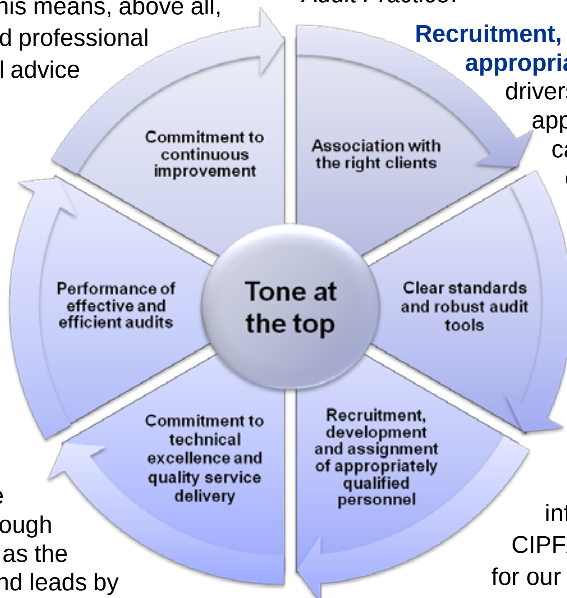
This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

KPMG's Audit Quality Framework consists of seven key drivers combined with the commitment of each individual in KPMG.

The diagram summarises our approach and each level is expanded upon.

At KPMG we consider audit quality is not just about reaching the right opinion, but how we reach that opinion. KPMG views the outcome of a quality audit as the delivery of an appropriate and independent opinion in compliance with the auditing standards. It is about the processes, thought and integrity behind the audit report. This means, above all, being independent, compliant with our legal and professional requirements, and offering insight and impartial advice to you, our client.

KPMG's Audit Quality Framework consists of seven key drivers combined with the commitment of each individual in KPMG. We use our seven drivers of audit quality to articulate what audit quality means to KPMG.



We believe it is important to be transparent about the processes that sit behind a KPMG audit report, so you can have absolute confidence in us and in the quality of our audit.

Tone at the top: We make it clear that audit quality is part of our culture and values and therefore non-negotiable. Tone at the top is the umbrella that covers all the drives of quality through a focused and consistent voice. Darren Gilbert as the Engagement Lead sets the tone on the audit and leads by example with a clearly articulated audit strategy and commits a significant proportion of his time throughout the audit directing and supporting the team.

Association with right clients: We undertake rigorous client and engagement acceptance and continuance procedures which are vital to the ability of KPMG to provide high-quality professional services to our clients.

Clear standards and robust audit tools: We expect our audit professionals to adhere to the clear standards we set and we provide a range of tools to support them in meeting these expectations. The global rollout of KPMG's eAudIT application has significantly enhanced existing audit functionality. eAudIT enables KPMG to deliver a highly technically enabled audit. All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.

Recruitment, development and assignment of appropriately qualified personnel: One of the key drivers of audit quality is assigning professionals appropriate to the Authority's risks. We take great care to assign the right people to the right clients based on a number of factors including their skill set, capacity and relevant experience.

We have a well developed technical infrastructure across the firm that puts us in a strong position to deal with any emerging issues. This includes:

- A national public sector technical director who has responsibility for co-ordinating our response to emerging accounting issues, influencing accounting bodies (such as CIPFA) as well as acting as a sounding board for our auditors.

- A national technical network of public sector audit professionals is established that meets on a monthly basis and is chaired by our national technical director.

- All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.

- A dedicated Department of Professional Practice comprised of over 100 staff that provide support to our audit teams and deliver our web-based quarterly technical training.

Appendix 2: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

Quality must build on the foundations of well trained staff and a robust methodology.

Page 69

Commitment to technical excellence and quality service delivery: Our professionals bring you up- the-minute and accurate technical solutions and together with our specialists are capable of solving complex audit issues and delivering valued insights.

Our audit team draws upon specialist resources including Forensic, Corporate Finance, Transaction Services, Advisory, Taxation, Actuarial and IT. We promote technical excellence and quality service delivery through training and accreditation, developing business understanding and sector knowledge, investment in technical support, development of specialist networks and effective consultation processes.

Performance of effective and efficient audits: We understand that how an audit is conducted is as important as the final result. Our drivers of audit quality maximise the performance of the engagement team during the conduct of every audit. We expect our people to demonstrate certain key behaviors in the performance of effective and efficient audits. The key behaviors that our auditors apply throughout the audit process to deliver effective and efficient audits are outlined below:

- timely Engagement Lead and manager involvement;
- critical assessment of audit evidence;
- exercise of professional judgment and professional scepticism;
- ongoing mentoring and on the job coaching, supervision and review;
- appropriately supported and documented conclusions;
- if relevant, appropriate involvement of the Engagement Quality Control reviewer (EQC review);
- clear reporting of significant findings;
- insightful, open and honest two-way communication with those charged with governance; and
- client confidentiality, information security and data privacy.

Commitment to continuous improvement: We employ a broad range of mechanisms to monitor our performance, respond to feedback and understand our opportunities for improvement.

Our quality review results

We are able to evidence the quality of our audits through the results of National Audit Office and Audit Commission reviews. The Audit Commission publishes information on the quality of work provided by KPMG (and all other firms) for audits undertaken on behalf of them (http://www.audit-commission.gov.uk/audit-regime/audit-quality-review-programme/principal-audits/kpmg-audit-quality).

The latest Annual Regulatory Compliance and Quality Report (issued June 2013) showed that we performed highly against the Audit Commission's criteria. We were one of only two firms to receive a combined audit quality and regulatory compliance rating of green for 2012/13.

Appendix 3: Materiality and reporting of audit differences

When we determine our audit strategy we set a monetary materiality level for planning purposes.

For 2013/14 we have set this at £4.9 million based on the group accounts.

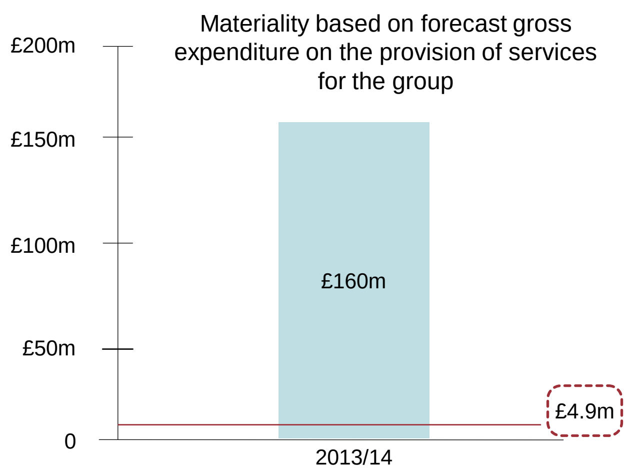
We will report all audit differences over £245k to the Audit & Governance Committee.

Page 70

Materiality

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects: materiality by value, nature and context.

- Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.
- Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.
- Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.



Materiality for planning purposes has been set £4.8 million for the Authority's standalone accounts, and at £4.9 million for the group accounts, which in both cases equates to around 3 percent of gross expenditure on the provision of services.

We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Audit & Governance Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work.

Under ISA 260, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £245k.

If management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit & Governance Committee to assist it in fulfilling its governance responsibilities.

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Gloucester City Council

Meeting:	**Audit and Governance**	**:**	**17 March 2014**
Subject:	**Treasury Management Update – Quarter 3 Report 2013/14**		
Report Of:	**Corporate Director of Resources**		
Wards Affected:	**All**		
Key Decision:	**No**	**Budget/Policy Framework:**	**Yes**
Contact Officer:	**Jon Topping**		
	jon.topping@gloucester.gov.uk		**Tel: 396242**
Appendices:	**1. Prudential and Treasury Indicators** **2. Treasury Management Investments** **3. Economic Outlook** **4. Interest rate forecasts**		

1.0 Purpose of Report

1.1 One of the requirements of the revised Code of Practice for Treasury Management in November 2011 recommends that members should be updated on treasury management activities at least twice a year, but preferably quarterly. This report covers Quarter 3, 1st October 2013 to 31st December 2013.

1.2 This report will highlight issues specific to the Council and also highlight the overall economic outlook as provided by the Councils treasury advisors Capita Asset Services.

1.3 The body of the report provides an overview of the Councils performance in Quarter 3 ;

- **Appendix 1** highlights the key performance indicators in line with the Councils Treasury Management Strategy.
- **Appendix 2** is the investments held at the end of quarter 3.
- **Appendix 3** is an economic summary provided by the Councils treasury advisors.
- **Appendix 4** is a detailed commentary on interest rate forecasts

2.0 Recommendations

2.1 Audit and Governance Committee is asked to **RESOLVE** that the report be noted and note that no changes are required to the prudential indicators.

3.0 Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2013/14, which includes the Annual Investment Strategy, was approved by the Council on 10th April 2013. It sets out the Council's investment priorities as being:

- Security of capital;
- Liquidity; and
- Yield

3.1 The Council will also aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term to cover cashflow needs, but also to seek out value available in periods up to 12 months, with highly credit rated financial institutions, using our suggested creditworthiness approach, including sovereign credit rating and Credit Default Swap (CDS) overlay information.

3.2 Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the quarter ended 31st December 2013.

3.3 Investment rates available in the market have continued at historically low levels and have fallen further during the quarter as a result of the Funding for Lending Scheme. The average level of funds available for investment purposes during the quarter was £8.5m. These funds were available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme.

3.4 Investment performance for quarter ended 31st December 2013

Benchmark	Benchmark Return	Council Performance	Investment Interest Earned
7 day	0.35%	0.38%	£7.962

As illustrated, the Council outperformed the benchmark by 2.6 bps. The Council's budgeted investment return for 2013/14 is £45,770 and performance for the year to date is in line with the budget.

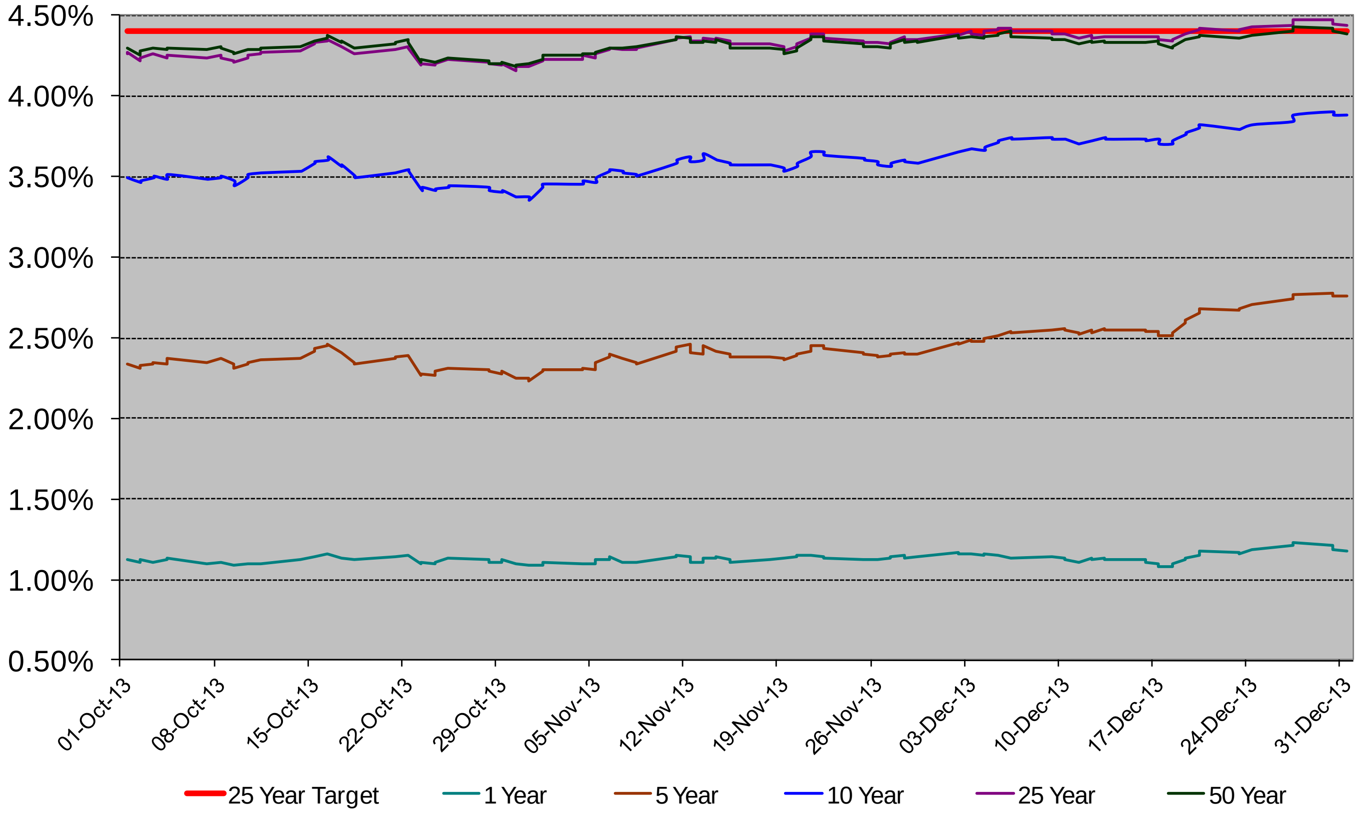
4.0 New Borrowing

4.1 The 25 year PWLB target rate for new long term borrowing for the quarter remained at 4.40%.

4.2 No borrowing was undertaken during the quarter.

4.3 PWLB certainty rates, quarter ended 31st December 2013

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.08%	2.23%	3.35%	4.16%	4.18%
Date	17/12/2013	31/10/2013	31/10/2013	30/10/2013	30/10/2013
High	1.23%	2.78%	3.90%	4.47%	4.43%
Date	27/12/2013	30/12/2013	30/12/2013	27/12/2013	27/12/2013
Average	1.13%	2.43%	3.59%	4.32%	4.31%



4.4 To minimise investment risk, the Council has reduced external investments in lieu of new external borrowing. This was achieved by reducing the overall debt liability by repaying £5,000,000 of external debt. However, this policy will require ongoing monitoring in the event that upside risk to gilt yields prevails.

4.5 **Borrowing in advance of need.**

The Council has not borrowed in advance of need during the quarter ended 31st December 2013 and has no intention to borrow in advance in 2013/14

5.0 Debt Rescheduling

5.1 Debt rescheduling opportunities have been limited in the current economic climate and following the increase in the margin added to gilt yields which has impacted PWLB new borrowing rates since October 2010. During the quarter ended 31st December 2013, no debt rescheduling was undertaken.

6.0 Compliance with Treasury and Prudential Limits

6.1 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) are included in the approved TMSS.

6.2 During the financial year to date the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices. The prudential and treasury Indicators are shown in appendix 1.

7.0 Other

7.1 During the first half of 2013/14 the Council continued to maintain an under-borrowing position. As at 31st December 2013 the position is almost level with a small under borrowing of £0.1m.

7.2 This under-borrowing reflects that the Council resources such as reserves and provisions will have reduced debt rather than be externally invested. This strategy is sensible, at this point in time, for two reasons. Firstly, there is no differential between the marginal borrowing rate and investment rate so there is nothing to be gained by investing Council resources externally. Secondly, by using the resources to reduce debt the Council will reduce exposure to investment counterparty risk.

APPENDIX 1

Prudential and Treasury Indicators as at 31st December 2013

Treasury Indicators	2013/14 Budget £'000	Quarter 3 Actual £'000
Authorised limit for external debt	£84M	£67.6M
Operational boundary for external debt	£83M	£67.6M
Gross external debt	£84M	£67.6M
Investments	Nil	£5.5M
Net borrowing	£84m	£62.1M
Maturity structure of fixed rate borrowing - upper and lower limits		
Under 12 months	0% - 85%	31.9%
12 months to 2 years	0% - 85%	0%
2 years to 5 years	0% - 85%	21.3%
5 years to 10 years	0% - 90%	6.6%
10 years to 20 years *1	5% - 95%	13.6%
20 years to 30 years *1	5% - 95%	26.6%
30 years to 40 years *1	5% - 95%	0%
40 years to 50 years *1	5% - 95%	0%
Upper limit of fixed interest rates based on net debt *2	100%	55.6%
Upper limit of variable interest rates based on net debt *2	100%	44.4%
Upper limit for principal sums invested for over 364 days	£2m	Nil

Prudential Indicators	2013/14 Budget £'000	Quarter 3 Actual £'000
Capital expenditure * • **HRA** • **GF**	£5.066M £7.208M	£2.207M £2.794M
Capital Financing Requirement (CFR) * • **HRA** • **GF**	£62.750m £17.436m	N/A N/A
Annual change in CFR *	£5.021	N/A
In year borrowing requirement	NIL	NIL
Ratio of financing costs to net revenue stream * • **HRA** • **GF**	12.7% 9.4%	N/A N/A

Incremental impact of capital investment decisions:-		
a) Increase in council tax (band change) per annum.	£2.41	N/A
b) Increase in precept for police, fire or other precepting authorities.	£0.00	N/A
c) Increase in average housing rent per week (housing authorities only).	£0.63	£2.76

APPENDIX 2

Investment Portfolio

Investments held as at 31st December 2013 compared to our counterparty list:

Name	**£'000**	**Date of Redemption**	**Counterparty Limits**
Goldman Sachs	£1,000	Overnight	£5m
Natwest	£4,500	Overnight	£5m
	£5,500	**Total Investments as at 31/12/13**	

Appendix 3:

Detailed economic commentary on developments during quarter ended 31st Dec 2013

1.0 Economic Background

1.1 After strong UK growth of 0.7% in quarter 2 and 0.8% in quarter 3, it appears that UK Gross Domestic Product (GDP) is likely to have grown at an even faster pace in quarter 4 of 2013. Forward surveys are also very encouraging in terms of strong growth and there are positive indications that recovery is broadening away from reliance on consumer spending and the housing market into construction, manufacturing, business investment and exporting. This strong growth has resulted in unemployment falling much faster towards the threshold of 7%, set by the Monetary Policy Committee (MPC) before it said it would consider any increases in Bank Rate, than it expected last August when that threshold was initially set. Accordingly, markets are expecting a first increase in early 2015 though recent comments from MPC members have emphasised they would want to see strong growth well established, and an increase in real incomes, before they would consider raising Bank Rate.

1.1.1 Also encouraging has been a sharp fall in inflation Consumer Price Index (CPI) to 2.1% in November and forward indications are that inflation will continue to be subdued. The return to strong growth has also helped lower forecasts for the increase in Government debt by £73bn over the next five years, as announced in the Autumn Statement, and fostered optimism for achieving a balance in the cyclically adjusted budget within five years, a year earlier than previously forecast.

1.1.2 The big news in financial markets was that the Federal Reserve, in December, felt sufficiently confident that the premise for strong growth had been established in America that it could start to taper its asset purchases by reducing them by $10bn per month from January 2014. These encouraging growth scenarios in the USA and UK led to a sharp jump up, in December, in short dated gilts; this, accordingly, impacted 5 and 10 year Public Works Loan Board (PWLB)rates.

1.1.3 The third quarter of 2013 saw:

- Signs that GDP growth may have accelerated;
- Evidence pointed to a moderation of household spending growth;
- Inflation fell to its lowest level since November 2009;
- Unemployment approached the MPC's 7% forward guidance threshold;
- The MPC maintained the stance of monetary policy;
- 10-year gilt yields rose to 3% and the Financial Times Stock Exchange (FTSE) 100 reach 6749;
- The Federal Reserve decided to reduce the size of its monthly asset purchases by $10bn (from $85bn to $75bn).

1.1.4 After growing at a healthy quarterly rate of 0.8% in Q3, some of the early signs are that GDP growth was even stronger in the final quarter of last year. On the basis of past form, the Chartered Institute of Purchasing and Supply (CIPS)/Markit business activity surveys point to quarterly GDP growth of around 1.5% in the final quarter. The official data available for the fourth quarter so far have also been encouraging. For example, if October's 0.4% monthly expansion in industrial output was matched in the final two months of the year, quarterly growth in Q4 would have been almost 1%.

1.1.5 Household spending growth, though, may have slowed. Numerous indicators of retail sales, including the official measure and those produced by the Confederation of British Industry (CBI) and British Retail consortium (BRC), suggest that consumer spending growth was weak in the first two months of Q4. This is not to say the consumer recovery has run its course. Indeed, the CBI survey showed a strong pick-up in sales in December. And the official measure of retail sales in the same month will be boosted by the inclusion of 'Black Friday' (despite this actually falling in the last week of November) which more timely data suggests saw a strong surge in sales. But it would take monthly growth of 1.6% in December for retail sales just to flat line in Q4 as a whole.

1.1.6 Nevertheless, growth in sales off the high street may not have done so badly. For instance, although growth in new car registrations slowed in Q4, it remained fairly strong, achieving 7% annual growth in December. So it still seems likely that overall household spending rose in the fourth quarter.

1.1.7 Although it is still high, the unemployment rate has been falling quickly towards the Monetary Policy Committee's (MPC) 7% threshold for re-assessing the stance of monetary policy. Employment rose by 250,000 in the three months to October, the largest quarterly gain since mid-2010. This brought the unemployment rate down to 7.4%, compared to a rate of 7.7% in the three months to July. What's more, the Office for National Statistics (ONS)' experimental single-month estimate of unemployment reached 7% in October.

1.1.8 The decline in unemployment, which has been faster than the MPC predicted in November, has prompted overnight index swap markets to price in a rate rise as soon as Q1 2015. But Committee members have increasingly emphasised that the 7% unemployment rate is a threshold for reconsidering policy, rather than a trigger for raising rates. Indeed, the Bank's Chief Economist Spencer Dale said that interest rates would remain low not just until unemployment had dropped, but also until the economy had "seen a prolonged period of strong growth...[and] real incomes are higher".

1.1.9 The recent fall in, and improvement in the outlook for, inflation, suggests that interest rates will probably remain on hold even if the unemployment rate falls quickly to the 7% threshold. Indeed, CPI inflation has fallen quite sharply, reaching 2.1% in November. This was the lowest rate in four years. A number of factors contributed to this. Falling commodity prices put downward pressure on food and petrol prices, while sterling's 7% appreciation on a trade-weighted basis since its low point in July may have helped core inflation to fall. Admittedly, CPI inflation might have ticked up again in December when energy companies raised their prices. But inflation should continue to fall after that, given that commodity prices have been flat over the past year or so and sterling's recent strength has reduced import prices, which should begin feed into prices on the high street.

1.1.10 The housing market continued to recover in Q4, supported by the earlier implementation of the mortgage guarantee element of the Government's Help to Buy Scheme. Prices rose at an annual rate of 8.4% and 6.4% in November according to the Halifax and Nationwide measures, respectively. And would-be buyers continue to enter the market more quickly than sellers, with the Royal Institute of Chartered Surveyors (RICS) survey pointing to further price rises. The cost of new mortgages remains low, too, with the quoted interest rate on a 5-year fixed mortgage at a 75% loan-to-value ratio at 3.36% in November, 2 basis points lower than the average in Q3 and 81 basis points lower than when the Funding for Lending Scheme (FLS) was introduced in July 2012. But talk of a housing bubble on the national level still seems to be wide of the mark, with prices well below their pre-crisis peak in real terms. Moreover, the FLS was adjusted so that it no longer provides cheap finance for mortgages.

1.1.11 Meanwhile, there were few surprises in the Autumn Statement. The Chancellor announced a fiscally neutral package of policies, with measures to ease the cost of households' utility bills offset by further spending cuts. More bullish forecasts from the OBR left expected public borrowing over the next five years £73 billion lower than projected in the March Budget. All this left Mr Osborne expected to meet his primary fiscal mandate to balance the cyclically adjusted current budget in five years a year early, though he still misses the supplementary target for the debt to GDP ratio to be falling in 2015/16.

1.1.12 Internationally, the biggest news was the Federal Reserve's decision at its December meeting to begin tapering its asset purchases. Although the announcement that the Fed's monthly purchases would be reduced by $10bn was not the consensus view, which saw tapering beginning in the early part of 2014, it was not a big surprise. The decision reflected the relative strength of the US labour market, which on average added over 200,000 jobs per month in the four months up to November.

1.1.13 Markets took the Fed's move in their stride, with equities and bond yields up slightly on the day. Over the quarter, equities performed well domestically and overseas as economic prospects improved. The FTSE 100 was up by 4.4% to 6749, while the S&P 500 rose by almost 10%. Gilt yields also rose, with the ten-year rate ending Q4 28 basis points higher at 3%, having closely tracked US Treasury yields. Sterling rose by 2.3% against the dollar to finish the year at 1.66, while it rose by 0.5% against the euro to 1.20.

1.1.14 Activity indicators in the Eurozone point towards continued weak, albeit positive, economic growth in the fourth quarter of 2013 after a mere 0.1% quarterly expansion in Q3. And disinflationary pressures are intense. Although CPI inflation rose from 0.7% to 0.9% in November, it remains well below the European Central Bank (ECB)'s target of below but close to 2%. This is despite the ECB cutting its main refinancing rate by 25 basis points to 0.25% in November.

2.1 Interest Rate Forecast

The Council's treasury advisor, Capita Asset Services, has provided the following forecast:

	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17
Bank rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.00%	1.25%
5yr PWLB rate	2.50%	2.60%	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.40%
10yr PWLB rate	3.60%	3.70%	3.80%	3.80%	3.90%	3.90%	4.00%	4.10%	4.20%	4.30%	4.30%	4.40%	4.50%
25yr PWLB rate	4.40%	4.50%	4.50%	4.60%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.10%	5.10%	5.10%
50yr PWLB rate	4.40%	4.50%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.20%	5.20%	5.20%

Capita Asset Services undertook a review of its interest rate forecasts in late November, after the Bank of England's latest quarterly Inflation Report. This latest forecast now includes a first increase in Bank Rate in quarter 2 of 2016 (previously quarter 3) and reflects greater caution as to the speed with which the MPC will start increasing Bank Rate than the current expectations of financial markets.

3.1 Summary Outlook

Until 2013, the economic recovery in the UK since 2008 had been the worst and slowest recovery in recent history. However, growth has rebounded during 2013 to surpass all expectations, propelled by recovery in consumer spending and the housing market, Forward surveys are currently very positive in indicating that growth prospects are also strong for 2014, not only in the UK economy as a whole, but in all three main sectors, services, manufacturing and construction. This is very encouraging as there does need to be a significant rebalancing of the economy away from consumer spending to construction, manufacturing, business investment and exporting in order for this start to recovery to become more firmly established. One drag on the economy is that wage inflation continues to remain significantly below CPI inflation so disposable income and living standards are under pressure, although income tax cuts have ameliorated this to some extent. Labour productivity must improve significantly before increases in pay rates are warranted. With regard to the US, the main world economy, it faces similar debt problems to those of the UK, but thanks to reasonable growth, cuts in government expenditure and tax rises, the annual government deficit has been halved from its peak without appearing to do too much damage to growth, although labour force participation rates remain lower than ideal.

As for the Eurozone, concerns have subsided considerably in 2013. However, sovereign debt difficulties have not gone away and major concerns could return in respect of any countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise to levels that could result in a loss of investor confidence in the financial viability of such countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed.

Appendix 4

Detailed Commentary on Interest rate forecasts

THE UK ECONOMY

Economic growth. Until 2013, the economic recovery in the UK since 2008 had been the worst and slowest recovery in recent history. However, growth strongly rebounded in 2013 - quarter 1 (+0.3%), 2 (+0.7%) and 3 (+0.8%), to surpass all expectations as all three main sectors, services, manufacturing and construction contributed to this strong upturn. The Bank of England has, therefore, upgraded growth forecasts in the August and November quarterly Inflation Reports for 2013 from 1.2% to 1.6% and for 2014 from 1.7% to 2.8%, (2015 unchanged at 2.3%). The November Report stated that: -

> *In the United Kingdom, recovery has finally taken hold. The economy is growing robustly as lifting uncertainty and thawing credit conditions start to unlock pent-up demand. But significant headwinds — both at home and abroad — remain, and there is a long way to go before the aftermath of the financial crisis has cleared and economic conditions normalise. That underpins the MPC's intention to maintain the exceptionally stimulative stance of monetary policy until there has been a substantial reduction in the degree of economic slack. The pace at which that slack is eroded, and the durability of the recovery, will depend on the extent to which productivity picks up alongside demand. Productivity growth has risen in recent quarters, although unemployment has fallen by slightly more than expected on the back of strong output growth.*

Forward surveys are currently very positive in indicating that growth prospects are also strong for 2014, not only in the UK economy as a whole, but in all three main sectors, services, manufacturing and construction. This is very encouraging as there does need to be a significant rebalancing of the economy away from consumer spending to construction, manufacturing, business investment and exporting in order for this start to recovery to become more firmly established. One drag on the economy is that wage inflation continues to remain significantly below CPI inflation so disposable income and living standards are under pressure, although income tax cuts have ameliorated this to some extent. This therefore means that labour productivity must improve significantly for this situation to be corrected by the warranting of increases in pay rates.

Forward guidance. The Bank of England issued forward guidance in August which said that the Bank will not start to consider raising interest rates until the jobless rate (Labour Force Survey / ILO i.e. not the claimant count measure) has fallen to 7% or below. This would require the creation of about 750,000 jobs and was forecast to take three years in August, but revised to possibly quarter 4 2014 in November. The UK unemployment rate has already fallen to 7.4% on the three month rate to October 2013 (although the rate in October alone was actually 7.0%). The Bank's guidance is subject to three provisos, mainly around inflation; breaching any of them would sever the link between interest rates and unemployment levels. This actually makes forecasting Bank Rate much more complex given the lack of available reliable forecasts by economists over a three year plus horizon. The recession since 2007 was notable for how unemployment did NOT rise to the levels that would normally be expected in a major recession and the August Inflation Report noted that productivity had sunk to 2005 levels. There has, therefore, been a significant level of retention of labour, which will mean that there is potential for a significant amount of GDP growth to be accommodated without a major reduction in unemployment. However, it has been particularly encouraging that the strong economic growth in 2013 has also been accompanied by a rapid increase in employment and forward hiring indicators are also currently very positive. It is therefore increasingly likely that early in 2014, the MPC will need to amend its forward guidance by reducing its 7.0% threshold rate and/or by adding further wording similar to the Fed's move in December (see above).

Credit conditions. While Bank Rate has remained unchanged at 0.5% and quantitative easing has remained unchanged at £375bn in 2013, the Funding for Lending Scheme (FLS) was extended to encourage banks to expand lending to small and medium size enterprises. The second phase of Help to Buy aimed at supporting the purchase of second hand properties, will also start in earnest in January 2014. These measures have been so successful in boosting the supply of credit for mortgages, and so of increasing house purchases, (though levels are still far below the pre-crisis level), that the Bank of England announced at the end of November that the FLS for mortgages would end in February 2014. While there have been concerns that these schemes are creating a bubble in the housing market, house price increases outside of London and the south-east have been minimal. However, bank lending to small and medium enterprises continues to remain weak and inhibited by banks still repairing their balance sheets and anticipating tightening of regulatory requirements.

Inflation. Inflation has fallen from a peak of 3.1% in June 2013 to 2.1% in November. It is expected to remain near to the 2% target level over the MPC's two year time horizon.

AAA rating. The UK has lost its AAA rating from Fitch and Moody's but that caused little market reaction.

THE GLOBAL ECONOMY

The Eurozone (EZ). The sovereign debt crisis has eased considerably during 2013 which has been a year of comparative calm after the hiatus of the Cyprus bailout in the spring. In December, Ireland escaped from its three year EZ bailout programme as it had dynamically addressed the need to substantially cut the growth in government debt, reduce internal price and wage levels and promote economic growth. The EZ finally escaped from seven quarters of recession in quarter 2 of 2013 but growth is likely to remain weak and so will dampen UK growth. The ECB's pledge to buy unlimited amounts of bonds of countries which ask for a bail out, has provided heavily indebted countries with a strong defence against market forces. This has bought them time to make progress with their economies to return to growth or to reduce the degree of recession. However, debt to GDP ratios (2012 figures) of Greece 176%, Italy 131%, Portugal 124%, Ireland 123% and Cyprus 110%, remain a cause of concern, especially as many of these countries are experiencing continuing rates of increase in debt in excess of their rate of economic growth i.e. these debt ratios are continuing to deteriorate. Any sharp downturn in economic growth would make these countries particularly vulnerable to a new bout of sovereign debt crisis. It should also be noted that Italy has the third biggest debt mountain in the world behind Japan and the US. Greece remains particularly vulnerable and continues to struggle to meet EZ targets for fiscal correction. Whilst a Greek exit from the Euro is now improbable in the short term, as Greece has made considerable progress in reducing its annual government deficit and a return towards some economic growth, some commentators still view an eventual exit as being likely. There are also concerns that austerity measures in Cyprus could also end up in forcing an exit. The question remains as to how much damage an exit by one country would do and whether contagion would spread to other countries. However, the longer a Greek exit is delayed, the less are likely to be the repercussions beyond Greece on other countries and on EU banks.

Sentiment in financial markets has improved considerably during 2013 as a result of firm Eurozone commitment to support struggling countries and to keep the Eurozone intact. However, the foundations to this current "solution" to the Eurozone debt crisis are still weak and events could easily conspire to put this into reverse. There are particular concerns as to whether democratically elected governments will lose the support of electorates suffering under EZ imposed austerity programmes, especially in countries like Greece and Spain which have unemployment rates of over 26% and unemployment among younger people of over 50%. The Italian political situation is also fraught with difficulties in maintaining a viable coalition which will implement an EZ imposed austerity programme and undertake overdue reforms to government and the economy. There are also concerns over the lack of political will in France to address issues of poor international competitiveness,

USA. The economy has managed to return to robust growth in Q2 2013 of 2.5% y/y and 4.1% y/y in Q3, in spite of the fiscal cliff induced sharp cuts in federal expenditure that kicked in on 1 March, and increases in taxation. The Federal Reserve therefore decided in December to reduce its $85bn per month asset purchases programme of quantitative easing by $10bn. It also amended its forward guidance on its pledge not to increase the central rate until unemployment falls to 6.5% by adding that there would be no increases in the central rate until 'well past the time that the unemployment rate declines below 6.5%, especially if projected inflation continues to run below the 2% longer run goal'. Consumer, investor and business confidence levels have all improved markedly in 2013. The housing market has turned a corner and house sales and increases in house prices have returned to healthy levels. Many house owners have, therefore, been helped to escape from negative equity and banks have also largely repaired their damaged balance sheets so that they can resume healthy levels of lending. All this portends well for a reasonable growth rate looking forward.

China. There are concerns that Chinese growth could be on an overall marginal downward annual trend. There are also concerns that the new Chinese leadership have only started to address an unbalanced economy which is heavily dependent on new investment expenditure, and for a potential bubble in the property sector to burst, as it did in Japan in the 1990s, with its consequent impact on the financial health of the banking sector. There are also concerns around the potential size, and dubious creditworthiness, of some bank lending to local government organisations and major corporates. This primarily occurred during the government promoted expansion of credit, which was aimed at protecting the overall rate of growth in the economy after the Lehmans crisis.

Japan. The initial euphoria generated by "Abenomics", the huge QE operation instituted by the Japanese government to buy Japanese debt, has tempered as the follow through of measures to reform the financial system and the introduction of other economic reforms, appears to have stalled. However, at long last, Japan has seen a return to reasonable growth and positive inflation during 2013 which augurs well for the hopes that Japan can escape from the bog of stagnation and deflation and so help to support world growth. The fiscal challenges though are huge; the gross debt to GDP ratio is about 245% in 2013 while the government is currently running an annual fiscal deficit of around 50% of total government expenditure. Within two years, the central bank will end up purchasing about

Y190 trillion (£1,200 billion) of government debt. In addition, the population is ageing due to a low birth rate and, on current trends, will fall from 128m to 100m by 2050.

CAPITA ASSET SERVICES FORWARD VIEW

Economic forecasting remains difficult with so many external influences weighing on the UK. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, and safer bonds.

There could well be volatility in gilt yields over the next year as financial markets anticipate further tapering of asset purchases by the Fed. The timing and degree of tapering could have a significant effect on both Treasury and gilt yields. Equally, while the political deadlock and infighting between Democrats and Republicans over the budget has almost been resolved the raising of the debt limit, has only been kicked down the road. A final resolution of these issues could have a significant effect on gilt yields during 2014.

The longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. Increasing investor confidence in economic recovery is also likely to compound this effect as a continuation of recovery will further encourage investors to switch back from bonds to equities.

The overall balance of risks to economic recovery in the UK is currently evenly weighted. However, only time will tell just how long this period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

The interest rate forecasts in this report are based on an initial assumption that there will not be a major resurgence of the EZ debt crisis, or a break-up of the EZ, but rather that there will be a managed, albeit painful and tortuous, resolution of the debt crisis where EZ institutions and governments eventually do what is necessary - but only when all else has been tried and failed. Under this assumed scenario, growth within the EZ will be tepid for the next couple of years and some EZ countries experiencing low or negative growth, will, over that time period, see a significant increase in total government debt to GDP ratios. There is a significant danger that these ratios could rise to the point where markets lose confidence in the financial viability of one, or more, countries. However, it is impossible to forecast whether any individual country will lose such confidence, or when, and so precipitate a resurgence of the EZ debt crisis. While the ECB has adequate resources to manage a debt crisis in a small EZ country, if one, or more, of the large countries were to experience a major crisis of market confidence, this would present a serious challenge to the ECB and to EZ politicians.

Downside risks currently include:

- UK strong economic growth is currently very dependent on consumer spending and recovery in the housing market. This is unlikely to endure much beyond 2014 as most consumers are maxed out on borrowing and wage inflation is less than CPI inflation, so disposable income is being eroded.
- A weak rebalancing of UK growth to exporting and business investment causing a major weakening of overall economic growth beyond 2014
- Weak growth or recession in the UK's main trading partners - the EU and US, depressing economic recovery in the UK.
- Prolonged political disagreement over the raising of the US debt ceiling.

- A return to weak economic growth in the US, UK and China causing major disappointment in investor and market expectations.
- A resurgence of the Eurozone sovereign debt crisis caused by ongoing deterioration in government debt to GDP ratios to the point where financial markets lose confidence in the financial viability of one or more countries and in the ability of the ECB and Eurozone governments to deal with the potential size of the crisis.
- The potential for a significant increase in negative reactions of populaces in Eurozone countries against austerity programmes, especially in countries with very high unemployment rates e.g. Greece and Spain, which face huge challenges in engineering economic growth to correct their budget deficits on a sustainable basis.
- The Italian political situation is frail and unstable; this will cause major difficulties in implementing austerity measures and a programme of overdue reforms. Italy has the third highest government debt mountain in the world.
- Problems in other Eurozone heavily indebted countries (e.g. Cyprus and Portugal) which could also generate safe haven flows into UK gilts, especially if it looks likely that one, or more countries, will need to leave the Eurozone.
- A lack of political will in France, (the second largest economy in the EZ), to dynamically address fundamental issues of low growth, poor international uncompetitiveness and the need for overdue reforms of the economy.
- Monetary policy action failing to stimulate sustainable growth in western economies, especially the Eurozone and Japan.
- Geopolitical risks e.g. Syria, Iran, North Korea, which could trigger safe haven flows back into bonds.

The potential for upside risks to UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- A sharp upturn in investor confidence that sustainable robust world economic growth is firmly expected, causing a surge in the flow of funds out of bonds into equities.
- A reversal of Sterling's safe-haven status on a sustainable improvement in financial stresses in the Eurozone.
- UK inflation being significantly higher than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.
- In the longer term – an earlier than currently expected reversal of Quantitative Easing (QE) in the UK; this could initially be implemented by allowing gilts held by the Bank to mature without reinvesting in new purchases, followed later by outright sale of gilts currently held.

Gloucester City Council

Meeting:	**Cabinet** **Audit and Governance Committee** **Council**	**Date:**	**5th March 2014** **17th March 2014** **27th March 2014**
Subject:	**Treasury Management Strategy 2014/15**		
Report Of:	**Corporate Director of Resources**		
Wards Affected:	**All**		
Key Decision:	**No**	**Budget/Policy Framework:**	**Yes**
Contact Officer:	**Peter Gillett**		
	Email: peter.gillett@gloucester.gov.uk		**Tel: 396400**
Appendices:	**1. Treasury Management Strategy 2014/15**		

FOR GENERAL RELEASE

1.0 Purpose of Report

1.1 To formally recommend that Full Council approves the attached Treasury Management Strategy, the Prudential Indicators and note the treasury activities.

2.0 Recommendations

2.1 Cabinet is asked to **RESOLVE** that the recommendations to Council be noted and endorsed.

2.2 Council is asked to **RESOLVE** that

(1) The treasury management strategy which sets out how the Council's treasury service will manage external borrowing and investments in support of the capital programme be approved;

(2) The borrowing authorised borrowing limit be approved at:-
   a. 2014/15 £86m
   b. 2015/16 £86m
   c. 2016/17 £86m

(3) The Housing Revenue Account capital financing requirement be limited to £62.750m in accordance with the debt cap imposed through the HRA self financing regime.

(4) The prudential indicators set on in section two of the strategy which set out the capital plans, financing, minimum revenue provision policy statement and affordability on the Council tax and rents be approved.

2.3 Audit and Governance Committee is asked to **RESOLVE** that the Treasury Management Strategy and the treasury implications of the potential CoCo be noted.

3.0 Background and Key Issues

3.1 The treasury management strategy for 2013/14 proposed a continuation of the existing successful strategy to move to an under-borrowing position. In previous years the Council's level of external debt exceeded the capital financing requirement. The Council during 2013/14 has continued this strategy as at 31st March 2013 this over-borrowing had reduced to £0.2m and the forecast position at 31st March 2014 is 4.596m under borrowing.

3.2 This under-borrowing reflects that the Council resources such as reserves and provisions will have reduced debt rather than be externally invested. This strategy is sensible, at this point in time, for two reasons. Firstly, there is no differential between the marginal borrowing rate and investment rate so there is nothing to be gained by investing Council resources externally. Secondly, by using the resources to reduce debt the Council will reduce exposure to investment counterparty risk.

3.3 There will be short term cashflow balances that will be invested for short periods within the year. Section 4 of the strategy outlines the Annual Investment Strategy, in particular in outlines the creditworthiness policy through the use of credit ratings.

3.4 The borrowing strategy is straight-forward, use investments to reduce short term borrowing and long term debt as it becomes repayable. Once investments have been applied it is anticipated that any new debt will be short term as the current market rates are attractive and this also maximises future flexibility. This flexibility is important because the potential creation of the CoCo will have treasury implications as the Housing Revenue Account accounts for almost 80% of external debt. The treasury implications of the CoCo will be actively considered during the negotiation and approval process.

3.5 The strategy allows for either debt rescheduling or new long term fixed rate borrowing in place of short term borrowing if circumstances were to change during 2014/15 although the decision will take account of potential CoCo position.

3.6 The strategy also includes the minimum revenue provision (MRP) policy statement. This policy continues with the practice approved last year. MRP is the revenue charge to reduce debt and is only required by the General Fund. This option provides for a reduction in the borrowing need over the approximate asset life. For clarity the options for reduction are explained and can either be through an annuity calculation (providing a consistent overall annual borrowing charge) or straight line (where the principal repayment is the same each year).

4.0 Alternative Options Considered

4.1 The Strategy considered the following options.

- The potential to borrow long term rather than sort term. This remains an option should interest rates change but at the moment short terms rates are only 0.35% whereas long term rates are over 3% (10 years plus).

- Another option which has been discounted is that internal resources such as reserves could be externally invested rather than invested internally. The income from the external investment is the same as the cost of temporary borrowing so there is nothing to be gained by externally investing reserves at this point in time. In other circumstances, usually when long term rates are lower than short term investment rates there is sometimes merit in external investment of reserves and this will be considered if circumstances change.

5.0 Reasons for Recommendations

5.1 As outlined in the legal implications the recommendations require Council approval.

6.0 Future Work and Conclusions

6.1 The treasury management strategy provides a logical basis to fund the capital financing requirement and successful move to a fully under-borrowed position. The main issue that will impact of the strategy is the CoCo and this will require future work as part of the negotiation and approval process.

7.0 Financial Implications

7.1 The expenditure and income arising from treasury management activities are included within the Council General Fund and Housing Revenue Account budgets.

8.0 Legal Implications

8.1 The Treasury Management Strategy is required to meet the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

9.0 Risk & Opportunity Management Implications

9.1 There is a risk that short term and long term interest rates increase and this will be monitored both in-house and by the Council Treasury Management Advisor, Capita Asset Services. In this event the risk will be managed through the opportunities either to reschedule debt or new long term fixed rate borrowing in place of short term borrowing.

9.2 The risk of deposits not being returned by the counterparty is minimised by moving to a fully under borrowed position and then only investing short term cash flow monies with counterparties on the approved lending list. All counterparties on this list meet minimum credit rating criteria, ensuring the risk is kept extremely low although not eliminated.

9.3 The treasury management risks associated with the potential creation of the CoCo will be actively managed through the negotiation and approval processes.

10.0 People Impact Assessment (PIA):

10.1 A PIA screening assessment has been undertaken and the impact is neutral. A full PIA is not required.

11.0 Other Corporate Implications

Community Safety

11.1 None

Sustainability

11.2 None

Staffing & Trade Union

11.3 None

Background Documents:
Local Government Act 2003,
CIPFA Treasury Management Code
CIPFA Prudential Code,
CLG MRP Guidance,

Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement
and Annual Investment Strategy

Gloucester City Council
2014/15

INDEX

1 INTRODUCTION

1.1 Background

The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

CIPFA defines treasury management as:

> *"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."*

1.2 Reporting requirements

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.

Prudential and treasury indicators and treasury strategy (this report) - The first, and most important report covers:

- the capital plans (including prudential indicators);
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

Quarterly Treasury update reports - This will update members on a quarterly basis with the progress of the capital position, amending prudential indicators as necessary, and whether the treasury strategy is meeting the strategy or whether any policies require revision.

An annual treasury report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Scrutiny
The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Audit and Governance Committee.

1.3 Treasury Management Strategy for 2014/15

The strategy for 2014/15 covers two main areas:

Capital issues

- the capital plans and the prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management issues

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

1.4 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsibe for scrutiny. Training for Members has been provided in the past and further training will be arranged as required during 2014/15. The training needs of treasury management officers are periodically reviewed.

1.5 Treasury management consultants

The Council uses Capita Asset Services, Treasury solutions as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

2 THE CAPITAL PRUDENTIAL INDICATORS 2014/15 – 2016/17

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

2.1 Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Capital expenditure £m	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Regeneration	2.164	1.287	4.703	2.050	2.050
Services & Neighbourhood	2.317	0.317	0.975	0	0
Resources	0.794	0	0.415	0.200	0.200
Housing General Fund	0	0.245	0.789	0.684	0.684
Total Non-HRA	**5.275**	**1.850**	**6.882**	**2.934**	**2.934**
HRA	7.772	5.101	7.100	0	0
Total	**13.047**	**6.951**	**13.982**	**2.934**	**2.934**

The Council has other long term liabilities which relate to the difference between the Local Government Pension Liabilities and assets. These do not have any treasury impact on Gloucester City Council as the Pension Fund is managed by Gloucestershire County Council. Therefore, other long term liabilities have been excluded from this strategy.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital expenditure £m	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Non-HRA	5.275	1.850	6.882	2.934	2.934
HRA	7.772	5.101	7.100	0	0
Total	**13.047**	**6.951**	**13.982**	**2.934**	**2.934**
Financed by:					
Capital receipts	3.328	1.437	3.439	0	0
Capital grants	1.619	0.413	1.887	0.084	0.084
HRA Major repairs	3.129	2.000	1.487	0	0
HRA Revenue	0	2.900	2.900	0	0
Net financing need for the year	**4.971**	**0.201**	**4.268**	**2.850**	**2.850**

2.2 The Council's borrowing need (the Capital Financing Requirement)

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

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each assets life.

The Council is asked to approve the CFR projections below:

£000	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Capital Financing Requirement					
Closing CFR	76,700	76,438	80,218	82,502	84,745
Movement in CFR	4,547	(262)	3,779	2,284	2,243

Movement in CFR represented by					
Net financing need for the year (above)	4,971	201	4,268	2,850	2,850
Less MRP/VRP and other financing movements	(424)	(463)	(488)	(566)	(607)
Movement in CFR	4,547	(262)	3,779	2,284	2,243

2.3 Minimum revenue provision (MRP) policy statement

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

CLG regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

- **Existing practice** - MRP will follow the existing practice outlined in former CLG regulations (option 1); This option provides for an approximate 4% reduction in the borrowing need (CFR) each year.
  ;

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset life method –** MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3); This options provide for a reduction in the borrowing need over approximately the asset's life.

There is no requirement on the HRA to make a minimum revenue provision, instead depreciation forms a real charge to the HRA balance.

2.4 Affordability prudential indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

2.5 Ratio of financing costs to net revenue stream

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream and shows how much of the Council's net revenue stream is committed to the costs of capital financing represented by interest payable on borrowings and the Minimum Revenue Provision.

	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Non-HRA	4.27%	3.71%	5.09%	5.71%	6.32%
HRA	13.25%	13.64%	14.05%	14.48%	14.91%

The estimates of financing costs include current commitments and the proposals in this budget report.

2.6 Incremental impact of capital investment decisions on council tax and Housing Rents

This indicator identifies the revenue costs associated with proposed changes to the three year capital programme recommended in this budget report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period.

Incremental impact of capital investment decisions on the band D council tax

£	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Council tax - band D	10.16	-3.24	5.38	3.32	2.26

Incremental impact of capital investment decisions on average housing rent

£	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Average weekly rent	0.04	0.81	0.63	0.00	0.00

3 BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of approporiate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current portfolio position

The Council's treasury portfolio position at 31 March 2013, with forward projections are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£000	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
External Debt					
Debt at 1 April	89,105	76,932	71,842	71,842	74,042
Expected change in Debt	(12,173)	(5,090)	0	2,200	2,200
Other long-term liabilities (OLTL)	0	0	0	0	0
Expected change in OLTL	0	0	0	0	0
Actual gross debt at 31 March	**76,932**	**71,842**	**71,842**	**74,042**	**76,242**
The Capital Financing Requirement	76,700	76,438	80,218	82,502	84,745
Under / (over) borrowing	**(£232)**	**4,596**	**8,376**	**8,460**	**8,503**

£000	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Investments at 31st March					
Investments	**5,993**	**4,600**	**800**	**800**	**800**
Investment Change	**(10,126)**	**(5,193)**	**-**	**-**	**-**

At the 31st March 2013 there was an over borrowing of £232,000 compared with the capital financing requirement. It is estimated that by 31st March 2013 the position will have changed to £4.596 million under-borrowing with debt lower than the capital financing requirement. This change is consistent with the approved Treasury Management Strategy and has been achieved by using external investments to fund the in year capital financing requirement.

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2014/15 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Director of Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3.2 Treasury Indicators: limits to borrowing activity

The operational boundary. This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Operational boundary £000	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Debt	85,000	85,000	85,000	85,000
Other long term liabilities	0	0	0	0
Total	85,000	85,000	85,000	85,000

The authorised limit for external debt. A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
2. The Council is asked to approve the following authorised limit:

Authorised limit £000	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Debt	86,000	86,000	86,000	86,000
Other long term liabilities	0	0	0	0
Total	86,000	86,000	86,000	86,000

3.3 Prospects for interest rates

The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives our central view.

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)		
		5 year	25 year	50 year
Mar 2014	0.50	2. 60	4.40	4.40
Jun 2014	0.50	2.60	4.40	4.50
Sep 2014	0.50	2.70	4.50	4.50
Dec 2014	0.50	2.80	4.60	4.60
Mar 2015	0.50	2.90	4.70	4.70
Jun 2015	0.50	2.90	4.70	4.80
Sep 2015	0.50	3.00	4.80	4.90
Dec 2015	0.75	3.10	4.90	5.00
Mar 2016	0.75	3.20	5.00	5.10
Jun 2016	1.00	3.20	5.00	5.10
Sep 2016	1.25	3.30	5.10	5.10
Dec 2016	1.50	3.40	5.10	5.20
Mar 2017	1.75	3.50	5.10	5.20

Until 2013, the economic recovery in the UK since 2008 had been the worst and slowest recovery in recent history. However, growth has rebounded during 2013 to surpass all expectations, propelled by recovery in consumer spending and the housing market. Forward surveys are also currently very positive in indicating that growth prospects are strong for 2014, not only in the UK economy as a whole, but in all three main sectors, services, manufacturing and construction. This is very encouraging as there does need to be a significant rebalancing of the economy away from consumer spending to construction, manufacturing, business investment and exporting in order for this start to recovery to become more firmly established. One drag on the economy is that wage inflation continues to remain significantly below CPI inflation so disposable income and living standards are under pressure, although income tax cuts have ameliorated this to some extent. This therefore means that labour productivity must improve significantly for this situation to be corrected by the warranting of increases in pay rates. The US, the main world economy, faces similar debt problems to the UK, but thanks to reasonable growth, cuts in government expenditure and tax rises, the annual government deficit has been halved from its peak without appearing to do too much damage to growth.

The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- As for the Eurozone, concerns have subsided considerably in 2013. However, sovereign debt difficulties have not gone away and major concerns could return in respect of any countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise to levels that could result in a loss of investor confidence in the financial viability of such countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed. Counterparty risks therefore remain elevated. This continues to suggest the use of higher quality counterparties for shorter time periods;

- Investment returns are likely to remain relatively low during 2014/15 and beyond;

- Borrowing interest rates have risen significantly during 2013 and are on a rising trend. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring even higher borrowing costs, which are now looming ever closer, where authorities will not be able to avoid new borrowing to finance new capital expenditure and/or to refinance maturing debt, in the near future;

- There will remain a cost of carry to any new borrowing which causes an increase in investments as this will incur a revenue loss between borrowing costs and investment returns.

3.4 Borrowing strategy

The Council is moving from an over to an under borrowed position. This means that investments are being used as they mature to fund the in year capital financing requirement or reduce external debt. This has resulted in external debt being lower than the capital financing requirement with Council reserves and balances being utilised to reduce debt rather than being externally invested. This strategy is prudent as there is no differential between temporary borrowing and investment rates and this will also reduce counterparty risk.

The Housing Revenue Account accounts for almost 80% of the capital financing requirement and external debt. The potential creation of a Co-Co will have a significant impact and the Council will actively consider the treasury implications during the negotiation and approval processes.

Against this background and the risks within the economic forecast, caution will be adopted with the 2014/15 treasury operations. The Director of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates* (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from a greater than expected increase in the anticipated rate to US tapering of asset purchases, or in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

Any decisions will be reported to the appropriate decision making body at the next available opportunity.

Treasury management limits on activity

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates.

However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits

The Council is asked to approve the following treasury indicators and limits:

£m	2014/15	2015/16	2016/17
Interest rate exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	£85m	£85m	£85m
Limits on variable interest rates based on net debt	£30m	£30m	£30m
Maturity structure of fixed interest rate borrowing 2014/15			
		Lower	**Upper**
Under 12 months		0%	50%
12 months to 2 years		0%	50%
2 years to 5 years		0%	50%
5 years to 10 years		0%	50%
10 years and above		0%	80%
Maturity structure of variable interest rate borrowing 2014/15			
		Lower	Upper
Under 12 months		0%	100%
12 months to 2 years		0%	100%
2 years to 5 years		0%	100%
5 years to 10 years		0%	80%
10 years and above		0%	50%

3.5 Policy on borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

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

3.6 Debt rescheduling

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

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to the Cabinet, at the earliest meeting following its action.

4 ANNUAL INVESTMENT STRATEGY

4.1 Investment policy

The Council's investment policy has regard to 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"). The Council's investment priorities will be security first, liquidity second and then return.

In accordance with guidance from the CLG and CIPFA, and in order to minimise the risk to investments, the Council has below clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list. The creditworthiness methodology used to create the counterparty list fully accounts for the ratings, watches and outlooks published by all three ratings agencies with a full understanding of what these reflect in the eyes of each agency. Using our ratings service potential counterparty ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

Furthermore, the Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings. This is fully integrated into the credit methodology provided by the advisors, Capita Asset Services in producing its colour codings which show the varying degrees of suggested creditworthiness.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

The intention of the strategy is to provide security of investment and minimisation of risk.

Investment instruments identified for use in the financial year are listed in appendix 5.3 under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Council's treasury management practices – schedules.

4.2 Creditworthiness policy

This Council applies the creditworthiness service provided by Capita Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;

- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years *
- Dark pink 5 years for Enhanced money market funds (EMMFs) with a credit score of 1.25
- Light pink 5 years for Enhanced money market funds (EMMFs) with a credit score of 1.5
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

	Colour (and long term rating where applicable)	Money and/or % Limit	Time Limit
Banks *	**yellow**	**£5m**	**5yrs**
Banks	**purple**	**£5m**	**2 yrs**
Banks	**orange**	**£5m**	**1 yr**
Banks – part nationalised	**blue**	**£5m**	**1 yr**
Banks	**red**	**£5m**	**6 mths**
Banks	**green**	**£0m**	**100 days**
Banks	**No colour**	**Not to be used**	
Limit 3 category – Council's banker (not meeting Banks 1)	**XXX**	**£5m**	**1 day**
DMADF	**AAA**	**unlimited**	**6 months**
Local authorities	**n/a**	**£100 %**	**1 yr**
Money market funds	**AAA**	**£100 %**	**liquid**
Enhanced money market funds with a credit score of 1.25	**Dark pink / AAA**	**£100 %**	**liquid**

Enhanced money market funds with a credit score of 1.5	**Light pink / AAA**	**£100 %**	**liquid**

Our creditworthiness service uses a wider array of information than just primary ratings and by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of short term rating F1, long term rating A-, viability rating of A-, and a support rating of 1 There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored daily. The Council is alerted to changes to ratings of all three agencies through its use of our creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on government support for banks and the credit ratings of that supporting government.

4.3 Country limits

The Council has determined that it will only use approved counterparties from other countries (where the approved counterparties from outside of the UK are from countries with a minimum sovereign credit rating of AAA from Fitch). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5.5. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

4.4 Investment strategy

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

Investment returns expectations. Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 4 of 2015. Bank Rate forecasts for financial year ends (March) are:

- 2013/14 0.50%
- 2014/15 0.50%
- 2015/16 0.75%
- 2016/17 1.75%

There are upside risks to these forecasts (i.e. start of increases in Bank Rate occurs sooner) if economic growth remains strong and unemployment falls faster than expected. However, should the pace of growth fall back, there could be downside risk.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year for the next four years are as follows:

2014/15	0.50%
2015/16	0.60%
2016/17	1.50%
2017/18	2.25%

Investment treasury indicator and limit - total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

Maximum principal sums invested > 364 days			
£m	**2014/15**	**2015/16**	**2016/17**
Principal sums invested > 364 days	£m Nil	£m Nil	£m Nil

4.5 Icelandic bank investments

Heritable Bank

Heritable bank is a UK registered bank under Scottish law. The company was placed in administration on 7 October 2008. The current position on actual payments received and estimated future payouts is as shown in the table below and this council has used these estimates to calculate the impairment based on recovering 88.61p in the £.

Date	Repayment
Received to date	77.30%
July 2013	5.50%
January 2014	5.81%

Recoveries are expressed as a percentage of the authority's claim in the administration, which includes interest accrued up to 6 October 2008.

4.6 End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

5 APPENDICES

(These can be appended to the report or omitted as required)

1. Interest rate forecasts
2. Economic background
3. Treasury management practice 1 – credit and counterparty risk management (option 1)
4. Approved countries for investments
5. Treasury management scheme of delegation
6. The treasury management role of the section 151 officer

5.1 APPENDIX: Interest Rate Forecasts 2014 – 2017

Please note – The current PWLB rates and forecast shown below have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012.

Capita Asset Services Interest Rate View	Now	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17
Bank Rate View	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.25%	1.50%	1.75%
3 Month LIBID	0.40%	0.50%	0.50%	0.50%	0.50%	0.50%	0.60%	0.70%	0.80%	0.90%	1.00%	1.20%	1.50%	1.70%
6 Month LIBID	0.49%	0.60%	0.60%	0.60%	0.60%	0.60%	0.70%	0.80%	1.00%	1.20%	1.30%	1.50%	1.70%	2.00%
12 Month LIBID	0.78%	0.80%	0.80%	0.80%	0.80%	0.90%	1.10%	1.20%	1.40%	1.60%	1.70%	1.90%	2.10%	2.30%
5yr PWLB Rate	2.63%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.40%	3.50%
10yr PWLB Rate	3.66%	3.70%	3.70%	3.80%	3.80%	3.90%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.50%
25yr PWLB Rate	4.32%	4.40%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%	4.90%	5.00%	5.00%	5.10%	5.10%	5.10%
50yr PWLB Rate	4.29%	4.40%	4.50%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.10%	5.10%	5.20%	5.20%
Bank Rate														
Capita Asset Services	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.50%	1.75%
UBS	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	-	-	-	-	-
Capital Economics	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	-	-	-	-	-
5yr PWLB Rate														
Capita Asset Services	2.63%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.40%	3.50%
UBS	2.63%	-	-	-	-	-	-	-	-	-	-	-	-	-
Capital Economics	2.63%	2.60%	2.60%	2.60%	2.60%	2.70%	2.80%	3.00%	3.20%	-	-	-	-	-
10yr PWLB Rate														
Capita Asset Services	3.66%	3.70%	3.70%	3.80%	3.80%	3.90%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.50%
UBS	3.66%	3.70%	3.80%	3.90%	4.05%	4.05%	4.30%	4.55%	4.55%	-	-	-	-	-
Capital Economics	3.66%	3.80%	3.80%	3.80%	3.80%	3.80%	3.80%	3.80%	4.05%	-	-	-	-	-
25yr PWLB Rate														
Capita Asset Services	4.32%	4.40%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%	4.90%	5.00%	5.00%	5.10%	5.10%	5.10%
UBS	4.32%	4.55%	4.55%	4.80%	4.80%	5.05%	5.05%	5.30%	5.30%	-	-	-	-	-
Capital Economics	4.32%	4.35%	4.35%	4.35%	4.35%	4.35%	4.35%	4.35%	4.45%	-	-	-	-	-
50yr PWLB Rate														
Capita Asset Services	4.29%	4.40%	4.50%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.10%	5.10%	5.20%	5.20%
UBS	4.29%	4.45%	4.45%	4.70%	4.70%	4.90%	4.90%	5.05%	5.05%	-	-	-	-	-
Capital Economics	4.29%	4.50%	4.50%	4.50%	4.50%	4.50%	4.50%	4.50%	4.60%	-	-	-	-	-

5.2. APPENDIX: Economic Background

THE UK ECONOMY

Economic growth. Until 2013, the economic recovery in the UK since 2008 had been the worst and slowest recovery in recent history. However, growth strongly rebounded in 2013 - quarter 1 (+0.3%), 2 (+0.7%) and 3 (+0.7%), to surpass all expectations as all three main sectors, services, manufacturing and construction contributed to this strong upturn. The Bank of England has, therefore, upgraded growth forecasts in the February quarterly Inflation Report for 2014 to 3.4%, 2015 to 2.7% and 2016 to 2.8% The February Report stated that: -

> *The UK recovery has gained momentum and inflation has returned to the 2% target. Reduced uncertainty, easier credit conditions and the stimulative stance of monetary policy should support continued solid economic growth, with the expansion in demand becoming more entrenched and more broadly based.*
> *Robust growth has not so far been accompanied by a material pickup in productivity. Instead, employment gains have been exceptionally strong and unemployment has fallen much more rapidly than expected. The LFS headline unemployment rate is likely to reach the MPC's 7% threshold by the spring of this year. Even so, the Committee judges that there remains spare capacity, concentrated in the labour market.*
> *Inflation is likely to remain close to the target over the forecast period. Given this, and with spare capacity remaining, the MPC judges that there remains scope to absorb slack further before raising Bank Rate. Moreover, the continuation of significant headwinds — both at home and from abroad — mean that Bank Rate may need to remain at low levels for some time to come.*

Forward guidance. The Bank of England issued forward guidance in August which stated that the Bank will not start to consider raising interest rates until the jobless rate (Labour Force Survey / ILO i.e. not the claimant count measure), had fallen to 7% or below. However, unemployment has fallen much quicker than the Bank expected and currently (17.2.14), stands at 7.1%. Accordingly, in the February Report, the Bank has now broadened its approach as follows: -

1. The MPC reckons there is spare capacity in the economy of 1-1.5% of GDP, mainly in the labour market
2. They will refrain from raising Bank Rate until a significant inroad has been made into reducing this spare capacity
3. They will provide additional forecasts based on eighteen economic indicators which they will take into account in considering the path of Bank Rate and QE
4. First increase in Bank Rate likely to be around Q2 2015
5. Rate rises will be slow and gradual (translation - probably 25bp per quarter)
6. Governor Carney expected that Bank Rate would be around 2% in three years time i.e. Q1 2017
7. Bank Rate is unlikely to get back up to pre crisis levels of 5% even when the economy has returned to normal
8. The Bank will not sell any of their portfolio of asset purchases before the first rise in the Bank Rate (but that does not mean they WILL start then!) and will also reinvest maturing gilts until then
9. They were more pessimistic on growth of productivity which has failed to keep pace with rises in output

10. They will make it a priority to protect growth in the economy provided inflation remains subdued (inflation forecast to be well behaved over the next two years: 1.9% in two year's time)

Forward surveys are currently very positive in indicating that growth prospects are strong for 2014, not only in the UK economy as a whole, but in all three main sectors, services, manufacturing and construction. This is very encouraging as there does need to be a significant rebalancing of the economy away from consumer spending to construction, manufacturing, business investment and exporting in order for this start to recovery to become more firmly established. One drag on the economy is that wage inflation continues to remain significantly below CPI inflation so disposable income and living standards are under pressure, although income tax cuts have ameliorated this to some extent. This, therefore, means that labour productivity must improve significantly for this situation to be corrected by the warranting of increases in pay rates.

Credit conditions. While Bank Rate has remained unchanged at 0.5% and quantitative easing has remained unchanged at £375bn in 2013, the Funding for Lending Scheme (FLS) was extended to encourage banks to expand lending to small and medium size enterprises. The second phase of Help to Buy, aimed at supporting the purchase of second hand properties, started in earnest in January 2014. These measures have been so successful in boosting the supply of credit for mortgages, and so of increasing house purchases, (though levels are still far below the pre-crisis level), that the Bank of England announced at the end of November that the FLS for mortgages would end in February 2014. While there have been concerns that these schemes are creating a bubble in the housing market, house price increases outside of London and the south-east have been much weaker. The Bank does not feel that Bank Rate increases would be effective in reducing house price inflation in London as a large part of property purchase is being done as cash transactions and / or by foreign purchasers, and is aggravated by a major short fall in new housing supply compared to the level of demand. As for bank lending to small and medium enterprises, this continues to remain weak and inhibited by banks still repairing their balance sheets and anticipating tightening of regulatory requirements.

Inflation. Inflation has fallen from a peak of 3.1% in June 2013 to 2.0% in December. It is expected to remain near to the 2% target level over the MPC's two year time horizon.

AAA rating. The UK has lost its AAA rating from Fitch and Moody's but that caused little market reaction.

THE GLOBAL ECONOMY

The Eurozone (EZ). The sovereign debt crisis has eased considerably during 2013 which has been a year of comparative calm after the hiatus of the Cyprus bailout in the spring. In December, Ireland escaped from its three year EZ bailout programme as it had dynamically addressed the need to substantially cut the growth in government debt, reduce internal price and wage levels and promote economic growth. The EZ finally escaped from seven quarters of recession in quarter 2 of 2013 but growth is likely to remain weak and so will dampen UK growth. The ECB's pledge to buy unlimited amounts of bonds of countries which ask for a bail out has provided heavily indebted countries with a strong defence against market forces. This has bought them time to make progress with their economies to return to growth or to reduce the degree of recession. However, debt to GDP ratios (2012 figures) of Greece 176%, Italy 131%, Portugal 124%, Ireland 123% and Cyprus 110%, remain a cause of concern, especially as many of these countries are experiencing continuing rates of increase in debt in excess of their rate of economic growth i.e. these debt ratios are continuing to deteriorate. Any sharp downturn in economic growth would make these countries particularly vulnerable to a new bout of sovereign debt crisis. It should also be noted that Italy has the third biggest debt mountain in the world behind Japan and the US. Greece remains particularly vulnerable and continues to struggle to meet EZ targets for fiscal correction. Whilst a Greek exit from the Euro is now improbable in the short term, as Greece has made considerable progress in reducing its annual government deficit and a return towards some economic growth, some commentators still view an eventual exit as being likely. There are also concerns that austerity measures in Cyprus could also end up in forcing an exit. The question remains as to how much damage an exit by one country would do and whether contagion would spread to other countries. However, the longer a Greek exit is delayed, the less are likely to be the repercussions beyond Greece on other countries and on EU banks.

Sentiment in financial markets has improved considerably during 2013 as a result of firm Eurozone commitment to support struggling countries and to keep the Eurozone intact. However, the foundations to this current “solution” to the Eurozone debt crisis are still weak and events could easily conspire to put this into reverse. There are particular concerns as to whether democratically elected governments will lose the support of electorates suffering under EZ imposed austerity programmes, especially in countries like Greece and Spain which have unemployment rates of over 26% and unemployment among younger people of over 50 – 60%. The Italian political situation is also fraught with difficulties in maintaining a viable coalition which will implement an EZ imposed austerity programme and undertake overdue reforms to government and the economy. There are also concerns over the lack of political will in France to address issues of poor international competitiveness,

USA. The economy has managed to return to robust growth in Q2 2013 of 2.5% y/y and 3.6% y/y in Q3, in spite of the fiscal cliff induced sharp cuts in federal expenditure that kicked in on 1 March, and increases in taxation. The Federal Reserve therefore decided in December to reduce its $85bn per month asset purchases programme of quantitative easing by $10bn and by another $10bn in January. It also amended its forward guidance on its pledge not to increase the central rate until unemployment falls to 6.5% by adding that there would be no increases in the central rate until ‘well past the time that the unemployment rate declines below 6.5%, especially if projected inflation continues to run below the 2% longer run goal’. Consumer, investor and business confidence levels have all improved markedly in 2013. The housing market has turned a corner and house sales and increases in house prices have returned to healthy levels. Many house owners have, therefore, been helped to escape from negative equity and banks have also largely repaired their damaged balance sheets so that they can resume healthy levels of lending. All this portends well for a reasonable growth rate looking forward.

China. There are concerns that Chinese growth could be on an overall marginal downward annual trend. There are also concerns that the new Chinese leadership have only started to address an unbalanced economy which is heavily dependent on new investment expenditure, and for a potential bubble in the property sector to burst, as it did in Japan in the 1990s, with its consequent impact on the financial health of the banking sector. There are also concerns around the potential size, and dubious creditworthiness, of some bank lending to local government organisations and major corporates. This primarily occurred during the government promoted expansion of credit, which was aimed at protecting the overall rate of growth in the economy after the Lehmans crisis.

Japan. The initial euphoria generated by “Abenomics”, the huge QE operation instituted by the Japanese government to buy Japanese debt, has tempered as the follow through of measures to reform the financial system and the introduction of other economic reforms, appears to have stalled. However, at long last, Japan has seen a return to reasonable growth and positive inflation during 2013 which augurs well for the hopes that Japan can escape from the bog of stagnation and deflation and so help to support world growth. The fiscal challenges though are huge; the gross debt to GDP ratio is about 245% in 2013 while the government is currently running an annual fiscal deficit of around 50% of total government expenditure. Within two years, the central bank will end up purchasing about Y190 trillion (£1,200 billion) of government debt. In addition, the population is ageing due to a low birth rate and, on current trends, will fall from 128m to 100m by 2050.

CAPITA ASSET SERVICES FORWARD VIEW

Economic forecasting remains difficult with so many external influences weighing on the UK. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, and safer bonds.

There could well be volatility in gilt yields over the next year as financial markets anticipate further tapering of asset purchases by the Fed. The timing and degree of tapering could have a significant effect on both Treasury and gilt yields. However, the political deadlock and infighting between Democrats and Republicans over the US budget and raising of the debt limit, has finally been resolved. This removes two destabilising issues for bond yields but investor concerns over the impact of tapering on emerging market countries created a surge of volatility during January, and especially in reaction to adverse political and economic developments in Argentina and Turkey.

The longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. Increasing investor confidence in economic recovery is also likely to compound this effect as a continuation of recovery will further encourage investors to switch back from bonds to equities.

The overall balance of risks to economic recovery in the UK is currently evenly weighted. However, only time will tell just how long this period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

The interest rate forecasts in this report are based on an initial assumption that there will not be a major resurgence of the EZ debt crisis, or a break-up of the EZ, but rather that there will be a managed, albeit painful and tortuous, resolution of the debt crisis where EZ institutions and governments eventually do what is necessary - but only when all else has been tried and failed. Under this assumed scenario, growth within the EZ will be tepid for the next couple of years and some EZ countries experiencing low or negative growth, will, over that time period, see a significant increase in total government debt to GDP ratios. There is a significant danger that these ratios could rise to the point where markets lose confidence in the financial viability of one, or more, countries. However, it is impossible to forecast whether any individual country will lose such confidence, or when, and so precipitate a resurgence of the EZ debt crisis. While the ECB has adequate resources to manage a debt crisis in a small EZ country, if one, or more, of the large countries were to experience a major crisis of market confidence, this would present a serious challenge to the ECB and to EZ politicians.

Downside risks currently include:

- UK strong economic growth is currently very dependent on consumer spending and recovery in the housing market. This is unlikely to endure much beyond 2014 as most consumers are maxed out on borrowing and wage inflation is less than CPI inflation, so disposable income is being eroded.
- A weak rebalancing of UK growth to exporting and business investment causing a major weakening of overall economic growth beyond 2014
- Weak growth or recession in the UK's main trading partners - the EU and US, depressing economic recovery in the UK.
- Prolonged political disagreement over the raising of the US debt ceiling.
- A return to weak economic growth in the US, UK and China causing major disappointment in investor and market expectations.
- A resurgence of the Eurozone sovereign debt crisis caused by ongoing deterioration in government debt to GDP ratios to the point where financial markets lose confidence in the financial viability of one or more countries and in the ability of the ECB and Eurozone governments to deal with the potential size of the crisis.
- Recapitalising of European banks requiring more government financial support
- Lack of support by populaces in Eurozone countries against austerity programmes, especially in countries with very high unemployment rates e.g. Greece and Spain, which face huge challenges in engineering economic growth to correct their budget deficits on a sustainable basis.
- The Italian political situation is frail and unstable; this will cause major difficulties in implementing austerity measures and a programme of overdue reforms. Italy has the third highest government debt mountain in the world.
- A lack of political will in France, (the second largest economy in the EZ), to dynamically address fundamental issues of low growth, poor international uncompetitiveness and the need for overdue reforms of the economy.
- Monetary policy action failing to stimulate sustainable growth in western economies, especially the Eurozone and Japan.
- Heightened political risks in the Middle East and East Asia which could trigger safe haven flows back into bonds.

The potential for upside risks to UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- A further upturn in investor confidence that robust world economic growth is firmly expected, causing a flow of funds out of bonds into equities.
- UK inflation being significantly higher than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

5.3 APPENDIX: Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management

SPECIFIED INVESTMENTS: All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable.

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the specified investment criteria. A maximum of 50% ** will be held in aggregate in non-specified investment

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.

The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

	*** Minimum credit criteria / colour band**	**** Max % of total investments/ £ limit per institution**	**Max. maturity period**
DMADF – UK Government	N/A	**100%**	**6 months**
UK Government gilts	UK sovereign rating	50%	5 years
UK Government Treasury blls	UK sovereign rating	50%	6 months
Bonds issued by multilateral development banks	UK sovereign rating	50%	6 months
Money market funds	AAA	100%	Liquid
Local authorities	N/A	100%	1 year
Term deposits with banks and building societies	Yellow Purple Blue Orange Red Green No Colour	£5m £5m £5m £5m £5m 0	Up to 5 years Up to 2 years Up to 1 year Up to 1 year Up to 6 Months Up to 100 days Not for use

CDs or corporate bonds with banks and building societies	Yellow Purple Blue Orange Red Green No Colour	0 0 0 0 0 0	Up to 5 years Up to 2 years Up to 1 year Up to 1 year Up to 6 Months Up to 100 days Not for use
Corporate bond funds		Nil	
Gilt funds	UK sovereign rating	Nil	
Property funds		Nil	

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

5.4 APPENDIX: Approved countries for investments

Based on lowest available rating

AAA

- Australia
- Canada
- Denmark
- Finland
- Germany
- Luxembourg
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Hong Kong
- Netherlands
- U.K.
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Qatar

AA-

- Belgium
- Saudi Arabia

5.5 APPENDIX: Treasury management scheme of delegation

(i) Full board/council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Boards/committees/council/responsible body

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Body/person(s) with responsibility for scrutiny

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

5.6 APPENDIX: The treasury management role of the section 151 officer

The S151 (responsible) officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

Meeting:	**Audit & Governance Committee**	**Date:**	**17th March 2014**
Subject:	**Internal Audit Plan 2013/14 – Monitoring Report**		
Report Of:	**Audit, Risk & Assurance Manager**		
Wards Affected:	**Not applicable**		
Key Decision:	**No**	**Budget/Policy Framework:**	**No**
Contact Officer:	**Terry Rodway, Audit, Risk & Assurance Manager**		
	Email: Terry.Rodway@gloucester.gov.uk	**Tel: 396430**	
Appendices:	**A: List of the audits completed – November 2013 to February 2014** **B: Rank 1 'High Priority' Recommendations Not Implemented by Agreed Date**		

FOR GENERAL RELEASE

1.0 Purpose of Report

1.1 To inform Members of the audits completed as part of the approved Internal Audit Plan 2013/14.

2.0 Recommendations.

2.1 Audit & Governance Committee is asked to **RESOLVE** that:-

(1) Members endorse the audit work undertaken to date, and the assurance given on the adequacy of internal controls operating in the systems audited.

3.0 Background and Key Issues

3.1 At the Audit & Governance Committee meeting held on 18th March 2013, Members approved the Internal Audit Plan 2013/14. In accordance with the Public Sector Internal Audit Standards, this report details the outcomes of internal audit work carried out in accordance with the approved Plan.

3.2 This report includes details of the audits completed during the period November 2013 to February 2014. The performance monitoring information is based on the number of completed audits vs. the number of planned audits (i.e. an output measure). The indicator for the 11 month period ending 28th February 2014 is 78% (21 out of 27 planned audits completed) compared to a target of 90%. These figures do not include two audits that were at Final Report stage, and one audit that was substantially complete, as at the end of February 2014.

3.3 The main reasons for the non-achievement of the audit target are: (a) a number of audits taking longer to complete than originally planned, and (b) a member of the team recently carrying out duties as a recognised union representative, the time for which is allowed for in the appropriate council policy, but this time was not included in the original agreed Audit Plan.

3.4 Details of the audits completed, together with the overall conclusion reached on each audit, have been provided in **Appendix A**. This should provide Members with a view on the adequacy of the controls operating within each area audited.

3.5 It has previously been agreed that Members would be notified of all ‘Rank 1 Fundamental’ recommendations that have not been implemented within the agreed timescale. Subject to the comments below in para. 4.0, re the Markets Audit, one other Rank 1 recommendation has been identified as not being implemented by the agreed date – see Appendix B for details.

4.0 Markets Audit – Follow up to Audit Recommendations

4.1 At the previous meeting of the Audit & Governance Committee, Members requested that the Follow-Up audit to the Markets Audit be undertaken. It was agreed by the Audit, Risk and Assurance Manager that this audit would be undertaken in January 2014.

4.3 There were two Rank 1 ‘High Priority’ recommendations that were subject to review, with one, relating to the calculation of gross costs, only being partially implemented by the agreed date. Details have been provided in **Appendix B.**

5.0 Alternative Options Considered

5.1 No other options have been considered as the purpose of the report is to inform the Committee of the audit work undertaken to date, and the assurance given on the adequacy of internal controls operating in the systems audited.

6.0 Reasons for Recommendations

6.1 The Public Sector Internal Audit Standards state that the Audit, Risk & Assurance Manager should report on the outcomes of internal audit work, in sufficient detail, to allow the Committee to understand what assurance it can take from that work and/or what unresolved risks or issues it needs to address.

7.0 Future Work and Conclusions

7.1 The role of the Audit & Assurance service is to examine, evaluate and report upon the adequacy of internal controls. Where weaknesses have been identified, recommendations have been made to improve the level of control.

8.0 Financial Implications

8.1 As detailed in this report.

(Financial Services have been consulted in the preparation this report).

9.0 Legal Implications

9.1 None specific to this report.

(Legal Services have been consulted in the preparation this report).

10.0 Risk & Opportunity Management Implications

10.1 Delays in response to acceptance/implementation of audit recommendations lead to weaknesses continuing to exist in systems, which has the potential for fraud and error to occur.

11.0 People Impact Assessment (PIA):

11.1 A requirement of the Accounts & Audit Regulations 2011 is for the Council to undertake an adequate and effective internal audit of its accounting records and of its system of internal control. The internal audit service is delivered by the in house team. Equality in service delivery is demonstrated by the team being subject to, and complying with, the Council's equality policies.

11.2 The PIA Screening Stage was completed and did not identify any potential or actual negative impact, therefore a full PIA was not required.

12.0 Other Corporate Implications

Community Safety

12.1 There are no community safety implications arising out of the recommendation in this report.

Sustainability

12.2 There are no sustainability implications arising out of the recommendation in this report.

Staffing & Trade Union

12.3 There are no staffing and trade union implications arising out of the recommendation in this report.

Background Documents:

Internal Audit Plan 2013/14
Public Sector Internal Audit Standards

APPENDIX A

List of the audits completed – November 2013 to February 2014

Audit	Comments	Level of Assurance
FMS Upgrade	<u>Audit Objective</u> The Financial Management System was identified as requiring an upgrade. Internal Audit were invited to partake in the project from commencement of implementation with the aim of reviewing activities and progress. <u>Audit Opinion</u> A good level of assurance has been provided that the project for upgrading the Financial Management System to e-Financials V4.1 has been completed and that the transfer of data has been successfully reconciled.	Good
BT&T	<u>Audit Objective</u> The audit objective was to ensure that controls are in place and operating effectively over: • Network Controls • Disaster recovery and business continuity • Application controls i.e. inventory; interfaces; insurance. **NB** An assurance level has not been provided as part of this audit for controls around application security, user privileges, logical access, parameters / functionality testing, and reporting and monitoring, as these areas are covered by individual audits in the various service areas. <u>Audit Opinion</u> On the basis of the work carried out during this audit, and the level of error identified through audit testing, the audit opinion is that there is a **Good** level of assurance in relation to Application Controls, and a **Satisfactory** level of assurance in relation to Network Controls. There is a **Limited** level of assurance in relation to Business Continuity. The main area of weakness identified, for which one 'High' priority recommendation has been made relates to the BT&T Business Continuity Plan (BCP) being out-of date. As this BCP is considered to be the primary document for the Council's Disaster Recovery arrangements, there is also a **Limited** level of assurance in relation to Disaster Recovery.	Good/Satisfactory/ Limited

Audit	Comments	Level of Assurance
Social Media Policy	<u>Audit Objective</u> The audit was carried out in order to provide management with a level of assurance that controls are both in place and operating effectively towards mitigating risks associated with the Council’s use of social media. The audit objective was to ensure that controls are in place and operating effectively over : • Social media policy and guidance • Social media users and security • Social media effectiveness and use <u>Audit Opinion</u> On the basis of the work carried out during this audit, and the level of error identified through audit testing, the audit opinion is that there is a **Good** level of assurance in relation to ‘Effectiveness and Use’, and a **Satisfactory** level of assurance in relation to ‘Policy & Guidance’, that the risk of reputational damage to the Council, through misuse of social media, is being mitigated to an acceptable level. There is a **Limited** level of assurance in relation to ‘Users and Security’. The main area of weakness identified, for which one Rank 1 ‘High Priority’ and one Rank 2 ‘Medium Priority’ recommendations have been made relate to the lack of a periodic review of users, or regular password changes, nor any formal controls or procedures around leavers that have had access to the Council’s social media accounts.	Good/Satisfactory/ Limited
Council Tax	<u>Audit Objective</u> The objective of the audit was to ensure the following key controls were in place and operating effectively:- • Periodic reconciliation of Council Tax system to Valuation Office listings; • Periodic reconciliation of Council Tax system to the Cash Receipting system; • Periodic reconciliation of Council Tax system to the General Ledger; • Independent review of exceptions e.g. banding changes, suppressed accounts, overpayments and refunds; • Periodic production and independent review of Council Tax arrears and collection reports	Good/Limited

Audit	Comments	Level of Assurance
	<u>Audit Opinion</u> On the basis of the work carried out during this audit, and the level of error identified through audit testing, the audit opinion is that there is a **Good** level of assurance in all areas covered by the audit except for the testing in relation to suppressed accounts, for which a **Limited** level of assurance has been provided. The main areas of weakness, for which two 'Medium Priority' recommendations have been made relate to:- • The lack of documentary evidence that CTAX inhibits identified within the Batch Billing Exception Reports are being reviewed on a regular basis. • The lack of documentary evidence that CTAX inhibits are being reviewed in line with the reporting timeframe.	
NNDR	<u>Audit Objective</u> The objective of the audit was to ensure the following key controls were in place and operating effectively:- • Periodic reconciliation of the NNDR system to the Valuation Office rateable value listing; • Periodic reconciliation of the NNDR system to the cash receipting system; • Periodic reconciliation of the NNDR system to the general ledger; • Periodic review of exceptions: e.g. rateable value changes, suppressed accounts, overpayments and refunds; • Periodic production of NNDR arrears and collection reports and independent review <u>Audit Opinion</u> On the basis of the work carried out during this audit, and the level of error identified through audit testing, the audit opinion is that there is a **Good** level of assurance in all areas covered by the audit except for the testing in relation to suppressed accounts for which a **Limited** level of assurance has been provided. The main areas of weakness, for which two 'Medium Priority' recommendations have been made relate to:- • The lack of documentary evidence that CTAX inhibits identified within the Batch Billing Exception Reports are being reviewed on a regular basis. • The lack of documentary evidence that CTAX inhibits are being reviewed in line with the reporting timeframe. .	Good/Limited

Audit	Comments	Level of Assurance
Parking	<u>Audit Objective</u> The objective of the audit was to ensure the following controls were in place and operating effectively:- , • Payments to the Contractor / partner can be substantiated to supporting documentation; • Key performance data is monitored and profit share amended as necessary. • Income from contractor / partner can be substantiated to supporting documentation. • Penalty Charge Notices are appropriately processed, income received is adequately controlled, and, cases taken to court comply with the enforcement timetable. • Pay & Display meters are regularly emptied and the takings verified. • Permits are adequately controlled. <u>Audit Opinion</u> On the basis of the work carried out during this audit, and the level of error identified through audit testing, the audit opinion is that there is a **Good** level of assurance in all areas covered by the audit except for income for which a **Limited** level of assurance has been provided. The main areas of weakness for which three Rank 2 'Medium Priority' recommendations have been made relate to:- • The lack of checking of current staff/member parking permits to ensure the correct payments are being made; • Software interface issues with the system software that has resulted in bailiff payments having not been updated on the system since April / May 13, and have also resulted in the council not being able to issue any new cases to the bailiff for the same period.	Good/Limited

The report includes an audit opinion on the adequacy of controls in the area that has been audited, classified in accordance with the following descriptions:-

CONTROL LEVEL	DESCRIPTION
Good	Robust framework of controls – provides substantial assurance. A few minor recommendations (if any) i.e. Rank 3 (Low Priority).
Satisfactory	Sufficient framework of controls – provides satisfactory level of assurance – minimal risk. A few areas identified where changes would be beneficial. Recommendations mainly Rank 3 (Low Priority), but one of two in Rank 2 (Medium Priority).

Limited	Some lapses in framework of controls – provides limited level of assurance. A number of areas identified for improvement. Mainly Rank 2 (Medium Priority) recommendations, but one or two Rank 1 (High Priority) recommendations.
Unsatisfactory	Significant breakdown in framework of controls – provides an unsatisfactory level of assurance. Unacceptable risks identified – fundamental changes required. A number of Rank 1 (High Priority) recommendations.

Ranking of Recommendations:-

RANK		**DESCRIPTION**
1	High Priority	Necessary due to statutory obligation, legal requirement, Council policy or major risk of loss or damage to Council assets, information or reputation, or, compliance with External Audit key control.
2	Medium Priority	Could cause limited loss of assets or information or adverse publicity or embarrassment. Necessary for sound internal control and confidence in the system to exist.
3	Low Priority	Current procedure is not best practice and could lead to minor in-efficiencies.

Appendix B

Rank 1 'High Priority' Recommendations Not Implemented by Agreed Date

Audit	Date	Recommendation	Agreed Action	Responsible Officer	Agreed Implementation Date	Management comment
Procurement	July 2013	The use of supplier lists is to be fully assessed to ensure that the process is legal and that it does not infringe upon other Procurement Strategy objectives such as competition and access, best value, and ethics	Procurement Officer will raise with the Legal & Democratic Services Manager at next procurement update meeting in July.	Legal & Democratic Services Manager & Procurement Officer	July 2013	The Head of Legal & Policy Development has advised that the issue of supplier lists is one of many items to be assessed under the planned revision of the contract procedure rules. Whilst supplier lists have historically drifted in and out of favour it is accepted that actions are required to assess whether they infringe upon other Procurement Strategy objectives such as competition and access, best value, and ethics or if such lists are even legal under EU procurement rules. Consideration should also be given to the fact that a revision to the EU procurement rules is anticipated to come into effect circa 2014/15 and that any revision of GCC's contract procedure rules will require having to take account of any changes coming into effect during the 2014/15 financial year. Revised implementation date -

Audit	Date	Recommendation	Agreed Action	Responsible Officer	Agreed Implementation Date	Management comment
						March 2014.
Markets	July 2013	Each of the gross costs being used to calculate the stallholder charges are to be revisited with actions being taken to ensure that the costs incurred by the City Council are being fully accounted for.	The service charge costs are to be reviewed. The service charge costs are to be loaded onto the costing spreadsheet. Stallholder invoices for 2013/14 are to be reviewed to ensure that they are in line with the values calculated from the costing spreadsheet	Markets Manager	September 2013	Food, Licensing & Markets Manager – Partially implemented. Once the Asset Management Team determine the new licence fees, each stall holder will be given 3 months written notice of new fees taking effect – Revised implementation date - March 2014.
Markets	July 2013	Actions are to be taken to ensure that the ongoing issue of stallholders being charged an incorrect monthly proportion of their annual charge is addressed and rectified.	Decision will have to be made upon how far to take back any under or over charges, with actions being taken as required. All stallholder invoices to be reviewed and actioned as required dependant upon the decision.	Markets Manager	September 2013	Food, Licensing & Markets Manager -Once fees are determined, write to each stall licence holder to inform them changes to their fees allowing 3 months notice to take effect. Ensure effective dates reflect a Monday in accordance with their licence and also in line with Sundry Debtors billing timescales – Revised implementation date April 2014.

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Gloucester City Council

Meeting:	**Audit & Governance Committee**	**Date:**	**17th March 2014**
Subject:	**Internal Audit Plan 2014/15**		
Report Of:	**Audit, Risk & Assurance Manager**		
Wards Affected:	**Not applicable**		
Key Decision:	**No**	**Budget/Policy Framework:**	**No**
Contact Officer:	**Terry Rodway - Audit, Risk & Assurance Manager**		
	Email: terry.rodway@gloucester.gov.uk		**Tel: 396430**
Appendices:	**A. Internal Audit Plan 2014/15** **B. Internal Audit Risk Assessment**		

FOR GENERAL RELEASE

1.0 Purpose of Report

1.1 To present to Members, for their consideration and approval, the Internal Audit Plan 2014/15.

2.0 Recommendations

2.1 Audit & Governance Committee is asked to **RESOLVE** that:-

(1) Members approve the Internal Audit Plan 2014/15 as detailed in **Appendix A**.

3.0 Background and Key Issues

3.1 The work of Internal Audit is carried out in accordance with, and is assessed against, the professional code of practice in Internal Audit. This Code includes a requirement for the Audit, Risk & Assurance Manager to prepare a risk-based plan that should be fixed for a period of no longer than one year.

4.0 Progress

4.1 The proposed Internal Audit Plan for 2014/15 follows risk-based principles and starts with the completion of an audit needs assessment of all the areas of the Council that could be included within an annual audit plan. The risk-based approach has taken into account the following:-

- 'Known' changes to service delivery (budget/legislation);
- Joint Working protocol with the Council's external auditor;
- Audit Commission publication 'Protecting the Public Purse';
- Internal Audit Risk Assessment

4.2 The proposed Internal Audit Plan is split into the following main areas:-

4.2.1 Corporate Governance/Annual Governance Statement (AGS)
The production of the AGS is a requirement under the Accounts and Audit Regulations 2011. The purpose of the AGS is to provide assurance that the Council's governance framework is adequate and effective. This area of Audit & Assurance audit work is one of the key components of the internal control assessment that supports the completion of the AGS.

4.2.2 Work on fundamental financial systems
This is the work on the Council's financial systems, which are significant in relation to financial control and materiality. The work supports the Corporate Director of Resources to discharge his duties as the Council's s.151 Officer. It also forms a key element of the Joint Working Protocol with the Council's External Auditors, as the External Auditor can place reliance on the internal audit work on these systems. This will help inform their judgement on the Council's financial control environment, and is also one of the factors taken into account when calculating the External Audit fee.

4.2.3 Work of a service based or cross Council nature
This is all of the other service activities or cross cutting themed audit reviews that could be undertaken, which are risk scored using the risk-based approach detailed in paragraph 4.3 below.

4.2.4 Follow-up reviews
The plan will include follow-up reviews, which will ensure recommendations have been adopted and successfully implemented, providing the enhanced control/reduced level of risk exposure intended. The extent of this work will again be risk based dependant upon the audit findings and the recommendations made within the original audit reports.

4.2.5 Audit work brought forward
There will be a number of audit reviews, which are ongoing as at 31st March. Provision to complete this work is made in the annual plan.

4.2.6 Contingency
In line with the Code, the Annual Plan includes a contingency element to accommodate assignments which could not have been reasonably foreseen, eg. investigation of alleged fraud.

4.2.7 Work for Gloucester City Homes (GCH)
The Audit & Assurance team undertakes work for GCH under a service level agreement. A similar risk-based approach has been adopted to inform the annual audit plan for GCH.

4.3 The next stage is to apply the risk-based approach. The approach adopted borrows from various models and is based on allocating scores to a number of objective and subjective factors which, when multiplied together, produce a total risk score. The aim of the model is to indicate the relative risk of one activity over another based on knowledge of the assessment factors.

4.4 The various factors considered in determining the risk of an activity include the statutory requirement to undertaken the function; the internal audit review of the control environment based on previously completed audit work; the financial value of the activity; the period since the last audit review; the complexity of system in use; and the level of inherent risk. Details of the risk assessment approach are included in **Appendix B**.

4.5 In addition to the risk assessment outlined in paragraph 4.3, the Council's senior managers have been consulted on the key risk areas within their areas of responsibility.

4.6 Due to the nature and relevance of the assurance work for the AGS (para 4.2.1), and the audit work on the fundamental financial systems (para 4.2.2), both will automatically be included in the Annual Plan and not be subject to the detailed risk assessment.

4.7 Having completed the risk assessment, the next stage is for the assessment to be compared to resource availability; i.e. the number of audit days available. This is calculated as the gross number of days available during the year, less an allocation for leave, training, sickness etc. The number of available days for audit for 2014/15, based on the current establishment of 2.6 FTE audit staff is 500 days (192 days per FTE).

4.8 Risk is key to the planning process, but risk is not static, therefore the plan needs to be flexible to be able to reflect the changing risks and priorities of the organisation. Whilst some provision for flexibility is made through the inclusion in the plan of a contingency, this usually covers other unplanned items, which may impact on a small section, eg. additional sickness or investigation of alleged fraud. Any significant matters that may jeopardise the delivery of the Plan, or require changes to the Plan, will be identified and reported to the Audit & Governance Committee.

5.0 Alternative Options Considered

5.1 None.

6.0 Reasons for Recommendations

6.1 A requirement of the professional Code of Practice for Internal Audit is for the risk-based Internal Audit plan to be approved by the appropriate body. In the case of the City Council, this is the Audit & Governance Council.

7.0 Future Work and Conclusions

7.1 Regular reports on achievement against the Plan, and any significant control issues identified, will be presented to the Audit & Governance Committee.

7.2 The professional code of practice for Internal Audit includes a requirement for the Audit, Risk & Assurance Manager to prepare a risk-based plan that should be fixed for a period of no longer than one year. The proposed Internal Audit Plan for 2014/15 follows risk-based principles and starts with the completion of an audit needs assessment of all the areas of the Council that could be included within an annual audit plan.

8.0 Financial Implications

8.1 There are no specific financial implications.

(Financial Services have been consulted in the preparation this report.)

9.0 Legal Implications

9.1 There are no specific legal implications.

(Legal Services have been consulted in the preparation this report.)

10.0 Risk & Opportunity Management Implications

10.1 The organisation is responsible for establishing and maintaining appropriate risk management processes, control systems, accounting records and governance arrangements. Internal audit, through the delivery of the annual audit plan, plays a vital part in advising the organisation that these arrangements are in place and operating properly.

11.0 People Impact Assessment (PIA):

11.1 The PIA Screening Stage was completed and did not identify any potential or actual negative impact, therefore a full PIA was not required.

12.0 Other Corporate Implications

Community Safety

12.1 There are no specific Community Safety implications identified.

Sustainability

12.2 There are no specific Sustainability implications identified.

Staffing & Trade Union

12.3 There are no specific Staffing and Trade Union implications identified.

Background Documents: The Public Sector Internal Audit Standards

APPENDIX A

PROPOSED INTERNAL AUDIT PLAN 2014-2015

Main Area	Audit	Estimated Days	Comment
Corporate Governance/Work to support the AGS	• Risk Management • Performance Management	• 15 • 15	• Review of management of significant risks • Review of PI reporting and data quality arrangements
Work on Fundamental Financial Systems	• Civica – Benefits • Civica – NNDR • Civica – Council Tax • Payroll (including Client Monitoring) • Creditors • Civica – Debtors • Treasury Management (SBA) • Budgetary Control (SBA) • Cash & Bank • Capital Accounting (SBA) • General Ledger • Financial Services Improvement Plan	• 25 • 8 • 8 • 15 • 10 • 8 • 8 • 15 • 10 • 15 • 10 • 10	Annual compliance testing of high level key controls in fundamental financial systems, in accordance with the Joint Working Protocol the Audit Team has with the Council's External Auditor. 3 year cyclical plan of system based audits (SBA) on fundamental financial systems to gain assurance on adequacy of control framework.
Work of a Service Based or Cross Cutting Theme	• Civica – IT • Client Monitoring of Contracts – Civica • Streetcare Contract • Benefit Fraud	• 20 • 10 • 15 • 10	• Main areas (as per CIPFA Control Matrices) to be audited over a 3 year period • Review of controls relating to client monitoring of contract • Review of controls relating to client monitoring of contract. • Review of controls to prevent and detect fraud and corruption

	• NDR Rate Relief claims • Council Tax Discounts • S106 Agreements • Contract Audit • Glos Supports Business Programme • Guildhall/Blackfriars • Members Expenses • Elections	• 10 • 10 • 10 • 25 • 10 • 15 • 10 • 10	• Review of controls to prevent and detect fraud and corruption • Review of controls to prevent and detect fraud and corruption • Review of controls to ensure all Agreements identified and requirements complied with. • Contract Management arrangements/Final Account auditing • Review of compliance with conditions of grant • Income and expenditure audit • Review to ensure payments made in accordance with approved scheme • Review of claims
Glos City Homes		• 50	Audits as per agreed plan with GCH
Follow – Up Reviews	26 audits at 2 days per follow-up	• 52	Allocation of days to carry out Follow-Up audits to ensure agreed audit recommendations have been implemented.
Contingency		• 46	Allocation of days for unplanned tasks.
Audit Work Brought Forward		• 25	Allocation of days to complete previous year audit work outstanding as at 31st March.
TOTAL DAYS		**500**	

APPENDIX B

INTERNAL AUDIT RISK ASSESSMENT

ASSESSMENT	SCORE	DESCRIPTION
Monetary Value – Sum of income and expenditure	8	>£3.0M
	6	>£1.0M <£3.0M
	4	>£0.5M <£1.0M
	2	>£100K <£0.5M
	1	<£100k
Inherent Risk	5	High exposure to public scrutiny, complex legal framework, high volume of transactions, statutory function, outsources/partnership arrangement for service delivery
	4	High volume of ‘cash’ transactions, and/or exposure to public scrutiny, and/or statutory function
	3	High volume of ‘cash’ transactions, and/ or statutory function
	2	Low volume of ‘cash’ transactions, non-statutory function
	1	Low volume of transaction, non-statutory function.
Internal Audit Control Perception	4	Poor control system, and/or high opportunity for fraud and corruption/Unsatisfactory level of assurance
	3	Control weakness that needed rectification last audit/Limited level of assurance
	2	Control environment proved adequate last audit/Satisfactory level of assurance
	1	Control environment has proved adequate for a number of years/good level of assurance
Complexity of Systems	5	Very complex systems and processes used in generating significant service related results
	4	Complex data inputs, or strategically/operationally important outputs
	3	Moderate systems but accuracy of process has significant impact, systems stability issues
	2	Complex or moderate systems with stable performance and processing history
	1	Simple or no ICT system used
Period since last audit	4	3+ years – pre 2011
	3	3 years – 2011/12
	2	2 years – 2012/13
	1	Last financial year - 2013/14

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Gloucester City Council

Meeting:	**Audit & Governance Committee**	**Date:**	**17 March 2014**
	Constitutional and Electoral Working Group		**25 March 2014**
	Council		**27 March 2014**
Subject:	**Review of Terms of Reference for Audit and Governance Committee**		
Report Of:	**Head of Legal and Policy Development**		
Wards Affected:	**All**		
Key Decision:	**No**	**Budget/Policy Framework:**	**No**
Contact Officer:	**Sue Mullins, Head of Legal and Policy Development**		
	Email: sue.mullins@gloucester.gov.uk	**Tel:**	**396110**
Appendices:	**1. Table showing current Terms of Reference and CIPFA suggested Terms of Reference** **2. Proposed Terms of Reference**		

1.0 Purpose of Report

1.1 To consider updated Terms of Reference for the Committee for adoption by the Council.

2.0 Recommendations

2.1 Audit and Governance Committee is asked to **RECOMMEND** to Constitutional and Electoral Working Group and Council that the Terms of Reference at Appendix 2 be approved;

2.2 Constitutional and Electoral Working Group is asked to **RECOMMEND** to Council that the Terms of Reference at Appendix 2 be approved;

2.3 Council is asked to **RESOLVE** that the Terms of Reference at Appendix 2 be approved.

3.0 Background and Key Issues

3.1 The Audit & Governance Committee's current Terms of Reference were set in 2012 and include Terms of Reference from the former Standards Committee.

3.2 Following the Committee meeting on 25 November 2013, a Working Group was formed to consider the Terms of reference for the Committee. The Working Group met on 6 March 2014 and considered the table shown at Appendix 1. The Working Group's recommendation is that the suggested Terms of Reference shown at Appendix 2, be recommended for adoption.

3.3 The Committee is asked to note that the anticipated CIPFA guidance does not suggest Terms of Reference in relation to the Committee's standards responsibilities. The Committee's suggested standards functions are based on the parts of the former Standards Committee's responsibilities that remain relevant following the changes made by the Localism Act.

4.0 Alternative Options Considered

4.1 No other options have been considered.

5.0 Reasons for Recommendations

5.1 It is good practice to regularly review the Terms of Reference for the Committee to ensure that they remain up-to-date and reflect best practice.

6.0 Future Work and Conclusions

6.1 As has been identified in the report

7.0 Financial Implications

7.1 There are no direct financial implications arising out of this report.

(Financial Services have been consulted in the preparation this report.)

8.0 Legal Implications

8.1 Under the Local Government Act 2000, the Council is required to have a Constitution setting out its governance arrangements. CIPFA guidance also requires the Committee to regularly review its effectiveness and this includes ensuring that its Terms of Reference are appropriate for the functions an audit committee should perform.

(Legal Services have been consulted in the preparation this report.)

9.0 Risk & Opportunity Management Implications

9.1 If the Terms of Reference for the Committee are not reviewed, there is a risk that they will cease to reflect best practice or be appropriate for the functions the Committee needs to perform.

10.0 People Impact Assessment (PIA):

10.1 The PIA Screening Stage was completed and did not identify any potential or actual negative impact, therefore a full PIA was not required.

11.0 Other Corporate Implications

Community Safety

11.1 There are no specific Community Safety implications relating to the recommendation made in this report.

Sustainability

11.2 There are no specific Sustainability implications relating to the recommendation made in this report.

Staffing & Trade Union

11.3 There are no staffing or trade union implications arising from this report.

Background Documents: None.

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Appendix 1 - Comparison of current Terms of Reference and CIPFA suggested Terms of Reference for Audit Committees

	Current Terms of Reference/Powers and Responsibilities	CIPFA Suggested Terms of Reference
		Governance, risk and control
1.	To consider the Council's arrangements for corporate governance and recommend the necessary action to ensure compliance with best practice.	To review the Council's corporate governance arrangements against the good governance framework and consider annual governance reports and assurances.
2.	To approve the statement of accounts and the annual governance statement.	To review the Annual Governance Statement prior to approval and consider whether it properly reflects the risk environment and supporting assurances, taking into account internal audit's opinion on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control.
3.		To consider the Council's arrangements to secure value for money and review assurances and assessments on the effectiveness of these arrangements.
4.		To consider the Council's framework of assurance and ensure that it adequately addresses the risks and priorities of the council.
5.	To monitor the effective development and operation of risk management and corporate governance.	To monitor the effective development and operation of risk management in the council.
6.		To monitor progress in addressing risk-related issues reported to the committee.
7.	To consider the Group Manager, Audit and Assurance's annual report and a summary of the internal audit activity (actual and proposed) and the level of assurance it can give over the Council's corporate governance arrangements, including an opinion on the overall	To consider reports on the effectiveness of internal controls and monitor the implementation of agreed actions.

	adequacy and effectiveness of the Council's internal control environment.	
8.	To approve the Council's anti-fraud and corruption policies and any other governance policies deemed necessary.	To review the assessment of fraud risks and potential harm to the Council from fraud and corruption.
9.		To monitor the counter-fraud strategy, actions and resources.
		Internal Audit
10.		To approve the internal audit charter.
11.	To liaise with the Audit Commission over the appointment of the Council's external auditor.	To review proposals made in relation to the appointment of external providers of internal audit services and to make recommendations.
12.	To approve the Internal Audit Periodic Plan, receive reports on progress and as a consequence approve any material changes to the plan	To approve the risk-based internal audit plan, including internal audit's resource requirements, the approach to using other sources of assurance and any work required to place reliance upon those other sources.
13.		To approve significant interim changes to the risk-based internal audit plan and resource requirements.
14.		To make appropriate enquiries of both management and the head of internal audit to determine if there are any inappropriate scope or resource limitations.
15.		To consider reports from the head of internal audit on internal audit's performance during the year, including the performance of external providers of internal audit services. These will include:- a) Updates on the work of internal audit including key findings, issues of concern and action in hand as a result of internal audit work.

		b) Regular reports on the results of the Quality Assurance and Improvement Programme. c) Reports on instances where the internal audit function does not conform to the Public Sector Internal Audit Standards and Local Government Application Note, considering whether the non-conformance is significant enough that it must be included in the Annual governance Statement.
16.	To consider the Group Manager, Audit and Assurance's annual report and a summary of the internal audit activity (actual and proposed) and the level of assurance it can give over the Council's corporate governance arrangements, including an opinion on the overall adequacy and effectiveness of the Council's internal control environment.	To consider the head of internal audit's annual report: a) The statement of the level of conformance with the Public Sector Internal Audit Standards and Local Government Application Note and the results of the Quality Assurance and Improvement Programme that supports the statement – these will indicate the reliability of the conclusions of internal audit. b) The opinion on the overall adequacy and effectiveness of the council's framework of governance, risk management and control together with a summary of the work supporting the opinion – these will assist the committee in reviewing the Annual Governance Statement
17.	To consider summaries of specific internal audit reports, quarterly.	To consider summaries of specific internal audit reports as requested.
18.	To consider a report from internal audit on agreed recommendations not implemented within a reasonable timescale.	To receive reports outlining the action taken where the head of internal audit has concluded that management has accepted a level of risk that may be unacceptable to the authority or there are concerns about progress with the implementation of agreed actions.
19.		To contribute to the Quality and Improvement Programme and in particular, to the external quality assessment of internal audit that takes place at least once every five years.
20.	To consider an annual report on the performance of the internal audit service and review the effectiveness of the	To consider a report on the effectiveness of internal audit to support the Annual Governance Statement, where required to do

	service in accordance with the Accounts and Audit Regulations.	so by the Accounts and Audit Regulations.
21.		To support the development of effective communication with the head of internal audit.
		External Audit
22.	To consider the external auditor's annual letter, relevant reports, and the report of those charged with governance.	To consider the external auditor's annual letter, relevant reports, and the report of those charged with governance.
23.	To consider specific reports as agreed with the external auditor.	To consider specific reports as agreed with the external auditor.
24.	To comment on the scope and depth of external audit work and to ensure it gives value for money.	To comment on the scope and depth of external audit work and to ensure it gives value for money
25.	To commission work from internal and external audit.	To commission work from internal and external audit.
26.		To advise and recommend on the effectiveness of relationships between external and internal audit and other inspection agencies or relevant bodies.
		Financial Reporting
27.	To review the annual statement of accounts. Specifically, to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements or from the audit that need to be brought to the attention of the Council.	To review the statement of accounts. Specifically, to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements or from the audit that need to be brought to the attention of the Council.
28.	To consider the external auditor's report on issues arising	To consider the external auditor's report to those charged with

	from the audit of the accounts	governance on issues arising from the audit of the accounts.
29.	To approve the statement of accounts and the annual governance statement.	
		Treasury Management
30.		To review and monitor treasury management arrangements in accordance with the CIPFA Treasury Management Code of Practice.
		Accountability arrangements
31.		To report to those charged with governance on the committee's findings, conclusions and recommendations concerning the adequacy and effectiveness of their governance, risk management and internal control frameworks; financial reporting arrangements, and internal and external audit functions.
32.		To report to full council on a regular basis on the committee's performance in relation to the terms of reference and the effectiveness of the committee in meeting its purpose.
33.	To consider and review changes to the Council's constitution in respect of Contract Standing Orders, Financial Regulations, and Codes of Conduct and behaviour.	
34.	To monitor the operation of the Council's codes and protocols (see Part 5 of this Constitution) and the Council's complaints process and to advise the Council on the adoption or revision of such codes.	
35.	To consider the Council's compliance with it's own	

	published standards and controls.	
36.	To review any issues referred to it by the Chief Executive or a Corporate Director or any Council body.	
	Standards	
37.	To receive allegations and any accompanying report from the Monitoring Officer and to refer the allegation to the Monitoring Officer for formal investigation or informal resolution.	
38.	To set up, where necessary, a Hearings Panel to consider any alleged breach of the Members' Code of Conduct.	
39.	To promote and maintain high standards of conduct by Councillors and co-opted Members.	
40.	To assist Councillors and co-opted Members to observe the Members' Code of Conduct.	
41.	To advise the Council on the adoption, revision of, or publicity on the Members' Code of Conduct.	
42.	To advise, train or arrange to train Councillors and co-opted Members on matters relating to the Members' Code of Conduct.	
43.	To grant dispensations to Councillors and co-opted Members from the requirements relating to interests set out in the Members' Code of Conduct or other Council	

	codes and protocols where: (a) without the dispensation, the representation of different political groups on the body transacting the business would be so upset as to alter the outcome of any vote on the matter; (b) the Committee considers that the dispensation is in the interests of persons living in the Council's area; or (c) the Committee considers that it is otherwise appropriate to grant a dispensation.	
44.	To consider appeals against decisions made by the Monitoring Officer in exercise of their dispensation powers;	
45.	The exercise of (-) to (-) above in relation to Quedgeley Parish Council and the Members of the Parish Council;	
46.	To set up, where necessary, a Sub-Committee to shortlist and interview candidates for the role of Independent Person and to make recommendations to Council regarding the appointment of Independent Persons.	
47.	To provide such advice and assistance as appropriate regarding the appointment of the Independent Person as required under Part 7 of the Localism Act 2011.	
48.	To set the allowances and expenses payable to the Independent Person and Reserve Independent Persons.	

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Appendix 2

Proposed Terms of Reference - Audit and Governance Committee

Governance, risk and control

1. To review the Council's corporate governance arrangements against the good governance framework and consider annual governance reports and assurances.
2. To review the Annual Governance Statement prior to approval and consider whether it properly reflects the risk environment and supporting assurances, taking into account internal audit's opinion on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control.
3. To consider the Council's arrangements to secure value for money and review assurances and assessments on the effectiveness of these arrangements.
4. To consider the Council's framework of assurance and ensure that it adequately addresses the risks and priorities of the Council.
5. To monitor the effective development and operation of risk management in the Council.
6. To monitor progress in addressing risk-related issues reported to the Committee.
7. To consider reports on the effectiveness of internal controls and monitor the implementation of agreed actions.
8. To review the assessment of fraud risks and potential harm to the Council from fraud and corruption.
9. To monitor the counter-fraud strategy, actions and resources.

Internal Audit

10. To approve the internal audit charter.
11. To review proposals made in relation to the appointment of external providers of internal audit services and to make recommendations.
12. To approve the risk-based internal audit plan, including internal audit's resource requirements, the approach to using other sources of assurance and any work required to place reliance upon those other sources.
13. To approve significant interim changes to the risk-based internal audit plan and resource requirements.
14. To make appropriate enquiries of both management and the Head of internal audit to determine if there are any inappropriate scope or resource limitations.
15. To consider reports from the Head of internal audit on internal audit's performance during the year, including the performance of external providers of internal audit services. These will include:-
    a. Updates on the work of internal audit including key findings, issues of concern and action in hand as a result of internal audit work.
    b. Regular reports on the results of the Quality Assurance and Improvement Programme.
    c. Reports on instances where the internal audit function does not conform to the Public Sector Internal Audit Standards and Local Government Application Note, considering whether the non-conformance is significant enough that it must be included in the Annual Governance Statement.

16. To consider the Head of internal audit's annual report:
    a. The statement of the level of conformance with the Public Sector Internal Audit Standards and Local Government Application Note and the results of the Quality Assurance and Improvement Programme that supports the statement.
    b. The opinion on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control together with a summary of the work supporting the opinion.
17. To consider summaries of specific internal audit reports as requested.
18. To receive reports outlining the action taken where the Head of internal audit has concluded that management has accepted a level of risk that may be unacceptable to the authority or there are concerns about progress with the implementation of agreed actions.
19. To contribute to the Quality and Improvement Programme and in particular, to the external quality assessment of internal audit that takes place at least once every five years.
20. To consider a report on the effectiveness of internal audit to support the Annual Governance Statement, where required to do so by the Accounts and Audit Regulations.
21. To support the development of effective communication with the Head of internal audit.

External Audit

22. To consider the external auditor's annual letter, relevant reports, and the report of those charged with governance.
23. To consider specific reports as agreed with the external auditor.
24. To comment on the scope and depth of external audit work and to ensure it gives value for money.
25. To commission work from internal and external audit.
26. To advise and recommend on the effectiveness of relationships between external and internal audit and other inspection agencies or relevant bodies.

Financial reporting

27. To review the statement of accounts. Specifically, to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements or from the audit that need to be brought to the attention of the Council.
28. To consider the external auditor's report to those charges with governance on issues arising from the audit of the accounts.

Treasury Management

29. To review and monitor treasury management arrangements in accordance with the CIPFA Treasury Management Code of Practice.

Accountability arrangements

30. To report to those charged with governance on the Committee's findings, conclusions and recommendations concerning the adequacy and effectiveness of their governance, risk management and internal control frameworks; financial reporting arrangements, and internal and external audit functions.

31. To report to full Council on a regular basis on the Committee's performance in relation to the terms of reference and the effectiveness of the Committee in meeting its purpose.

Constitution and Standards

32. To consider and review changes to the Council's constitution in respect of Contract Standing Orders, Financial Regulations, and Codes of Conduct and behaviour.
33. To monitor the operation of the Council's codes and protocols (see Part 5 of this Constitution) and the Council's complaints process and to advise the Council on the adoption or revision of such codes.
34. To consider the Council's compliance with it's own published standards and controls.
35. To review any issues referred to it by the Chief Executive or a Corporate Director or any Council body.
36. To receive allegations and any accompanying report from the Monitoring Officer and to refer the allegation to the Monitoring Officer for formal investigation or informal resolution.
37. To set up, where necessary, a Hearings Panel to consider any alleged breach of the Members' Code of Conduct.
38. To promote and maintain high standards of conduct by Councillors and co-opted Members.
39. To assist Councillors and co-opted Members to observe the Members' Code of Conduct.
40. To advise the Council on the adoption, revision of, or publicity on the Members' Code of Conduct.
41. To advise, train or arrange to train Councillors and co-opted Members on matters relating to the Members' Code of Conduct.
42. To grant dispensations to Councillors and co-opted Members from the requirements relating to interests set out in the Members' Code of Conduct or other Council codes and protocols where:
    (a) without the dispensation, the representation of different political groups on the body transacting the business would be so upset as to alter the outcome of any vote on the matter;
    (b) the Committee considers that the dispensation is in the interests of persons living in the Council's area; or
    (c) the Committee considers that it is otherwise appropriate to grant a dispensation.
42. To consider appeals against decisions made by the Monitoring Officer in exercise of their dispensation powers;
43. To set up, where necessary, a Sub-Committee to shortlist and interview candidates for the role of Independent Person and to make recommendations to Council regarding the appointment of Independent Persons.
44. To provide such advice and assistance as appropriate regarding the appointment of the Independent Person as required under Part 7 of the Localism Act 2011.
45. To set the allowances and expenses payable to the Independent Person and Reserve Independent Persons.

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Gloucester City Council
Audit and Governance Work Programme 2013-14
(updated 7 March 2014)

Item	Format	Lead Officer	Comments
26 JUNE 2014:			
1. Committee Training on Treasury Management	Presentation	Director of Resources/Head of Finance	To take place before start of the main Committee
2. Audit and Governance Committee Action Plan	Timetable	------------	Standing agenda item requested by the Committee
3. Annual Audit Letter 2013/14	Letter	Darren Gilbert, KPMG	Part of the Committee's annual work programme
4. Annual Audit Fee 2014/15	Letter	Darren Gilbert, KPMG	Part of the Committee's annual work programme
5. Draft Statement of Accounts 2013/14	Written report	Corporate Director of Resources	Part of the Committee's annual work programme
6. Internal Audit Plan – Quarterly Monitoring Report	Written report	Audit, Risk and Assurance Manager	Part of the Committee's annual work programme
7. Internal Audit Annual Report 2013/14	Written report	Audit, Risk and Assurance Manager	Part of the Committee's annual work programme
8. Review of the Effectiveness of Internal Audit	Written report	Audit, Risk and Assurance Manager	Part of the Committee's annual work programme
9. Treasury Management Performance – Quarter 4	Written report	Head of Finance	Part of the Committee's annual work programme

26 JUNE 2014: (continued)			
Item	**Format**	**Lead Officer**	**Comments**
10. Treasury Management Strategy 2014/15	Written report	Head of Finance	Part of the Committee's annual work programme
11. Annual Governance Statement	Written report	Corporate Director of Resources	Part of the Committee's annual work programme
12. Annual Complaints Monitoring	Written report	Head of Legal & Policy Development	Part of the Committee's annual work programme
13. Annual Standards Report	Written report	Head of Legal & Policy Development	Part of the Committee's annual work programme
14. Business Rates Pooling Annual Report	Written report	Corporate Director of Resources	Part of the Committee's annual work programme
15. Annual Report of the Audit Committee	Written report	Audit, Risk and Assurance Manager	Part of the Committee's annual work programme
16. Draft Protocol for the Independent Person	Written report	Head of Legal and Policy Development	Part of the Committee's annual work programme
17. Committee Work Programme	Timetable	------------	Standing agenda item

Item	Format	Lead Officer	Comments
8 SEPTEMBER 2014:			
1. Audit and Governance Committee Action Plan	Timetable	------------	Standing agenda item requested by the Committee
2. Internal Audit Plan – Quarterly Monitoring Report	Written report	Audit, Risk and Assurance Manager	Part of the Committee's annual work programme
3. Audit and Governance Committee Work Programme	Timetable	------------	Standing agenda item

FUTURE AGENDA ITEMS (NO DATE FIXED YET):

- Review of the Whistleblowing Policy
- Review of the Council's Anti-Fraud Arrangements

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